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QUESTION 1

It is not appropriate to refer a reader of an auditor's report to a financial statement footnote for details concerning:

- A. Subsequent events.
- B. The pro forma effects of a business combination.
- C. Sale of a discontinued operation.
- D. The results of confirmation of receivables.

Correct Answer: D

Explanation:

Choice "d" is correct. Details concerning the results of audit procedures (such as the results of confirmation of receivables) generally do not appear in the footnotes.

Choice "a" is incorrect. Subsequent events may be discussed in an explanatory paragraph of the auditor's report, which would also refer to the related footnote.

Choice "b" is incorrect. The pro forma effects of a business combination may be included in an explanatory paragraph of the auditor's report, which would also refer to the related footnote.

Choice "c" is incorrect. Sale of a discontinued operation may be discussed in an explanatory paragraph of the auditor's report, which would also refer to the related footnote.

QUESTION 2

Having identified their mission, overall strategy, and critical success factors, organizations often review the internal and external factors that will contribute to their success. This analysis is often referred to as:

- A. TOC evaluation.
- B. Brainstorming.
- C. Balanced scorecard review.
- D. SWOT analysis.

Correct Answer: D

Explanation: Choice "d" is correct. Evaluation of internal and external factors contributing to an organization's success is referred to as Strengths, Weaknesses, Opportunities and Threats (SWOT) analysis. Strengths and weaknesses focus on internal factors while opportunities and threats relate to external factors. Choice "a" is incorrect. The acronym TOC stands for Theory of Constraints, which is an evaluation technique for optimizing throughput time, it does not relate to overall strategy evaluation. Choice "b" is incorrect. Brainstorming is a meeting technique used to generate ideas. Although brainstorming could be used as part of an organization's approach to SWOT analysis, it is not, itself, the



evaluation of internal and external factors. Choice "c" is incorrect. A review of the balanced scorecard, which summarizes measures of achievement of critical success factors, does not represent the objective review of internal and external factors that may impact achievement of strategy.

QUESTION 3

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

- A. Vouching the receipt and deposit of interest checks.
- B. Confirming the bond interest rate with the issuer of the bonds.
- C. Recomputing the interest earned on the basis of face amount, interest rate, and period held.
- D. Testing the internal controls over cash receipts.

Correct Answer: C

Explanation:

Choice "c" is correct. Recomputing the interest earned is the most likely method of auditing interest earned on bond investments.

Choice "a" is incorrect. Vouching cash receipts would only verify the recording of checks received. This may not be the same as interest earned, since interest is accrued between cash payment dates.

Choice "b" is incorrect. Confirmation of the bond interest rate with the issuer is not sufficient, as the rate still needs to be applied based on face amount and period held.

Choice "d" is incorrect. Internal control testing of cash receipts would not provide evidence that earned interest was properly recorded, since interest is accrued between cash payment dates.

QUESTION 4

When audited financial statements are presented in a client's document containing other information, the auditor should:

- A. Perform inquiry and analytical procedures to ascertain whether the other information is reasonable.
- B. Add an explanatory paragraph to the auditor's report without changing the opinion on the financial statements.
- C. Perform the appropriate substantive auditing procedures to corroborate the other information.
- D. Read the other information to determine that it is consistent with the audited financial statements.

Correct Answer: D

Explanation:



Choice "d" is correct. The auditor should read the "other information" in a client's document containing audited FS to determine that it is consistent with the audited FS.

Choice "a" is incorrect. Performing analytical procedures or any other procedure is not necessary.

Choice "b" is incorrect. An explanatory paragraph is not required.

Choice "c" is incorrect. The auditor has no obligation to perform any procedure to corroborate "other information" contained in a document such as an annual report.

QUESTION 5

Which of the following is not an audit procedure that the independent auditor would perform concerning litigation, claims, and assessments?

- A. Obtain assurance from management that it has disclosed all unasserted claims that the lawyer has advised are probable of assertion and must be disclosed.
- B. Confirm directly with the client's lawyer that all claims have been recorded in the financial statements.
- C. Inquire of and discuss with management the controls adopted for identifying, evaluating, and accounting for litigation, claims, and assessments.
- D. Obtain from management a description and evaluation of litigation, claims, and assessments existing at the balance sheet date.

Correct Answer: B

Explanation: Choice "b" is correct. The independent auditor would not confirm directly with the client's lawyer that all claims have been recorded in the financial statements. Management has the responsibility to include all claims in the financial statements, not the lawyers. The purpose of a legal letter is to obtain outside corroboration of the information furnished by management concerning litigation, claims, and assessments. Choice "a" is incorrect. The auditor should obtain assurance from management that it has disclosed all unasserted claims that the lawyer has advised are probable of assertion and must be disclosed. Choice "c" is incorrect. The auditor should inquire of and discuss with management the controls adopted for identifying, evaluating, and accounting for litigation, claims, and assessments. Choice "d" is incorrect. The auditor should obtain from management a description and evaluation of litigation, claims, and assessments existing at the balance sheet date.