

**BIRZEIT UNIVERSITY**  
**FACULTY OF BUSINESS AND ECONOMICS**  
**ACCOUNTING DEPARTMENT**

LECTURER: SUHA ZALLOUM

FIRST SEM. 2013/2014

FIRST HOUR EXAM

ACCT. "339"

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**Part I - Answer Sheet**

|    |   |   |
|----|---|---|
| 1  | D | ✓ |
| 2  | C | ✓ |
| 3  | B | ✓ |
| 4  | B | ✓ |
| 5  | D | ✗ |
| 6  | D | ✗ |
| 7  | C | ✓ |
| 8  | C | ✗ |
| 9  | D | ✓ |
| 10 | D | ✓ |
| 11 | C | ✓ |
| 12 | C | ✓ |
| 13 | D | ✓ |
| 14 | B | ✓ |
| 15 | B | ✗ |
| 16 | C | ✓ |
| 17 | D | ✓ |
| 18 | C | ✓ |
| 19 | C | ✓ |
| 20 | A | ✗ |
| 21 | C | ✓ |

sp. A  
B  
A  
A  
B

Mc. 16 → 32  
20.5  

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52.5

52.5  

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70

## Part I: Multiple Choice Questions

Select the best answer for each of the following:

1. An audit of historical financial statements most commonly includes the:
  - A. Balance sheet, statement of retained earnings, and the statement of cash flows.
  - B. Income statement, the statement of cash flows, and the statement of net working capital. ~~x~~
  - C. Statement of cash flows, balance sheet, and the statement of retained earnings.
  - D. Balance sheet, income statement, and the statement of cash flows. ✓
  
2. In "auditing" financial accounting data, the primary concern is with:
  - A. Determining if fraud has occurred.
  - B. Determining if taxable income has been calculated correctly.
  - C. Determining whether recorded information properly reflects the economic events that occurred during the accounting period. ✓
  - D. Analyzing the financial information to be sure that it complies with government requirements.
  
3. An auditor concludes that a client's illegal act, which has a material effect on the financial statements, has not been properly accounted for or disclosed. Depending on the materiality of the effect on the financial statements, the auditor should express either a(an):
  - A. Adverse opinion or a disclaimer of opinion.
  - B. Qualified opinion or an adverse opinion. ✓
  - C. Disclaimer of opinion or an unqualified opinion with a separate explanatory paragraph.
  - D. Unqualified opinion with a separate explanatory paragraph or a qualified opinion.

*CAAPP  
Qualified  
Adverse ✓*
  
4. The audit report date on a standard unqualified report indicates:
  - A. The last day of the fiscal period. ✓
  - B. The last day of the auditor's responsibility for the review of significant events that occurred subsequent to the date of the financial statements. ✓ *Subseq*
  - C. The date on which the financial statements were filed with the Securities and Exchange Commission. ✓
  - D. The last date on which users may institute a lawsuit against either client or auditor. ✓
  
5. Which of the following services provides the lowest level of assurance on a financial statement?
  - A. A review. ✓
  - B. An audit.
  - C. Neither service provides assurance on financial statements.
  - D. Each service provides the same level of assurance on financial statements. ✓
  
6. The Public Company Accounting Oversight Board:
  - A. Establish auditing standards that must be followed by CPAs on all audits. ✓
  - B. Perform inspections of the quality controls at audit firms that audit public companies. ✓ *PCAOB*
  - C. Oversee auditors of private companies. ~~x~~
  - D. Perform any of the above functions. ✓

7. Which of the following is not an essential component of quality control?
- A. Policies and procedures to ensure that the work performed by firm personnel meet applicable professional standards.
  - B. Policies to ensure that personnel maintain their independence in fact and in appearance.
  - C. Policies and procedures to ensure that firm personnel are actively engaged in marketing strategies.
  - D. Policies that ensure that monitoring activities are effectively applied.
8. Brown Co.'s financial statements adequately disclose uncertainties that concern future events, the outcome of which are not reasonably estimable. The auditor's report should be a(n):
- A. Unqualified opinion.
  - B. Disclaimer.
  - C. Qualified opinion.
  - D. Adverse opinion.
9. Which of the following statements most accurately captures the intent of the standards of field work?
- A. Field work standards are primarily concerned with personal attributes necessary during the conduct of the audit. *PIE*
  - B. Field work standards provide extensive guidance regarding the conduct of an audit.
  - C. Field work standards are primarily concerned with the conduct of substantive testing as opposed to testing of internal controls.
  - D. Field work standards are primarily directed at the auditor's planning, understanding of internal control, and evidence accumulation.
10. When financial statements contain a departure from GAAP, the auditor should explain the circumstances for the departure in a separate paragraph and express an opinion that is:
- A. Unqualified.
  - B. Qualified.
  - C. Adverse.
  - D. Qualified or adverse, depending on materiality.
11. 2) "Independence" in auditing means:
- A. Maintaining an indirect financial interest. ✓
  - B. Not being financially dependent on a client. ✓
  - C. Taking an unbiased and objective viewpoint.
  - D. Being an advocate for a client. ✓
12. An auditor's report includes the following statement: "The financial statements do not present fairly the financial position, results of operations, or cash flows in conformity with generally accepted accounting principles." This auditor's report was most likely issued in connection with financial statements that are
- A. Inconsistent
  - B. Based on prospective financial information.
  - C. Misleading.
  - D. Affected by a material uncertainty.

13. Which of the following services are allowed by the SEC whenever a CPA also audits the company?

- A. Internal audit outsourcing ✓
- B. Legal services unrelated to the audit ✗
- C. Appraisal or valuation services ✗
- D. Services related to assessing the effectiveness of internal control over financial reporting.

14. An auditor would express an unqualified opinion with an explanatory paragraph added to the auditor's report for:

|                                     | <u>Justified accounting change</u> | <u>A material weakness in the internal control</u> |
|-------------------------------------|------------------------------------|--|
| A.                                  | Yes                                | Yes  |
| <input checked="" type="radio"/> B. | Yes                                | No   |
| C.                                  | No                                 | Yes  |
| D.                                  | No                                 | No   |

15. How many audits of public companies per year does a CPA firm that is registered with the Public Company Accounting Oversight Board (PCAOB) have to perform before it receives an annual inspection from the PCAOB?

- A. More than 100 audits.
- B. More than 50 audits.
- C. More than 10 audits.
- D. One audit.

16. An example of an "indirect ownership interest in a client" would be ownership of a client's stock by a member's:

- A. Dependent child. ✗
- B. Spouse. ✗
- C. Non-dependent grandfather.
- D. All of the above are examples of indirect ownership. ✗

17. When disclaiming an opinion due to a client-imposed scope limitation, an auditor should indicate in a separate paragraph why the audit did not comply with the generally accepted auditing standards. The auditor should also omit the:

|                                     | <u>Scope paragraph</u> | <u>Opinion Paragraph</u> |
|-------------------------------------|------------------------|--------------------------|
| A.                                  | No                     | Yes                      |
| B.                                  | Yes                    | Yes                      |
| C.                                  | No                     | No                       |
| <input checked="" type="radio"/> D. | Yes                    | No                       |

18. According to AICPA Code of Professional Conduct, which of the following financial interests in the client during the period of the engagement impairs a CPA's independence?

- A. All direct and indirect financial interests.
- B. Only direct financial interests.
- C. All direct and material indirect financial interests.
- D. Only material financial interests.

19. Which of the following statements best describes the ethical standard of the profession pertaining to advertising and solicitation?

- A. All forms of advertising and solicitation are prohibited.
- B. There are no prohibitions regarding the manner in which CPAs may solicit new business.
- C. A CPA may advertise in any manner that is not false, misleading, or deceptive.
- D. A CPA may only solicit new clients through mass mailings.

20. A CPA who is not in public practice is obligated to follow which of the following rules of conduct?

- A. Independence.
- B. Integrity and objectivity.
- C. Contingent fees.
- D. Commissions.

21. The concept of materiality would be least important to an auditor when considering the:

- A. Adequacy of disclosure of the client's illegal act.
- B. Discovery of weaknesses in the Client's internal control.
- C. Effects of a direct financial interest in the client on the CPA's independence.
- D. None.

**Part II: Essay Questions**

A. Ray and Robin, CPAs, are independent auditors who previously expressed an unqualified opinion on Hillsburg Hardware Company prior year financial statements. For the current year, another CPA has audited a wholly-owned subsidiary of Hillsburg Hardware Company. The total assets and revenues of the subsidiary represent 17% and 18%, respectively, of the total assets and revenues of Hillsburg Hardware Company being audited.

For each of the situations listed in the table below, identify the appropriate opinion type and the appropriate report modification.

| Situation  | Opinion Type | Introductory Paragraph (Omit/Change/Modify) | Scope Paragraph (Omit/Change/Modify) | Opinion Paragraph (Omit/Change/Modify) | Explanatory Paragraph (Non required/Insert Before opinion/Insert After opinion) |
|--|--------------|---|--------------------------------------|--|---|
| 1. Assume that Ray and Robin decide to take <u>responsibility</u> for the work of the other CPA, who issued an unqualified opinion.  | unqualified  | NC  | NC                                   | modify                                 | add before opinion  |
| 2. Assume that Ray and Robin do <u>not</u> wish to assume responsibility for the work of the other CPA, who issued an unqualified opinion.   | qualified    | NC  | NC                                   | modify                                 | add before opinion  |
| 3. Assume that Ray and Robin decide to take responsibility for the work of the other CPA, who issued a qualified opinion on the subsidiary's financial statements. The subject of the qualification is <u>very material</u> to the <u>subsidiary</u> but <u>not material</u> in relation to the overall consolidated financial statements.                 | qualified    | NC  | NC                                   | modify                                 | add before opinion  |
| 4. Assume that Ray and Robin do <u>not</u> wish to assume responsibility for the work of the other CPA, who issued a qualified opinion on the subsidiary's financial statements. The subject of the qualification is <u>very material</u> to the <u>subsidiary</u> , but <u>not material</u> in relation to the overall consolidated financial statements. | qualified    | NC  | NC                                   | modify                                 | add before opinion  |

immaterial responsibility  
qualified  
unqualified

CAMP  
unqualified  
415

B. For the following cases / services, indicate whether there is a violation of AICPA's code of professional conduct or AICPA rules or SEC rules.

|     | Service   | Violation?<br>(YES /NO) |
|-----|---|-------------------------|
| 1.  | Providing <u>bookkeeping services</u> to a <u>public company</u> . The services were pre-approved by the audit committee of the company.  | Yes ✓                   |
| 2.  | Providing internal audit services to a public company that is an <u>audit client</u> .  | No ✗                    |
| 3.  | Compiling the financial statements of a client that employed the CPA's spouse as a bookkeeper.  | No ✓                    |
| 4.  | Implementing a financial information system designed by <u>(management)</u> for a Public company.   | Yes ✓                   |
| 5.  | Ahmad is the <u>(partner)</u> in charge of the audit of Southern Bank. Ahmad is in the process of purchasing a building and has obtained the financing from Southern Bank, the financing is partially collateralized.   | Yes ✓                   |
| 6.  | Fayez is a CPA with <u>3 years of professional experience with CPA firm</u> . He owns <u>25 shares of stock in an audit client of the firm</u> , he is in-charge in the audit of the client, the amount of stocks is not material in relation to his total wealth.  | Yes ✓                   |
| 7.  | Houston, CPAs, is performing consultancy services to help management of Global Services Company streamline its production operations. Houston structured the fee for this engagement to be a <u>fixed percentage of cost savings</u> that result once processes are implemented. Houston performs no other services for Global Service Company. | No ✓                    |
| 8.  | The client owes the auditor fees for more than two years prior to the issuance of the audit report.   | Yes ✓                   |
| 9.  | A client leases part of an office building from the CPA, resulting in a <u>material indirect financial interest</u> to the CPA.   | Yes ✓                   |
| 10. | A CPA Contracted with a client to supervise the client's office personnel.  | No ✗                    |

(8)

C. There are five conditions that must be met before an auditor can issue a standard unqualified report for the audit of a U.S. public company. Please discuss each of these five conditions.

- ① it must achieve the general standards and technical. the auditor should be independent, competence.
- ② sufficient appropriate evidence, and the fieldwork standards. understand the company & environment.
- ③ full disclosures, according to GAAP that reflects the economic events and footnote. all are available
- ④ financial statements - B.S, I.S, statement of cash flow, retained earnings all should be available.
- ⑤ they should follow consistency and accounting principles and express their opinion.

Good Luck

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**Question 5 (12 points)**

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12

Space Company is involved in a number of projects related to its future success. Some of these projects are considered operational activities while others are considered research and development (R&D) activities. Space must determine the proper accounting treatment in assessing certain expenditures for the year.

From the answer choices listed below, select the proper accounting treatment for each of the expenditures listed below. Each choice may be used once, more than once, or not at all.

| Expenditure  | Choice       |
|--|--------------|
| 1. Executive Salaries  | H            |
| 2. Costs incurred to upgrade current production facility                                       | C            |
| 3. Legal fees to obtain a patent on a new rocket engine  | B            |
| 4. Salaries of research staff designing new rocket engine                                      | F            |
| 5. Marketing research costs to promote new rocket engine                                       | H            |
| 6. Costs incurred to improve engine currently in production ?                                  | <del>X</del> |
| 7. Material, labor, and overhead costs of new rocket engine                                    | <del>X</del> |
| 8. Costs incurred to successfully defend patent on the new rocket engine                       | B            |
| 9. Acquisition of machinery to be used on current and future R&D projects                      | D            |
| 10. Research costs by Electro Company under contract for new rocket engine                     | <del>A</del> |
| 11. Research costs incurred under contract for Palestine Company and billed monthly            | <del>X</del> |
| 12. Costs of quality control in <u>early stages</u> of new rocket engine commercial production | H            |

| Answer Choices                              |                                       |
|---|---------------------------------------|
| A. Record as receivable                     | E. Expense as consumed as R&D expense |
| B. Capitalize and amortize                  | F. Expense immediately as R&D expense |
| C. Capitalize and depreciate                | G. Expense as manufacturing cost      |
| D. Capitalize and depreciate as R&D expense | H. Expense as operating expense       |