



# Your Crash Course In CPA Exam Mentorship & Practice Questions

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Questions? My business email: [bryan@cpaexamguide.com](mailto:bryan@cpaexamguide.com)

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# How To Become A CPA Exam Survivor

Greetings Future CPA!

Are you ready to become a CPA exam survivor?

Thanks for grabbing my FREE CPA exam mentorship masterclass + 100 Sample CPA Exam Practice KeslerQs™.

My name is Bryan Kesler, CPA, and my team of CPAs, professors, and I created these never-before-seen questions and explanations from scratch just for you.

I have four selfless (and one selfish) reasons for giving you this smorgasbord of FREE CPA resources.

- 1) I want you to be able to quickly test your understanding on a sample of the topics tested on each CPA exam.
- 2) I want you to LEARN something new today.
- 3) I want you to understand how difficult the CPA exam is (and a PROVEN way that will maximize your odds of pass)
- 4) I love helping people pass the CPA exam and I want you to easily be able to do the same by sharing these CPA exam questions with as many people as possible.
- 5) Finally, **I'm bribing you** with free KeslerQs™ and mentorship because I want you to tap into my BRAND NEW CPA exam support system, Kesler CPA Review ([keslercpareview.com](https://keslercpareview.com)), so that I can:
  - a. Personally teach you how to pass,
  - b. Give you access to study materials that will teach you the AICPA blueprints and
  - c. Provide you with 1-on-1 tutoring to save time and give you the ability to outsource researching topics you don't know!

## What is Kesler CPA Review and what is a KeslerQ™?

Kesler CPA Review is a BRAND NEW way to tackle the CPA exam, and KeslerQs are the questions and explanations that are going to be the key to unlocking the AICPA blueprints for you.

Kesler CPA Review is a subscription-based CPA exam support system unlike anything you've ever seen that includes:

- Combining Confidence-Building Mentorship, Score-Boosting Study Materials, Time-Saving Tutoring & FUN To Ensure YOU Succeed

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- Full access to the NEW Kesler CPA Review with iOS/Android apps + thousands of KeslerQs™ (unlike any questions in the industry) & KeslerCards™ (mini-sims in your pocket) + full mock exams covering all four CPA sections to boot.
- FREE access to PROVEN Ultimate CPA Exam Guide Mentorship to teach you a step-by-step method for passing FAR, REG, AUD & BEC (normally \$697)
- FREE access to Kesler CPA Tutor Boost, which includes 1 FREE Tutor Boost Video Credit/month (exclusive 1-on-1 tutoring for all four CPA sections, \$50/month value)
- Email Support, Accountability, Community, VIP Bonuses & much more!
- Instant access to everything. Monthly subscription. No credit check. Cancel anytime. 30 day refund guarantee!

## What CPA Candidates Are Saying About KeslerQs

★★★★★

"Kesler CPA Review will be game changer for me. I love the study plan and the daily looping goals and the flashcard section. I really appreciate the notes section. Now I can keep track of everything instead of keeping separate notebooks!"

Julie

Ultimate CPA + Kesler CPA Review User



★★★★★

"I absolutely love Kesler CPA Review as the questions really forces me to think and understand the concept."

Yasmin

Ultimate CPA + Kesler CPA Review User



★★★★★

"I'm enjoying your new product (Kesler CPA Review)! It's got different types of questions than Roger & Ninja, so it complements them well. Your questions are much tougher than Roger's, and that really helped me understand in depth."

Mizzotini

Passed 3 of 3 sections with Kesler CPA  
+ UWorld Roger  
BEC 90 | AUD 88 | REG 88 |



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## What Is CPA Exam Mentorship?

Knowing HOW to study (and manage your time and anxiety) is just as important as the study materials you use.

I've seen the most competent candidates fail because they knew how to pass college but didn't take the time to learn how to study for the CPA exam.

I've also seen 4.0 GPA candidates give up on the CPA exam because they failed a section and assumed they didn't have what it took.

**FUN FACT:** Failing the CPA exam is by design... the AICPA wants to see how you react to it and if your first inclination is to give up, then in their eyes, you don't deserve the license.

So with that being said... let's stick to the AICPA together and master the CPA exam studying, failure preparation (just in case), and passing process!

The best place to start is my CPA exam study personality quiz.

It's going to connect you to relevant training and resources you need to optimize how you study with your study materials.

You can access the quiz here (it takes about 45 seconds to complete): [www.freecpaquiz.com](http://www.freecpaquiz.com)

Once you complete the quiz, it will provide you with my best mentorship advice for your specific situation!

Once you complete the quiz and check out the mentorship resources... it's time to come back here and start dominating some practice questions!

## BONUS: Online CPA Exam Readiness Exam

PDFs are great, but if you want a more accessible way to test your readiness for each section of the CPA

Head here to my free online CPA exam readiness exam:

<https://keslercpareview.com/cpa-exam-readiness-exam/>

If you are old school, go ahead and print out this worksheet front and back and start testing your knowledge below with our exclusive KeslerQs™!

## Disclaimers

#1: All questions below are trademarked and copyrighted by Kesler CPA Review and are NOT to be used for commercial purposes without our express permission. These are not AICPA-released questions.

You know this already, but this document provides no guarantees that you will pass the CPA exam. It goes without saying that if you do nothing then you will achieve nothing.

All I can do is show you the way to passing the CPA exam. You have to do the rest.

#2: You have permission, and I encourage you to share this PDF with anyone you know (or interact with in a study group) studying for the CPA exam if you feel that it will help them pass.



# TEST YOUR FAR MIGHT

## FAR KeslerQ™ #1:

Which is correct regarding interim financial reporting?

- I. Interim financial reporting is not required under GAAP.
  - II. Permanent inventory declines incurred during interim periods should NOT be recorded at the time of their decline, but rather should be reported at year-end.
  - III. Revenues and expenses should be allocated evenly over interim reporting periods, regardless of when they actually occurred.
- 
- A. I only
  - B. II only
  - C. I and II only
  - D. I, II, and III

**Solution: The correct answer is A.**

I is correct. Interim reporting is *not* required under GAAP. Interim reporting is required by the US SEC for publicly traded companies under the Federal Securities Act of 1934.

A report comes out every quarter to provide timely information to the users, but the information is only reviewed, not audited, so reliability may be affected. Interim reporting emphasizes timeliness over reliability.

Each statement must be marked “unaudited” so the users are put on notice. Interim financial reporting should be viewed as reporting for an integral part of an annual period.

II is incorrect. Permanent inventory losses from market declines should be reflected in the interim period in which they occur. Market increases in subsequent interim periods should be recognized in the recovery interim period not to exceed the losses included in prior interim periods.

Quarterly reporting requires the use of the same accounting methods as annual reporting.

III is incorrect. Revenues should be recognized as earned during an interim period in the same manner as they are for a full year. Costs and expenses that benefit more than one period should be allocated among interim periods, for example, property taxes.

Costs and expenses incurred and benefiting only that period, should be expensed as incurred.

**FAR KeslerQ™ #2:**

Calhoun Corp. had a beginning cash balance in Year 12 of \$20,000. They had net cash provided by operating activities of \$320,000 for Year 12, net cash used by investing activities of \$402,000, and cash provided by financing activities of \$262,000.

During the year, there was a sale of a fixed asset that resulted in a loss of \$10,000 and proceeds of \$42,000 were received from the sale. What was Calhoun Corp.'s cash balance at the end of Year 12?

- A. \$200,000
- B. \$232,000
- C. \$168,000
- D. \$148,000



**Solution: The correct answer is A.**

Beginning cash balance	\$20,000
Net cash provided by operating activities	+\$320,000
Net cash used by investing activities	-\$402,000
Net cash provided by financing activities	+\$262,000
Ending cash balance	<u>\$200,000</u>

The loss on sale of the fixed asset was already included as part of cash flows from investing activities and does not get considered separately.

**FAR KeslerQ™ #3:**

Which of the following is correct regarding the reporting of comprehensive income?

- I. Comprehensive income can be presented together with the income statement as a single financial statement.
- II. Comprehensive income may be shown separately on its own financial statement.

- A. I only**
- B. II only**
- C. Both I and II**
- D. Neither I nor II**

**Solution: The correct answer is C.**

I and II are correct. Comprehensive income can be presented on a single financial statement with net income.

Comprehensive income also may be shown separately on its own financial statement.

Comprehensive income is an element of the financial statements that includes all differences between beginning and ending equity other than transactions between a firm and its owners.

**FAR KeslerQ™ #4:**

In its consolidated financial statements in the current year, Benson Corp. included a subsidiary it acquired several years ago that was appropriately excluded from consolidation last year. How should this be reported?

- A. By note disclosure only**
- B. Currently and prospectively**
- C. Currently with note disclosure of pro forma effects of retrospective application**
- D. By retrospective application of all prior periods presented**

**Solution: The correct answer is D.**

This situation exhibits one in which there was a change in reporting entity.

A change in reporting entity is accounted for in a similar manner to a change in accounting principle and must be retrospectively applied to all prior periods presented.

Note only disclosure would not be appropriate, as this is a reportable transaction that requires recognition in the financial statements.

Current and prospective treatment applies to changes in accounting estimate, not changes in a reporting entity.

**FAR KeslerQ™ #5:**

From a study routine perspective, what is the most effective way to grasp the AICPA Blueprints?

- I. Watch ALL the lectures, read ALL the text and answer ALL the questions without reviewing as you go.
  - II. Focus on moving through the content as fast as possible but also taking time to loop back and review everything you have learned up to that point.
  - III. Spend time figuring out how you learn best so you can determine what study tools are useful and which ones waste your time.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**Solution: The correct answer is C.**

I is incorrect because you don't have time to complete all three of these resources. The CPA Exam is too broad. You need to be laser focused on understanding how you learn best and cut out any study resources that don't help you learn efficiently.

II is CORRECT because if you don't review what's in chapter 1 consistently then you will forget everything you learned by the time you hit your final chapter.

Keep everything in equal focus by performing study loops on a daily/weekly basis.

FUN FACT: Kesler CPA Review has study looping technology built into the platform to ensure you can easily review everything you have learned while also moving forward.

III is CORRECT because if you don't know how you learn best then you risk creating busy work for yourself which holds you back and wastes your time!

This is why finding a mentor to help you with this is crucial.

**FAR KeslerQ™ #6:**

Dartam Center is a private not-for-profit educational organization in support of homeschooled kids. How should Dartam Center report contributions of \$1,000,000 in cash in the statement of cash flows if the money is donor-restricted for 5 years and then can be spent at the discretion of the governing body?

- A. Operating activity inflow**
- B. Investing activity inflow**
- C. Financing activity inflow**
- D. Either operating or investing inflow**



**Solution: The correct answer is C.**

Contributions of cash that are donor-restricted for 5 years represent temporarily restricted net assets.

Proceeds received from restricted contributions are included in the financing section of the statement of cash flows whether permanently or temporarily restricted.

Also included as financing inflows are cash flows related to borrowing. Interest and dividend income restricted to reinvestment are classified as financing inflows as well.

**FAR KeslerQ™ #7:**

On January 1, Year 8, Ashbrook Corp. changed from one accounting method to another. The change in principle better presents the financial information of Ashbrook Corp. Under the old method the pretax accounting income was \$600,000. Had Ashbrook Corp. been using the new method, pretax accounting income would have been \$900,000. Ashbrook Corp.'s effective tax rate is 30%.

How should Ashbrook Corp. report the cumulative effect of a change in accounting principle for Year 8?

- A. \$300,000 additional income on the income statement**
- B. \$210,000 additional income on the income statement**
- C. \$300,000 increase to beginning retained earnings balance**
- D. \$210,000 increase to beginning retained earnings balance**

**Solution: The correct answer is D.**

The cumulative effect adjustment is recognized by adjusting beginning retained earnings, net of tax.

The difference between the pretax accounting income under the old method, \$600,000, and the pretax accounting under the new method, \$900,000, results in a higher profit of \$300,000 prior to January 1, Year 8.

With a tax rate of 30%, Ashbrook Corp. will adjust the beginning balance of Year 8 retained earnings for \$210,000.

**FAR KeslerQ™ #8:**

Storage Inc. owns a warehouse and leases space under a variety of agreements. Some customers pay in advance, and others fall behind on their rent. Storage Inc.'s financial records contained the following data:

	<b>Year 1</b>	<b>Year 2</b>
Rent receivable	\$7,600	\$8,200
Unearned rent	\$28,000	\$21,000

During Year 2, Storage Inc. received \$60,000 cash from tenants. What amount of rental revenue should Storage Inc. record for Year 2?

- A. \$60,000**
- B. \$67,600**
- C. \$52,400**
- D. \$68,240**

**Solution: The correct answer is B.**

Cash basis collections	\$60,000
Rent receivable, ending	+8,200
Rent receivable, beginning	-7,600
Unearned revenue	↓
Beginning	+\$28,000
Ending	<u>-\$21,000</u>
Accrual basis rent revenue	\$67,600

**FAR KeslerQ™ #9:**

Ulacia Corp. is obligated to repurchase receivables that have been sold and needs to record a loss contingency. Ulacia Corp. has estimated a range of losses between \$75,000 and \$150,000. Which of the following is correct?

- I. If no amount in the range is a better estimate than any other amount, the minimum amount, \$75,000, should be accrued as the contingent loss.
- II. The maximum amount of the range, \$150,000, should be recorded.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is A.**

I is correct. Under US GAAP, if no amount in the range is a better estimate than any other amount, the minimum amount in the range should be accrued, in this case \$75,000, and a note describing the possibility of an additional \$75,000 loss should be presented.

**FAR KeslerQ™ #10:**

The risks of not finding a CPA exam mentor to help you on your journey to passing include:

- I. No one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.
- II. No one to coach you on how to recover from failure or what to do when the going get's tough. Someone who has been there and done that.
- III. No one to help you study more efficiently. You will spend more time studying and get less results.

- A. I only**
- B. II only**
- C. II and III only**
- D. I, II, and III**



**Solution: The correct answer is D.**

If you don't have someone who understands how to pass the CPA exam (or recover from failure)...

You will have no one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.

No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.

No one to help you study more efficiently. You will spend more time studying and get less results.

**This is why Kesler CPA Review was created! To provide you with access to all three.**

**FAR KeslerQ™ #11:**

For financial statement reporting purposes, which of the following methods of recognizing bad debts is consistent with US GAAP since it provides for matching of revenues with expenses incurred to generate those revenues in the same accounting period?

- I. Direct write-off method
- II. Allowance method

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

It is correct. The allowance method is consistent with US GAAP because it provides for matching of current year credit sales with the estimated uncollectible expenses from those sales.

**FAR KeslerQ™ #12:**

Olympic Fascination Corp. has inventory with a FIFO cost of \$16,730, net realizable value of \$16,850, replacement cost of \$16,490, and net realizable value less normal profit of \$16,545. What amount should Olympic report as ending inventory in its balance sheet at year-end?

- A. \$16,730
- B. \$16,850
- C. \$16,490
- D. \$16,545

**Solution: The correct answer is D.**

Currently, under US GAAP, inventory is valued at the lower of cost or market. Market is defined as the median value between the market “ceiling” (net realizable value), the market “floor” (net realizable value less a normal profit margin), and the replacement cost.

Whichever value is in the middle of those three is the market. The designated market price in this question would, therefore, be \$16,545, which is the median value between net realizable value (“ceiling”) of \$16,850, net realizable value less a normal profit margin (“floor”) of \$16,545, and replacement cost of \$16,490.

Since the cost (\$16,730) is higher than designated market (\$16,545), Olympic should report the ending inventory at \$16,545, the lower of cost or market.

**FAR KeslerQ™ #13:**

For Year 13, the Franklin Corp. has beginning inventory of \$41,875 and ending inventory of \$32,109. Purchase returns and freight in are \$20,200 and \$24,360, respectively. Purchases are \$112,800 and freight out is \$5,733. How much is cost of goods sold for Year 13?

- A. \$126,726
- B. \$158,835
- C. \$134,475
- D. \$118,406

**Solution: The correct answer is A.**

Cost of goods sold is calculated as follows:

Beginning inventory	\$41,875
Purchases	+\$112,800
Purchase returns	-\$20,200
Freight in	+\$24,360
Total available for sale	\$158,835
Ending inventory	-\$32,109
Cost of goods sold	\$126,726

**FAR KeslerQ™ #14:**

Rochelle Corp. acquired 40% of Clark Inc.'s voting common stock on January 2, Year 13, for \$400,000. The carrying amount of Clark's net assets at the purchase date totaled \$900,000. Fair values equaled carrying amounts for all items except equipment, for which fair values exceeded carrying amounts by \$100,000. The equipment has a 5-year life. During Year 13, Clark reported net income of \$150,000. What amount of income from this investment should Rochelle Corp. report in its Year 13 income statement?

- A. \$56,000
- B. \$60,000
- C. \$52,000
- D. \$68,000



**Solution: The correct answer is C.**

Under the equity method, adjustments to the investment account result from the differences between the price paid for the investment and the book value of the investee's net assets acquired. The premium paid for the investment is calculated as follows:

Total book value of the investee's net assets	\$900,000
Percent acquired	<u>× 40%</u>
Book value of the 40% of the investee's net assets acquired	\$360,000
Cost to acquire the 40% of the investee's net assets	<u>−\$400,000</u>
Premium paid above book value for the 40% ownership	(\$40,000)

The \$40,000 premium paid needs to be amortized based on what caused the premium in the first place. The facts indicate that there is undervalued equipment on the books of Clark Corp. and that alone is the rationale for the premium paid of \$40,000 for the investment. Therefore:

Undervalued equipment \$100,000 × 40% acquired	\$40,000
5-year life of equipment	<u>÷ 5 years</u>
Annual amortization for 5 years	\$8,000

The \$8,000 of amortization relating to the under-valued equipment needs to be recorded each year for 5 years and will serve to reduce investee earnings of Clark Corp. each year.

Therefore, for the next 5 years, each time Clark Corp. reports earnings, Rochelle Corp. will recognize 40% of those earnings but then subtract \$8,000 of amortization. The calculation of investee earnings net of amortization for Year 13 for Rochelle Corp. is as follows:

Investee earnings \$150,000 × 40% ownership	\$60,000
Less annual amortization of undervalued equipment	<u>−\$8,000</u>
Equity method investment income	\$52,000

**FAR KeslerQ™ #15:**

The risks of not finding a CPA exam accountability partner include:

- I. Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
  - II. Your friends and family will start to resent you for spending more time studying than with them.
  - III. Studying won't be fun. No one to share in your wins for hitting study goals.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**Solution: The correct answer is D.**

There's nothing wrong with it taking a village to pass the CPA exam!

In fact, getting the people in your life involved in the process is crucial to your sanity (and theirs) because....

- 1) Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
- 2) Your friends and family will start to resent you for spending more time studying than with them.
- 3) Studying won't be fun. No one to share in your wins for hitting study goals.

**FAR KeslerQ™ #16:**

Weis Co. borrowed \$125,000 on November 1, Year 1, and signed a two-year note bearing interest of 10% on that date. Interest is compounded annually and is payable in full at the note's maturity date of March 31, Year 3. What amount of liability for interest should Weis have accrued as of December 31, Year 2?

- A. \$14,791
- B. \$12,500
- C. \$2,083
- D. \$0

**Solution: The correct answer is A.**

Accrued interest payable at December 31, Year 2, is interest that has been incurred by December 31, Year 2, that has not yet been paid by that date. Weis borrowed the \$125,000 on November 1, Year 1, and the total interest payable is not due until March 31, Year 3, the note maturity date.

Therefore, at December 31, Year 2, there should be 14 months (November 1, Year 1, to December 31, Year 2) of interest payable (accrued). Interest for Year 1 can be computed as follows:  $\$125,000 \times 10\% \times 212$  (November 1, Year 1 through December 31, Year 1) = \$2,083.

Since interest is compounded annually, this unpaid (accrued) interest must be added to the \$125,000 note principal when computing interest for Year 2. Accrued interest for Year 2 can, therefore, be calculated as  $(\$125,000 + \$2,083) \times 10\% = \$12,708$ .

Thus, at December 31, Year 2, Weis should have a liability for accrued interest reported on its balance sheet in the total amount of \$14,791 (\$2,083 from Year 1 + \$12,708 from Year 2).

**FAR KeslerQ™ #17:**

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Reynolds Corp. issued \$200,000 worth of 11% bonds for par on January 31, Year 5. The bonds are dated December 31, Year 1, and pay interest semiannually on June 30 and December 31. What amount of accrued interest payable should Reynolds Corp. report in its September 30, Year 5, balance sheet?

- A. \$5,500
- B. \$7,333
- C. \$11,000
- D. \$1,833

**Solution: The correct answer is A.**

Accrued interest at September 30, Year 5, is the interest owed at year-end since the June 30, Year 5, interest payment. Accrued interest is calculated as  $\$200,000 \times 11\% \times 3/12 = \$5,500$ .

The period of time from June 30 through September 30, 3 months, needs to be accrued on the September 30 balance sheet.

The journal entry at September 30 (end of year) would include a debit to interest expense of \$5,500 and a credit to interest payable of \$5,500.

**FAR KeslerQ™ #18:**

On January 1, Year 9, Hayley Corp. traded delivery trucks with Dylan Corp. and paid \$5,000 cash to Dylan Corp. Hayley Corp.'s truck had a fair value of \$95,000 and accumulated depreciation of \$75,000 on the date of exchange. Hayley Corp.'s asset had an original cost of \$130,000.

Hayley estimated that the value of Dylan Corp.'s truck was \$90,000 on the date of exchange. The book value of Dylan Corp.'s truck on January 1, Year 9, was \$70,000. The transaction had commercial substance.

Under US GAAP, what amount of gain should be recorded by Hayley Corp.?

- A. \$0
- B. \$35,000
- C. \$40,000
- D. \$55,000



**Solution: The correct answer is C.**

When a nonmonetary transaction has commercial substance, gains and losses are recognized immediately based on the difference between the asset's fair value and book value at the time of exchange.

Since the exchange has commercial substance, the entire gain is recognized by Hayley Corp. despite the payment of \$5,000 in cash to Dylan Corp. For Hayley Corp., gain on the asset given up is calculated as follows:

Fair value	\$95,000
Subtract book value (cost \$130,000 – accumulated depreciation \$75,000)–	\$55,000
Gain	\$40,000

**FAR KeslerQ™ #19:**

Which of the following is correct regarding patent costs under US GAAP?

- I. Fees to acquire a patent from a third party are expensed.
  - II. Most costs incurred to internally generate a patent are expensed.
  - III. Costs associated with either a successful or unsuccessful patent defense should be capitalized.
- 
- A. I only
  - B. I and II only
  - C. I, II, and III
  - D. II only

**Solution: The correct answer is D.**

I is incorrect. Fees to acquire a patent and other intangible assets from third parties are capitalized and amortized over the shorter of the patent's remaining legal life or estimated life using the straight line amortization method. Legal fees and registration fees associated with patents are also capitalized.

II is correct. Under US GAAP, costs incurred to internally develop a patent are expensed as research and development. US GAAP requires research and development costs to be expensed although certain costs like consulting fees, design costs, and registration fees associated with an internally generated patent are capitalized.

Notice that the manner of acquisition of intangible assets (e.g., patents) is a factor in determining whether the intangible asset is capitalized or expensed. Intangible assets that are purchased from third parties are capitalized. Intangible assets that are internally developed are expensed as research and development.

III is incorrect. Only costs associated with a successful patent defense are capitalized. Costs associated with an unsuccessful patent defense are expensed.

**FAR KeslerQ™ #20:**

The risks of not finding a CPA exam tutor include:

- I. Spending too much time on research that could be spent better elsewhere.
- II. Never achieving a grasp of a complex topic that could tank your scores.
- III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.

- A. I only
- B. II only
- C. II and III only
- D. I, II, and III

**Solution: The correct answer is D.**

I wasted SO much time spinning my wheels trying to figure things out on my own...

Don't make this mistake!

Time is your most precious commodity and you don't have more than 10-15 minutes to spend on any given topic considering the breadth and the depth of what's tested.

This is why outsourcing to CPA exam tutors can be a lifesend!

When you don't have a CPA exam tutor... you risk:

- I. Spending too much time on research that could be spent better elsewhere.
- II. Never achieving a grasp of a complex topic that could tank your scores.
- III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.

**This is why when you are a member of Kesler CPA Review we give you monthly tutor credits for our tutors for your most difficult questions!**

**FAR KeslerQ™ #21:**

The partnership of Heaslip and Shapiro are considering adding Kenneth as a partner. When admitting Kenneth into the partnership, Kenneth's capital account equals the amount of his actual contribution under which of the following methods?

- I. Bonus method
- II. Goodwill method

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

It is correct. Under the goodwill method, the incoming partner's capital account is his or her actual contribution.

Goodwill is then determined based on the incoming partner's contribution and shared by the existing partners only; therefore, the incoming partner's capital account is credited for the exact amount of the new partner's contribution.

**FAR KeslerQ™ #22:**

Losses due to write-downs of assets under a quasi-reorganization would affect which of the following under US GAAP?

- I. Retained earnings
- II. Income statement

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II



**Solution: The correct answer is A.**

I is correct. Under US GAAP losses from write-down of assets under quasi-reorganization would affect retained earnings.

**FAR KeslerQ™ #23:**

Which of the following regarding funds and fund accounting is correct?

- I. Fund accounting supports financial control by helping prevent overspending.
- II. A fund is a sum of money set aside to accomplish a specific goal.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. Fund accounting supports financial control by helping prevent overspending and making sure that legally restricted and designated monies are spent as intended.

Fund accounting makes it easier to monitor compliance with legal restrictions and spending limits. By using fund accounting, the governing body attempts to demonstrate fiscal accountability.

II is correct. A fund is a sum of money set aside to accomplish a specific goal. The purpose of fund accounting is to isolate the recording of each activity or group of activities.

With fund accounting used by governmental units, resources are segregated for the purpose of carrying on specific activities and attaining certain objectives.

Therefore, a self-balancing set of accounts is established for the fire department, the community pool, the subway system, and so on. Each of these sets of accounts is known as a fund.

**FAR KeslerQ™ #24:**

For a governmental entity, which of the following is an example of a derived revenue?

- I. Sales tax
  - II. Income tax
  - III. Property tax
- 
- A. Both I and II**
  - B. Both I and III**
  - C. Both II and III**
  - D. I, II, and III**

**Solution: The correct answer is A.**

I and II are correct. Sales tax and income tax are examples of derived revenue for a governmental entity.

Derived revenue is where the underlying event is being taxed.

**FAR KeslerQ™ #25:**

Which of the following could NOT be reported as cash or cash equivalents?

- A. Money market accounts**
- B. Demand deposits**
- C. US treasury bills with an original maturity of 60 days from date purchased**
- D. Legally restricted deposits held as compensating balances against borrowing arrangements with a lending institution**

**Solution: The correct answer is D.**

Compensating balances are not included as cash or cash equivalents if the deposit is legally restricted. Compensating balances may be included as a cash or cash equivalent if the deposit is not restricted.

Compensating balances are often required by lenders so that a debtor can borrow from the institution but must leave some amount behind as collateral.

If the amount left behind is legally restricted, it would be reported separately as a current asset but not part of cash or cash equivalents.

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# TEST YOUR AUD MIGHT

## AUD KeslerQ™ #1:

According to the generally accepted auditing standards (GAAS), which of the following must be expressed in a standard auditor's report?

- I. The auditor's conclusion that consistent accounting principles were applied from period to period
  - II. The auditor's opinion that the financial statement disclosures and footnotes are sufficient and appropriate in the circumstances
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II



**Solution: The correct answer is D.**

I is wrong. In the auditor's report, consistency of accounting principles from period to period is implied and only referred to explicitly if there is an inconsistency. For example, if the client used FIFO in Year 1 for inventory valuation, it's implied that he or she also used FIFO in Year 2.

This would be consistent and, therefore, would NOT have to be expressed in the auditor's report. However, if the client used FIFO in Year 1 and Average Cost in Year 2, this would represent an inconsistency and would need to be expressed in the report.

II is wrong. In an auditor's standard report the fact that client disclosures and footnotes are adequate need not be indicated.

The auditor would mention disclosures and footnotes only if there were problems with them. Otherwise, it is implied in a standard audit report that client footnotes and disclosures are adequate.

**AUD KeslerQ™ #2:**

A CPA should decide NOT to accept a new client for an audit engagement if:

- I. the CPA lacks an understanding of the client's industry and accounting principles prior to acceptance
- II. the client's management has unusually high turnover

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is D.**

I is wrong. If a CPA lacks an understanding of the client's industry and accounting principles but feels confident that such information and knowledge can be obtained prior to commencement of the audit, the engagement can still be accepted.

II is wrong. If the client's management has unusually high turnover, the engagement can still be accepted, although the high turnover would be considered a fraud risk factor.

**AUD KeslerQ™ #3:**

Inherent risk is:

- I. not influenced by the amount of work or other testing performed by the independent auditor
  - II. a characteristic of the accounting system and the personnel who work in that system
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. Inherent risk is a client characteristic that is evaluated by the auditor. The more work and testing done by the auditor, the better the chances that the evaluation will be accurate.

II is correct. The quantity of work performed by the auditor will not impact the actual amount of inherent risk present within the reporting company; it is a characteristic of the accounting system and the personnel who work in that system.

**AUD KeslerQ™ #4:**

Which of the following is viewed as a fraud risk factor that indicates that management or other employees have the incentive or pressure to carry out fraudulent financial reporting?

- I. Decline in customer demand
- II. Negative cash flows from operations
- III. Company plans to obtain additional debt financing

- A. I, II, and III
- B. II and III only
- C. I and II only
- D. I and III only

**Solution: The correct answer is A.**

I is correct. Declining demand and a shrinking industry result in lower sales and would add to the pressure or incentive to commit fraudulent financial reporting.

II is correct. Negative cash flows from operations could also create pressure to commit fraudulent financial reporting. Inability to generate cash flows from operations while somehow reporting substantial earnings growth would be a fraud risk factor for fraudulent financial reporting.

III is correct. If the company were seeking debt financing, higher interest rates would be charged if the company were shown to have a high risk for default.

The incentive for fraudulent financial reporting would be increased in order to make the company look like a better credit risk.

**AUD KeslerQ™ #5:**

From a study routine perspective, what is the most effective way to grasp the AICPA Blueprints?

- I. Watch ALL the lectures, read ALL the text and answer ALL the questions without reviewing as you go.
  - II. Focus on moving through the content as fast as possible but also taking time to loop back and review everything you have learned up to that point.
  - III. Spend time figuring out how you learn best so you can determine what study tools are useful and which ones waste your time.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III



**SOLUTION is C.**

I is incorrect because you don't have time to complete all three of these resources. The CPA Exam is too broad. You need to be laser focused on understanding how you learn best and cut out any study resources that don't help you learn efficiently.

II is CORRECT because if you don't review what's in chapter 1 consistently then you will forget everything you learned by the time you hit your final chapter.

Keep everything in equal focus by performing study loops on a daily/weekly basis.

FUN FACT: Kesler CPA Review has study looping technology built into the platform to ensure you can easily review everything you have learned while also moving forward.

III is CORRECT because if you don't know how you learn best then you risk creating busy work for yourself which holds you back and wastes your time!

This is why finding a mentor to help you with this is crucial.

**AUD KeslerQ™ #6:**

The auditor is likely to focus the assessment of control risk on the entity's:

- I. reporting controls
- II. operational controls

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is A.**

I is correct. An auditor's primary consideration in evaluating controls is whether specific controls affect the account balances on the client's financial statements, since ultimately the auditor must render an opinion on whether the financial statements are fairly presented.

II is wrong. Operational controls are relevant to the entity, its operating units, and its business functions. Operational controls are not a primary concern of the independent auditor. The auditor is only concerned with controls that affect the financial statements.

**AUD KeslerQ™ #7:**

An auditor gains an understanding of the client's attempt to keep internal controls up to date. This ongoing process of keeping controls effective:

- I. refers to the monitoring component of internal control
- II. is often performed by the internal audit function

- A. I only**
- B. II only**
- C. Both I and II**
- D. Neither I nor II**

**Solution: The correct answer is C.**

I is correct. The monitoring component of internal control involves assessing the design and operation of controls on a timely basis and taking necessary corrective actions. The auditor looks to see if monitoring of internal control is a priority of the client company because this will impact the auditor's assessment of control risk.

II is correct. The monitoring component of internal control involves assessing the design and operation of controls on a timely basis and taking necessary corrective actions. Monitoring is an internal function often performed by the client's internal audit department.

**AUD KeslerQ™ #8:**

Which of the following represents an inherent limitation of internal control?

- I. Management override
- II. Incompatible duties

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is A.**

I is correct. Management override of controls is an inherent limitation of internal control. An example of an inherent limitation would be if the CEO is the only employee who can request a check with no purchase order.

II is wrong. Incompatible duties are internal control weaknesses but not inherent limitations. An inherent limitation is built in and cannot entirely be prevented. Incompatible duties can be corrected and, therefore, are not inherent limitations.

**AUD KeslerQ™ #9:**

How many main sections are found in a standard unmodified audit report?

- A. 3
- B. 4
- C. 5
- D. 6



**Solution: The correct answer is B.**

There are four main sections in a standard unmodified audit report: an introductory section, management's responsibility section, auditor's responsibility section, and opinion section.

**AUD KeslerQ™ #10:**

The risks of not finding a CPA exam mentor to help you on your journey to passing include:

- I. No one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.
- II. No one to coach you on how to recover from failure or what to do when the going get's tough. Someone who has been there and done that.
- III. No one to help you study more efficiently. You will spend more time studying and get less results.

- A. I only
- B. II only
- C. II and III only
- D. I, II, and III

**Solution: The correct answer is D.**

If you don't have someone who understands how to pass the CPA exam (or recover from failure)...

You will have no one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.

No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.

No one to help you study more efficiently. You will spend more time studying and get less results.

**This is why Kesler CPA Review was created! To provide you with access to all three.**

**AUD KeslerQ™ #11:**

A review for a nonissuer that is prepared unmodified from the standard review report will contain how many paragraphs?

- A. 4
- B. 5
- C. 2
- D. 3

**Solution: The correct answer is A.**

An unmodified review report under Statements on Standards for Accounting and Review Services (SSARS) for a nonissuer contains four paragraphs:

- (1) introductory paragraph,
- (2) management responsibility paragraph,
- (3) CPA's responsibility paragraph, and
- (4) limited assurance paragraph.

**AUD KeslerQ™ #12:**

A dual opinion on special purpose frameworks and GAAP would be required if the financial statements were prepared on which of the following frameworks?

- I. Income tax basis
  - II. Cash basis
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is D.**

I is wrong. A dual opinion on special purpose framework and GAAP would not be required if the financial statements were prepared on the income tax basis.

II is wrong. A dual opinion on special purpose framework and GAAP would not be required if the financial statements were prepared on the cash basis.

A dual opinion would apply only to financial statements prepared on a regulatory basis that are intended for general use. Then and only then would the auditor have to give an opinion on both conformity with GAAP and also whether the statements present fairly in accordance with the special purpose framework designed by the regulatory agency.

**AUD KeslerQ™ #13:**

An auditor's report on compliance would include a restriction of use if the report on compliance was:

- I. issued separately from the report on the financial statements
  - II. included as an other-matters paragraph in a report on the complete financial statements
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**



**Solution: The correct answer is C.**

I is correct. The auditor's report on compliance should contain a restriction on the use of the report if the report is issued separately.

II is correct. The auditor's report on compliance should include a restriction on the use of the report as an other-matters paragraph if the report on compliance is not issued separately but included as part of an auditor's report on complete financial statements.

**AUD KeslerQ™ #14:**

SSAE standards do NOT apply to reports and services relating to:

- I. internal control
- II. consulting

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. Consulting engagements fall under the standards of Statements on Standards for Consulting Services.

I is wrong. SSAE apply to engagements involving the auditor examining internal control, pro forma financial reporting, compliance, agreed-upon procedures, forecasts, and projections.

**AUD KeslerQ™ #15:**

The risks of not finding a CPA exam accountability partner include:

- I. Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
  - II. Your friends and family will start to resent you for spending more time studying than with them.
  - III. Studying won't be fun. No one to share in your wins for hitting study goals.
- A. I only**
  - B. II only**
  - C. II and III only**
  - D. I, II, and III**

**Solution: The correct answer is D.**

There's nothing wrong with it taking a village to pass the CPA exam!

In fact, getting the people in your life involved in the process is crucial to your sanity (and theirs) because....

- 1) Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
- 2) Your friends and family will start to resent you for spending more time studying than with them.
- 3) Studying won't be fun. No one to share in your wins for hitting study goals.

**AUD KeslerQ™ #16:**

Recalculation of invoice amounts and inspection of certain documents for authorization are audit procedures designed to test which of the following assertions?

- I. Cutoff
  - II. Valuation
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. Recalculating (footing and cross-footing) invoices helps test valuation. Inspection of documents also assists with valuation because the auditor would look for authorization.

For example, if the auditor sees that credit was checked before goods were shipped to a customer, accounts receivable is likely to be properly valued. The auditor will look for approvals on sales orders.

I is wrong. Checking math accuracy will NOT help with cut-off testing. Examining transactions just before and just after the end of the year for proper accounting period recognition (to see when they were recorded) would be a cutoff test.

**AUD KeslerQ™ #17:**

When an independent auditor uses professional judgment to make decisions about the “nature, extent, and timing” of audit procedures, what does the term *nature* refer to?

- I. The amount of testing to be performed
  - II. The type of test to be performed
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**



**Solution: The correct answer is B.**

II is correct. In the phrase “nature, extent, and timing” of audit procedures, the term *nature* refers to the type of test performed, whether the test is a test of controls or perhaps a substantive test.

I is wrong. In the phrase “nature, extent, and timing” of audit procedures, the term *nature* does not refer to the amount of testing. The term *extent* refers to the amount of testing.

**AUD KeslerQ™ #18:**

Which of the following involves a theft of receivables followed by a delay in the posting of credits to specific customer accounts?

- I. Kiting
- II. Lapping

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. Lapping involves the theft of receivables by an employee.

The employee then must cover the theft by giving credit to the customer who paid. However, lapping results in a delay in the recording of specific credits to customer accounts because today's collection covers up yesterday's theft. Lapping can be prevented by proper segregation of duties.

The same employee should not be able to both deposit customer checks and post the credits to the customer accounts.

I is wrong. Kiting has nothing to do with receivables. Kiting involves cash that appears to be in two company bank accounts at the same time.

**AUD KeslerQ™ #19:**

An auditor is concerned that the company is increasing reported net income by producing sales invoices for goods that were never ordered or shipped.

- I. The auditor should select a sample of sales invoices and verify that matching sales orders and bills of lading exist.
- II. If the auditor finds sales invoices with no related shipping documents, this would be a test of the occurrence assertion rather than the completeness assertion.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. The auditor wants to know, if a sales invoice is prepared, were the goods actually ordered and shipped? The auditor should start by selecting a sample from the sales invoices and look to see if there are shipping documents to support the sales invoices. The auditor always starts with the event that is assumed to have happened and moves to the event that is uncertain.

II is correct. If the auditor finds sales invoices with no related shipping documents, this would be a test for overstatement of sales, rather than understatement. The occurrence assertion is affected rather than the completeness assertion when the fear is overstatement.

**AUD KeslerQ™ #20:**

The risks of not finding a CPA exam tutor include:

- I. Spending too much time on research that could be spent better elsewhere.
  - II. Never achieving a grasp of a complex topic that could tank your scores.
  - III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**Solution: The correct answer is D.**

I wasted SO much time spinning my wheels trying to figure things out on my own...

Don't make this mistake!

Time is your most precious commodity and you don't have more than 10-15 minutes to spend on any given topic considering the breadth and the depth of what's tested.

This is why outsourcing to CPA exam tutors can be a lifesend!

When you don't have a CPA exam tutor... you risk:

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**This is why when you are a member of Kesler CPA Review we give you monthly tutor credits for our tutors for your most difficult questions!**

**AUD KeslerQ™ #21:**

To test the existence assertion for accounts receivable an auditor would:

- I. send accounts receivable confirmation requests to a sample of client customers
- II. inspect and verify the credit-granting policies of the client

- A. I only**
- B. II only**
- C. Both I and II**
- D. Neither I nor II**



**Solution: The correct answer is A.**

I is correct. External confirmations provide evidence to support the existence assertion. External confirmations are meant to ascertain that the balances shown on the company's records actually do exist; the customer is real and not fictitious. For this reason, the auditor mails the confirmations to the client's customers and the customers are asked to respond directly to the auditor so that the client cannot intervene.

The auditor should be in charge of mailing the confirmations to ensure that they actually do get mailed. Either the auditor or the client can prepare the confirmations, but if the client is involved, the auditor should make a careful review. Because of confidentiality, a representative of the client must sign the confirmations, but all other actions are taken by the auditor, both the mailing and the receiving of the responses.

II is wrong. Credit verification refers to the valuation of accounts receivable. By checking credit before shipping goods, the client is trying to minimize the likelihood of selling goods and then having to write off the debt as uncollectible. Any question about accounts receivable that deals with the uncollectible accounts or the aging schedule deals with the valuation assertion rather than existence.

**AUD KeslerQ™ #22:**

Which of the following is an example of audit evidence generated by the client in the purchasing cycle?

- I. Bills of lading
  - II. Receiving reports
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**

**Solution: The correct answer is B.**

II is correct. Receiving reports are client-generated documents in the purchasing cycle.

I is wrong. Bills of lading, although they may be generated by the client, are documents generated in the sales cycle, not the purchasing cycle.

**AUD KeslerQ™ #23:**

The auditor believes the actual error rate of an activity is 2% but can tolerate a rate of up to 5 percent. The auditor wants to reduce sampling risk to 10 percent. The appropriate sample size is determined and selected, and an error rate of 3 percent is discovered. A chart is examined that indicates that the upper deviation rate is 4.4 percent. Which is correct?

- I. The auditor should assess the control activity as having too many errors.
- II. The tolerable rate is higher than the upper deviation rate.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. The tolerable rate, given as 5%, is higher than the upper deviation rate, given as 4.4%. Therefore, the auditor will likely view the control as reliable and lower his or her assessment of control risk, thus leading to less substantive testing in this area of the audit.

I is wrong. Although there were errors, the sample error rate of 3% translated into an upper deviation rate of 4.4%. Therefore, the auditor would not conclude that there were too many errors, since the upper deviation rate of 4.4% error was lower than the tolerable error rate of 5%.

**AUD KeslerQ™ #24:**

Which of the following is considered a procedure involving the auditor's search for contingent liabilities?

- I. Reviewing a bank confirmation letter
  - II. Reviewing a customer's response to a negative confirmation
  - III. Examining client invoices received from professionals who have provided service
- 
- A. I only
  - B. I and III only
  - C. I, II, and III
  - D. III only

**Solution: The correct answer is B.**

I is correct. A primary objective when auditing liabilities is to determine that they are all properly included. Accordingly, the auditor has to search for liabilities that exist as of the balance sheet date. In searching for contingent liabilities, the auditor will typically review bank confirmation letters for any indication of direct or contingent liabilities.

If the client's bank loan contained a debt covenant that required the current ratio to be 2:1 or better at all times, a direct or contingent liability would exist if the client were to fall below that ratio.

III is correct. Examining invoices for professional services, especially from attorneys who may be working on pending litigation, may provide evidence of contingent liabilities.

II is wrong. Accounts receivable confirmations provide evidence regarding assets, not liabilities.

**AUD KeslerQ™ #25:**

When an independent auditor hires a specialist to perform certain substantive tests, an understanding should exist among which of the following parties as to the nature of the work to be performed?

- I. The auditor
  - II. The client
  - III. The specialist
- 
- A. I and II only**
  - B. I and III only**
  - C. II and III only**
  - D. I, II, and III**



**Solution: The correct answer is D.**

I, II, and III are correct. When an independent auditor hires a specialist to perform certain substantive tests, an understanding should exist among the auditor, the client, and the specialist as to the nature of the work to be performed.

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# TEST YOUR BEC MIGHT

## **BEC KeslerQ™ #1:**

Inventoriable costs include:

- I. product costs
- II. period costs

- A. I only**
- B. II only**
- C. Both I and II**
- D. Neither I nor II**

**Solution: The correct answer is A.**

I is correct. Product costs are inventoriable. They are assets and remain on the balance sheet until the product is sold.

II is wrong. Period costs are expensed immediately in the period incurred.

**BEC KeslerQ™ #2:**

Variable costs:

- I. per unit remain unchanged in the relevant range
- II. increase in total as unit volume increases

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is C.**

I and II are correct. Variable costs per unit remain unchanged in the relevant range. Variable costs increase in total as unit volume increases.

**BEC KeslerQ™ #3:**

In a job costing system, issuing indirect materials to production increases which account(s)?

- I. Factory overhead applied
  - II. Factory overhead control
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. The cost of indirect materials used increases the factory overhead control account and decreases materials control. All actual overhead costs are debited to the overhead control T account.

I is wrong. Overhead applied is based on estimates, not actual costs. If the estimates are higher than actual costs, a credit balance remains in the factory overhead control account.

**BEC KeslerQ™ #4:**

Under the contribution approach, which of the following would contain only variable costs?

- I. Ending inventory
- II. Cost of goods sold

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II



**Solution: The correct answer is C.**

I and II are correct. Using variable costing, all fixed factory overhead is treated as a period cost and is expensed in the period incurred.

The cost of inventory includes only variable manufacturing costs, so the cost of goods sold includes only variable costs.

**BEC KeslerQ™ #5:**

From a study routine perspective, what is the most effective way to grasp the AICPA Blueprints?

- I. Watch ALL the lectures, read ALL the text and answer ALL the questions without reviewing as you go.
  - II. Focus on moving through the content as fast as possible but also taking time to loop back and review everything you have learned up to that point.
  - III. Spend time figuring out how you learn best so you can determine what study tools are useful and which ones waste your time.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

## **SOLUTION IS C.**

I is incorrect because you don't have time to complete all three of these resources. The CPA Exam is too broad. You need to be laser focused on understanding how you learn best and cut out any study resources that don't help you learn efficiently.

II is CORRECT because if you don't review what's in chapter 1 consistently then you will forget everything you learned by the time you hit your final chapter.

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III is CORRECT because if you don't know how you learn best then you risk creating busy work for yourself which holds you back and wastes your time!

This is why finding a mentor to help you with this is crucial.

**BEC KeslerQ™ #6:**

Homer Company developed its business plan based on the assumption that units would sell at a price of \$400 each. The variable costs for each unit were projected at \$200, and the annual fixed costs were budgeted at \$80,000. Homer's after-tax profit objective was \$160,000; the company's effective tax rate is 30%. If no changes are made to the selling price or cost structure, determine the number of units that Homer must sell in order to break even.

- A. 400
- B. 367
- C. 350
- D. 250

**Solution: The correct answer is A.**

Four hundred units must be sold to break even. To find the breakeven point, divide the total fixed cost (\$80,000) by the contribution margin per unit (\$200).

**BEC KeslerQ™ #7:**

Breakeven analysis assumes that which of the following would be constant on a per unit basis?

- I. All variable costs
  - II. Revenue
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is C.**

I and II are correct. Breakeven analysis assumes that all variable costs and revenues are constant on a per unit basis and linear over a relevant range.

**BEC KeslerQ™ #8:**

The operational decision method, referred to as marginal analysis, would NOT be useful when analyzing which of the following business decisions?

- I. Accepting or rejecting special orders
  - II. Making versus buying a product or service
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II



**Solution: The correct answer is D.**

I and II are wrong. Note that this is a NOT question.

The operational decision method, referred to as marginal analysis, *is* used when analyzing business decisions such as acceptance or rejection of special orders and making versus buying a product or service.

**BEC KeslerQ™ #9:**

Which of the following would be found in the operating rather than the financial budget?

- I. Pro forma income statement
  - II. Capital expenditures budget
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is A.**

I is correct. The operating budget process includes the pro forma income statement and all budgets except the cash budget and capital purchases.

II is wrong. The financial budget process includes cash and capital purchases budgets, the budgeted balance sheet, and the statement of cash flows.

**BEC KeslerQ™ #10:**

The risks of not finding a CPA exam mentor to help you on your journey to passing include:

- I. No one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.
- II. No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.
- III. No one to help you study more efficiently. You will spend more time studying and get less results.

- A. I only
- B. II only
- C. II and III only
- D. I, II, and III

**Solution: The correct answer is D.**

If you don't have someone who understands how to pass the CPA exam (or recover from failure)...

You will have no one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.

No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.

No one to help you study more efficiently. You will spend more time studying and get less results.

**This is why Kesler CPA Review was created! To provide you with access to all three.**

**BEC KeslerQ™ #11:**

Mallard Inc. is in the process of preparing its annual budget. The following beginning and ending inventory levels (in units) are planned for the year ending December 31, Year 4:

	<b>Beginning Inventory</b>	<b>Ending Inventory</b>
Raw material	30,000	40,000
Work in process	20,000	20,000
Finished goods	60,000	40,000

Two units of raw material are needed to produce each unit of finished product. If Mallard plans to sell 380,000 units during Year 4, how many units would it have to manufacture during the year?

- A. 400,000 units**
- B. 360,000 units**
- C. 350,000 units**
- D. 325,000 units**

**Solution: The correct answer is B.**

As calculated below, 360,000 units would need to be manufactured during Year 4 to support sales of 380,000 units:

Projected sales (units)	380,000
Desired ending inventory	<u>+40,000</u>
Required units	420,000
Beginning inventory	<u>-60,000</u>
Required units to manufacture	360,000

**BEC KeslerQ™ #12:**

The direct labor efficiency variance:

- I.     could be unfavorable as a result of an unfavorable material usage variance
  - II.    is calculated by using the standard wage rate rather than the actual wage rate
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**



**Solution: The correct answer is C.**

I and II are correct. An unfavorable direct labor efficiency variance could be caused by an unfavorable material usage variance.

Poor quality materials could mean unfavorable material usage and cause inefficient labor usage.

In addition, the actual hours at the standard rate compared to the standard hours at the standard rate is referred to as the direct labor efficiency variance.

**BEC KeslerQ™ #13:**

The cash management technique that focuses on cash disbursements is:

- A. depository transfer checks**
- B. a lockbox system**
- C. zero-balance accounts**
- D. concentration banking**

**Solution: The correct answer is C.**

The zero balance account technique is a cash management technique for cash disbursements whereby, at the end of each day of processing, the bank transfers just enough funds from an entity's master account to cover all checks presented against the zero balance account that day. This allows an entity to maintain higher cash balances in its master account, which can be used for short-term investing.

A is wrong. Depository transfer checks are checks used by a designated collection bank for depositing the daily receipts of an entity from multiple locations.

They are used in connection with concentration banking, which is a cash management technique.

B is wrong. A lockbox system is a cash receipts technique that expedites the funds availability of customer payments received by an entity. It involves having customers remit their payments to a post office box that is managed and maintained by a bank, whose personnel remove envelopes from the mailbox and immediately deposit the check payments in the entity's account. This is a particularly useful technique for entities that do business nationwide.

D is wrong. Concentration banking is a cash receipts technique whereby payments from customers are routed to a firm's local branch offices rather than to the firm's headquarters.

The branch office deposits the checks at a local bank, and then surplus funds are transferred to the firm's primary bank periodically. This technique helps expedite the collection of customer payments.

**BEC KeslerQ™ #14:**

The discounted cash flow model is considered the best for long-term decisions. Which of the following are discounted cash flow methods?

- I. Net present value
- II. Internal rate of return
- III. Profitability index

- A. I, II, and III
- B. I and II
- C. I and III
- D. II and III

**Solution: The correct answer is A.**

I, II, and III are correct. The discounted cash flow model is the best for long-term decisions. Discounted cash flow methods include the net present value, internal rate of return, and profitability index.

The profitability index is most useful when funds are limited and projects must be selected based on highest returns.

**BEC KeslerQ™ #15:**

The risks of not finding a CPA exam accountability partner include:

- I. Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
  - II. Your friends and family will start to resent you for spending more time studying than with them.
  - III. Studying won't be fun. No one to share in your wins for hitting study goals.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**Solution: The correct answer is D.**

There's nothing wrong with it taking a village to pass the CPA exam!

In fact, getting the people in your life involved in the process is crucial to your sanity (and theirs) because....

- 1) Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
- 2) Your friends and family will start to resent you for spending more time studying than with them.
- 3) Studying won't be fun. No one to share in your wins for hitting study goals.

**BEC KeslerQ™ #16:**

Dupree Corp. is evaluating its potential investment in a piece of equipment with a four-year life and no salvage value. The tax rate is 35%. Discounted pretax cash flows are \$399,874, undiscounted after-tax cash flows are \$286,600, and discounted after-tax cash flows are \$237,992.

The company's hurdle rate is 9%, and it anticipates that pretax cash flows in each of the three years will equal 25%, 30%, and 50%, respectively, of the investment's face value. If the investment costs \$244,500, what is the net present value of the investment?

- A. (\$6,508)
- B. \$6,508
- C. (\$42,100)
- D. None of the above



**Solution: The correct answer is A.**

The net present value of an investment is equal to the discounted after-tax cash flows from the investment minus the initial cost of the investment.

In this question, the discounted cash flows are \$237,992 and the investment was \$244,500, yielding a negative (unsatisfactory) net present value of \$6,508.

**BEC KeslerQ™ #17:**

Investments that provide a return that exceeds which of the following should continuously add to the value of the firm?

- I. Internal rate of return
  - II. Weighted average cost of capital (WACC)
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**

**Solution: The correct answer is C.**

I and II are correct. The WACC is frequently used as the hurdle rate within capital budgeting techniques. Investments that provide a return that exceeds the WACC should continuously add value to the firm.

WACC is most commonly compared to the internal rate of return to evaluate whether to make an investment. The internal rate of return is the rate of return that sets cash outflows to cash inflows.

**BEC KeslerQ™ #18:**

Linden Stove Inc. is a manufacturer. The terms of trade are 4/10, net 30 with a particular supplier of raw materials. What is the cost on an annual basis of NOT taking the discount? Assume a 360-day year.

- A. 75.06%**
- B. 18.00%**
- C. 57.07%**
- D. 37.03%**

**Solution: The correct answer is A.**

Annual percentage cost of not taking the discount is equal to 360 divided by the (total pay period minus the discount period) times discount divided by (100% minus discount).

$$360(30-10) \times 4\% (100\% - 4\%)$$

$$= 36020 \times 4\% (96\%)$$

$$= 18 \times 4.17\% = 75.06\%$$

Note that the formula to determine the cost of not paying within the discount period appears above. The formula would be the same if calculating the cost of offering a discount to customers in exchange for their quick payment.

**BEC KeslerQ™ #19:**

Which of the following would NOT be relevant to EOQ?

- I. Purchase price per unit
- II. Annual sales volume

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is A.**

I is correct. The question asked which of the following would *not* be relevant to EOQ. The purchase price per unit is not a component of EOQ but rather the cost per purchase order. II is wrong. Annual sales volume *is* a key variable in the EOQ formula.

The components of the EOQ formula include demand in units for the product, the ordering cost per purchase order, and the carrying cost for one unit.

**BEC KeslerQ™ #20:**

The risks of not finding a CPA exam tutor include:

- I. Spending too much time on research that could be spent better elsewhere.
  - II. Never achieving a grasp of a complex topic that could tank your scores.
  - III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III



**Solution: The correct answer is D.**

I wasted SO much time spinning my wheels trying to figure things out on my own...

Don't make this mistake!

Time is your most precious commodity and you don't have more than 10-15 minutes to spend on any given topic considering the breadth and the depth of what's tested.

This is why outsourcing to CPA exam tutors can be a lifesend!

When you don't have a CPA exam tutor... you risk:

- I. Spending too much time on research that could be spent better elsewhere.
- II. Never achieving a grasp of a complex topic that could tank your scores.
- III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.

**This is why when you are a member of Kesler CPA Review we give you monthly tutor credits for our tutors for your most difficult questions!**

**BEC KeslerQ™ #21:**

For better segregation of duties involving the computer program, which of the following IT jobs is an example of an authorization role that should be segregated from the custody role?

- A. Librarian**
- B. Computer operator**
- C. Programmer**
- D. Systems analyst**

**Solution: The correct answer is D.**

A systems analyst designs the overall application system. The systems analyst is authorized to design the system, and that role should be segregated from the custody of the program, which will belong to the librarian.

A is wrong. The librarian has a custodian role over the program, not an authorization role.

B is wrong. A computer operator has a record-keeping job rather than authorization.

C is wrong. Programmers have a record-keeping function rather than an authorization function.

**BEC KeslerQ™ #22:**

Which of the following is characteristic of business-to-business (B2B) e-commerce?

- I. Decreased inventory levels
  - II. Increased costs for information technology infrastructure
  - III. Increased market efficiency
- 
- A. II and III only**
  - B. I and III only**
  - C. I, II, and III**
  - D. III only**

**Solution: The correct answer is C.**

I, II, and III are correct. Decreased inventory levels, increased costs for informational technology infrastructure, and increase market efficiency are all characteristic of B2B (business-to-business) e-commerce.

B2B e-commerce provides for more effective coordination of delivery of inventory and can, therefore, make better use of inventory.

B2B e-commerce also allows companies to connect directly with suppliers to obtain easy access to price quotes from various suppliers and, consequently, receive better pricing.

Finally, implementing B2B e-commerce does require significant investment in equipment, software, and training.

**BEC KeslerQ™ #23:**

Gross domestic product (GDP) includes:

1. the value of used goods that have been resold
2. foreign-owned factories operating within the United States

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. GDP includes all final goods and services produced by resources within a country regardless of who owns the resources. Final US GDP would include output from a car factory in Detroit whether it's a factory owned by a US car company or a factory owned by a Japanese car company.

I is wrong. GDP includes all final goods and services. Used goods that are resold would be excluded from GDP because they were already counted once when they were final.

**BEC KeslerQ™ #24:**

Which of the following economic cycles is characterized by significant excess production capacity?

- A. Peak**
- B. Trough**
- C. Expansion**
- D. Contraction**



**Solution: The correct answer is B.**

A trough is a low point of economic activity.

Firm profits are at their lowest level, so cost cutting is essential for survival. Since jobs have been cut, demand for products is low and excess capacity would be expected.

**BEC KeslerQ™ #25:**

When demand for a product is unit elastic, which of the following would be correct?

- I. A price increase will decrease total revenue.
- II. A price decrease will increase total revenue.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is D.**

I and II are wrong. When demand for a product is unit elastic, elasticity is equal to 1.

Any price change would be offset by an equal change in demand, so a price increase would be offset by an equal drop in demand, resulting in no change in total revenue. In addition, when demand for a product is unit elastic, elasticity is equal to 1.

Any price change would be offset by an equal change in demand, so a price decrease would be offset by an equal increase in demand, resulting in no change in total revenue.

## **YOU DID IT!**

If you got more than 20+ questions correct then you are well on your way to passing REG



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# TEST YOUR REG MIGHT!

## REG KeslerQ™ #1:

Kleinman bought Series EE US savings bonds. Redemption proceeds from the bonds will be used to pay for the college tuition of his dependent daughter. One of the conditions that must be met for tax exemption of accumulated interest on these bonds is that:

- I. Kleinman must be the sole owner of the bonds (or joint owner with his spouse)
- II. the bonds must have been purchased by Kleinman before Kleinman reached the age of 24
- III. the bonds must be transferred to the college for redemption by the college rather than by Kleinman

- A. I only
- B. II only
- C. I and III only
- D. II and III only

**Solution: The correct answer is A.**

Accumulated interest on Series EE US savings bonds may be exempt from tax but *only if* certain conditions are met:

- (1) the bonds have been issued to the taxpayer after December 31, 1989,
- (2) the bonds must be purchased by the taxpayer or taxpayer's spouse and kept in the taxpayer's name (i.e., the taxpayer must be the sole owner of the bonds or joint owner with his or her spouse),
- (3) the taxpayer (owner) must be 24 years or older before the bond's issue date (i.e., the taxpayer or owner must be 24 years old when purchasing the bonds), and
- (4) redemption proceeds from the bonds must be used to pay for higher education costs (usually college costs) for the taxpayer, taxpayer's spouse, or taxpayer's dependents.

**REG KeslerQ™ #2:**

Jay, a dentist, billed Lou \$600 for dental services. Lou paid Jay \$200 cash for these services and catered a party for Jay's office staff in full settlement of the bill. Lou caters comparable parties for \$350 and makes a profit of approximately \$250 per party.

What amount should Jay include in taxable income as a result of this transaction?

- A. \$200
- B. \$450
- C. \$550
- D. \$600

**Solution: The correct answer is C.**

In performing a service, if a taxpayer receives an asset other than cash, the FMV of the asset received is taxable as ordinary income.

In this case, Jay received \$200 cash plus a catered party that had an FMV of \$350; thus Jay would report \$550 as taxable income from this transaction.

Note that the \$250 that Lou earns as profit on these types of parties does not impact the taxable income attributable to Jay.

\$200 Cash  
\$350 fair value of the party  
\$550 total income

**REG KeslerQ™ #3:**

Rocky owns the following assets: recreational skis and a limousine that is used in her personal limousine service business for transporting passengers to and from airports. Which of these assets should Rocky classify as part of capital assets?

- A. The recreational skis only**
- B. The limousine only**
- C. Both the recreational skis and the limousine**
- D. Neither the recreational skis or the limousine**



**Solution: The correct answer is A.**

Capital assets are assets used for personal enjoyment or held for investment.

Section 1231 assets, on the other hand, include “business assets” used in the business to generate revenue, which are held for more than one year. In the question, the limousine is being used in the limousine service business to transport passengers to and from airports (i.e., it is being used in the business to generate revenues) and therefore would be classified as a Section 1231 asset, not a capital asset.

The recreational skis are assets Rocky is using for personal enjoyment and consequently would be classified as a capital asset.

**REG KeslerQ™ #4:**

Ziga is single with no dependents. He showed a loss on his Schedule C of \$8,000. He has dividend income of \$200 and interest income of \$100. He also has a profit of \$500 from a rental activity on Schedule E. Which is correct?

- I. Because Ziga's income is very low, he should qualify for the earned income credit.
  - II. Ziga's income from rental activities of \$500 is considered passive income.
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is B.**

I is wrong. In order to qualify for earned income credit, the taxpayer must have some earned income. Ziga had income but no earned income, so he would *not* qualify for the earned income credit.

II is correct. The rental income is considered passive income; the interest and dividends are portfolio income. Neither the rental income nor the interest and dividends would qualify Ziga for the earned income credit.

**REG KeslerQ™ #5:**

From a study routine perspective, what is the most effective way to grasp the AICPA Blueprints?

- I. Watch ALL the lectures, read ALL the text and answer ALL the questions without reviewing as you go.
  - II. Focus on moving through the content as fast as possible but also taking time to loop back and review everything you have learned up to that point.
  - III. Spend time figuring out how you learn best so you can determine what study tools are useful and which ones waste your time.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**SOLUTION is C.**

I is incorrect because you don't have time to complete all three of these resources. The CPA Exam is too broad. You need to be laser focused on understanding how you learn best and cut out any study resources that don't help you learn efficiently.

II is CORRECT because if you don't review what's in chapter 1 consistently then you will forget everything you learned by the time you hit your final chapter.

Keep everything in equal focus by performing study loops on a daily/weekly basis.

FUN FACT: Kesler CPA Review has study looping technology built into the platform to ensure you can easily review everything you have learned while also moving forward.

III is CORRECT because if you don't know how you learn best then you risk creating busy work for yourself which holds you back and wastes your time!

This is why finding a mentor to help you with this is crucial.

**REG KeslerQ™ #6:**

Berman, an unmarried taxpayer, qualified to itemize Year 3 deductions. Berman's Year 3 AGI was \$40,000. Berman donated art in Year 3, valued at \$11,000, to a local art museum. Berman had purchased the artwork two years earlier for \$2,000. What was the maximum amount of the charitable contribution allowable as an itemized deduction on Berman's Year 3 income tax return?

- A. \$2,000
- B. \$9,000
- C. \$11,000
- D. \$12,000

**Solution: The correct answer is C.**

Since Berman held the artwork for longer than one year, he is entitled to the full FMV, \$11,000, as a deduction.

The built-in gain of \$9,000 is not taxable. The next step is to compare the \$11,000 deduction to 30% of AGI: \$12,000. The deduction for any long-term capital gain property is limited to 30% of AGI each year.

The deduction for property contributions is not allowed to exceed 30% of AGI.

AGI \$40,000  $\times$  30% limit = \$12,000

Therefore, the \$11,000 charitable deduction is allowed in full.

**REG KeslerQ™ #7:**

During the current year, Pelosi was assessed a deficiency on a prior year's federal income tax return. As a result of this assessment, he was required to pay \$2,750 determined as follows:

Additional federal income tax	\$2,350
Late filing penalty	\$150
Negligence penalty	\$50
Interest on late paid taxes	\$200

What portion of the \$2,750 paid by Pelosi would qualify as an itemized deduction on Schedule A?

- A. \$0
- B. \$200
- C. \$350
- D. \$2,750



**Solution: The correct answer is A.**

Federal income tax is *not* deductible. Penalties and interest related to federal income tax matters are not deductible.

**REG KeslerQ™ #8:**

Under the sales article of the Uniform Commercial Code (UCC), unless otherwise agreed to, the seller's obligation to the buyer is to:

- A. deliver all the goods called for in the contract to a common carrier**
- B. set aside conforming goods for inspection by the buyer before delivery**
- C. hold conforming goods and give the buyer whatever notification is reasonably necessary to enable the buyer to take delivery**
- D. deliver the goods to the buyer's place of business**

**Solution: The correct answer is C.**

Unless the contract calls for delivery, the seller only has to set aside the goods called for in the contract, conforming goods, and hold those goods and give the buyer notification to take his or her own delivery.

**REG KeslerQ™ #9:**

Drake Corp., a calendar-year C (regular) corporation, had the following capital gains and capital losses during Year 5:

Short-term capital gain \$7,500

Short-term capital loss \$5,000

Long-term capital gain \$2,500

Long-term capital loss \$2,500

In addition, Drake realized taxable income of \$56,000 from its regular business operations for calendar Year 5. What is Drake Corp.'s total taxable income for Year 5?

- A. \$56,000**
- B. \$62,000**
- C. \$60,500**
- D. \$58,500**

**Solution: The correct answer is D.**

The net capital gains of \$2,500 are added to taxable income from operations of \$56,000 to determine total taxable income of \$58,500. There is no difference in the tax rates for capital gains, unlike an individual. Drake Corp. must first net its capital transactions together as follows: the net capital gain simply gets added to the ordinary income of \$56,000.

Total capital gains of \$10,000 (\$7,500 short-term capital gain + \$2,500 long-term capital gain) – capital losses of \$7,500 (\$5,000 short-term capital loss + \$2,500 long-term capital loss) = \$2,500 net capital gain

**REG KeslerQ™ #10:**

The risks of not finding a CPA exam mentor to help you on your journey to passing include:

- I. No one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.
- II. No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.
- III. No one to help you study more efficiently. You will spend more time studying and get less results.

- A. I only
- B. II only
- C. II and III only
- D. I, II, and III

**Solution: The correct answer is D.**

If you don't have someone who understands how to pass the CPA exam (or recover from failure)...

You will have no one to tell you if you are making rookie mistakes that could tank your scores. You don't know what you don't know.

No one to coach you on how to recover from failure or what to do when the going gets tough. Someone who has been there and done that.

No one to help you study more efficiently. You will spend more time studying and get less results.

**This is why Kesler CPA Review was created! To provide you with access to all three.**

**REG KeslerQ™ #11:**

Which of the following items are reportable on a corporation's Schedule M-1 book to taxable income reconciliation?

- I. Interest expense on a loan to carry US savings bonds
  - II. State income tax provision
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**



**Solution: The correct answer is D.**

An item only makes the M-1 reconciliation if it's treated differently for tax purposes and book purposes. Interest on US savings bonds is considered income for both books and taxes.

State income tax is an expense on the books *and* a deduction for taxes. State income tax expense on the books is a tax deduction, but federal income tax expense on the books is not a tax deduction.

**REG KeslerQ™ #12:**

If NOT expressly granted, which of the following implied powers would a trustee have?

- I. Power to sell trust property
- II. Power to borrow from the trust
- III. Power to pay trust expenses

- A. I and III only**
- B. I and II only**
- C. II and III only**
- D. I, II, and III**

**Solution: The correct answer is A.**

I is correct. The trustee has the power to sell trust property. A trustee is a fiduciary who has the duty to manage the trust and carry out the trust purpose according to its terms.

III is correct. The trustee has the power to pay trust expenses. The trustee must use his or her own skill, prudence, and judgment as a reasonable person would in making trust decisions and must abide by the trust instrument.

II is wrong. The trustee does not have the implied power to borrow from the trust. Trustees may not profit personally from the role as trustee other than to receive whatever compensation is called for. Trustees cannot commingle personal assets with that of the trust.

**REG KeslerQ™ #13:**

Which of the following is correct regarding uniform capitalization rules?

- I. Officers' compensation NOT attributed to production would be expensed even if a company were subject to uniform capitalization.
  - II. Service companies, like accounting and law firms, are NOT subject to uniform capitalization.
- 
- A. I only
  - B. II only
  - C. Both I and II
  - D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. A company subject to uniform capitalization rules would still be able to expense officers' compensation that is *not* attributed to production.

II is correct. Service companies, like accounting and law firms, are *not* subject to uniform capitalization rules.

Companies would be subject to uniform capitalization if their average sales of inventory exceed \$10,000,000 over a three-year period.

**REG KeslerQ™ #14:**

Contracts made under which of the following conditions are voidable?

- I. Duress
- II. Undue influence

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. Duress involves threatening someone and physically forcing that person to enter a contract against his or her will. Duress would result in a voidable agreement.

II is correct. Undue influence involves using one's position to take unfair advantage of a person in a close personal relationship. Lawyers and accountants could easily influence an individual into making a contract that they would otherwise not make.

In addition to fraud and unilateral mistake, duress and undue influence are two additional situations where someone would have a defense and could back out of a contract.

**REG KeslerQ™ #15:**

The risks of not finding a CPA exam accountability partner include:

- II. Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
  - III. Your friends and family will start to resent you for spending more time studying than with them.
  - IV. Studying won't be fun. No one to share in your wins for hitting study goals.
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III



**Solution: The correct answer is D.**

There's nothing wrong with it taking a village to pass the CPA exam!

In fact, getting the people in your life involved in the process is crucial to your sanity (and theirs) because....

- 1) Studying in isolation without anyone checking in on you or helping you stay on track which can lead to loss of motivation and CPA exam depression.
- 2) Your friends and family will start to resent you for spending more time studying than with them.
- 3) Studying won't be fun. No one to share in your wins for hitting study goals.

**REG KeslerQ™ #16:**

Under the sales article of the UCC, a firm offer will be created only if the:

- I. offeree and offeror are both merchants
  - II. offeree gives some form of consideration
  - III. offer is made by a merchant in a signed writing
- 
- A. I, II, and III**
  - B. I and III only**
  - C. II and III only**
  - D. III only**

**Solution: The correct answer is D.**

III is correct. A firm offer must be in writing, for the sale of goods, and signed by a merchant. The firm offer must contain some assurance that the offer will be held open.

I is wrong. Under the sales article of the UCC, a firm offer will be created only if the offeror is a merchant. The offeree need not be a merchant for the offeror to create a firm offer.

II is wrong. Under the sales article of the UCC, a firm offer does *not* require consideration to be given in exchange for the irrevocable offer.

Note that this is different than the option contract under the common law that did require consideration to be exchanged. The option contract requires consideration; the firm offer does not.

**REG KeslerQ™ #17:**

Under the UCC, risk of loss passes to the buyer:

- A. when the goods are delivered to the carrier if the terms are FOB destination**
- B. when the goods are placed on the seller's loading dock if the terms are FOB destination**
- C. when the goods are placed on the seller's loading dock if the terms are FOB shipping point**
- D. when the goods are delivered to the carrier if the terms are FOB shipping point**

**Solution: The correct answer is D.**

Under the UCC, risk of loss passes to the buyer when the goods are delivered to the carrier if the terms are FOB shipping point. In FOB shipping point, the seller is responsible only until the goods are delivered to the carrier.

**REG KeslerQ™ #18:**

Which of the following is correct regarding a written contract for the sale of goods in order for the agreement to be enforceable under the UCC?

- I. The written contract must contain the quantity of the goods to be sold.
  - II. The written contract must contain the signature of the party seeking to enforce the contract.
- 
- A. I only**
  - B. II only**
  - C. Both I and II**
  - D. Neither I nor II**

**Solution: The correct answer is A.**

I is correct. In a written contract under the UCC, the quantity is considered material to the contract and cannot be left open. Price would be allowed open but not quantity.

II is wrong. To enforce a written contract against another party, the written contract must contain the signature of the party against whom enforcement is sought. If A wanted to hold B liable on a written contract, A would need to show the court B's signature.

If A signed the contract but B didn't, that would not help A seeking to enforce the contract.

**REG KeslerQ™ #19:**

Under the UCC governing transactions involving debtor/creditor relationships, which of the following is correct regarding the attachment of the security interest?

- I. The security interest is enforceable once the security agreement has been signed.
- II. The security interest is intended to give the creditor rights against the debtor in the event of default.

- A. I only**
- B. II only**
- C. Both I and II**
- D. Neither I nor II**



**Solution: The correct answer is B.**

I is wrong. A security interest is *not* enforceable until the debtor has rights in the collateral. For a security interest to attach and be enforceable, there is often a written security agreement between the debtor and creditor.

In the case of a consumer purchasing a car, the written security agreement is signed by the debtor at the dealership but is not enforceable until the debtor has the keys to the car.

For example, if the security agreement is signed Saturday night at the dealership but the car is not delivered to the debtor until Monday morning, the security interest is not enforceable until Monday morning when the debtor gets behind the wheel.

In this example, the CPA exam will ask which day attachment took place: Saturday night at the dealership when the security agreement was signed or Monday when the debtor had the rights to the car.

The answer is that attachment took place Monday when the debtor got the car—the creditor would then have attachment of a nonpossessory security interest.

The UCC considers the creditor's security interest to be nonpossessory in this example since the creditor is *not* in possession of the car during the term of the security interest.

II is correct. In case of default, the security agreement allows the creditor to repossess the car and sell it to apply proceeds to satisfy the debt. In this way, the creditor has rights against the debtor.

The term that describes the creditor's rights against the debtor is *attachment*.

**REG KeslerQ™ #20:**

The risks of not finding a CPA exam tutor include:

- I. Spending too much time on research that could be spent better elsewhere.
  - II. Never achieving a grasp of a complex topic that could tank your scores.
  - III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.
- 
- A. I only
  - B. II only
  - C. II and III only
  - D. I, II, and III

**Solution: The correct answer is D.**

I wasted SO much time spinning my wheels trying to figure things out on my own...

Don't make this mistake!

Time is your most precious commodity and you don't have more than 10-15 minutes to spend on any given topic considering the breadth and the depth of what's tested.

This is why outsourcing to CPA exam tutors can be a lifesend!

When you don't have a CPA exam tutor... you risk:

- I. Spending too much time on research that could be spent better elsewhere.
- II. Never achieving a grasp of a complex topic that could tank your scores.
- III. Having to deal with multiple day lead times waiting to hear back from your CPA review course.

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**REG KeslerQ™ #21:**

If a CPA is found to have breached a duty of professional care and competence by lacking reasonable care in the conduct of the engagement, which of the following will the CPA most likely be sued for?

- A. Gross negligence**
- B. Ordinary negligence**
- C. Constructive fraud**
- D. Actual or common law fraud**

**Solution: The correct answer is B.**

The CPA will likely be sued for negligence. When a CPA lacks professional care and competence during the course of the engagement, the CPA has committed negligence.

A and C are wrong. For the injured party to prove that the CPA acted with gross negligence and therefore committed constructive fraud would mean that the CPA would have acted “recklessly” with regard to the rights of others, and there was no indication that the CPA acted “recklessly” in the question.

D is wrong. Actual or common law fraud would have required the injured party to prove that the CPA acted with scienter or bad faith, that is, with intent to deceive or cheat. There was no indication of that in the facts.

**REG KeslerQ™ #22:**

Lucas owns 200 shares of Shea Corp. cumulative preferred stock. In the absence of any specific contrary provisions in Shea's articles of incorporation, which of the following statements is correct?

- A. If Shea declares a dividend on its common stock, Lucas will be entitled to participate with the common stock shareholders in any dividend distribution made after preferred dividends are paid.**
- B. Lucas will be entitled to vote if dividend payments are in arrears.**
- C. Lucas is entitled to convert the 200 shares of preferred stock to a like number of shares of common stock.**
- D. If Shea declares a cash dividend on its preferred stock, Lucas becomes an unsecured creditor of Shea.**

**Solution: The correct answer is D.**

Once a dividend is duly declared by the board of directors, the stockholders become unsecured creditors of the corporation. Thus once Shea declares a cash dividend, Lucas became an unsecured creditor of Shea.

C is wrong. A preferred stockholder is not entitled to convert preferred stock into common stock unless this right is specifically authorized.

A is wrong. Lucas is a holder of cumulative preferred stock, not participating preferred stock. Only participating preferred stock shareholders may participate with common stock shareholders on dividend distributions.

B is wrong. Cumulative preferred stock is usually nonvoting stock. Whether voting or nonvoting depends on the stock, not on whether dividend payments are in arrears.

**REG KeslerQ™ #23:**

Larry, an employee of Hanson Manufacturing, Inc., was injured in the course of employment while operating a forklift manufactured and sold to Hanson by Suzy Wong, Inc. Under the state's mandatory workers' compensation statute, Larry will be successful in obtaining:

- I. workers' compensation even if Larry was negligent
- II. legal action against Hanson, Inc.
- III. legal action against Suzy Wong, Inc.

- A. I and III
- B. I, II, and III
- C. II and III
- D. I and II



**Solution: The correct answer is A.**

I is correct. Workers' compensation is available even if the employee is negligent. III is correct. A negligence action could be brought against Suzy Wong, Inc., if Suzy Wong, Inc., were determined to be a third-party manufacturer of faulty equipment.

II is incorrect. No negligence action can be brought against Hanson, the employer, since the employer carries the workers' compensation policy and the employee can immediately collect on the policy (even if the employee was negligent).

**REG KeslerQ™ #24:**

Nonqualified stock options are granted to employees on February 3, Year 1. Ordinary income is paid by the employees based on the options having a readily ascertainable value. Which of the following is correct?

- I. If the options are exercised, the holding period for the shares begins with the date the options are granted.
- II. If the options expire without being exercised, the employees have a capital loss based on the ordinary income already recognized.

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is B.**

II is correct. If the employee allows the options to lapse (not exercised), there is a capital loss based on the value of the options previously taxed. If there is a readily ascertainable value, the employee recognizes ordinary income in that amount in the year granted.

If there is a cost to the employee, then the ordinary income is the value of the option minus the cost. If the options lapse, that amount previously recognized can be taken as a capital loss.

I is wrong. If the options are exercised, the holding period begins with the exercise date, not the grant date.

**REG KeslerQ™ #25:**

Assessment of the \$100 preparer penalty for failure to employ due diligence in connection with the earned income credit applies to:

- I. determining the client's eligibility for the earned income credit
- II. determining the amount of the client's earned income credit

- A. I only
- B. II only
- C. Both I and II
- D. Neither I nor II

**Solution: The correct answer is C.**

I is correct. A penalty of \$100 may be assessed to the tax preparer who fails to be diligent with regard to whether the client is eligible for the earned income credit.

The earned income credit has been widely abused for decades, and in recent years, the IRS has enlisted the tax preparer as something of a gatekeeper. The tax preparer must fill out a checklist that includes computational worksheets, with the goal of determining whether the client is eligible for the earned income credit.

II is correct. A penalty of \$100 may be assessed to the tax preparer who fails to be diligent with regard to the amount of the client's earned income credit. The requirements for due diligence with respect to the earned income credit include eligibility checklists, computational worksheets, record retention, and inquiry of the taxpayer.

The penalty for failure to be diligent will not apply if the tax return preparer can demonstrate that the preparer's normal office procedures were reasonably designed and routinely followed to ensure due diligence compliance and the failure to meet the due diligence requirements was isolated and inadvertent.

## **YOU DID IT!**

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