 VERSION #1

Answer Multiple choice questions (#1-28) on your scantron, WRITE YOUR VERSION ON YOUR SCANTRON.
Answer #29 & 30 in the space provided within this exam.
Answer the simulation assignment in your blue book.

1. You just assessed control risk at "less than high", what are you going to do now?
   A) Tests of design and operating effectiveness  
   B) More substantive tests of details.  
   C) Tests of design  
   D) I'm going to Disneyland

2. Which of the following statements is not correct?
   A) Reviewing interbank transfers is important to the auditor because of the possibility that the client
      may be engaged in kiting or mistakenly have reported only one side of a transfer between bank
      accounts.
   B) Confirmation of cash need not be performed if the bank statement agrees to the bank reconciliation
      which reconciles the bank balance to the balance recorded in the general ledger.
   C) Cash is important to the audit process because of its vulnerability to misappropriation, despite the
      fact that the balance at the balance sheet date may be immaterial.
   D) Even though the year end cash balance can be verified by vouching to the bank statement,
      confirmations should still be sent directly to the bank and include additional questions about
      restrictions upon the cash and any financing arrangements with the bank.

3. An internal control questionnaire indicates that an approved receiving report is required to accompany
   every check request for payment of merchandise. Which of the following procedures provides the best
   evidence on operating effectiveness?
   A) Select and examine canceled checks and test whether the related receiving reports are dated no
      earlier than the checks.
   B) Select and examine receiving reports and test whether the related canceled checks are dated no
      earlier than the receiving reports.
   C) Select and examine canceled checks and test whether the related receiving reports are dated no
      later than the checks.
   D) Select and examine receiving reports and test whether the related canceled checks are dated no
      later than the receiving reports.

4. Which of the following is not an assertion that is made in the financial statements by management
   concerning each major account and class of transaction?
   A) Presentation and disclosure.  
   B) Completeness.  
   C) Rights and obligations.  
   D) Legality.

5. If an auditor is selecting a sample, the auditor must document:
   A) Only how the items were selected
   B) Selection criteria is not necessary, but the specific items selected should always be documented
   C) Who knows (ps, this is not a very wise answer)
   D) How the items were selected, as well as the items selected in a fashion which can be reperformed
6. There is a presumption that the auditor will not test 100% of the activity. In certain instances, the auditor will use her judgment in determining which items to select, while in others, the auditor will not use judgment. In such instances, the auditor is relying upon:
   A) Non-statistical sampling techniques  C) Judgmental sampling techniques
   B) Random number tables  D) Statistical sampling techniques

7. Auditing cash will generally include which of the following substantive procedures?
   A) Sending confirmations directly to the bank
   B) Obtaining bank reconciliations
   C) Validating that the bank reconciliation agrees to the "bank balance"
   D) All of these

8. Which of the following is least likely to be evidence on operating effectiveness?
   A) Confirmations of accounts receivable.
   B) Signatures on authorization forms.
   C) Cancelled supporting documents.
   D) Records documenting usage of computer programs.

9. Which of the following may cause internal controls to be ineffective?
   A) Lack of monitoring  B) Human error  C) Management override  D) All of these.

10. What is most likely to identify a material misstatement in a financial statement?
    A) Tests of integrity  C) Tests of design
    B) Substantive audit procedures  D) Tests of operating effectiveness

11. Statistical sampling may be used to test:
    A) Both qualitative and quantitative characteristics- both TOE's and substantive tests of details
    B) Qualitative characteristics, such as test of operating effectiveness of controls ONLY;
    C) Quantitative characteristics, such as substantive tests of details ONLY
    D) None of these

12. We are auditing XYZ, Co. and discover a fraud risk related to retail store employees giving free merchandise to their friends. The auditors determine that the risk of material misstatement due to this fraud risk is low and that XYZ, Co. has taken appropriate measures to reduce this fraud risk to the greatest extent possible and that they have taken measures to account for the "shrinkage" resulting from this fraudulent activity. Which of the following statements is most accurate regarding how the auditor should proceed relative to this fraud risk factor:
    A) The auditor should immediately resign from the engagement and notify the audit committee of the reason for their resignation;
    B) The auditor should continue as if nothing happened as they are only responsible for material misstatements.
    C) The auditor should update their planning to incorporate this factor (if not already identified during planning), but based on the likelihood of misstatement and the measures already taken by management, is not obligated to do anything further.
    D) The auditor should immediately resign from the engagement and notify the department of justice of the reason for their resignation;
13. During financial statement audits, the auditors' consideration of their clients' internal control is integral to both assessing control risk and to:
   B) Providing a reasonable basis for an opinion on compliance with applicable laws.
   C) Planning the audit.
   D) Assessing inherent risk.

14. After obtaining an understanding of internal control and arriving at a planned assessed level of control risk, an auditor decided to perform tests of controls. The auditor most likely decided that:
   A) There were many internal control deficiencies that would allow misstatements to enter the accounting system.
   B) It would be efficient to perform tests of controls that would result in a reduction in planned substantive tests.
   C) Additional evidence to support a reduction in the assessed level of control risk is not available.
   D) An increase in the assessed level of control risk is justified for certain financial statement assertions.

15. Audit planning should be performed:
   A) At the beginning of the engagement and updated continuously based on information obtained during the performance of the audit.
   B) At the beginning of the engagement.
   C) Prior to performing any substantive audit procedures and prior to assessing control risk.
   D) Prior to performing any substantive audit procedures.

16. Which of the following are benefits of statistical sampling?
   A) It helps the auditor to focus their time and attention to the areas of highest risk.
   B) It provides the auditor with a rational means of supporting the amount of work performed in the event that sufficiency of their work is called into question.
   C) Audit fees would not be reasonable if auditors had to audit 100% of all balances and activity.
   D) All of these answers are true.

17. The Sarbanes-Oxley Act of 2002 requires that the audit committee:
   A) Be directly responsible for the appointment, compensation and oversight of the work of the CPA firm.
   B) Require that the company's CPA firm rotate the partner in charge of the audit.
   C) Review the level of management compensation.
   D) Annually reassess control risk using information from the CPA firm.

18. Preliminary arrangements agreed to by the auditors and the client should be reduced to writing by the auditors. The best place to set forth these arrangements is in:
   A) A client representation letter.
   B) A confirmation letter attached to the constructive services letter.
   C) An engagement letter.
   D) A memorandum to be placed in the permanent section of the auditing working papers.

19. Which of the following is not generally used for selecting samples?
   A) Systematic selection.
   B) Random number tables.
   C) Random number generators.
   D) Physical representation numbers.
20. Which statement is correct concerning the relevance of various types of controls to a financial statement audit?
   A) Controls over safeguarding assets and liabilities are of primary importance, while controls over the reliability of financial reporting may also be relevant.
   B) An auditor may ordinarily ignore a consideration of controls when a substantive audit approach is used.
   C) All controls are ordinarily relevant to an audit.
   D) Controls over the reliability of financial reporting are ordinarily most directly relevant to an audit, but other controls may also be relevant.

21. Which of the following is generally not true about statistical sampling as compared to nonstatistical sampling?
   A) Statistical sampling allows a more objective evaluation of sample results.
   B) Statistical sampling may assist the auditors in designing more efficient samples.
   C) Statistical sample plans involve additional costs of evaluation.
   D) Statistical samples are more representative of the population.

22. Which of the following is not a control that generally is established over cash receipts?
   A) To prevent theft of cash, receipts should be deposited daily.
   B) To prevent abstraction of cash, a control listing of cash receipts should be prepared by mailroom personnel.
   C) To insure accurate posting, the accounts receivable clerk should post the customers' receipts from customers' checks.
   D) To insure accuracy of the accounts receivable records, the records should be reconciled monthly to the accounts receivable controlling account.

23. It's a good idea for the mail-room to create a control listing of all checks received before forwarding the mail and checks to the appropriate department so that:
   A) The Company can validate the performance of internal controls.
   B) The Company has a log in case a customer indicates that they sent a payment.
   C) The Company can compare to the deposits to be sure all checks received are accounted for.
   D) The Company has a log which will be important for the bank reconciliation.

24. The decision to accept or continue a relationship with a client is based upon which type of risk?
   A) Audit Risk  B) Acceptance risk  C) Engagement risk  D) Detection risk

25. Many companies have strong internal control processes, but those are not well documented, easily tested or related to financial reporting. This is a result of, and the impact to the auditor is:
   A) Governmental regulation- allowing reliance by the auditor;
   B) Striving to have an easy audit- allowing reliance by the auditor;
   C) Years of operating their business in the most productive way possible- but does not lend to controls the auditor may rely upon;
   D) None of the above.

26. Under SEC Staff Accounting Bulletin No. 99, materiality assessments should include consideration of:
   A) Quantitative factors only;  C) Neither Qualitative nor Quantitative factors.
   B) Both Qualitative and Quantitative factors;  D) Qualitative factors only;
27. Which of the following statements is true about materiality:
   A) An item which would impact the decision of a reasonable financial statement user is material regardless of its dollar impact.
   B) B&C are true.
   C) An item impacting net income by an immaterial dollar amount (less than 5% of net income) is not material.
   D) Materiality is based on both quantitative and qualitative factors.

28. The valuation assertion does not pertain to which item?
   A) Sales   B) Accounts receivable   C) Cash   D) Investments

29. What are the factors of a control environment.

30. We document in an APG the procedures to be performed. Document the substantive procedures to be performed in the standard audit of one of a client's cash accounts.
Answer Key

1. A
2. B
3. C
4. D
5. D
6. D
7. D
8. A
9. D
10. B
11. A
12. C
13. C
14. B
15. A
16. D
17. A
18. C
19. D
20. D
21. D
22. C
23. C
24. C
25. C
26. B
27. B
28. C
29. n
  n Integrity and ethical values
  n Commitment to competence
  n Human resource policies and practices
  n Assignment of authority and responsibility
  n Management philosophy and operating style
  n Board of directors or audit committee

  Organizational structure
30. 1) Obtain the bank reconciliation
  2) Obtain the bank statement.
  3) Test the bank reconciliation to ensure that it (a) reconciles the bank balance to the general ledger balance (b) the reconciling items are appropriate-- see below item (4).
  4) Ensure that checks outstanding are complete by comparing to the subsequent month bank statement. ensure that deposits in transit did in fact clear the bank in the subsequent month.
  5) Send third party confirmation directly to the bank.
  6) Review intercompany transfers near the end of the period for evidence of kiting.