

## Chapter 1 The Demand for Audit and Other Assurance Services

### 1.1 Describe Auditing

1) Which of the following illustrates the definition of auditing with respect to the evidence analysis process?

- A) accumulation and evaluation of evidence about balance sheet accounts
- B) learning about different types of computing technology, such as mainframes
- C) writing an operational audit report that is tailored to the client's situation
- D) making sure that the auditor is competent and understands evidence gathering

Answer: A

Diff: 1 Type: MC Page Ref: 3

Learning Obj.: 1-1 Describe auditing

2) Auditing should be done by a qualified

- A) chartered accountant.
- B) certified management accountant.
- C) competent and independent person.
- D) professional accountant.

Answer: C

Diff: 2 Type: MC Page Ref: 3

Learning Obj.: 1-1 Describe auditing

3) Which of the following illustrates the definition of auditing with respect to the reporting process?

- A) accumulation and evaluation of evidence about balance sheet accounts
- B) reporting on the degree of correspondence between financial statements and ASPE
- C) writing an operational audit report that is tailored to the client's situation
- D) making sure that the auditor is competent and understands evidence gathering

Answer: B

Diff: 2 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

4) In the audit of historical financial statements by PA firms, the criteria used are

- A) generally accepted auditing standards.
- B) generally accepted accounting principles.
- C) regulations of the Canada Revenue Agency.
- D) regulations of the provincial securities commissions.

Answer: B

Diff: 1 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

5) A large PA firm has assessed evidence collected during an engagement. Criteria used to assess the financial statements were International Financial Reporting Standards (IFRS). A high level of assurance was obtained. The type of engagement conducted was

- A) an audit.
- B) a review.
- C) management consulting.
- D) a compilation.

Answer: A

Diff: 2 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

6) The auditor and the entities should agree on the criteria to be used in the audit

- A) before the audit starts.
- B) after the audit planning has been done.
- C) as they progress with the audit, as they can determine which criteria are most suitable.
- D) at the end of the audit.

Answer: A

Diff: 1 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

7) George had a conversation with the accounting personnel and documented information about how the accounting systems function. He has also placed copies of accounting forms in his files. George is performing which task?

- A) accounting procedures
- B) evidence gathering
- C) tax audit
- D) audit report preparation

Answer: B

Diff: 3 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

8) One of the reasons that an auditor must be competent is so that they can

- A) understand the engagement risks and the criteria used by the client.
- B) explain to staff how the bookkeeping should be done.
- C) record the transactions properly for the underlying records.
- D) capture the information properly in the computer files.

Answer: A

Diff: 2 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

9) One of the reasons that an auditor must be competent is so that they can

- A) select the type and amount of evidence to accumulate.
- B) explain to staff how the bookkeeping should be done.
- C) record the transactions properly for the underlying records.
- D) capture the information properly in the computer files.

Answer: A

Diff: 2 Type: MC Page Ref: 4

Learning Obj.: 1-1 Describe auditing

10) It is important for the auditor to be independent because

- A) otherwise the auditor would not charge a fair rate to the client.
- B) otherwise the auditor might not be as knowledgeable of the subject matter and the criteria.
- C) this will prevent bias in accumulating and evaluating evidence.
- D) the Canadian tax authorities require that the auditor be independent.

Answer: C

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

11) Because an external auditor is paid a fee by a client company, he or she

- A) is absolutely independent and may conduct an audit.
- B) may be sufficiently independent to conduct an audit.
- C) is never considered to be independent.
- D) must receive approval from the relevant provincial securities commission before conducting an audit.

Answer: B

Diff: 1 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

12) The independent auditor's report is the

- A) communication of the result of the audit to the users.
- B) set of audited financial statements.
- C) invoice of the auditor detailing the work they have performed.
- D) report presented to management about the possible improvements.

Answer: A

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

13) In the audit of an individual's tax return, the auditor should demonstrate competence in the use of

- A) external databases that contain economic statistics.
- B) standard personal and corporate tax preparation software.
- C) the *Income Tax Act* and accompanying regulations.
- D) database management software for the use of client based research.

Answer: C

Diff: 1 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

14) In the audit of an individual's tax return, the criteria used would be

- A) an accounting framework.
- B) the *Income Tax Act*.
- C) the client's policies for taxable income.
- D) the auditor's judgment.

Answer: B

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

15) In the audit of a corporate tax return, the report provided by the Canada Revenue Agency auditor would describe

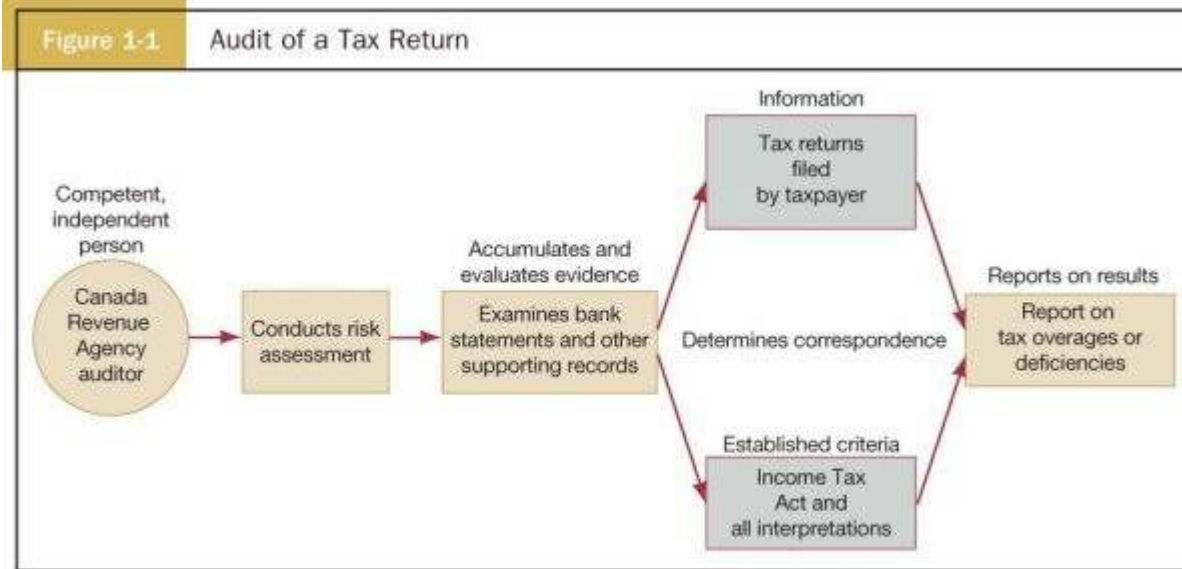
- A) an opinion on the likelihood of tax return error.
- B) the likely accounting errors that could contribute to tax errors.
- C) management issues with respect to accurately reporting taxes.
- D) corporate income tax overages or income tax underpayments.

Answer: D

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Describe auditing

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Use your knowledge of the definition of auditing and Figure 1-1: Audit of a Tax Return to explain how an auditor would conduct a privacy audit.

Answer: First, the concept of a competent, independent person requires that the practitioner who is conducting an assurance engagement should have "adequate proficiency," which means that the privacy auditor should be competent in the fields of privacy and the fields that need to be assessed, such as information systems security, data management and access controls, and privacy risks and controls. The auditor should also use due care and have an objective state of mind. This means that the auditor should be independent of the client and do their best using their skills when conducting the engagement.

The second part of Figure 1-1 relates to accumulation and evaluation of evidence using a risk-based approach. This means that the auditor would collect evidence based upon risks of privacy violations at the client.

The next three parts are connected. The auditor determines the correspondence of the information provided by the client (which could be a management report about the quality of its privacy procedures) to established criteria.

Finally, the auditor issues a report to summarize the findings.

Diff: 2 Type: ES Page Ref: 3-4

Learning Obj.: 1-1 Describe auditing

## 1.2 Distinguish between auditing and accounting

1) Joe is recording sales transactions in the accounting system so that they can be summarized in a logical manner for the purpose of providing financial information for decision-making. Joe is performing

- A) accounting.
- B) auditing.
- C) review.
- D) management consulting.

Answer: A

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

2) Which of the following is an example of accounting rather than auditing?

- A) gathering evidence about the quality of accounts receivable
- B) entering sales transactions into the sales order system
- C) reviewing sales invoices to see if they have been calculated correctly
- D) comparing bank deposit documents to the recorded cash received

Answer: B

Diff: 3 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

3) In auditing accounting data, the concern is with

- A) determining whether recorded information properly reflects the economic events that occurred during the accounting period.
- B) determining if fraud has occurred.
- C) determining if taxable income has been calculated correctly.
- D) analyzing the financial information to be sure that it complies with government requirements.

Answer: A

Diff: 1 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

4) The need to implement philosophies and practices commonly referred to as "improved business practices" comes from

- A) increased competition resulting in public accounting firms being concerned about keeping clients and maintaining a reasonable profit.
- B) a CAS pronouncement.
- C) a GAAP pronouncement.
- D) a need to increase profitability on assurance type mandates.

Answer: A

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

5) Which of the following is an example of auditing rather than accounting?

- A) recording purchase amounts in the expense accounts
- B) posting the daily sales totals to the general ledger
- C) recording cash received in the customer account files
- D) evaluating whether accounts receivable are collectible

Answer: D

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

6) An accountant records information. When conducting an audit, the auditor must possess

- A) an ability to interpret generally accepted accounting frameworks.
- B) an education beyond the bachelor's degree.
- C) an ability to classify transactions by type.
- D) an ability to organize and summarize economic events.

Answer: A

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

7) Discuss the differences and similarities between the roles of accountants and auditors. What additional expertise must an auditor possess beyond that of an accountant?

Answer: The role of accountants is to record, classify, and summarize economic events in a logical manner for the purpose of providing financial information for decision making. To do this, accountants must have a sound understanding of the principles and rules that provide the basis for preparing the financial information. In addition, accountants are responsible for developing systems to ensure that the entity's economic events are properly recorded on a timely basis and at a reasonable cost.

The role of auditors is to determine whether the financial information prepared by accountants properly reflects the economic events that occurred. To do this, the auditor must not only understand the principles and rules that provide the basis for preparing financial information, but must also possess expertise in the accumulation and evaluation of audit evidence. It is this latter expertise that distinguishes auditors from accountants.

Diff: 1 Type: ES Page Ref: 6

Learning Obj.: 1-2 Distinguish between auditing and accounting

### 1.3 Explain the importance of auditing in reducing information risk

1) How does a financial statement audit affect a bank manager's decisions in providing loans to a corporate client?

- A) Information risk could be reduced, so the bank manager may lower the interest rate charged.
- B) The bank manager will lower the risk-free interest rate that applies to the corporation.
- C) The business risk for the client will be reduced, so the borrowing costs will decline.
- D) The business risk for the client will be increased, so the borrowing costs will be lowered.

Answer: A

Diff: 3 Type: MC Page Ref: 7

Learning Obj.: 1-3 Explain the importance of auditing in reducing information risk

2) What is the most appropriate method for an organization to lower information risk related to its financial statements?

- A) Have good bookkeeping work completed on the accounts.
- B) Use a high quality software package keep track of information.
- C) Have an independent financial statement audit conducted.
- D) Have an independent operational audit conducted on effectiveness.

Answer: C

Diff: 2 Type: MC Page Ref: 7

Learning Obj.: 1-3 Explain the importance of auditing in reducing information risk

3) Frederic is an account manager at a large Canadian bank. Frederic has to decide if the bank will make a loan to Frost Corp, a snow removal company. Further, Frederic has to decide how much they will lend to Frost and at what rate.

Assuming that Frederic makes the loan, what factors will he use to decide the rate of interest? What factors are impacted by auditing and how?

Answer: Factors:

1. Risk free interest rate: The rate the bank could earn in a risk-free investment such as government bonds.
2. Business risk for the customer: Possibility that the customer will not be able to repay their loan because of economic or business conditions.
3. Information risk: Possibility that the information upon which the business decision was made was inaccurate.

The audit impacts information risk. Having a set of audited financial statements can reduce the information risk and increase the likelihood that the bank will make the loan.

Diff: 3 Type: ES Page Ref: 6-7

Learning Obj.: 1-3 Explain the importance of auditing in reducing information risk



1.4 List the causes of information risk, and explain how the risk can be reduced

1) Which of the following is *not* a cause of information risk?

- A) simple exchange transactions
- B) voluminous data
- C) remoteness of information
- D) biases and motives of the provider

Answer: A

Diff: 2 Type: MC Page Ref: 7

Learning Obj.: 1-4 List the causes of information risk and explain how this risk can be reduced

2) Which of the following terms best describes the increased likelihood that unreliable information will be provided to decision makers?

- A) audit risk
- B) information risk
- C) inherent risk
- D) business risk

Answer: B

Diff: 2 Type: MC Page Ref: 7

Learning Obj.: 1-4 List the causes of information risk and explain how this risk can be reduced

3) What is the nature of the service provided when a auditor evaluates information using suitable criteria and issues a report that attests to the reliability of the information?

- A) internal audit engagement
- B) review engagement
- C) compilation engagement
- D) attestation engagement

Answer: D

Diff: 2 Type: MC Page Ref: 8

Learning Obj.: 1-4 List the causes of information risk and explain how this risk can be reduced

## 1.5 Identify major types of audits and auditors

1) Blader Ng. Inc. has recently placed new air-cleaning systems in their smokestacks to meet air quality regulations. An auditing firm has been engaged to assess air quality and compare results to legislated requirements. What type of audit or engagement is the auditor conducting?

- A) financial statement
- B) compliance
- C) operational
- D) review

Answer: B

Diff: 3 Type: MC Page Ref: 9

Learning Obj.: 1-5 Identify major types of audits and auditors

2) As part of its loan agreement, Big Bank requires that only accounts receivable less than 60 days old be used as collateral. An auditor has been engaged to provide assurance that the accounts receivable on the list provided to the bank are indeed less than 60 days old. What type of engagement is the auditor conducting?

- A) financial statement
- B) compliance
- C) operational
- D) review

Answer: B

Diff: 3 Type: MC Page Ref: 9

Learning Obj.: 1-5 Identify major types of audits and auditors

3) A review of any part of an organization's procedures and methods for the purpose of evaluating efficiency and effectiveness is classified as a(n)

- A) audit of financial statements.
- B) compliance audit.
- C) operational audit.
- D) production audit.

Answer: C

Diff: 1 Type: MC Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

4) Which of the following is most difficult to evaluate objectively?

- A) efficiency and effectiveness of operations
- B) compliance with government regulations
- C) presentation of financial statements in accordance with a generally accepted accounting framework
- D) internal controls in use at a small company

Answer: A

Diff: 3 Type: MC Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

- 5) A typical objective of an operational audit is for the auditor to
- A) determine whether the financial statements fairly present the entity's operations.
  - B) evaluate the feasibility of attaining the entity's operational objectives.
  - C) evaluate the effectiveness of an internal process.
  - D) report on the entity's relative success in attaining profit maximization.

Answer: C

Diff: 1 Type: MC Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

- 6) Which of the following audits can be regarded as being solely "compliance" audits?
- A) Canada Revenue Agency's examinations of the returns of taxpayers
  - B) the Auditor General's evaluation of the computer operations of governmental units
  - C) an internal auditor's review of his employer's payroll authorization procedures
  - D) a public accounting firm's audit of the local school district

Answer: A

Diff: 2 Type: MC Page Ref: 9

Learning Obj.: 1-5 Identify major types of audits and auditors

- 7) Which of the following is an example of a financial statement audit?
- A) determining whether ABC's financial statements overall do not violate any debt covenants
  - B) determining whether ABC's overall financial statements are stated in conformity with IFRS
  - C) evaluating the effectiveness and efficiency of internal controls used to create account balance
  - D) evaluating the effectiveness and efficiency of internal controls used to record transactions

Answer: B

Diff: 2 Type: MC Page Ref: 9

Learning Obj.: 1-5 Identify major types of audits and auditors

- 8) What is the primary difference between internal and external auditors?
- A) the methodology used to conduct financial statement audits
  - B) the level of competence required
  - C) the parties to whom the auditor is responsible
  - D) the level of objectivity required

Answer: C

Diff: 2 Type: MC Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

- 9) Who is responsible for developing financial statement audit and assurance standards in Canada?
- A) AASB (Auditing and Assurance Standards Board)
  - B) standards staff at the CICA (Canadian Institute of Chartered Accountants)
  - C) national accounting bodies such as CGA Canada
  - D) the accounting firms who conduct financial statement audits

Answer: A

Diff: 1 Type: MC Page Ref: 13

Learning Obj.: 1-5 Identify major types of audits and auditors

10) Which of the following organizations establishes ethical standards and standards for the practice of Internal Auditing?

- A) Information Systems Audit and Control Association (ISACA)
- B) Institute of Internal Auditors (IIA)
- C) Society of Management Accountants of Canada (SMAC)
- D) Canadian Institute of Chartered Accountants (CICA)

Answer: B

Diff: 1 Type: MC Page Ref: 10-11

Learning Obj.: 1-5 Identify major types of audits and auditors

11) Auditors General are responsible for auditing which types of organizations?

- A) public companies with shares issued to investors
- B) private companies that have loans outstanding to banks or other creditors
- C) ministries, departments, agencies, and crown corporations
- D) any organization that submits tax returns to the tax authorities

Answer: C

Diff: 2 Type: MC Page Ref: 11

Learning Obj.: 1-5 Identify major types of audits and auditors

12) The extent and the scope of the audits conducted by Auditors General are determined by

- A) legislation in the Auditor General's jurisdiction.
- B) audit partner planning and audit program development.
- C) the Auditor General and his/her staff.
- D) the financial statement auditors of the client.

Answer: A

Diff: 3 Type: MC Page Ref: 11

Learning Obj.: 1-5 Identify major types of audits and auditors

13) To operate effectively, an internal auditor must be independent of the

- A) line functions of the organization.
- B) entity that is being audited.
- C) employer-employee relationship that exists for other employees in the organization.
- D) outsourcing organizations used.

Answer: A

Diff: 3 Type: MC Page Ref: 10

Learning Obj.: 1-5 Identify major types of audits and auditors

14) The internal audit group typically reports directly to the

- A) board of directors.
- B) management of the company.
- C) external auditor.
- D) audit committee.

Answer: D

Diff: 3 Type: MC Page Ref: 10

Learning Obj.: 1-5 Identify major types of audits and auditors

15) We discuss four types of auditors: public accountants, government auditors, Canada Revenue Agency auditors, and internal auditors. Briefly describe the work and responsibilities of each type of auditor.

Answer:

Public Accountants: Primary function is the audit of financial statements of publicly traded companies and of other organizations requiring audits. The type of audit normally performed is known as an attestation engagement because they attest to the fair presentation of the financial statements. To conduct the audit of financial statements, the auditor must be a licensed public accountant.

Government Auditors: Primary function is the audit of ministries, departments, and agencies that report to the government. A government auditor performs the audit function for the government.

Canada Revenue Agency Auditors: Primary responsibility is the enforcement of federal tax laws. The Canada Revenue Agency auditors audit the returns of taxpayers to determine whether they have complied with the tax laws. They only perform compliance audits.

Internal Auditors: Internal auditors are normally members of the IIA and work for individual companies to audit for management. The internal auditor's responsibilities can vary considerably but often include operations auditing and reporting their findings directly to the board of directors and audit committee. The internal auditor must be independent from the line function in the organization he/she is auditing.

Diff: 3 Type: ES Page Ref: 9-13

Learning Obj.: 1-5 Identify major types of audits and auditors

16) To do an audit, it is necessary to have information in a verifiable form and some criteria by which the auditor can evaluate the information.

**Required:**

A) What information and criteria would a public accounting firm use when auditing a company's financial statements?

B) What information and criteria would a Canada Revenue Agency auditor use when auditing that same company's tax return?

C) What information and criteria would an internal auditor use when performing an operational audit to evaluate whether the company's computerized payroll processing system is operating efficiently and effectively?

Answer: A) The information used by a public accounting firm in a financial statement audit is the financial information in the company's financial statements. The criteria used are a generally accepted financial reporting framework such as IFRS.

B) The information used by a Canada Revenue Agency auditor is the financial information in the auditee's federal tax return. The criteria is the *Income Tax Act* and interpretations.

C) The information used by an internal auditor when performing an operational audit of the payroll system could include various items such as the number of errors made, costs incurred by the payroll department, and number of payroll records processed each month. The criteria would consist of company standards for departmental efficiency and effectiveness.

Diff: 3 Type: ES Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

17) Mega Manufacturing Company (Mega) is thinking about acquiring Localized Small Producer Inc. (LSP), a small manufacturing company that produces related products. Mega has examined the financial statements of LSP, which show only a small profit in the last five years. Management of LSP has taken reasonable salaries, and cost of goods sold is higher than the industry average for LSP. Mega believes that it will be able to introduce operational efficiencies at LSP, improving the profitability of the small company, if acquired.

**Required:**

A) What type of engagement should be conducted to assess the operational efficiencies of LSP? Justify your response.

B) Who should be engaged to conduct the engagement?

C) What major problems might the auditors encounter when conducting the audit and writing the report?

Answer:

A) Mega should have an operational audit conducted. An operational audit is a review of any part of an organization's operating procedures and methods for the purpose of evaluating economy, efficiency, and effectiveness.

B) The operational audit could be conducted by Mega's internal auditors, assuming that they have internal auditors. It could also be conducted by a public accounting firm. For reasons of independence, if Mega is a listed company (see Chapter 2 of the textbook), then Mega should engage a different public accounting firm than its present auditors.

C) Operational audits are not easily defined. First, the auditors would need to prepare criteria with the assistance of management to define efficiency. Then, the auditors would need to consider the type of evidence that might be available. For example, if LSP has older manufacturing equipment than Mega, LSP might be operating at peak efficiency - evidence will need to be geared to the criteria. Then, the report will need to be prepared in the context of the criteria and the evidence that will be collected. As there are no standard reports in operational auditing, the auditors will need to customize the report based upon the criteria and evidence collected.

Diff: 2 Type: ES Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

18) Jordan set up a nonprofit corporation several years ago to provide scholarships to disadvantaged youth in his community. Scholarships Get Up and Go Foundation now has assets of over \$5 million and provides about ten university scholarships every year. Jordan is proud of the new doctors, dentists, and other healthcare practitioners that his foundation has funded.

Jordan is thinking of starting another foundation in an old building that he has purchased. It would be a youth drop-in centre offering music lessons, art facilities, and gym facilities, and would have links to local highschools to offer homework clubs to encourage good grades.

**Required:**

- A) Why should Jordan have the financial statements of both of these foundations audited?
- B) Who would be the users of the financial statements of the foundations?
- C) What other types of services could PAs provide to Jordan and the foundations?

Answer:

A) Auditing provides added assurance with respect to the information provided in the financial statements: perhaps he could get a better interest rate on invested funds at a financial institution. It might also give added credibility to potential donors of funds, and would also show the assets, liabilities, and any surplus/deficit are reported in the proper entity and have not been reported or used in the wrong entity.

B) Users could be financial institutions that are holding the Foundations' money, Jordan, his employees, donors and potential donors, tax authorities, and organizations that regulate charitable organizations, such as provincial and federal regulatory agencies. If the foundations receive government funding, then the organizations providing funding would also be users of the financial statements.

C) PAs could provide advice on how to invest the capital funding that is used for the scholarships. They could help design the accounting procedures in place at both foundations. They could provide bookkeeping and compilation assistance, as well as prepare tax returns and any regulatory filings. They could assist the foundation in obtaining working capital funding for the new drop-in centre, if needed.

Diff: 2 Type: ES Page Ref: 9-10

Learning Obj.: 1-5 Identify major types of audits and auditors

1.6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

1) The No-Name Agency conducts an independent service for a company to determine if its suppliers have complied with health and safety regulations, child labour guidelines, and other employee welfare issues. What type of service is No-Name providing?

- A) assurance
- B) attest
- C) review
- D) compilation

Answer: A

Diff: 2 Type: MC Page Ref: 17

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

2) Which of the following is an example of an attestation engagement?

- A) accounting and bookkeeping services for the accounts
- B) an audit of internal controls over financial reporting
- C) preparation of the annual financial statements with notes
- D) completion of provincial and federal tax returns

Answer: B

Diff: 1 Type: MC Page Ref: 14

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

3) When do individuals and organizations typically need assurance services?

- A) usually only when organizations obtain debt or other loans
- B) for five years from the start of an organization until debt is retired
- C) only when historical data, such as financial information, needs to be audited
- D) on an ongoing basis, as demand for forward-looking information increases

Answer: D

Diff: 2 Type: MC Page Ref: 14

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

4) What impact is the presence of factors such as real-time information (such as via the Internet) expected to have upon the demand for assurance services?

- A) Demand is expected to decline due to the lack of adequate resources.
- B) Demand is expected to grow due to the increase in large corporations.
- C) Demand is expected to grow due to the need for forward-looking information.
- D) Demand is expected to decline as small businesses use the Internet more.

Answer: C

Diff: 2 Type: MC Page Ref: 14

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services



5) A major type of assurance service performed by large public accounting firms is

- A) auditing.
- B) reviewing.
- C) compilation.
- D) management consulting.

Answer: A

Diff: 1 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

6) In Canada, publicly traded companies are

- A) required to have audits.
- B) strongly encouraged to have audits.
- C) not required to have an audit if they have a review.
- D) not required to have an audit.

Answer: A

Diff: 2 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

7) A shareholder of a public Canadian firm can have access to the audited financial statements

- A) on the Internet.
- B) by calling the accounting department of the company.
- C) by requesting a copy from the auditors.
- D) if he/she holds more than 1% of the shares of the company.

Answer: A

Diff: 1 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

8) What type of information is available from [www.sedar.com](http://www.sedar.com) (System for Electronic Document Analysis and Retrieval)?

- A) minutes of shareholders and directors meetings
- B) transaction reports from major credit card companies
- C) annual reports and management discussion and analysis
- D) listings of all of the shareholders on record

Answer: C

Diff: 2 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

- 9) A reason for a nonprofit organization to be audited is to
- A) comply with the laws requiring them to be audited.
  - B) meet requirements of lenders or funding sources.
  - C) have a professional accountant perform their bookkeeping.
  - D) ensure that their financial statements do not contain errors.

Answer: B

Diff: 3 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

- 10) Which of the following services provides a moderate level of assurance about the client's financial statements?
- A) forecasts and projections
  - B) compliance
  - C) review
  - D) audit

Answer: C

Diff: 1 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

- 11) Which of the following is an advantage of a review engagement as compared to an audit engagement?
- A) For the review engagement, information risk is reduced more than for an audit.
  - B) For the review engagement, the documentation to be provided by the client is greater.
  - C) For the review engagement, the financial statements assessed will have more detail.
  - D) The review engagement requires considerably less work, so is less costly.

Answer: D

Diff: 2 Type: MC Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

- 12) The *Sarbanes-Oxley Act* requires the auditor to attest to the
- A) accuracy of the financial statements.
  - B) efficiency of the internal controls in financial reporting.
  - C) effectiveness of internal controls.
  - D) compliance of the company with the generally accepted accounting framework.

Answer: C

Diff: 1 Type: MC Page Ref: 16

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

13) The reasoning behind the requirements of the *Sarbanes Oxley Act's* section 404 (attestation on internal control over financial reporting) is that

- A) effective controls result in greater profits to organizations, reducing business failures.
- B) effective controls reduce the likelihood of future misstatements in the financial statements.
- C) better internal controls can be implemented at lower cost, improving product quality.
- D) automated controls improve customer service, resulting in higher product sales.

Answer: B

Diff: 3 Type: MC Page Ref: 16

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

14) There is an increasing demand for assurance about computer controls surrounding financial information transacted electronically and the security of the information related to the transaction. This is in large part due to

- A) the increasing presence of Internet sales in many businesses.
- B) the use of computer-assisted auditing tools.
- C) the large volume of transactions and information shared online and in real-time by companies.
- D) client's uncertainty about the proper functioning of their computer systems.

Answer: C

Diff: 2 Type: MC Page Ref: 16-17

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

15) Trust Services principles and criteria for controls relate to ensuring that

- A) controls over security availability, processing integrity, and confidentiality or privacy have been complied with.
- B) information systems are reliable in areas such as security, data integrity, and program quality.
- C) controls over information systems implemented by the company are used consistently and reliably.
- D) there will not be any unauthorized access to the website or other systems used by the client organization.

Answer: A

Diff: 3 Type: MC Page Ref: 16-17

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

16) Which of the following services results in assurance that the company's e-commerce activities on its website comply with Trust Services principles?

- A) review engagement
- B) internal controls assessment
- C) SysTrust
- D) WebTrust

Answer: D

Diff: 2 Type: MC Page Ref: 17

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

17) A PA is attempting to sell a service to clients that will provide assurance on the accuracy, availability, and security of information systems. The PA is attempting to sell a(n)

- A) WebTrust service.
- B) compilation service.
- C) SysTrust service.
- D) audit engagement.

Answer: A

Diff: 3 Type: MC Page Ref: 17

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

18) Which of the following services provides no assurance about the client's financial statements?

- A) compilation
- B) review
- C) audit
- D) SysTrust

Answer: A

Diff: 1 Type: MC Page Ref: 18

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

19) Herbert Zora is having financial statements prepared by his PA to accompany his tax return. His primary concern is cost. Of the following, the lowest-cost engagement that the PA can perform for Zora's financial statements is

- A) compilation.
- B) review.
- C) audit.
- D) WebTrust.

Answer: A

Diff: 2 Type: MC Page Ref: 18

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

20) When readers are cautioned that the financial statements may not be appropriate for their purposes, the non-assurance service is called a(n)

- A) SysTrust.
- B) compilation.
- C) review.
- D) audit.

Answer: B

Diff: 3 Type: MC Page Ref: 18

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

21) Two types of services provided by public accounting firms are audits and reviews. Discuss the similarities and differences between these two types of services. Which type provides the most assurance?

Answer: Two primary types of services are audits of historical financial statements and reviews of historical financial statements. While both services involve the accumulation and evaluation of evidence regarding assertions made by management in the company's financial statements, an audit involves a more extensive examination and provides a higher level of assurance about the client's financial statements than a review.

Diff: 1 Type: ES Page Ref: 15

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services

22) As a PA, you have been asked to prepare your sister Betty's year-end financial statements. Betty is a photographer and is the sole shareholder of a small company called Best Weddings Ltd. She photographs weddings, graduations, and schools, and earns about \$75 000 per year. Betty has said that she only needs the financial statements for her tax returns and would like you to prepare the tax returns too.

**Required:**

- A) Would you be able to prepare the financial statements for your sister? Why or why not?
- B) If yes, what type of report would you prepare to accompany the financial statements?
- C) Would you be able to prepare the tax returns for your sister? Why or why not?

Answer:

- A) Yes the PA would be able to prepare the financial statements as a bookkeeping (or compilation) assignment. No assurance is provided for a compilation, so independence is not required. An audit or review could not be prepared because for those engagements, assurance is provided, which means that the PA would need to be independent.
- B) A compilation report would be prepared to accompany the financial statements. The report would need to disclose the relationship and that independence was absent.
- C) Yes, the PA would be able to prepare the tax returns, as assurance is not required for tax returns. Identification of the preparer is required on tax returns. It would be important to discuss with your sister why she wants you to prepare the tax returns (Does she just want to save some money? Or is she trying to prepare tax returns that are fraudulent?). It would be inappropriate (and professionally dangerous) to be associated with false and misleading information, as one could be sued by the tax department and expelled from the profession.

Diff: 3 Type: ES Page Ref: 18

Learning Obj.: 1-6 Describe assurance services provided by public accountants and distinguish the audit of financial statements from other assurance and nonassurance services