

FINANCIAL ACCOUNTING AND REPORTING-CPA PRACTICE EXAM (SAMPLE) STUDY GUIDE



Prepare with structure. Pass with confidence



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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 – 45 minutes). Review a handful of questions, reflect on the explanations.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning. Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly, adapt the tips above to fit your pace and learning style. You've got this!

Questions

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- 1. Which of the following is NOT a common type of derivative?**
 - A. Options Contract
 - B. Stock Contract
 - C. Futures Contract
 - D. Swap Contract

- 2. When is a loss contingency considered "reasonably possible"?**
 - A. It is expected to definitely occur.
 - B. It may occur but probably will not.
 - C. It is certain to occur in the near future.
 - D. It is remote and unlikely to happen.

- 3. Which of the following is NOT considered a Legal Entity under the VIE standards?**
 - A. A corporation
 - B. A partnership
 - C. A nonprofit organization
 - D. An LLC

- 4. How should Norina Co. classify its marketable securities and report unrealized gains?**
 - A. Classified as trading; gains are reported as part of income from operations.
 - B. Classified as available-for-sale; gains are recognized in current earnings.
 - C. Classified as trading; losses are reported in other comprehensive income.
 - D. Classified as available-for-sale; gains reported as separate component of OCI.

- 5. In a Troubled Debt Restructuring, what financial measurement represents the difference between the carrying amount of the payable and the fair value of the asset transferred?**
 - A. Loss on extinguishment of debt
 - B. Gain on extinguishment of debt
 - C. Interest Expense
 - D. Modification Gain

- 6. What kind of expense is recognized when a creditor receives assets/equity for a Troubled Debt?**
- A. Administrative Expense
 - B. Bad Debt Expense
 - C. Operational Expense
 - D. Interest Expense
- 7. Which term is used to describe a promise by a corporation to pay bondholders a specific sum at maturity?**
- A. Loan contract
 - B. Bond indenture
 - C. Bond covenant
 - D. Bond agreement
- 8. What is the liability recognized by the lessor for refundable security deposits?**
- A. Reported as a receivable until refunded
 - B. Recognized as revenue immediately
 - C. Classified as a liability until returned
 - D. Not recorded in financial statements
- 9. How is the discount on bonds amortized?**
- A. Equally over the life of the bond
 - B. It represents additional payments to investors at issuance
 - C. It increases reported cash payments at maturity
 - D. It increases interest expense each period
- 10. How is the amortization calculated for the straight-line method?**
- A. By multiplying the coupon rate by the bond face value.
 - B. By dividing the premium or discount by the number of periods.
 - C. By adding bond issuance costs to the recorded interest expense.
 - D. By determining the market rate at issuance.

Answers

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1. B
2. B
3. C
4. D
5. B
6. B
7. B
8. C
9. D
10. B

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Explanations

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1. Which of the following is NOT a common type of derivative?

- A. Options Contract
- B. Stock Contract**
- C. Futures Contract
- D. Swap Contract

In the realm of financial derivatives, common types include options contracts, futures contracts, and swap contracts. Each of these serves specific purposes in risk management and investment strategies. An options contract provides the purchaser the right, but not the obligation, to buy or sell an underlying asset at a predetermined price before a certain date. This flexibility allows investors to hedge or speculate based on anticipated price movements. A futures contract obligates the parties to buy or sell an asset at a predetermined future date and price. Futures are standardized and traded on exchanges, allowing for liquidity and effective price discovery. A swap contract involves the exchange of cash flows or liabilities between two parties, typically related to interest rates, currency, or commodities. Swaps are often used to manage exposure to fluctuations in interest rates and currencies. In contrast, a stock contract is not a standard derivative type. While one can create contracts based on stocks, such as options on stock or futures on stock indexes, stock contracts themselves do not represent a derivative financial instrument with specific underlying mechanisms like the recognized categories mentioned. This distinction is significant in financial reporting and accounting, as derivatives must meet specific definitions and characteristics as defined by accounting standards.

2. When is a loss contingency considered "reasonably possible"?

- A. It is expected to definitely occur.
- B. It may occur but probably will not.**
- C. It is certain to occur in the near future.
- D. It is remote and unlikely to happen.

A loss contingency is considered "reasonably possible" when the likelihood of occurrence is more than remote but less than probable. This means that there is a chance that the event may occur, but it's not expected to happen with a high degree of certainty. Specifically, this term is used within the context of accounting to help determine how to report potential losses stemming from events like lawsuits or warranty claims. In accounting standards, "reasonably possible" implies that while the event is not guaranteed to happen, there is a higher chance of it occurring than it being completely unlikely. This helps organizations prepare for potential future losses that are not inevitable, allowing for more prudent financial planning and reporting. The distinction is essential to ensure that financial statements accurately reflect the risks associated with the organization's operations.

3. Which of the following is NOT considered a Legal Entity under the VIE standards?

- A. A corporation
- B. A partnership
- C. A nonprofit organization**
- D. An LLC

Under the Variable Interest Entity (VIE) standards, a legal entity is defined based on its ownership structure and characteristics that affect its financial reporting and consolidation. Corporations, partnerships, and limited liability companies (LLCs) are all recognized as legal entities since they can own assets, incur liabilities, and enter into contracts in their own names, independently of their stakeholders. Nonprofit organizations, while often considered entities, typically do not operate with profit motives and can have different reporting requirements. The legal structure of a nonprofit organization does not align with the characteristics required to classify it specifically under the same VIE criteria as the for-profit entities mentioned. Therefore, nonprofits are generally not treated as legal entities under VIE standards in the same manner as for-profit entities, which is why this choice stands out as the correct answer. The focus here is that the essence of VIE standards is rooted in the consolidation and financial reporting of entities that operate with profit motives and stakeholder interests, which nonprofit organizations typically do not encompass.

4. How should Norina Co. classify its marketable securities and report unrealized gains?

- A. Classified as trading; gains are reported as part of income from operations.
- B. Classified as available-for-sale; gains are recognized in current earnings.
- C. Classified as trading; losses are reported in other comprehensive income.
- D. Classified as available-for-sale; gains reported as separate component of OCI.**

Norina Co. should classify its marketable securities as available-for-sale, and unrealized gains should be reported as a separate component of other comprehensive income (OCI). This classification follows the rules outlined in the Financial Accounting Standards Board (FASB) standards, which state that available-for-sale securities are reported at fair value, with any unrealized gains or losses excluded from net income and instead included in OCI. This treatment provides a clearer picture of the company's operational performance by not mixing these unrealized gains into current earnings, which could distort financial analysis. The reporting of these unrealized gains in OCI rather than in earnings reinforces the distinction between the fluctuations in market value and the realized gains or losses that actually impact the cash flows of the company. The approach is designed to mitigate the effects of short-term market volatility on the reported income. In contrast, trading securities are marked to market with both unrealized gains and losses recognized in earnings, reflecting their impact on net income. Therefore, classifying the securities as available-for-sale is appropriate for those intended for other than short-term trading, and recognizing unrealized gains in OCI aligns with the accounting standards principles.

5. In a Troubled Debt Restructuring, what financial measurement represents the difference between the carrying amount of the payable and the fair value of the asset transferred?

- A. Loss on extinguishment of debt
- B. Gain on extinguishment of debt**
- C. Interest Expense
- D. Modification Gain

In a Troubled Debt Restructuring, the appropriate financial measurement that represents the difference between the carrying amount of the payable and the fair value of the asset transferred is the gain on extinguishment of debt. When a debtor transfers assets, such as cash or property, to settle a liability at a value lower than its carrying amount, the debtor recognizes a gain. This gain is calculated as the difference between the carrying amount of the loan being extinguished and the fair market value of the assets given up in the restructuring. In this scenario, if the fair value of the assets transferred is greater than the carrying amount of the debt, the debtor effectively benefits from a reduction in liabilities greater than the asset given. This situation typically arises in troubled debt restructurings where the lender agrees to accept less than the full amount owed, leading to a financial benefit to the borrower recognized as a gain on extinguishment of debt. The other options, while relevant in different contexts, do not accurately describe this specific financial measurement. For instance, a loss on extinguishment of debt would apply when the carrying amount of the payable exceeds the fair value of the assets transferred, resulting in an expense rather than a gain. Additionally, interest expense pertains to the cost of borrowing and does

6. What kind of expense is recognized when a creditor receives assets/equity for a Troubled Debt?

- A. Administrative Expense
- B. Bad Debt Expense**
- C. Operational Expense
- D. Interest Expense

When a creditor receives assets or equity in settlement of a troubled debt, this transaction often leads to the recognition of a bad debt expense. This situation arises when a debtor is unable to meet the payment obligations on their debt, prompting the creditor to agree to a settlement that may involve the creditor accepting less than the full amount owed. In these cases, the creditor will evaluate the fair value of the assets or equity received. If the fair value of what is received is less than the carrying amount of the debt, the creditor must recognize a loss, which is reflected as a bad debt expense in their financial statements. This is consistent with the principle of recognizing losses on assets that are not collectible or realizable at their recorded amounts. Administrative, operational, and interest expenses do not fit this scenario because they are classified differently in accounting practices. Administrative expenses generally relate to overhead costs that are not directly tied to the production of goods or services, operational expenses pertain to costs necessary for the day-to-day functions of a business, and interest expense relates to the cost of borrowing money. Each of these expense types does not directly address the specifics of transactions involving troubled debts and their settlement through asset or equity transfer.

7. Which term is used to describe a promise by a corporation to pay bondholders a specific sum at maturity?

- A. Loan contract
- B. Bond indenture**
- C. Bond covenant
- D. Bond agreement

The term that describes a promise by a corporation to pay bondholders a specific sum at maturity is the bond indenture. A bond indenture is a formal agreement between the bond issuer (the corporation) and the bondholders, detailing the terms of the bond, including the principal amount to be paid at maturity, the interest rate, and the payment schedule. This document serves as a contract that outlines the rights and responsibilities of both parties involved in the bond transaction. It ensures that the bondholders have a clear understanding of what to expect in terms of repayment and any other covenants or restrictions that the issuer must adhere to during the life of the bond. While other terms like loan contract, bond covenant, and bond agreement are related to financial agreements, they do not specifically capture the essence of the promise tied to the payment of the principal amount at maturity in the way that a bond indenture does. For example, a bond covenant refers to specific agreements or conditions that the issuer must follow as part of the indenture, rather than the promise itself. Understanding these distinctions clarifies the importance of the bond indenture in the context of bonds and corporate finance.

8. What is the liability recognized by the lessor for refundable security deposits?

- A. Reported as a receivable until refunded
- B. Recognized as revenue immediately
- C. Classified as a liability until returned**
- D. Not recorded in financial statements

The correct response is that refundable security deposits are classified as a liability until they are returned. This classification arises because the lessor is obligated to return the deposit to the tenant at the end of the lease term, assuming the conditions of the lease are met. Therefore, the amount received from the tenant is not treated as income or revenue for the lessor; rather, it is recognized as a liability on the balance sheet, reflecting the legal obligation to repay the deposit. When the lessor receives the security deposit, it does not represent an ongoing income-generating activity; instead, it is merely a temporary holding of funds that will ultimately be refunded. Until the point of return, the lessor must recognize the deposit as a liability, ensuring that the financial statements accurately depict the obligations of the company. In contrast, classifying the deposit as a receivable or recognizing it as immediate revenue would not appropriately reflect the lessor's obligation. Additionally, stating that the deposit is not recorded suggests a failure to account for the legal and financial responsibility tied to it, which is contrary to the principles of responsible financial reporting.

9. How is the discount on bonds amortized?

- A. Equally over the life of the bond
- B. It represents additional payments to investors at issuance
- C. It increases reported cash payments at maturity
- D. It increases interest expense each period**

Amortization of the discount on bonds occurs as a way to recognize the additional interest expense that is effectively paid by the borrower to compensate investors for purchasing the bond at a price lower than its face value. This discount represents the difference between the face value of the bonds and their issue price. As the bond approaches maturity, the issuer recognizes this discount as an increase in interest expense over the life of the bond. Each period, a portion of the discount is amortized, which enhances the total interest expense reflected on the income statement. This is aligned with the effective interest method or the straight-line method of amortization, but the critical point is that the amortization will lead to an increase in the reported interest expense for each period. In this context, the other options do not correctly describe how the discount is treated. The discount does not represent additional payments to investors at issuance nor does it increase reported cash payments at maturity. Discount amortization does not distribute the same expense equally over the life of the bond; instead, it influences the interest expense variable each period until the bond matures. Thus, the correct approach is recognizing the increase in interest expense through the amortization process associated with the bond discount.

10. How is the amortization calculated for the straight-line method?

- A. By multiplying the coupon rate by the bond face value.
- B. By dividing the premium or discount by the number of periods.**
- C. By adding bond issuance costs to the recorded interest expense.
- D. By determining the market rate at issuance.

The correct method for calculating amortization using the straight-line method involves dividing the premium or discount by the number of periods remaining until maturity. This approach evenly allocates the total premium or discount over the bond's life, ensuring that each accounting period reflects an equal portion of the total amortization expense. In the context of bonds, a premium arises when bonds are issued at a price above their face value, while a discount occurs when they are sold for less than their face value. By dividing the premium or discount by the total number of periods, entities can systematically recognize the amortization as part of each period's interest expense, which aligns with the objective of matching expenses with revenues over time. Understanding this method is crucial as it simplifies the amortization process and provides a consistent approach for financial reporting. Other methods of amortization may involve more complex calculations or varying amounts per period, but the straight-line method stands out for its simplicity and ease of application.

Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

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We wish you the very best on your exam journey. You've got this!

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