

# Financial Statement Analysis Practice Test (Sample)

## Study Guide



**Everything you need from our exam experts!**

**This is a sample study guide. To access the full version with hundreds of questions,**

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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. Don't worry about getting everything right, 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, and take breaks to retain information better.**

## 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.**

## 7. Use Other Tools

**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!**

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## **Questions**

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- 1. Which financial statement section typically includes nonrecurring items?**
  - A. Operating Section**
  - B. Bottom Section**
  - C. Cash Flow Section**
  - D. Equity Section**
  
- 2. Expenses are best defined as what?**
  - A. Revenue generated from sales**
  - B. Costs incurred to produce revenues**
  - C. Funds set aside for growth**
  - D. Dividends paid to stockholders**
  
- 3. Which ratio explains the difference between return on assets and return on equity?**
  - A. Debt to Equity Ratio**
  - B. Financial Leverage**
  - C. Asset Turnover Ratio**
  - D. Equity Multiplier**
  
- 4. Which organization is NOT involved in setting accounting or auditing standards?**
  - A. PCAOB**
  - B. AICPA**
  - C. IRS**
  - D. FASB**
  
- 5. What does working capital represent?**
  - A. The total assets of a company**
  - B. The difference between current assets and current liabilities**
  - C. The total liabilities of a company**
  - D. The cash position of a company at a specific date**

**6. What term describes the process of examining the financial performance of a company over time?**

- A. Trend analysis**
- B. Comparative analysis**
- C. Financial forecasting**
- D. Breach analysis**

**7. Which of the following best describes current assets?**

- A. Assets expected to last more than one year**
- B. Assets that provide liquidity within a year**
- C. Assets that can be quickly liquidated**
- D. Fixed investments in property and equipment**

**8. Which organization defines the ethical behavior code of professional conduct for accountants?**

- A. PCAOB**
- B. AICPA**
- C. FASB**
- D. SEC**

**9. What is the concept of economic value added (EVA)?**

- A. The measure of a company's financial performance based on the residual wealth calculated by deducting its cost of capital from its operating profit**
- B. The additional value gained through mergers and acquisitions**
- C. The profit a company retains after paying all expenses**
- D. The increased revenue from new product launches**

**10. What information does a common size balance sheet provide?**

- A. Comparison of revenues over multiple years**
- B. Comparison of amounts within one year to total liabilities**
- C. Comparison of amounts within one year to total assets**
- D. Summary of net income from all years**

## **Answers**

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

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## **Explanations**

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**1. Which financial statement section typically includes nonrecurring items?**

- A. Operating Section**
- B. Bottom Section**
- C. Cash Flow Section**
- D. Equity Section**

The bottom section of a financial statement, often referred to as the bottom line or net income section, typically includes nonrecurring items. These items are unusual and infrequent in nature, such as gains or losses from the sale of assets, restructuring charges, or natural disaster impacts. Including these items in the bottom section allows analysts and users of financial statements to see how these occurrences affect the overall profitability of the company in that particular reporting period. In contrast, operating sections focus on regular, ongoing revenue and expenses related to the core business activities. The cash flow section emphasizes the inflows and outflows of cash, detailing how money moves in and out of the business without specific regard to nonrecurring gains or losses. The equity section outlines owners' equity accounts and does not typically present items related to day-to-day operations or nonrecurring events. Thus, the bottom section is the most appropriate place for reporting nonrecurring items, making it the correct choice in this context.

**2. Expenses are best defined as what?**

- A. Revenue generated from sales**
- B. Costs incurred to produce revenues**
- C. Funds set aside for growth**
- D. Dividends paid to stockholders**

Expenses are best defined as costs incurred to produce revenues. This definition is foundational in accounting, where expenses represent the outflows of resources that a business must pay to operate and generate income. When an organization engages in activities that lead to revenue generation—such as producing goods, providing services, or maintaining operations—it incurs various costs like salaries, utilities, raw materials, and administrative expenses. Recognizing expenses is crucial for measuring profitability, as they directly impact net income when subtracted from total revenues. Understanding this relationship helps stakeholders evaluate the efficiency of a company's operations and its ability to translate revenues into profits. This definition accurately captures the essence of expenses within the context of financial statements, ensuring clarity in financial analysis and decision-making processes.

**3. Which ratio explains the difference between return on assets and return on equity?**

- A. Debt to Equity Ratio**
- B. Financial Leverage**
- C. Asset Turnover Ratio**
- D. Equity Multiplier**

The correct answer is financial leverage, which plays a crucial role in differentiating return on assets (ROA) and return on equity (ROE). Financial leverage reflects the extent to which a company uses debt to finance its operations. When a company employs debt, it can amplify its ROE compared to its ROA. This happens because ROA measures how efficiently a company utilizes its assets to generate earnings, regardless of how those assets are financed. On the other hand, ROE assesses the returns generated on the equity invested by shareholders. When a firm uses debt, it effectively increases its potential return on equity, as the profit generated from assets financed through debt contributes to equity holders, thus inflating the ROE in comparison to ROA. The other options provided do not directly relate to the relationship between ROA and ROE in this context. For instance, the debt to equity ratio specifically measures the proportion of debt and equity funding used by a company but does not clarify the operational efficiency or profitability metrics themselves. The asset turnover ratio focuses on how effectively a company utilizes its assets to generate sales, which is separate from evaluating returns on equity versus assets. The equity multiplier, while it includes debt in its calculation of financial leverage, serves as a tool

**4. Which organization is NOT involved in setting accounting or auditing standards?**

- A. PCAOB**
- B. AICPA**
- C. IRS**
- D. FASB**

The Internal Revenue Service (IRS) is primarily responsible for tax administration and enforcement in the United States. Its focus is on ensuring compliance with tax laws and managing tax collection rather than establishing accounting or auditing standards. While other organizations listed—such as the Public Company Accounting Oversight Board (PCAOB), the American Institute of Certified Public Accountants (AICPA), and the Financial Accounting Standards Board (FASB)—are directly involved in creating and overseeing accounting and auditing standards, the IRS's role does not extend to these areas. The PCAOB oversees the audits of public companies, the AICPA sets professional and ethical standards for CPAs, and the FASB establishes financial accounting and reporting standards, thereby emphasizing the distinct role of the IRS in the tax domain rather than in standard-setting for financial reporting or auditing.

## 5. What does working capital represent?

- A. The total assets of a company
- B. The difference between current assets and current liabilities**
- C. The total liabilities of a company
- D. The cash position of a company at a specific date

Working capital is a key financial metric that represents the difference between current assets and current liabilities. It is an indicator of a company's short-term financial health and operational efficiency. Current assets include cash, accounts receivable, and inventory, which are expected to be converted into cash or used up within one year. Current liabilities are obligations that the company needs to settle within the same timeframe, such as accounts payable and short-term debt. Having positive working capital indicates that a company can easily meet its short-term financial obligations, whereas negative working capital could signal potential liquidity problems. This measure is crucial for assessing how well a business is managing its operational efficiency and funding its day-to-day operations. It allows analysts and investors to evaluate whether a company has sufficient resources to continue its operations without the risk of financial distress. Understanding and monitoring working capital helps in making informed financial decisions and ensures a business remains solvent in the short term.

## 6. What term describes the process of examining the financial performance of a company over time?

- A. Trend analysis**
- B. Comparative analysis
- C. Financial forecasting
- D. Breach analysis

The term that describes the process of examining the financial performance of a company over time is trend analysis. This approach involves looking at historical financial data to identify patterns or trends that can inform decision-making and future expectations. By analyzing financial statements over multiple periods, analysts can determine whether a company's performance is improving, declining, or remaining stable. Trend analysis often focuses on specific metrics like revenue growth, profit margins, and expenses, allowing stakeholders to recognize long-term movements in financial health. In this context, comparative analysis refers to assessing a company's performance against another company or industry benchmarks, which is not specifically focused on the company's own historical performance. Financial forecasting involves predicting future financial outcomes based on historical data and assumptions, rather than just examining past performance. Breach analysis typically concerns itself with violations, such as security breaches or compliance issues, and is not related to financial performance analysis. Therefore, trend analysis accurately captures the essence of evaluating a company's financial performance over time.

**7. Which of the following best describes current assets?**

- A. Assets expected to last more than one year**
- B. Assets that provide liquidity within a year**
- C. Assets that can be quickly liquidated**
- D. Fixed investments in property and equipment**

Current assets are best described as assets that provide liquidity within a year. This definition is rooted in the classification of assets based on their liquidity and the expected timeframe for conversion to cash. Current assets are generally expected to be converted into cash, sold, or consumed within one year or within the business's operating cycle, whichever is longer. Common examples include cash and cash equivalents, accounts receivable, inventory, and short-term investments. The focus on liquidity emphasizes the role of current assets in meeting short-term financial obligations and supporting operational activities. The other descriptions do not align with the definition of current assets. Assets expected to last more than one year pertain to long-term assets, while the description of assets that can be quickly liquidated may apply to both current assets and other liquid marketable securities, but it does not specifically define current assets. Fixed investments in property and equipment are categorized as fixed or long-term assets, further distinguishing them from the concept of current assets.

**8. Which organization defines the ethical behavior code of professional conduct for accountants?**

- A. PCAOB**
- B. AICPA**
- C. FASB**
- D. SEC**

The American Institute of Certified Public Accountants (AICPA) is the organization responsible for defining the ethical behavior code of professional conduct for accountants. The AICPA sets forth the professional ethical standards that certified public accountants (CPAs) are expected to follow in their work, which includes guidance on integrity, objectivity, confidentiality, and professional behavior. This code serves as a framework for ethical practice among accountants, ensuring that they adhere to high standards of professionalism and accountability in their services. The other organizations listed have different roles within the accounting and financial reporting landscape. For instance, the Public Company Accounting Oversight Board (PCAOB) oversees the audits of public companies to protect investor interests; the Financial Accounting Standards Board (FASB) establishes financial accounting and reporting standards; and the Securities and Exchange Commission (SEC) regulates the securities industry and ensures that public companies provide accurate financial information to investors. While these organizations are influential in shaping the accounting profession, it is the AICPA that specifically addresses the ethical conduct of accountants.

## 9. What is the concept of economic value added (EVA)?

- A. The measure of a company's financial performance based on the residual wealth calculated by deducting its cost of capital from its operating profit**
- B. The additional value gained through mergers and acquisitions**
- C. The profit a company retains after paying all expenses**
- D. The increased revenue from new product launches**

The concept of economic value added (EVA) focuses on assessing a company's financial performance by looking at the residual wealth created after accounting for the cost of capital. In essence, EVA measures how much value a company generates for its shareholders over and above the cost of financing its operations. It is calculated by taking the operating profit of a company, typically referred to as net operating profit after taxes (NOPAT), and subtracting the capital charge, which is the product of the company's total capital and its weighted average cost of capital (WACC). If the resulting number is positive, it indicates that the company is generating value over and above its capital costs, thus demonstrating effective use of its assets. This definition captures the notion that true profitability is not merely about generating revenues but also about ensuring that those revenues exceed the costs associated with generating them, including the cost of equity and debt. This concept aligns tightly with shareholder value maximization, making it a critical metric in financial analysis.

## 10. What information does a common size balance sheet provide?

- A. Comparison of revenues over multiple years**
- B. Comparison of amounts within one year to total liabilities**
- C. Comparison of amounts within one year to total assets**
- D. Summary of net income from all years**

A common size balance sheet presents each line item as a percentage of total assets, allowing for an easy comparison of the relative size of different asset categories, liabilities, and shareholders' equity within a single year. This method facilitates the analysis of how much each individual component constitutes of the overall financial position of the company. By representing everything on a proportional basis, it allows stakeholders to assess the balance sheet's structure and the company's financial health without being influenced by absolute dollar amounts, which can vary significantly between companies or due to changes in total assets. This context is especially useful when comparing companies of different sizes or analyzing changes over time. The other options do not accurately reflect what a common size balance sheet illustrates. While comparing amounts to total liabilities or revenues is important for financial analysis, those comparisons pertain to specific line items and do not represent the focus of a common size balance sheet. A summary of net income pertains to the income statement and is unrelated to the structure and analysis presented by a common size balance sheet.

# 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](mailto:hello@examzify.com).**

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

**<https://financialstatementanalysis.examzify.com>**

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

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