

Accounting Workbook

Here, we give you 25 questions you can use to test your understanding of what you've learned in this book. We've chosen at least one question from each chapter in *Idiot's Guides: Introductory Accounting*, and the correct answers appear at the end. The answers reinforce the correct answer and also explain common misunderstandings behind the incorrect responses.

Questions

1. T accounts are an effective mechanism for mapping accounting transactions. Paying a bill to a vendor for both inventory and office supplies results in which set of T accounts?
 - A. Debit to Cash, Debit to Inventory, Debit to Office Supplies
 - B. Debit to Cash, Credit to Inventory, Credit to Office Supplies
 - C. Credit to Cash, Debit to Cost of Goods Sold, Debit to Office Supplies
 - D. Credit to Cash, Debit to Inventory, Debit to Office Supplies
2. Which entity choices offer the best legal liability protection to all owners of a business?
 - A. Corporation
 - B. Partnership
 - C. Limited liability corporation
 - D. Sole proprietorship

3. Cloud-based accounting programs offer many benefits desktop programs can't. They also come with limitations. What's one current superior benefit to cloud accounting versus desktop?
- A. One-time licensing fees for a given version of the software
 - B. Advanced inventory management features
 - C. Immediate access to books from anywhere
 - D. Control over feature and screen changes
4. When establishing a chart of accounts, which account type would you assign to an account for Office Supplies?
- A. Cost of Goods Sold
 - B. Current Asset
 - C. Expenses
 - D. Other Expense
5. Which costing method provides the best representation of inventory costs within your business?
- A. Average Cost
 - B. First In, First Out
 - C. Last In, First Out
 - D. Stock Items
6. Money from customers in the form of refundable deposits or retainers should be initially posted in what type of account on your books?
- A. Asset
 - B. Expense
 - C. Liability
 - D. Revenue

7. Which account balance can you safely correct by way of a journal entry?
- A. Accounts Payable
 - B. Accounts Receivable
 - C. Inventory
 - D. Prepaid Expenses
8. You should periodically reconcile all these accounts except:
- A. Checking
 - B. Credit card
 - C. Inventory
 - D. Savings
9. New employees should always complete form I-9 and:
- A. Form W-2
 - B. Form W-4
 - C. Form 1040
 - D. Form 1099
10. Which type of insurance is mandatory for most businesses that have one or more employees?
- A. Liability insurance
 - B. Life insurance
 - C. Property insurance
 - D. Workers' compensation insurance
11. Which of the following is a now disused term for a small business retirement plan?
- A. 401(k) plan
 - B. Keogh plan
 - C. SEP IRA
 - D. SIMPLE IRA

12. The following types of payroll taxes apply in most states except:
- A. Federal unemployment
 - B. FICA withholding
 - C. State unemployment
 - D. Temporary Disability Insurance
13. How should you correct situations in which a customer or vendor has two or more transactions that net to 0 on an aging report?
- A. Enter a credit memo to offset the debit balance.
 - B. Enter a journal entry.
 - C. Enter a new invoice or bill to offset the credit balance.
 - D. Enter a receipt or payment transaction to apply the transactions against each other.
14. Which financial statement reports the net change in your cash balance within a given accounting period?
- A. Aged Accounts Receivable Report
 - B. Balance sheet
 - C. Income statement
 - D. Statement of cash flows
15. Which of the following represents a best practice for creating a password to protect your accounting records?
- A. B00k5Ar3Fun!
 - B. Fido
 - C. Password1
 - D. 0704

16. Which of the following ratios does not specifically measure the financial liquidity of a business?

- A. Cash Coverage Ratio
- B. Current Ratio
- C. Gross Profit Margin
- D. Quick Ratio

17. Which of the following instances should not be cause for concern when reviewing your balance sheet?

- A. Accounts Receivable balance doesn't match the Aged Accounts Receivable Report
- B. Inventory Account doesn't match the Inventory Valuation Report
- C. A Payroll Taxes Payable account reflects a balance even though you've remitted all taxes due
- D. The sum of Distributions, Retained Earnings, and Net Income is greater than 0

18. Most businesses are required to file all the following returns quarterly with what possible exception?

- A. Form 940
- B. Form 941
- C. State Unemployment Tax Return
- D. State Withholding Return (for states with income tax)

19. Your share of income or loss from a partnership, LLC, or S corporation is reported to you on what tax form?

- A. 1099
- B. K-1
- C. Schedule C
- D. W-2

20. Which business records should you keep for at least 7 years?
- A. Bank statements
 - B. Expired insurance policies
 - C. Federal payroll tax returns
 - D. Personnel records for terminated employees
21. Which of the following is not a spreadsheet program?
- A. Excel
 - B. Numbers
 - C. Google Sheets
 - D. Xero
22. The following analytical features are only available in Excel 2013 and later except:
- A. Quick Analysis
 - B. Recommended Charts
 - C. Recommended Pivot Tables
 - D. Templates
23. Apps that enable you to back up or otherwise archive accounting data include all these except:
- A. Carbonite
 - B. Dropbox
 - C. Evernote
 - D. LastPass
24. Recording an invoice from a customer has what effect on your books?
- A. Debit cash and credit revenue
 - B. Credit cash and debit revenue
 - C. Debit accounts receivable and credit revenue
 - D. Credit accounts receivable and debit cash

25. You'll most likely see a mix of the following transaction types on your general ledger except:

- A. Checks
- B. Estimates
- C. Invoices
- D. Journal entries

Answers

1. D.

- A. In this case, all three amounts would appear on the left side of the respective Ts. At least one amount must appear on the right.
- B. The amounts in this scenario are all on the opposite side of the Ts where they belong.
- C. The purchase of inventory is an asset. Your Cost of Goods Sold account is only affected when you sell inventory, rather than purchase it.
- D. In this case, the amount you pay in cash is to the right of the Cash T, with Inventory and Office Supplies on the left of their respective Ts. The sum of the amounts on the left must balance with the sum of any amounts on the right.

2. A.

- A. Both S and C corporations provide a legal firewall between the business operations and the owners' personal finances, except in cases of criminal misconduct.
- B. Within a partnership, limited partners are often shielded from legal exposure, but one or more general partners will be fully on the hook.
- C. Incorrect. The correct terminology is limited liability company, which offers legal protection to owners no matter whether the LLC opts to be taxed as a partnership or a corporation.
- D. In this situation, you personally are the business and, therefore, personally responsible for any and all obligations and liabilities.

3. C.

- A. Cloud-based accounting programs require ongoing monthly subscription fees that, over time, can exceed the cost of a desktop-based accounting program. However, accounting software vendors are slowly moving toward subscription-based pricing for desktop programs as well.
- B. Most cloud-based products either do not offer inventory or provide only limited functionality. This gap can sometimes be breached with third-party add-ons, but at present, desktop programs offer the most robust inventory functionality.
- C. Cloud-based accounting programs are generally available all the time, except for brief maintenance downtime. You can establish remote access to your desktop accounting program, but this is easily disrupted by the computer being turned off or your internet access being slow or disrupted.

- D. Features come and go without notice in cloud-based accounting programs. You can decide if and when to install new versions and updates to desktop accounting programs.
4. C.
- A. Office Supplies are designated for use within the business, rather than for sale to customers. Your accounting software automatically transfers the cost of inventory items you sell to Cost of Goods Sold as you make sales to customers.
 - B. In this context, office supplies are a consumable item you'll use immediately. Current Assets include cash, accounts receivable, and inventory, all of which can be turned into cash rather quickly.
 - C. This account appears on your income statement in the Operating Expenses section, which reflects ongoing expenses of running your business.
 - D. Office Supplies directly relate to running your business; Other Expenses is designed for nonoperational expenses such as tax penalties or parking tickets.
5. B.
- A. This approach averages the price of all your inventory purchases together, which might dilute the actual costs of inventory on hand.
 - B. FIFO applies the oldest costs of inventory items first, which is the best use of the matching principle in accounting.
 - C. LIFO applies the newest cost of inventory items first, and in certain cases, can provide misleading cost of goods sold amounts on your income statement.
 - D. Stock Items are a type of inventory item rather than a costing method.
6. C.
- A. The money temporarily increases an asset account, your cash account, but the money isn't truly an asset of your business yet.
 - B. The only situation in which money from a customer might be classified as an expense is when the customer is reimbursing an expense you paid on his or her behalf.
 - C. You can move the money out of a liability account by including the amount on an invoice, recording a journal entry, or writing a check to your customer if a refund is required.
 - D. Ultimately, this amount becomes revenue on your books at the time you provide the agreed-upon goods and/or services.

7. D.

- A. Forcing changes to your Accounts Payable account without using vendor credit memos or entering new bills causes the account to not balance with your Aged Payables account.
- B. Making direct adjustments to your Accounts Receivable account causes your Aged Receivables report not to reconcile with the Accounts Receivable amount on your balance sheet. Always use customer credit memos instead.
- C. Always take care to only affect your inventory account by way of inventory adjustment transactions instead of journal entries. Forcing changes to inventory can result in income tax complications, and the IRS pays close attention to inventory accounts.
- D. You can use recurring or memorized transactions in your accounting software to automate monthly transfers such as this.

8. C.

- A. Depending on the nature of your business, you might want to reconcile your checking account as frequently as once a day.
- B. It's just as important to reconcile credit card accounts as cash accounts so you stay abreast of credit usage and record expenses in a timely fashion.
- C. Account reconciliation involves comparing your account balances with the records of a corresponding financial institution. You'll periodically perform a physical inventory to count items on hand, but reconciliation isn't applicable to inventory.
- D. You might opt to reconcile a savings account with little activity once per month.

9. B.

- A. Employers issue Form W-2 to employees at the end of each calendar year to report total wages and withholdings.
- B. The IRS provides an online calculator to help employees determine the number of withholding exemptions to request on their W-4.
- C. All individual taxpayers in the United States who have taxable income must file some version of Form 1040 each year.
- D. Businesses issue Form 1099 at the end of each year to report nonemployee compensation and rents.

10. D.

- A. Although optional, every business should carry one or more forms of liability insurance to manage the risk of unexpected civil litigation.
- B. No businesses are required to purchase life insurance, although many use key-person policies to manage the exposure that can arise from the death or disability of one or more key employees.
- C. Property insurance is optional, but an uninsured loss of property or equipment can be devastating to many small businesses.
- D. Certain states allow owners and/or officers to exempt themselves from workers' compensation, but severe penalties apply to businesses that don't put coverage in place for all other employees.

11. B.

- A. 401(k) refers to the subchapter of the U.S. tax code for this widely used form of retirement planning.
- B. The plan name is a nod to Representative Eugene J. Keogh, who initially spearheaded legislation for this type of retirement plan. The SEP IRA is the closest equivalent to what were formerly known as Keogh plans.
- C. The Self-Employed Pension (SEP) Individual Retirement Account (IRA) allows certain small businesses to tax defer much larger amounts of money for retirement than is possible under other retirement plans.
- D. The Savings Incentive Match Plan for Employees (SIMPLE) plan is heralded as an ideal starting point for businesses that don't yet offer a retirement plan.

12. D.

- A. With few exceptions, every business is required to pay into the federal unemployment system, which, in turn, supports state unemployment plans.
- B. Most wages are subject to Social Security and Medicare withholding, collectively called FICA. This tax is split evenly between employers and employees.
- C. All 50 states require employers to pay state unemployment taxes.
- D. Only a few states mandate that employers pay into a Temporary Disability Insurance fund that provides replacement income to certain employees who experience a short-term disability.

13. D.

- A. Although this action would eliminate the 0 balance, it would misstate your books in such a way that you could inadvertently issue a refund to your customer or take an unwarranted discount against a vendor's bill.
- B. Journal entries have no impact on aging reports and should never be used to try to correct issues with customer or vendor balances.
- C. In this case, you'd eliminate the 0 balance by adding phantom revenue or expense and show a false balance due.
- D. The resulting receipt or payment has a 0 balance but also clears up your aging report.

14. D.

- A. The Aged Accounts Receivable Report is not a formal financial statement but rather a supporting schedule.
- B. Your balance sheet reports your ending cash balance as of the report date.
- C. This report, sometimes referred to as a Profit and Loss Statement, does not reflect asset accounts such as cash.
- D. The statement of cash flows report provides insight into exactly how your business was funded during a given period of time.

15. A.

- A. In this case, the pass phrase is Books Are Fun! with no spaces and numbers in place of certain letters. Maintain a mix of upper- and lowercase letters plus punctuation when possible.
- B. Pet and family member names are easily guessed and provide little protection as passwords.
- C. Users often mistakenly believe that adding an extra digit to a commonly used word protects information and records.
- D. Assuming everyone knows you were born on the Fourth of July, this password can be easily guessed.

16. C.

- A. The Cash Coverage Ratio compares operating cash flow to total debt to determine if a company's debt load is manageable.
- B. The Current Ratio compares current assets to current liabilities and is often the first liquidity ratio used.
- C. The Gross Profit Margin reflects the pricing effectiveness for a business but has no direct relationship to liquidity.
- D. The Quick Ratio is sometimes referred to as the Acid Test and compares current assets other than inventory against current liabilities.

17. D.

- A. This typically indicates that a user has tried to adjust a customer balance by way of a journal entry, or a user mistakenly referenced the accounts receivable account in lieu of a revenue account on an invoice.
- B. Users sometimes mistakenly record inventory balances to account for damage or spoilage as journal entries instead of using the inventory adjustment feature within the accounting software. Journal entries cannot update the quantity on hand of inventory items.
- C. Users sometimes mistakenly post payroll tax remittances to the Payroll Tax Expense account. Your accounting software automatically posts the employer share of payroll taxes to the expense account, so always use the liability account when recording a payroll tax payment.
- D. When the sum of these numbers is less than 0, excessive distributions to owners may have occurred, which can trigger a taxable event on your federal and state income tax returns.

18. A.

- A. Form 940 for reporting Federal Unemployment Taxes can be filed annually if the total liability is less than \$500 for a given year.
- B. Form 941 is used to report federal withholding, as well as Social Security and Medicare taxes, and it reconciles the quarterly tax liability with tax deposits.
- C. All 50 states require most businesses file unemployment returns on a quarterly basis.
- D. States that levy an income tax require businesses to file a return that reconciles the quarterly tax liability with the tax deposits made.

19. B.

- A. Incorrect. You might receive a Form 1099 from your business for nonemployee compensation such as rents, but this form doesn't reflect your share of income or loss from the business.
- B. Formally known as Schedule K-1, this form details each owner's share of income and loss for certain business entity types.
- C. Only sole proprietorships utilize this form to report income and loss as part of Form 1040.
- D. Any wages paid to you as an employee are reported annually on Form W-2.

20. D.

- A. It doesn't hurt to keep bank statements for extended periods, but you can get copies from your financial institution upon request, should a need arise.
- B. You may choose to keep expired insurance policies perpetually, but if the coverage year ended with no claims being filed, you can safely discard expired policies.
- C. Some states require that you retain payroll tax returns for 7 years or longer, but the federal government loses interest after 4 years when returns have been filed correctly.
- D. Federal regulations stipulate that personnel records for terminated employees be kept on file for at least 7 years.

21. D.

- A. Microsoft Excel is the most widely used spreadsheet. Most accounting software programs provide the ability to send reports directly or indirectly to Excel.
- B. This spreadsheet program is only available on Apple computers but is generally able to open any Excel-compatible documents, including reports exported from your accounting software.
- C. This cloud-based spreadsheet program competes with Microsoft Excel. Certain cloud-based accounting programs offer the ability to send reports to Google Sheets, but in most cases, you need to save reports as an Excel spreadsheet first and then open the document manually in Google Sheets.
- D. Xero is a cloud-based accounting software program. You can export reports from Xero to a spreadsheet program.

22. D.

- A. When you select a range of data in Excel 2013 and later, this feature provides instant access to data visualization and analysis tools.
- B. This feature provides live mock-ups of what selected data would look like in chart form within Excel 2013 and later.
- C. This feature provides live mock-ups of what list-based data would look like in pivot table form in Excel 2013 and later.
- D. Every version of Excel, as well as most other spreadsheet programs, offer an array of prebuilt spreadsheets known as templates that can give you a jump-start on building spreadsheets.

23. D.

- A. Carbonite is a subscription-based, cloud-based backup service you can use to easily create an offsite backup of the entire contents of your computer.
- B. Dropbox provides free and subscription-based levels of online storage space while also automatically synchronizing files and documents among as many computers and devices as you choose.
- C. Evernote can be best thought of as offering free and subscription-based tiers that serve as an online filing cabinet for storing notes, documents, and other business-related records.
- D. LastPass and competitor Dashlane provide password management tools you can use with online and offline software tools.

24. C.

- A. Sales receipt transactions immediately increase your cash account and your revenue account, but invoices do not immediately affect cash.
- B. Increases to cash are recorded as debits, while increases to revenues are posted as credits.
- C. Your accounting software automatically posts the transaction to these accounts unless you mistakenly reference a nonrevenue account when entering an invoice.
- D. The invoice payment or receipt transaction you record when the customer pays his or her invoice reduces accounts receivable and increases cash.

25. B.

- A. Payments to vendors and employees typically reduce your cash account and increase one or more expense accounts, although checks also can reduce liability accounts and increase asset accounts.
- B. Purchase orders, sales orders, and estimates are all considered nonposting transactions that never appear on your general ledger.
- C. Customer invoices typically appear in your accounts receivable account and one or more revenue accounts.
- D. Your accounting software automatically posts certain types of journal entries, such as when you sell inventory items. Journal entries are also used to record noncash transactions and to make corrections to your general ledger.