



Continuing Professional Development Programme

A Refresher Course on Current Auditing Standards

(Programme Code: CAW131111)

Programme Dates: 11, 21, 25, 28 November & 8 December 2013

Facilitators: Ms Winnie Chan & Ms Eky Liu

Examination Date: 8 December 2013

Examination Time: 11:00 a.m. – 12:00 noon

Time Allowed	1 hour
No. of questions	16 MC Questions

Do not open this question paper until instructed by the facilitator.

You are required to use the appropriate answer sheet to answer all questions in the examination paper. Failure to do so may render your examination script invalid.

This question paper must not be taken out of the examination hall.

Candidate Name: _____

Membership No.: _____

Question 1

Which of the following are more likely to be examples of related party transactions that give rise to significant risks under HKSA 550 Related parties?

1. Sales of goods to a related party with a commitment to repurchase after certain period.
2. Purchase of raw materials from a related party at normal discounts.
3. Transactions with off-shore related entities in jurisdictions with weak corporate laws.
4. Leasing of a property by entity to a related party at market rate.

- A (1) and (2) only
- B (1) and (3) only
- C (2) and (4) only
- D (2), (3) and (4) only
- E All of the above

Answer 1 B

HKSA 550.18 states that the auditor shall treat identified significant related party transactions outside the entity's normal course of business as giving rise to significant risks. Sentences (1) and (3) are examples of significant related party transactions that are carried out outside the entity's normal course of business.

Question 2

Which of the following statement is INCORRECT regarding factors which influence sample sizes for tests of internal control or tests of details?

- A An increase in the number of sampling units within the population will not increase the sample size for tests of internal control.
- B A decrease in the expected rate of deviation of controls will decrease the sample size for tests of internal control.
- C An increase in the extent to which the risk of misstatement is reduced by the operating effectiveness of controls will increase the sample size for tests of internal control.
- D An increase in the amount of misstatement the auditor expects to find in the population will increase the sample size for test of details.
- E A decrease in the tolerable misstatement will decrease the sample size for test of details.

Answer 2 E

- A is CORRECT. According to Appendix 2&3 of HKSA 530, for an increase in the number of sampling units within the population, there is only negligible effect on the sample size for both test of controls and test of details.
- B Is CORRECT. The lower the expected rate of deviation, the smaller the sample size needs to be so that the auditor is in a position to make a reasonable estimate of the actual rate of deviation.
- C is CORRECT. The greater the amount of misstatement the auditor expects to find in the population, the larger the sample size needs to be in order to make a reasonable estimate of the actual amount of misstatement in the population.
- D is CORRECT. The more the reliance placed on the tests of internal controls, the more sample size is needed to obtain more audit evidence from test of internal controls.
- E is INCORRECT. The lower the tolerable misstatement, the larger the sample size needs to be.

Question 3

Which of the following statements about materiality levels are INCORRECT under HKSA 320 Materiality in planning and performing an audit and HKSA 450 Evaluation of misstatements Identified during the audit?

- 1 Application of professional judgement is crucial when determining materiality.
- 2 There are only two types of materiality levels that need to be determined for each annual audit.
- 3 Non-compliance of debt covenant is unlikely to be considered as a material misstatement.
- 4 As a starting point in determining overall materiality (i.e. materiality for the financial statements as a whole), a percentage is often applied to a chosen benchmark.

- A (1) and (2) only
- B (2) and (3) only
- C (1), (2) and (3) only
- D (2), (3) and (4) only
- E All of the above are incorrect

Answer 3 B

- 1 is CORRECT. HKSA 320.4 mentions that the auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements.
- 2 is INCORRECT. For each audit, the auditor needs to determine at least three types of materiality levels, including materiality for the financial statements as a whole, performance materiality and clearly trivial.
- 3 is INCORRECT. HKSA 450.11 states that when evaluating the effect of uncorrected misstatements, both the size and nature of the misstatements must be considered. Non-compliance of debt covenant may affect the classification of borrowings and have impact on going-concern etc.
- 4 Is CORRECT. Refer to HKSA 320.A3.

Question 4

Which of the following statements about group audits are CORRECT under HKSA 600 Special considerations – audits of group financial statements (including the work of component auditors)?

- 1 If a component has a risk which is likely to be included as a significant risk of material misstatement of the group financial statements, that component is a significant component to the group.
 - 2 The determination of the components depends on the financial reporting structure of the group. A component can be a function, process, product, service or even a subgroup.
 - 3 The group engagement team needs to determine the component materiality for all the components that are under audit or review by the component auditors.
 - 4 For all significant components, a full audit using component materiality must be performed by the component auditors.
- A (1) and (2) only
B (2) and (3) only
C (1), (2) and (3) only
D (2), (3) and (4) only
E All of the above are correct

Answer 4 C

- 1 is CORRECT. HKSA 600.9 (m) definition of significant components.
- 2 Is CORRECT. HKSA 600.A2 and A4 mentions that some groups, however, may organize their financial reporting system by function, process, product or service (or by groups of products or services), or geographic locations. In these cases, the entity or business activity for which group or component management prepares financial information that is included in the group financial statements may be a function, process, product or service (or group of products or services), or geographic location.
- 3 Is CORRECT. HKSA 600.21(c) states that component materiality is determined for those components where component auditors will perform an audit or a review for purposes of the group audit.
- 4 Is INCORRECT. HKSA 600. 27 states that for a significant component due to the significant risks of material misstatements can perform a full audit or audit or specified audit procedures on the significant risks.

Question 5

Which of the following statements about responses to assessed risks are CORRECT under HKSA 330 The auditor's responses to assessed risks?

- 1 The auditor must design "overall responses" to address the financial statement level risks.
 - 2 When the approach to a significant risk consists only of substantive procedures, those procedures must include tests of details.
 - 3 If controls are extremely strong, the auditor need not perform any substantive procedures for any classes of transactions, account balances and disclosures.
 - 4 If the auditor plans to use audit evidence from a previous audit about the operating effectiveness of specific controls, the auditor does not need to test the controls again in the subsequent years until the controls change.
- A (1) and (2) only
B (2) and (3) only
C (3) and (4) only
D (1), (2) and (3) only
E (2), (3) and (4) only

Answer 5 A

- 1 is CORRECT. HKSA 330.5 states that the auditor shall design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.
- 2 is CORRECT. HKSA 330.21 states that when the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details.
- 3 is INCORRECT. HKSA 330.18 states that irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.
- 4 is INCORRECT. HKSA 330.14(b) states that if there have not been such changes, the auditor shall test the controls at least once in every third audit, and shall test some controls each audit to avoid the possibility of testing all the controls on which the auditor intends to rely in a single audit period with no testing of controls in the subsequent two audit periods.

Question 6

Which of the following statements about comparative information are CORRECT under HKSA 710?

- 1 Corresponding figures are amounts and other disclosures included as an integral part of the current period financial statements.
 - 2 When corresponding figures are included, the auditor's report refers to each period (current and prior) separately.
 - 3 If corresponding figures have not been audited, the auditor must state that the corresponding figures are unaudited in an 'other matter' paragraph and the auditor must obtain sufficient appropriate audit evidence that the opening figures do not contain material misstatements that affect the current period.
 - 4 If comparative financial statements have been audited by another auditor and the other auditor's report has not been included with the current period auditor's report, the auditor must state that the comparative financial statements were audited by a different firm in an 'emphasis of matter paragraph'.
- A (1) and (2) only
B (1) and (3) only
C (2) and (4) only
D (1), (2) and (3) only
E (1), (3) and (4) only

Answer 6 B

- 1 is CORRECT. Corresponding figures are defined as comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as current period figures). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.
- 2 is INCORRECT. When corresponding figures are included, the auditor's report refers to the **current period only** unless there is a prior period unresolved modification.
- 3 is CORRECT. HKSA710.14 states that if the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the

auditor's report that the corresponding figures are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

- 4 is INCORRECT. HKSA710.13 states that if the financial statements of the prior period were audited by a predecessor auditor and the auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures and decides to do so, the auditor shall state in an Other Matter paragraph in the auditor's report: (a) That the financial statements of the prior period were audited by the predecessor auditor; (b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and (c) The date of that report.

Question 7

Which of the following statement(s) is/are CORRECT about going concern assumption under HKSA 570?

- 1 Inability to pay creditors on due dates is an example of a condition that could cast doubt about the use of the going concern assumption.
- 2 Reliance on long term borrowings to finance long term assets is an example of a condition that cast doubt about the use of the going concern assumption.
- 3 If management has prepared an assessment of the entity's ability to continue as a going concern then the auditor must check that it covers a period of at least 12 months from the date of financial statements.
- 4 If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern, one of the additional audit procedures that the auditor must perform is requesting written representations from management, regarding their plans for future action and the feasibility of these plans.

- A (1) only
- B (1) and (2) only
- C (1) and (3) only
- D (1), (3) and (4) only
- E (2), (3) and (4) only

Answer 7 D

- 1 Is CORRECT. Inability to pay creditors on due dates is an example of a condition that could cast doubt about the use of the going concern assumption.
- 2 Is INCORRECT. Excessive reliance on short term borrowings to finance long term assets would be cause for concern but using long term funding to finance long term assets does not in itself cast doubt.
- 3 is CORRECT. If management has prepared an assessment of the entity's ability to continue a going concern then the auditor will check that it covers a period of at least 12 months from the date of the financial statements.
- 4 Is CORRECT. Refer to HKSA 570.16(e).

Question 8

Which of the following statements about fraud in an audit of financial statements under HKSA 240 are CORRECT?

1. There are mainly two types of fraud that cause material misstatements in financial statements. They include fraudulent financial reporting and misappropriation of assets.
2. High turnover of senior management and inadequate internal controls are examples of fraud risk factors.
3. There are two presumed significant risks as required under HKSA 240.
4. Testing journal entries is one of the audit procedures to address management override of controls.

- A (1) and (2) only
B (2) and (3) only
C (1), (2) and (4) only
D (1), (3) and (4) only
E All of the above are correct

Answer 8 E

- 1 is CORRECT. Refer to HKSA 240.2
2 is CORRECT. Refer to Appendix 1 of HKSA 240.
4 Is CORRECT. Refer to HKSA 240.26 and 31.
4 Is CORRECT. Refer to HKSA 240.32 (a)

Question 9

Which of the following statements are INCORRECT under HKSA 540 Audit of accounting estimates, including fair value accounting estimates and disclosures?

1. Estimation uncertainty is defined in terms of both the accounting estimate itself and the related disclosure.
 2. The higher the degree of estimation uncertainty, the lower the risk of material misstatement from an estimate.
 3. The degree of estimation uncertainty is higher if the accounting estimate is sensitive to changes in assumptions.
 4. The auditor does not need to review the outcome of accounting estimates included in the prior period financial statements or where applicable their re-estimation for the current period.
- A (1) and (2) only
B (1) and (3) only
C (2) and (4) only
D (1), (2) and (4) only
E (2), (3) and (4) only

Answer 9 C

- 1 Is CORRECT. Estimation uncertainty includes both the financial statements items involving accounting estimates and also its related disclosures.
- 2 is INCORRECT. Estimation uncertainty refers to the susceptibility of an accounting estimate and related disclosures to an inherent lack of precision in its measurement under HKSA 540. Therefore, a higher estimation uncertainty implies a higher risk of material misstatement.
- 3 Is CORRECT. According to HKSA 540.A92, if the accounting estimates is highly sensitive to certain assumptions and therefore subject to higher estimation uncertainty, indicating the accounting estimate may be a significant risk.
- 4 Is INCORRECT. According to HKSA 540.9, the auditor shall review the outcome of accounting estimates included in the prior period financial statements, or, where applicable, their subsequent re-estimation for the purpose of the current period.

Question 10

Which of the following statements are CORRECT under HKSA 580 Written representations and HKSA 450 Evaluation of misstatements identified during the audit?

- 1 Written representations from management is required for every annual audit.
 - 2 The written representation letter must be dated as near as practicable to, but not after, the financial year end date.
 - 3 The auditors request management to represent that they have fulfilled their responsibility for the preparation of the financial statements.
 - 4 A list of uncorrected misstatements is included in or attached to the written representation letter.
- A (1) and (2) only
B (2) and (3) only
C (2) and (4) only
D (1), (3) and (4) only
E All of the above are correct

Answer 10 D

- 1 is CORRECT. According to HKSA 580.3, audit evidence is the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Written representations are necessary information that the auditor requires in connection with the audit of the entity's financial statements. Accordingly, similar to responses to inquiries, written representations are audit evidence.
- 2 Is INCORRECT. According to HKSA 580.14, the date of the written representations shall be as near as practicable to, but not after, the date of the auditor's report on the financial statements. The written representations shall be for all financial statements and period(s) referred to in the auditor's report.
- 3 Is CORRECT. According to HKSA 580.10, the auditor shall request management to provide a written representation that it has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation, as set out in the terms of the audit engagement
- 4 Is CORRECT. According to Appendix 2 of HKSA 580 and HKSA 450.14, a listed of uncorrected misstatement is attached to the written representation letter.

Question 11

Which of the following statements about using the work of an auditor's expert are CORRECT under HKSA 620?

- 1 An auditor's expert refers to an individual or organization possessing expertise other than accounting or auditing field.
 - 2 The auditor must evaluate the competence, capability and objectivity of the auditor's expert.
 - 3 The auditor's report must not refer to the work of an auditor's expert unless required by law and regulations.
 - 4 An auditor's expert may be either an internal expert or an external expert.
-
- A (1) and (2) only
 - B (2) and (4) only
 - C (1), (2) and (3) only
 - D (2), (3) and (4) only
 - E All of the above are correct.

Answer 11 E

- 1 is CORRECT. HKSA 620.6(a) mentions that Auditor's expert – An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence.
- 2 is CORRECT. HKSA 620.9 mentions that the auditor shall evaluate whether the auditor's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. In the case of an auditor's external expert, the evaluation of objectivity shall include inquiry regarding interests and relationships that may create a threat to that expert's objectivity.
- 3 is CORRECT. The engagement partner is solely responsible for the audit opinion of the financial statements and cannot refer to the work of others in the audit opinion unless required by law and regulations.
- 4 is CORRECT. An auditor's expert may be either an auditor's internal expert (who is a partner or staff, including temporary staff, of the auditor's firm or a network firm), or an auditor's external expert.

Question 12

Which of the following statements about internal control component and control risk are CORRECT?

- 1 Monitoring of controls are the processes to assess the effectiveness of internal control performance over time.
 - 2 Control environment sets the tone of an organization influencing the control awareness of its people.
 - 3 A company that is based in a highly competitive industry where products have to be developed and launched quickly in order to keep up is more exposed to control risk.
 - 4 A company which has suffered from the loss of several senior members of the finance team is more exposed to inherent risk.
- A (1) and (2) only
B (3) and (4) only
C (1), (2) and (3) only
D (1), (2) and (4) only
E (2), (3) and (4) only

Answer 12 A

- 1 is CORRECT. HKSA 315.22 mentions that monitoring of controls refers to activities that the entity uses to monitor internal control over financial reporting, including those related to those control activities relevant to the audit, and how the entity initiates remedial actions to deficiencies in its controls.
- 2 is CORRECT. HKSA 315.A69 mentions that the control environment sets the tone of an organization, influencing the control consciousness of its people.
- 3 is INCORRECT. The risk involved is inherent risk rather than control risk.
- 4 Is INCORRECT. The loss of several senior members of the finance team may pose risk to the implementation of internal controls relevant to financial reporting and hence, exposed to control risk.

Question 13

Which of the following statement(s) on 'subsequent events' is/are CORRECT under HKSA 560?

- 1 Between the date of the financial statements and the date of the auditor's report, the auditor must perform audit procedures designed to obtain sufficient appropriate evidence that all events that require adjustment or disclosure have been identified.
 - 2 After the date the financial statements have been issued, the auditor has no obligations to perform further audit procedures or respond to facts which become known.
 - 3 Dividends declared after the year-end is an example of non-adjusting event.
 - 4 One of the audit procedures to test subsequent events is to review the latest subsequent interim financial statements, budgets, cash flow forecasts and other management reports.
- A (1) only
B (1) and (2) only
C (1) and (4) only
D (1), (3) and (4) only
E (2), (3) and (4) only

Answer 13 D

- 1 Is CORRECT. HKSA 560.6 states that the auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified. The auditor is not, however, expected to perform additional audit procedures on matters to which previously applied audit procedures have provided satisfactory conclusions
- 2 is INCORRECT. HKSA 560.14 states that after the financial statements have been issued, the auditor has no obligation to perform any audit procedures regarding such financial statements. However, if, after the financial statements have been issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:

- (a) Discuss the matter with management and, where appropriate, those charged with governance; (b) Determine whether the financial statements need amendment; and, if so, (c) Inquire how management intends to address the matter in the financial statements.
- 3 is CORRECT. Dividend declared after the year end are events that provide evidence of conditions that arose after the date of the financial statements.
- 4 is CORRECT. Refer to HKSA 560.7 (d).

Question 14

Which of the following circumstances will an auditor need to modify the audit opinion?

- 1 If the auditor is unable to obtain sufficient appropriate evidence to form a conclusion due to limitation imposed by management.
 - 2 If the auditor agrees that there is material uncertainty in relation to the ability of the entity to continue as a going concern which has been disclosed properly in the financial statements.
 - 3 If the auditor concludes that the financial statements are materially misstated due to the selection of an inappropriate accounting policy.
 - 4 If the opening balances contain a misstatement that materially affect the current year's financial statements and the effect of the misstatement is not appropriately accounted for, or not adequately presented or disclosed.
- A (1) and (2) only
B (1) and (3) only
C (1), (3) and (4) only
D (2), (3) and (4) only
E All of the above

Answer 14 C

- 1 Is CORRECT. HKSA 700.17 states that If the auditor: (a) concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or (b) is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor shall modify the opinion in the auditor's report in accordance with HKSA 705.
- 2 is INCORRECT. If there is a material uncertainty in relation to going concern which has been disclosed properly, a modification of the audit opinion will not be required. Instead an emphasis of matter paragraph is used to highlight the matter.
- 3 Is CORRECT. HKSA 700.17 states that If the auditor: (a) concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or (b) is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor shall modify the opinion in the auditor's report in accordance with HKSA 705.
- 4 is CORRECT. See HKSA 510.11

Question 15

Which of the following statements about using substantive analytical procedures are CORRECT?

- 1 Substantive analytical procedure is a mandatory audit procedure for every audit.
 - 2 The higher the auditor's assessment of risk, the higher the amount of difference considered acceptable without investigation.
 - 3 The auditor's determination of the amount of difference from expectation that can be accepted without further investigation is influenced by materiality.
 - 4 The maximum acceptable difference may be defined as a numerical value or as a percentage.
-
- A (1) and (2) only
 - B (3) and (4) only
 - C (2), (3) and (4) only
 - D (1), (3) and (4) only
 - E All of the above are correct

Answer 15 B

- 1 Is INCORRECT. There are no requirements under HKSA 330 and HKSA 520 that substantive analytical procedures must be performed in every audit.
- 2 Is INCORRECT. HKSA 330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of risk. Accordingly, as the assessed risk increases, the amount of difference considered acceptable without investigation decreases in order to achieve the desired level of persuasive evidence.
- 3 Is CORRECT. HKSA 520.A16 that the auditor's determination of the amount of difference from the expectation that can be accepted without further investigation is influenced by materiality and the consistency with the desired level of assurance, taking account of the possibility that a misstatement, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.
- 4 Is CORRECT. The maximum acceptable difference may be defined as a numerical value or as a percentage.

Question 16

Which of the following statements about quality control under HKSQC 1 are CORRECT?

- 1 An audit firm must assign an engagement quality control reviewer for all audits of financial statements of listed entities.
 - 2 Monitoring process includes ongoing evaluation of the firm's quality control system and inspection of at least one completed engagement for each engagement partner on a cyclical basis.
 - 3 Monitoring applies to all practices. There is no exemption on the grounds of size or nature of client base.
 - 4 The time limit for the completion of the assembly of audit engagement files would ordinarily not be more than 60 days after the date of the auditor's report, unless specified by law or regulation.
- A (1) and (2) only
B (2) and (3) only
C (1), (2) and (4) only
D (1), (3) and (4) only
E All of the above are correct

Answer 16 **E**

- 1 is CORRECT. Refer to the HKSQC 1.35(a)
- 2 is CORRECT. Refer to the HKSQC 1.48(a)
- 3 is CORRECT. Refer to the HKSQC 1.4 which mentions that HKSQC 1 applies to all firms of professional accountants. Paragraph A68 mentions how monitoring can be applied to smaller firms.
- 4 is CORRECT. Refer to the HKSQC.A54