Test Bank for Advanced Accounting in Canada CDN 2nd Johnstone

Advanced Financial Accounting in Canada, 2Ce **(Johnstone)**
Chapter 1 Introduction to Advanced Financial Accounting

1.1 Describe the accounting standards used in Canada and how they apply to different reporting entities.

1) A private company in Canada that is closely held, has no debt, and wants to simplify the accounting process is most likely to report under which part of the *CPA Canada Handbook*?
A) Part II — Accounting Standards for Private Enterprises (ASPE)
B) Part IV — Accounting Standards for Pensions
C) Part I — International Financial Reporting Standards (IFRS)
D) Part III — Accounting Standards for Not-for-Profit Organizations
Answer: A
Diff: 1 Type: MC
Taxonomy Category: Understanding
Learning Outcome: 1.1 Describe the accounting standards used in Canada and how they apply to different reporting entities.

2) In Canada, a private company has the choice to report under International Financial Reporting Standards (IFRS) or Accounting Standards for Private Enterprises (ASPE). Describe why the *CPA Canada Handbook* provides the option for private enterprises.
Answer: IFRS is meant to create consistency and comparability in international markets. One of the limitations of IFRS is the complexity of reporting for equity investments that are meant to provide information to shareholders for decision-making purposes. Many private companies are held by a small group of shareholders who are often involved in the running of the business or have access to that information. As a result, the cost of applying more complex accounting policies outweighs the benefit of the information provided to this closely held group of shareholders. To address this, the Accounting Standards Board developed the Accounting Standards for Private Enterprises to meet the needs of private enterprises. Private enterprises have the option to adopt IFRS or ASPE depending on the needs of the financial statement users.
Diff: 2 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.1 Describe the accounting standards used in Canada and how they apply to different reporting entities.

3) What are the four parts of the *CPA Canada Handbook* — Accounting and which entities are they applicable to?
Answer: The four parts are:
- Part I — International Financial Reporting Standards (IFRS) — applicable to publicly accountable, private, or not-for-profit entities.
- Part II — Accounting Standards for Private Enterprises (ASPE) — applicable to private entities.
- Part III — Accounting Standards for Not-for-Profit Organizations — applicable to not-for-profit entities.
- Part IV — Accounting Standards for Pension Plans — applicable to pension plans.

Diff: 1 Type: ES
Taxonomy Category: Remembering
Learning Outcome: 1.1 Describe the accounting standards used in Canada and how they apply to different reporting entities.

4) In 2011, Canada adopted International Financial Reporting Standards (IFRS) for publicly accountable enterprises. Explain the rationale for adopting IFRS in Canada.
Answer: As the global economy expanded, the Accounting Standards Board (AcSB) chose to adopt IFRS in Canada to improve consistency and comparability in the international capital markets.
Diff: 1 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.1 Describe the accounting standards used in Canada and how they apply to different reporting entities.

1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

1) Laliberte Products Ltd. (LPL), a public company, made several equity investments in the current year. Which of the following investments would most likely be classified as an associate in LPL's financial statements?
A) 25,000 of the 30,000 outstanding voting common shares of Glabman Inc. There are significant intercompany transactions between the two companies.
B) 13,500 of the 45,000 outstanding voting common shares of CCL Ltd. There are significant intercompany transactions between the two companies.
C) 1,000 of the 20,000 outstanding voting common shares of Petruck Inc. There are no transactions between the two corporations and LPL plans to hold these shares for less than a year.
D) 3,000 of the 3,500 outstanding non-voting preferred shares of Paradise Ltd. There is a small number of intercompany transactions between the two companies.
Answer: B
Diff: 2 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

2) Which of the following is NOT an indicator of significant influence?
A) There are significant intercompany transactions between the investor and investee.
B) The investor has the ability to shape the policies of the investee.
C) The investor and investee are located in the same city and use the same legal firm.
D) The ability to choose representation on the investee's board of directors or governing body.
Answer: C
Diff: 1 Type: MC
Taxonomy Category: Understanding
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

3) Kemi Inc., a public company following IFRS, owns 25% of the voting shares of Eunji Ltd. The next largest shareholder owns 15% of the voting shares. Kemi Inc. has some intercompany transactions with Eunji Ltd. and has the ability to elect one of the five members of the board of directors. Which of the following statements best describes how Kemi Inc. should account for its investment in Eunji Ltd.?
A) Kemi Inc. should classify Eunji Ltd. as an associate and use proportionate consolidation to account for its investment.
B) Kemi Inc. should classify Eunji as a passive investment and account for the investment using the equity method to account for its investment.
C) Kemi Inc. controls Eunji Ltd. and should use the consolidation method to account for its investment.
D) Kemi Inc. should classify Eunji Ltd. as an associate and use the equity method to account for its investment.
Answer: D
Diff: 3 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

4) Which of the following investments in equity investments held by MajaCo (MC) would NOT be classified as a subsidiary?
A) MC owns 49% of the voting shares of DeltaCo (DC). No other investor owns more than 2% of the remaining voting shares.
B) MC owns 50% of the voting shares of Epsilon Ltd. (EL). JakovCo owns the other 50% of the voting shares. The two companies agree that they will participate equally in the running of EL.
C) MC owns 75% of the voting shares of TC Inc.
D) MC owns 45% of the voting shares of FishelCo. A wholly owned subsidiary of MC owns 25% of the voting shares of FishelCo. The remaining shares are widely held.
Answer: B
Diff: 3 Type: MC
Taxonomy Category: Evaluating
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

5) Which of the following factors is NOT an indication of an investor having significant influence over an investee?
A) Ownership of 19% of the voting shares of ABC Corporation, where the remaining voting shares are owned by a husband and wife
B) The ability to elect two members of a seven-member board of directors
C) Significant intercompany transactions between the investor and investee
D) The ability to participate in the shaping of the policies of an investee
Answer: A
Diff: 2 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

6) In the current year, AcqCo Ltd., a private company reporting under ASPE, purchased 42% of the voting shares of Woodward Inc. The remaining 58% of the voting shares are held by the original founder and her immediate family. To date, the family has elected all of the board members, and AcqCo Ltd. has not been able to obtain a seat on the board of directors.

AcqCo Ltd. does not have any intercompany transactions with Woodward Inc. nor is there any exchange of management or technology. How should AcqCo Ltd. classify its investment in Woodward Inc.?
A) Subsidiary
B) Associate
C) Passive investment with the option to classify as a fair value through other comprehensive income or fair value through profit and loss
D) Passive investment with the option to classify the investment as a fair value through profit and loss or as a cost investment
Answer: D
Diff: 2 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

7) ABC Corporation Inc. (ABC) owns 60% of the voting common shares of Reich Corporation Ltd. (RCL), while TieCo owns 25%, and Platinum Inc. (PI) owns the remaining 15%. ABC has significant intercompany transactions with RCL. TieCo and PI have no intercompany transactions with RCL. ABC appoints eight of RCL's 10 board members; TieCo and PI each appoint one board member. Which of the following statements is TRUE?
A) TieCo has significant influence over RCL.
B) TieCo and PI have significant influence over RCL.
C) TieCo has no influence over RCL and should classify their investment in RCL as a passive investment.
D) ABC should classify its investment in RCL as an associate since it does not have control of RCL.
Answer: C
Diff: 2 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

8) Below is a list of the shareholders holding voting common shares in Karam Co.:

Kayman Corporation — 45%
Peng Ltd. — 40%
Povhe Inc. — 15%

Kayman Corporation and Peng Ltd. each have 2 seats on the five-person board of directors. Peng Ltd. has significant intercompany transactions with Karam Co. All of the companies report under IFRS. Which of the following statements is TRUE?
A) Kayman Corporation controls Karam Co and should classify its investment as a subsidiary.
B) Peng Ltd. has significant influence and should classify its investment as an associate.
C) Peng Ltd. should classify their investment as a passive investment.
D) Peng Ltd. controls Karam Co and should classify its investment as a subsidiary.
Answer: B
Diff: 3 Type: MC
Taxonomy Category: Analyzing
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

9) What is the definition of control provided in IFRS 10?
Answer: IFRS 10 states that an investor has control only when all of the following three criteria are met: The power over the investee, exposure to the variable returns of the investee, and the ability to use that power to affect the earnings of the investee. First, the power to direct the relevant activities over the investee typically arises from a right such as voting rights, the right to choose key personnel or enforcement/veto rights. Power over the relevant activities would include the ability to direct the selling or buying of goods and services, direct research and development, budgeting, and the management of financial assets. Second, variable returns are defined as not fixed and with the potential to vary as a result of the performance of the investee. Finally, there must be a link between the power to control the relevant activities and the return on the investment.
Diff: 2 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

10) List the four different classifications of investments and provide a definition for each type of investment classification.
Answer: The four classifications along with a definition are given below:
1. Passive Investment is an equity investment that does not meet the definition of an associate (significant influence under ASPE), joint arrangement, or subsidiary. These investments tend to be more short term and temporary in nature. These can be classified as fair value through other comprehensive income, fair value through profit and loss, and in some rare cases, cost.
2. Associate (Significant Influence under ASPE) is an equity investment where the investor has the ability to influence the activities of the investee but does not have control.
3. Joint Arrangement is a contractual agreement where the parties have joint control over the investment. These can be classified as either joint ventures or joint operations.
4. Subsidiary is an equity investment where the investor has the ability to control the activities of the investee.
Diff: 2 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

11) What is a financial asset? Would a non-strategic equity investment be included in this definition?
Answer: A financial asset, as defined in IAS 32, is any of the following:
- Cash
- An equity investment in another company
- A contractual right to receive cash or another asset from another company
- A contractual right to exchange another financial instrument under potentially favourable conditions

Investments in equities are listed in the definition of a financial asset; therefore, a non-strategic equity investment would meet the definition.
Diff: 2 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

12) What factors may indicate that an investor has significant influence over an investee?
Answer: IAS 28 defines significant influence as the ability to participate in or influence the operating, investing, and financial policy decisions of the investee. This means that the investor can play a role in the income-earning process. IAS 28, paragraph 6 provides additional guidance in determining the ability to influence the activities of the investee as:
- The ability to choose some representation on the investee's board of directors.
- The ability to participate in shaping the policies of the investee.
- Significant intercompany transactions between the investee and investor. The definition of significant intercompany transactions requires professional judgment.
- The loaning of management personnel to the investee.
- The investor holds essential technical knowledge, patented technology, or processes needed by the investee.

Diff: 2 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.2 Define, identify, and classify strategic and non-strategic intercorporate investments made by reporting entities.

1.3 Compare the classification requirements for intercorporate investments of International Financial Reporting Standards (IFRS) and Accounting Standards for Private Enterprises (ASPE).

1) Which of the following statements is TRUE?
A) A company reporting under ASPE has two options for reporting non-strategic investments: fair value through profit and loss (FVTPL) and fair value through other comprehensive income (FVOCI).
B) When a company reports under IFRS, the default category for non-strategic investments is FVOCI.
C) For strategic investments where an investor has influence but not control, the terminology is different between IFRS and ASPE. IFRS uses the term "significant influence" while ASPE uses the term "associate."
D) The starting point for determining whether influence exists or not is the same under IFRS and ASPE. Both IFRS and ASPE start with the threshold of owning at least 20% of the voting interest while considering other factors.
Answer: D
Diff: 1 Type: MC
Taxonomy Category: Understanding
Learning Outcome: 1.3 Compare the classification requirements for intercorporate investments of International Financial Reporting Standards (IFRS) and Accounting Standards for Private Enterprises (ASPE).

2) In Canada, a private profit-oriented corporation may report under International Financial Reporting Standards (IFRS) or Accounting Standards for Private Enterprises (ASPE). Explain the rationale for having the option, and how the investment classification would differ.
Answer: Accounting for equity investments can be more complex when reporting under IFRS than when reporting under ASPE. The reason for offering ASPE to private companies is to remove some of those complexities for closely held organizations and their financial statement users. When a company is closely held, the owners tend to be more involved with the running of the entity and therefore have access to the inner working of the business. The following are differences in the classification of equity investments under IFRS and ASPE:

Passive investments:
Companies reporting under IFRS have three options to classify a passive investment: FVTPL, FVOCI, and Cost.
Companies reporting under ASPE have two options for classifying passive investments: FVTPL and Cost. Other comprehensive income does not exist under ASPE.

Strategic investments:
A) Investments where the acquirer has significant influence:
Companies reporting under IFRS classify these investments as associates, whereas companies reporting under ASPE would classify their investment as a significant influence investment. Similar factors are used to determine the classification of an investment.
B) Investments where the acquirer has control:
Companies reporting under IFRS and ASPE both classify an investment under their control as a subsidiary. Similar factors are used to determine the classification of an investment.
Diff: 1 Type: ES
Taxonomy Category: Understanding
Learning Outcome: 1.3 Compare the classification requirements for intercorporate investments of International Financial Reporting Standards (IFRS) and Accounting Standards for Private Enterprises (ASPE).