

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

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

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

Answer: A

Diff: 1 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 2) Auditing should be done by a qualified 2) _____

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

Answer: A

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

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

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

Answer: C

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

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

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

Answer: D

Diff: 1 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 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(n) 5) _____

A) compilation. B) management consulting.
C) audit. D) review.

Answer: C

Diff: 2 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 6) The auditor and the entities should agree on the criteria to be used in the audit 6) _____
- A) before the audit starts.
 - B) as they progress with the audit as they can determine which criteria is more suitable.
 - C) after the audit planning has been done.
 - D) at the end of the audit.

Answer: A

Diff: 1 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

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

Answer: D

Diff: 3 Type: MC Page Ref: 5

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 8) One of the reasons that an auditor must be competent is to be able to 8) _____
- A) record the transactions properly for the underlying records.
 - B) understand the engagement risks and the criteria used by the client.
 - C) capture the information properly in the computer files.
 - D) explain how the bookkeeping should be done to his staff.

Answer: B

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 9) One of the reasons that an auditor must be competent is to be able to 9) _____
- A) explain how the bookkeeping should be done to his staff.
 - B) capture the information properly in the computer files.
 - C) record the transactions properly for the underlying records.
 - D) select the type and amount of evidence to accumulate.

Answer: D

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 10) It is important for the auditor to be independent because 10) _____
- A) the auditor would not charge a fair rate to the client.
 - B) the auditor might not be as knowledgeable of the subject matter and the criteria.
 - C) the Canadian Tax Authorities require that the auditor be independent.
 - D) this will prevent bias in accumulating and evaluating evidence.

Answer: D

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 11) Because an external auditor is paid a fee by a client company, he or she 11) _____
A) may be sufficiently independent to conduct an audit.
B) must receive approval of the relevant provincial securities commission before conducting an audit.
C) is absolutely independent and may conduct an audit.
D) is never considered to be independent.

Answer: A

Diff: 1 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 12) The independent auditor's report is the 12) _____
A) communication of the result of the audit to the users.
B) report presented to management about the possible improvements.
C) invoice of the auditor detailing the work they have performed.
D) set of audited financial statements.

Answer: A

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 13) In the audit of an individual's tax return, the auditor should demonstrate competence in the use of 13) _____
A) external databases that contain economic statistics.
B) database management software for the use of client based research.
C) the Income Tax Act and accompanying regulations.
D) standard personal and corporate tax preparation software.

Answer: C

Diff: 1 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 14) In the audit of an individual's tax return, the criteria used would be 14) _____
A) the client's policies for taxable income. B) an accounting framework.
C) the Income Tax Act. D) the auditor's judgment.

Answer: C

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 15) In the audit of a corporate tax return, the report provided by the Canada Revenue Agency auditor 15) _____
would describe
A) the likely accounting errors that could contribute to tax errors.
B) an opinion on the likelihood of tax return error.
C) management issues with respect to accurately reporting taxes.
D) corporate income tax overages or income tax under payments.

Answer: D

Diff: 2 Type: MC Page Ref: 6

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

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

Answer: D

Diff: 2 Type: MC Page Ref: 7

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 17) Which of the following is an example of accounting rather than auditing? _____
- A) reviewing sales invoices to see if they have been calculated correctly
B) entering sales transactions into the sales order system
C) gathering evidence about the quality of accounts receivable
D) comparing bank deposit documents to the recorded cash received

Answer: B

Diff: 3 Type: MC Page Ref: 7

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

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

Answer: D

Diff: 1 Type: MC Page Ref: 7

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 19) Which of the following is an example of auditing rather than accounting? _____
- A) recording cash received in the customer account files
B) recording purchase amounts in the expense accounts
C) posting the daily sales totals to the general ledger
D) evaluating whether accounts receivable are collectible

Answer: D

Diff: 2 Type: MC Page Ref: 7

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 20) An accountant records information. When conducting an audit, the auditor must possess _____
- A) an ability to organize and summarize economic events.
B) an education beyond the bachelor's degree.
C) an ability to classify transactions by type.
D) an ability to interpret generally accepted accounting frameworks.

Answer: D

Diff: 2 Type: MC Page Ref: 8

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 21) How does a financial statement audit affect a bank manager's decision in providing loans to a corporate client? 21) _____
- A) Information risk could be reduced, so the bank manager may lower the interest rate charged.
 - B) The business risk for the client will be increased, so the borrowing costs will be lowered.
 - C) The business risk for the client will be reduced, so the borrowing costs will decline.
 - D) The bank manager will lower the risk-free interest rate that applies to the corporation.

Answer: A

Diff: 3 Type: MC Page Ref: 8

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 22) What is the most appropriate method for an organization to lower information risk related to its financial statements? To have 22) _____
- A) an independent operational audit conducted on effectiveness.
 - B) an independent financial statement audit conducted.
 - C) a high quality software package keep track of information.
 - D) good bookkeeping work completed on the accounts.

Answer: B

Diff: 2 Type: MC Page Ref: 8

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

- 23) 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: 7

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

- 24) 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: 1. Risk free interest rate: Rate 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 the 3rd factor. The importance of an audit is reflected as there is less risk of the financial misstatement containing material errors if they have been audited. 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: 8

Learning Obj.: 1-1 Identify the components of an audit and explain why there is a demand for audits

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

- 25) The No-Name Advertising Rating Agency conducts independent surveys to determine the sources of purchases by consumers (e.g. newspaper ad, magazine ad, television ad). This information is then used by those media (i.e. newspapers, magazines, and television broadcasters) to indicate to purchasers of advertising the breadth of coverage that they have. For example, Small Local Newspaper can say that 10% of the purchasers of soap products made their decisions based upon their ads. This helps in selling advertising. What type of service is No-Name providing? 25) _____
A) Compilation B) Assurance C) Review D) Attest

Answer: B

Diff: 2 Type: MC Page Ref: 9

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 26) Which of the following is an example of an attestation engagement? 26) _____
A) Preparation of the annual financial statements, with notes
B) Accounting and bookkeeping services for the accounts
C) An audit of internal controls over financial reporting
D) Completion of provincial and federal tax returns

Answer: C

Diff: 1 Type: MC Page Ref: 9

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 27) For how many years will assurance engagements be required by individuals or organizations? 27) _____
A) only when historical such as financial information needs to be audited
B) on an ongoing basis, as organizations and society's needs evolve
C) usually only when organizations obtain debt or other loans
D) for five years from the start of an organization until debt is retired

Answer: B

Diff: 2 Type: MC Page Ref: 10

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

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

Answer: B

Diff: 2 Type: MC Page Ref: 10

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 29) A major type of assurance service performed by large public accounting firms is _____
A) management consulting. B) compilation.
C) review. D) audit.

Answer: D

Diff: 1 Type: MC Page Ref: 10

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 30) In Canada, publicly traded companies are _____
A) strongly encouraged to have audits.
B) not required to have an audit if they have a review.
C) required to have audits.
D) not required to have an audit.

Answer: C

Diff: 2 Type: MC Page Ref: 10

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 31) A shareholder of a public Canadian firm can have access to the audited financial statements _____
A) by calling the accounting department of the company.
B) if he holds more than 1% of the shares of the company.
C) requesting a copy from the auditors.
D) on the internet.

Answer: D

Diff: 1 Type: MC Page Ref: 10

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 32) What type of information is available from www.sedar.com (System for Electronic Document Analysis and Retrieval)? Documents such as _____
A) annual reports and management discussion and analysis.
B) minutes of shareholders and directors meetings.
C) listings of all of the shareholders on record.
D) transaction reports from major credit card companies.

Answer: A

Diff: 2 Type: MC Page Ref: 10-11

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 33) A reason for a not-for-profit organization to be audited is 33) _____
A) complying with the laws requiring them to be audited.
B) ensuring that their financial statement do not contain errors.
C) having a professional accountant perform their bookkeeping.
D) meeting requirements of lenders or funding sources.

Answer: D

Diff: 3 Type: MC Page Ref: 11

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 34) Which of the following services provides a moderate level of assurance about the client's financial statements? 34) _____
A) Review B) Compliance
C) Audit D) Forecasts and projections

Answer: A

Diff: 1 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 35) Which of the following is an advantage of a review engagement as compared to an audit engagement? For the review engagement 35) _____
A) it requires considerably less work, so is less costly.
B) the documentation to be provided by the client is greater.
C) information risk is reduced more than for an audit.
D) the financial statements assessed will have more detail.

Answer: A

Diff: 2 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 36) The Sarbanes-Oxley Act requires the auditor to attest to the 36) _____
A) effectiveness of internal controls.
B) efficiency of the internal controls in financial reporting.
C) accuracy of the financial statements.
D) compliance of the company with the generally accepted accounting framework.

Answer: A

Diff: 1 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 37) The reasoning behind the requirements of the Sarbanes Oxley Act's section 404 (attestation on internal control over financial reporting) is that 37) _____
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) automated controls improve customer service, resulting in higher product sales.
D) better internal controls can be implemented at lower cost, improving product quality.

Answer: B

Diff: 3 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

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

38) _____

Answer: A

Diff: 2 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 39) The purpose of a *WebTrust* service is to assure the user that
- A) there will not be any unauthorized access to the web site or other systems used by the client organization.
 - B) controls over information systems implemented by the company are used consistently and reliably.
 - C) criteria related to business practices, transaction integrity, and information processes have been met.
 - D) information systems are reliable in areas such as security, data integrity, and program quality.

39) _____

Answer: C

Diff: 3 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 40) Which of the following services results in the placement of an electronic seal affixed to the web site?
- A) SysTrust
 - B) WebTrust
 - C) internal controls assessment
 - D) review engagement

40) _____

Answer: B

Diff: 2 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 41) PA is attempting to sell a service to his clients that will provide assurance on information systems reliability. PA is attempting to sell a(n)
- A) WebTrust service.
 - B) audit engagement.
 - C) SysTrust service.
 - D) compilation service.

41) _____

Answer: C

Diff: 3 Type: MC Page Ref: 12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 42) Which of the following services provides no assurance about the client's financial statements?
- A) review
 - B) compilation
 - C) audit
 - D) SysTrust

42) _____

Answer: B

Diff: 1 Type: MC Page Ref: 13

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 43) 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 43) _____
A) audit. B) WebTrust. C) review. D) compilation.
Answer: D
Diff: 2 Type: MC Page Ref: 13
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided
- 44) When a compilation engagement is performed, the report attached is called a 44) _____
A) Notice to Reader. B) Compilation Report.
C) Auditor's Report. D) No Assurance Report.
Answer: A
Diff: 3 Type: MC Page Ref: 13
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided
- 45) Blader Ng. Inc. has recently placed into production new air-cleaning systems in their smoke-stacks to meet clean-air quality regulations. PA has been engaged to assess air quality and compare results to legislated requirements. What type of audit or engagement is PA conducting? 45) _____
A) review B) compliance
C) financial statement D) operational
Answer: B
Diff: 3 Type: MC Page Ref: 14
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided
- 46) Big Bank requires, as part of its loan agreement, 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? 46) _____
A) operational B) compliance
C) review D) financial statement
Answer: B
Diff: 3 Type: MC Page Ref: 14
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided
- 47) 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) 47) _____
A) audit of financial statements. B) production audit.
C) operational audit. D) compliance audit.
Answer: C
Diff: 1 Type: MC Page Ref: 14
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided
- 48) Which one of the following is more difficult to evaluate objectively? 48) _____
A) efficiency and effectiveness of operations
B) compliance with government regulations
C) internal controls in use at a small company.
D) presentation of financial statements in accordance with a generally accepted accounting framework
Answer: A
Diff: 3 Type: MC Page Ref: 14
Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 49) A typical objective of an operational audit is for the auditor to 49) _____
A) report on the entity's relative success in attaining profit maximization.
B) determine whether the financial statements fairly present the entity's operations.
C) evaluate the effectiveness of an internal process.
D) evaluate the feasibility of attaining the entity's operational objectives.

Answer: C

Diff: 1 Type: MC Page Ref: 14

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 50) Which of the following audits can be regarded as being solely "compliance" audits? 50) _____
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) a public accounting firm's audit of the local school district
D) an internal auditor's review of his employer's payroll authorization procedures

Answer: A

Diff: 2 Type: MC Page Ref: 14

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 51) Which of the following is an example of a financial statement audit? 51) _____
A) evaluating the effectiveness and efficiency of internal controls used to create account balance
B) determining whether ABC's financial statements overall do not violate any debt covenants
C) determining whether ABC's overall financial statements are stated in conformity with IFRS
D) evaluating the effectiveness and efficiency of internal controls used to record transactions

Answer: C

Diff: 2 Type: MC Page Ref: 14

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 52) What is the primary difference between internal and external auditors? The 52) _____
A) methodology used to conduct financial statement audits.
B) parties to whom the auditor is responsible.
C) level of competence required.
D) level of objectivity required.

Answer: B

Diff: 2 Type: MC Page Ref: 15

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 53) Why might the decisions about materiality and risks be different for the internal auditor than for 53) _____
the external auditor when conducting an audit of a system?
A) internal auditors will focus only on the potential for dollar errors internally
B) the auditors are applying different skills during the conduct of the audit
C) external users may have different needs than management
D) external auditors have different expectations with respect to quality control

Answer: C

Diff: 3 Type: MC Page Ref: 15

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

- 54) 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: 14-15

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 55) 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: 10-12

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

56) 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: 14-15

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

- 57) Jordan set up a nonprofit corporation several years ago to provide scholarships to poor youth in his community. From a small start, 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 health care 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, with music lessons, art facilities, basketball facilities in a gym, with linkages to local high schools so that there could be a homework club 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 preparing 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: 14-15

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

58) You, PA, have been asked to prepare the year-end financial statements of your sister. Betty is a photographer, and is the sole shareholder of a small company called Best Weddings Ltd. She photographs weddings, graduations and schools, earning 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, I 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 I 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, I 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 my sister why she wants me to prepare the tax returns (does she just want to save some money?) or is she trying to prepare tax returns that are fraudulent (to save taxes). Even for a sister, it would be inappropriate (and professionally dangerous) to be associated with false and misleading information, with the potential to be sued by the tax department and expelled from the profession.

Diff: 3 Type: ES Page Ref: 13

Learning Obj.: 1-2 Link the nature of assurance services to examples of actual services provided

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

59) Who is responsible for developing financial statement audit and assurance standards in Canada? 59) _____

- A) The accounting firms who conduct financial statement audits
- B) National accounting bodies such as CGA Canada
- C) AASB (Auditing and Assurance Standards Board)
- D) Standards staff at the CICA (Canadian Institute of Chartered Accountants)

Answer: C

Diff: 1 Type: MC Page Ref: 15

Learning Obj.: 1-3 Explore the different types of accountants and what they do

60) Which of the following organizations establishes ethical standards and standards for the practice of Internal Auditing? 60) _____

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

Answer: A

Diff: 1 Type: MC Page Ref: 53

Learning Obj.: 1-3 Explore the different types of accountants and what they do

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

61) _____

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

Answer: C

Diff: 2 Type: MC Page Ref: 17

Learning Obj.: 1-3 Explore the different types of accountants and what they do

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

62) _____

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

Answer: B

Diff: 3 Type: MC Page Ref: 17

Learning Obj.: 1-3 Explore the different types of accountants and what they do

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

63) _____

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

Answer: A

Diff: 3 Type: MC Page Ref: 18

Learning Obj.: 1-3 Explore the different types of accountants and what they do

64) The internal audit group typically reports directly to the

64) _____

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

Answer: B

Diff: 3 Type: MC Page Ref: 18

Learning Obj.: 1-3 Explore the different types of accountants and what they do

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

- 65) 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.

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.

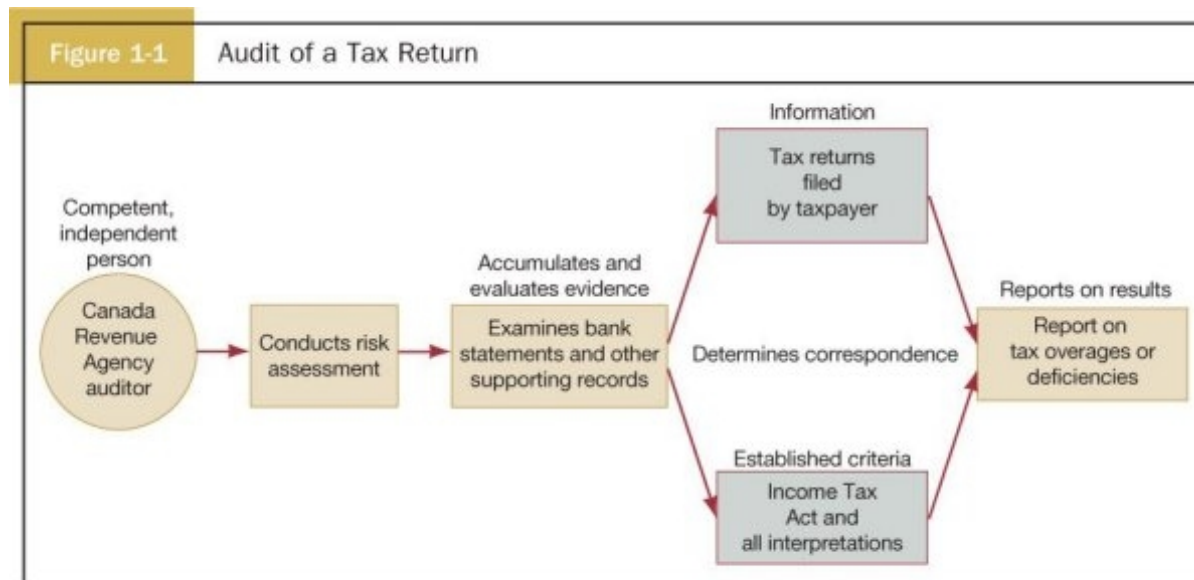
Government Auditors: Primary function is the audit of ministries, departments and agencies which report to the government. A government auditor performs the audit function for the government.

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 report 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: 17-18

Learning Obj.: 1-3 Explore the different types of accountants and what they do



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[Note: If this question is used as part of an examination question, *Figure 1-1. Audit of a Tax Return* will need to be included as part of the examination.]

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, 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

Answer: 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* (GAPP, generally accepted privacy principles, available from: <http://www.cica.ca/resources-and-member-benefits/privacy-resources-for-firms-and-organizations/general-accepted-privacy-principles/index.aspx>)

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

Diff: 2 Type: ES Page Ref: 5

Learning Obj.: 1-3 Explore the different types of accountants and what they do