

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

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SECOND SEM. 2014/2015

SECOND EXAM

ACCT. "339"

Student Name

Student #: \_\_\_\_\_

**Part I – Answer Sheet**

1	C	+
2	E	+
3	C	✓
4	C	+
5	A	✓
6	E	✓
7	E	+
8	C	✓
9	D	+
10	E	✓
11	D	✓
12	D	✓
13	E	+
14	B	✓
15	A	✓

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## Part I - Multiple Choice Questions

1. The rights and obligations assertion applies to:
- a. current liability items only.
  - b. revenue and expense items only.
  - c. both income statement and balance sheet items.
  - d. assets that are not owned by the company.
  - e. balance sheet items only.
2. Which of these is not a risk factor?
- a. Inherent risk.
  - b. Control risk.
  - c. Detection risk.
  - d. Assurance risk. I-ER
  - e. All of the above are risk factors.
3. When planning the audit, the auditor must make the following important decisions except the:
- a. assignment of staff to perform audit tests.
  - b. nature of tests to be performed.
  - c. characteristics of tests to be performed.
  - d. extent of tests to be performed. ✓
  - e. timing of tests to be performed. ✓
4. The subject of the auditing procedure observing is least likely to be:
- a. personnel. ✓
  - b. procedures. ✓
  - c. processes. ✓
  - d. inventory taking. }
  - e. physical assets. }
5. Which of the following auditing procedures is least likely to disclose an understatement?
- a. Vouching
  - b. Tracing
  - c. Inquiring
  - d. Counting
  - e. Confirming
6. The assessed risk of material misstatement influences audit decisions about audit procedures. Which of the following decisions is more appropriate when the risk of material misstatement is assessed as low rather than when it is assessed as high?
- a. Performing audit procedures at the balance sheet date. ✓
  - b. Performing audit procedures on a larger proportion of the population. ✓
  - c. Obtaining audit evidence primarily with substantive tests. ✓
  - d. Including the most experienced individuals on the audit team. ✓
  - e. Choosing substantive audit procedures that provide less persuasive evidence when considering benefits and costs.
7. In accepting an engagement, an auditor takes on professional responsibilities to:
- a. the public. ✓
  - b. the client. ✓
  - c. other members of the public accounting profession.
  - d. the public, the client, and other members of the public accounting profession.
  - e. the client and the public.

8. The main purpose of the **engagement letter** is to:
- a. avoid litigation.
  - b. indicate the likely opinion to be issued.
  - c. confirm the terms of the engagement.
  - d. clearly delineate management's responsibility for the conduct of the audit.
  - e. clearly delineate the auditor's responsibility for the conduct of the audit.
9. Which one of the following is not a key step in planning the audit?
- a. Perform analytical procedures.
  - b. Consider audit risk.
  - c. Make preliminary judgments about materiality levels.
  - d. Develop preliminary audit strategies for significant assertions.
  - e. Obtain an understanding of the client's external controls.
10. Which of the following best describes the auditor's responsibilities concerning related parties?
- a. investigate those transactions encountered during the audit
  - b. as related parties are discovered during the course of the audit, their existence should be noted in the working papers
  - c. obtain a list of all board members and place in the working papers
  - d. investigate the background of all related parties
  - e. determine, in the planning stage, the existence of related parties
11. In planning the audit, the auditor should assess materiality at two levels:
- a. the preliminary level and the final level.
  - b. the company level and the divisional level.
  - c. the account balance level and the detailed item level.
  - d. the financial statement level and the account balance level.
  - e. the account balance level and the transaction level.
12. In allocating financial statement materiality to the various accounts, the auditor should consider:
- a. the likelihood of misstatements in the account.
  - b. the probable cost of verifying the account.
  - c. neither the likelihood of misstatements in the account nor the probable cost of verifying the account.
  - d. both the likelihood of misstatements in the account and the probable cost of verifying the account.
  - e. the likelihood of misstatements in a transaction.
13. The auditor has some control over:
- a. the assessed level of inherent risk.
  - b. the actual level of inherent risk.
  - c. both the actual level and the assessed levels of inherent risk.
  - d. neither the actual level nor the assessed level of inherent risk.
  - e. the projected level of inherent risk.
14. For a particular assertion, control risk is the risk that:
- a. a material misstatement will occur in the accounting process.
  - b. controls will not detect a material misstatement that occurs.
  - c. audit procedures will fail to detect a weak control system.
  - d. the prescribed control procedures will not be applied uniformly.
  - e. an immaterial misstatement will occur in the accounting process.

15. In the investigation of a potential new client, if the client refuses to give permission to inquire of the predecessor auditor, or if the predecessor does not respond fully, the successor auditor should:
- a. consider the implications (effects) in making the accept/reject decision.
  - b. not accept the engagement.
  - c. request an AICPA-sanctioned peer review of the predecessor.
  - d. request assistance from the SEC.
  - e. immediately inform the appropriate state board of accountancy.

**Part II-Essay Questions**

**Q1.** Below are 12 audit procedures. Classify each procedure according to the following types of audit evidence: (1) physical examination, (2) confirmation, (3) recalculation, (4) observation, (5) inquiry of the client, (6) reperformance, (7) Inspection and (8) analytical procedure.

AUDIT PROCEDURE	TYPE OF AUDIT EVIDENCE
1. Watch client employees count inventory to determine whether company procedures are being followed.	Observation ✓
2. Trace postings from the sales journal to the general ledger accounts.	Reperformance ✓
3. Calculate the ratio of cost of goods sold to sales as a test of overall reasonableness of gross margin relative to the preceding year.	Analytical Procedure ✓
4. Obtain information about the client's internal controls by asking questions of client personnel.	Inquiry of the client ✓
5. Examine a piece of equipment to make sure a recent purchase of equipment was actually received and is in operation.	Inspection ✓
6. Review the total of repairs and maintenance for each month to determine whether any month's total was unusually large.	Reperformance ✗
7. Compare vendor names and amounts on purchase invoices with entries in the purchases journal.	Inspection ✓
8. Foot entries in the sales journal to determine whether they were correctly totaled by the client.	Recalculation ✓
9. Make a surprise count of petty cash to verify that the amount of the petty cash fund is complete.	Physical examination ✓
10. Obtain a written statement from the client's bank stating the client's year-end balance on deposit.	Confirmation ✓

(B)

Q2. The professional standards identify five categories of assertions made by management that are contained in the financial statements. If any of these assertions is a misrepresentation, the statements could be materially misstated. The categories of assertions identified by the profession are:

- A. Existence or occurrence
- B. Completeness
- C. Rights and obligations
- D. Valuation or allocation
- E. Presentation and disclosure

Following is a list of errors encountered during the conduct of an audit.

**REQUIRED:** Using the letters given above, indicate the assertion that is being misrepresented by each listed error.

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- B ✓ 1. A short-term loan obtained from the bank was not recorded.
  - D ✗ 2. The current portion of long-term debt was excluded from the current liabilities section of the balance sheet.
  - D ✗ 3. Reported sales include transactions from the subsequent period.
  - B ✓ 4. A number of shipments were made that were never billed. \*
  - D ✓ 5. Clerical errors were made in the compilation of the physical inventory count.
  - A ✓ 6. Several fictitious sales were booked during the period.
  - AE ✗ 7. Some of the inventory is obsolete, with no current market.
  - D ✗ 8. Accrued liabilities include the utility bills of the owner.
  - C ✗ 9. The disposal of several pieces of machinery was never recorded. •
  - EX ✗ 10. A piece of land, carried as an investment, has been written up to reflect current appraisals of the property.

Q3. Assume materiality for the financial statements as a whole is \$100,000 and performance materiality for accounts receivable is set at 40,000. If the auditor finds on receivable that is overstated by \$55,000, what should the auditor do?

After comparing the sum of misstatement for each account with the materiality of for financial statement, if it ~~exceed~~ <sup>Good Luck</sup> if the auditor may ~~not~~ reverse the ~~set~~ of materiality and performance materiality. specially for those account where the misstatement exceed the performance materiality or discuss it with the management to see if it reasonable for this account to have these over stated

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