

GAAP Fundamentals and Balance Sheet Essentials

Get a solid foundation in GAAP with this opening section of the comprehensive guide. Focused on the balance sheet, this course walks through core questions and answers that help clarify how assets, liabilities, and equity are presented under GAAP. Whether you're refreshing your knowledge or building a stronger technical base, this course addresses the practical issues that come up most often when preparing or reviewing GAAP-compliant financial statements.

CREDIT HOURS 2

FIELD OF STUDY ACCOUNTING

EXAM QUESTIONS 10

[Start Course ↓](#)[Final Exam Copy ↓](#)

LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Recall the accounting treatment for non-monetary exchanges.
- Recognize the formula for measuring an impairment of real estate.
- Identify the accounting for different types of investments, such as securities, investments using the equity method, and partnerships.

Copyright Notice

© 2026 Pacific CPE, LP. All rights reserved.

This course and test have been adapted from supplemental material and uses the materials entitled GAAP- Tax-Basis Q&A - 2026 © 2026 Fustolo Publishing LLC. Displayed by permission of the author. All rights reserved.

The materials in this course — including the text, illustrations, exhibits, examples, exam questions, and review questions — are the copyrighted property of Pacific CPE, LP. No portion of this course may be reproduced, stored in a retrieval system, distributed, or transmitted in any form or by any means (electronic, mechanical, photocopying, recording, or otherwise) without the prior written permission of Pacific CPE, LP, except for the personal, non-commercial use of the registered learner.

Pacific CPE, LP grants the registered learner a single-seat, non-transferable license to access this course for the purpose of completing the associated continuing professional education credit. Account credentials may not be shared.

This course is provided "as is" for educational purposes. While Pacific CPE, LP makes a reasonable effort to ensure the content is current and accurate, the materials should not be relied upon as a substitute for professional advice. Pacific CPE, LP disclaims all liability for any error, omission, or loss arising from the use of, or reliance on, the course content.

Publication Date: March 2026

TABLE OF CONTENTS

CHAPTER

01

Section 1. Gaap Q & A..... 4

1.01 Introduction..... 4

1.02 I. Balance Sheet 4

1.03 A. Comparative Statements/Individual Statements 4

1.04 B. Property And Equipment 6

Test Your Knowledge..... 31

CHAPTER

02

Section 2..... 37

2.01 C. Cash And Investments..... 37

Test Your Knowledge..... 59

Final Exam Copy..... 66

Index 66

SECTION 1. GAAP Q & A

Chapter Objective

After completing this section, you should be able to:

- Recall the accounting treatment for non-monetary exchanges.
- Recognize the formula for measuring an impairment of real estate.

INTRODUCTION

In 2009, the FASB *completed* its *Accounting Standards Codification*[™] (Codification), which was published in FASB No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles (FASB ASC 105)*. The Codification was effective for interim and annual periods ending after September 15, 2009.

With the Codification, the FASB had as its goal to consolidate U.S. GAAP into one system that can be more easily researched by topic, rather than by reference number. The Codification changes the citations for GAAP from the typical FASB or APB statement number to an Accounting Standards Codification (FASB ASC) reference. For example, FASB No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, has been codified into FASB ASC Topic 825, *Financial Instruments*^{**}.

In this course, the author has, in some instances, included the original U.S. GAAP reference (e.g., FASB No. 115) parenthetically along with the FASB ASC topic number under the Codification (e.g., FASB ASC 320). For abbreviation purposes, the author uses the terms ASC, FASB ASC and FASB ASC Topic, interchangeably.

I. BALANCE SHEET

A. COMPARATIVE STATEMENTS/INDIVIDUAL STATEMENTS

Question: Are both a balance sheet and an income statement (and also a statement of cash flows) required for all annual reports, and must all such statements be in comparative form for at least two years?

Response: ASC 205, *Presentation of Financial Statements*, recommends, but does not require comparative financial statements. However, the SEC requires comparative financial statements for publicly held companies.

Question: Is either the balance sheet or income statement alone a fair presentation? Does a balance sheet alone fairly present the financial position if the client incurred a material operating loss during the current year?

Response: With respect to presenting one financial statement, reference can be made to SAS No. 122, AU-C Section 805, *Special Considerations – Audits of Single Financial Statements and Specific Elements, or Items of a Financial Statement*.¹

1. AU-C 805 permits the auditor to report on a single financial statement, such as a balance sheet or income statement.

An auditor may be asked to report on one basic financial statement and not on the others. For example, he or she may be asked to report on the balance sheet and not on the statements of income, retained earnings, or cash flows. These engagements do not involve scope limitations if the auditor's access to information underlying the basic financial statements is not limited and if the auditor applies all the procedures the auditor considers necessary in the circumstances.

Therefore, a separate balance sheet may fairly present financial position, and a separate *statement of income* may fairly present results of operations.

Question: When financial statements are presented, should the notes to financial statements disclose details for both periods?

Response: Generally, notes should relate to all periods presented, provided such information is relevant to both periods. In practice, many practitioners present certain *disclosures* comparatively (e.g., fixed assets, long-term debt), yet other disclosures for the current period only (e.g., short-term notes receivable and payable).

Amendment made by ASU 2025-12:

In December 2025, the FASB issued ASU 2025-12: *Codification Improvements*. The ASU amends ASC 205, Presentation of Financial Statements, to clarify which financial statements should be presented comparatively when an entity chooses to present comparative financial statements. Prior to the ASU 2025-12 amendment, the language in ASC 205 was ambiguous as to whether a statement of cash flows and a statement of comprehensive income were part of “financial statements” that should be presented comparatively if comparative financial statements were presented.

More specifically, ASC 205-10-45-2, *Presentation of Financial Statements- Overall- Other Presentation Matters*, states that, when comparative financial statements are issued, an entity should typically present the following elements comparatively (current year and one or more preceding years).

- Statement of financial position
- Income statement, and

- Statement of changes in equity

This list excludes a statement of cash flows and statement of comprehensive income, suggesting that if comparative financial statements were to be issued, single-year financial statements could be issued for the statement of cash flows and statement of comprehensive income.

Yet, ASC 205-10-45-2 language indicates that a full set of financial statements should include a statement of cash flows and the statement of comprehensive income.

Thus, there was a contradiction of language found within ASC 205, which required clarification.

ASU 2025-12 clears up the confusion by amending ASC 205-10-45-2 to remove specifically listed financial statements and replace them with the term “financial statements,” which *includes* the statement of cash flows and, if applicable, the statement of comprehensive income. Now, if an entity does issue comparative financial statements, all financial statements (including the statement of cash flows and statement of comprehensive income) should be presented comparatively.

The amendment made by ASU 2025-12 is effective for all entities for annual reporting periods beginning after December 15, 2026. Early application is permitted.

B. PROPERTY AND EQUIPMENT

1. Idle Property and Equipment

Question: What is the appropriate balance sheet classification and presentation of idle property and equipment? Should the property and equipment continue to be depreciated while idle?

Response: ASC 360, Property, Plant and Equipment, states that when a long-lived asset ceases to be used, the carrying amount of the asset should equal its salvage value, which should not be less than zero. Accounting Research Study No. 7, **Inventory of Generally Accepted Accounting Principles for Business Enterprises**, provides further guidance by stating:

“Plant assets may include property held with reasonable expectation of it being used in the business. It is not customary to segregate or indicate the existence of temporarily idle plant, reserve, or standby equipment.

Property abandoned but not physically retired or no longer adapted for use in the business, if material in amount, should be removed from plant accounts and recorded separately at an estimated (net) realizable amount, appropriately explained.

When a material portion of plant and equipment has been idle for a protracted period with no apparent likelihood of resuming operations, the amount should be set forth separately with an appropriate caption.

Depreciation should continue only if the equipment is temporarily idle and it is expected that operations will resume at some time.”

2. Categorization of a Building

Question: A corporation purchased a building and intends to sell it within six months. Should it be accounted for as an investment or fixed asset? Should it be depreciated?

Response: ASC 360, *Property, Plant and Equipment*, states that GAAP requires that the cost of a productive facility be spread over its expected useful life. Because the building is not a productive facility, and no services will be derived from it, it should not be depreciated. Instead, it should be carried at the lower of cost or net realizable value (estimated selling price less selling costs) and categorized as a current asset since it will be converted into cash within six months.

3. Deposit on Machinery

Question: What is the balance sheet classification of a deposit on machinery to be purchased within one year?

Response: ASC 340, *Other Assets and Deferred Costs*, states that the concept of a current asset excludes any resources that are restricted as to withdrawal or use for other than current operations. Accordingly, the deposit should be presented as a long-term asset even though the equipment will be purchased within one year.

4. Non-Monetary Exchanges

Question: What are the accounting rules for non-monetary exchanges?

Response: The authority for non-monetary transactions is found in ASC 845, *Non-Monetary Transactions*.

The general rule is that exchanges of non-monetary assets should be accounted for at the fair value of the asset surrendered or asset received, whichever is more determinable.

ASC 845 provides three exceptions from the general rule under which the transaction is recorded at carrying value (book value) instead of fair value. These exceptions are:

- a. Fair value is not determinable: The fair value of the asset(s) received, or the asset(s) relinquished, is not determinable within reasonable limits.
- b. Exchange transaction to facilitate sales to customers: The transaction is an exchange of a product or property held for sale in the ordinary course of business for a product or property to be sold in the same line of business to facilitate sales to customers other than the parties to the exchange.
- c. Exchange transaction that lacks commercial substance: The transaction lacks commercial substance.

Lacks commercial substance exception:

Under the lacks commercial substance rule, if an exchange of nonmonetary assets lacks commercial substance, it is accounted for at book value, not fair value.

1. A transaction lacks commercial substance if:

- a) The configuration of future cash flows of the asset received do not differ significantly from the future cash flows of the asset transferred, or
- b) The entity-specific *value of the asset received* does not differ significantly from the entity-specific value of the asset given.

Note

The three elements of configuration of future cash flows consist of risk, timing, and amount of cash flows.

- 2. Under the lack of commercial substance exception, transactions are recorded using a book value approach (rather than using fair value) with no gain or loss recognized.
- 3. If an exchange transaction lacks commercial substance (such as most motor vehicle trade ins), ASC 845 requires the transaction to be accounted for at book value as follows:

$$\text{Book value of the asset given} + \text{Cash paid}_2 = \text{Cost of the asset received}$$

- 4. Most exchanges of similar type assets, such as motor vehicle and truck trade-ins, where the overall purpose and use of the assets does not differ, and there is not a significant amount of cash (boot) given, qualify for the book value approach in ASC 845.
- 5. If the exchange involves 25% or more of monetary consideration (e.g., cash given or received), the transaction does not lack commercial substance and should be accounted for at fair value as follows:

Entry:	dr	cr
Asset received (fair value)	XX	
Book value of old asset given		XX
Cash given or loan payable		XX
Gain on transaction		XX

Note

Most motor vehicle trade-ins lack commercial substance and are accounted for at book value as long as the cash paid with the trade in is less than 25% of the total fair value of the transaction. Moreover, financing obtained is considered cash in determining the 25% threshold.

How do you determine whether a transaction lacks commercial substance?

ASC 845 provides that the assessment of commercial substance may be made either quantitatively (e.g., cash flow analysis) or qualitatively by comparing the configuration (risk, timing, and amount) of the future cash flows of the assets exchanged. Further, ASC 845 states that a significant difference in any one of the three elements (risk, timing and amount) of cash flows means that the transaction has commercial substance and thus is recorded at fair value.

A practical way in which to determine whether a transaction lacks commercial substance is to focus only on the “timing” element of future cash flows because it can be easily assessed qualitatively. This *qualitative assessment* of the timing of cash flows can be made simply by comparing the remaining useful lives of the exchanged assets with the theory being that the useful lives represent the remaining time over which the assets will generate cash flows for the entity.

If the remaining useful life of the asset received differs significantly from the useful life of the asset surrendered, the transaction has commercial substance and is recorded at fair value. Conversely, if the useful lives do not differ significantly, a carrying value approach should be used.

Following are several examples that illustrate the application of ASC 845.

Example 1: Company X trades in a motor vehicle with a carrying value of \$10,000 for a new motor vehicle. No cash is exchanged. The remaining useful life of the old motor vehicle at the time of the exchange is 3 years. The useful life of the new motor vehicle is 3 years.

Conclusion: The transaction lacks commercial substance and is recorded at carrying value. The configuration (risk, timing, and amount) of future cash flows of the motor vehicle received *does not differ significantly* from that of the motor vehicle transferred. More specifically, the timing of the cash flows to be generated from the asset received (3 years) is the same as the timing of the cash flows generated from the asset given (3 years).

Entry:	dr	cr
New motor vehicle	10,000	
Book value of old motor vehicle		10,000

Example 2: Company X trades in an old truck with a carrying value of \$100,000 for a new truck plus \$30,000 cash paid. The fair value of the new truck received is \$220,000.

In general, the configuration of future cash flows of the motor vehicle received *does not differ significantly* from the future cash flows of the motor vehicle transferred.

Conclusion: Because cash is given, X must make sure that the cash paid of \$30,000 is less than 25% of the total fair value of the transaction. If it is, the transaction is nonmonetary and is recorded at book value as it lacks commercial substance.

In this example, cash of \$30,000 is only 13.6% of the total fair value of the transaction ($\$30,000/\$220,000 = 13.6\%$).

Further, because the configuration of the future cash flows of the new motor vehicle does not differ significantly from the future cash flows of the motor vehicle transferred, the transaction lacks commercial substance, and a book value approach is used to record the transaction.

Company X records the asset at the book value of the truck given, plus the \$30,000 of cash paid as follows:

<u>Entry: Book purposes:</u>	<u>dr</u>	<u>cr</u>
New truck	130,000	
Book value of old truck		100,000
Cash		30,000

What if the cash given equals or exceeds 25% of the fair value of the transaction?

For GAAP, most trade ins of motor vehicles lack commercial substance and use a book value approach as long as the amount of cash given does not equal or exceed 25% of the fair value. In the previous example, cash of \$30,000 is only 13.6% of the total fair value of the transaction ($\$30,000/\$220,000 = 13.6\%$) so that a book value approach is required under GAAP.

Let's change the facts:

Assume in the previous example, cash given is \$30,000 plus a \$40,000 bank loan.

Total cash given is \$70,000 (\$30,000 cash plus \$40,000 loan), which is 32% of total fair value as follows: $\$70,000/\$220,000 = 32\%$.

In such a case, ASC 845 provides that the transaction *does not lack commercial substance* because the cash is 25% or more of the total fair value of the transaction. Thus, the transaction is recorded at *fair value for GAAP* as follows: