Examination Questions: Accounting Theory, Friday Afternoon, November 17, 1933

Michigan State Board of Accountancy
Question 1:
What is the difference between repairs, maintenance and renewals? What method should be followed in handling these items on the books of account?

Question 2:
In some lines of business, where containers used are of sufficient value, the customers are charged a deposit until the container is returned. How should the "containers-out" and the corresponding liability account be shown on a balance sheet?

Question 3:
A piece of business property was improved by a building set up by the lessee under a long-term lease. Under such lease, the building becomes the property of the lessor at the expiration of the lease. How should the building be handled on the books of the lessor (a) during the life of the lease and (b) after the expiration of the lease?

Question 4:
In order to secure industries in a certain town, the local chamber of commerce offers to donate a parcel of land to any new business if, after a period of five years, it had met certain conditions relative to annual payroll, improvement of property, and so forth, title to remain in the donor until the conditions had been met. How would you treat this item on your balance sheet (a) during the five-year period, and (b) after the conditions had been met? Would your answer be the same if title had passed to the company immediately?

Question 5:
In August, 1929, the Krakow Manufacturing Company had its plant appraised in connection with the flotation of a first-mortgage-bond issue. The
balance sheet submitted by the auditors incorporated the appraised values, showing reproduction cost new less accrued depreciation. Appreciation surplus of $263,575.00 resulted from taking up the appraised value. Depreciation charged to operations in subsequent periods was based upon appraised values; profit or loss on the disposition of assets acquired prior to the appraisal was also based on appraised values. No change was made in the appraisal surplus, the amount remaining at $263,575.00 on December 31, 1932.

What comments or criticisms have you to make on the procedure followed?

Question 6:

A newly organized corporation conducts an extensive advertising campaign through the mediums of newspapers, billboards and magazines. The management of the company believes that the current period should not stand the full cost of the advertising in view of the fact that the benefits in the way of future sales would not be received until later. Discuss the points involved and what you would consider to be the proper method of handling advertising expenditures. Would your answer be different if the company was a well-established concern and used its advertising campaigns to maintain its sales position?

Question 7:

A company having branches throughout the country follows the practice of shipping merchandise to warehouses from which its branches may withdraw stock as sales are made. Accounts in the receivables ledger are maintained with each branch which are charged at selling price with all merchandise shipped to the various warehouses, in order that an adequate record of the location of all merchandise can be kept. What criticisms and what recommendations would you make with regard to this procedure?

Question 8:

In auditing the books and records of the Starr Company, a distributor of radio products, for the fiscal year ending July 31, 1933, you find that certain radios were properly valued in the closing inventory at the then catalog price of the manufacturer, less discounts. However, in August, 1933, the entire stock of this particular model was sold outright for $10,000.00 less than the inventory price.

(a) Assume that the management knew at July 31 that the stock was to be sold at less than the inventory price. How would you reflect this information in the balance sheet?

(b) Would your answer be different if these facts were not known to the management until August, 1933?
Question 9:
In what manner should profits from the sale of capital assets be recorded on the books of account and in financial statements?

Question 10:
Certain states now permit the payment of dividends to preferred shareholders from paid-in surplus without special authority therefor from the stockholders. Give reasons why you believe this policy to be either wise or bad.

Question 11:
Many of the corporate laws of the larger states now permit a corporation to purchase its own shares and hold them for resale, provided the cost of such purchases does not exceed earned surplus. The statutes of one State, California, require such purchases to be charged to earned surplus account. In preparing the balance sheet of a corporation domiciled in any of these states, how would you display the item of treasury stock?

Question 12:
A company in its earlier years has suffered losses from operation. Commencing with the year 1932, however, it made a large profit, although such profit was not large enough to absorb the previously existing losses. In your opinion, would it be proper to declare a dividend to stockholders from the profits of 1932?