

Chapter 01

1. The need for independent assurance arises because the interests of the users of information may be different from the interests of those responsible for providing information.

- a. True
- b. False

ANSWER: True

2. A financial statement audit is a systematic process of objectively obtaining and evaluating evidence.

- a. True
- b. False

ANSWER: True

3. A bank using Milton Company's financial statements to evaluate Milton's loan application is an example of a user's need for unbiased reporting.

- a. True
- b. False

ANSWER: True

4. An integrated audit requires the auditor to assess the effectiveness of internal controls.

- a. True
- b. False

ANSWER: True

5. Auditors obtain and evaluate evidence regarding assertions about economic actions and events to verify the accuracy of those assertions.

- a. True
- b. False

ANSWER: False

6. Auditing is the process of verifying and assuring the complete accuracy of the financial statements.

- a. True
- b. False

ANSWER: False

7. Management may have incentives to present biased financial information, but the various users of the statements are likely to have the same interest in the financial information.

- a. True
- b. False

ANSWER: False

8. Auditing exists because users need unbiased information on which to assess management performance and make economic decisions.

- a. True
- b. False

ANSWER: True

Chapter 01

9. Users rely on the auditors' independent assessment of financial statement presentation because few users have direct knowledge of the company's operations.

- a. True
- b. False

ANSWER: True

10. If the auditor has no reservations about management's financial statements, then the auditor will issue a qualified opinion.

- a. True
- b. False

ANSWER: False

11. Independence is often referred to as the cornerstone of the auditing profession.

- a. True
- b. False

ANSWER: True

12. Auditors generally need quantitative and mathematical skills more than they need communication and leadership skills.

- a. True
- b. False

ANSWER: False

13. The overall objective of an audit is to guarantee the financial statements are free of misstatement.

- a. True
- b. False

ANSWER: False

14. The foundation for the audit opinion formulation process relies on obtaining evidence to support the auditor's opinion.

- a. True
- b. False

ANSWER: True

15. Complex transactions, information, and processing systems provide an opportunity for management to mislead users of financial statements.

- a. True
- b. False

ANSWER: True

16. Users of audited financial statements include a company's bondholders but not its stockholders, who are the owners of the company.

- a. True

Chapter 01

b. False

ANSWER: False

17. A key responsibility of the internal audit function is to provide assurance on the reliability of financial information reported to external users of audited financial statements.

a. True
b. False

ANSWER: False

18. The audit committee oversees both the internal and external auditors.

a. True
b. False

ANSWER: True

19. A CPA is a certified public accountant who is licensed by a state board of accountancy.

a. True
b. False

ANSWER: True

20. Internal controls are the responsibility of management.

a. True
b. False

ANSWER: True

21. Audit staff performing audit work must be appropriately supervised by partners and managers.

a. True
b. False

ANSWER: True

22. An auditor who has reservations about the effectiveness of a client company's internal controls would issue an adverse opinion on internal controls.

a. True
b. False

ANSWER: True

23. Audit firm culture is one of the primary drivers of audit quality.

a. True
b. False

ANSWER: True

24. Effective audit processes, by themselves, are sufficient to achieve audit quality.

a. True
b. False

Chapter 01

ANSWER:

False

25. A quality audit is one performed “in accordance with generally accepted auditing standards (GAAS) to provide reasonable assurance that the audited financial statements and related disclosures are presented in accordance with generally accepted accounting principles (GAAP) and are not materially misstated whether due to errors or fraud.”

- a. True
- b. False

ANSWER:

True

26. Audit quality is driven, in part, by the skills and personal qualities of audit partners and staff.

- a. True
- b. False

ANSWER:

True

27. The amount of time allotted for the completion of the audit is a factor that affects audit quality and is outside the direct control of the auditor.

- a. True
- b. False

ANSWER:

False

28. Auditors should conduct their work with an attitude of professional skepticism.

- a. True
- b. False

ANSWER:

True

29. In the United States, auditors form conclusions about whether the financial statements are presented fairly in accordance with generally accepted auditing standards (GAAS).

- a. True
- b. False

ANSWER:

False

30. To ensure audit quality, audits of public companies must be performed by multinational accounting firms.

- a. True
- b. False

ANSWER:

False

31. The PCAOB requires disclosure of the names of engagement partners for all public company audits.

- a. True
- b. False

ANSWER:

True

32. The PCAOB is a public board, appointed by Congress, to provide oversight of the firms that audit public companies registered with the SEC.

Chapter 01

- a. True
- b. False

ANSWER: False

33. The SEC is the governmental body with oversight responsibility for the efficient operation of capital markets in the United States.

- a. True
- b. False

ANSWER: True

34. The PCAOB provides the criteria against which the auditor measures the fairness of financial statement presentation.

- a. True
- b. False

ANSWER: False

35. The AICPA sets auditing standards for nonpublic companies.

- a. True
- b. False

ANSWER: True

36. Though often relying on the FASB, the SEC has authority to establish GAAP for public companies.

- a. True
- b. False

ANSWER: True

37. The Center for Audit Quality is responsible for the oversight of the peer review process for registered audit firms.

- a. True
- b. False

ANSWER: False

38. Compliance with the AICPA Code of Professional Conduct depends primarily on the threat of disciplinary actions for violating the Code.

- a. True
- b. False

ANSWER: False

39. The AICPA's conceptual framework of "threats and safeguards" included in the Code of Professional Conduct applies only to AICPA members in public practice.

- a. True
- b. False

ANSWER: True

Chapter 01

40. Threats to an auditor's independence may occur when the auditor has a long-standing relationship with an important person associated with the client.

- a. True
- b. False

ANSWER: True

41. A safeguard is an action or other measure that may eliminate a threat or reduce the threat to an acceptable level.

- a. True
- b. False

ANSWER: True

42. Safeguards implemented by the audit client include mandatory audit partner rotation requirements for public companies.

- a. True
- b. False

ANSWER: False

43. An AICPA member who is not in public practice is not subject to any of the Principles of Professional Conduct.

- a. True
- b. False

ANSWER: False

44. An individual does not need to agree to uphold the AICPA's Code of Professional Conduct in order to become licensed as a CPA.

- a. True
- b. False

ANSWER: False

45. A covered member's investment in a mutual fund owns stock in a firm being audited by the covered member. This investment is a direct financial interest which results in the impairment of independence.

- a. True
- b. False

ANSWER: False

46. When an auditor identifies threats to compliance with the rules of conduct, the auditor must demonstrate that safeguards were applied to eliminate the threat.

- a. True
- b. False

ANSWER: False

47. A covered member who has an immaterial direct financial interest in an audit client is still considered to be independent.

Chapter 01

- a. True
- b. False

ANSWER: False

48. Auditors are permitted to perform for a contingent fee an audit of the financial statements if the audit committee approves the agreement in advance of the services being provided.

- a. True
- b. False

ANSWER: False

49. An auditor may not disclose any confidential client information unless the auditor determines that disclosure is in the public interest.

- a. True
- b. False

ANSWER: False

50. Contingent fees are prohibited for any client for which the auditor performs audit services, but are otherwise permitted.

- a. True
- b. False

ANSWER: False

51. Commissions and referral fees are allowed to audit firms as long as the audit client is informed of the fees.

- a. True
- b. False

ANSWER: False

52. A covered member under the AICPA's rules includes individuals on the engagement team, any individual in a position to influence the engagement team, and a partner or manager who provides more than 10 hours of nonattest services to the audit client within a fiscal year.

- a. True
- b. False

ANSWER: True

53. The AICPA may suspend a member's CPA license for violating its Code of Professional Conduct.

- a. True
- b. False

ANSWER: True

54. A new staff member on an audit engagement may own stock in that client until the audit report is issued.

- a. True
- b. False

ANSWER: False

Chapter 01

55. A contingent fee is a situation in which no fee will be charged unless a specified finding or result is attained.

- a. True
- b. False

ANSWER: True

56. Rule 102, Integrity and Objectivity, of the AICPA Professional Code of Conduct, does not apply to a CPA who is a corporate CFO.

- a. True
- b. False

ANSWER: False

57. Loans between the auditor and the client are permitted in some circumstances.

- a. True
- b. False

ANSWER: True

58. The auditor is permitted to violate the confidentiality rule in providing relevant information to an inquiry by a major shareholder of the client.

- a. True
- b. False

ANSWER: False

59. A covered member's independence would be impaired if an immediate family member was employed by the client company in any position.

- a. True
- b. False

ANSWER: False

60. The AICPA Code of Professional Conduct prohibits an auditor from providing any non-audit services to audit clients because of the threat posed to the auditor's independence.

- a. True
- b. False

ANSWER: False

61. The SEC and PCOAB have independence requirements that apply only to auditors of public companies.

- a. True
- b. False

ANSWER: True

62. Prior to an audit firm accepting a new client, the audit firm contacts the predecessor audit firm. Auditing standards require the predecessor audit firm to respond in a timely manner.

- a. True
- b. False

ANSWER: True

Chapter 01

63. An engagement letter includes the responsibilities of management, but does not include the responsibilities of the auditors.

- a. True
- b. False

ANSWER: False

64. According to the framework for professional decision making, the first step in decision-making is to structure the audit problem.

- a. True
- b. False

ANSWER: True

65. According to Rights Theory, the highest-order rights include rights granted by the government, such as civil rights, legal rights, rights to own property, and license privileges.

- a. True
- b. False

ANSWER: False

66. An ethical dilemma occurs in a situation in which moral duties or obligations conflict.

- a. True
- b. False

ANSWER: True

67. An ethical dilemma occurs when an ethically correct action may conflict with an individual's immediate self-interest.

- a. True
- b. False

ANSWER: True

68. Rights theory focuses on evaluating actions in terms of the fundamental rights of the parties involved.

- a. True
- b. False

ANSWER: True

69. There is a hierarchy of rights to consider when applying rights theory.

- a. True
- b. False

ANSWER: True

70. Utilitarian theory is an approach for addressing ethical problems by identifying a hierarchy of rights that should be considered in solving ethical dilemmas.

- a. True
- b. False

Chapter 01

ANSWER: False

71. Professional judgment is an attitude that includes a questioning mind and a critical evaluation of audit evidence.

- a. True
- b. False

ANSWER: False

72. Without professional skepticism, auditors are susceptible to accepting weak or inaccurate audit evidence.

- a. True
- b. False

ANSWER: True

73. Both client acceptance decisions and client continuance decisions are based on an evaluation of relative risk and audit fees.

- a. True
- b. False

ANSWER: True

74. Auditors consider both quantitative and qualitative risk factors when making client acceptance or continuance decisions.

- a. True
- b. False

ANSWER: True

75. An auditor is not permitted to contact the predecessor auditor when considering a prospective new client.

- a. True
- b. False

ANSWER: False

76. Engagement letters issued to new clients do not specify the amount of audit fees to be charged because fees cannot be determined until the audit has been completed.

- a. True
- b. False

ANSWER: False

77. Professional judgment is rarely required when determining whether the auditor has collected sufficient appropriate audit evidence.

- a. True
- b. False

ANSWER: False

78. Data analytics are an important tool in completing audits and CPAs need to understand how and when to use data analytics.

Chapter 01

- a. True
- b. False

ANSWER: True

79. Round numbers are more common in fraudulent journal entries.

- a. True
- b. False

ANSWER: True

80. Data-analytics tools include only quantitative techniques that auditors use to enhance productivity and effectiveness.

- a. True
- b. False

ANSWER: False

81. Data-analytics tools can facilitate testing 100% of a population.

- a. True
- b. False

ANSWER: True

82. Although data-analytics tools can be useful in an audit, the CPA exam does not include any competency related to data-analytics.

- a. True
- b. False

ANSWER: False

83. A repository for data that enables users to categorize and store any type of data is called a data center.

- a. True
- b. False

ANSWER: False

84. Data validation involves visualizing and presenting the data in order to make a recommendation.

- a. True
- b. False

ANSWER: False

85. Cleaning the data could involve changing the date format from MM/DD/YY to DD/MM/YY to ensure consistency within the data.

- a. True
- b. False

ANSWER: True

86. When performing data analytics, an auditor will decide on an appropriate statistical software package in the Validation Phase (Phase 5).

Chapter 01

- a. True
- b. False

ANSWER: False

87. Tableau is a data visualization tool that auditors can use in data analytics.

- a. True
- b. False

ANSWER: True

88. If an auditor follows the data-analytics process framework exactly, they will not need to exercise any professional judgment.

- a. True
- b. False

ANSWER: False

89. The term data architecture is used to describe organizational procedures that articulate how users collect, store, organize, and use data.

- a. True
- b. False

ANSWER: True

90. Data science has become very important to auditors as it increases the efficiency and effectiveness of the audit.

- a. True
- b. False

ANSWER: True

91. Data visualization refers to the presenting of data to the appropriate audience.

- a. True
- b. False

ANSWER: True

92. Understanding the underlying data to be used in a data analytics procedure is the first step in data analytics.

- a. True
- b. False

ANSWER: False

93. The results of data analytics procedures should always be reported to the board of directors in a visualization.

- a. True
- b. False

ANSWER: True

94. It is always important for an auditor to document the approach and the results of data analytics.

Chapter 01

- a. True
- b. False

ANSWER: True

95. Data science is an interdisciplinary field that aims to help users gain insights from structured and unstructured data.

- a. True
- b. False

ANSWER: True

96. Data analytics can be qualitative or quantitative.

- a. True
- b. False

ANSWER: True

97. Which of the following is not a reason for audits of financial statements of public companies?

- a. Potential bias in providing information.
- b. Greater likelihood of fraud in large public companies.
- c. Complexity of the processing systems.
- d. Remoteness between a user and the organization.

ANSWER: b

98. What is the term used to describe a systematic process of objectively obtaining evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users?

- a. Internal audit.
- b. Financial statement audit.
- c. External audit.
- d. Program audit.

ANSWER: b

99. An Integrated Audit Report provides opinion(s) on which of the following?

- a. The financial statements.
- b. Internal controls.
- c. Both financial statements and internal controls.
- d. Neither financial statements nor internal controls.

ANSWER: c

100. Who are the users of the financial statements?

- a. Management.
- b. Auditors.
- c. Taxing Authorities.

Chapter 01

- d. Both A and C.

ANSWER:

d

101. Which of the following is a factor that creates a need for an independent auditor's assessment of the financial statement presentation?

- a. Complexity of transactions affecting the financial statements.
- b. Lack of criteria on which to base information.
- c. Remoteness of the user from the organization.
- d. Both A and C.

ANSWER:

d

102. What can users of the audit report reasonably expect from the audited financial statements?

- a. The financial statements are complete and contain many of the important financial disclosures.
- b. The financial statements are presented fairly according to the substance of GAAP.
- c. The financial statements are free from all errors.
- d. Auditors have reported any and all fraud.

ANSWER:

b

103. To conduct an audit, what must an auditor do?

- a. Comply with relevant ethical standards.
- b. Exercise perfect judgment.
- c. Obtain sufficient appropriate evidence to provide absolute assurance.
- d. All of these.

ANSWER:

a

104. What is the first phase in an audit?

- a. Client acceptance or client continuance.
- b. Understanding the client.
- c. Understanding internal controls.
- d. Testing of account balances.

ANSWER:

a

105. How is the audit report referred to when the auditor has no reservations about management's financial statements?

- a. An unqualified report.
- b. A qualified report.
- c. An adverse report.
- d. An integrated report.

ANSWER:

a

106. Why is auditing important in a free market society?

Chapter 01

- a. The public requires auditors to function as divisions of regulatory bodies.
- b. Auditors detect all errors and fraud perpetrated by company employees.
- c. Audits provide reliable information upon which to judge economic performance.
- d. The auditor is a form of insurance policy for investors.

ANSWER:

c

107. What document communicates the conclusions of the financial statement audit?

- a. The financial statements.
- b. Written management assertions.
- c. The audit report.
- d. The engagement letter.

ANSWER:

c

108. Who is responsible for internal controls within an organization?

- a. The internal auditor.
- b. The external auditor.
- c. Management.
- d. The PCAOB.

ANSWER:

c

109. What is the primary objective of the independent auditor's report on financial statements?

- a. To report on all instances of fraud.
- b. To assist the board in evaluating management's effectiveness.
- c. To attest to the credit-worthiness of the client.
- d. To give credibility to management's prepared financial statements.

ANSWER:

d

110. Which of the following is not part of the systematic process called auditing?

- a. Communicating results of the audit to users.
- b. Procuring and evaluating evidence.
- c. Assisting management in designing internal controls.
- d. Comparing evidence regarding assertions to certain established criteria.

ANSWER:

c

111. Which of the following is one of the Big 4 multinational accounting firms?

- a. Moore Stephens.
- b. BDO Dunwoody.
- c. Baker Tilly.
- d. PwC.

ANSWER:

d

Chapter 01

112. Which of the following is not a primary driver of audit quality?

- a. Skills and personal qualities of audit staff.
- b. Size of the audit firm.
- c. Effective audit processes.
- d. Audit firm culture.

ANSWER: b

113. According to the Financial Reporting Council (FRC), when is the culture of an audit firm likely to provide a positive contribution to audit quality?

- a. When the leadership of the audit firm ensures partners and other staff have sufficient time and resources to deal with difficult issues as they arise.
- b. When the leadership of the audit firm ensures robust systems for client acceptance and continuation based on the likelihood of increased audit fees.
- c. When the leadership of the audit firm creates an environment where achieving efficiency is valued, invested in and rewarded.
- d. When the leadership of the audit firm ensures financial considerations drive actions.

ANSWER: a

114. Which of the following is a driver of audit quality?

- a. Audit firm culture.
- b. Engagement team skills and attributes.
- c. Factors outside control of auditors.
- d. All of these.

ANSWER: d

115. Which of the following items should an auditor communicate to an audit committee?

- a. Any meaningful threats to auditor objectivity.
- b. The scope of the audit.
- c. The qualitative aspects of the entity's accounting and reporting and potential ways of improving financial reporting.
- d. All of these.

ANSWER: d

116. The Center for Audit Quality is dedicated to enhancing investor confidence in what?

- a. The global capital markets.
- b. Management.
- c. External Auditors.
- d. Internal Auditors.

ANSWER: a

117. International Standards on Auditing (ISAs) are set by which of the following organizations?

Chapter 01

- a. International Center for Audit Quality.
- b. International Auditing and Assurance Standards Board.
- c. American Institute of Certified Public Accountants
- d. All of these organizations participate in setting ISAs.

ANSWER:

b

118. Which of the following is a factor outside of the control of auditors?

- a. Correct understanding of the client business.
- b. Proper Corporate Governance procedures.
- c. Complete audit documentation.
- d. Training of audit staff.

ANSWER:

b

119. Which organization must audit firms register with in order to perform financial statement audits for public companies?

- a. Register with the American Institute of Certified Public Accountants.
- b. Register with the Institute of Internal Auditors.
- c. Register with the U.S. General Accounting Office.
- d. Register with the Public Company Accounting Oversight Board.

ANSWER:

d

120. Which term describes the type of threat that occurs when top management threatens to replace the audit firm because of a disagreement over an accounting issue?

- a. Management participation threat.
- b. Undue influence threat.
- c. Adverse interest threat.
- d. Financial self-interest threat.

ANSWER:

d

121. Which of the following is a correct statement regarding the Code of Ethics of the International Ethics Standards Board for Accountants (IESBA)?

- a. The IESBA Code applies only to members in public practice.
- b. The five fundamental principles of the IESBA Code are identical to the AICPA's principles of professional conduct.
- c. The IESBA Code contains specific standards addressing many of the same issues addressed in the AICPA Code of Professional Conduct.
- d. Only internal auditors need to follow the Code of Ethics set out by the IESBA.

ANSWER:

c

122. Which of the following is not a primary responsibility of the PCAOB regarding public companies in the United States?

Chapter 01

- a. Issuing CPA licenses to auditors who perform audits of public companies.
- b. Registering audit firms that audit public companies.
- c. Periodically inspecting registered audit firms.
- d. Investigating and disciplining registered audit firms for violations of relevant laws and professional standards.

ANSWER: a

123. Congress authorized which of the following organizations to establish generally accepted accounting principles?

- a. SEC.
- b. PCAOB.
- c. AICPA.
- d. FASB.

ANSWER: a

124. Mark Pulley is an auditor at Pulley and Hurst, LLC. If Pulley's five-year-old daughter owns shares of stock in McBurgers Corporation, then what is Pulley considered to have?

- a. A problem with competence.
- b. An indirect financial interest in the McBurgers Corporation.
- c. A loophole for claiming independence from McBurgers Corporation.
- d. A direct financial interest in McBurgers Corporation.

ANSWER: d

125. Which of the following employment positions could an auditor's spouse hold in a client without violating the independence requirements?

- a. Controller.
- b. Treasurer.
- c. Order entry staff.
- d. Internal audit director.

ANSWER: c

126. Julie Webb, CPA, takes out an automobile loan with First National Bank of Wellville (FNBW) while attending the University of Wellville. Julie graduates one year later and is hired as an auditor by Best and Driftwood, LLP. Her first assigned audit engagement is with First National Bank of Wellville, a client of Best and Driftwood. As a new audit assistant, Julie continues to pay her automobile loan payments each month. Which of the following best describes Julie's independence status?

- a. Impaired because Julie has a direct financial interest in FNBW.
- b. Impaired because Julie has a material indirect financial interest in FNBW.
- c. Not impaired because Julie has an immaterial indirect financial interest in FNBW.
- d. Not impaired because Julie is permitted to take normal loans from FNBW.

ANSWER: d

Chapter 01

127. Julie Webb, CPA takes out an automobile loan with First National Bank of Wellville (FNBW) while attending the University of Wellville. Julie graduates one year later and is hired as an auditor by Best and Driftwood, LLP. Her first assigned audit engagement is with First National Bank of Wellville, a client of Best and Driftwood. As a new audit assistant, Julie continues to pay her automobile loan payments each month. According to the AICPA, why is Julie is considered a covered member for FNBW independence purposes?

- a. She will be working on the engagement.
- b. She has a direct financial interest in FNBW.
- c. She graduated in the same geographical area as the client is operating.
- d. She has an immaterial direct financial interest in FNBW.

ANSWER:

a

128. Which of the following represents a situation in which an auditor is independent of its client?

- a. The audit fee paid by the client represents 5% of the auditor's annual gross revenue.
- b. The auditor takes a personal loan from the president of the company.
- c. The auditor's dependent son holds 25 shares of the client's common stock.
- d. The auditor has not received payment for the previous audit services.

ANSWER:

a

129. For which of the following engagements are members of the AICPA required to act with integrity and objectivity?

- a. Tax preparation.
- b. Financial statement review services.
- c. Financial statement audits.
- d. All engagements.

ANSWER:

d

130. Which of the following is not an aspect of Rule 201 of the General Standards of the Code of Professional Conduct?

- a. A member must not take on an engagement that is beyond the member's professional competence.
- b. A member must exercise duties prudently and professionally.
- c. A member must adequately plan and supervise the performance of professional services.
- d. A member firm must not advertise services to competing clients.

ANSWER:

d

131. A member of the AICPA must safeguard the confidentiality of client information. Which of the following is not a valid reason to disclose information to non-clients?

- a. To discuss information relating to inadequate disclosure in an audit report.
- b. To comply with a validly issued and enforceable subpoena or summons.
- c. To accommodate the review of client audit work papers under AICPA, PCAOB, or State Board of Accountancy authority.
- d. To explain to shareholders the likelihood that the company will not meet its earnings projections.

ANSWER:

d

Chapter 01

132. Which of the independence threats occur when the audit firm prepares source documents that are used to produce financial statements?

- a. Self-interest threat.
- b. Self-review threat.
- c. Advocacy threat.
- d. Familiarity threat.

ANSWER:

b

133. In which of the following situations would a CPA be considered independent?

- a. A CPA has obtained an auto loan from a banking client.
- b. A CPA has obtained a 90-day signature loan from a client.
- c. A CPA has obtained a loan for investment purposes from a client.
- d. A CPA has obtained an interest-free loan from a banking client.

ANSWER:

a

134. In which of the following situations would a CPA be considered independent?

- a. A CPA's brother is the Vice-President of Sales at the CPA's audit client.
- b. A CPA's father was a salesman at the CPA's audit client, and now a major portion of the father's pension fund is invested in the audit client.
- c. A CPA's cousin works as a web-site designer at the audit client.
- d. A CPA's son works summers at the audit client and has earned 10 shares of stock in the audit client.

ANSWER:

c

135. The auditor is normally not permitted to divulge confidential information obtained from a client. Which of the following situations would violate the confidentiality standard?

- a. To respond to the information request of a major shareholder.
- b. To respond to a quality review request of the state board of accountancy.
- c. To initiate a complaint with the AICPA's ethics division.
- d. To ensure adequate disclosure in accordance with GAAP.

ANSWER:

a

136. Which of the following factors is not included in the General Standards of the AICPA Code of Professional Conduct?

- a. Due professional care.
- b. Integrity and objectivity.
- c. Planning and supervision.
- d. Sufficient relevant data.

ANSWER:

b

137. Independence is always required for which of the following types of services?

Chapter 01

- a. Audit work.
- b. Tax work.
- c. Consulting.
- d. Risk advisory services.

ANSWER:

a

138. Independence in mental attitude is required of auditors on all audit engagements. Which statement best describes the highest goal for independence?

- a. To comply with the AICPA Code of Professional Conduct.
- b. To be independent in fact and appearance.
- c. To be an advocate for shareholders and other users of financial information.
- d. To comply with SEC regulations.

ANSWER:

b

139. Under the General Standards, what best describes how an AIPCA member should act?

- a. With professional competence.
- b. With due professional care.
- c. With adequate planning and with appropriate supervision.
- d. All of these.

ANSWER:

d

140. Commissions and referral fees are never permitted for which types of services?

- a. Tax services.
- b. Financial planning services.
- c. Audits.
- d. Both B and C.

ANSWER:

c

141. Auditors of public companies have additional requirements that extend beyond those of the AICPA. Which of the following is not one of those additional requirements?

- a. Preapproval of audit services and permissible nonaudit services by the client's audit committee.
- b. Disclosure by the client of all fees paid to its auditors for audit, audit-related, tax, and other services.
- c. Changing audit partners every seven years with a two-year cooling off period.
- d. Rotating lead audit partners every three years with a five-year cooling off period.

ANSWER:

d

142. Jean is an auditor of JKJ Company. Jean has been asked to represent JKJ in tax court. Which of the following threats to independence may occur if Jean agrees?

- a. Advocacy Threat.
- b. Self-review Threat.
- c. Adverse Interest Threat.

Chapter 01

- d. Familiarity Threat.

ANSWER:

a

143. Dean is an auditor of RST Company. Dean has been asked to fire the accounts receivable manager. Which of the following threats to independence may occur if Jean agrees?

- a. Advocacy Threat.
- b. Management Participation Threat.
- c. Adverse Interest Threat.
- d. Familiarity Threat.

ANSWER:

b

144. Simon's auditing firm has been providing assurance services to ABC Consulting for the past five years. What is the decision the auditing firm has to make before providing assurance services to ABC Consulting this year?

- a. Client acceptance decision.
- b. Client continuance decision.
- c. Client risk decision.
- d. Client-initiated decision.

ANSWER:

b

145. When assessing whether to continue with auditing a client, the accounting firm considers the integrity of the client's management.

The assessment of management integrity is an example of the a(n)

- a. Governance risk.
- b. Financial reporting risk.
- c. Quantitative risk factor.
- d. Independence risk factor.

ANSWER:

a

146. What does utilitarian theory hold?

- a. There is a decision that exists that is optimal for all people.
- b. What is ethical is the action that achieves the least bad for the greatest number of people.
- c. What is ethical is the action that achieves the greatest good for the greatest number of people.
- d. What is ethical is the action that achieves the greatest good for all people.

ANSWER:

c

147. An auditor who is professionally skeptical will do which of the following?

- a. Critically question contradictory audit evidence.
- b. Carefully evaluate the reliability of audit evidence, especially in situations in which fraud risk is high.
- c. Reasonably question the authenticity of documentation, while accepting that documents are to be considered genuine unless there is reason to believe the contrary.

Chapter 01

d. All of these.

ANSWER:

d

148. Which term best describes a situation in which an individual is morally or ethically required to do something that conflicts with his or her immediate self-interest?

- a. An ethical risk.
- b. An ethical problem.
- c. An ethical theory.
- d. An objectivity decision.

ANSWER:

a

149. Which of following is not part of the ethical framework derived from utilitarianism and rights theories?

- a. Determination of relevant legal issues.
- b. Determination of affected parties and their rights.
- c. Determination of the most important rights.
- d. Development of alternative courses of action.

ANSWER:

a

150. What is the purpose of an ethical framework?

- a. To provide a defined methodology to solve the ethical problem.
- b. To provide a defined methodology to aid the user in making complex ethical decisions.
- c. To provide a defined program to solve ethical dilemmas.
- d. To eliminate any risk associated with unethical decisions.

ANSWER:

b

151. According to the framework for ethical decision making, which of the following should the decision maker consider?

- a. Only the alternative course of action that is the easiest to implement.
- b. The consequences associated with possible actions.
- c. Whether the rights framework would cause any course of action to be added.
- d. All of these.

ANSWER:

b

152. As it relates to an audit, which of the following statements about professional skepticism is true?

- a. Professional skepticism is not taken into consideration.
- b. Professional skepticism relates only to the nature of procedures performed.
- c. Professional skepticism is an attitude.
- d. Professional skepticism is determined based upon the importance to a user of the financial statements.

ANSWER:

c

Chapter 01

153. Which of the following best describes a reason an audit firm might decide not to accept a company as a client?

- a. The company is in a weak financial position.
- b. The company culture does not match the audit firm culture.
- c. The company is part of an industry that tends to have volatile stock prices.
- d. The company has a subsidiary in another country.

ANSWER:

a

154. Which of the following is an important consideration in client acceptance and continuance decisions?

- a. Integrity of the client company's management.
- b. Effectiveness of the client company's internal controls.
- c. The audit firm's growth strategy.
- d. All of these.

ANSWER:

d

155. The scope of the work to be done by the auditor on the audit is described in which document?

- a. Contract letter.
- b. Engagement letter.
- c. Representation letter.
- d. Management letter.

ANSWER:

b

156. Which of the following describes an auditor exercising professional skepticism?

- a. Quickly collecting evidence.
- b. Relying on management's explanations.
- c. Jumping right to a conclusion before gathering all the evidence.
- d. Questioning trends that appear 'too good to be true'.

ANSWER:

d

157. What term is used to describe the process of ensuring data is correct, consistent, free of inappropriate anomalies?

- a. Data architecture.
- b. Data servicing.
- c. Data cleaning.
- d. Data science.

ANSWER:

c

158. In data analytics, what does validation of the data include?

- a. Evaluating the results.
- b. Gathering data from different sources.
- c. Cleaning the data.

Chapter 01

- d. Building the appropriate model.

ANSWER:

a

159. Which of the following phases of data analytics includes cleansing the data?

- a. Data Understanding.
- b. Exploratory Analysis.
- c. Validation.
- d. Data Preparation.

ANSWER:

d

160. Which of the following actions would occur during the visualization and presentation phase of the data analytics process framework?

- a. The auditor decides to prepare an executive summary summarizing the results.
- b. The auditor determines the scope of work and the type of analysis.
- c. The auditor builds and assesses the analytical model.
- d. The auditor reviews the process and determines the next steps.

ANSWER:

a

161. Which of the following actions is characteristic of cleaning data?

- a. Gaining insight from complex data.
- b. Collecting and organizing the data.
- c. Correctly categorizing the data.
- d. Ensuring the data is free of inappropriate anomalies.

ANSWER:

d

162. Which of the following accurately describes an engagement letter?

- a. Prepared by the client and presented to the audit firm at the beginning of the audit.
- b. Documents the conclusions of the auditor based on the work performed.
- c. Includes both the responsibilities of the auditor and of management.
- d. Identifies the work that was performed and the controls that were tested during the audit.

ANSWER:

c

163. Which of the following describes a test where auditors extract values from lists of numbers that do not possess decimal places following the whole number?

- a. Round-number test.
- b. Decimal place test.
- c. Data cleaning test.
- d. Whole number test.

ANSWER:

a

164. An auditor is preparing a data analytics test on sales. The auditor collects the data and, subsequently,

Chapter 01

performs a procedure to remove duplicate sales invoices. What is this procedure called?

- a. Organizing the data.
- b. Data visualization.
- c. Cleaning the data.
- d. Attacking the data.

ANSWER:

c

165. Which of the following phases of data analytics includes determining if the appropriate data is available?

- a. Data Understanding.
- b. Exploratory Analysis.
- c. Validation.
- d. Data Preparation.

ANSWER:

a

166. Users of financial statements

Identify at least three types of users of financial statements. Describe their primary use of the financial statements and how the misstatement of those statements might injure the user.

ANSWER:

Users and their uses of audited financial statements may include:

- Management uses the audit report to determine whether the financial statements are presented in accordance with GAAP, whether the firm is availing itself of appropriate internal controls, and as a means of evaluating employee performance. Misstatement of the financial statements would cause the client to make erroneous decisions about financial position, internal controls and employee rewards and punishments.
- A financial institution that is asked to make a loan uses the financial statements to judge the credit worthiness of the borrower. Misstatements in the financial statements lead to errors in lending that jeopardize the assets of the bank and depositors.
- A vendor who is asked to grant credit uses the statements and faces injury in a manner similar to the financial institution.
- A third-party stockholder uses the financial statements to determine if the investment will provide the returns consistent with the needs of the investor. Misstatements of the financial statements will lead to different results or possible loss of the investment.
- Others: Potential stockholders, taxing authorities, regulatory agencies, labor unions, employees, bondholders, court system, retirement plans, or retired employees

167. Overview of Financial Statement Audit

What is a financial statement audit, and what is the overall objective of the audit? What must the auditor do to accomplish this objective?

ANSWER:

A financial statement audit has been defined as a “systematic process of actively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users.”

Chapter 01

The overall objective of a financial statement audit is to obtain reasonable assurance about whether the financial statements are free from material misstatement and to report the auditor's findings. To accomplish this objective the auditor:

- (1) complies with relevant ethical and professional conduct requirements;
- (2) conducts the audit in accordance with professional auditing standards;
- (3) exercises professional judgment, professional skepticism, and critical thinking;
- (4) obtains sufficient appropriate evidence, through a structured process, as a basis for the auditor's opinion on the financial statements.

168. The Need for Audited Financial Statements

Why do financial statement users need independent assurance about information provided by management?

ANSWER: The need for independent assurance arises from several factors:

Potential bias—Management has incentives to bias financial information in order to convey a better impression of the financial data than real circumstances might merit. For example, management's compensation may be tied to profitability or stock price, so managers may be tempted to "bend" GAAP to make the organization's performance look better.

Remoteness—An organization and the users of its financial information are often remote from each other, both in terms of geographic distance and the extent of information available to the both parties. Most users cannot interview management, tour a company's plant, or review its financial records firsthand; instead, they must rely on financial statements to communicate the results of management's performance. These factors can tempt management to keep information from users or bend GAAP so the organization looks better.

Complexity—Transactions, information, and processing systems are often very complex, so it can be difficult to determine their proper presentation. This factor provides an opportunity for management to mislead users.

Consequences—When financial information is not reliable, investors and other users lose a significant source of information that they need to make decisions that have important consequences. Without reliable financial information, users may invest in securities or may lend money to a company that is committing fraud and, once the fraud is revealed, users are in a position of losing significant amounts of money.

169. Audit Quality

What is audit quality?

ANSWER: One definition describes a quality audit as one performed "in accordance with generally accepted auditing standards (GAAS) to provide reasonable assurance that the audited financial statements and related disclosures are (1) presented in accordance with generally accepted accounting principles (GAAP) and (2) are not materially misstated whether due to errors or fraud."

170. Audit Quality Drivers

What are the primary drivers of audit quality according to the Financial Reporting Council's (FRC) "Audit Quality Framework?"

ANSWER: There are five primary drivers of audit quality, including (1) audit firm culture, (2) the skills and personal qualities of audit partners and staff, (3) the effectiveness of the audit process, (4) the reliability and usefulness of audit reporting, and (5) factors outside the control of auditors that affect audit quality.

171. Professional and regulatory organizations

Chapter 01

Identify at least four professional or regulatory organizations that affect the auditing profession. Explain how and why they assist and/or monitor the auditing profession.

ANSWER: **Public Company Accounting Oversight Board (PCAOB)** is a private sector, nonprofit organization that oversees auditors of public companies. Its primary four responsibilities include: 1) registering audit firms that audit public companies, 2) periodically inspecting registered audit firms, 3) establishing auditing and related standards for registered audit firms, and 4) investigating and disciplining registered audit firms that violate relevant laws or standards.

American Institute of Certified Public Accountants (AICPA) With the establishment of the PCAOB, the role of the AICPA has diminished. The AICPA establishes standards for audits of nonpublic companies and for other attestation services, accounting and review services, consulting, and tax services. It oversees a peer review program, organizes continuing education programs, and administers the Uniform CPA Examination.

State Boards of Accountancy license CPAs and are charged with regulating the profession at the state level.

Securities and Exchange Commission (SEC) has been granted authority to establish GAAP for publicly traded companies. Its primary mission is to protect the investing public; it has oversight of the PCAOB and all public companies traded on U.S. stock exchanges.

Financial Accounting Standards Board (FASB) is responsible for establishing generally accepted accounting principles (GAAP).

172. Professional Decision Making

To achieve audit quality, auditors must make quality decisions throughout the audit process. What are the characteristics of quality audit decisions?

ANSWER: Quality decisions by auditors are unbiased, meet the expectations of reasonable users, comply with professional standards, and incorporate sufficient appropriate evidence to justify the decisions made by the auditors.