1.   In determining the primary responsibility of the external auditor for a company’s financial statements, the auditor owes primary allegiance to:

a. The management of the company being audited because the auditor is hired and paid by management.

b. The audit committee of the company being audited because that committee is responsible for coordinating and reviewing all audit activities within the company.

c. Stockholders, creditors, and the investing public.

d. The SEC, because it determines accounting principles and auditor responsibility.

2.  AICPA auditing standards do not require auditors of financial statements to

a. Understand the nature of errors and frauds.

b. Assess the risk of occurrence of errors and frauds.

c. Design audits to provide reasonable assurance of detecting errors and frauds.

d. Report all finding of errors and frauds to police authorities.

3.  The risk that the auditors’ own work will lead to the decision that material misstatements do not exist in the financial statements, when in fact such misstatements do exist, is

a. Audit risk.

b. Inherent risk.

c. Control risk.

d. Detection risk.

4.  Confirmations of accounts receivable provide evidence primarily about these two assertions:

a. Completeness and valuation.

b. Valuation and rights and obligations.

c. Rights and obligations and existence.

d. Existence and completeness.

5.  One of the typical characteristics of management fraud is

a. Falsification of documents in order to steal money from an employer.

b. Victimization of investors through the use of materially misleading financial statements.

c. Illegal acts committed by management to evade laws and regulations.

d. Conversion of stolen inventory to cash deposited in a falsified bank account.

6.  With respect to the concept of materiality, which one of the following statements is correct?

a. Materiality depends only on the dollar amount of an item relative to other items in the financial statements.

b. Materiality depends on the nature of a transaction rather than the dollar amount of the transaction.

c. Materiality is determined by reference to AICPA guidelines.

d. Materiality is a matter of professional judgment.

7.  Which of the following is an advantage of computer-assisted audit tools and techniques (CAATTs)?

a. The CAATTs programs are all written in one identical computer language.

b. The software can be used for audits of clients that use differing computer equipment and file formats.

c. CAATTs has reduced the need for the auditor to study input controls for computerrelated procedures.

d. The use of CAATTs can be substituted for a relatively large part of the required testing

8.  The primary purpose for obtaining an understanding of an audit client’s internal control is to

a. Provide a basis for making constructive suggestions in a management letter.

b. Determine the nature, timing, and extent of tests to be performed in the audit.

c. Obtain sufficient competent audit evidence to afford a reasonable basis for an

opinion on the financial statements under examination.

d. Provide information for a communication of internal control-related matters to

management.

9.  In most audits of large companies, internal control risk assessment contributes to audit efficiency, which means

a. The cost of substantive procedures will exceed the cost of control evaluation work.

b. Auditors will be able to reduce the cost of substantive procedures by an amount more than the control evaluation costs.

c. The cost of control evaluation work will exceed the cost of substantive procedures.

d. Auditors will be able to reduce the cost of substantive procedures by an amount less than the control evaluation costs.

10.  Which of the following is a device designed to help the audit team obtain evidence about the control environment and about the accounting and control procedures of an audit client?

a. A narrative memorandum describing the control system.

b. An internal control questionnaire.

c. A flowchart of the documents and procedures used by the company.

d. All of the above.

11.  Which of the following statements is correct? As a result of the Sarbanes-Oxley Act of 2002,

a. Public companies must report on the quality of their internal controls.

b. CPA firms cannot provide consulting services to any public company.

c. CPA firms can provide tax services only to nonpublic companies.

d. Accounting standards are set by the PCAOB.

12.  Which of the following is an inappropriate description of management’s role in preparing financial statements and reports on internal control over financial reporting? Management has the primary responsibility for:

a. Determining the scope of internal and external audit activities.

b. Preparing financial statements that are fairly presented in accordance with

GAAP.

c. Selecting accounting principles that best portray the economic reality of the

organization’s transactions and current state.

e. Developing, implementing, and assessing the internal control processes over financial reporting.

13.  The second standard of fieldwork requires the auditor to do all of the following except:

a. Understand the business and its environment.

b. Understand the risks related to financial reporting.

c. Perform analytical procedures to identify potential misstatements in the financial statements.

d. Obtain an understanding of internal control and potential weaknesses in controls.

14.  The Sarbanes-Oxley Act prohibits public accounting firms from providing certain services to audit clients that are public companies. Which of the following

services is not prohibited?

a. Internal audit services

b. Financial information systems design and implementation services

c. Appraisal services

d. Tax preparation services

15.  According to the AICPA’s ethical standards, an auditor would be considered independent in which of the following instances?

a. The auditor has an automobile loan from a client bank.

b. The auditor is also an attorney who advises the client as its general counsel.

c. An employee of the auditor donates service as treasurer of a charitable organization that is a client.

d. The client owes the auditor fees for two consecutive annual audits.

16.  An engagement letter should be written before the start of an audit because:

a. It may limit the auditor’s legal liability by specifying the auditor’s responsibilities.

b. It specifies the client’s responsibility for preparing schedules and making the

records available to the auditor.

c. It specifies the basis for billing the audit for the upcoming year.

d. All of the above

17.  If the auditor has concerns about the integrity of management, which of the following would not be an appropriate action?

a. Refuse to accept the engagement because a client does not have an inalienable right to an audit.

b. Expand audit procedures in areas where management representations are normally important by requesting outside verifiable evidence.

c. Raise the audit fees to compensate for the risk inherent in the audit, but do

not plan any extended audit procedures.

d. Plan the audit with a higher degree of skepticism, including specific procedures that should be effective in uncovering management fraud.

18.  Which of the following would not be considered a limitation of the audit risk

model?

a. The model treats each risk component as a separate and independent factor

when some of the factors are related.

b. Inherent risk is difficult, if not impossible, to formally assess.

c. It is difficult, if not impossible, to formally assess either control or detection

risk.

d. The model provides an overall framework for determining the allocation of

audit work to risk areas.

19.  The auditor concludes that a public company has significant deficiencies in its internal controls over financial reporting. Which of the following is a proper response to this finding?

a. Report the deficiencies to management and the audit committee.

b. Report the deficiencies in the report to shareholders.

c. Expand the planned testing of account balances to consider the types of errors

that might occur because of the deficiency.

d. All of the above

e. a and c only

20.   Which of the following would be considered a significant deficiency in an organization’s control environment?

a. The internal audit function is outsourced to a public accounting firm that is

not performing the financial statement audit.

b. Management has approximately 50 percent of its compensation in stock options, but the options cannot be exercised for five years.

c. Management relies on the external audit as its primary source of monitoring

controls.

d. The audit committee meets with the external auditor and the internal auditor

but does not allow the CFO to participate in these meetings.

21.  Which of the following controls would be most effective in assisting the organization in achieving the completeness objective?

a. All employee time cards should be collected by the supervisor and transmitted

directly to the payroll department for processing.

b. All shipments must be approved by the credit manager to ensure that the total

invoice amount does not exceed approved limits.

c. All receipts of merchandise must be independently counted or weighed by

someone in the receiving department who also reviews the goods for quality

control deficiencies.

d. All shipments must be recorded on prenumbered shipping documents that are

independently accounted for.

22.  Segregation of duties is best accomplished when the auditor can determine that:

a. Employees perform only one job; for example, someone working on accounts

payable does not have access to other accounting records such as the detail in

property, plant, and equipment.

b. The internal audit department performs an independent test of transactions

throughout the year and reports any errors to departmental managers.

c. The person responsible for reconciling the bank account is responsible for cash disbursements, not cash receipts.

d. The payroll department cannot add employees to the payroll or change pay

rates without the explicit authorization of the personnel department.

23.  The auditor wishes to gather evidence to test the assertion that the client’s capitalization of leased equipment assets is properly valued. Which of the following sources of evidence will the auditor find to be the most persuasive (most reliable and relevant)?

a. Direct observation of the leased equipment

b. Examination of the lease contract and recomputation of capitalized amount

and current amortization

c. Confirmation of the current purchase price for similar equipment with vendors

d. Confirmation of the original cost of the equipment with the lessor

24.  An auditor determines that management integrity is high, the risk of account

misstatements is low, and the client’s information system is reliable.  Which of the following conclusions can be reached regarding the need to perform direct tests of account balances?

a. Direct tests should be limited to material account balances, and the extent of

testing should be sufficient to corroborate the auditor’s assessment of low risk.

b. Direct tests of account balances are not needed.

c. Direct tests of account balances are necessary if audit risk was set at a low level, but are not necessary if audit risk was set at a high level.

d. Direct tests should be performed on all account balances to independently verify the correctness of the financial statements.

25.  An auditor observes inventory held by the client and notes that some of the inventory appears to be old, but in good condition. Which of the following conclusions is justified by the audit procedure?

I. The older inventory is obsolete.

II. The inventory is owned by the company.

III. Inventory needs to be reduced to current market value.

a. I only

b. II only

c. I and III only

d. III only

26.   Which of the following statements is not true concerning the auditor’s documentation?

a. The auditor should document the reasoning process and conclusions reached

for significant account balances even if audit tests show no exceptions.

b. Documentation review is facilitated if a standard documentation format is

used.

c. Audit documents should cross-reference other documents if the other documents contain work that affects the auditor’s overall conclusion.

d. The client should not prepare documentation schedules for the auditor even if

the auditor independently tests them.

27.  Which of the following statements are correct regarding access controls:

I. Proper implementation of access controls requires the firm to identify all

users and the access they should have to data.

II. Retina scans cannot be duplicated and thus are the best method to authenticate

users.

III. Passwords are the most widely used method of authentication.

a. I

b. I and III

c. II and III

d. I, II, and III

28.  Which of the following procedures is least likely to be performed by an auditor using generalized audit software (GAS)?

a. Selection and printing of accounts receivable confirmations from a client’s

master file.

b. Evaluation of the audit results based on a statistical sample of inventory.

c. Identification and selection of inventory items that have characteristics that the

auditor believes indicate obsolete inventory.

d. Creation of a detailed printout of a file so that an auditor can read the complete

file and select items for audit verification.