LO.a: Describe the components of the income statement and alternative presentation formats of that statement.

1. Angels Corporation incurs two types of depreciation expenses. Depreciation is charged on the factory machinery used for production purposes and for office equipment. The accountant of the firm presents both these expenses under a single heading, depreciation expense, in the income statement. This is *most likely* to be:
   A. grouping by function.
   B. grouping by nature.
   C. direct method.

2. The accountant at Demons Ltd. presents the subtotals for gross profit and operating profit in the income statement. The format adopted here is *most likely*:
   A. multi-step.
   B. single-step.
   C. indirect.

3. The income statement *least likely* includes which of the following elements?
   A. Operating income.
   B. Accounts receivable.
   C. Income before tax.

LO.b: Describe general principles of revenue recognition and accrual accounting, specific revenue recognition applications (including accounting for long-term contracts, installment sales, barter transactions, gross and net reporting of revenue), and implications of revenue recognition principles for financial analysis.

4. A company entered into a three-year construction project with a total contract price of $11.2 million and an expected total cost of $8.7 million. The following table provides cash flow information relating to the contract:

All figures in millions	Year 1	Year 2	Year 3
Costs incurred and paid	$2.2	$3.5	$3.0
Amounts billed and payments received	$3.5	$4.1	$3.6

   If the company uses the percentage-of-completion method, the amount of revenue recognized (in millions) in Year 2 is *closest* to:
   A. $4.5.
   B. $5.7.
   C. $7.6.

5. A customer orders customized industrial equipment from a manufacturing company in June. The equipment was shipped and delivered to the customer in August. The customer was invoiced in August and payment was made to the manufacturing company in September. The *most* appropriate month in which the manufacturing company should show the revenue is:

A. June.
B. August.
C. September.

6. Which of the following is *least likely* correct regarding revenue recognition principles?
   A. Revenue can only be recognized when cash is received.
   B. Under U.S. GAAP, the price needs to be either determined or determinable for revenue to be recognized.
   C. The IFRS criteria for recognizing royalties is that it is probable that the economic benefits associated with the transaction will flow to the entity and the amount of revenue can be reliably measured.

7. Telecom Ltd. has a four year license to provide communication services to a corporation. The total amount of the license fee that Telecom Ltd. will receive is $50,000. Revenue is recognized on a prorated basis as it is a long term contract. What revenue would Telecom Ltd. recognize at the end of year 1?
   A. $0.
   B. $12,500.
   C. $50,000.

8. Which of the following standards states that the revenue from barter transactions can be recognized at fair value only if the company has historically received cash payments for such services?
   A. IFRS.
   B. U.S. GAAP.
   C. Neither IFRS nor U.S. GAAP.

9. Under U.S. GAAP, which of the following is *not* a criterion for deciding whether to report gross revenues rather than net revenue?
   A. The company is a primary obligator under the contract.
   B. The company has reasonable latitude to establish the price.
   C. The company does not bear the inventory risk.

10. Under IFRS, which of the following is *not* a condition to recognize revenue from the sale of goods on the income statement?
    A. Amount of revenue can be measured reliably.
    B. Customer has made the payment.
    C. Entity has transferred the risk and rewards of ownership of goods to the buyer.

11. Under US GAAP, which of the following is *least likely* a criterion for determining when revenue is realized and earned?
    A. The price is determinable.
    B. The seller is reasonably sure of collecting the payment from the buyer.
    C. The product has been shipped, but not yet delivered.

12. Under US GAAP, a revenue recognition method used for long-term projects where the outcome cannot be measured reliably is *most likely* the:
    A. Percentage-of-completion method.
    B. Completed contract method.
    C. Cost recovery method.

13. During 2013, Company A sold a piece of land with a cost of $3 million to Company B for $5 million. Company B made a $1 million down payment with the remaining balance to be paid over the next 5 years. It has been determined that there is significant doubt about the ability and commitment of the buyer to complete all payments. Company A would *most likely* report a profit in 2013 of:
    A. $2 million using the accrual method.
    B. $0.4 million using the installment method.
    C. $1 million using the cost recovery method.

14. Ken Miller buys a house for $ 1 million with the payments spread over 10 years. His ability to complete the payments is doubtful. The *least* appropriate method to recognize revenue after the house is sold is:
    A. Installment method.
    B. Cost recovery method.
    C. Percentage of completion method.

LO.c: Calculate revenue given information that might influence the choice of revenue recognition method.

15. Dynamo Construction Company uses the percentage-of-completion method to recognize revenue from its long term construction contracts and estimates percent completion based on expenditures incurred as a percentage of total estimated expenditures. A three-year contract for €15 million was undertaken. The project is now at the end of its second year, and the following end-of-year information is available:

	Year 1	**Year 2**
Costs incurred during year	4,150,000	3,800,000
Estimated total costs	8,500,000	8,500,000

    The profit recognized in year 2 is *closest* to:
    A. €2.9 million.
    B. €3.0 million.
    C. €10.2 million.

16. A company entered into a three-year construction project with a total contract price (all figures in ‘000s $) of $5,000 and expected costs of $4,500. The company recognizes revenue using the percentage of completion method. The data below relate to the contract.

(All figures in ‘000s $)	**Year 1**	**Year 2**	**Year 3**
Costs incurred and paid	1,500	2,000	1,000

Amounts billed and payments received	1,000	2,000	2,000

The amount of revenue (in $‘000s) the company will recognize in Year 2 is *closest* to:
A. 2,222.
B. 2,865.
C. 3,890.

LO.d Describe key aspects of the converged accounting standards issued by the International Accounting Standards Board and Financial Accounting Standards Board in May 2014.

17. The core principle of the converged revenue recognition standard (issued by IASB and FASB) is that revenue should be recognized to “depict the transfer of promised goods or services to customers in an amount that reflects:
    A. the consideration that the entity has actually received in an exchange for those goods or services.”
    B. the consideration to which the entity expects to be entitled in an exchange for those goods or services.”
    C. the costs that the entity has incurred to produce those goods or services.”

18. Two analysts are discussing the converged standards issues by IASB and FASB in May 2014. Their comments are as follow: Analyst 1: Revenue recognition requires the application of a five-step process. The process includes identification of the contract with the customer and identification of performance obligations in the contract. Analyst 2: The performance obligations within a contract represent promises to transfer distinct goods or services.
    A. Analyst 1 is correct.
    B. Analyst 2 is correct.
    C. Both analysts are correct.

LO.e: Describe general principles of expense recognition, specific expense recognition applications, and implications of expense recognition choices for financial analysis.

19. Omega Enterprises is in the process of developing a more efficient production process for one of its primary products. If the company prepares its financial statements in accordance with IFRS, the *most* appropriate accounting treatment for those costs incurred in the project is to:
    A. expense them as incurred.
    B. capitalize costs directly related to the development.
    C. expense costs until technical feasibility has been established.

20. A company records a doubtful accounts expense of $4 million in 2015. What is the most appropriate interpretation of this expense?
    A. The expense represents credit losses on customer receivables in 2015.
    B. The expense represents an estimate of how much of the 2015 revenue will ultimately be uncollectible.

C. The net revenue shown on the income statement will be reduced by $4 million.

21. Tera Computers Company has switched to high margin premium-priced products with the most innovative features as part of its product differentiation strategy. Which of the following other changes is *most* consistent with this strategy?
    A. An increase in inventory levels.
    B. A decrease in R&D expenditures.
    C. An increase in advertising expenditures.

22. On 1 January 2011, a company issued €10,000,000 of bonds with a 10-year maturity paying annual coupon at 4% at an issue price of €96.04 per €100. Market interest rates at the time of issue were 4.5%. If the company uses IFRS, its interest expense in 2011 is *closest* to:
    A. €384,160.
    B. €432,180.
    C. €450,000.

23. Which of the following principles is followed for expense recognition?
    A. Going concern.
    B. Matching.
    C. Prudence.

24. Which inventory costing method is likely to have the highest ending inventory in a period of rising prices?
    A. FIFO.
    B. LIFO.
    C. Weighted average cost.

25. Mega Games Ltd. started business on January 1, 2012. On January 15, it purchased 1000 games at a cost of $75 each. 900 of these were sold in the first quarter at a price of $100 each. On April 1, more inventory was purchased comprising of 500 games at $80 each. In the second quarter, 550 games were sold. What is the ending inventory *most likely* to be if the inventory costing method followed is LIFO?
    A. $3,750.
    B. $4,000.
    C. $4,500.

26. Which of the following statements is *most likely* to be correct?
    A. The matching principle requires the adoption of the direct write-off method where a loss is only recognized when the customer actually defaults.
    B. A company estimates uncollectible accounts based on previous experience and this is recorded as a direct reduction of revenues.
    C. Under the matching principle, the estimated warranty expense is recognized in the period of the sale and not when the cost is actually incurred.

27. Lavish Leathers Ltd. purchased a machine worth $100,000. The machine will be used for five years. The estimated salvage value at the end of Year 5 is $15,000. The company

charges depreciation using the straight line method. Which of the following is *most likely* to be the net book value of the machine at the end of Year 3?
A. $17,000.
B. $40,000.
C. $49,000.

28. Lazy Leathers Ltd. purchased a machine worth $100,000.The machine will be used for five years. The estimated salvage value at the end of Year 5 is $15,000. The company charges depreciation using the double declining balance method. Which of the following is *most likely* to be the depreciation expense of the machine for Year 1?
A. $17,000.
B. $40,000.
C. $15,000.

LO.f: Describe the financial reporting treatment and analysis of non-recurring items (including discontinued operations, extraordinary items, unusual or infrequent items) and changes in accounting standards.

29. An analyst is estimating the net profit margin of a manufacturing company for next year. The method he adopts is to average the net profit margin for the past five years. Which of the following statements is *most likely* accurate with respect to the items used for his projections?
A. He must not include the gain on sale of investments, as it is a manufacturing firm.
B. He uses the most recent year's tax rate, which was only 60% of the previous two years' rate.
C. He must include the losses incurred due to discontinued operations in each of the five years.

30. Which of the following categories is *not* permitted under IFRS?
A. Discontinued operations.
B. Extraordinary items.
C. Unusual or infrequent items.

31. Retrospective application refers to:
A. correction of an error for a prior period.
B. changes in accounting estimates rather than accounting policies.
C. presentation of financial statements for previous fiscal years according to newly adopted principles.

LO.g: Distinguish between the operating and non-operating components of the income statement.

32. The following information for the current year is available for a company that prepares its financial statements in accordance with U.S. GAAP:

Revenue	$500,000
Cost of goods sold	$180,000
Other operating expenses	$100,000

Restructuring costs $50,000
Interest expense $30,000
The company's operating profit is *closest* to:
A. $220,000.
B. $170,000.
C. $140,000.

33. ABC Manufacturing Company prepares its financial statements in accordance with U.S. GAAP. Data for ABC is presented below:

	$000s
Revenue	10,000
Cost of goods sold	6,000
Other operating expenses	1,500
Restructuring costs (infrequent but not unusual)	300
Interest expense	400

ABC's operating profit (in $000s) is *closest* to:
A. 2,200.
B. 1,900.
C. 2,100.

LO.h: Describe how earnings per share is calculated and calculate and interpret a company's earnings per share (both basic and diluted earnings per share) for both simple and complex capital structures.

34. The following information is available on a company for the current year:
Net Income: $2,500,000
Average number of shares outstanding: 150,000
Convertible preferred shares outstanding: 5,000
Preferred dividend per share: $5
Each preferred is convertible into 5 shares of common stock
Convertible bonds, $100 face value per bond at 6% coupon: $60,000
Each bond is convertible into 20 shares of common stock
Corporate tax rate: 35%
The diluted EPS is *closest* to:
A. $13.38.
B. $14.29.
C. $15.29.

35. Selected information of a company's common equity over the course of the year is presented below:
Outstanding shares, at the start of the year: 3,000,000
Stock options outstanding, at start and end of the year: 100,000; Exercise price: $10.00
Shares issued on April 1: 500,000
Shares repurchased (treasury shares) on July 1: 100,000

Average market price of common shares for the year: $20/share
If the company's net income for the year is $5,000,000, its diluted EPS is *closest* to:
A. $1.50.
B. $1.48.
C. $1.46.

36. Xander Inc.'s financial information is available at the end of the year:

	Share Information		
Security	Authorized	Issued & outstanding	Other features
Common Stock	500,000	300,000	Currently pays a dividend of $2 per share
Preferred stock, type A	25,000	20,000	Nonconvertible, cumulative; pays a dividend of $6 per share.
Preferred stock, type B	25,000	15,000	Convertible; pays a dividend of $7.50 per share. Each share is convertible into 2 common shares.
Additional Information: Retained earnings at start of year = $5,000,000 Reported income for the year = $2,000,000			

The diluted EPS is *closest* to:
A. $5.70.
B. $6.12.
C. $6.23.

37. A company has earnings of 10 million for 2013. The preferred dividend for the year is 2 million and the common stock dividend is 1 million. The number of shares outstanding for the year is 20 million. What is the basic EPS?
A. 0.40.
B. 0.35.
C. 0.50.

38. Dan Motors reported a net income of $1 million for the year ended December 31, 2012. The company had 50,000 common shares outstanding for the year, and 15,000 shares of preferred stock paying $17 dividend per share. Each share is convertible into 1 share of common stock. What is the diluted EPS for the company?
A. 11.46.
B. 14.90.
C. 15.38.

LO.i: Distinguish between dilutive and antidilutive securities, and describe the implications of each for the earnings per share calculation.

39. Convertible securities are antidilutive if they result in a:

A. Diluted EPS higher than the basic EPS.
B. Diluted EPS lower than the basic EPS.
C. Diluted EPS the same as that of the basic EPS.

LO.j: Convert income statements to common-size income statements.

40. Which of the following statements regarding common size statements is *least* accurate? Common size statements:
A. highlight the differences in the companies' strategies.
B. help in performing cross-sectional analysis.
C. can be used to compare companies with different accounting policies.

41. The following data is available for a company:

	$ (millions)
Total assets	220
Total revenues	485
Total expenses	373
R&D expenses	35

Under a common-size analysis, the R&D expense is *closest* to:
A. 15.9%.
B. 9.38%.
C. 7.21%.

LO.k: Evaluate a company's financial performance using common-size income statements and financial ratios based on the income statement.

42. Income statements for two companies (A and B) and the common-sized income statement for the industry are provided below:

All $ figures in '000s	**Company A**	**Company B**	**Industry**
Sales	854	620	100%
Cost of goods sold	548	394	73%
Selling, general, and administrative expenses	213	143	12%
Interest expense	85	72	9%
Pretax earnings	8	11	6%
Taxes	2	3	2%
Net earnings	6	8	4%

The *best* conclusion an analyst can make is that:
A. company B's interest rate is lower than the industry average.
B. both companies' tax rates are lower than the industry average.
C. company A earns a higher gross margin than both Company B and the industry.

43. The following table shows the income statements for three hypothetical companies.

	A	B	C
Sales	1,000,000	800,000	900,000
Cost of sales	750,000	600,000	650,000
Gross Profit	250,000	200,000	250,000
Selling expenses	75,000	60,000	80,000
General expenses	80,000	60,000	60,000
Operating Profit	95,000	80,000	110,000
Finance expense	20,000	20,000	20,000
Earnings before tax	75,000	60,000	90,000
Tax	30,000	24,000	36,000
Net Profit	45,000	36,000	54,000

Which of the following statements is *most likely* correct?

A. Company B has a greater profit margin compared to Company C and a lower profit margin compared to Company A.

B. The tax rate for Company A differs from that of Company B.

C. The operating profit margin for Company C is the highest.

LO.l: Describe, calculate, and interpret comprehensive income.

44. The following information is from a company's accounting records:

	€ millions
Revenues for the year	8,500
Total expenses for the year	6,900
Gains from available-for-sale securities	630
Loss on foreign currency translation adjustments on a foreign subsidiary	870
Dividends paid	500

The company's total comprehensive income (in € millions) is *closest* to

A. 860.

B. 1,100.

C. 1,360.

45. Under US GAAP, the change in equity during a period resulting from transactions and other events that are excluded from net income is best known as:

A. Total comprehensive income.

B. Unrealized gains and losses.

C. Translation adjustments.

LO.m: Describe other comprehensive income, and identify major types of items included in it.

46. Other comprehensive income *least likely* includes which of the following?
    A. Unrealized holding gains and losses on available-for-sale securities.
    B. Foreign currency translation adjustments.
    C. Unrealized gains and losses on held for trading securities.

47. The following information about a company is given:

	€ million
Beginning shareholder's equity	1,000
Net income	100
Cash dividends paid	20
Ending shareholder's equity	1200

    If no common stock was issued or repurchased, the other comprehensive income is *closest* to in (€ million):
    A. 80.
    B. 100.
    C. 120.

48. Other comprehensive income *least likely* includes which of the following? Gains and losses on:
    A. Foreign currency translation adjustments of subsidiaries.
    B. Derivative contracts accounted for as hedges.
    C. Sale of discontinued operations.

Solutions

1. B is correct. This is an example of grouping by nature.

2. A is correct. When subtotals are presented, the income statement follows a multi-step format.

3. B is correct. It is an element of the balance sheet.

4. A is correct. The revenue reported is equal to the percentage of the contract that is completed in that period, where percentage completion is based on costs.
   In Year 2: $\left(\frac{3.5}{8.7}\right) * 11.2 = 4.5$.

5. B is correct. The appropriate time to recognize revenue would be in the month of August; the risks and rewards have been transferred to the buyer (shipped and delivered), the revenue can be reliably measured, and it is probable that the economic benefits will flow to the seller.

6. A is correct. Receiving cash is not a pre-requisite for revenue recognition.

7. B is correct. The revenue recognized will be the total amount divided by the time period. Therefore, $\frac{\$50,000}{4}$ = $12,500.

8. B is correct. Under U.S. GAAP, revenue from barter transactions can be recognized at fair value only if the company has historically received cash payments for such services.

9. C is correct. Under U.S. GAAP, one of the criteria for deciding whether to report revenues gross or net is that the company *does* bear the inventory risk.

10. B is correct.

11. C is correct. Under US GAAP, revenue is recognized only when the product has been delivered, or the services have been rendered.

12. B is correct. When the outcome can be measured reliably the percentage-of-completion method is used. When the outcome cannot be measured reliably the completed contract method is used. The cost recovery method is used for installment sales, not for long-term projects.

13. B is correct. Under the installment method, the portion of the total profit that is recognized in each period is determined by the percentage of the total sales price for which the seller has received cash. For Company A, $\frac{2}{5} * 1$ = $0.4 million. Note: cost recovery method could be used in this case, but the reported profit would be $0.

14. C is correct. Percentage of completion is used for long term contracts before the goods are delivered. After the goods are delivered, installment method and cost recovery methods are used.

15. A is correct. In year 2, the revenue is: 15 million * $\frac{3,800,000}{8,500,000}$ = 6,705,882. The profit is: $6,705,882 - 3,800,000 = 2,905,882.$

16. A is correct. (2,000 / 4,500) * 5,000 = 2,222

17. B is correct. The core principle of the converged standard is that revenue should be recognized to "depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in an exchange for those goods or services".

18. C is correct. Both analysts are correct. Analyst 1 has identified the first two steps in the process. Analyst 2 correctly elaborates on the second step.

19. C is correct. Under IFRS, research and development costs are expensed until certain criteria are met, including that technical feasibility has been established and the company intends to use it

20. B is correct. Option A depicts the 'direct write-off method' which is a violation of the matching principle. Option B is consistent with the matching principle. Option C is not correct because the doubtful accounts expense is shown as a separate expense on the income statement and not as a reduction in revenue.

21. C is correct. Expenditures on advertising and research are required to support a product differentiation strategy. The effect on inventory is uncertain.

22. B is correct. IFRS requires the effective interest method for the amortization of bond discounts/premiums. The bond is issued for 0.9604 * €10 million = €9.604 million.
    Interest expense = Liability value * Market rate at issuance: 0.045 × €9.604 million = €432,180.

23. B is correct. The matching concept is followed for expense recognition, whereby revenues and expenses are matched.

24. A is correct. The FIFO costing method is first in, first out. Therefore, the ending inventory comprises of the latest items purchased which are likely to have greater prices. In a period of rising prices, FIFO has the highest ending inventory.

25. A is correct.
    Quarter 1 inventory: (1000-900) * 75 = $7,500
    Quarter 2 inventory: (1000-900-50) * 75 = $3,750
    Inventory remaining: $3,750

This concept is covered in more detail in the reading on inventory.

26. C is correct. Statement A is incorrect because the matching principle requires the company to estimate the uncollectible accounts and not adopt the direct write off method. Statement B is incorrect because the estimate is recorded as an expense. Statement C is correct.

27. C is correct.

$$\text{Depreciation Expense} = \frac{\text{Purchase Price} - \text{Residual Value}}{\text{Life of Asset}} = \frac{100{,}000 - 15{,}000}{5} = 17{,}000$$

$$\text{Balance of machine after three years} = 100{,}000 - (17{,}000 * \ 3) = \$49{,}000$$

28. B is correct. With the double declining method, depreciation is twice that compared to straight line depreciation. Since the straight line depreciation would be 20%, the double declining method depreciation is 40%. Hence, the depreciation is 40,000 for Year 1.

29. A is correct. Investments are not part of the core business. Discontinued operations are non-recurring items.

30. B is correct. IFRS prohibits items to be categorized as extraordinary, while U.S. GAAP permits this categorization.

31. C is correct. Retrospective application applies to the presentation of financial statements for previous fiscal years, according to newly adopted principles.

32. B is correct.
Operating Profit = 500,000 – 180,000 – 100,000 – 50,000 = 170,000.

33. A is correct.

	$’000s	
Revenue	10,000	
Less: Cost of goods sold	(6,000)	
Less: Other operating expenses	(1,500)	
Less: Restructuring costs	(300)	Restructuring charges are classified as operating items under U.S GAAP
Operating Profit	2,200	

34. A is correct.

	Basic EPS	Diluted EPS: Bonds converted	Diluted EPS: Preferred converted	Diluted EPS: Both converted
NI	2,500,000	2,500,000	2,500,000	2,500,000
Preferred	(25,000)	(25,000)		

dividends				
After-tax cost of interest .06 x 60,000 x (1-.35)		2,340		2,340
Numerator	2,475,000	2,477,340	2,500,000	2,502,340
Shares	150,000	150,000	150,000	150,000
Preferred converted			25,000	25,000
Bond converted		12,000		12,000
Denominator	150,000	162,000	175,000	187,000
EPS	16.5	15.29	14.29	13.38

35. B is correct.
Incremental shares issued from stock option exercise (Treasury Stock Method):
100,000 shares – $\frac{100,000*10}{20}$ = 50,000 shares

Weighted average shares outstanding:
Original shares = 3,000,000 [3,000,000 shares × 12 months/12 months]
Incremental shares issued assuming options were exercised = 50,000 [50,000 shares × 12 months/12 months]
Shares issued, April 1 = 375,000 [500,000 shares × 9 months/12 months]
Shares repurchased, July 1 = (50,000) [100,000 shares × 6 months/12 months]
Weighted average shares outstanding = 3,375,000

Diluted EPS
5,000,000 / 3,375,000 = $1.48/share

36. A is correct.

	Basic EPS	Diluted EPS	
NI	2,000,000	2,000,000	Currently pays a dividend of $2 per share
Preferred stock, type A	(120,000)	(120,000)	20,000 * $6
Preferred stock, type B	(112,500)	0	15,000 * $7.5
Earnings available to common shareholder	1,767,500	1,880,000	
Shares	300,000	300,000	
Shares, if converted	-	30,000	2 * 15,000
Weighted average common shares	300,000	330,000	
EPS	5.89	5.70	

37. A is correct. Basic EPS $= \frac{(\text{Net Income – Preferred Dividend})}{\text{Number of shares outstanding}} = \frac{8}{20}$ = 0.40.

38. B is correct.
    Diluted earnings per share
    $$= \frac{\text{Net income}}{\text{Weighted average number of shares outstanding} + \text{New common shares}}$$
    $$\text{Diluted earning per share} = \frac{1{,}000{,}000}{50{,}000 + 15{,}000} = 15.38$$
    $$\text{Basic earning per share} = \frac{\text{Net income} - \text{Preferred Dividends}}{\text{Weighted average number of shares outstanding}}$$
    $$\text{Basic earning per share} = \frac{1{,}000{,}000 - 255{,}000}{50{,}000} = 14.9$$
    Since the diluted EPS exceeds the basic EPS, the reported diluted EPS is equal to basic EPS.

39. A is correct. Diluted EPS will always be less than or equal to basic EPS. Convertible securities are not included in the calculation if they result in a higher diluted EPS than basic EPS.

40. C is correct. Since it is a ratio, differences in accounting policies and accounting calendars make comparison difficult.

41. C is correct. In a common-size income statement, each element is expressed as a percentage of revenue.

42. B is correct.
    Tax rate for industry = 2/6 = 33.33%
    Tax rate for Company A = 2/8 = 25%
    Tax rate for Company B = 3/11 = 27%
    Gross margin for industry = 100 – 73 = 27%
    Gross margin for Company A = $\frac{854 - 548}{854}$ = 35.8%
    Gross margin for Company B = $\frac{620 - 394}{620}$= 36.5%
    The interest rate is not a function of sales and cannot be analyzed on a common-sized income statement.

43. C is correct. The profit margin for the company is given by$\frac{(\text{Net Profit})}{\text{Sales}} * 100\%$. The profit margins for Company A, B, and C are 4.5%, 4.5%, and 6% respectively. Therefore, statement A is incorrect.
    The tax rate for the company is given by$\left(\frac{\text{Tax}}{\text{EBT}}\right) * 100\%$. The tax rate for the three companies is 40%. So, statement B is incorrect.
    The operating profit margin for the company is given by$\frac{(\text{Operating Profit})}{\text{Sales}} * 100\%$. The operating profit margin for Company A, B, and C are 9.5%, 10%, and 12.2%. So, statement C is correct.

44. C is correct.
    Total comprehensive income = Net income + other comprehensive income
    Net income = Revenues – Expenses
    Other comprehensive income includes gains or losses on available-for-sale securities and translations adjustments on foreign subsidiaries.
    (Revenues – Expenses) + Gain on AFS – Loss on FX translation
    (8500 – 6900) + 630 – 870 = 1,360.

45. A is correct.

46. C is correct.

47. C is correct. Beginning Equity + Net Income + OCI – Dividend = Ending Equity. Hence: 1,000 + 100 + OCI – 20 = 1,200. OCI = 1200 – (1000 + 100 - 20) = 120.

48. C is correct.