AUDITING THEORY TEST BANK

ASSURANCE SERVICES

1. Which of the following statements best describes assurance services?

A. Independent professional services that are intended to enhance the credibility of information to meet the needs of an intended user.

B. Services designed to express an opinion on the fairness of historical financial statements based on the results of an audit.

C. The preparation of financial statements or the collection, classification, and summarization of other financial information.

D. Services designed for the improvement of operations, resulting in better outcomes.

2. Which of the following is not an assurance service?

A. Examination of prospective financial information

B. Audit of historical financial statements

C. Review of financial statements

D. Compilation of financial information

3. Suitable criteria are required for reasonably consistent evaluation or measurement of the subject matter of an assurance engagement. Which of the following statements concerning the characteristics of suitable criteria is correct?

A. Reliable criteria contribute to conclusions that are clear, comprehensive, and not subject to significantly different interpretations.

B. Relevant criteria allow reasonably consistent evaluation or measurement of the subject matter including, where relevant, presentation and disclosure, when used in similar circumstances by similarly qualified practitioners.

C. Neutral criteria contribute to conclusions that are free from bias.

D. Criteria are sufficiently complete when they contribute to conclusions that are clear, comprehensive, and not subject to different interpretations.

4. In an assurance engagement, the outcome of the evaluation or measurement of a subject matter against criteria is called

A. Subject matter information

B. Subject matter

C. Assurance

D. Conclusion

5. What type of assurance engagement is involved when the practitioner expresses a positive form of conclusion?

A. Limited assurance engagement

B. Positive assurance engagement

C. Reasonable assurance engagement

D. Absolute assurance engagement

6. What type of assurance engagement is involved when the practitioner expresses a negative form of conclusion?

A. Reasonable assurance engagement

B. Negative assurance engagement

C. Assertion-based assurance engagement

D. Limited assurance engagement

7.  Which of the following statements is true concerning evidence in an assurance engagement?

A. Sufficiency is the measure of the quantity of evidence.

B. Appropriateness is the measure of the quality of evidence, that is, its reliability and persuasiveness.

C. The reliability of evidence is influenced not by its nature but by its source.

D. Obtaining more evidence may compensate for its poor quality.

8. Assurance engagement risk is the risk

A. That the practitioner expresses an inappropriate conclusion when the subject matter information is materially misstated.

B. Of expressing an inappropriate conclusion when the subject matter information is not materially misstated.

C. Through loss from litigation, adverse publicity, or other events arising in connection with a subject matter reported on.

D. Of expressing an inappropriate conclusion when the subject matter information is either materially misstated or not materially misstated.

9. Reducing assurance engagement risk to zero is very rarely attainable or cost beneficial as a result of the following factors, except

A. The use of selective testing.

B. The fact that much of the evidence available to the practitioner is persuasive rather than conclusive.

C. The practitioner may not have the required assurance knowledge and skills to gather and evaluate evidence.

D. The use of judgment in gathering and evaluating evidence and forming conclusions based on that evidence.

10. The Philippine Framework for Assurance Engagements

A. Contains basic principles, essential procedures, and related guidance for the performance of assurance engagements.

B. Defines and describes the elements and objectives of an assurance engagement, and identifies engagements to which PSAs, PSREs, and PSAEs apply.

C. Provides a frame of reference for CPAs in public practice when performing audits, reviews, and compilations of historical financial information.

D. Establishes standards and provides procedural requirements for the performance of assurance engagements.

AUDITING AND RELATED SERVICES

11. PSRE 2400 (Engagements to Review Financial Statements), as amended by the AASC in February 2008, applies to

A. Reviews of any historical financial information of an audit client.

B. Reviews of any historical financial information by a practitioner other than the entity’s auditor.

C. Reviews of historical financial or other information by a practitioner other than the entity’s auditor.

D. Reviews of historical financial or other information of an audit client.

12. When performing a compilation engagement, the accountant is required to

A. Assess internal controls.

B. Make inquiries of management to assess the reliability and completeness of the information provided.

C. Verify matters and explanations.

D. Obtain a general knowledge of the business and operations of the entity.

13. Inquiries and analytical procedures ordinarily form the basis for which type of engagement?

A. Agreed-upon procedures.

B. Audit.

C. Examination.

D. Review.

14. A practitioner should accept an assurance engagement only if

A. The subject matter is in the form of financial information.

B. The criteria to be used are not available to the intended users.

C. The practitioner’s conclusion is to be contained in a written report.

D. The subject matter is the responsibility of either the intended users or the practitioner.

15. The auditor is required to maintain professional skepticism throughout the audit. Which of the following statements concerning professional skepticism is false?

A. A belief that management and those charged with governance are honest and have integrity relieves the auditor of the need to maintain professional skepticism.

B. Maintaining professional skepticism throughout the audit reduces the risk of using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.

C. Professional skepticism is necessary to the critical assessment of audit evidence.

D. Professional skepticism is an attitude that includes questioning contradictory audit evidence obtained.

16. Which of the following best describes the reason why independent auditors report on financial statements?

A. A management fraud may exist and it is more likely to be detected by independent auditors.

B. Different interests may exist between the company preparing the statements and the persons using the statements.

C. A misstatement of account balances may exist and is generally corrected as the result of the independent auditors’ work.

D. Poorly designed internal control may be in existence.

17. Which of the following professionals has primary responsibility for the performance of an audit?

A. The managing partner of the firm.

B. The senior assigned to the engagement.

C. The manager assigned to the engagement.

D. The partner in charge of the engagement.

18. What is the proper organizational role of internal auditing?

A. To serve as an independent, objective assurance and consulting activity that adds value to operations.

B. To assist the external auditor in order to reduce external audit fees.

C. To perform studies to assist in the attainment of more efficient operations.

D. To serve as the investigative arm of the audit committee of the board of directors.

19. Operational audits generally have been conducted by internal and COA auditors, but may be performed by certified public accountants. A primary purpose of an operational audit is to provide

A. A measure of management performance in meeting organizational goals.

B. The results of internal examinations of financial and accounting matters to a company’s top-level management.

C. Aid to the independent auditor, who is conducting the examination of the financial statements.

D. A means of assurance that internal accounting controls are functioning as planned.

20. Which of the following terms best describes the audit of a taxpayer’s return by a BIR auditor?

A. Operational audit.

B. Internal audit.

C. Compliance audit.

D. Government audit.

21. Which of the following statements concerning consulting services is false?

A. The performance of consulting services for audit clients does not, in and of itself, impair the auditor’s independence.

B. Consulting services differ fundamentally from the CPA’s function of attesting to the assertions of other parties.

C. Consulting services ordinarily involve external reporting.

D. Most CPAs, including those who provide audit and tax services, also provide consulting services to their clients.

22. Which of the following is the most appropriate action to be taken by a CPA who has been asked to perform a consulting services engagement concerning the analysis of a potential merger if he/she has little experience with the industry involved?

A. Accept the engagement but he/she should conduct research or consult with others to obtain sufficient competence.

B. Decline the engagement because he/she lacks sufficient knowledge.

C. Accept the engagement and issue a report that contains his/her opinion on the achievability of the results of the merger.

D. Accept the engagement and perform it in accordance with Philippine Standards on Auditing (PSAs).

23. An objective of a performance audit is to determine whether an entity’s

A. Operational information is in accordance with government auditing standards.

B. Specific operating units are functioning economically and efficiently.

C. Financial statements present fairly the results of operations.

D. Internal control is adequately operating as designed.

24. The internal auditing department’s responsibility for deterring fraud is to

A. Establish an effective internal control system.

B. Maintain internal control.

C. Examine and evaluate the system of internal control.

D. Exercise operating authority over fraud prevention activities.

25. Internal auditors review the adequacy of the company’s internal control system primarily to

A. Help determine the nature, timing, and extent of tests necessary to achieve audit objectives.

B. Determine whether the internal control system provides reasonable assurance that the company’s objectives and goals are met efficiently and economically.

C. Ensure that material weaknesses in the system of internal control are corrected.

D. Determine whether the internal control system ensures that financial statements are fairly presented.

THE ACCOUNTANCY PROFESSION

26. The members of the Professional Regulatory Board of Accountancy shall be appointed by the

A. Philippine Institute of CPAs (PICPA).

B. Professional Regulation Commission (PRC).

C. President of the Philippines.

D. Association of CPAs in Public Practice (ACPAPP).

27. The following statements relate to the submission of nominations to the Board of Accountancy. Which is correct?

A. The Accredited National Professional Organization of CPAs (APO) shall submit its nominations to the president of the Philippines not later than sixty (60) days prior to the expiry of the term of an incumbent chairman or member.

B. The APO shall submit its nominations to the PRC not later than thirty (30) days prior to the expiry of the term of an incumbent chairman or member.

C. If the APO fails to submit its own nominee(s) to the PRC within the required period, the PRC in consultation with the Board of Accountancy shall submit to the president of the Philippines a list of five (5) nominees for each position.

D. There should be adequate documentation to show the qualifications and primary field of professional activity of each nominee.

28. The following statements relate to the term of office of the chairman and members of the Board of Accountancy (BOA). Which is false?

A. The chairman and members of the BOA shall hold office for a term of three (3) years.

B. Any vacancy occurring within the term of a member shall be filled up for the unexpired portion of the term only.

C. No person who has served two successive complete terms as chairman or member shall be eligible for reappointment until the lapse of two (2) years.

D. Appointment to fill up an unexpired term is not to be considered as a complete term.

29. The Board of Accountancy has the power to conduct an oversight into the quality of audits of financial statements through a review of the quality control measures instituted by auditors in order to ensure compliance with the accounting and auditing standards and practices. This power of the BOA is called

A. Quality assurance review C. Appraisal

B. Peer review D. Quality control

30. Which of the following statements concerning the issuance of Certificates of Registration and Professional Identification Cards to successful examinees is correct?

A. The Certificate of Registration issued to successful examinees is renewable every three (3) years.

B. The Professional Identification Card issued to successful examinees shall remain in full force and effect until withdrawn, suspended or revoked in accordance with RA 9298.

C. The BOA shall not register and issue a Certificate of Registration and Professional Identification Card to any successful examinee of unsound mind.

D. The BOA may, after the expiration of three (3) years from the date of revocation of a Certificate of Registration, reinstate the validity of a revoked Certificate of Registration.

31. Which of the following statements concerning ownership of working papers is incorrect?

A. All working papers made by a CPA and his/her staff in the course of an examination remain the property of such CPA in the absence of a written agreement between the CPA and the client to the contrary.

B. Working papers include schedules and memoranda prepared and submitted by the client of the CPA.

C. Working papers include reports submitted by a CPA to his/her client.

D. Working papers shall be treated confidential and privileged unless such documents are required to be produced through subpoena issued by any court, tribunal, or government regulatory or administrative body.

32. Any person who shall violate any of the provisions of the Accountancy Act or any of its implementing rules and regulations promulgated by the Board of Accountancy subject to the approval of the PRC, shall, upon conviction, be punished by

A. A fine of not more than P50,000.

B. Imprisonment for a period not exceeding two years.

C. A fine of not less than P50,000 or by imprisonment for a period not exceeding two years or both.

D. Lethal injection.

33. A partner surviving the death or withdrawal of all the other partners in a partnership may continue to practice under the partnership name for a period of not more than how many years after becoming a sole proprietor?

A. 1 C. 3

B. 2 D. 4

34. The death or disability of an individual CPA and/or the dissolution and liquidation of a firm or partnership of CPAs shall be reported to the BOA not later than how many days from the date of such death, dissolution or liquidation.

A. 15 C. 60

B. 30 D. 90

35. Which of the following statements concerning a CPA’s disclosure of confidential client information is ordinarily correct?

A. Disclosure may be made to any party on consent of the client.

B. Disclosure should not be made even if such disclosure will protect the CPA’s professional interests in legal proceedings.

C. Disclosure should be made only if there is a legal or professional duty to make the disclosure.

D. Disclosure may be made to any government agency without subpoena.

THE CPA’S PROFESSIONAL RESPONSIBILITIES

36. Which of the following statements best explains why the CPA profession has found it essential to establish ethical standards and means for ensuring their observance?

A. Vigorous enforcement of an established code of ethics is the best way to prevent unscrupulous acts.

B. Ethical standards that emphasize excellence in performance over material rewards establish a reputation for competence and character.

C. A distinguishing mark of a profession is its acceptance of responsibility to the public.

D. A requirement for a profession is to establish ethical standards that stress primarily a responsibility to clients and colleagues.

37. Which of the following will not create self-interest threat for a professional accountant in public practice?

A. The possibility of losing a significant client.

B. Direct financial interest in the assurance client.

C. Undue dependence on total fees from a client.

D. Preparing the original data used to generate records that are the subject matter of the assurance engagement.

38. Familiarity threat could be created under the following circumstances except

A. A professional accountant accepting gifts from a client whose value is inconsequential or trivial.

B. Senior personnel having a long association with the assurance client.

C. A director or officer of the client or an employee in a position to exert significant influence over the subject matter of the engagement having recently served as the engagement partner.

D. A member of the engagement team having a close or immediate family member who is a director or officer of the client.

39. Which of the following circumstances may create advocacy threat for a professional accountant in public practice?

A. The firm promoting shares in an audit client.

B. A firm issuing an assurance report on the effectiveness of the operation of financial systems after designing or implementing the systems.

C. A firm being threatened with dismissal from a client engagement.

D. A firm being concerned about the possibility of losing a significant client.

40. The following circumstances may create intimidation threats, except

A. Being threatened with dismissal or replacement in related to a client engagement.

B. Being pressured to reduce inappropriately the extent of work performed in order to reduce fees.

C. Being threatened with litigation.

D. A member of the assurance team being, or having recently been, a director or officer of the client.

41. Which of the following is an example of engagement-specific safeguards in the work environment?

A. Advising partners and professional staff of those assurance clients and related entities from which they must be independent.

B. Disclosing to those charged with governance of the client the nature of service provided and extent of fees charged.

C. A disciplinary mechanism to promote compliance with the firm’s policies and procedures.

D. Published policies and procedures to encourage and empower staff to communicate to senior levels within the firm any issue relating to compliance with the fundamental principles that concerns them.

42. According to Section 240 of the Code of Ethics, fees charged for assurance engagements should be a fair reflection of the value of the work involved. In determining professional fees, the following should be taken into account, except

A. The time necessarily occupied by each person engaged on the work.

B. The outcome or result of a transaction or the result of the work performed.

C. The skill and knowledge required for the type of work involved.

D. The level of training and experience of the persons necessarily engaged on the work.

43. Financial interests may be held through an intermediary (for example, a collective investment vehicle, estate or trust). When control over the investment vehicle or the ability to influence investment decisions exists, the code defines that financial interest to be

A. Direct financial interest.

B. Material direct financial interest.

C. Indirect financial interest.

D. Material indirect financial interest.

44. The concept of materiality is least important to an auditor when considering the

A. Effects of a direct financial interest in the client upon the auditor’s independence.

B. Decision whether to use positive or negative confirmations of accounts receivable.

C. Adequacy of disclosure of a client’s illegal act.

D. Discovery of weaknesses in a client’s internal control.

45. A direct financial interest or a material indirect financial interest in the audit client of a member of the audit team or his immediate family member may create a significant self-interest threat. Which of the following safeguards would be least likely considered to eliminate the threat or reduce it to an acceptable level?

A. Discuss the matter with those charged with governance of the audit client.

B. Dispose of the direct financial interest prior to the individual becoming a member of the audit team.

C. Dispose of the indirect financial interest in total or dispose of a sufficient amount of it so that the remaining interest is no longer material prior to the individual becoming a member of the audit team.

D. Remove the member of the audit team from the audit engagement.

46. When an immediate family member of a member of the assurance team is a director, an officer, or an employee of the assurance client in a position to exert direct and significant influence over the subject matter information of the assurance engagement, or was in such a position during the period covered by the engagement, the threats to independence can only be reduced to an acceptable level by

A. Where possible, structuring the responsibilities of the assurance team so that the professional does not deal with matters that are within the responsibility of the immediate family member.

B. Withdrawing from the assurance engagement.

C. Removing the individual from the assurance team.

D. Discussing the issue with those charged with governance, such as the audit committee.

47. Which of the following would not generally create a threat to independence?

A. The purchase of goods and services from an assurance client by the firm (or from a financial statement audit client by a network firm) or a member of the assurance team provided that the transaction is in the normal course of business and on an arm’s length basis.

B. A partner or employee of the firm or a network firm serves as Company Secretary for a financial statement audit client.

C. Determining which recommendations of the firm should be implemented.

D. Reporting, in a management role, to those charged with governance.

48. The following forms of assistance to a financial statement audit client do not generally threaten the firm’s independence, except

A. Analyzing and accumulating information for regulatory reporting.

B. Assisting in resolving account reconciliation problems.

C. Authorizing or approving transactions.

D. Assisting in the preparation of consolidated financial statements.

49. The following statements relate to the provision of taxation, internal audit or IT Systems services to audit clients. Which is false?

A. Preparing calculations of current and deferred tax liabilities (or assets) for an audit client for the purpose of preparing accounting entries that will be subsequently audited by the firm creates a self-interest threat.

B. A self-review threat may be created when a firm, or network firm, provides internal audit services to an audit client.

C. The provision of services by a firm or network firm to an audit client that involve the design and implementation of financial information technology systems that are used to generate information forming part of a client’s financial statements may create a self-review threat.

D. The provision of services in connection with the assessment, design, and implementation of internal accounting controls and risk management controls does not create a threat to independence provided that firm or network firm personnel do not perform management functions.

50. What threat to independence is created when the litigation support services provided to an audit client include the estimation of the possible outcome and thereby affects the amounts or disclosures to be reflected in the financial statements?

A. Self-review threat

B. Advocacy threat

C. Intimidation threat

D. Familiarity threat

51. What threat to independence may be created if fees due from an assurance client for professional services remain unpaid for a long time, especially if a significant part is not paid before the issue of the assurance report for the following year?

A. Advocacy threat

B. Self-interest threat

C. Intimidation threat

D. Self-review threat

52. These are fees calculated on a predetermined basis relating to the outcome or result of a transaction or the result of the work performed.

A. Contingent fees

B. Fixed fees

C. Predetermined fees

D. Commissions.

53. As defined in the Code of Ethics, what is the communication to the public of information as to the services or skills provided by professional accountants in public practice with a view to procuring professional business?

A. Advertising

B. Publicity

C. Solicitation

D. Marketing professional services

54. As defined in the Code of Ethics, what is the communication to the public of facts about a professional accountant which are not designed for the deliberate promotion of that professional accountant?

A. Advertising

B. Publicity

C. Solicitation

D. Marketing professional services

55. Which of the following statements concerning publicity is incorrect?

A. Booklets and other documents bearing the name of a professional accountant and giving technical information for the assistance of staff or clients may be issued to such persons, other professional accountants or other interested parties.

B. Professional accountants who author books or articles on professional subjects may state their name and professional qualifications; give the name of their organization; and give any information as to the services that the firm provides.

C. Appropriate newspapers or magazines may be used to inform the public of the establishment of a new practice, of changes in the composition of a partnership of professional accountants in public practice, or of any alteration in the address of a practice.

D. A professional accountant may develop and maintain a website in the Internet in such suitable length and style which may also include announcements, press releases, publications and such other necessary and factual information.

56. A professional accountant in public practice is allowed to

A. Refer to, use or cite actual or purported testimonials by third parties.

B. Publish services in billboard (e.g., tarpaulin, streamers, etc.) advertisements.

C. Publish and compare fees with other CPAs or CPA firms or compare those services with those provided by another firm or CPA practitioner.

D. Inform interested parties through any medium that a partnership or salaried employment of an accountancy nature is being sought.

57. After evaluating the significance of the threat created by an actual or threatened litigation, the following safeguards should be applied to reduce the threat to an acceptable level, except

A. Disclosing to the audit committee, or others charged with governance, the extent and nature of the litigation.

B. If the litigation involves a member of the assurance team, removing that individual from the assurance team.

C. Involving an additional professional accountant in the firm who was not a member of the assurance team to review the work or otherwise advise as necessary.

D. Withdraw from, or refuse to accept, the assurance engagement.

58. The following statements relate to the provision of legal services to an audit client. Which is incorrect?

A. The provision of legal services to an audit client involving matters that would not be expected to have a material effect on the financial statements may create a self-review threat.

B. Legal services to support an audit client in the execution of a transaction (e.g., contract support) may create a self-review threat.

C. Acting for an audit client in the resolution of a dispute or litigation in such circumstances when the amounts involved are material in relation to the financial statements of the audit client would create advocacy and self-review threats so significant no safeguards could reduce the threats to an acceptable level.

D. The appointment of a partner or an employee of the firm or network firm as General Counsel for legal affairs to an audit client would create self-review and advocacy threats that are so significant no safeguards could reduce the threats to an acceptable level.

59. The following circumstances create advocacy threats for a professional accountant in public practice except

A. Promoting shares in an audit client.

B. Acting as an advocate on behalf of an audit client in litigation or disputes with third parties.

C. Acting as campaign manager for the president of a client who is running for a public office.

D. A member of the assurance team having a significant close business relationship with an assurance client.

60. The primary purpose of establishing quality control policies and procedures for deciding whether to accept a new client is to

A. Anticipate before performing any fieldwork whether an unqualified opinion can be expressed.

B. Enable the CPA firm to attest to the reliability of the client.

C. Satisfy the CPA firm’s duty to the public concerning the acceptance of new clients.

D. Minimize the likelihood of association with clients whose management lacks integrity.

61. As defined in PSQC 1, what is a process comprising an ongoing consideration and evaluation of the firm’s system of quality control, including a periodic inspection of a selection of completed engagements, designed to provide the firm with reasonable assurance that its system of quality control is operating effectively?

A. Monitoring

B. Inspection

C. Engagement quality control review

D. Supervision

62. Which element of a system of quality control is addressed by the establishment of policies and procedures designed to provide the firm with reasonable assurance that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles?

A. Monitoring

B. Leadership responsibilities for quality within the firm

C. Human resources

D. Engagement performance

63. For audits of financial statements of listed entities, the engagement partner should not issue the auditor’s report until the completion of the

A. Engagement Quality Control Review

B. Management Review

C. Engagement Team Review

D. Engagement Partner Review

64. Who should take responsibility for the overall quality on each audit engagement?

A. Engagement quality control reviewer

B. Engagement partner

C. Engagement team

D. CPA firm

65. The engagement partner should take responsibility for the direction, supervision, and performance of the audit engagement in compliance with professional standards and regulatory and legal requirements, and for the auditor’s report that is issued to be appropriate in the circumstances. Supervision includes the following, except

A. Tracking the progress of the audit engagement.

B. Addressing significant issues arising during the audit engagement, considering their significance, and modifying the planned approach appropriately.

C. Informing the members of the engagement team of their responsibilities.

D. Identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement.

THE FINANCIAL STATEMENT AUDIT: CLIENT ACCEPTANCE AND PLANNING

66. Which of the following would an auditor most likely use in determining the auditor’s preliminary judgment about materiality?

A. The anticipated sample size of the planned substantive tests.

B. The entity’s annualized interim financial statements.

C. The results of the internal control questionnaire.

D. The contents of the management representation letter.

67. Which of the following statements concerning materiality is not correct?

A. When establishing the overall audit strategy, the auditor shall determine materiality for the financial statements as a whole.

B. If, in the specific circumstances of the entity, there is one or more particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements, the auditor shall also determine the materiality level or levels to those particular classes of transactions, account balances or disclosures.

C. Determining materiality involves the exercise of professional judgment.

D. The materiality level for the financial statements as a whole determined in the planning stage of the audit should not be affected by changes in the circumstances of the engagement.

68. Analytical procedures used in planning an audit should focus on

A. Reducing the scope of tests of controls and substantive tests.

B. Providing assurance that potential material misstatements will be identified.

C. Enhancing the auditor’s understanding of the client’s business and identifying areas of potential risk.

D. Assessing the adequacy of the available evidential matter.

69. Which of the following would not be considered an analytical procedure?

A. Estimating payroll expense by multiplying the number of employees by the average hourly wage rate and the total hours worked.

B. Projecting an error rate by comparing the results of a statistical sample with the actual population characteristics.

C. Computing accounts receivable turnover by dividing credit sales by the average net receivables.

D. Developing the expected sales based on the sales trend of the prior five years.

70. Which of the following auditing procedures most likely would assist an auditor in identifying related party transactions?

A. Inspecting correspondence with lawyers for evidence of unreported contingent liabilities.

B. Vouching accounting records for recurring transactions recorded just after the balance sheet date.

C. Reviewing confirmations of loans receivable and payable for indications of guarantees.

D. Performing analytical procedures for indications of possible financial difficulties.

71. Which of the following most likely would indicate the existence of related parties?

A. Writing down obsolete inventory just before year-end.

B. Failing to correct previously identified internal control deficiencies.

C. Depending on a single product for the success of the entity.

D. Borrowing money at an interest rate significantly below the market rate.

72. If the results of the auditor’s expert’s work do not provide sufficient appropriate audit evidence or are not consistent with other audit evidence, the auditor should

A. Report the matter to the appropriate regulatory agency of the government.

B. Resolve the matter.

C. Withdraw from the engagement.

D. Express an unqualified opinion with reference to the work of the expert.

RISK ASSESSMENTS AND INTERNAL CONTROL

73. A measure of how willing the auditor is to accept that the financial statements may be materially misstated after the audit is completed and an unmodified opinion has been issued is the

A. Inherent risk.

B. Acceptable audit risk.

C. Control risk.

D. Detection risk.

74. Which of the following is not one of the three primary objectives of effective internal control?

A. Reliability of financial reporting.

B. Efficiency and effectiveness of operations.

C. Compliance with laws and regulations.

D. Assurance of elimination of business risk.

75. Which of the following statements concerning the relevance of various types of controls to a financial statement audit is correct?

A. All controls are ordinarily relevant to a financial statement audit.

B. Controls over safeguarding of assets and liabilities are of primary importance, while controls over the reliability of financial reporting may also be relevant.

C. Controls over the reliability of financial reporting are ordinarily most directly relevant to a financial statement audit, but other controls may also be relevant.

D. An auditor may ordinarily ignore a consideration of controls when a substantive audit approach is taken.

76. An auditor should consider two key issues when obtaining an understanding of a client’s internal controls. These issues are

A. The effectiveness and efficiency of the controls.

B. The frequency and effectiveness of the controls.

C. The design and implementation of the controls.

D. The implementation and efficiency of the controls.

77. Authorizations can be either general or specific. Which of the following is not an example of a general authorization?

A. Automatic reorder points for raw materials inventory.

B. A sales manager’s authorization for a sales return.

C. Credit limits for various classes of transactions.

D. A sales price list for merchandise.

78. An auditor should obtain sufficient knowledge of an entity’s information system, including the related business processes relevant to financial reporting, to understand the

A. Policies used to detect the concealment of fraud.

B. Process used to prepare significant accounting estimates.

C. Safeguards used to limit access to computer facilities.

D. Procedures used to assure proper authorization of transactions.

79. Which of the following controls most likely would provide reasonable assurance that all credit sales transactions of an entity are recorded?

A. The accounting department supervisor controls the mailing of monthly statements to customers and investigates any differences reported by customers.

B. The accounting department supervisor independently reconciles, on a monthly basis, the accounts receivable subsidiary ledger to the accounts receivable control account.

C. The billing department supervisor matches prenumbered shipping documents with entries in the sales journal.

D. The billing department supervisor sends copies of approved sales orders to the credit department for comparison to authorized credit limits and current customer account balances.

80. Which of the following control activities in an entity’s revenue/receipt cycle would provide reasonable assurance that all billed sales are correctly posted to the accounts receivable ledger?

A. Each shipment of goods on credit is supported by a prenumbered sales invoice.

B. The accounts receivable subsidiary ledger is reconciled daily to the accounts receivable control account in the general ledger.

C. Daily sales summaries are compared to daily postings to the accounts receivable ledger.

D. Each sales invoice is supported by a prenumbered shipping document.

81. Which of the following controls is not usually performed in the accounts payable department?

A. Indicating on the voucher the affected asset and expense accounts to be debited.

B. Approving vouchers for payment by having an authorized employee sign the vouchers.

C. Accounting for unused prenumbered purchase orders and receiving reports.

D. Matching the vendor’s invoice with the related purchase requisition, purchase order, and receiving report.

82. After gaining an understanding of internal control and assessing the risks of material misstatement, an auditor decided to perform tests of controls. The auditor most likely decided that

A. Additional evidence to support a further reduction in control risk is not available.

B. It is not possible or practicable to reduce the risks of material misstatement at the assertion level to an acceptably low level with audit evidence obtained only from substantive test procedures.

C. There were many internal control weaknesses that could allow misstatements to enter the accounting system.

D. An increase in the assessed level of control risk is justified for certain financial statement assertions.

83. An auditor may decide to assess control risk at the maximum level for certain assertions because the auditor believes

A. Controls are unlikely to pertain to the assertions.

B. The entity’s control components are interrelated.

C. Sufficient appropriate audit evidence to support the assertions is likely to be available.

D. More emphasis on tests of controls than substantive tests is warranted.

84. Which of the following statements is correct concerning an auditor’s assessment of control risk?

A. Assessing control risk may be performed concurrently during an audit with obtaining an understanding of the entity’s internal control.

B. Evidence about the operation of controls in prior audits may not be considered during the current year’s assessment of control risk.

C. The basis for an auditor’s conclusions about the assessed level of control risk need not be documented unless control risk is assessed at the maximum level.

D. The lower the assessed level of control risk, the less assurance the evidence must provide that the controls are operating effectively.

85. In performing tests of the operating effectiveness of an entity’s controls, an auditor selects from a variety of techniques, including

A. Reperformance and observation.

B. Inquiry and analytical procedures.

C. Comparison and confirmation.

D. Inspection and verification.

86. Which of the following tests of controls most likely would help assure an auditor that goods shipped are properly billed?

A. Scan the sales journal for sequential and unusual entries.

B. Examine shipping documents for matching sales invoices.

C. Compare the accounts receivable ledger to daily sales summaries.

D. Inspect unused sales invoices for consecutive prenumbering.

87. When there are numerous property and equipment transactions during the year, an auditor who plans to assess control risk at a low level usually performs

A. Tests of controls and extensive tests of property and equipment balances at the end of the year.

B. Analytical procedures for current year property and equipment transactions.

C. Tests of controls and limited tests of current year property and equipment transactions.

D. Analytical procedures for property and equipment balances at the end of the year.

FRAUD AND ERROR

88. “Error” includes

A. Engaging in complex transactions that are structured to misrepresent the financial position or financial performance of the entity.

B. Concealing, or not disclosing, facts that could affect the amounts recorded in the financial statements.

C. An incorrect accounting estimate arising from oversight or misinterpretation of facts.

D. Intentional misapplication of accounting policies relating to amounts, classification, manner of presentation, or disclosure.

89. Fraud involving one or more members of management or those charged with governance is referred to as

A. Management fraud. C. Fraudulent financial reporting.

B. Employee fraud. D. Misappropriation of assets.

90. The auditor is concerned with fraud that causes a material misstatement in the financial statements. There are two types of intentional misstatements that are relevant to the auditor: misstatements resulting from fraudulent financial reporting and misstatements resulting from

A. Management fraud.

B. Employee fraud.

C. Misappropriation of assets.

D. Collusion within the entity or with third parties.

91. Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users. It may be accomplished in a number of ways, including

A. Embezzling receipts.

B. Stealing physical assets or intellectual property.

C. Using an entity’s assets for personal use.

D. Manipulation, falsification, or alteration of accounting records or supporting documentation from which the financial statements are prepared.

92. The following are examples of fraud risk factors relating to misstatements arising from misappropriation of assets, except

A. Recurring negative cash flows from operating activities while reporting earnings and earnings growth.

B. Inadequate physical safeguards over cash, investments, inventory, or fixed assets.

C. Inadequate segregation of duties or independent checks.

D. Adverse relationship between the entity and employees with access to cash or other assets susceptible to theft created by recent changes made to employee compensation or benefit plans.

93. Opportunities to misappropriate assets increase when there are

A. Known or anticipated future employee layoffs.

B. Promotions, compensation, or other rewards inconsistent with expectations.

C. Recent or anticipated changes to employee compensation or benefit plans.

D. Inventory items that are small in size, of high value, or in high demand.

94. Which of the following conditions or events may create incentives/pressures to commit fraud?

A. Inadequate system of authorization and approval of transactions.

B. Lack of mandatory vacations for employees performing key control functions.

C. Excessive pressure on management or operating personnel to meet financial targets established by those charged with governance, including sales or profitability incentive goals.

D. Inadequate access controls over automated records.

95. When the auditor identifies a misstatement in the financial statements, the auditor should consider whether such a misstatement may be indicative of fraud and if there is such an indication, the auditor should

A. Consider the implications of the misstatement in relation to other aspects of the audit.

B. Withdraw from the engagement.

C. Communicate the information to regulatory and enforcement authorities.

D. Report the matter to the person or persons who made the audit appointment.

AUDITING IN A CIS/IT ENVIRONMENT

96. The use of a computer changes the processing, storage, and communication of financial information. A CIS environment may affect the following, except

A. The accounting and internal control systems of the entity.

B. The overall objective and scope of an audit.

C. The auditor’s design and performance of tests of control and substantive procedures to satisfy the audit objectives.

D. The specific procedures to obtain knowledge of the entity’s accounting and internal control systems.

97. The following are benefits of using IT-based controls, except

A. Ability to process large volume of transactions.

B. Over-reliance on computer-generated reports.

C. Ability to replace manual controls with computer-based controls.

D. Reduction in misstatements due to consistent processing of transactions.

98. Which of the following statements concerning the Internet is incorrect?

A. The Internet is a shared public network that enables communication with other entities and individuals around the world.

B. The Internet is a private network that only allows access to authorized persons or entities.

C. The Internet is interoperable, which means that any computer connected to the Internet can communicate with any other computer connected to the Internet.

D. The Internet is a worldwide network that allows entities to engage in e-commerce/e-business activities.

99. The auditor shall consider the entity’s CIS environment in designing audit procedures to reduce risk to an acceptably low level. Which of the following statements is incorrect?

A. The auditor’s specific audit objectives do not change whether financial information is processed manually or by computer.

B. The methods of applying audit procedures to gather audit evidence are not influenced by the methods of computer processing.

C. The auditor may use either manual audit procedures, computer-assisted audit techniques (CAATs), or a combination of both to obtain sufficient appropriate audit evidence.

D. In some CIS environments, it may be difficult or impossible for the auditor to obtain certain data for inspection, inquiry, or confirmation without the aid of a computer.

100. A characteristic that distinguishes computer processing from manual processing is

A. The potential for systematic error is ordinarily greater in manual processing than in computerized processing.

B. Errors or fraud in computer processing will be detected soon after their occurrences.

C. Most computer systems are designed so that transaction trails useful for audit purposes do not exist.

D. Computer processing virtually eliminates the occurrence of computational errors normally associated with manual processing.

101. Which of the following statements most likely represents a disadvantage for an entity that maintains data files on personal computers (PCs) rather than manually prepared files?

A. It is usually more difficult to compare recorded accountability with the physical count of assets.

B. Random error associated with processing similar transactions in different ways is usually greater.

C. Attention is focused on the accuracy of the programming process rather than errors in individual transactions.

D. It is usually easier for unauthorized persons to access and alter the files.

102. The internal controls over computer processing include both manual procedures and procedures designed into computer programs (programmed control procedures). These manual and programmed control procedures comprise the general CIS controls and CIS application controls. The purpose of general CIS controls is to

A. Establish specific control procedures over the accounting applications in order to provide reasonable assurance that all transactions are authorized and recorded and are processed completely, accurately, and on a timely basis.

B. Establish a framework of overall controls over the CIS activities and to provide a reasonable level of assurance that the overall objectives of internal control are achieved.

C. Provide reasonable assurance that systems are developed and maintained in an authorized and efficient manner.

D. Provide reasonable assurance that access to data and computer programs is restricted to authorized personnel.

103. An entity has recently converted its purchasing cycle from a manual process to an online computer system. Which of the following is a probable result associated with conversion to the new IT system?

A. Traditional duties are less separated.

B. Increased processing time.

C. Reduction in the entity’s risk exposure.

D. Increased processing errors.

104. An entity should plan the physical location of its computer facility. Which of the following is the primary consideration for selecting a computer site?

A. It should be in the basement or on the ground floor.

B. It should maximize the visibility of the computer.

C. It should minimize the distance that data control personnel must travel to deliver data and reports and be easily accessible by a majority of company personnel.

D. It should provide security.

105. An entity installed antivirus software on all its personal computers. The software was designed to prevent initial infections, stop replication attempts, detect infections after their occurrence, mark affected system components, and remove viruses from infected components. The major risk in relying on antivirus software is that it may

A. Consume too many system resources.

B. Interfere with system operations.

C. Not detect certain viruses.

D. Make software installation too complex.

AUDIT OBJECTIVES, PROCEDURES,EVIDENCE, AND DOCUMENTATION

106. Which of the following should be considered by the auditor in deciding which means (or combination of means) to use in selecting items for testing?

I. The risk of material misstatement related to the assertion being tested.

II. Audit efficiency.

A. I only C. Both I and II

B. II only D. Neither I nor II

107. The quantity of audit evidence needed is affected by the risk of misstatement and also by the quality of such audit evidence.

The reliability of audit evidence is influenced by its source and by its nature and is dependent on the individual circumstances under which it is obtained.

A. Both statements are true. C. True; False.

B. Both statements are false. D. False; True.

108. Which of the following is a false statement about audit objectives?

A. There should be a one-to-one relationship between audit objectives and procedures.

B. Audit objectives should be developed in light of management assertions about the financial statement components.

C. Selection of tests to meet audit objectives should depend upon the understanding of internal control.

D. The auditor should resolve any substantial doubt about any of management’s material financial statement assertions.

109. Which of the following statements concerning evidential matter is true?

A. Appropriate evidence supporting management’s assertions should be convincing rather than merely persuasive.

B. Effective internal control contributes little to the reliability of the evidence created within the entity.

C. The cost of obtaining evidence is not an important consideration to an auditor in deciding what evidence should be obtained.

D. A client’s accounting records cannot be considered sufficient evidence to support the financial statements.

110. Which of the following types of audit evidence is the most persuasive?

A. Prenumbered purchase order forms.

B. Client worksheets supporting cost allocations.

C. Bank statements obtained from the client.

D. Client representation letter.

111. Which of the following generalizations does not relate to the appropriateness of evidence?

A. Audit evidence from external sources (for example, confirmation received from a third party) is more reliable than that generated internally.

B. An auditor’s opinion, to be economically useful, is formed within reasonable time and based on evidence obtained at a reasonable cost.

C. Audit evidence generated internally is more reliable when the related accounting and internal control systems are effective.

D. Audit evidence obtained directly by the auditor is more reliable than that obtained from the entity.

112. Each of the following might, by itself, form a valid basis for an auditor to decide to omit a test except for the

A. Difficulty and expense involved in testing a particular item.

B. Assessment of control risk at a low level.

C. Inherent risk involved.

D. Relationship between the cost of obtaining evidence and its usefulness.

113. In which of the following circumstances would the use of the negative form of accounts receivable confirmation most likely be justified?

A. A substantial number of accounts may be in dispute and the accounts receivable balance arises from sales to a few major customers.

B. A substantial number of accounts may be in dispute and the accounts receivable balance arises from sales to many customers with small balances.

C. A small number of accounts may be in dispute and the accounts receivable balance arises from sales to a few major customers.

D. A small number of accounts may be in dispute and the accounts receivable balance arises from sales to many customers with small balances.

114. Which of the following statements is correct concerning the use of negative confirmation requests?

A. Unreturned negative confirmation requests rarely provide significant explicit evidence.

B. Negative confirmation requests are effective when detection risk is low.

C. Unreturned negative confirmation requests indicate that alternative procedures are necessary.

D. Negative confirmation requests are effective when understatements of account balances are suspected.

115. Which of the following most likely would give the most assurance concerning the valuation and allocation assertion of accounts receivable?

A. Vouching amounts in the subsidiary ledger to details on shipping documents.

B. Comparing receivable turnover ratios with industry statistics for reasonableness.

C. Inquiring about receivables pledged under loan agreements.

D. Assessing the allowance for uncollectible accounts for reasonableness.

116. Confirmation is “the process of obtaining and evaluating a direct communication from a third party in response to a request for information about a particular item affecting financial statement assertions.” Two assertions for which confirmation of accounts receivable balances provides primary evidence are

A. Completeness and valuation

B. Valuation and rights and obligations

C. Rights and obligations and existence

D. Existence and completeness

117. To gain assurance that all inventory items in a client’s inventory listing schedule are valid, an auditor most likely would vouch

A. Inventory tags noted during the auditor’s observation to items listed in the inventory listing schedule.

B. Inventory tags noted during the auditor’s observation to items listed in receiving reports and vendors’ invoices.

C. Items listed in the inventory listing schedule to inventory tags and the auditor’s recorded count sheets.

D. Items listed in receiving reports and vendors’ invoices to the inventory listing schedule.

118. Which of the following is not an audit procedure that the independent auditor would perform with respect to litigation, claims, and assessments?

A. Inquire of and discuss with management the policies and procedures adopted for litigation, claims, and assessments.

B. Obtain from management a description and evaluation of litigation, claims, and assessments that existed at the balance sheet date.

C. Obtain assurance from management that if has disclosed all unasserted claims that the lawyer has advised are probable of assertion and must be disclosed.

D. Confirm directly with the client’s lawyer that all claims have been recorded in the financial statements.

119. Audit documentation may be recorded on paper or on electronic or other media. The following are examples of audit documentation, except

A. Audit programs

B. Letters of confirmation and representation

C. Correspondence (including e-mail) concerning significant matters

D. The entity’s accounting records

120. The completion of the assembly of the final audit file after the date of the auditor’s report does not ordinarily involve

A. The performance of new audit procedures or the drawing of new conclusions.

B. Sorting, collating and cross-referencing working papers.

C. Deleting or discarding superseded documentation.

D. Signing off on completion checklists relating to the file assembly process.

AUDIT SAMPLING

121. Audit sampling involves the

A. Selection of all items over a certain amount.

B. Application of audit procedures to less than 100% of items within a class of transactions or an account balance such that all items have a chance of selection.

C. Application of audit procedures to all items that comprise a class of transactions or an account balance.

D. Application of audit procedures to all items over a certain amount and those that are unusual or have a history of error.

122. Population, as defined in PSA 530, means the entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions. It is important for the auditor to ensure that the population is

I. Appropriate to the objective of the audit procedure.

II. Complete.

A. I only C. Both I and II

B. II only D. Neither I nor II

123. An advantage of statistical over nonstatistical sampling methods in tests of controls is that the statistical methods

A. Afford greater assurance than a nonstatistical sample of equal size.

B. Provide an objective basis for quantitatively evaluating sampling risks.

C. Can more easily convert the sample into a dual-purpose test useful for substantive testing.

D. Eliminate the need to use judgment in determining appropriate sample sizes.

124. Which of the following best illustrates the concept of sampling risk?

A. A randomly chosen sample may not be representative of the population as a whole on the characteristic of interest.

B. An auditor may select audit procedures that are not appropriate to achieve the specific objective.

C. An auditor may fail to recognize errors in the documents examined for the chosen sample.

D. The documents related to the chosen sample may not be available for inspection.

125. Which of the following statistical selection techniques is least desirable for use by an auditor?

A. Systematic selection C. Block selection

B. Stratified selection D. Sequential selection

COMPLETING THE AUDIT AND POST-AUDIT RESPONSIBILITIES

126. Analytical procedures used in the overall review stage of the audit generally include

A. Retesting controls that appeared to be ineffective during the assessment of control risk.

B. Considering unusual or unexpected account balances that were not previously identified.

C. Gathering evidence concerning account balances that have not changed from the prior year.

D. Performing tests of transactions to corroborate management’s financial statement assertions.

127. Analytical procedures performed in the overall review stage of an audit suggest that several accounts have unexpected relationships. The results of these procedures most likely indicate that

A. The communication with the audit committee should be revised.

B. Irregularities exist among the relevant account balances.

C. Additional substantive tests of details are required.

D. Internal control activities are not operating effectively.

128. Which of the following events most likely indicates the existence of related parties?

A. Making a loan without scheduled terms for repayment of the funds.

B. Discussing merger terms with a company that is a major competitor.

C. Selling real estate at a price that differs significantly from its book value.

D. Borrowing a large sum of money at a variable rate of interest.

129. An auditor searching for related party transactions should obtain an understanding of each subsidiary’s relationship to the total entity because

A. This may permit the audit of intercompany account balances to be performed as of concurrent dates.

B. This may reveal whether particular transactions would have taken place if the parties had not been related.

C. The business structure may be deliberately designed to obscure related party transactions.

D. Intercompany transactions may have been consummated on terms equivalent to arm’s-length transactions.

130. After determining that a related party transaction has, in fact, occurred, an auditor should

A. Obtain an understanding of the business purpose of the transaction.

B. Substantiate that the transaction was consummated on terms equivalent to an arm’s-length transaction.

C. Add a separate paragraph to the auditor’s report to explain the transaction.

D. Perform analytical procedures to verify whether similar transactions occurred, but were not recorded.

131. Which of the following statements best describes the “date of the financial statements?”

A. The date on which those with the recognized authority assert that they have prepared the entity’s complete set of financial statements, including the related notes, and that they have taken responsibility for them.

B. The date that the auditor’s report and audited financial statements are made available to third parties.

C. The date of the end of the latest period covered by the financial statements, which is normally the date of the most recent balance sheet in the financial statements subject to audit.

D. The date on which the auditor has obtained sufficient appropriate audit evidence on which to base the opinion on the financial statements.

132. Which of the following procedures would an auditor most likely perform to obtain evidence about the occurrence of subsequent events?

A. Inquiring as to whether any unusual adjustments were made after the date of the financial statements.

B. Confirming a sample of material accounts receivable established after the date of the financial statements.

C. Comparing the financial statements being reported on with those of the prior period.

D. Investigating personnel changes in the accounting department occurring after the date of the financial statements.

133. Which of the following statements best expresses the auditor’s responsibility with respect to facts discovered after the date of the auditor’s report but before the date the financial statements are issued?

A. The auditor should amend the financial statements.

B. If the facts discovered will materially affect the financial statements, the auditor should issue a new report which contains either a qualified opinion or an adverse opinion.

C. The auditor should consider whether the financial statements need amendment, discuss the matter with management, and consider taking actions appropriate in the circumstances.

D. The auditor should withdraw from the engagement.

134. After issuing a report, an auditor has no obligation to make continuing inquiries or perform other procedures concerning the audited financial statements, unless

A. Final determinations or resolutions are made of contingencies that had been disclosed in the financial statements.

B. Information about an event that occurred after the date of the auditor’s report comes to the auditor’s attention.

C. The control environment changes after issuance of the report.

D. Information, which existed at the report date and may affect the report, comes to the auditor’s attention.

135. Which of the following events occurring after the issuance of an auditor’s report most likely would cause the auditor to make further inquiries about the previously issued financial statements?

A. A technological development that could affect the entity’s future ability to continue as a going concern.

B. The entity’s sale of a subsidiary that accounts for 30% of the entity’s consolidated sales.

C. The discovery of information regarding a contingency that existed before the financial statements were issued.

D. The final resolution of a lawsuit disclosed in the notes to the financial statements.

136. Which of the following statements best describes the auditor’s responsibility concerning the appropriateness of the going concern assumption in the preparation of the financial statements?

A. The auditor’s responsibility is to make a specific assessment of the entity’s ability to continue as a going concern.

B. The auditor’s responsibility is to predict future events or conditions that may cause the entity to cease to continue as a going concern.

C. The auditor’s responsibility is to consider the appropriateness of management’s use of the going concern assumption and consider whether there are material uncertainties about the entity’s ability to continue as a going concern that need to be disclosed in the financial statements.

D. The auditor’s responsibility is to give a guarantee in the audit report that the entity has the ability to continue as a going concern.

137. Which of the following conditions or events most likely would cause an auditor to have substantial doubt about an entity’s ability to continue as a going concern?

A. Cash flows from operating activities are negative.

B. Stock dividends replace annual cash dividends.

C. Significant related party transactions are pervasive.

D. Research and development projects are postponed.

138. Which of the following conditions or events most likely would cause an auditor to have substantial doubt about an entity’s ability to continue as a going concern?

A. Restrictions on the disposal of principal assets are present.

B. Usual trade credit from suppliers is denied.

C. Significant related party transactions are pervasive.

D. Arrearages in principal stock dividends are paid.

139. Which of the following audit procedures would most likely assist an auditor in identifying conditions and events that may indicate there could be substantial doubt about an entity’s ability to continue as a going concern?

A. Confirmation of bank balances.

B. Confirmation of accounts receivable from major customers.

C. Reconciliation of interest expense with debt outstanding.

D. Review of compliance with terms of debt agreements.

140. When an auditor concludes that there is substantial doubt about a continuing audit client’s ability to continue as a going concern for a reasonable period of time, the auditor’s responsibility is to

A. Consider the adequacy of disclosure about the client’s possible inability to continue as a going concern.

B. Issue a qualified or adverse opinion, depending upon materiality, due to the possible effects on the financial statements.

C. Report to the client’s audit committee that management’s accounting estimates may need to be adjusted.

D. Reissue the prior year’s auditor’s report and add an emphasis of matter paragraph that specifically refers to “substantial doubt” and “going concern.”

141. When an audit is made in accordance with generally accepted auditing standards, the auditor should always

A. Observe the taking of physical inventory on the balance sheet date.

B. Obtain certain written representations from management.

C. Employ analytical procedures as substantive tests to obtain evidence about specific assertions related to account balances.

D. Document the understanding of the client’s internal control and the basis for all conclusions about the assessed level of control risk for financial statement assertions.

142. When considering the use of management’s written representations as audit evidence about the completeness assertion, an auditor should understand that such representations

A. Constitute sufficient appropriate audit evidence to support the assertion when considered in combination with a sufficiently low assessed level of control risk.

B. Are not part of the audit evidence considered to support the assertion.

C. Replace a low assessed level of control risk as audit evidence to support the assertion.

D. Complement, but do not replace, substantive tests designed to support the assertion.

143. A written representation from a client’s management that, among other matters, acknowledges responsibility for the fair presentation of financial statements, should normally be signed by the

A. Chief financial officer and the chair of the board of directors.

B. Chief executive officer and the chief financial officer.

C. Chief executive officer, the chair of the board of directors, and the client’s lawyer.

D. Chair of the audit committee of the board of directors.

144. The date of the management representation letter should coincide with the date of the

A. Statement of Financial Position

B. Latest related party transaction

C. Auditor’s report

D. Latest interim financial information

145. Which of the following statements concerning management representations is incorrect?

A. Representations by management can be a substitute for other audit evidence that the auditor could reasonably expect to be available.

B. If the auditor is unable to obtain sufficient appropriate audit evidence regarding a matter, which has, or may have, a material effect on the financial statements and such audit evidence is expected to be available, this will constitute a limitation in the scope of the audit, even if a representation from management has been received on the matter.

C. If a representation by management is contradicted by other audit evidence, the auditor should investigate the circumstances and, when necessary, reconsider the reliability of other representations by management.

D. The auditor’s working papers would ordinarily include a summary of oral discussions with management or written representations from management.

146. What type of opinion should be expressed if the client’s management refuses to provide a representation that the auditor considers necessary?

A. Qualified opinion or a disclaimer of opinion.

B. Qualified opinion or an adverse opinion.

C. Adverse opinion or a disclaimer of opinion.

D. Unqualified opinion.

147. The primary reason an auditor requests that letters of inquiry be sent to a client’s attorneys is to provide the auditor with

A. A description and evaluation of litigation, claims, and assessments that existed at the balance sheet date.

B. The attorneys’ opinions of the client’s historical experiences in recent similar litigation.

C. Corroboration of the information furnished by management about litigation, claims, and assessments.

D. The probable outcome of asserted claims and pending or threatened litigation.

148. The letter of audit inquiry should be

A. Prepared and sent by the auditor.

B. Prepared by management and sent by the auditor.

C. Prepared and sent by management.

D. Prepared by the auditor and sent by management.

149. The refusal of a client’s lawyer to provide a representation on the legality of a particular act committed by the client is ordinarily

A. Proper grounds to withdraw from the engagement.

B. Insufficient reason to modify the auditor’s report because of the lawyer’s obligation of confidentiality.

C. Considered to be a scope limitation.

D. Sufficient reason to issue a “subject to” opinion.

150. Management’s refusal to give the auditor permission to communicate with the entity’s legal counsel is most likely to lead to

A. An adverse opinion.

B. A qualified opinion or an adverse opinion.

C. An unqualified opinion.

D. A qualified opinion or a disclaimer of opinion.

THE AUDITOR’S REPORT ON FINANCIAL STATEMENTS

151. The following statements relate to the date of the auditor’s report. Which is false?

A. The auditor should date the report as of the completion date of the audit.

B. The date of the auditor’s report should not be earlier than the date on which the financial statements are signed or approved by management.

C. The date of the auditor’s report should not be later than the date on which the financial statements are signed or approved by management.

D. The date of the auditor’s report should always be later than the date of the financial statements (i.e., the balance sheet date).

152. In which of the following circumstances would an auditor most likely add an emphasis of matter paragraph to the auditor’s report while expressing an unqualified opinion?

A. There is a substantial doubt about the entity’s ability to continue as a going concern.

B. Management’s estimates of the effects of future events are unreasonable.

C. No depreciation has been provided in the financial statements.

D. Certain transactions cannot be tested because of management’s records retention policy.

153. A note to the financial statements of the Prudent Bank indicates that all of the records relating to the bank’s business operations are stored on magnetic disks, and that no emergency backup systems or duplicate disks are stored because the bank and its auditors consider the occurrence of a catastrophe to be remote. Based upon this note, the auditor’s report should express

A. A qualified opinion C. An adverse opinion

B. An unmodified opinion D. A “subject to” opinion

154. When would the auditor refer to the work of an appraiser in the auditor’s report?

A. An adverse opinion is expressed based on a difference of opinion between the client and the outside appraiser as to the value of certain assets.

B. A disclaimer of opinion is expressed because of a scope limitation imposed on the auditor by the appraiser.

C. A qualified opinion is expressed because of a matter unrelated to the work of the appraiser.

D. An unqualified opinion is expressed and an emphasis of matter paragraph is added to disclose the use of the appraiser’s work.

155. When audited financial statements are presented in a document (e.g., annual report) containing other information, the auditor

A. Should read the other information to consider whether it is inconsistent with the audited financial statements.

B. Has no responsibility for the other information because it is not part of the basic financial statements.

C. Has an obligation to perform auditing procedures to corroborate the other information.

D. Is required to express a qualified opinion if the other information has a material misstatement of fact.

156. An auditor concludes that there is a material inconsistency in the other information in an annual report to shareholders containing audited financial statements. If the auditor concludes that the financial statements do not require revision, but the client refuses to revise or eliminate the material inconsistency, the auditor may

A. Disclaim an opinion on the financial statements after explaining the material inconsistency in an emphasis of matter paragraph.

B. Revise the auditor’s report to include an other matter paragraph describing the material inconsistency.

C. Express a qualified opinion after discussing the matter with the client’s directors.

D. Consider the matter closed because the other information is not in the audited statements.

157. In which of the following situations would an auditor ordinarily choose between expressing a qualified opinion or an adverse opinion?

A. The auditor wishes to emphasize an unusually important subsequent event.

B. The financial statements fail to disclose information that is required by Philippine Financial Reporting Standards.

C. Events disclosed in the financial statements cause the auditor to have substantial doubt about the entity’s ability to continue as a going concern.

D. The auditor did not observe the entity’s physical inventory and is unable to become satisfied as to its balance by other auditing procedures.

158. An auditor should disclose the substantive reasons for expressing an adverse opinion in the Basis for Adverse Opinion paragraph

A. Following the opinion paragraph.

B. Preceding the opinion paragraph.

C. Following the introductory paragraph.

D. Within the notes to the financial statements.

159. The predecessor auditor, who is satisfied after properly communicating with the incoming auditor, has reissued his/her auditor’s report on prior year financial statements. The predecessor auditor’s report should

A. Refer to the work of the incoming auditor in the scope and opinion paragraphs.

B. Refer to the report of the incoming auditor only in the scope paragraph.

C. Refer to both the work and the report of the incoming auditor only in the opinion paragraph.

D. Not refer to the report or the work of the incoming auditor.

160. The following statements relate to unaudited prior year financial statements that are presented in comparative form with audited current year financial statements. Which is incorrect?

A. The incoming auditor should state in the auditor’s report that the comparative financial statements are unaudited.

B. The incoming auditor need not perform audit procedures regarding opening balances of the current period.

C. Clear disclosure in the financial statements that the comparative financial statements are unaudited is encouraged.

D. In situations where the incoming auditor identifies that the prior year unaudited figures are materially misstated, the auditor should request management to revise the prior year’s figures or if management refuses to do so, appropriately modify the report.

OTHER REPORTING RESPONSIBILITIES

161. Financial statements of an entity that have been reviewed by an accountant should be accompanied by a report stating that a review

A. Provides only limited assurance that the financial statements are fairly presented.

B. Includes examining, on a test basis, information that is the representation of management.

C. Consists principally of inquiries of company personnel and analytical procedures applied to financial data.

D. Does not contemplate obtaining corroborating evidential matter or applying certain other procedures ordinarily performed during an audit.

162. An accountant’s report on a review of the financial statements of an entity should state that the accountant

A. Does not express an opinion or any form of limited assurance on the financial statements.

B. Conducted the review in accordance with the Philippine Standard on Review Engagements.

C. Obtained reasonable assurance about whether the financial statements are free of material misstatements.

D. Examined evidence, on a test basis, supporting the amounts and disclosures in the financial statements.

163. Financial statements of an entity that have been reviewed by an accountant should be accompanied by a report stating that

A. The scope of the inquiry and analytical procedures performed by the accountant has not been restricted.

B. The financial statements are the responsibility of the company’s management.

C. A review includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements.

D. A review is greater in scope than a compilation, the objective of which is to present financial statements that are free of material misstatements.

164. When compiling the financial statements of an entity, an accountant should

A. Review agreements with financial institutions for restrictions on cash balances.

B. Understand the accounting principles and practices of the entity’s industry.

C. Inquire of key personnel concerning related parties and subsequent events.

D. Perform ratio analyses of the financial data of comparable prior periods.

165. When compiling an entity’s financial statements, an accountant would be least likely to

A. Perform analytical procedures designed to identify relationships that appear to be unusual.

B. Read the compiled financial statements and consider whether they appear to include adequate disclosure.

C. Obtain an acknowledgment from management of its responsibility for the financial statements.

D. Plan the work so that an effective engagement will be performed.

166. Which of the following should not be included in an accountant’s report based upon the compilation of an entity’s financial statements?

A. A statement that a compilation of the company’s financial statements was made in accordance with the Philippine Standard on Related Services applicable to compilation engagements.

B. A statement that management is responsible for the financial statements.

C. A statement that the accountant has not audited or reviewed the statements.

D. A statement that the accountant does not express an opinion but provides only negative assurance on the statements.

167. An accountant may accept an engagement to apply agreed-upon procedures that are not sufficient to express an opinion on one or more specified accounts or items of a financial statement provided that

A. The accountant’s report does not enumerate the procedures performed.

B. The financial statements are prepared in accordance with a comprehensive basis of accounting other than generally accepted accounting principles.

C. Distribution of the accountant’s report is restricted.

D. The accountant is also the entity’s continuing auditor.

168. When an accountant examines prospective financial statements, the accountant’s report should include a separate paragraph that

A. Contains an opinion as to whether the prospective financial statements are properly prepared on the basis of the assumptions and are presented in accordance with generally accepted accounting principles in the Philippines.

B. Provides an explanation of the differences between an examination and an audit.

C. States that the accountant is responsible for events and circumstances up to 1 year after the report’s date.

D. Disclaims an opinion on whether the assumptions provide a reasonable basis for the prospective financial statements.

169. The following statements relate to the examination of prospective financial information. Which is false?

A. The auditor should express an opinion as to whether the results shown in the prospective financial information will be achieved.

B. Before accepting an engagement to examine prospective financial information, the auditor should consider the intended use of the information.

C. The auditor should not accept, or should withdraw from, an engagement to examine prospective financial information when the assumptions are clearly unrealistic.

D. When in the auditor’s judgment an appropriate level of satisfaction has been obtained, the auditor is not precluded from expressing positive assurance regarding the assumptions.

170. Which of the following is a prospective financial information for general use upon which an accountant may appropriately report?

A. Financial projection

B. Partial presentation

C. Pro forma financial statement

D. Financial forecast

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