CPA-TEST Q&As

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QUESTION 1

In assessing the competence and objectivity of an entity\\'s internal auditor, an independent auditor least likely would consider information obtained from:

A. Discussions with management personnel.

B. External quality reviews of the internal auditor\\'s activities.

C. Previous experience with the internal auditor.

D. The results of analytical procedures.

Correct Answer: D

Explanation: Choice "d" is correct. Analytical procedures may be used to enhance the auditor\\'s understanding of the client\\'s business or to evaluate financial statement assertions, but generally would not be helpful in assessing the competence and objectivity of an entity\\'s internal auditor. Choice "a" is incorrect. In assessing competence and objectivity, the auditor usually considers information obtained from discussions with management personnel. Choice "b" is incorrect. In assessing competence and objectivity, the auditor usually considers information

obtained from external quality reviews of internal audit activities.

Choice "c" is incorrect. In assessing competence and objectivity, the auditor usually considers information

obtained from previous experience with the internal audit function.

QUESTION 2

ABC Inc. is considering implementing a lock-box collection system at a cost of $80,000 per year. Annual sales are $90 million, and the lock-box system will reduce collection time by 3 days. If ABC can invest funds at 8 percent, should it use the lock-box system? Assume a 360-day year.

A. Yes, producing savings of $60,000 per year.

B. No, producing a loss of $20,000 per year.

C. No, producing a loss of $60,000 per year.

D. No, producing a loss of $140,000 per year.

Correct Answer: B

Explanation:

Choice "b" is correct. No, do not use the lock-box system, which produces a loss of $20,000 per year.

$$\frac{3\text{ days}}{360\text{ days}} \times \$90{,}000{,}000 \times \frac{8}{10} = \begin{array}{rl} \$80{,}000 & \text{Lock-box cost} \\ \underline{60{,}000} & \text{Investment income} \\ \underline{\underline{\$20{,}000}} & \text{Loss per year} \end{array}$$

QUESTION 3

A material loss should be presented separately as a component of income from continuing operations when it is:

A. An extraordinary item.

B. A cumulative effect type change in accounting principle.

C. Unusual in nature and infrequent in occurrence.

D. Not unusual in nature but infrequent in occurrence.

Correct Answer: D

Explanation:

Choice "d" is correct. Gains or losses that are unusual in nature or occur infrequently but not both, are presented as a component of income from continuing operations. Choice "a" is incorrect. Extraordinary items are shown net of tax in a separate section of the income statement after income from continuing operations. Choice "b" is incorrect. Cumulative effects of changes in accounting principle are now shown net of tax as an adjustment to the opening balance of retained earnings in the retained earnings statement. This treatment is called retrospective application. There really are no longer any cumulative effect types of changes in accounting principle. The cumulative effect is merely how the amount of the change is measured. Choice "c" is incorrect. This is the definition of an extraordinary item.

QUESTION 4

Which of the following should be disclosed in a summary of significant accounting policies?

I. Management\\'s intention to maintain or vary the dividend payout ratio.

II. Criteria for determining which investments are treated as cash equivalents.

III.

Composition of the sales order backlog by segment.

A.

I only.

B.

I and III.

C.

II only.

D. II and III.

Correct Answer: C

Explanation:

Choice "c" is correct. II only.

The criteria for determining which investments are treated as "cash equivalents" is a method of accounting

policies that needs to be disclosed in the summary of significant accounting policies.

Choice "a" is incorrect. Management\\'s intention to maintain or vary the "dividend payout ratio" is not an

"accounting policy."

Choices "b" and "d" are incorrect. Composition of the sales order backlog by segment is not an

"accounting policy."

QUESTION 5

When a partner in a general partnership lacks actual or apparent authority to contract on behalf of the partnership, and the party contracted with is aware of this fact, the partnership will be bound by the contract if the other partners:

	Ratify the contract	*Amend the partnership agreement*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

A. Option A

B. Option B

C. Option C

D. Option D

Correct Answer: B

Explanation:

Choice "b" is correct. "Yes - No."

Rule: The authority of partners is governed by agency law. Under agency law, a principal is not bound to the third party unless the agent had actual authority or apparent authority. When the agent has no actual authority and no apparent authority, the principal (in this case the partnership) will only be liable if it chooses to adopt the agreement (i.e., ratify).

Rule: Amending the partnership agreement (presumably to grant authority) will not cause the partnership to be bound because authority must exist at the time the contract is made or the partnership must ratify the contract.

Choices "a", "c", and "d" are incorrect, per the above rules.