

I - MULTIPLE CHOICE QUESTIONS (50%)

- 1. Independent auditing can best be described as:**
 - A. A branch of accounting.
 - B. A discipline that provides assurance regarding the results of accounting and other functional operations and data.
 - C. A professional activity that measures and communicates financial and business data.
 - D. A regulatory function that prevents the issuance of improper financial information.

- 2. The examination of all of a client's transactions would make an audit very costly. Thus, auditors rely heavily on sampling as a way to obtain evidence. Which of the following would result in a smaller sample?**
 - A. A decrease in the materiality level.
 - B. A decrease in the desired level of assurance.
 - C. An assessment that the account being audited is high risk.
 - D. An increase in the desired level of assurance.

- 3. The most favorable type of audit report opinion for the client to receive is:**
 - A. Qualified.
 - B. Unqualified.
 - C. Full assurance.
 - D. Exceptional.

- 4. Which of the following is generally not considered one of the five business processes or cycles?**
 - A. Information technology
 - B. Revenue [or sales]
 - C. Financing
 - D. Inventory management

- 5. Which of the following management assertions is generally of greatest importance in the audit of inventory?**
 - A. Existence
 - B. Completeness
 - C. Rights and Obligations
 - D. Presentation and Disclosure

- 6. To exercise due professional care, an auditor should:**
 - A. Attain the proper balance of professional experience and formal education.
 - B. Critically review the work performed and judgment exercised by those assisting in the audit.
 - C. Examine all available corroborating evidence supporting management's assertions.
 - D. Design the audit to detect all instances of illegal acts.

- 7. The responsibility for implementing sound accounting practices and principles, maintaining an adequate internal control structure, and making fair representations in the financial statements rests primarily with the:**
- A. Senior management
 - B. External auditors
 - C. Internal audit department
 - D. Shareholders
- 8. Which of the following is considered an example of a compliance audit?**
- A. The examination a company's claims that its product is superior to that of a competitor on specific dimensions.
 - B. The examination of a school district networked computer system.
 - C. The examination of a company's adherence to government-mandated safety provisions.
 - D. The examination of a company's financial statements.
- 9. Which of the following primarily shapes the context in which auditing takes place?**
- A. The American Institute of Certified Public Accountants [AICPA]
 - B. The Central Bank of Lebanon
 - C. The client company's business environment
 - D. Legislation passed by the Ministry of Finance
- 10. An "integrated audit" includes:**
- A. A special audit related to management fraud.
 - B. A financial statement audit and an audit of internal control over financial reporting.
 - C. A financial statement audit and a special audit related to management fraud.
 - D. A special audit related to management fraud and an audit of internal control over financial reporting.
- 11. The existence of audit risk is recognized by the statement in the auditor's standard report that the:**
- A. Auditor obtains reasonable assurance about whether the financial statements are free of material misstatements.
 - B. Auditor is responsible for expressing an opinion on the financial statements, which are the responsibility of management.
 - C. Financial statements are presented fairly, in all material respects, in conformity with GAAP.
 - D. Audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements.
- 12. Which of the following factors would an auditor least likely consider when assessing the inherent risk associated with client sales transactions?**
- A. Billings are made using the percentage-of-completion method of revenue recognition.
 - B. The nature of the credit authorization process.

- C. Some invoices are normally billed prior to shipments [which occur at a later date].
D. The conditions of the sale allow for a right of return or the right to modify the purchase agreement.
- 13. The risk that an auditor's procedures will lead to a conclusion that a material misstatement in an account balance does not exist, when in fact a misstatement did occur, is known as:**
- A. Audit risk.
 - B. Detection risk.
 - C. Inherent risk.
 - D. Business risk.
- 14. One of your clients recently upgraded their accounting system from a medium-scale general ledger package to a complex state-of-the-art enterprise resource planning system. This installation took place over the last nine months of their fiscal year and is nearly 100% complete by the balance sheet date. Which of the following best describes the main effect of this event on the audit risk model for the current year?**
- A. It will likely increase risk of material misstatement.
 - B. It will likely decrease risk of material misstatement.
 - C. It will likely decrease detection risk.
 - D. It will likely increase detection risk.
- 15. Which of the following factors is least likely to represent an opportunity to commit fraud?**
- A. The audit committee is ineffective.
 - B. Poor internal controls over cash transactions
 - C. The existence of highly complex transactions
 - D. Operating losses make a hostile takeover imminent.
- 16. The auditor obtains an understanding of the entity and its environment by performing all of the following assessment procedures except:**
- A. Inquiries of management and others.
 - B. Compute the level of detection risk.
 - C. Analytical procedures.
 - D. Observation and inspections.
- 17. As a result of analytical procedures, the auditor determines that the gross profit percentage has declined from 30% in the preceding year to 20% in the current year. The auditor should:**
- A. Express a qualified opinion due to inability of the client company to continue as a going concern
 - B. Evaluate management's performance in causing this decline
 - C. Require footnote disclosure
 - D. Consider the possibility of a misstatement in the financial statements

- 18. The negative form of accounts receivable confirmation request is useful except when**
- A. Internal control surrounding accounts receivable is considered to be effective
 - B. A large number of small balances are involved
 - C. The auditor has reason to believe the persons receiving the requests are likely to give them consideration
 - D. Individual account balances are relatively large
- 19. When evaluating the adequacy of the allowance for uncollectible accounts, an auditor reviews the entity's aging of receivables to support management's balance-related assertion of**
- A. Existence
 - B. Completeness
 - C. Valuation and allocation
 - D. Rights and obligations
- 20. From prior experience, a CPA is aware that the accounts receivable trial balance contains a few unusually large balances. In using statistical sampling, the CPA's best course of action is to**
- A. Eliminate any unusually large balances that appear in the sample
 - B. Continue to draw new samples until no unusually large balances appear in the sample
 - C. Stratify the accounts receivable population so that the unusually large balances are reviewed separately
 - D. Increase the sample size to lessen the effect of the unusually large balances.
- 21. A client erroneously recorded a large purchase twice. Which of the following internal control measures would be most likely to detect this error in a timely and efficient manner?**
- A. Footing the purchases journal
 - B. Reconciling vendors' monthly statements with subsidiary payable ledger accounts
 - C. Tracing totals from the purchases journal to the ledger accounts
 - D. Sending written quarterly confirmations to all vendors
- 22. Which of the following is an internal control that will prevent paid cash disbursement documents from being presented for payment a second time?**
- A. The date on cash disbursement documents must be within a few days of the date that the document is presented for payment
 - B. The official signing the check compares with the documents and should deface (تعطيل) the documents
 - C. Unsigned checks are prepared by individuals who are responsible for signing checks
 - D. Cash disbursement documents are approved by at least two responsible management officials.

- 23. In auditing accounts payable, an auditor's procedures most likely will focus primarily on management's assertion of**
- A. Existence
 - B. Realizable value
 - C. Completeness
 - D. Valuation and allocation
- 24. Which of the following controls most likely will justify a reduced assessed level of control risk concerning plant and equipment acquisitions?**
- A. Periodic physical inspection of plant and equipment by the internal audit staff
 - B. Comparison of current-year plant and equipment account balances with prior-year balances.
 - C. Review of prenumbered purchase orders to detect unrecorded trade-ins
 - D. Approval of periodic depreciation entries by a supervisor independent of the accounting department
- 25. Which of the following is not an internal control deficiency related to factory equipment?**
- A. Checks issued in payment of acquisitions of equipment are not signed by the controller
 - B. All acquisitions of factory equipment are required to be made by the department in need of the equipment
 - C. Factory equipment replacements are generally made when estimated useful lives, as indicated in depreciation schedules, have expired
 - D. Proceeds from sales of fully depreciated equipment are credited to other income
- 26. Which of the following analytical procedures should be applied to the income statement?**
- A. Select sales and expense items and trace amounts to related supporting documents
 - B. Ascertain that the new income amount in the statement of cash flows agrees with the net income amount in the income statement
 - C. Obtain from the proper client representatives the beginning and ending inventory amounts that were used to determine costs of sales
 - D. Compare the actual revenues and expenses with the corresponding figures of the previous year and investigate significant differences
- 27. In testing for unrecorded retirements of equipment, an auditor most likely will**
- A. Select items of equipment from the accounting records and then locate them during the plant tour
 - B. Compare depreciation journal entries with similar prior-year entries in search of fully depreciated equipment
 - C. Inspect items of equipment observed during the plant tour and then trace them to the equipment master file
 - D. Scan the journal for unusual equipment additions and excessive debits to repairs and maintenance expense.

- 28. In connection with the audit of the prepaid insurance account, which of the following procedures is usually not performed by the auditor?**
- A. Recompute the portion of the premium that expired during the year
 - B. Prepare excerpts (extracts) of the insurance policies for audit documentation
 - C. Confirm premium rates with an independent insurance broker
 - D. Examine support for premium payments
- 29. Which of the following audit procedures is least likely to detect an unrecorded liability?**
- A. Analysis and recomputation of interest expense
 - B. Analysis and recomputation of depreciation expense
 - C. Mailing of standard bank confirmation forms
 - D. Reading of the minutes of meetings of the board of directors
- 30. Before expressing an opinion concerning the audit of income and expenses, the auditor will best proceed with the audit of the income statement by**
- A. Applying a rigid measurement standard designed to test for understatement of net income
 - B. Analyzing the beginning and ending balance sheet inventory amounts
 - C. Making net income comparisons to published industry trends and ratios
 - D. Auditing income statement accounts concurrently with the related balance sheet accounts
- 31. In a company with materials and supplies that include a great number of items, a fundamental deficiency in control requirements will be indicated if**
- A. The cycle basis for physical inventory taking was to be used
 - B. Minor supply items were to be expensed when acquired
 - C. A perpetual inventory master file is not maintained for items of small value
 - D. The storekeeping function were to be combined with production and record keeping
- 32. When an auditor tests a client's cost accounting records, the auditor's tests are primarily designed to determine that**
- A. Costs have been correctly assigned to finished goods, work-in-process, and cost of goods sold
 - B. Quantities on hand have been computed based on acceptable cost account techniques that reasonable approximate actual quantities on hand
 - C. Physical inventories are in substantial agreement with book inventories
 - D. The internal controls are in accordance with generally accepted accounting principles and are functioning as planned
- 33. The accuracy of perpetual inventory master files may be established, in part, by comparing perpetual inventory records with**
- A. Purchase requisitions
 - B. Receiving reports
 - C. Purchase orders
 - D. Vendor payments

- 34. An inventory turnover analysis is useful to the auditor because it may detect**
- A. Inadequacies in inventory pricing
 - B. Methods of avoiding cyclical holding costs
 - C. The existence of obsolete merchandise
 - D. The optimum automatic reorder points
- 35. When obtaining evidence regarding litigation against a client, the CPA will be least interested in determining**
- A. The period in which the underlying cause of the litigation occurred
 - B. The probability of an unfavorable outcome
 - C. An estimate of when the matter will be resolved
 - D. An estimate of the potential loss
- 36. Subsequent events for reporting purposes are defined as events that occur subsequent to the**
- A. Balance sheet date
 - B. Date of the auditor's report
 - C. Balance sheet date but before the date of the auditor's report
 - D. Date of the auditor's report and concern contingencies that are not reflected in the financial statements
- 37. An example of an event occurring in the period of the auditor's field work subsequent to the end of the year being audited that normally will not require disclosure in the financial statements or auditor's report is**
- A. Serious damage to the company's plant from a widespread flood
 - B. Issuance of a widely advertised capital stock issue with restrictive covenants
 - C. Settlement of a large liability for considerably less than the amount recorded
 - D. Decreased sales volume resulting from a general business recession
- 38. Negative assurance is not permissible in:**
- A. Reports based upon a review engagement.
 - B. Letters required by security underwriters for data pertinent to SEC registration statements.
 - C. Reports based on an audit of interim financial statements of a closely held business entity.
 - D. Reports relating to the results of agreed-upon procedures to one or more specified elements, accounts, or items of financial statement.
- 39. If an auditor "proves" the bank statement in the month subsequent to the balance sheet date, it is primarily a test for:**
- A. Errors.
 - B. Omissions.
 - C. Kiting.
 - D. Intentional misstatements.

40. Using statistical sampling to assist in verifying the year-end accounts payable balance, an auditor has accumulated the following data:

	Number of accounts	Book balance	Balance determined by the auditor
Population:	4,100	\$5,000,000	?
Sample:	200	\$ 250,000	\$300,000

Using the ratio estimation technique, the auditor's estimate of year-end accounts payable balance would be:

- A. \$5,050,000.
 - B. \$5,125,000.
 - C. \$6,000,000.
 - D. \$6,150,000.
- 41. Which of the following is the least important consideration in determining the sample size of confirmations?**
- A. The types of confirmations being sent; that is, positive or negative.
 - B. The results of related analytical procedures.
 - C. Total annual credit sales.
 - D. The auditor's assessment of detection risk.
- 42. Which of the following is not a reason why the auditor requests that the client provide a letter of representation?**
- A. Professional auditing standards require the auditor to obtain a letter of representation.
 - B. It impresses upon management its responsibility for the accuracy of the information in the financial statements.
 - C. It provides written documentation of the oral responses already received to inquiries of management.
 - D. It provides written documentation, which is a higher quality of evidence than management's oral responses to inquiries.
- 43. Your accounting firm has accepted a compilation engagement from a client in which your firm is not independent. In that case you:**
- A. May not accept the engagement.
 - B. May accept the engagement and disclose the lack of independence. may accept the engagement and not disclose the lack of independence.
 - C. May accept the engagement and disclose the lack of independence and the reason for the lack of independence.

- 44. An accountant has accepted an engagement in which the audit procedures of inquiry and analytical procedures will be employed. These procedures will form the basis for issuance of:**
- A. A compilation report.
 - B. Audit report on supplemental information issued by the client.
 - C. Management advisory report requested by the audit committee.
 - D. Review report on comparative financial statements for a non-public company.
- 45. Which of the following internal controls in the payroll and personnel cycle is generally least important to an auditor?**
- A. Formal methods of informing payroll personnel of new employees.
 - B. Reconciliation of total payroll expense in the general ledger with the payroll tax returns and the tax forms.
 - C. Authorization of changes in pay rates.
 - D. Notice of the termination date of employees no longer working for the company.
- 46. When auditing a public warehouse, which of the following is the most important audit procedure with respect to disclosing unrecorded liabilities?**
- A. Observation of inventory.
 - B. Review of outstanding receipts.
 - C. Inspection of receiving and issuing procedures.
 - D. Confirmation of negotiable receipts with holders.
- 47. When an outside specialist has assumed full responsibility for taking the client's physical inventory, reliance on the specialist's report is acceptable if:**
- A. The auditor's report contains a reference to the assumption of full responsibility.
 - B. The auditor is satisfied through application of appropriate procedures as to the reputation and competence of the specialist.
 - C. The auditor conducted the same audit tests and procedures as would have been applicable if the client's employees took the physical inventory.
 - D. Circumstances made it impracticable or impossible for the auditor either to do the work personally or observe the work done by the inventory firm.
- 48. The auditor's responsibility with respect to events occurring between the balance sheet date and the end of the audit examination is best expressed by which of the following statements?**
- A. The auditor is fully responsible for events occurring in the subsequent period and should extend all detailed procedures through the last day of fieldwork.
 - B. The auditor is responsible for determining that a proper cutoff has been made and performing a general review of events occurring in the subsequent period.

- C. The auditor's responsibility is to determine that a proper cutoff has been made and that transactions recorded on or before the balance sheet date actually occurred.
- D. The auditor has no responsibility for events occurring in the subsequent period unless these events affect transactions recorded on or before the balance sheet date.

49. Analytical procedures must be performed in:

- A. The planning and test of control stages.
- B. Conjunction with tests of transactions and tests of details of balances.
- C. The planning and completion stages.
- D. The planning, test of control, and completion stages.

50. The failure to capitalize a permanent asset, or the recording of an asset acquisition at the improper amount, affects the balance sheet:

- E. Forever.
- F. For the current period.
- G. For the depreciable life of the asset.
- H. Until the firm disposes of the asset.

II) INDICATE WHETHER EACH OF THE FOLLOWING IS - TRUE OR FALSE (10%)

1. ____ The objective of the audit of financial statements by an independent auditor is to verify that the financial statements are free of misstatements and accurately represent the company's financial position and results of operations.
2. ____ The auditor's responsibility for uncovering direct-effect illegal acts is the same as for fraud.
3. ____ One disadvantage of functional auditing is the failure to evaluate interrelated functions.
4. ____ For each internal control deficiency identified by the auditor, he or she should design one or more tests of controls to assess the extent of the deficiency and its effect on the financial statements.
5. ____ For effective internal control, it is important that sales be recorded as soon after the customer order is received as possible to prevent the unintentional omission of transactions from the records and to make sure that sales are recorded in the proper period.
6. ____ To test for overstatement cutoff amounts when auditing Accounts payable, the auditor should trace receiving reports issued before year-end to related vendors' invoices to make sure they are not recorded as Accounts payable.
7. ____ When verifying the correct balance in Accounts payable, vendors' invoices are more useful than vendors' statements.

July Exam 2016

8. _____ Recording an acquisition of a fixed asset at an improper amount affects the balance sheet until the company disposes of the asset, but the income statement is not affected.
9. _____ Analytical procedures are used primarily to help the auditor analyze the debit and credit activity in an account.
10. _____ When auditing Accounts payable, the auditor is more concerned about the possibility of overstatements than understatements.

III) SHORT QUESTIONS (Please answer in bullet points) (15%)

Question 1:

A financial statement audit typically consists of four phases. Identify each of these four phases of an audit and discuss the major activities performed by the auditor in each phase.

Question 2:

ISA 700 *Forming an Opinion on Financial Statements* provides guidance on the form and content of the auditor's report and should contain a number of elements.

Required:

Name **eight** elements of an unmodified auditor's report.

Question 3:

Describe **three** situations in which the integrity of the auditor may be under threat.

IV- CASES (25%)

Case I (10%)

The fieldwork for the December 31, 2011 audit of NASA S.A.L. ended on March 17, 2012. The financial statements and auditor's report were issued and mailed to stockholders on March 29, 2012. In each of the material situations (1 through 5) below, indicate the appropriate action (a, b, c, d, or e). The possible actions are as follows:

- a. Adjust the December 31, 2011 financial statements.
- b. Disclose the information in a footnote in the December 31, 2011 financial statements.
- c. Request the client revise and reissue the December 31, 2011 financial statements. The revision should involve an adjustment to the December 31, 2011 financial statements.
- d. Request the client revise and reissue the December 31, 2011 financial statements. The revision should involve the addition of a footnote, but no adjustment, to the December 31, 2011 financial statements.
- e. No action is required.

The situations are as follows:

_____ 1. On April 5, 2012, you discovered that, on February 16, 2012 a flood destroyed the entire uninsured inventory in one of NASA S.A.L.'s warehouses.

_____ 2. On February 17, 2012, you discovered that, on February 16, 2012, a flood destroyed the entire uninsured inventory in one of NASA S.A.L.'s warehouses.

_____ 3. On February 17, 2012, you discovered that, on November 30, 2011, a flood destroyed the entire uninsured inventory in one of NASA S.A.L.'s warehouses.

_____ 4. On April 5, 2012, you discovered that, on March 30, 2012, a fire destroyed one of NASA S.A.L.'s 13 plants.

_____ 5. On April 7, 2012, you discovered that a debtor of NASA S.A.L. went bankrupt on January 6, 2012, due to gradual declining financial health.

Case II (15%)

Below are three audit procedures, all of which are tests of transactions associated with the audit of the acquisition and payment cycle. Also below are the six general transaction-related audit objectives and the five management assertions. For each audit procedure, indicate (1) its audit objective, and (2) the management assertion being tested.

<u>Audit Objectives</u>	<u>Assertions</u>
A. Occurrence	V. Occurrence
B. Completeness	W. Completeness
C. Accuracy	X. Accuracy
D. Posting and summarization	Y. Classification
E. Classification	Z. Cutoff
F. Timing	

1. Foot the purchases journal and trace the totals to the related general ledger accounts. (1) ____. (2) ____.	
2. Recompute the cash discounts taken by the client. (1) ____. (2) ____.	
3. Examine supporting documentation for a sample of transactions for authorized payee and amount and to determine services or goods were received. (1) ____. (2) ____.	