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CPA Auditing and Attestation Exam

AICPA AUD

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Topic Break Down

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QUESTION NO: 1

The monitoring component of internal control excludes:

A. Assessing information derived from external parties.

B. Assessing the quality of internal control performance over time.

C. Improving controls that are not operating effectively.

D. Eliminating controls that are not operating effectively.

ANSWER: D

Explanation:

Eliminating controls that are not operating effectively is excluded because monitoring is designed to evaluate whether internal control components and relevant controls continue to be present and functioning, identify deficiencies, communicate those deficiencies to responsible parties, and support corrective action. The purpose is to maintain or enhance the system's ability to provide reasonable assurance that organizational objectives are achieved. Corrective action normally involves remediating a deficiency, modifying the design of a control, replacing it with an effective alternative, or otherwise restoring the control environment to an effective condition. Simply eliminating an ineffective control, without establishing an appropriate replacement or redesigned control to address the underlying risk, does not itself represent the monitoring activity contemplated by an internal-control framework. COSO describes monitoring activities as ongoing evaluations, separate evaluations, or a combination of both, used to ascertain whether internal-control components are functioning. Auditing standards likewise require an understanding of how an entity monitors internal control and remediates identified deficiencies. See the COSO Internal Control—Integrated Framework executive summary and Sarbanes-Oxley Act section 404.

QUESTION NO: 2

Which of the following expressions most likely would be included in a management representation letter?

A. No events have occurred subsequent to the balance sheet date that require adjustment to, or disclosure in, the financial statements.

B. There are no significant deficiencies in internal control identified during the prior-year's audit of which those charged with governance are unaware.

C. We do not intend to provide any information that may be construed to constitute a waiver of the attorney-client privilege.

D. Certain computer files and other required audit evidence may exist only for a short period of time and only in computer-readable form.

ANSWER: A

Explanation:

"No events have occurred subsequent to the balance sheet date that require adjustment to, or disclosure in, the financial statements." is appropriately included in a written management representation letter. In a financial statement audit, management is responsible for identifying events occurring after the financial statement date and through the date of the auditor's report that may require recognition in the statements or disclosure in the notes. The auditor obtains management's written representation to support the audit evidence obtained regarding this responsibility and management's conclusion about subsequent events. This representation is normally dated as of the auditor's report date, because it addresses the period through that date and helps confirm that management has communicated relevant information arising after year-end. The representation is not a substitute for the auditor's subsequent-events procedures; rather, it complements those procedures by formally documenting management's acknowledgment and assertions. The PCAOB's management-representation standard specifically includes a representation that subsequent events requiring adjustment or disclosure have been appropriately addressed. See PCAOB AS 2805, Management Representations. The related framework for evaluating post-balance-sheet events is described in PCAOB AU 561, Subsequent Discovery of Facts Existing at the Date of the Auditor's Report.

QUESTION NO: 3

An auditor would most likely verify the interest earned on bond investments by:

A. Vouching the receipt and deposit of interest checks.

B. Confirming the bond interest rate with the issuer of the bonds.

C. Recomputing the interest earned on the basis of face amount, interest rate, and period held.

D. Testing the internal controls over cash receipts.

ANSWER: C

Explanation:

Recomputing the interest earned on the basis of face amount, interest rate, and period held is the most appropriate procedure because interest revenue on a bond investment is generally determinable through an independent calculation. The auditor can use the bond's stated or effective interest rate, its principal or carrying amount as applicable, and the precise period during which the entity held the investment to calculate the amount of interest that should have been recognized. This directly tests the recorded interest income assertion, including interest accrued at period-end but not yet collected in cash. The auditor should obtain reliable evidence supporting the calculation inputs, such as the investment agreement or broker/custodian records for the bond terms and ownership period, then compare the independently calculated amount with the client's recorded income. This is a substantive analytical/detail procedure that produces persuasive audit evidence because it is based on objective contractual terms and mathematical accuracy. AU-C section 500 recognizes recalculation as an audit procedure involving checking the mathematical accuracy of documents or records. The AICPA's auditing standards and related resources are available at AICPA Audit and Attest Standards, and the applicable evidence concepts are addressed in ISA 500, Audit Evidence.

QUESTION NO: 4

Which of the following internal controls most likely would be used to maintain accurate inventory records?

A. Perpetual inventory records are periodically compared with the current cost of individual inventory items.

B. A just-in-time inventory ordering system keeps inventory levels to a desired minimum.

C. Requisitions, receiving reports, and purchase orders are independently matched before payment is approved.

D. Periodic inventory counts are used to adjust the perpetual inventory records.

ANSWER: D

Explanation:

Periodic inventory counts are used to adjust the perpetual inventory records is correct because a perpetual inventory system records receipts, sales, returns, and other inventory movements continuously, but it can still develop discrepancies from recording errors, unrecorded transactions, damage, theft, spoilage, or misplaced goods. A physical count provides independent evidence of the quantities actually on hand. Comparing those count results with the perpetual records identifies differences that must be investigated and corrected, allowing the entity's recorded inventory quantities to remain reliable. This control is especially important when inventory records support both financial reporting and operational decisions, such as purchasing and production planning. Sound inventory-count procedures ordinarily include appropriate count instructions, segregation of inventory movement during the count or controls over such movement, review of count discrepancies, and timely adjustment of the perpetual records based on validated count results. The AICPA's auditing standards require auditors to attend physical inventory counting when inventory is material, when practicable, to evaluate management's count procedures and obtain evidence about the existence and condition of inventory. This audit emphasis reflects the importance of physical counts as a control and corroborative measure for inventory records. See AICPA Clarified Statements on Auditing Standards and PCAOB AU 331, Inventories.

QUESTION NO: 5

Which of the following factors most likely would lead a CPA to conclude that a potential audit engagement should be rejected?

A. The details of most recorded transactions are not available after a specified period of time.

B. Internal control activities requiring the segregation of duties are subject to management override.

C. It is unlikely that sufficient appropriate evidence is available to support an opinion on the financial statements.

D. Management has a reputation for consulting with several accounting firms about significant accounting issues.

ANSWER: C

Explanation:

It is unlikely that sufficient appropriate evidence is available to support an opinion on the financial statements. is correct because a CPA should accept or continue an audit engagement only when the auditor expects to be able to obtain the evidence needed to support the audit opinion. Before accepting an engagement, the auditor evaluates whether the preconditions for an audit are present, including whether management will provide access to information, persons, and records relevant to preparing and auditing the financial statements. If circumstances indicate that sufficient appropriate audit evidence will probably not be obtainable, the auditor would be unable to reduce audit risk to an acceptably low level or form a properly supported opinion. Accepting under those conditions could result in a scope limitation that prevents the CPA from completing an audit in accordance with generally accepted auditing standards. Accordingly, when the likely lack of evidence is apparent before acceptance, rejecting the prospective engagement is the appropriate conclusion rather than proceeding with an engagement that cannot support a valid audit report. This is consistent with AU-C 210, which addresses agreeing to the terms of audit engagements and requires the auditor to determine whether the preconditions for an audit are present. See AICPA AU-C 210, Agreeing Upon the Terms of Audit Engagements and ISA 210, Agreeing the Terms of Audit Engagements.

QUESTION NO: 6

Before accepting an audit engagement, a successor auditor should request that the prospective client authorize the predecessor auditor to respond fully to the successor auditor's inquiries. If the prospective client refuses to provide this authorization, the successor auditor ordinarily should:

A. Decline the engagement.

B. Accept the engagement after obtaining a representation from management.

C. Accept the engagement if the entity's internal control appears effective.

D. Issue a disclaimer of opinion after completing the audit.

ANSWER: A

Explanation:

A prospective client's refusal to authorize communication with the predecessor auditor raises questions about management's integrity and may prevent the successor auditor from obtaining information relevant to engagement acceptance. The successor auditor should inquire into the reasons for the refusal and ordinarily should decline the engagement when authorization is not provided. Communication with the predecessor auditor is an important acceptance procedure, particularly when it may reveal disagreements with management, fraud concerns, or other significant matters. See AU-C Section 210, Terms of Engagement.

QUESTION NO: 7

In evaluating the reasonableness of an entity's accounting estimates, an auditor normally would be concerned about assumptions that are:

A. Susceptible to bias.

B. Consistent with prior periods.

C. Insensitive to variations.

D. Similar to industry guidelines.

ANSWER: A

Explanation:

Susceptible to bias. is correct because accounting estimates inherently involve judgment, including management's selection of assumptions and data. An auditor must evaluate whether those assumptions are reasonable in light of the applicable financial reporting framework, information available when the estimate was made, and the entity's objectives and circumstances. Assumptions susceptible to bias warrant particular attention because management may, consciously or unconsciously, select assumptions that systematically produce a preferred reported outcome, such as higher earnings, lower expenses, or reduced liabilities.

Under AU-C section 540, the auditor is required to evaluate whether management's judgments in making accounting estimates provide indicators of possible management bias. The presence of bias does not by itself establish a misstatement or fraud; however, it increases the risk that an estimate is not reasonable and that the financial statements may be materially misstated. The auditor responds through procedures such as testing the data used, assessing the method and significant assumptions, considering contrary evidence, reviewing outcomes of prior estimates, and, when appropriate, developing an auditor's point estimate or range. See AICPA Clarified Statements on Auditing Standards and PCAOB AS 2501, Auditing Accounting Estimates.

QUESTION NO: 8

An auditor's risk assessment is based on the assumption that controls are operating effectively. Which of the following was not a step in making this assessment?

A. Evaluate the effectiveness of the internal controls with tests of controls.

B. Obtain an understanding of the entity's accounting system and control environment.

C. Perform tests of details of transactions to detect material misstatements in the financial statements.

D. Consider whether control activities can have a pervasive effect on financial statement assertions.

ANSWER: C

Explanation:

Perform tests of details of transactions to detect material misstatements in the financial statements is correct because tests of details are substantive procedures designed to detect material misstatements directly. They are ordinarily performed in response to assessed risks, rather than being a procedure used to establish the basis for an expectation that relevant controls are operating effectively. When the auditor plans to rely on controls and assesses control risk below the maximum level, the auditor obtains an understanding of the relevant components of internal control, identifies controls relevant to the assertions, and evaluates the design and implementation of those controls. The auditor then obtains sufficient appropriate audit evidence about operating effectiveness through tests of controls. This evidence supports the planned reliance on controls and affects the nature, timing, and extent of substantive procedures. The risk-assessment process also considers controls that may affect multiple financial-statement assertions broadly, since entity-level and pervasive controls can influence the effectiveness of other controls. Under AU-C section 330, substantive procedures—including tests of details—must be designed and performed in response to assessed risks of material misstatement; thus, they are not themselves a step in making the control-reliance assessment. See AICPA AU-C section 330, Performing Audit Procedures in Response to Assessed Risks and AICPA AU-C section 315, Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement.

QUESTION NO: 9

Which of the following procedures would yield the most reliable evidence?

A. A scanning of trial balances.

B. An inquiry of client personnel.

C. A comparison of beginning and ending retained earnings.

D. A recalculation of bad debt expense.

ANSWER: D

Explanation:

A recalculation of bad debt expense would yield the most reliable evidence because it is obtained directly by the auditor through independently checking the mathematical accuracy of the client's calculation. The auditor can obtain the underlying accounts-receivable aging, applicable estimated loss rates, write-off data, and the client's methodology, then recompute the expense and allowance amount. This creates evidence based on the auditor's own work rather than solely on information or representations supplied by client personnel.

Audit-evidence reliability is affected by its source and nature. Evidence obtained directly by the auditor, including inspection, observation, confirmation, and recalculation, is generally more reliable than evidence obtained indirectly. Recalculation is particularly persuasive for testing the accuracy of computations because it enables the auditor to independently verify the mathematical application of the entity's established assumptions and data. If the procedure also includes evaluating whether the assumptions used are reasonable, it can contribute evidence relevant to both the accuracy of the calculation and the reasonableness of the resulting estimate.

This treatment is consistent with the audit-evidence principles in PCAOB AS 1105, Audit Evidence and the AICPA's auditing standards resources.

QUESTION NO: 10

An auditor is selecting vouchers for testing an entity's internal control activities related to the proper approval of vouchers before checks are prepared. The auditor is matching random numbers with voucher numbers to determine which vouchers to inspect. If a random number matches a voided voucher, that voucher ordinarily would be replaced by another voucher in the random sample if the voided voucher:

A. Cannot be located in the voucher file.

B. Represents a dollar amount that is material.

C. Indicates a deviation from the prescribed activity.

D. Has been properly voided.

ANSWER: D

Explanation:

Has been properly voided. is correct because the auditor's objective is to test the operating effectiveness of the control requiring voucher approval before checks are prepared. A voucher that was properly voided is not an item for which a check should have been prepared or payment processing should have continued. Therefore, it is outside the population of transactions relevant to testing whether vouchers were properly approved before check preparation. In statistical or random sampling, an item that is properly excluded from the relevant population ordinarily is replaced so the auditor can examine the planned number of applicable sample items and obtain sufficient appropriate evidence about the control's operation.

The auditor should first inspect the voided voucher and related documentation to establish that the void was authorized and properly processed. Proper voiding supports the conclusion that the item does not represent an instance requiring testing of the approval-before-payment control. The replacement item should be selected in a manner consistent with the original random-selection approach so that the sample continues to provide evidence representative of the population being tested. This treatment is consistent with audit sampling principles requiring the auditor to define a population appropriate to the specific audit objective and evaluate sampled items in relation to that population. See PCAOB AU 350, Audit Sampling and AICPA Clarified Statements on Auditing Standards.

QUESTION NO: 11

When an accountant examines a financial forecast that fails to disclose several significant assumptions used to prepare the forecast, the accountant should describe the assumptions in the accountant's report and issue a (an):

A. "Except for" qualified opinion.

B. "Subject to" qualified opinion.

C. Unqualified opinion with a separate explanatory paragraph.

D. Adverse opinion.

ANSWER: D

Explanation:

An **Adverse opinion.** is appropriate because the significant assumptions underlying a financial forecast are fundamental to users' understanding of the forecast and the basis on which projected results were developed. A forecast is not simply a set of anticipated financial statements; it also communicates management's assumptions about future conditions and planned actions. Without disclosure of several significant assumptions, users cannot properly evaluate the forecast's reasonableness, limitations, or sensitivity to changes in those assumptions.

In an examination engagement on prospective financial information, the accountant evaluates whether the forecast is presented in conformity with applicable AICPA presentation guidelines. When departures from those guidelines are material and pervasive to the presentation, an adverse opinion is required. The omission of several significant assumptions is pervasive because those assumptions affect the framework for interpreting the forecast as a whole, rather than being confined to a limited item or disclosure. The report should identify and describe the omitted assumptions in the basis-for-adverse-opinion discussion so users understand the nature and significance of the departure. The applicable attestation standards and professional literature are available through the AICPA Attestation Standards and the AICPA Professional Standards resources.

QUESTION NO: 12

The quarterly data required by SEC Regulation S-K have been omitted. Which of the following statements must be included in the auditor's report?

A. The auditor was unable to review the data.

B. The company's internal control provides an adequate basis to complete the review.

C. The company has not presented the selected quarterly financial data.

D. The auditor will review the selected data during the review of the subsequent quarterly financial data.

ANSWER: C

Explanation:

The company has not presented the selected quarterly financial data. This is the required disclosure when selected quarterly financial data that are required to accompany the audited annual financial statements have been omitted. The auditor's report must explicitly alert financial-statement users to the omission, rather than implying that procedures were attempted or that a future review will resolve the matter. The statement identifies the missing information as selected quarterly financial data and makes clear that the company, not the auditor, did not present it. This reporting treatment is addressed in PCAOB Auditing Standard 2710, which covers information accompanying audited financial statements in SEC filings and prescribes an explanatory report paragraph when required selected quarterly data are omitted. See PCAOB AS 2710, Other Information in Documents Containing Audited Financial Statements. Although the SEC later eliminated the former Item 302(a) requirement for selected quarterly financial data for many filings, the question expressly assumes that Regulation S-K requires the data. Under that stated assumption, the auditor must communicate their nonpresentation in the auditor's report. The SEC's amendments eliminating the former requirement are available in SEC Release No. 33-10890.

QUESTION NO: 13

Under which of the following circumstances would the use of the blank form of confirmations of accounts receivable most likely be preferable to positive confirmations?

A. The recipients are likely to sign the confirmations without devoting proper attention to them.

B. Subsequent cash receipts are unusually difficult to verify.

C. Analytical procedures indicate that few exceptions are expected.

D. The combined assessed level of inherent risk and control risk is low.

ANSWER: A

Explanation:

The recipients are likely to sign the confirmations without devoting proper attention to them. A blank confirmation does not state the customer's recorded accounts-receivable balance; instead, it asks the customer to supply the amount owed or other requested information. This requires the respondent to independently retrieve and consider its records before replying. Consequently, it provides stronger evidence about the existence and accuracy of the receivable when there is a meaningful risk that a customer may mechanically sign a stated-balance confirmation without noticing an error. A standard positive confirmation requires a response indicating agreement or disagreement with an amount already printed by the auditor. Although positive confirmations ordinarily provide persuasive external audit evidence, their reliability is reduced if recipients are expected to respond carelessly. The blank format directly addresses that concern by increasing the respondent's required level of attention and reducing the possibility that an incorrect stated balance is simply accepted without review. Audit standards require auditors to consider the reliability of confirmation responses and recognize that the form of confirmation request can affect the quality of evidence obtained. See PCAOB AS 330, The Confirmation Process and AICPA AU-C 505, External Confirmations.

QUESTION NO: 14

Which of the following characteristics most likely would be an advantage of using classical variables sampling rather than probability-proportional-to-size (PPS) sampling?

A. The selection of negative balances requires no special design considerations.

B. The sampling process can begin before the complete population is available.

C. The auditor need not consider the preliminary judgments about materiality.

D. The sample will result in a smaller sample size if few errors are expected.

ANSWER: A

Explanation:

The selection of negative balances requires no special design considerations is correct because classical variables sampling treats the recorded value of each population item as the audit variable and can accommodate debit, credit, positive, and negative values within an appropriately designed statistical evaluation. The auditor estimates the population's misstatement using classical statistical methods, such as mean-per-unit or difference estimation, and evaluates the sampling result in relation to tolerable misstatement. Thus, a population containing negative balances does not inherently prevent use of the method or require a separate supplemental selection approach merely because those balances are negative.

In contrast, PPS sampling selects individual monetary units with probability related to their recorded amounts. Its usual design presumes positive book-value monetary units; negative or zero balances therefore require special treatment in defining the sampling population and selection approach. This makes classical variables sampling particularly useful when negative balances are a meaningful feature of the population. Audit-sampling standards require the auditor to design a sample that can support conclusions about the population and to evaluate the results in light of the sampling method selected. See PCAOB AU 350, Audit Sampling and the GAO Financial Audit Manual.

QUESTION NO: 15

Which of the following procedures would an auditor most likely perform in searching for unrecorded liabilities?

A. Vouch a sample of accounts payable entries recorded just before year-end to the unmatched receiving report file.

B. Compare a sample of purchase orders issued just after year-end with the year-end accounts payable trial balance.

C. Vouch a sample of cash disbursements recorded just after year-end to receiving reports and vendor invoices.

D. Scan the cash disbursements entries recorded just before year-end for indications of unusual transactions.

ANSWER: C

Explanation:

"Vouch a sample of cash disbursements recorded just after year-end to receiving reports and vendor invoices" is the appropriate procedure because the primary audit objective in searching for unrecorded liabilities is completeness. An entity may receive goods or services before the balance-sheet date but fail to record the related accounts payable liability until the vendor is paid in the following period. Reviewing subsequent cash disbursements identifies payments made shortly after year-end, and tracing those payments to vendor invoices and receiving reports allows the auditor to determine when the underlying goods were received or services were provided. If the supporting documentation shows that the obligation existed on or before year-end, the entity should have accrued or recorded the liability in its year-end financial statements. This subsequent-disbursements testing provides persuasive evidence about liabilities that existed at year-end but were omitted from the accounts payable listing. The approach is consistent with the auditor's responsibility to obtain sufficient appropriate evidence regarding account balances and to design procedures responsive to the risk of material misstatement, including misstatements caused by incomplete recording of obligations. See the AICPA's clarified auditing standards resources and the PCAOB's AS 2301, The Auditor's Responses to the Risks of Material Misstatement.

QUESTION NO: 16

When management's assertion about the effectiveness of a nonissuer's internal control is presented in a representation letter that will not accompany the CPA's report:

A. Use of the report is restricted to management and the board of directors.

B. The report should contain a statement of management's assertion.

C. The CPA should not accept the engagement.

D. The report should include a negative assurance with respect to the effectiveness of the entity's internal control.

ANSWER: B

Explanation:

The report should contain a statement of management's assertion. In an attestation engagement addressing a nonissuer's internal control effectiveness, management is responsible for evaluating the controls against suitable criteria and making a written assertion about that evaluation. The CPA's report ordinarily identifies management's assertion because it establishes the subject matter and clarifies the respective responsibilities of management and the practitioner. When the written assertion is contained in a representation letter but is not included with, or otherwise does not accompany, the CPA's report, report users would not have access to that essential statement from management. Accordingly, the CPA incorporates a statement of management's assertion into the report itself. This reporting presentation preserves the necessary context for the practitioner's conclusion and makes clear that the conclusion is expressed on management's assertion, rather than representing a management-free certification of internal control. The requirement is part of the AICPA attestation reporting framework for engagements on an entity's internal control. The AICPA's auditing and attestation standards resources are available at AICPA Auditing Standards, and the applicable attestation standards are cataloged through AICPA Attestation Standards.

QUESTION NO: 17

An auditor uses the knowledge provided by the understanding of internal control and the final assessed risk of material misstatement primarily to determine the nature, timing, and extent of the:

A. Attribute tests.

B. Compliance tests.

C. Tests of controls.

D. Substantive tests.

ANSWER: D

Explanation:

Substantive tests are correct because the auditor's assessed risks of material misstatement directly drive the overall audit response and the design of further audit procedures. After obtaining an understanding of internal control and assessing inherent and control risks, the auditor determines the nature of substantive procedures to obtain appropriate evidence, such as selecting tests of details, analytical procedures, or a combination. The risk assessment also affects timing: higher-risk assertions may require work closer to year-end rather than at an interim date. It affects extent as well, because greater assessed risk generally calls for more persuasive audit evidence, often achieved through larger samples, more extensive procedures, or procedures that provide stronger evidence. This risk-responsive approach helps the auditor reduce audit risk to an acceptably low level and obtain sufficient appropriate audit evidence supporting the opinion. AU-C section 330 requires the auditor to design and perform further audit procedures whose nature, timing, and extent are based on, and responsive to, the assessed risks of material misstatement. See AICPA Clarified Statements on Auditing Standards and PCAOB AS 2301, The Auditor's Responses to the Risks of Material Misstatement.

QUESTION NO: 18

This question will represent a statement, question, excerpt, or comment taken from various parts of an auditor's documentation file. Letter choices A-P represent a list of the likely sources of the statement, question, excerpt, or comment. Select, as the best answer for each item, the most likely source. Select only one source for each item. During our audit we discovered evidence of the company's failure to safeguard inventory from loss, damage, and misappropriation.

A. Practitioner's report on management's assertion about an entity's compliance with specified requirements.

B. Auditor's communications on significant deficiencies in internal control.

C. Audit inquiry letter to legal counsel.

D. Lawyer's response to audit inquiry letter.

E. Communication from those charged with governance to the auditor.

F. Auditor's communication to those charged with governance (other than with respect to significant deficiencies in internal control).

G. Report on the application of accounting principles.

H. Auditor's engagement letter.

I. Letter for underwriters.

J. Accounts receivable confirmation request.

K. Request for bank cutoff statement.

L. Explanatory paragraph of an auditor's report on financial statements.

M. Partner's engagement review notes.

N. Management representation letter.

O. Successor auditor's communication with predecessor auditor.

P. Predecessor auditor's communication with successor auditor.

ANSWER: B

Explanation:

“Auditor's communications on significant deficiencies in internal control.” is the most likely source because the observation identifies a control problem involving the protection of a financial-statement asset. Safeguarding inventory from loss, damage, and misappropriation is an important component of internal control: controls should provide reasonable assurance that inventory is protected and that inventory balances and related costs can be reliably reported. Evidence that the company has failed to safeguard inventory indicates that a deficiency exists in the design or operation of controls.

Under AU-C section 265, the auditor evaluates control deficiencies identified during the audit and communicates, in writing, significant deficiencies and material weaknesses to those charged with governance. A significant deficiency is important enough to merit the attention of those charged with governance because it could adversely affect the entity’s ability to initiate, authorize, record, process, or report financial information reliably. The quoted language is therefore characteristic of the factual description of a deficiency included in the auditor’s internal-control communication, along with its potential effect and recommendations or management responses where applicable. See AICPA AU-C Section 265, Communicating Internal Control Related Matters Identified in an Audit and the AICPA overview of clarified auditing standards.

QUESTION NO: 19

An auditor of a nonpublic company must conduct the audit in accordance with:

I. ASB standards.

II. PCAOB standards.

A. I.

B. Both I and II.

C. Either I or II, but not both.

D. II.

E. ASB standards.
II. PCAOB standards.

ANSWER: A

Explanation:

I. is correct because financial-statement audits of nonpublic entities are generally performed under generally accepted auditing standards issued by the AICPA Auditing Standards Board. These standards are codified in the AICPA’s Statements on Auditing Standards and the AU-C sections. They establish the auditor’s responsibilities for planning and performing the audit, obtaining sufficient appropriate audit evidence, evaluating misstatements, communicating with those charged with governance, and reporting on the financial statements. AU-C section 200 describes the overall objectives of the independent auditor and states that the auditor must comply with relevant ethical requirements and plan and perform the audit with professional skepticism in accordance with GAAS. Accordingly, an auditor engaged to audit a nonpublic company’s financial statements uses the ASB’s GAAS framework as the governing auditing standards. The AICPA identifies its clarified SASs and related auditing standards as the standards applicable to these nonissuer engagements. See the AICPA’s clarified Statements on Auditing Standards resources and AU-C section 200.

QUESTION NO: 20

Which of the following procedures most likely would not be included in a review engagement of a nonissuer?

A. Obtaining a management representation letter.

B. Considering whether the financial statements conform with GAAP.

C. Assessing control risk.

D. Inquiring about subsequent events.

ANSWER: C

Explanation:

Assessing control risk is the procedure most likely not included in a review engagement of a nonissuer. Under SSARS, a review is designed to provide limited assurance that the accountant is not aware of any material modifications needed for the financial statements to conform with the applicable financial reporting framework. The accountant performs primarily inquiry and analytical procedures, obtains appropriate representations from management, and considers matters such as subsequent events and financial-statement presentation. The engagement does not require the accountant to obtain an understanding of internal control, test controls, or assess control risk. Those procedures are associated with an audit, in which the auditor obtains reasonable assurance and plans further audit procedures in response to assessed risks of material misstatement. Although an accountant performing a review may become aware of control-related matters through inquiries or other work, this does not constitute a formal control-risk assessment. The review report's limited-assurance conclusion reflects the substantially narrower scope of a review compared with an audit. See the AICPA's Compilation and Review Services overview and the SSARS resources for guidance on review engagements.

QUESTION NO: 21

An auditor is required to establish an understanding with a client regarding the services to be performed for each engagement. This understanding generally includes:

A. The auditor's responsibility for determining the preliminary judgments about materiality and audit risk factors.

B. Management's responsibility for identifying mitigating factors when the auditor has doubt about the entity's ability to continue as a going concern.

C. The auditor's responsibility for ensuring that those charged with governance are aware of any significant deficiencies in internal control that come to the auditor's attention.

D. Management's responsibility for providing the auditor with an assessment of the risk of material misstatement due to fraud.

ANSWER: C

Explanation:

The auditor's responsibility for ensuring that those charged with governance are aware of any significant deficiencies in internal control that come to the auditor's attention is correct. Under AU-C section 210, the auditor must agree on the terms of the audit engagement with management or those charged with governance, as appropriate. The agreed understanding addresses the respective responsibilities of the auditor and management, normally through an engagement letter or other suitable written agreement.

An auditor's responsibilities described in the engagement terms include conducting the audit under generally accepted auditing standards and communicating applicable internal-control matters identified during the audit. AU-C section 265 requires the auditor to communicate significant deficiencies and material weaknesses in internal control identified in an audit to management and those charged with governance. Accordingly, informing those charged with governance about significant deficiencies that come to the auditor's attention is an auditor responsibility that appropriately forms part of the engagement understanding. This communication supports governance oversight and clarifies the nature and limits of the audit engagement from its outset.

See the AICPA's Professional Standards resource, including AU-C sections 210 and 265, and the AICPA's overview of clarified auditing standards.

QUESTION NO: 22

Internal control is relevant to:

A. An entire entity.

B. An entity's operating units.

C. An entity's business functions.

D. All of the above.

ANSWER: D

Explanation:

“All of the above.” is correct because internal control is an entity-wide process, not a process confined to one organizational level or department. It encompasses the full entity, including governance and management activities, individual operating units such as divisions or locations, and business functions such as finance, purchasing, production, human resources, and information technology. Controls may be designed and implemented centrally, locally within a particular operating unit, or within a function that serves multiple units. Together, these controls support the entity’s objectives concerning operations, reporting, and compliance.

For an audit of financial statements, the auditor obtains an understanding of the aspects of the entity’s system of internal control that are relevant to identifying and assessing risks of material misstatement. That understanding can include controls operating at the entity level as well as transaction-processing and information-system controls within operating units and functional areas. The COSO Internal Control—Integrated Framework similarly describes internal control as a process effected by an entity’s board, management, and other personnel, emphasizing that it permeates the organization rather than residing in a single component. See the COSO internal control guidance and the AICPA clarified auditing standards.

QUESTION NO: 23

An attest engagement is one in which a CPA is engaged to:

A. Issue an examination, a review, or an agreed-upon procedures report on subject matter, or on an assertion about the subject matter, that is the responsibility of another party.

B. Provide tax advice or prepare a tax return based on financial information the CPA has not audited or reviewed.

C. Testify as an expert witness in accounting, auditing, or tax matters, given certain stipulated facts.

D. Assemble the financial statements of a nonissuer based on the assumptions of the entity's management without expressing any assurance.

ANSWER: A

Explanation:

“Issue an examination, a review, or an agreed-upon procedures report on subject matter, or on an assertion about the subject matter, that is the responsibility of another party.” is correct because it states the essential scope of an attest engagement under the AICPA’s attestation standards. In such an engagement, the practitioner is engaged to report on identified subject matter or on a responsible party’s assertion concerning that subject matter. The responsible party, rather than the practitioner, is accountable for the underlying subject matter and, when applicable, for making the assertion. The CPA’s role is to apply appropriate attestation procedures and issue a report in the form required for the particular service: an examination, review, or agreed-upon procedures engagement. This framework permits attestation services to address matters beyond historical financial statements, such as compliance, internal control, prospective information, or other measurable or evaluable subject matter, provided the applicable attestation requirements are met. The wording correctly identifies both the permitted report types and the fundamental requirement that the subject matter or assertion is another party’s responsibility. The AICPA’s audit and attest standards resources provide the professional framework for these engagements, including the Statements on Standards for Attestation Engagements. See the AICPA Audit and Attest Standards resources and the AICPA Assurance Services resources.

QUESTION NO: 24

This question presents independent factual situations an auditor might encounter in conducting an audit. List A represents the types of opinions the auditor ordinarily would issue. Select as the best answer for this item, the action the auditor normally would take. The types of opinions in List A may be selected once, more than once, or not at all.

Assume:

• The auditor is independent.

• The auditor previously expressed an unqualified opinion on the prior year's financial statements.

• Only single-year (not comparative) statements are presented for the current year.

• The conditions for an unqualified opinion exist unless contradicted in the factual situations.

• The conditions stated in the factual situations are material.

• No report modifications are to be made except in response to the factual situation.

Item to Be Answered

An entity discloses in the notes to the financial statements certain lease obligations. The auditor believes that the failure to capitalize these leases is a departure from generally accepted accounting principles.

List A

Types of Options

A. An "except for" qualified opinion.

B. An unqualified opinion.

C. An adverse opinion.

D. A disclaimer of opinion.

E. Either an "except for" qualified opinion or an adverse opinion.

F. Either a disclaimer of opinion or an "except for" qualified opinion.

G. Either an adverse opinion or a disclaimer of opinion.

ANSWER: A

Explanation:

An "except for" qualified opinion is appropriate because the entity's failure to capitalize leases is a material departure from the applicable financial reporting framework. Disclosure of the lease obligations in the notes does not, by itself, cure an improper recognition or measurement treatment when GAAP requires capitalization. The financial statements therefore contain a material misstatement arising from an inappropriate accounting policy rather than from an inability to obtain sufficient appropriate audit evidence.

Under AU-C Section 705, an auditor issues a qualified opinion when the auditor concludes that misstatements are material but not pervasive to the financial statements. The question explicitly establishes materiality but does not establish that the effects are pervasive. Accordingly, the normal conclusion is an opinion qualified for the effects of the GAAP departure, expressed using "except for" language. This communicates that, except for the identified lease-accounting misstatement, the financial statements are presented fairly in accordance with GAAP.

The AICPA's clarified auditing standards identify AU-C Section 705 as the standard governing modifications to the opinion in the independent auditor's report. See the AICPA clarified Statements on Auditing Standards and the AICPA clarified auditing standards resources.

QUESTION NO: 25

Which of the following

Explanation:s most likely would satisfy an auditor who questions management about significant debits to the accumulated depreciation accounts?

A. The estimated remaining useful lives of plant assets were revised upward.

B. Plant assets were retired during the year.

C. The prior year's depreciation expense was erroneously understated.

D. Overhead allocations were revised at year-end.

ANSWER: B

Explanation:

Plant assets were retired during the year. is correct because accumulated depreciation is a contra-asset account with a normal credit balance, and disposal or retirement requires removing both the asset's recorded cost and the accumulated depreciation associated with that specific asset from the accounting records. The entry for a retirement generally debits accumulated depreciation for the depreciation previously recorded, thereby reducing the account's balance. For example, when equipment is retired, the entity debits accumulated depreciation, credits the equipment account for its cost, and recognizes any resulting gain or loss when applicable. Consequently, significant debits in accumulated depreciation may reasonably reflect substantial asset retirements, replacements, sales, or other disposals during the period. An auditor would corroborate management's explanation by examining retirement authorizations, disposal records, fixed-asset subledger detail, and evidence supporting removal of the related assets from service. This treatment is consistent with the accounting model in which depreciation accumulates over an asset's useful life and is derecognized when the asset itself is derecognized. See the Financial Accounting Standards Board's guidance overview on property, plant, and equipment at FASB Accounting Standards Codification, Topic 360 and the SEC's discussion of depreciation and asset derecognition concepts at SEC filing example.

QUESTION NO: 26

Due to a scope limitation, an auditor disclaimed an opinion on the financial statements taken as a whole, but the auditor's report included a statement that the current asset portion of the entity's balance sheet was fairly stated. The inclusion of this statement is:

A. Not appropriate because it may tend to overshadow the auditor's disclaimer of opinion.

B. Not appropriate because the auditor is prohibited from reporting on only one basic financial statement.

C. Appropriate provided the auditor's scope paragraph adequately describes the scope limitation.

D. Appropriate provided the statement is in a separate paragraph preceding the disclaimer of opinion paragraph.

ANSWER: A

Explanation:

"Not appropriate because it may tend to overshadow the auditor's disclaimer of opinion." is correct. A disclaimer of opinion is required when a scope limitation is both material and pervasive, such that the auditor cannot obtain sufficient appropriate audit evidence on which to base an opinion on the financial statements as a whole. In that circumstance, the report must clearly communicate that the auditor does not express an opinion. Including a favorable conclusion that the current asset portion of the balance sheet is fairly stated creates a piecemeal opinion within the same report. Because current assets commonly are a significant component of an entity's financial position, readers could give undue weight to that favorable statement and fail to appreciate the significance of the auditor's inability to form an overall opinion. This would impair the clarity and prominence of the disclaimer. Auditing standards therefore prohibit an auditor who disclaims an opinion on the financial statements as a whole from also expressing an opinion on a single financial statement or on one or more specific elements, accounts, or items when doing so would contradict or overshadow the disclaimer. The applicable reporting principles are addressed in AICPA SAS No. 134 and the related SAS No. 140 reporting amendments.

QUESTION NO: 27

When unaudited financial statements are presented in comparative form with audited financial statements in a document filed with the Securities and Exchange Commission, such statements should be:

	Marked as "unaudited"	Withheld until audited	Referred to in the auditors report
A.	Yes	No	No
B.	Yes	No	Yes
C.	No	Yes	Yes
D.	No	Yes	No

A. Clearly marked as “unaudited.”

B. Presented separately from the audited financial statements.

C. Withheld from the filing until they have been audited.

D. Referred to in the auditor’s report.

ANSWER: A

Explanation:

Unaudited financial statements presented alongside audited financial statements in an SEC filing should be clearly marked as “unaudited.” Clear labeling informs users that the comparative information was not subjected to the audit procedures and opinion applicable to the audited financial statements. This presentation is especially relevant when interim financial information, such as a subsequent first-quarter balance sheet and results of operations, accompanies annual audited financial statements. The auditor’s report expresses an opinion on the identified audited financial statements and does not extend that opinion to separately presented unaudited information merely because it appears in the same filing. SEC rules permit interim financial statements to be unaudited, subject to the applicable interim-reporting requirements, so the essential presentation safeguard is prominent identification of their unaudited status. See SEC Regulation S-X, Rule 10-01, which addresses interim financial statements and states that such statements need not be audited: 17 C.F.R. § 210.10-01. The PCAOB’s auditor-reporting standard also describes that the report identifies the financial statements that were audited and expresses an opinion on those statements: PCAOB AS 3101.

QUESTION NO: 28

An accountant had begun to audit the financial statements of a nonissuer. Which of the following circumstances most likely would be considered a reasonable basis for agreeing to the entity's request to change the engagement to a compilation?

A. The entity's management does not provide the accountant with a signed representation letter.

B. The accountant is prohibited from corresponding with the entity's legal counsel.

C. The entity's principal creditors no longer require the entity to furnish audited financial statements.

D. The accountant is prevented from examining the minutes of the board of directors' meetings.

ANSWER: C

Explanation:

The entity's principal creditors no longer require the entity to furnish audited financial statements is a reasonable basis for agreeing to change the engagement to a compilation. Under AU-C section 210, an auditor may agree to a requested change in engagement terms when there is reasonable justification for the request. A genuine change in the financial statement users' needs is specifically the type of changed circumstance that can provide that justification. Here, the entity initially needed an audit to satisfy its creditors, but that external reporting requirement has been removed. Management may therefore have a legitimate revised need for financial statements accompanied by compilation services rather than the higher level of assurance provided by an audit. Before accepting the revised engagement, the accountant should consider the circumstances surrounding the request and determine that the change is not intended to avoid reporting a scope limitation or other issue encountered during the audit. If the change is accepted, the accountant and management should agree on the revised terms, ordinarily documented in an updated engagement letter. The compilation engagement is then performed and reported under the applicable SSARS requirements, rather than audit standards. See AICPA AU-C Section 210, Terms of Engagement and AICPA Compilation and Review Standards.

QUESTION NO: 29

Performing inquiry and analytical procedures is the primary basis for an accountant to issue a:

A. Report on compliance with requirements governing major federal assistance programs in accordance with the Single Audit Act.

B. Review report on prospective financial statements that present an entity's expected financial position, given one or more hypothetical assumptions.

C. Management advisory report prepared at the request of a client's audit committee.

D. Review report on comparative financial statements for a nonissuer in its second year of operations.

ANSWER: D

Explanation:

A review report on comparative financial statements for a nonissuer in its second year of operations is correct because a review engagement provides limited assurance and is performed primarily through inquiries of management and analytical procedures. The accountant obtains an understanding of the entity and its environment sufficient to identify areas in which material misstatements are likely to arise, makes inquiries about significant accounting matters and changes in the business, and applies analytics to identify unusual relationships or fluctuations that may require further inquiry. The accountant then evaluates whether the financial statements require material modifications for conformity with the applicable financial reporting framework.

Comparative financial statements do not change the fundamental nature of a review engagement. When prior- and current-period statements are presented together, the accountant applies review procedures to the periods covered by the report and communicates limited assurance in the review report. A nonissuer is eligible for a financial-statement review under the accounting and review services standards, provided management accepts its responsibilities, including responsibility for the financial statements and internal control relevant to their preparation. The AICPA describes reviews as engagements based principally on analytical procedures and inquiries that result in limited assurance. See the AICPA's overview of review, compilation, and preparation services and the AICPA Statements on Standards for Accounting and Review Services resources.

QUESTION NO: 30

For effective internal accounting control, the accounts payable department should compare the information on each vendor's invoice with the:

A. Receiving report and the purchase order.

B. Receiving report and the voucher.

C. Vendor's packing slip and the purchase order.

D. Vendor's packing slip and the voucher.

ANSWER: A

Explanation:

The correct answer is **"Receiving report and the purchase order."** This comparison is the core of the three-way match used in a well-designed purchases and payables process. The purchase order provides evidence that the acquisition was properly authorized before goods or services were ordered. The receiving report is prepared from the receiving function's inspection and documents the quantities and types of goods actually received. Comparing those records with the vendor invoice allows accounts payable to verify the vendor, items, quantities, prices, extensions, terms, and invoice total before recording the liability and authorizing payment.

This control supports the relevant financial-statement assertions for purchases and accounts payable, particularly occurrence, accuracy, and proper authorization. It also helps prevent payment for unordered items, quantities not received, duplicate billings, or amounts that differ from authorized purchase terms. Effective segregation of duties reinforces the control: purchasing authorizes orders, receiving documents delivery, and accounts payable performs the independent matching and payment-processing function. The AICPA's auditing standards describe the auditor's responsibility to understand controls relevant to financial reporting and to evaluate their design and implementation; a three-way match is a common example of such a transaction-processing control. See AICPA Auditing Standards and the GAO Green Book on internal control.

QUESTION NO: 31

In performing an attest engagement, a CPA typically:

A. Supplies litigation support services.

B. Assesses control risk at a low level.

C. Issues a report on subject matter (or on an assertion about subject matter) that is the responsibility of another party.

D. Provides management consulting advice.

ANSWER: C

Explanation:

In an attest engagement, a CPA issues a practitioner's report on a subject matter or on an assertion about subject matter for which another party is responsible. This reflects the essential structure of an attest service: an appropriate party, ordinarily management or another responsible party, is accountable for the underlying subject matter or for preparing an assertion regarding it, while the CPA applies appropriate procedures and communicates a conclusion in a written report. Depending on the level of service, that conclusion may provide examination-level assurance, review-level assurance, or findings from agreed-upon procedures; however, the defining feature is the CPA's reporting role regarding information or subject matter attributable to a responsible party. The subject matter can include financial information, internal control, compliance with requirements, sustainability information, or other matters capable of evaluation or measurement against suitable criteria. This framework helps preserve the CPA's independence and distinguishes attest work from advisory services in which the CPA's primary role is to provide recommendations or assistance rather than report a conclusion on another party's subject matter or assertion. The AICPA describes attest engagements and the applicable reporting framework in its Statements on Standards for Attestation Engagements. See the AICPA Attestation Standards and the AICPA SSAEs.

QUESTION NO: 32

Smith, CPA, has been asked to issue a review report on the balance sheet of Cone Company, a nonissuer, and not on the other related financial statements. Smith may do so only if:

A. Smith compiles and reports on the related statements of income, retained earnings, and cash flows.

B. Smith is not aware of any material modifications needed for the balance sheet to conform with GAAP.

C. The scope of Smith's inquiry and analytical procedures is not restricted.

D. Cone is a new client and Smith accepts the engagement after the end of Cone's fiscal year.

ANSWER: C

Explanation:

The scope of Smith's inquiry and analytical procedures is not restricted. A review engagement performed under SSARS may be undertaken for a single financial statement, such as a balance sheet, rather than for a complete set of financial statements. The fact that the engagement concerns only the balance sheet does not, by itself, prevent the accountant from issuing a review report.

However, the accountant must be able to perform the inquiries of management and the analytical procedures the accountant considers necessary in the circumstances to obtain a reasonable basis for reporting. A management-imposed restriction that prevents the performance of those necessary review procedures is a scope limitation and would preclude issuance of the standard review report on that financial statement. Thus, Smith can report on Cone's balance sheet alone when the review work is not restricted and Smith can comply with the applicable review standards for that statement.

This conclusion follows the AICPA Statements on Standards for Accounting and Review Services, which govern review engagements for nonissuers and require the accountant to obtain an appropriate basis for the review conclusion. See the AICPA's Compilation and Review Standards resources and its SSARS standards and guidance page.

QUESTION NO: 33

This question will represent a statement, question, excerpt, or comment taken from various parts of an auditor's documentation file. Letter choices A-P represent a list of the likely sources of the statement, question, excerpt, or comment. Select, as the best answer for each item, the most likely source. Select only one source for each item.

Was the difference of opinion on the accrued pension liabilities that existed between the engagement personnel and the actuarial specialist resolved in accordance with firm policy and appropriately documented?

A. Practitioner's report on management's assertion about an entity's compliance with specified requirements.

B. Auditor's communications on significant deficiencies in internal control.

C. Audit inquiry letter to legal counsel.

D. Lawyer's response to audit inquiry letter.

E. Communication from those charged with governance to the auditor.

F. Auditor's communication to those charged with governance (other than with respect to significant deficiencies in internal control).

G. Report on the application of accounting principles.

H. Auditor's engagement letter.

I. Letter for underwriters.

J. Accounts receivable confirmation request.

K. Request for bank cutoff statement.

L. Explanatory paragraph of an auditor's report on financial statements.

M. Partner's engagement review notes.

N. Management representation letter.

O. Successor auditor's communication with predecessor auditor.

P. Predecessor auditor's communication with successor auditor.

ANSWER: M

Explanation:

Partner's engagement review notes are the most likely source because the question is a review-level prompt directed at whether the engagement team followed the firm's procedures for resolving and documenting a professional disagreement. Accrued pension liabilities commonly involve specialized actuarial knowledge, so a difference of opinion between engagement personnel and an actuarial specialist is an important engagement-quality matter requiring clear resolution and documentation. The engagement partner is responsible for the overall direction, supervision, performance, and review of the audit engagement, including determining that significant matters requiring consultation or resolution were handled under the firm's policies. Review notes provide a practical means for the partner to evidence that responsibility by asking whether the disagreement was resolved appropriately and whether the audit file contains support for the conclusion reached. This inquiry is therefore characteristic of an engagement partner's review of working papers rather than a representation, confirmation, external communication, or report. AICPA quality-management standards emphasize engagement-level responsibilities and the need for appropriate consultation and resolution of differences of opinion. See the AICPA's Quality Management resources and its Auditing Standards and Guidance.

QUESTION NO: 34

Reporting standards for financial audits under Government Auditing Standards (the Yellow Book) differ from reporting under generally accepted auditing standards in that Government Auditing Standards require the auditor to:

A. Provide positive assurance that control activities regarding segregation of duties are consistent with the entity's control objectives.

B. Present the results of the auditor's tests of controls.

C. Provide negative assurance that the auditor discovered no evidence of intentional override of internal controls.

D. Describe the scope of the auditor's principal substantive tests.

ANSWER: B

Explanation:

Present the results of the auditor's tests of controls is correct because Government Auditing Standards add financial-audit reporting responsibilities beyond the standard auditor's report issued under generally accepted auditing standards. When performing a financial audit under the Yellow Book, the auditor must report on internal control over financial reporting and on compliance with provisions of laws, regulations, contracts, and grant agreements that have a material effect on the financial statements. This reporting communicates both the scope of the auditor's work in these areas and the results of that work, including identified deficiencies in internal control and instances of noncompliance that meet the applicable reporting criteria.

The required report may be included in the financial-statement auditor's report or issued separately. Importantly, its purpose is to provide transparency to users of governmental audit reports regarding the auditor's consideration and testing of internal control and compliance in connection with the financial audit. The Yellow Book treats these matters as essential reporting elements because public accountability often requires users to understand not only whether the financial statements are fairly presented, but also significant matters identified in the related control and compliance work. See the GAO's Government Auditing Standards (Yellow Book), particularly the financial-audit reporting requirements, and the GAO's Yellow Book resource page.

QUESTION NO: 35

Which of the following statements concerning material weaknesses and significant deficiencies is correct with respect to an audit of a nonissuer?

A. An auditor need not identify and communicate material weaknesses separately from significant deficiencies.

B. All material weaknesses are significant deficiencies.

C. An auditor should report immediately material weaknesses and significant deficiencies discovered during an audit.

D. All significant deficiencies are material weaknesses.

E. A material weakness is more severe than a significant deficiency.

ANSWER: E

Explanation:

"A material weakness is more severe than a significant deficiency" is correct under the current AICPA auditing standards for nonissuers. AU-C section 265 defines a material weakness as a deficiency, or combination of deficiencies, in internal control for which there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is defined as a deficiency, or combination of deficiencies, that is less severe than a material weakness but important enough to merit attention by those charged with governance. Thus, the standards establish material weaknesses and significant deficiencies as distinct levels of control-deficiency severity; a material weakness is the more serious classification. The auditor communicates significant deficiencies and material weaknesses identified during the audit in writing to management and those charged with governance, consistent with AU-C section 265. This terminology reflects the clarified auditing standards and differs from older terminology that defined a material weakness as a type of significant deficiency. The AICPA's current auditing and attestation standards resources are available at AICPA Audit and Assurance Standards; the applicable requirements are in AICPA Professional Standards, AU-C section 265.

QUESTION NO: 36

In considering materiality for planning purposes, an auditor believes that misstatements aggregating $10,000 would have a material effect on an entity's income statement, but that misstatements would have to aggregate $20,000 to materially affect the balance sheet. Ordinarily, it would be appropriate to design auditing procedures that would be expected to detect misstatements that aggregate:

A. $10,000

B. $15,000

C. $20,000

D. $30,000

ANSWER: A

Explanation:

$10,000 is correct because, when planning an audit of a complete set of financial statements, the auditor ordinarily bases planning materiality on the lowest amount of misstatement that could be material to any individual financial statement. The income statement and balance sheet are linked: a misstatement affecting income generally also affects retained earnings or another equity account on the balance sheet. Nevertheless, the auditor's audit plan must be responsive to the financial statement that is more sensitive to misstatement. Here, an aggregate misstatement of $10,000 could materially affect the income statement, even though $20,000 would be needed to materially affect the balance sheet. Therefore, audit procedures should be designed to provide reasonable assurance of detecting aggregate misstatements at the $10,000 level. This approach helps the auditor reduce audit risk to an appropriately low level and supports a conclusion that the financial statements, considered as a whole, are free of material misstatement. AU-C section 320 explains that materiality is applied both in planning and performing the audit and that the auditor considers materiality for the financial statements as a whole. See the AICPA Clarified Statements on Auditing Standards and the PCAOB guidance on consideration of materiality.

QUESTION NO: 37

In using the work of a specialist, an auditor referred to the specialist's findings in the auditor's report. This would be an appropriate reporting practice if the:

A. Client is not familiar with the professional certification, personal reputation, or particular competence of the specialist.

B. Auditor, as a result of the specialist's findings, adds an explanatory paragraph emphasizing a matter regarding the financial statements.

C. Auditor understands the form and content of the specialist's findings in relation to the representations in the financial statements.

D. Auditor, as a result of the specialist's findings, decides to indicate a division of responsibility with the specialist.

ANSWER: B

Explanation:

“Auditor, as a result of the specialist's findings, adds an explanatory paragraph emphasizing a matter regarding the financial statements.” is correct because an auditor normally accepts responsibility for the audit conclusion and does not refer to the specialist in a standard unmodified auditor’s report. A reference can be appropriate, however, when the specialist’s work gives rise to a matter that must be communicated in an explanatory (under modern standards, emphasis-of-matter or other-matter) paragraph or contributes to a modification of the opinion. In that circumstance, identifying the specialist or describing the specialist’s findings may help users understand the significant financial-statement matter being highlighted and the basis for the auditor’s reporting communication. The auditor must still evaluate the specialist’s competence, capabilities, objectivity, and the adequacy of the specialist’s work for audit purposes; the reference does not transfer or divide the auditor’s responsibility for the opinion. AU-C section 620 addresses using the work of an auditor’s specialist, while AU-C section 706 addresses explanatory paragraphs used to draw users’ attention to appropriately presented matters that are fundamental to understanding the financial statements. See the AICPA AU-C 620 guidance and the AICPA AU-C 706 guidance.

QUESTION NO: 38

In assessing the objectivity of internal auditors, an independent auditor should:

A. Evaluate the quality control program in effect for the internal auditors.

B. Examine documentary evidence of the work performed by the internal auditors.

C. Test a sample of the transactions and balances that the internal auditors examined.

D. Determine the organizational level to which the internal auditors report.

ANSWER: D

Explanation:

The independent auditor should determine the organizational level to which the internal auditors report because an internal audit function’s reporting relationship is a central indicator of its organizational status and ability to act objectively. Under AU-C section 610, the external auditor evaluates whether the internal audit function’s organizational status and relevant policies and procedures support the objectivity of its work. Relevant considerations include whether the function reports to those charged with governance or to an officer with sufficient authority to promote broad audit coverage and ensure that internal-audit findings and recommendations receive appropriate consideration and action. A reporting line with appropriate stature helps reduce the risk that internal auditors’ scope, judgments, or communications will be inappropriately influenced by the areas or personnel they audit. The assessment is made in the context of deciding whether, and to what extent, the external auditor may use the work of the internal audit function. The auditor also considers factors such as restrictions imposed on the function, management’s role in employment decisions affecting internal audit, and whether internal auditors are free to communicate directly with those charged with governance. These matters collectively provide evidence about whether the internal audit function can perform its responsibilities without undue influence. See PCAOB AU 322, The Auditor’s Consideration of the Internal Audit Function and AICPA AU-C Section 610.

QUESTION NO: 39

In testing long-term investments, an auditor ordinarily would use analytical procedures to ascertain the reasonableness of the:

A. Completeness of recorded investment income.

B. Classification between balance sheet portfolios.

C. Valuation of marketable equity securities.

D. Existence of unrealized gains or losses in the portfolio.

ANSWER: A

Explanation:

Completeness of recorded investment income is correct because analytical procedures are particularly well suited to developing an independent expectation of income that should have been recognized from an entity's investment holdings. The auditor can use the quantity and type of investments held, contractual interest rates, payment dates, dividend declarations, investee financial information, and prior-period results to estimate a reasonable amount of interest and dividend income. Comparing that expectation with the amount recorded in the general ledger helps the auditor identify potentially omitted income and therefore provides evidence relevant to the completeness assertion.

This work is ordinarily performed as part of the auditor's substantive analytical procedures. The expectation should be sufficiently precise for the auditor's assessed risk, and material or unusual differences should be investigated through additional audit procedures. For example, where a bond was held throughout the year, applying its stated coupon rate to the relevant principal balance produces a direct expectation of interest income. Similarly, dividends declared on shares owned can be compared with dividend income recorded. This approach links reliable external or contractual information with the entity's accounting records. The AICPA's clarified auditing standards include requirements and application guidance for analytical procedures in AU-C section 520; see AICPA Clarified Statements on Auditing Standards. Related audit evidence principles are addressed in SAS No. 142.

QUESTION NO: 40

An auditor selected items for test counts while observing a client's physical inventory. The auditor then traced the test counts to the client's inventory listing. This procedure most likely obtained evidence concerning management's assertion of:

A. Rights and obligations.

B. Completeness.

C. Existence.

D. Valuation.

ANSWER: B

Explanation:

Completeness. is correct because the direction of the auditor's testing begins with inventory physically observed during the count and follows those items into the client's inventory records. This "floor-to-sheet" direction tests whether inventory that exists at the count location has been captured in the final inventory listing. It therefore provides evidence that recorded inventory quantities are not understated because items on hand were omitted from the listing.

During a physical inventory observation, the auditor commonly performs test counts in both directions. Starting with items selected from the client's inventory listing and locating them on the warehouse floor addresses whether recorded items actually exist. In contrast, independently selecting items on the floor, performing test counts, and tracing them to the listing addresses whether all inventory observed has been recorded. The stated procedure uses the latter direction and is therefore directed at the completeness assertion for inventory.

This approach is consistent with the AICPA auditing standards' requirement that an auditor obtain sufficient appropriate evidence about the existence and condition of inventory when inventory is material, including through attendance at physical inventory counting when practicable. See AICPA Clarified Statements on Auditing Standards and PCAOB guidance on observing inventories.

QUESTION NO: 41

The audit plan usually cannot be finalized until the:

A. Consideration of the entity's internal control has been completed.

B. Representation letter has been signed by the client.

C. Significant deficiencies in internal control have been communicated to those charged with governance.

D. Search for unrecorded liabilities has been performed and documented.

ANSWER: A

Explanation:

“Consideration of the entity's internal control has been completed.” is correct because an auditor must obtain an understanding of the entity and its environment, including the system of internal control, before finalizing the audit plan. This understanding is a required risk-assessment procedure and provides the basis for identifying and assessing risks of material misstatement at the financial-statement and assertion levels. The auditor uses those risk assessments to determine the nature, timing, and extent of further audit procedures, including which controls, if any, will be tested and what substantive procedures are necessary. Accordingly, while planning begins early and remains iterative throughout the engagement, the detailed audit plan cannot ordinarily be completed until the auditor has considered the relevant components of internal control and evaluated how identified risks affect the planned audit response. The plan may subsequently be revised if new information or changed circumstances arise during the audit; finalizing the initial plan does not mean it is immutable. This requirement is addressed in AU-C section 315, which requires an understanding of the entity’s system of internal control to identify and assess risks, and AU-C section 300, which requires the auditor to develop an audit plan based on planning activities. See AICPA AU-C 315 and AICPA AU-C 300.

QUESTION NO: 42

When an entity changes its method of accounting for income taxes, which has a material effect on comparability, the auditor should refer to the change in an explanatory paragraph added to the auditor's report. This paragraph should identify the nature of the change and:

A. Explain why the change is justified under generally accepted accounting principles.

B. Describe the cumulative effect of the change on the audited financial statements.

C. State the auditor's explicit concurrence with or opposition to the change.

D. Refer to the financial statement note that discusses the change in detail.

ANSWER: D

Explanation:

“Refer to the financial statement note that discusses the change in detail.

” is correct because the financial statements—not the auditor’s report—are the primary source of the detailed disclosure about a change in accounting principle. When a material accounting change affects comparability, the entity’s notes should describe the change and the relevant financial-statement effects in accordance with the applicable financial reporting framework. The auditor’s reporting role is to draw users’ attention to that disclosure through an explanatory (or, under current AICPA terminology, emphasis-of-matter) paragraph, provided the accounting and disclosure are appropriate.

This reporting approach keeps the auditor’s communication concise and clearly directs financial-statement users to the location containing the entity’s complete explanation. A customary formulation is: “As discussed in Note X to the financial statements, the Company changed its method of accounting for income taxes in 20X2.” The reference both identifies the nature of the accounting change and connects it to the note where readers can evaluate its detailed presentation. AICPA auditing standards addressing consistency and emphasis-of-matter communications are available through the AICPA Audit and Attest Standards. Comparable guidance for issuer audits appears in PCAOB AS 2820, Evaluating Consistency of Financial Statements.

QUESTION NO: 43

How are management's responsibility and the auditor's responsibility represented in the standard auditor's report?

	Management's responsibility	Auditor's responsibility
A.	Explicitly	Explicitly
B.	Implicitly	Implicitly
C.	Implicitly	Explicitly
D.	Explicitly	Implicitly

A. Management's responsibility and the auditor's responsibility are stated explicitly in the introductory paragraph of the standard auditor's report.

B. Option B

C. Option C

D. Option D

ANSWER: A

Explanation:

In the standard auditor's report format addressed by this question, both responsibilities are expressly stated in the introductory paragraph. That paragraph identifies the financial statements that were audited, states that management is responsible for preparing and fairly presenting those financial statements, and states that the auditor's responsibility is to express an opinion on them based on the audit. This division is fundamental to the audit engagement: management prepares the financial statements and maintains responsibility for their fair presentation, while the independent auditor evaluates the statements and supporting evidence under applicable auditing standards to provide an opinion. Thus, describing both management's responsibility and the auditor's responsibility explicitly in the introductory paragraph accurately reflects the report form tested here. Auditing-report requirements and terminology have evolved; in the current clarified reporting model, these responsibilities are generally presented in separately captioned sections. Nevertheless, the allocation of responsibility remains the same, and the answer reflects the historical standard-report presentation shown in the question. See the AICPA's Professional Standards resources and the PCAOB's discussion of the auditor's report.

QUESTION NO: 44

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

A. Add a separate paragraph to the auditor's standard report to explain the transaction.

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

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

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

ANSWER: C

Explanation:

"Obtain an understanding of the business purpose of the transaction." is correct because identifying that a transaction involves a related party is not the end of the auditor's work. Under AU-C section 550, the auditor performs procedures to understand the transaction's business purpose and evaluates whether it has been appropriately accounted for and disclosed in accordance with the applicable financial reporting framework. Understanding the business rationale helps the auditor assess whether the transaction may indicate unusual terms, conflicts of interest, management bias, fraud risk, or a risk of material misstatement in the financial statements.

The auditor’s work should focus on the substance and circumstances of the transaction, including its terms, authorization, supporting documentation, and financial-statement effects. The nature and extent of further procedures depend on the auditor’s risk assessment and the facts identified. Related-party transactions may be valid and properly conducted, but their non-arm’s-length nature can make the business purpose and accounting implications especially important audit considerations. This approach supports the auditor’s overall responsibilities to obtain sufficient appropriate audit evidence and evaluate presentation and disclosure. See the AICPA’s Audit and Assurance Standards resources and the PCAOB’s closely aligned AS 2410, Related Parties.

QUESTION NO: 45

The date of the management representation letter should coincide with the date of the:

A. Balance sheet.

B. Latest interim financial information.

C. Auditor's report.

D. Latest related party transaction.

ANSWER: C

Explanation:

The correct answer is **Auditor's report.** Management representations are written representations from management that are necessary audit evidence and that confirm management’s responsibility for the financial statements and the completeness of information provided to the auditor. Because these representations encompass matters arising throughout the audit, including events that occur after the financial-statement date, the representation letter is dated as of the date of the auditor’s report. This dating aligns management’s representations with the end of the auditor’s responsibility for evaluating subsequent events and obtaining sufficient appropriate audit evidence before releasing the report.

AU-C section 580 states that the date of the written representations should be as near as practicable to, but not after, the date of the auditor’s report on the financial statements. In a financial-statement audit, the letter is ordinarily signed and dated on the auditor’s report date. This provides the auditor with current written confirmation from those charged with preparing the financial statements at the point when the audit opinion is finalized. See the AICPA’s Clarified Statements on Auditing Standards and the PCAOB’s AS 2805, Management Representations.

QUESTION NO: 46

An auditor may achieve audit objectives related to particular assertions by:

A. Performing analytical procedures.

B. Adhering to a system of quality control.

C. Preparing audit documentation.

D. Increasing the level of detection risk.

ANSWER: A

Explanation:

Performing analytical procedures is correct because analytical procedures are audit procedures that evaluate plausible relationships among financial and nonfinancial data. When appropriately designed and performed as substantive analytical procedures, they can provide audit evidence directly relevant to management assertions for account balances, transactions, or disclosures. For example, an auditor may develop an expectation for revenue using production, sales-volume, or pricing data and investigate material differences between that expectation and the recorded amount. This work can address assertions such as occurrence, completeness, accuracy, valuation, and cutoff, depending on the account and the procedure’s design.

The auditor must determine whether the procedure is sufficiently precise, whether the underlying data are reliable, and whether the expected relationship is predictable enough to provide the required level of assurance. Substantive analytical procedures may be used alone for an assertion when the assessed risk and available evidence support that approach, or they may be combined with tests of details. The AICPA's auditing standards identify analytical procedures as a substantive procedure and require the auditor to design and perform procedures responsive to assessed risks at the assertion level. See the AICPA's Auditing Standards resources and AU-C section 520, Analytical Procedures.

QUESTION NO: 47

A successor auditor should request the new client to authorize the predecessor auditor to allow a review of the predecessor's:

	Engagement letter	Audit Documentation
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

A. Option A

B. Option B

C. Audit documentation

D. Option D

ANSWER: C

Explanation:

Audit documentation is the appropriate item for the successor auditor to request permission to review. Before accepting an engagement, the successor auditor communicates with the predecessor auditor after obtaining the prospective client's authorization. If the engagement is accepted, the successor may also request access to relevant audit documentation. Reviewing that documentation assists the successor in evaluating matters that affect the current engagement, particularly opening balances, consistency in accounting-principle application, and information relevant to the predecessor's conclusions on the prior-period financial statements.

The predecessor auditor retains ownership and custody of its audit documentation, so the client's authorization is necessary before access can be provided. The predecessor ordinarily determines the nature and extent of access and may provide information through discussion, copies, or review arrangements as appropriate. This process supports an orderly transition between auditors while preserving the confidentiality obligations applicable to client information. The AICPA's successor-auditor guidance addresses communication with the predecessor and access to audit documentation in AU-C section 210 and AU-C section 510. See AICPA AU-C Section 210, Terms of Engagement and AICPA AU-C Section 510, Opening Balances.

QUESTION NO: 48

Which of the following is an analytical procedure that an auditor most likely would perform when planning an audit?

A. Confirming bank balances with the financial institutions.

B. Scanning accounts receivable for amounts over credit limits.

C. Recalculating inventory extensions of physical inventory counts.

D. Comparing the current-year account balances for conformity with predictable patterns.

ANSWER: D

Explanation:

Comparing the current-year account balances for conformity with predictable patterns is the appropriate planning analytical procedure because it evaluates relationships in financial information at an aggregated level. During audit planning, the auditor uses such comparisons to develop an understanding of the entity, identify areas that may present elevated risks of material misstatement, and direct the nature, timing, and extent of further audit work. Predictable patterns may arise from prior-period results, budgets, industry trends, seasonal activity, or stable relationships among financial-statement accounts. For example, an auditor may expect payroll expense to move consistently with headcount or sales, or expect gross margin to remain within a reasonable range absent changes in pricing, product mix, or production costs. Significant unexpected fluctuations prompt further inquiry and risk assessment. This use of analytical procedures is consistent with the AICPA's audit and attest standards framework, which requires risk-assessment procedures in planning and recognizes analytical procedures as a means of identifying unusual relationships and potential misstatements. The comparison is therefore well suited to the planning stage because it gives the auditor a broad, efficient basis for focusing subsequent procedures on accounts and assertions that warrant closer attention. See the AICPA Audit and Attest Standards and the related discussion of planning analytical procedures in PCAOB AS 2305, Substantive Analytical Procedures.

QUESTION NO: 49

Before accepting an engagement to audit a new client, an auditor is required to:

A. Make inquiries of the predecessor auditor after obtaining the consent of the prospective client.

B. Obtain an understanding of the entity and its environment, including its internal control.

C. Prepare a memorandum setting forth the staffing requirements and documenting the preliminary audit plan.

D. Discuss the management representation letter with the prospective client's audit committee.

ANSWER: A

Explanation:

Before accepting an initial audit engagement, the prospective auditor is required to communicate with the predecessor auditor, provided that the prospective client authorizes the communication. This required client consent protects the confidentiality of information obtained during the predecessor auditor's professional relationship with the client. The communication is an essential acceptance procedure because it helps the prospective auditor assess matters that may affect the decision to accept the engagement, including management's integrity, disagreements about accounting or auditing matters, significant deficiencies or material weaknesses in internal control, fraud or suspected fraud, and the reasons for the auditor change. The prospective auditor should request the client to authorize the predecessor auditor to respond fully; if permission is denied or the predecessor's response is limited, the prospective auditor considers the implications when deciding whether to accept the engagement. This procedure supports the auditor's broader obligation under generally accepted auditing standards to undertake an engagement only when the auditor has considered whether the engagement can be performed in accordance with professional standards and applicable legal or ethical requirements. Authoritative guidance appears in AU-C section 210, Communication With Predecessor Auditors, and the AICPA's audit-engagement acceptance resources at AICPA Audit and Assurance.

QUESTION NO: 50

The overall attitude and awareness of those charged with governance (i.e., an entity's board of directors) concerning the importance of internal control usually is reflected in its:

A. Computer-based controls.

B. System of segregation of duties.

C. Control environment.

D. Safeguards over access to assets.

ANSWER: C

Explanation:

The correct answer is **Control environment.** Under the COSO Internal Control—Integrated Framework, the control environment is the foundation for an effective system of internal control. It encompasses the organization's standards, processes, and structures for carrying out internal control, including the oversight responsibilities and expectations established by the board of directors. The board's and senior management's commitment to integrity and ethical values, independence in governance oversight, assignment of authority and responsibility, and accountability directly communicate how seriously the entity regards internal control. This pervasive tone influences the control consciousness of personnel throughout the organization and supports the design, implementation, and operation of the remaining components of internal control. In the audit context, AU-C section 315 requires the auditor to obtain an understanding of the entity's control environment as part of understanding the system of internal control and assessing risks of material misstatement. Accordingly, the overall attitude and awareness of those charged with governance toward the importance of controls is reflected in the entity's control environment. See the COSO Internal Control guidance and AICPA AU-C Section 315.

QUESTION NO: 51

Which of the following conditions is necessary for a practitioner to accept an attest engagement to examine and report on a nonissuer's internal control over financial reporting?

A. The practitioner anticipates relying on the entity's internal control in a financial statement audit.

B. Management presents its written assertion about the effectiveness of internal control.

C. The practitioner is a continuing auditor who previously has audited the entity's financial statements.

D. Management agrees not to present the practitioner's report in a general-use document to stockholders.

ANSWER: B

Explanation:

Management presents its written assertion about the effectiveness of internal control is necessary because an examination-level attestation engagement on a nonissuer's internal control over financial reporting is performed on management's assertion regarding the effectiveness of that control. The written assertion identifies the subject matter being evaluated and provides the representation against which the practitioner obtains sufficient appropriate evidence and expresses an opinion. Management's assertion also reflects management's responsibility for establishing and maintaining effective internal control and for evaluating its effectiveness using suitable criteria. The practitioner's role is independent: the practitioner examines management's assertion and reports whether it is fairly stated, in all material respects, based on the applicable criteria. Accordingly, obtaining management's written assertion is a fundamental acceptance and performance condition for this form of examination engagement. The applicable attestation standards are included in the AICPA's Statements on Standards for Attestation Engagements. Related professional requirements for reporting on internal control in an audit context are available in AU-C section 265.

QUESTION NO: 52

Which of the following statements most likely represents a disadvantage for an entity that keeps microcomputer-prepared data files rather than manually prepared files?

A. It is usually more difficult to detect transposition errors.

B. Transactions are usually authorized before they are executed and recorded.

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

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

ANSWER: C

Explanation:

It is usually easier for unauthorized persons to access and alter the files. This is a significant potential disadvantage of microcomputer-prepared files because electronic data can be accessed, copied, changed, or deleted rapidly by anyone who has inappropriate physical or logical access. In a microcomputer environment, files may be broadly available through shared devices, local drives, networks, removable media, or user accounts. Without appropriately designed controls—such as unique user identification, strong authentication, role-based access privileges, encryption, audit logs, and timely review of access activity—an individual may alter accounting information without authorization and potentially without an immediately visible record of the change. Effective internal control requires management to safeguard assets and maintain reliable information, including restricting access to records to authorized personnel and protecting data from unauthorized modification. The AICPA's auditing standards describe the importance of information-system controls in addressing risks arising from IT, while the NIST access-control guidance outlines measures for limiting system access to authorized users and functions. See AICPA Audit and Attest Standards and NIST SP 800-53, Access Control.

QUESTION NO: 53

Which of the following best describes the responsibility of the auditor with respect to significant deficiencies and material weaknesses in an audit of an issuer?

	Must be Communicated to Management and the Audit Committee	*Results in an Adverse Opinion on the Effectiveness of Internal Control*
A.	Both significant deficiencies and material weaknesses	Both significant deficiencies and material weaknesses
B.	Both significant deficiencies and material weaknesses	Material weaknesses but not significant deficiencies
C.	Material weaknesses but not significant deficiencies	Both significant deficiencies and material weaknesses
D.	Material weaknesses but not significant deficiencies	Material weaknesses but not significant deficiencies

A. The auditor communicates significant deficiencies and material weaknesses to management and the audit committee and issues an adverse opinion on internal control for either type of deficiency.

B. The auditor communicates significant deficiencies and material weaknesses to management and the audit committee and issues an adverse opinion on internal control only when a material weakness exists.

C. The auditor communicates only material weaknesses to management and the audit committee and issues an adverse opinion on internal control only when a material weakness exists.

D. The auditor communicates significant deficiencies and material weaknesses to management and the audit committee but does not issue an adverse opinion on internal control for a material weakness.

ANSWER: B

Explanation:

In an integrated audit of an issuer, the auditor must evaluate identified control deficiencies to determine whether they are significant deficiencies or material weaknesses. The auditor is required to communicate significant deficiencies and material weaknesses in writing to management and the audit committee. This communication is an important part of the auditor's responsibilities because it informs those charged with governance of deficiencies that merit their attention, even when the deficiencies do not prevent the auditor from concluding that internal control over financial reporting is effective.

An adverse opinion on the effectiveness of internal control over financial reporting is required when one or more material weaknesses exist as of the assessment date. A material weakness means there is a reasonable possibility that a material misstatement of the financial statements will not be prevented or detected on a timely basis. Accordingly, the statement that the auditor communicates both significant deficiencies and material weaknesses to management and the audit committee, but issues an adverse internal-control opinion only for material weaknesses, accurately states the auditor's responsibility. PCAOB Auditing Standard 2201 addresses the required written communications and the adverse-opinion consequence of material weaknesses. See PCAOB AS 2201 and PCAOB AS 1305.

QUESTION NO: 54

Which of the following should be included as a written representation from management?

A. The belief that misstatements identified by the auditor and not corrected are immaterial.

B. The belief that misstatements identified by the auditor and corrected are material.

C. The belief that the auditor is responsible for the fair presentation of the financial statements in conformity with generally accepted accounting principles.

D. The belief that the financial statements are completely accurate in all respects.

ANSWER: A

Explanation:

The belief that misstatements identified by the auditor and not corrected are immaterial is required in management's written representations when such uncorrected misstatements exist. Under AU-C 580, management's representation letter must acknowledge its responsibility for preparing and fairly presenting the financial statements and provide specified representations relevant to the audit. One required representation is management's belief that the effects of uncorrected misstatements are immaterial, individually and in the aggregate, to the financial statements as a whole. The auditor ordinarily attaches or includes a summary of the uncorrected misstatements so management can make this representation with a clear understanding of the items involved. This representation is important because management is responsible for the financial statements and for deciding whether proposed adjustments should be recorded. It also provides audit evidence supporting the auditor's evaluation of the aggregate effect of identified misstatements on the financial statements. The representation concerns materiality rather than asserting that no misstatements exist; financial statements may contain uncorrected differences that management concludes do not materially affect fair presentation. See AICPA Clarified Statements on Auditing Standards and PCAOB AU 333, Management Representations.

QUESTION NO: 55

Which of the following internal controls most likely would 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 actual balances.

C. The review of prenumbered purchase orders to detect unrecorded trade-ins.

D. Approval of periodic depreciation entries by a supervisor independent of the accounting department.

ANSWER: A

Explanation:

Periodic physical inspection of plant and equipment by the internal audit staff is the control most likely to support a reduced assessment of control risk for plant and equipment acquisitions. A physical inspection provides direct evidence that capital assets recorded as acquired are actually present and in use. It therefore addresses the existence assertion for recorded equipment additions and can help reveal fictitious, unsupported, or improperly recorded acquisitions. When performed periodically by internal audit personnel, the inspection also has enhanced monitoring value because the individuals performing it are ordinarily independent of the day-to-day fixed-asset accounting function. The control is particularly persuasive when inspection results are compared with fixed-asset records, discrepancies are investigated promptly, and appropriate corrections or follow-up actions are documented. In assessing control risk below the maximum level, an auditor considers whether relevant controls are suitably designed and have operated effectively enough to prevent, or detect and correct, material misstatements. A recurring internal-audit inspection is a substantive monitoring control that can generate evidence on the reliability of recorded plant and equipment balances and additions. This is consistent with the auditor's evaluation of controls and responses to assessed risks described in PCAOB AS 2201 and with the monitoring component of the COSO Internal Control—Integrated Framework.

QUESTION NO: 56

This question consists of an item pertaining to possible deficiencies in an accountant's review report. Jordan & Stone, CPAs, audited the financial statements of Tech Co., a nonissuer, for the year ended December 31, 20X1, and expressed an unqualified opinion. For the year ended December 31, 20X2, Tech issued comparative financial statements. Jordan & Stone reviewed Tech's 20X2 financial statements and Kent, an assistant on the engagement, drafted the accountants' review report below.

Land, the engagement supervisor, decided not to reissue the prior year's auditors' report, but instructed Kent to include a separate paragraph in the current year's review report describing the responsibility assumed for the prior year's audited financial statements. This is an appropriate reporting procedure.

Land reviewed Kent's draft and indicated in the Supervisor's Review Notes below that there were several deficiencies in Kent's draft.

Accountant's Review Report

We have reviewed and audited the accompanying balance sheets of Tech Co. as of December 31, 20X2 and 20X1, and the related statements of income, retained earnings, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants and generally accepted auditing standards. All information included in these financial statements is the representation of the management of Tech Co.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements. Because of the inherent limitations of a review engagement, this report is intended for the information of management and should not be used for any other purpose.

The financial statements for the year ended December 31, 20X1, were audited by us and our report was dated March 2, 20X2. We have no responsibility for updating that report for events and circumstances occurring after that date.

Jordan and Stone, CPAs March 1, 20X3

Supervisor's Review Notes

There should be no comparison of the scope of a review to an audit in the second (scope) paragraph.

A. Correct

B. Incorrect

ANSWER: B

Explanation:

Incorrect is correct because the standard review report for a nonissuer appropriately describes the review's limited procedures and contrasts its scope with that of an audit. Under SSARS, a review consists principally of performing analytical procedures and making inquiries of management and others within the entity. The report also explains that a review is substantially less in scope than an audit, whose objective is to obtain reasonable assurance and express an opinion on the financial statements as a whole. This comparison communicates the level of assurance provided by the review and is a key feature that helps report users understand that the accountant does not express an audit opinion.

Accordingly, the sentence in the draft stating that a review is substantially less in scope than an audit is appropriate in substance, rather than a deficiency requiring removal. The supervisor's statement that there should be no comparison of review scope to audit scope is therefore incorrect. The applicable reporting concepts are reflected in the AICPA's SSARS framework for review engagements, including AICPA Statements on Standards for Accounting and Review Services. The distinction between a review's limited assurance and an audit's reasonable assurance is also summarized in the AICPA compilation and review standards resources.

QUESTION NO: 57

Which of the following procedures would an auditor most likely perform for year-end accounts receivable confirmations when the auditor did not receive replies to second requests?

A. Review the cash receipts journal for the month prior to the year-end.

B. Intensify the study of the internal control structure concerning the revenue cycle.

C. Increase the assessed level of detection risk for the existence assertion.

D. Inspect the shipping records documenting the merchandise sold to the debtors.

ANSWER: D

Explanation:

Inspect the shipping records documenting the merchandise sold to the debtors is the appropriate alternative procedure because the lack of responses to confirmation requests leaves the auditor without direct external evidence for the confirmed receivable balances. The auditor should obtain other relevant and reliable audit evidence addressing whether the year-end receivables existed and represented bona fide sales to customers. Shipping documents, such as bills of lading and shipping logs, provide evidence that goods were dispatched to the customer. When traced and matched to the related sales invoice, customer account, and timing around year-end, those records support that the recorded sale occurred and that a receivable from the debtor was valid at the reporting date. The auditor should focus especially on shipments immediately before and after year-end to evaluate whether the entity recorded revenue and receivables in the proper period. This work is an example of an alternative procedure used when confirmation evidence is unavailable; the nature and extent of the work should be sufficient to reduce audit risk to an acceptable level. AU-C section 505 requires auditors to perform alternative procedures for nonresponses to positive confirmation requests when necessary to obtain sufficient appropriate audit evidence. See [AICPA AU-C Section 505, External Confirmations] and [PCAOB AU 330, The Confirmation Process].

QUESTION NO: 58

Which of the following controls most likely would help ensure that all credit sales transactions of an entity are recorded?

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

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

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

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

ANSWER: D

Explanation:

The billing department supervisor matches prenumbered shipping documents with entries in the sales journal. This control directly addresses the completeness assertion for credit sales: every shipment to a customer that represents a sale should result in a corresponding sales-journal entry. Shipping documents provide persuasive source evidence that goods were shipped, and using documents that are prenumbered permits the entity to account for the numerical sequence. The supervisor can select shipping documents, trace each document to the sales journal, and investigate any document that lacks a recorded sale. Such an exception could indicate that a valid credit sale was omitted from the accounting records. This procedure is especially effective because it begins with the underlying business event—shipment—and traces forward into the accounting records, which is the appropriate direction for testing completeness. AU-C 315 explains that auditors consider relevant assertions, including completeness, when identifying and assessing risks of material misstatement, and AU-C 330 requires audit procedures responsive to those assessed risks. In the revenue cycle, controls linking sequential shipping documentation to recorded sales help management prevent or detect an understatement of revenue and accounts receivable. See the AICPA's [clarified auditing standards resources] and the PCAOB's discussion of [assertions and risk assessment].

QUESTION NO: 59

A practitioner's report on agreed-upon procedures that is in the form of procedures and findings should contain:

A. Negative assurance that the procedures did not necessarily disclose all significant deficiencies in internal control.

B. An acknowledgment of the practitioner's responsibility for the sufficiency of the procedures.

C. A statement of restrictions on the use of the report.

D. A disclaimer of opinion on the entity's financial statements.

ANSWER: C

Explanation:

A statement of restrictions on the use of the report is required in the agreed-upon-procedures reporting framework reflected in this question. An agreed-upon-procedures engagement is performed for specified parties that have agreed to the procedures to be applied. The practitioner reports the procedures performed and the related findings, rather than expressing an audit opinion, a review conclusion, or any other form of assurance. Because parties outside the intended users may not understand why these particular procedures were selected or how to interpret the resulting findings, the report identifies that its use is restricted to the parties that agreed upon the procedures.

The restriction is therefore an essential communication feature of this form of report: it aligns the report's use with the parties' shared understanding of the procedures and the purpose for which they were designed. The report's content is factual and procedure-specific, enabling intended users to evaluate the findings in light of their own agreed needs. AICPA guidance on agreed-upon-procedures engagements is available at AICPA SSAE No. 19 resources. The AICPA's attestation standards resources are also available at AICPA Attestation Standards.

QUESTION NO: 60

An entity with a large volume of customer remittances by mail could most likely reduce the risk of employee misappropriation of cash by using:

A. Employee fidelity bonds.

B. Independently prepared mailroom prelists.

C. Daily check summaries.

D. A bank lockbox system.

ANSWER: D

Explanation:

A bank lockbox system is the most effective control for an entity receiving a large volume of customer remittances by mail because customers send payments directly to a bank-controlled post-office box rather than to the entity's own employees. Bank personnel open the mail, process the remittances, and deposit the funds directly into the entity's bank account. The bank then provides the entity with deposit information, remittance documents, or electronic images that can be used to record and reconcile cash receipts.

This arrangement materially reduces the opportunity for misappropriation because employees who record receivables and perform reconciliations do not take physical custody of customer checks. It also supports segregation of duties: the bank handles initial receipt and deposit, while entity personnel independently record the transaction and reconcile bank activity. For high mail-remittance volume, this control is particularly practical because it centralizes processing and accelerates deposits while limiting employee access to incoming cash receipts. The AICPA's audit-risk framework recognizes that effective controls address risks of material misstatement, including risks arising from asset misappropriation. See the AICPA resources and the COSO internal-control guidance.

QUESTION NO: 61

Which of the following is least likely to aid the auditor in evaluating the risk of improper revenue recognition due to fraud?

A. Analysis of sales commissions over the most recent five-year period.

B. Comparison of sales volume, as determined from recorded revenue amounts, with production capacity.

C. Trend analysis of revenues and sales returns by month.

D. Comparison of revenue reported by month and by product line for the current and prior years.

ANSWER: A

Explanation:

Analysis of sales commissions over the most recent five-year period is least likely to aid the auditor in evaluating the risk of fraudulent revenue recognition. Although commission data can sometimes provide contextual information about sales incentives, commission expense is affected by many factors that do not reflect whether reported revenue is valid, earned, or recorded in the proper period. For example, changes in commission rates, compensation plans, sales-force composition, payment timing, territory assignments, or caps and thresholds can materially change commission trends without indicating a revenue-recognition misstatement.

In a fraud-risk assessment, the auditor seeks procedures that produce more direct, relevant evidence about unusual revenue relationships, unsupported transactions, fictitious sales, premature recognition, or subsequent reversals. A multiyear commission analysis is comparatively indirect and may be difficult to interpret because the relationship between commissions and revenue need not remain stable over time. The applicable auditing standards require the auditor to presume that fraud risks exist in revenue recognition and to evaluate the types of revenue, transactions, and assertions that may create such risks. See the PCAOB's AS 2401, Consideration of Fraud in a Financial Statement Audit and the AICPA's risk assessment standards resources.

QUESTION NO: 62

Which of the following procedures would an auditor most likely include in the initial planning of a financial statement audit?

A. Obtaining a written representation letter from the client's management.

B. Examining documents to detect illegal acts having a material effect on the financial statements.

C. Considering whether the client's accounting estimates are reasonable in the circumstances.

D. Determining the extent of involvement of the client's internal auditors.

ANSWER: D

Explanation:

Determining the extent of involvement of the client's internal auditors is an initial-planning activity because planning requires the auditor to establish the overall audit strategy and develop an audit plan responsive to the engagement's circumstances. As part of that strategy, the auditor considers available resources and how work may be assigned, supervised, and reviewed. When an entity has an internal audit function, the external auditor evaluates whether, and in which audit areas, the work of internal auditors can be used as audit evidence or whether internal auditors may provide direct assistance, when permitted. This decision affects the planned nature, timing, and extent of audit procedures, staffing, coordination, and supervision. The auditor's determination is not automatic: it depends on evaluating the internal audit function's objectivity, competence, and use of a systematic and disciplined approach, including quality control. These considerations must occur early enough to shape an efficient and appropriate audit approach. AU-C section 300 identifies planning activities as establishing the overall audit strategy and audit plan, while AU-C section 610 addresses using the work of internal auditors. See AICPA AU-C 300, Planning an Audit and AICPA AU-C 610, Using the Work of Internal Auditors.

QUESTION NO: 63

In a computerized payroll system environment, an auditor would be least likely to use test data to test controls related to:

A. Missing employee numbers.
Missing employee numbers.

B. Proper approval of overtime by supervisors.

C. Time tickets with invalid job numbers.
Time tickets with invalid job numbers.

D. Agreement of hours per clock cards with hours on time tickets.

Agreement of hours per clock card with hours on time tickets.

ANSWER: B

Explanation:

Proper approval of overtime by supervisors is correct because this control ordinarily depends on evidence of a supervisor's authorization, such as a signature, electronic workflow approval, or review of supporting payroll documentation. Although a payroll application may process overtime hours after they are entered, test data primarily evaluates automated application controls by submitting auditor-designed transactions with known characteristics and observing whether programmed edit checks, validations, calculations, and processing rules operate as intended. The existence and propriety of a supervisor's approval is generally a manual control activity that requires inspection of the approval evidence, inquiry, observation, or reperformance of the approval process rather than merely running data through the system. An auditor must obtain sufficient appropriate audit evidence regarding relevant controls and tailor testing procedures to the nature of the control being tested. Accordingly, where overtime authorization is performed by a person rather than enforced through a programmed system rule, audit procedures directed at the underlying approval documentation provide the relevant evidence. This treatment is consistent with the control-testing principles in AICPA AU-C Section 330 and the discussion of tests of controls in PCAOB AS 2301.

QUESTION NO: 64

Which of the following statements is correct about the auditor's use of the work of a specialist?

A. The specialist should not have an understanding of the auditor's corroborative use of the specialist's findings.

B. The auditor is required to perform substantive procedures to verify the specialist's assumptions and findings.

C. The client should not have an understanding of the nature of the work to be performed by the specialist.

D. The auditor should obtain an understanding of the methods and assumptions used by the specialist.

ANSWER: D

Explanation:

The auditor should obtain an understanding of the methods and assumptions used by the specialist. When audit evidence includes the work of an auditor's specialist, the auditor remains responsible for reaching the audit conclusion and must evaluate whether that work is adequate for the auditor's purposes. That evaluation requires the auditor to understand the nature of the specialist's work and to assess whether the specialist's findings are relevant and reasonable in the circumstances. In particular, the auditor evaluates the appropriateness and reasonableness of significant methods and assumptions used by the specialist, as well as the relevance, completeness, and accuracy of significant source data used in the work. The depth of the auditor's understanding and evaluation is affected by factors such as the significance of the specialist's work to the financial statements, the degree of subjectivity involved, and the risk of material misstatement. This requirement does not transfer the auditor's professional responsibility to the specialist; instead, it enables the auditor to determine whether the specialist's findings provide sufficient appropriate audit evidence. See AICPA AU-C Section 620, Using the Work of an Auditor's Specialist, especially the requirements for evaluating the adequacy of the specialist's work, and the AICPA's Auditing Standards resources.

QUESTION NO: 65

This question consists of an item pertaining to possible deficiencies in an accountant's review report. Jordan & Stone, CPAs, audited the financial statements of Tech Co., a nonissuer, for the year ended December 31, 20X1, and expressed an unqualified opinion. For the year ended December 31, 20X2, Tech issued comparative financial statements. Jordan & Stone reviewed Tech's 20X2 financial statements and Kent, an assistant on the engagement, drafted the accountants' review report below.

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Land reviewed Kent's draft and indicated in the Supervisor's Review Notes below that there were several deficiencies in Kent's draft.

Accountant's Review Report

We have reviewed and audited the accompanying balance sheets of Tech Co. as of December 31, 20X2 and 20X1, and the related statements of income, retained earnings, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants and generally accepted auditing standards. All information included in these financial statements is the representation of the management of Tech Co.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements. Because of the inherent limitations of a review engagement, this report is intended for the information of management and should not be used for any other purpose.

The financial statements for the year ended December 31, 20X1, were audited by us and our report was dated March 2, 20X2. We have no responsibility for updating that report for events and circumstances occurring after that date.

Jordan and Stone, CPAs March 1, 20X3

Supervisor's Review Notes

There should be no reference to "updating the prior year's auditor's report for events and circumstances occurring after that date" in the fourth (separate) paragraph.

A. Correct

B. Incorrect

ANSWER: A

Explanation:

Correct. When comparative financial statements include a current-period review and a prior-period audit performed by the same accountant, and the prior audit report is not reissued, the current review report may include a separate paragraph identifying that the prior-period financial statements were audited, the date of the auditor's report, and the opinion expressed. This provides appropriate context for users regarding the differing levels of service applied to the comparative periods.

However, the separate paragraph is not a mechanism for adding a broad disclaimer that the accountant has no responsibility for updating the earlier audit report for subsequent events and circumstances. The review report addresses the accountant's current reporting responsibilities for the comparative financial statements and should use the reporting elements prescribed by the applicable SSARS requirements. Accordingly, removing the sentence about updating the earlier auditor's report is an appropriate correction to the draft. The AICPA describes review engagements as providing limited assurance through inquiry and analytical procedures and governs reporting for nonissuer review engagements through SSARS, including AR-C section 90. See the AICPA Compilation and Review Services resources and the AICPA SSARS Codification.

QUESTION NO: 66

Which of the following fraudulent activities most likely could be perpetrated due to the lack of effective internal controls in the revenue cycle?

A. Merchandise received is not promptly reconciled to the outstanding purchase order file.

B. Obsolete items included in inventory balances are rarely reduced to the lower of cost or market value.

C. The write-off of receivables by personnel who receive cash permits the misappropriation of cash.

D. Fictitious transactions are recorded that cause an understatement of revenue and overstatement of receivables.

ANSWER: C

Explanation:

The write-off of receivables by personnel who receive cash permits the misappropriation of cash. Cash receipts are a custody function, whereas authorizing or processing accounts-receivable write-offs is a recording and authorization function. Effective revenue-cycle controls segregate these duties so that the person handling customer payments cannot conceal a theft by removing the related customer balance from the accounting records.

For example, an employee who receives a customer's payment could divert the cash instead of depositing it. If that same employee can subsequently approve or record a write-off, the employee can eliminate the outstanding receivable and make the customer account appear settled or uncollectible. This concealment may delay detection because the accounts-receivable subsidiary ledger no longer identifies the customer balance that should have been collected.

Appropriate controls include independent authorization of credit memos and write-offs, restricted system access, timely reconciliation of remittance records to deposits and receivable postings, and management review of write-off trends. These controls address the risk that one individual could both access an asset and alter records concerning that asset. The importance of segregation of duties and controls over authorization is consistent with the PCAOB's discussion of controls over financial reporting in AS 2201 and the COSO Internal Control—Integrated Framework.

QUESTION NO: 67

An auditor confirmed accounts receivable as of an interim date, and all confirmations were returned and appeared reasonable. Which of the following additional procedures most likely should be performed at year-end?

A. Send confirmations for all new customer balances incurred from the interim date to year-end.

B. Resend confirmations for any significant customer balances remaining at year-end.

C. Review supporting documents for new large balances occurring after the interim date, and evaluate any significant changes in balances at year-end.

D. Review cash collections subsequent to the interim date and the year-end.

ANSWER: C

Explanation:

Review supporting documents for new large balances occurring after the interim date, and evaluate any significant changes in balances at year-end. When substantive audit procedures, including receivables confirmations, are performed before the balance-sheet date, the auditor must perform additional procedures covering the remaining period to provide a reasonable basis for extending the interim audit conclusion to year-end. The nature and extent of those procedures depend on the auditor's assessment of risk and the length of the remaining period. A focused review of large new receivable balances and significant changes in existing balances addresses transactions and events occurring after the interim confirmation date that could materially affect the year-end accounts receivable balance. Supporting documentation may include sales invoices, shipping documents, customer orders, and credit files, as appropriate. The auditor also evaluates whether year-end changes are consistent with the entity's business activity and whether they indicate heightened risk related to existence, valuation, or cutoff. This targeted roll-forward work appropriately complements the reliable confirmation evidence obtained at the interim date while concentrating year-end testing on potentially material activity. See the AICPA's clarified auditing standards resources and AU-C section 330's requirements for substantive procedures performed at an interim date, available through the AICPA Professional Standards.

QUESTION NO: 68

Which of the following controls would a company most likely use to safeguard marketable securities when an independent trust agent is not employed?

A. The investment committee of the board of directors periodically reviews the investment decisions delegated to the treasurer.

B. Two company officials have joint control of marketable securities, which are kept in a bank safedeposit box.

C. The internal auditor and the controller independently trace all purchases and sales of marketable securities from the subsidiary ledgers to the general ledger.

D. The chairman of the board verifies the marketable securities, which are kept in a bank safe-deposit box, each year on the balance sheet date.

ANSWER: B

Explanation:

Two company officials have joint control of marketable securities, which are kept in a bank safedeposit box. This is an effective physical safeguarding control because it restricts access to negotiable assets through dual custody. Requiring two authorized officials to act together to obtain the securities makes an unauthorized removal substantially more difficult: a misappropriation would generally require collusion rather than action by one person with sole access. Keeping the certificates in a bank safe-deposit box also provides secure off-premises physical protection against theft, loss, or damage. The control is especially appropriate when an independent trust agent does not hold the securities, because the company must establish an internal custody arrangement that provides comparable protection and accountability. Proper design would include documented authorization, controlled access to the box, and records of deposits and withdrawals, allowing management to maintain responsibility for the securities while reducing the opportunity for unauthorized disposition. This approach reflects the segregation-of-duties and safeguarding concepts underlying internal control: access to assets should be limited to authorized individuals, and responsibilities should be divided so that no single person can both access and conceal a misappropriation. See the [COSO Internal Control—Integrated Framework resources]() and the [PCAOB guidance on internal control over financial reporting]().

QUESTION NO: 69

A CPA in public practice is required to comply with the provisions of the Statements on Standards for Attestation Engagements (SSAE) when:

	Testifying as an expert witness in accounting and auditing matters given stipulated facts	*Compiling a client's financial projection that presents a hypothetical course of action*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

A. Option A

B. Option B

C. Compiling a financial projection, but not testifying as an expert witness.

D. Option D

ANSWER: C

Explanation:

Compiling a financial projection, but not testifying as an expert witness, is correct because a compilation engagement for prospective financial information is governed by the SSAEs. A financial projection is prospective financial information that presents an entity's expected financial position, results of operations, or cash flows based on one or more hypothetical assumptions. When a practitioner is engaged to compile that projection, the practitioner applies the relevant SSAE requirements, including obtaining an understanding of the engagement, agreeing on the terms with the responsible party, and issuing an appropriate compilation report. The compilation report communicates that the CPA has not examined or reviewed the prospective financial information and therefore does not provide an opinion or conclusion on it. The standards also establish requirements for presentation and disclosure appropriate to prospective financial information, so users understand the hypothetical nature of the assumptions underlying a projection. These requirements are part of the attestation standards framework rather than merely general consulting guidance. The AICPA's attestation standards resources are available at AICPA Attestation Standards. The AICPA's Professional Standards access and standards resources can also be found at AICPA Professional Standards.

QUESTION NO: 70

An auditor has determined that a misstatement is material but not pervasive to an entity's financial statements. Management refuses to correct the misstatement. The auditor should express a:

A. Qualified opinion.

B. Disclaimer of opinion.

C. Adverse opinion.

D. Unmodified opinion with an emphasis-of-matter paragraph.

ANSWER: A

Explanation:

Qualified opinion is appropriate when the auditor concludes that the financial statements are materially misstated but the effects of the misstatement are not pervasive. The auditor describes the matter in a Basis for Qualified Opinion section and states that, except for the effects of the matter described, the financial statements are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

An adverse opinion is required only when the auditor concludes that misstatements are both material and pervasive. A disclaimer is associated with an inability to obtain sufficient appropriate audit evidence, rather than an identified misstatement. AU-C section 705 addresses modifications to the opinion in the independent auditor's report.

QUESTION NO: 71

An auditor concludes that there is a material inconsistency in the other information in an annual report to shareholders containing audited financial statements. The auditor believes that the financial statements do not require revision, but the client is unwilling to revise or eliminate the material inconsistency in the other information. Under these circumstances, what action would the auditor most likely take?

A. Consider the situation closed because the other information is not in the audited financial statements.

B. Issue an "except for" qualified opinion after discussing the matter with the client's audit committee.

C. Disclaim an opinion on the financial statements after explaining the material inconsistency in a separate explanatory paragraph.

D. Revise the auditor's report to include a separate explanatory paragraph describing the material inconsistency.

ANSWER: D

Explanation:

“Revise the auditor's report to include a separate explanatory paragraph describing the material inconsistency.” is correct. Under AU-C 720, an auditor must read other information included in documents containing audited financial statements and consider whether that information is materially inconsistent with the financial statements or contains a material misstatement of fact. This responsibility applies even though the other information is not itself subject to audit. Here, the auditor has concluded that the financial statements are not misstated and therefore do not need revision. The issue instead is the unresolved material inconsistency in the accompanying other information. Because management will not correct or remove it, the auditor should communicate the matter to those charged with governance and take action to alert users. If the auditor’s report has not yet been released, the appropriate response is to modify the report by adding a separate other-matter paragraph that describes the material inconsistency. The paragraph makes clear that the matter concerns the accompanying other information rather than the audited financial statements and provides users with relevant context before relying on the annual report as a whole. This treatment follows the auditor’s required response to uncorrected material inconsistencies in other information. See AICPA Statement on Auditing Standards No. 118, Other Information in Documents Containing Audited Financial Statements and AICPA Audit and Attest Standards resources.

QUESTION NO: 72

An entity's internal control requires for every check request that there be an approved voucher, supported by a prenumbered purchase order and a prenumbered receiving report. To determine whether checks are being issued for unauthorized expenditures, an auditor most likely would select items for testing from the population of all:

A. Purchase orders.

B. Canceled checks.

C. Receiving reports.

D. Approved vouchers.

ANSWER: B

Explanation:

Canceled checks. is correct because the audit objective is to test whether disbursements that actually occurred were authorized and supported by the entity’s required documentation. The relevant population is therefore the population of payments made—represented by canceled checks (or, in modern electronic-payment environments, cleared disbursements). Starting with each canceled check and tracing backward to the approved voucher, purchase order, and receiving report tests whether an issued check has the prescribed authorization and evidence of a valid purchase and receipt of goods or services. This direction of testing addresses the risk that a disbursement was made without required support, including payments for fictitious, unreceived, or otherwise unauthorized items. It is a test of controls and transaction authorization designed around the occurrence of the cash disbursement. Audit procedures commonly use vouching from recorded transactions or disbursements to underlying source documents when the concern is whether recorded or paid transactions are valid, authorized, and supported. The AICPA’s auditing standards require auditors to obtain sufficient appropriate audit evidence by designing and performing procedures responsive to assessed risks; selecting payments made and inspecting the related authorization documents provides relevant evidence for this control objective. See AICPA Clarified Statements on Auditing Standards and PCAOB AS 2315, Audit Sampling.

QUESTION NO: 73

For a nonissuer, a previously communicated significant deficiency that has not been corrected, ordinarily should be communicated again:

A. Only if the deficiency has a material effect on the auditor's assessment of control risk.

B. Unless the entity accepts that degree of risk because of cost-benefit considerations.

C. Only if the deficiency is considered a material weakness.

D. In writing, during the current audit.

ANSWER: D

Explanation:

“In writing, during the current audit.

” is correct. Under AU-C section 265, the auditor must communicate significant deficiencies and material weaknesses identified during an audit to those charged with governance in writing. When a significant deficiency was communicated in an earlier audit and remains uncorrected, it ordinarily remains relevant to the current audit because it continues to represent a control issue that merits the attention of governance. Accordingly, the auditor ordinarily communicates the matter again in the current audit’s written internal-control communication. This recurring communication helps ensure that those charged with governance remain informed of unresolved deficiencies and can continue to evaluate remediation, oversight, and related risks. The communication is tied to the auditor’s current audit responsibilities and is not contingent on a separate reassessment or on management’s prior acceptance of the risk. AU-C 265 also establishes a timeliness requirement: written communication should be made no later than 60 days following the report-release date. The AICPA’s auditing standards, including AU-C section 265, are available through the AICPA Auditing Standards resources. Additional context on the auditor’s communication responsibilities can be found in the AICPA audit and accounting guidance resources.

QUESTION NO: 74

An audit partner is developing an office training program to familiarize his professional staff with statistical decision models applicable to the audit of dollar value balances. He wishes to demonstrate the relationship of sample sizes to population size and variability and the auditor's specifications as to tolerable misstatement and risk of incorrect acceptance. The partner prepared the following table to show comparative population characteristics and audit specifications of two populations.

	Characteristics of Population 1 Relative to Population 2		Audit Specifications as to a Sample from Population 1 Relative to a Sample from Population 2	
	Size	Variability	Specified Tolerable Misstatement	Specified Risk of Incorrect Acceptance
Case 1	Equal	Equal	Equal	Lower
Case 2	Equal	Larger	Larger	Equal
Case 3	Larger	Equal	Smaller	Higher
Case 4	Smaller	Smaller	Equal	Higher
Case 5	Larger	Equal	Equal	Lower

You are to indicate for the specified case from the above table the required sample size to be selected from population 1 relative to the sample from population 2. In case 3 the required sample size from population 1 is:

A. Larger than the required sample size from population 2.

B. Equal to the required sample size from population 2.

C. Smaller than the required sample size from population 2.

D. Indeterminate relative to the required sample size from population 2.

ANSWER: D

Explanation:

“Indeterminate relative to the required sample size from population 2.” is correct because case 3 changes audit specifications in opposing directions. A lower tolerable misstatement requires greater assurance that the sample will detect a material population misstatement and therefore tends to increase the required sample size. At the same time, a higher acceptable risk of incorrect acceptance permits the auditor to accept more sampling risk, which tends to decrease the required sample size. Without the applicable numerical values and the statistical model's resulting calculations, the relative magnitude of those offsetting effects cannot be known. Consequently, the information provided does not establish whether the sample from population 1 must be larger, smaller, or the same as the sample from population 2. Audit sampling standards require sample size to be sufficient to reduce sampling risk to an acceptably low level and recognize that sample size is affected by the auditor's assessed risk and tolerable misstatement. See the AICPA's Audit and Attest Standards and PCAOB AS 2315, Audit Sampling.

QUESTION NO: 75

Which of the following factors is most important concerning an auditor's responsibility to detect errors and fraud?

A. The susceptibility of the accounting records to intentional manipulations, alterations, and the misapplication of accounting principles.

B. The probability that unreasonable accounting estimates result from unintentional bias or intentional attempts to misstate the financial statements.

C. The possibility that management fraud, defalcations, and the misappropriation of assets may indicate the existence of illegal acts.

D. The risk that mistakes, falsifications, and omissions may cause the financial statements to contain material misstatements.

ANSWER: D

Explanation:

The risk that mistakes, falsifications, and omissions may cause the financial statements to contain material misstatements is correct because the auditor's fundamental responsibility is to obtain reasonable assurance that the financial statements as a whole are free of material misstatement, whether caused by fraud or error. Materiality is central to this responsibility: an auditor plans and performs procedures to address misstatements that, individually or in the aggregate, could reasonably be expected to influence users' economic decisions based on the financial statements. Fraud may involve intentional falsification, concealment, or omission, while errors are unintentional misstatements; both are relevant when they create a risk of material misstatement. The auditor is not an insurer or guarantor that every error or fraud will be found. Rather, the auditor applies professional skepticism, assesses risks, designs responsive audit procedures, and evaluates audit evidence to reduce audit risk to an acceptably low level. This focus on material misstatement properly connects the nature of errors and fraud with the objective of a financial statement audit. The AICPA's clarified auditing standards describe this reasonable-assurance objective in its Clarified Statements on Auditing Standards; comparable authoritative guidance is also stated in PCAOB AS 1015, Due Professional Care in the Performance of Work.

QUESTION NO: 76

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

A. Recomputing a sample of large-dollar transactions occurring after year-end for arithmetic accuracy.

B. Investigating changes in stockholders' equity occurring after year-end.

C. Inquiring of the entity's legal counsel concerning litigation, claims, and assessments arising after yearend.

D. Confirming bank accounts established after year-end.

ANSWER: C

Explanation:

Inquiring of the entity's legal counsel concerning litigation, claims, and assessments arising after yearend is an appropriate subsequent-events procedure because legal matters may arise, become known, or materially develop after the balance-sheet date but before the auditor's report is issued. The auditor needs sufficient appropriate evidence to determine whether such matters require adjustment of amounts or disclosures in the financial statements, or whether they reveal conditions that existed at the financial-statement date. Management's representations and internal records may not fully identify the status, likelihood, or potential financial effect of legal contingencies. Direct communication with legal counsel can provide evidence about pending or threatened litigation, unasserted claims that counsel believes are likely to be asserted and require disclosure, the progress of matters after year-end, and estimates of possible loss where available. This inquiry therefore directly addresses events and conditions occurring through the subsequent-events review period and supports the auditor's evaluation under the subsequent-events auditing standard. The AICPA's clarified auditing standards include the requirements for auditing subsequent events in AU-C section 560, Subsequent Events and Subsequently Discovered Facts. Related requirements for obtaining audit evidence regarding litigation, claims, and assessments are addressed in AU-C section 501.

QUESTION NO: 77

When using classical variables sampling for estimation, an auditor normally evaluates the sampling results by calculating the possible error in either direction. This statistical concept is known as:

A. Precision.

B. Reliability.

C. Projected error.

D. Standard deviation.

ANSWER: A

Explanation:

Precision. is correct. In classical variables sampling, the auditor uses sample results to estimate a monetary characteristic of a population, such as its recorded or audited value. The resulting point estimate alone does not fully communicate the uncertainty inherent in drawing a sample rather than examining every item. Accordingly, the auditor calculates an allowance around that estimate for sampling risk. Precision expresses the possible amount by which the actual population value may differ from the estimate, in either direction, at a selected confidence (reliability) level. It is therefore commonly described as the half-width of the confidence interval: the estimated misstatement or population value is presented with a plus-or-minus amount representing precision. This calculation enables the auditor to assess whether the range of reasonably possible population misstatement is compatible with the tolerable misstatement established for the audit. The AICPA's audit sampling guidance discusses evaluating sample results, including projecting misstatements and considering sampling risk when forming conclusions. See the AICPA clarified auditing standards and the AICPA's Audit Sampling Guide.

QUESTION NO: 78

When an entity uses a trust company as custodian of its marketable securities, the possibility of concealing fraud most likely would be reduced if the:

A. Trust company has no direct contact with the entity employees responsible for maintaining investment accounting records.

B. Securities are registered in the name of the trust company, rather than the entity itself.

C. Interest and dividend checks are mailed directly to an entity employee who is authorized to sell securities.

D. Trust company places the securities in a bank safe-deposit vault under the custodian's exclusive control.

ANSWER: A

Explanation:

“Trust company has no direct contact with the entity employees responsible for maintaining investment accounting records” is correct because it strengthens segregation of duties between the independent custodian and the personnel who record and reconcile investment transactions. The trust company’s custody records provide an independent source of evidence regarding securities held, purchases, sales, and related activity. Restricting direct contact with employees who maintain the investment accounting records makes it more difficult for those employees to coordinate, alter, or suppress custodial information in a way that conceals an unauthorized transaction or a misstatement in the entity’s records.

An effective reconciliation control depends on comparing the entity’s accounting records with information obtained independently from the custodian. This structure supports reliable detection because the employee performing the reconciliation can identify discrepancies between the ledger and the trust company’s statements or confirmations without the accounting-records personnel influencing the custodian’s communications. More broadly, internal-control frameworks emphasize separating custody, recordkeeping, authorization, and reconciliation functions to reduce opportunities both to commit and to conceal improper activity. The GAO’s Standards for Internal Control in the Federal Government discusses segregation of duties as a key control activity, and the PCAOB’s AS 2201 addresses evaluating controls that prevent or detect material misstatements.

QUESTION NO: 79

In connection with a proposal to obtain a new client, an accountant in public practice is asked to prepare a written report on the application of accounting principles to a specific transaction. The accountant's report should include a statement that:

A. Any difference in the facts, circumstances, or assumptions presented may change the report.

B. The engagement was performed in accordance with Statements on Standards for Consulting Services.

C. The guidance provided is for management use only and may not be communicated to the prior or continuing auditors.

D. Nothing came to the accountant's attention that caused the accountant to believe that the accounting principles violated GAAP.

ANSWER: A

Explanation:

“Any difference in the facts, circumstances, or assumptions presented may change the report.” is correct because a report on the application of an accounting principle to a specific transaction is necessarily based on the particular facts, circumstances, and assumptions supplied to the accountant. The report is not a general conclusion that can automatically be applied if the transaction changes or if additional relevant facts emerge. Accordingly, the accountant must explicitly alert the specified users that the conclusion could differ when the underlying information differs from that considered in forming the conclusion.

This disclosure appropriately defines the conditional nature and scope of the accountant’s professional judgment. It helps prevent a report prepared in connection with a prospective client relationship from being relied upon as though it addressed all possible variations of the transaction. The requirement is consistent with the reporting guidance in AU-C section 915, which addresses reports on the application of an applicable financial reporting framework, including required report content and restricted use. See the AICPA AU-C section 915 guidance and the AICPA’s Audit and Attest Standards resources.

QUESTION NO: 80

Which of the following controls is most likely to prevent the improper disposition of equipment?

A. A separation of duties between those authorized to dispose of equipment and those authorized to approve removal work orders.

B. The use of serial numbers to identify equipment that could be sold.

C. Periodic comparison of removal work orders to authorizing documentation.

D. A periodic analysis of the scrap sales and the repairs and maintenance accounts.

ANSWER: A

Explanation:

A separation of duties between those authorized to dispose of equipment and those authorized to approve removal work orders is the control most likely to prevent an improper equipment disposition. Equipment removals ordinarily begin with a work order or similar authorization documenting the legitimate business reason for taking an asset out of service. Requiring an independent person to approve that authorization, while assigning disposal authority to a different person, means that no one individual can both initiate an unsupported removal and direct the asset's sale, transfer, scrap, or other disposition. This division creates a preventive authorization checkpoint before the asset leaves the entity's custody and makes collusion necessary to bypass the control. It also promotes clear accountability for the asset's physical movement and ultimate disposition. The GAO's internal-control framework identifies segregation of duties as a key control activity and specifically emphasizes separating incompatible responsibilities such as authorization, custody, and recordkeeping. The COSO framework likewise describes control activities, including segregation of duties, as actions designed to mitigate risks to acceptable levels. See the GAO Standards for Internal Control in the Federal Government and COSO Internal Control—Integrated Framework.

QUESTION NO: 81

Which of the following statements is correct regarding the auditor's consideration of the possibility of illegal acts by clients?

A. The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance that no illegal acts have been committed by clients.

B. The auditor's training, experience, and understanding of the client should be used to provide a basis for the determination as to whether illegal acts have occurred.

C. If specific information concerning an illegal act comes to the auditor's attention, the auditor should apply audit procedures specifically directed to ascertaining whether an illegal act has occurred.

D. If an illegal act has occurred, the auditor should express a qualified opinion or an adverse opinion on the financial statements taken as a whole.

ANSWER: C

Explanation:

If specific information concerning an illegal act comes to the auditor's attention, the auditor should apply audit procedures specifically directed to ascertaining whether an illegal act has occurred. Under AU-C section 250, an auditor is not expected to possess legal expertise or to identify every instance of noncompliance with laws and regulations. Nevertheless, information suggesting possible noncompliance creates an audit responsibility to investigate the matter sufficiently. The auditor should obtain an understanding of the nature and circumstances of the matter and gather additional information to evaluate its possible effect on the financial statements. Depending on the facts, appropriate procedures can include examining supporting documentation, making inquiries of management and those charged with governance, consulting legal counsel when appropriate, and evaluating whether related liabilities, loss contingencies, disclosures, or other financial-statement effects have been properly recognized or disclosed. This focused response is necessary because an illegal act may produce a material misstatement even when the matter does not initially appear in the accounting records. The auditor's ultimate concern is the effect of the matter on the financial statements and the audit opinion. See the AICPA's auditing standards resources and the closely corresponding PCAOB guidance on illegal acts by clients.

QUESTION NO: 82

In assessing the objectivity of internal auditors, the independent CPA who is auditing the entity's financial statements most likely would consider the:

A. Internal auditing standards developed by The Institute of Internal Auditors.

B. Tests of internal control activities that could detect errors and fraud.

C. Materiality of the accounts recently inspected by the internal auditors.

D. Results of the tests of transactions recently performed by the internal auditor.

ANSWER: A

Explanation:

“Internal auditing standards developed by The Institute of Internal Auditors.” is correct because those professional standards establish the expected framework for an internal audit function’s independence and objectivity. When an independent auditor considers using internal auditors’ work, the auditor must evaluate whether the internal audit function can perform its responsibilities with sufficient objectivity. Relevant considerations include the internal audit function’s organizational status, whether it reports at an appropriate level within the entity, and whether policies protect internal auditors from auditing activities for which they have operational responsibility. Professional internal auditing standards are pertinent because they articulate these safeguards and provide a benchmark for evaluating how the function is structured and governed. The independent auditor may also obtain information through discussions with management, prior experience with the function, and any available external quality assessments. This assessment supports the auditor’s determination of the extent to which internal-audit work may be used in the financial-statement audit, while preserving the independent auditor’s sole responsibility for the audit opinion. See the AICPA’s guidance on using the work of internal auditors at AU-C Section 610 and the Institute of Internal Auditors’ Global Internal Audit Standards.

QUESTION NO: 83

Moore, CPA, has been asked to issue a review report on the balance sheet of Dover Co., a nonissuer.

Moore will not be reporting on Dover's statements of income, retained earnings, and cash flows. Moore may issue the review report provided the:

A. Balance sheet is presented in a prescribed form of an industry trade association.

B. Scope of the inquiry and analytical procedures has not been restricted.

C. Balance sheet is not to be used to obtain credit or distributed to creditors.

D. Specialized accounting principles and practices of Dover's industry are disclosed.

ANSWER: B

Explanation:

“Scope of the inquiry and analytical procedures has not been restricted.” is correct. Under SSARS, an accountant may perform a review engagement on a single financial statement or on specified elements, accounts, or items of a financial statement. A balance sheet is therefore eligible to be the subject of a standalone review report even when the accountant is not engaged to review the related income statement, statement of retained earnings (or equity), or cash flow statement. The critical condition is that the accountant must be able to perform the review procedures considered necessary in the circumstances. Those procedures include making inquiries of management and performing analytical procedures, as well as obtaining sufficient appropriate review evidence to provide limited assurance that the accountant is unaware of material modifications needed for the financial statement to conform with the applicable financial reporting framework. If management restricts the accountant’s inquiries or analytical procedures, the accountant cannot simply issue the standard review conclusion because the engagement scope has been limited. The review report should also clearly identify the specific financial statement reviewed—here, Dover’s balance sheet—and describe the applicable reporting framework. This treatment is consistent with AR-C section 90, which addresses reviews of financial statements and permits engagements involving a single financial statement. See AICPA: Compilation, Review, and Preparation Engagements and AICPA SSARS No. 21 resources.

QUESTION NO: 84

Green, CPA, is requested to render an opinion on the application of accounting principles by an entity that is audited by another CPA. Green may:

A. Not accept such an engagement because to do so would be considered unethical.

B. Not accept such an engagement because Green would lack the necessary information on which to base an opinion without conducting an audit.

C. Accept the engagement but should form an independent opinion without consulting with the continuing CPA.

D. Accept the engagement but should consult with the continuing CPA to ascertain all the available facts relevant to forming a professional judgment.

ANSWER: D

Explanation:

“Accept the engagement but should consult with the continuing CPA to ascertain all the available facts relevant to forming a professional judgment.

” is correct. A CPA in public practice may be asked to provide an opinion on the application of accounting principles to a specific transaction or circumstance for an entity whose financial statements are audited by another CPA. This type of engagement is permissible; the fact that another practitioner audits the entity does not itself create an ethical prohibition or require Green to perform a separate audit.

Before reaching and communicating a professional conclusion, however, Green should consult with the continuing CPA—the accountant currently engaged to audit the entity. That consultation helps Green obtain the relevant facts and understand matters that may affect the accounting conclusion, including the entity’s circumstances, prior accounting treatment, and other information known through the audit relationship. Green then uses the available facts and applicable financial reporting framework to exercise independent professional judgment. Consultation is an important professional-ethics safeguard because an accounting conclusion based on incomplete facts could be misleading or inappropriate.

This treatment is consistent with the AICPA Code of Professional Conduct’s guidance addressing opinions on financial statements and the importance of obtaining relevant information when another accountant has an ongoing engagement. See the AICPA Code of Professional Conduct and the AICPA Professional Ethics resources.

QUESTION NO: 85

Dunn, CPA, is auditing the financial statements of Taft Co. Taft uses Quick Service Center (QSC) to process its payroll. Price, CPA, is expressing an opinion on a description of the controls placed in operation at QSC regarding the processing of its customers' payroll transactions. Dunn expects to consider the effects of Price's report on the Taft engagement. Price's report should contain a (an):

A. Description of the scope and nature of Price's procedures.

B. Statement that Dunn may assess control risk based on Price's report.

C. Assertion that Price assumes no responsibility to determine whether QSC's controls are suitably designed.

D. Opinion on the operating effectiveness of QSC's internal controls.

ANSWER: A

Explanation:

Description of the scope and nature of Price's procedures. is correct. Price is functioning as a service auditor and is reporting on QSC’s description of its system and the controls that were placed in operation as of a specified date. This is analogous to a SOC 1 Type 1 engagement: the service auditor expresses an opinion on whether the system description is fairly presented and whether the controls were suitably designed to achieve the stated control objectives at that date. To make the report understandable and useful to user auditors such as Dunn, the service auditor’s report identifies the nature and scope of the examination procedures performed. That description communicates the basis for Price’s opinion and the level of assurance obtained. In a current SOC reporting framework, the report also describes the relevant system, the applicable control objectives, and the criteria used in the engagement. The AICPA describes a SOC 1 Type 1 report as addressing the fairness of the presentation of management’s system description and the suitability of the design of controls as of a specified date. See the AICPA SOC suite of services overview and the AICPA service organization reporting resources.

QUESTION NO: 86

Audit documentation prepared by an auditor in connection with an audit engagement is the property of the:

A. Auditor.

B. Entity whose financial statements are audited.

C. Entity's audit committee.

D. Regulatory agency having jurisdiction over the entity.

ANSWER: A

Explanation:

Audit documentation is the property of the auditor. Although the documentation may contain client-provided information and is subject to confidentiality requirements, the client does not own the auditor's working papers. The auditor is responsible for retaining audit documentation for a sufficient period to meet professional standards, legal requirements, and the firm's policies. See AU-C Section 230, Audit Documentation.

QUESTION NO: 87

Which of the following factors most likely would cause a CPA to not accept a new audit engagement?

A. The prospective client has already completed its physical inventory count.

B. The CPA lacks an understanding of the prospective client's operations and industry.

C. The CPA is unable to review the predecessor auditor's audit documentation.

D. The prospective client is unwilling to make all financial records available to the CPA.

ANSWER: D

Explanation:

The prospective client is unwilling to make all financial records available to the CPA is correct because management’s acceptance of responsibility for preparing the financial statements and providing the auditor with access to all information relevant to their preparation is a fundamental precondition to an audit. Before accepting an engagement, the auditor must determine whether those preconditions are present and whether management is sufficiently trustworthy to support a reasonable expectation that it will cooperate throughout the audit. A client’s refusal to provide all financial records creates a scope limitation that may prevent the auditor from obtaining sufficient appropriate audit evidence. It also raises serious concerns about management integrity and whether information may be withheld deliberately. If management imposes such a limitation before engagement acceptance and the auditor believes it would likely require a disclaimer of opinion, the auditor generally should not accept the engagement unless law or regulation requires acceptance. Accordingly, an unwillingness to make all financial records available is a strong basis for declining a prospective audit client. See PCAOB AS 2101, Audit Planning and AICPA Clarified Statements on Auditing Standards.

QUESTION NO: 88

Payroll Data Co. (PDC) processes payroll transactions for a retailer. Cook, CPA, is engaged to express an opinion on a description of PDC's internal controls placed in operation as of a specific date. These controls are relevant to the retailer's internal control, so Cook's report may be useful in providing the retailer's independent auditor with information necessary to plan a financial statement audit. Cook's report should:

A. Contain a disclaimer of opinion on the operating effectiveness of PDC's controls.

B. State whether PDC's controls were suitably designed to achieve the retailer's objectives.

C. Identify PDC's controls relevant to specific financial statement assertions.

D. Disclose Cook's assessed level of control risk for PDC.

ANSWER: A

Explanation:

“Contain a disclaimer of opinion on the operating effectiveness of PDC's controls.” is correct because the engagement described is a SOC 1 Type 1 examination: the service auditor reports on management’s description of the service organization’s system and on the suitability of the design of controls as of a specified date. A Type 1 report addresses whether the controls were placed in operation and suitably designed to provide reasonable assurance that the relevant service commitments and system requirements would be achieved if the controls operate as designed. It does not include tests of controls over a period of time and does not provide an opinion on their operating effectiveness. Accordingly, the report must make clear that no opinion is expressed on operating effectiveness. This distinction is important to the retailer’s auditor because a Type 1 report can assist in understanding the service organization’s controls and in planning the audit, but it cannot by itself provide audit evidence supporting a reduced assessed level of control risk based on operating effectiveness. A SOC 1 Type 2 examination, by contrast, includes tests of controls and reports on operating effectiveness throughout a specified period. The AICPA describes the SOC reporting framework at AICPA SOC Suite of Services; related user-auditor considerations are addressed in AICPA Clarified Statements on Auditing Standards.

QUESTION NO: 89

An auditor who wishes to capture an entity's data as transactions are processed and continuously test the entity's computerized information system most likely would use which of the following techniques?

A. Snapshot application.

B. Embedded audit module.

C. Integrated data check.

D. Test data generator.

ANSWER: B

Explanation:

Embedded audit module. is correct because it is audit code incorporated into the entity’s application program that identifies, selects, and records specified transactions or transaction attributes while normal processing occurs. This permits the auditor to obtain information continuously, rather than only at a particular point in time or from a separately prepared population. The module can be designed to flag transactions meeting audit-defined criteria, capture relevant processing details, and create an audit trail for subsequent evaluation. Accordingly, it is particularly useful where the auditor needs ongoing evidence about the operation of automated processing and controls in a computerized information system.

This approach supports the auditor’s responsibility to obtain sufficient appropriate audit evidence using procedures responsive to assessed risks. Information captured through the module may help the auditor evaluate whether transactions were processed as intended throughout the period and investigate exceptions identified by the programmed selection criteria. The auditor should plan, test, control access to, and evaluate the reliability of the module and its resulting data, because the evidence remains dependent on the design and operation of the underlying system. The AICPA’s audit-evidence standard addresses the need for sufficient appropriate evidence, including evidence produced by the entity’s information systems: AU-C Section 500, Audit Evidence. Related requirements for responding to risks through audit procedures appear in AU-C Section 330.

QUESTION NO: 90

What is an auditor's responsibility for supplementary information required by the GASB that is placed outside the basic financial statements?

A. Label the information as unaudited and expand the auditor's report to include a disclaimer on the information.

B. Add an explanatory paragraph to the auditor's report and refer to the information as "required supplementary information."

C. Apply limited procedures to the information and report deficiencies in, or the omission of, the information.

D. Audit the required supplementary information in accordance with generally accepted governmental auditing standards.

ANSWER: C

Explanation:

“Apply limited procedures to the information and report deficiencies in, or the omission of, the information.” is correct because GASB-required supplementary information is not part of the basic financial statements on which the auditor expresses the primary audit opinion. Nevertheless, when management presents required supplementary information, auditing standards require the auditor to perform specified limited procedures. These procedures generally include inquiries of management about how the information was prepared, determining whether it was prepared using prescribed methods, comparing the information for consistency with management’s responses and the audited financial statements, and considering whether the presentation conforms to applicable GASB guidelines. The auditor does not obtain the level of assurance provided in an audit of the basic financial statements solely by performing these limited procedures. The auditor’s report ordinarily identifies the required supplementary information and describes the limited nature of the procedures performed. If the required information is omitted, materially deficient, or the auditor cannot complete the prescribed procedures, the auditor communicates that matter in the report as required by the applicable reporting standard. This approach gives financial-statement users appropriate context about information that GASB requires to accompany governmental financial statements while preserving the distinction between the audited basic statements and required supplementary information. See AICPA Clarified Statements on Auditing Standards and GASB.

QUESTION NO: 91

Which of the following statements about performing tests of controls to support a lower level of control risk is not true?

A. Observation by the auditor provides more assurance than inquiry alone.

B. Inquiry alone generally will support a conclusion for a lower assessed level of control risk.

C. Prior audits may be considered by the auditor in assessing control risk in the current audit.

D. An audit of financial statements is a cumulative process.

ANSWER: B

Explanation:

Inquiry alone generally will support a conclusion for a lower assessed level of control risk is the statement that is not true. When an auditor plans to rely on the operating effectiveness of controls and thereby assess control risk below the maximum level, the auditor must obtain sufficient appropriate audit evidence through tests of controls. Inquiry can contribute to the auditor’s understanding of how a control is designed and performed, but it is ordinarily not sufficient by itself to establish that the control operated effectively throughout the relevant period. The persuasiveness of evidence is enhanced by combining inquiry with other procedures, such as inspection of documentation, observation of control performance, reperformance, or examination of evidence that the control operated. The nature, timing, and extent of these procedures are based on the control being tested and the intended degree of reliance. This principle supports a sound assessment of control risk and an appropriately tailored substantive audit approach. The AICPA’s auditing standards describe the auditor’s responsibilities for obtaining audit evidence and responding to assessed risks; see the AICPA Audit and Attest Standards and the PCAOB standard on responses to risks of material misstatement.

QUESTION NO: 92

A registration statement filed with the SEC contains the reports of two independent auditors on their audits of financial statements for different periods. The predecessor auditor who audited the prior-period financial statements generally should obtain a letter of representation from the:

A. Successor independent auditor.

B. Client's audit committee.

C. Principal underwriter.

D. Securities and Exchange Commission.

ANSWER: A

Explanation:

The correct answer is **Successor independent auditor.** When a predecessor auditor's report on prior-period financial statements is included in an SEC registration statement, the predecessor auditor generally performs specified procedures before reissuing or consenting to the inclusion of that report. Those procedures include reading the current-period financial statements, comparing the prior-period financial statements on which the predecessor reported with the comparative information being presented, and obtaining written representations. The predecessor obtains a representation letter from current management concerning matters such as changes to prior representations and subsequent events that could affect the prior-period financial statements. The predecessor also obtains a representation letter from the successor independent auditor. The successor's letter provides information about whether the successor's audit or other work identified matters that might have a material effect on the prior-period financial statements or the predecessor auditor's report. This communication is important because the successor auditor has performed audit work on the later period and may be aware of developments relevant to the financial statements covered by the predecessor's report. The applicable guidance is found in AU-C section 560, which addresses subsequent discovery of facts and reissuance of previously issued audit reports, and SEC rules governing accountant consents in registration statements. See PCAOB AU 561 and SEC Rule 436.

QUESTION NO: 93

When auditing an entity's financial statements in accordance with Government Auditing Standards (the Yellow Book), an auditor is required to report on:

I. Recommendations for actions to improve operations.

II. The scope of the auditor's tests of compliance with laws and regulations.

A. I only.

B. II only.

C. Both I and II.

D. Neither I nor II.

E. Recommendations for actions to improve operations.
II. The scope of the auditor's tests of compliance with laws and regulations.

ANSWER: B

Explanation:

II only. is correct. In a financial audit performed under Government Auditing Standards (GAGAS), the auditor's reporting responsibilities extend beyond the opinion on the financial statements. GAGAS requires the auditor to issue a report describing the scope of the auditor's testing of compliance with provisions of laws, regulations, contracts, and grant agreements that could have a material effect on the financial statements. The report also communicates the results of those tests. This reporting gives financial-statement users, oversight bodies, and grantors important context about the nature of the compliance work performed and whether matters requiring communication were identified.

The compliance report may be presented as part of the financial-audit report or in a separate report. Its purpose is not to provide an opinion on compliance unless the auditor was specifically engaged to perform such an audit and applicable criteria support that opinion. Rather, it transparently states the scope and results of the compliance testing performed in connection with the financial audit. This requirement is set out in the GAO's GAGAS financial-audit reporting standards, which address reporting on internal control and compliance. See the GAO Government Auditing Standards (Yellow Book), particularly the financial-audit reporting provisions, and the GAO Yellow Book resource page.

QUESTION NO: 94

Which of the following procedures would an auditor most likely perform during an audit engagement's overall review stage in formulating an opinion on an entity's financial statements?

A. Obtain assurance from the entity's attorney that all material litigation has been disclosed in the financial statements.

B. Verify the clerical accuracy of the entity's proof of cash and its bank cutoff statement.

C. Determine whether inadequate provisions for the safeguarding of assets have been corrected.

D. Consider whether the results of audit procedures affect the assessment of the risk of material misstatement due to fraud.

ANSWER: D

Explanation:

“Consider whether the results of audit procedures affect the assessment of the risk of material misstatement due to fraud.” is the procedure most likely performed in the overall review stage. The completion phase requires the auditor to step back and evaluate the accumulated results of the audit before forming an opinion. That evaluation includes considering whether information obtained throughout the engagement, including identified misstatements, unusual relationships, contradictory evidence, or changes in conditions, indicates that the original fraud-risk assessment should be revised. Fraud risk is not a one-time planning conclusion; it is assessed and reconsidered as audit evidence is gathered. If audit results indicate a previously unrecognized fraud risk or suggest that planned procedures were insufficient, the auditor must respond appropriately, including modifying further audit procedures when necessary. This concluding assessment supports the auditor’s overall determination of whether sufficient appropriate audit evidence has been obtained and whether the financial statements are materially misstated. The AICPA’s auditing standards resources describe the auditor’s responsibilities under generally accepted auditing standards, including risk assessment and evidence evaluation: AICPA Audit and Attest Standards. The comparable fraud standard also explicitly requires auditors to reassess fraud risk as audit evidence is obtained: PCAOB AS 2401, Consideration of Fraud in a Financial Statement Audit.

QUESTION NO: 95

Which of the following procedures would an auditor ordinarily perform first in evaluating management's accounting estimates for reasonableness?

A. Develop independent expectations of management's estimates.

B. Consider the appropriateness of the key factors or assumptions used in preparing the estimates.

C. Test the calculations used by management in developing the estimates.

D. Obtain an understanding of how management developed its estimates.

ANSWER: D

Explanation:

“Obtain an understanding of how management developed its estimates.” is the procedure ordinarily performed first. Before the auditor can assess whether an accounting estimate is reasonable, the auditor needs to understand management’s process for making it. This understanding includes the method or model selected, the significant data used, relevant assumptions, the degree of estimation uncertainty, the use of specialists or complex techniques where applicable, and the controls over the development and approval of the estimate. It establishes the basis for identifying and assessing risks of material misstatement and for designing further audit procedures that respond appropriately to those risks.

After obtaining this understanding, the auditor may test management’s process, develop an independent point estimate or range, or evaluate audit evidence from events occurring through the date of the auditor’s report. The nature, timing, and extent of those procedures depend on the assessed risks and characteristics of the particular estimate. This sequencing is reflected in AICPA AU-C section 540, which requires the auditor to obtain an understanding of accounting estimates and how they are made as part of risk assessment before undertaking responsive substantive work. See AICPA AU-C Section 540, Auditing Accounting Estimates and AICPA Audit and Attest Standards.

QUESTION NO: 96

An auditor's inquiries of management disclosed that the entity recently invested in a series of energy derivatives to hedge against the risks associated with fluctuating oil prices. Under these circumstances, the auditor should:

A. Perform analytical procedures to determine if the derivatives are properly valued.

B. Examine the contracts for possible risk exposure and the need to recognize losses.

C. Confirm the marketability of the derivatives with a commodity specialist.

D. Document the derivatives in the auditor's communication with those charged with governance.

ANSWER: B

Explanation:

Examine the contracts for possible risk exposure and the need to recognize losses. is correct because the accounting and audit implications of energy derivatives depend on the actual contractual terms and on whether the transactions qualify for hedge accounting. The auditor should inspect the derivative agreements and related hedge documentation to identify the underlying risk being hedged, the notional amounts, maturity dates, settlement provisions, counterparties, and the nature of the entity's exposure to oil-price fluctuations. This evidence enables the auditor to assess management's accounting assertions regarding derivative recognition, fair-value measurement, hedge designation, hedge effectiveness, and the timing and location of gains or losses in the financial statements.

Under FASB ASC Topic 815, derivatives generally are recognized at fair value, and special hedge-accounting treatment requires contemporaneous documentation of the hedging relationship, the risk-management objective and strategy, the hedged risk, and the method used to assess effectiveness. Contract examination is therefore a direct and relevant audit procedure for determining whether reported results and disclosures reflect the entity's rights, obligations, and risk exposure. The auditor also uses the contracts as a foundation for evaluating management's valuation inputs and loss-recognition conclusions. See the FASB Accounting Standards Codification and the PCAOB's guidance on auditing fair-value measurements and estimates in AS 2501.

QUESTION NO: 97

The primary purpose of establishing quality control policies and procedures for deciding whether to accept new clients is to:

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

B. Monitor significant deficiencies in the design and operation of the client's internal control.

C. Identify noncompliance with aspects of contractual agreements that affect the financial statements.

D. Provide reasonable assurance that personnel will be adequately trained to fulfill their assigned responsibilities.

ANSWER: A

Explanation:

The primary purpose is to minimize the likelihood of association with clients whose management lacks integrity. Client acceptance and continuance is a core component of a CPA firm's system of quality management because the firm should accept or retain only those client relationships for which it has considered whether management and, when appropriate, those charged with governance demonstrate integrity and ethical values. Before accepting an engagement, the firm evaluates information obtained about the prospective client, including the reputation and integrity of its principal owners, key management, and governance personnel. This process helps the firm avoid relationships that may expose it to unacceptable risks, including risks that management may be dishonest, unwilling to provide necessary information, or likely to impair the firm's ability to perform a quality engagement in accordance with professional standards and applicable legal and regulatory requirements. The acceptance decision also considers whether the firm is competent and capable of performing the engagement and can comply with ethical requirements, but management integrity is the central concern reflected in this question. AICPA quality-management standards address acceptance and continuance decisions in SQMS No. 1 and require firms to establish quality objectives and responses for these relationships and engagements. See AICPA Statement on Quality Management Standards No. 1 and the AICPA Professional Standards—Quality Management.

QUESTION NO: 98

In planning an audit of a new client, an auditor most likely would consider the methods used to process accounting information because such methods:

A. Influence the design of internal control.

B. Affect the auditor's preliminary judgment about materiality levels.

C. Assist in evaluating the planned audit objectives.

D. Determine the auditor's acceptable level of audit risk.

ANSWER: A

Explanation:

"Influence the design of internal control." is correct because an entity's information-processing methods are integral to its system of internal control. In planning the audit, the auditor obtains an understanding of the information system, including the related business processes relevant to financial reporting and how transactions are initiated, authorized, recorded, processed, corrected, posted, and reported. Whether the entity uses primarily manual processes, automated applications, complex integrated systems, or a combination of these methods affects how controls are designed and implemented. For example, automated processing may embed controls in program logic and system access settings, while manual processing may rely more heavily on review, approval, reconciliation, and segregation-of-duties controls. The processing methods also affect the audit approach because they help the auditor identify relevant controls, assess risks of material misstatement, and determine the nature, timing, and extent of further audit procedures. This understanding is particularly important for a new client because the auditor has not gained knowledge from prior engagements. AU-C section 315 requires the auditor to understand the entity's information system and communication relevant to preparing the financial statements, including related business processes. See the [AICPA AU-C section 315] and the [PCAOB AS 2110].

QUESTION NO: 99

To establish the existence and ownership of a long-term investment in the common stock of a publicly traded company, an auditor ordinarily performs a security count or:

A. Relies on the client's internal accounting controls if the auditor has reasonable assurance that the control activities are being applied as prescribed.

B. Confirms the number of shares owned that are held by an independent custodian.

C. Determines the market price per share at the balance sheet date from published quotations.

D. Confirms the number of shares owned with the issuing company.

ANSWER: B

Explanation:

"Confirms the number of shares owned that are held by an independent custodian." is correct because a direct confirmation from the independent custodian provides persuasive audit evidence that the securities exist at the confirmation date and that the custodian holds the identified shares for the client. When certificated securities are not physically available for the auditor to inspect and count, confirmation is the ordinary alternative procedure. The auditor should control the confirmation process, including sending the request directly to the custodian and receiving the response directly, so the evidence is obtained from an independent external source rather than through the client.

The confirmation should identify the investment sufficiently to support the relevant assertions, such as the issuer, class of stock, number of shares, account or registration details, and any liens or restrictions reported by the custodian. This evidence addresses both the physical or recorded existence of the investment and the client's rights or ownership interest in it. Audit standards recognize external confirmations as audit evidence obtained directly from a third party and emphasize the auditor's control over the confirmation process. See the AICPA's [clarified auditing standards] and PCAOB [AS 2310, The Confirmation Process].

QUESTION NO: 100

To which of the following matters would materiality limits not apply when obtaining written client representations?

A. Losses from sales commitments.

B. Unasserted claims and assessments.

C. Fraud involving management.

D. Noncompliance with contractual agreements.

ANSWER: C

Explanation:

Fraud involving management is correct because management representations about fraud are not ordinarily qualified by materiality. Under AU-C section 580, written representations must state that management has disclosed to the auditor its knowledge of fraud or suspected fraud affecting the entity involving management, employees with significant roles in internal control, or others when the fraud could materially affect the financial statements. Fraud by management presents a distinct audit concern because management is in a position to override controls, influence accounting records, and affect the reliability of representations and other audit evidence. Even an amount that is quantitatively small can be qualitatively material when it involves senior management's integrity or indicates a broader risk of management override. Accordingly, the auditor needs an unqualified representation regarding management's knowledge of such fraud rather than one limited to matters above a specified monetary threshold. This representation helps the auditor assess fraud risk and evaluate the reliability of information received from management throughout the audit. The AICPA's AU-C 580 discusses the required written representations, while AU-C 240 addresses the auditor's responsibilities relating to fraud and management override. See AICPA Clarified Statements on Auditing Standards and PCAOB guidance on consideration of fraud.

QUESTION NO: 101

The ultimate purpose of assessing control risk is to contribute to the auditor's evaluation of the:

A. Factors that raise doubts about the auditability of the financial statements.

B. Operating effectiveness of internal control activities.

C. Risk that material misstatements exist in the financial statements.

D. Possibility that the nature and extent of substantive tests may be reduced.

ANSWER: C

Explanation:

"Risk that material misstatements exist in the financial statements" is correct because control risk is a component of the risk of material misstatement. It represents the risk that a misstatement that could be material, either individually or in combination with other misstatements, will not be prevented or detected and corrected on a timely basis by the entity's system of internal control. In assessing this risk, the auditor obtains an understanding of relevant controls and, when planning to rely on controls, evaluates and tests their operating effectiveness. That assessment helps the auditor identify where material misstatements may arise at the assertion level and determine an appropriate overall audit response and further audit procedures. Thus, the assessment is not an end in itself; it supports the auditor's broader evaluation of the likelihood of material misstatement in the financial statements and provides a basis for designing audit procedures responsive to that risk. This relationship is reflected in professional auditing standards addressing the auditor's assessment of risks of material misstatement and responses to assessed risks. See the PCAOB standard on identifying and assessing risks of material misstatement and the AICPA auditing standards resources.

QUESTION NO: 102

This question presents independent factual situations an auditor might encounter in conducting an audit. List A represents the types of opinions the auditor ordinarily would issue. Select as the best answer for this item, the action the auditor normally would take. The types of opinions in List A may be selected once, more than once, or not at all.

Assume:

• The auditor is independent.

• The auditor previously expressed an unqualified opinion on the prior year's financial statements.

• Only single-year (not comparative) statements are presented for the current year.

• The conditions for an unqualified opinion exist unless contradicted in the factual situations.

• The conditions stated in the factual situations are material.

• No report modifications are to be made except in response to the factual situation.

Item to Be Answered

An entity changes its depreciation method for production equipment from the straight-line to a units-of production method based on hours of utilization. The auditor concurs with the change although it has a material effect on the comparability of the entity's financial statements.

List A

Types of Options

A. An “except for” qualified opinion.

B. An unqualified opinion.

C. An adverse opinion.

D. A disclaimer of opinion.

E. Either an “except for” qualified opinion or an adverse opinion.

F. Either a disclaimer of opinion or an “except for” qualified opinion.

G. Either an adverse opinion or a disclaimer of opinion.

ANSWER: B

Explanation:

An unqualified opinion is appropriate because the auditor concurs that the revised units-of-production depreciation method is acceptable and the question stipulates that the requirements for an unqualified opinion otherwise have been met. A depreciation-method change reflects revised expectations about the pattern in which an asset’s future economic benefits are consumed. Under the accounting guidance, a change in depreciation method is treated as a change in accounting estimate effected through a change in accounting principle and is generally accounted for prospectively. Accordingly, the entity applies the new method to current and future periods rather than restating the prior year solely because the pattern of expected utilization has been reassessed.

The financial statements must adequately disclose the nature and effect of the change when required by the applicable reporting framework, enabling users to understand the effect on comparability. Materiality to comparability does not, by itself, mean that the current-year statements are materially misstated or that the auditor lacks sufficient evidence. Because the changed method is acceptable, properly accounted for, and appropriately disclosed, the auditor’s opinion remains unqualified. The applicable auditing framework addresses consistency and reporting considerations in PCAOB AS 2820, Consistency of Application of Generally Accepted Accounting Principles; the profession’s auditing standards resources are available from the AICPA Auditing and Attestation Standards.

QUESTION NO: 103

An accountant has been asked to issue a review report on the balance sheet of a nonissuer without reporting on the related statements of income, retained earnings, and cash flows. The accountant may issue the requested review report only if:

A. The balance sheet is not to be used to obtain credit or distributed to the entity's creditors.

B. The balance sheet is part of a comprehensive personal financial plan developed to assist the entity.

C. There have been no material changes during the year in the entity's accounting principles.

D. The scope of the accountant's inquiry and analytical procedures has not been restricted.

ANSWER: D

Explanation:

The scope of the accountant's inquiry and analytical procedures has not been restricted is correct because a review engagement may be performed and reported on for a single financial statement, such as a balance sheet, rather than a complete set of financial statements. The omission of the related statements does not itself prevent issuance of a review report. However, the accountant must be able to perform the review procedures considered necessary under the applicable review standards and obtain sufficient appropriate review evidence to provide limited assurance that no material modifications are needed for the balance sheet to conform with the applicable financial reporting framework.

A restriction on the accountant's inquiry or analytical procedures is a scope limitation. When such a limitation prevents the accountant from completing the procedures necessary for the engagement, the accountant cannot appropriately issue the requested review report on that financial statement. The engagement must therefore permit the accountant to carry out the required inquiries of management and analytical procedures without restriction. This conclusion follows the review-engagement requirements in the Statements on Standards for Accounting and Review Services, which govern reviews of nonissuer financial statements. See the AICPA's Compilation and Review Standards resources and AICPA assurance and advisory services guidance.