

## 2014 S1 A1

1.1 Which one of the following types of audit tests would be the most persuasive if an internal auditor wanted assurance of the existence of inventory stored in a warehouse?

1. **Physically inspecting the inventory in the warehouse.**
2. Obtaining written confirmation from management as to the existence of the inventory.
3. Examination of the warehouse receipts contained in the auditee's records.
4. Examination of the shipping documents supporting recorded transfers to and from the warehouse.

1.2 Which one of the following is the best source for an internal audit team to use in identifying common external risks faced by a company?

1. Questionnaires.
2. **Current research reported in professional journals and textbooks.**
3. Flowcharts.
4. Review lists or reminder lists.

1.3 Working papers should include ...

1. All working papers prepared during a previous audit.
2. **Documentation substantiating the examination and evaluation of the adequacy and effectiveness of the system of internal control.**
3. Copies of all procedures that were reviewed during the internal audit.
4. Copies of all source documents examined in the course of the internal audit.

1.4 An internal auditor found that the supervisor does not properly approve employee time records in one department. Which one of the following errors can result from this?

1. Duplicate pay cheques might be issued.
2. The wrong hourly rate could be used to calculate gross wages.
3. **Employees might be paid for hours they did not work.**
4. Payroll cheques might not be distributed to the appropriate payees.

1.5 Which one of the following is an audit objective?

1. Recalculate each month's bank reconciliation.

2. Analyse the pattern of any cash shortages.
3. Observe the deposit of the day's cash receipts.
- 4. Evaluate whether cash receipts are adequately safeguarded.**

1.6 Which of the following conduct violates the integrity principle of the Code of Ethics?

1. The internal auditors perform a detailed risk assessment and identify the key controls with regard to credit sales before they decided on the tests to be performed.
2. An internal auditor is assigned to an audit of controls in the procurement section, which is headed by his father.
3. While auditing the controls over wage pay-outs, an auditor finds that some controls have been circumvented. She discusses her finding of a possible fraud with her colleague in the canteen over lunch.
- 4. The internal auditor uses an unrevised audit programme, used three years ago, to conduct an organisation-wide audit on credit sales.**

1.7 Observation is considered a reliable audit procedure, but one that is limited in usefulness. However, it is used in a number of different engagement situations. Which of the following statements is true regarding observation as an engagement technique?

1. It is the most effective audit method to use in filling out internal control questionnaires.
2. It is the most persuasive technique for determining if fraud has occurred.
- 3. It is rarely sufficient to satisfy any assertion other than existence.**
4. It is the most persuasive methodology to learn how transactions are really processed during the period under review.

1.8 An internal auditor has set an engagement objective of determining whether mail room staff is fully productive. Which of the following engagement techniques will best meet this objective?

1. Inquiry.
2. Observation.
- 3. Analytical review entailing comparison between this mail room staff's productivity levels with similar organisations.**
4. Inspection of documents.

1.9 Which of the following does not describe one of the functions of the audit working papers?

1. Facilitates third-party reviews.
- 2. Aids in the professional development of the operating staff.**
3. Aids in the planning, performance and review of audits.
4. Provides the principal support for audit communications.

1.10 Which of the following are elements included in the control environment described in the COSO internal control framework?

- 1. Integrity and ethical values, management's philosophy and operating style, and human policies.**
2. Organisational structure, commitment to competence and planning.
3. Competence of personnel, backup facilities, laws and regulations.
4. Risk assessment, assignment of responsibility and human resource practices.

1.11 The policies and procedures helping to ensure that management directives are executed and actions are taken to address risks to the achievement of objectives describes...

- 1. Control activities.**
2. Risk assessments.
3. Control environments.
4. Monitoring.

1.12 In a final audit report, which attribute should be addressed by the recommendation?

1. Condition.
- 2. Cause.**
3. Effect.
4. Criteria.

1.13 According to the IIA Standards, final engagement communication should be distributed to those members of the organisation who are able to ensure that engagement results are given due consideration. For higher-level members of the organisation, that requirement can be usually satisfied with...

1. Oral reports.
2. Interim reports.

### 3. Summary reports

4. Final written reports only.

1.14 Which option best describes why, during an internal audit assignment, an internal auditor compares the inventory turnover rate of a company with established industry standards?

1. To evaluate the accuracy of internal financial reports of the company.
2. To test the company's controls designed to safeguard assets.
- 3. To assess the reasonableness of the disclosed performance (profits) of the company and to determine where additional audit work may be needed.**
4. To determine whether the company is complying with established procedures regarding inventory levels.

1.15 An internal auditor has set an audit objective of determining whether all cash receipts are deposited daily. To achieve this objective, the internal auditor interviewed the supervisor, who assured him that all cash receipts are deposited as soon as is reasonably possible. The assurance of the supervisor can be used as evidence that is...

1. Sufficient but not reliable or relevant.
2. Sufficient, reliable and relevant.
3. Not sufficient, reliable or relevant.
- 4. Relevant but not sufficient or reliable.**

1.16 The identification of damaged and obsolete inventory is important when valuing inventory. The best auditing procedure to discover damaged inventory included in closing inventory is to...

1. Compare the physical quantities of slow-moving items with corresponding quantities of the previous year.
2. Review management's inventory certificate for accuracy.
3. Test the overall fairness of the inventory values by comparing the company's inventory turnover ratio with the industry average.
- 4. Inspect inventory during the physical inventory count.**

1.17 Statistical sampling differs from other sampling methods in the sense that...

1. An auditor does not have to exercise professional judgement when applying statistical sampling as he/she must when applying other sampling methods.

2. Statistical sampling produces representative samples, whereas the other methods do not.
3. Statistical sampling can deliver absolute assurance, which is not possible with other sampling methods.
4. **Statistical sampling is based on the theory of probability, which is not the case with other sampling methods.**

1.18 Which form of audit evidence would the internal auditor consider to be the most reliable?

1. A sales invoice of the organisation together with a delivery note signed by the customer.
2. **Direct confirmation from a debtor of his account balance after the internal auditor has mailed the account personally to the debtor.**
3. A crossed cheque and bank statement submitted by the auditee to the internal auditor upon his request during the audit.
4. A pay sheet prepared by the wage clerk and checked and approved by the accountant.

1.19 The main reason for issuing an internal audit report is to...

1. Give auditees an opportunity to respond to the matters addressed by the report.
2. **Report to interested parties on audit findings and recommendations.**
3. Give management an opportunity to take corrective action for reported findings.
4. Provide the external auditors with a basis for relying on the work of the internal auditor.

1.20 All the members of your audit team received training that enables them to discuss the conclusions and recommendations during an exit interview with the appropriate manager before the final audit report is issued. What is a primary reason for such an exit interview?

1. **The notes on the interview can be a valuable aid if disputes arise during the discussion of the final audit report.**
2. The notes of the interview become a basis for follow-up audits.
3. The IIA Standards require an exit interview.
4. The information learnt can be used to utilise scarce audit resources better in future audits.

## 2014 S1 A2

1.1 Which one of the following options violates the objectivity principle of the Code of Ethics?

- A. The internal audit activity publishes an informative article on the organisation's intranet, setting out the advantages of introducing a time-management clock-in system for the administrative staff.
- B. Since everyone in the organisation is aware of the IT department's inability to arrange suitable back-up facilities for the financial systems of the organisation, the internal auditor makes no mention of the fact in his report following an audit of the general IT controls.**
- C. An internal audit activity appoints a chartered accountant who has recently completed her articles with an auditing firm and assigns her to lead an audit of control of the purchasing and implementation of new IT systems.
- D. While auditing controls over wage pay-outs, an auditor finds that some controls have been circumvented. She discusses her finding of a possible fraud with the internal audit manager in his office.

1.2 Two organisations have recently merged. The audit committee has asked the internal auditors from both organisations to assess risks that should be addressed after the merger. One manager has suggested that the engagement teams jointly examine the organisational culture and the tone at the top to identify control risks associated with the proposed merger. Which one of the following statement is true?

- A. The organisational culture is not a part of the control environment and therefore should not be considered for a proposed engagement.
- B. Although the organisational culture could be considered part of the control environment, the assessment of such an environment would be highly subjective and therefore not useful.
- C. Differences in the organisational culture should be systemically identified because the difference may present major risks to the success of the merger. However, identifying difference is not an appropriate activity because it is political and subjective.
- D. None of the answers are correct.**

1.3 The primary purpose of an engagement working paper prepared in connection with payroll expense is to...

- A. Verify the work done by the internal auditor.
- B. Record the names of all the employees.
- C. Record payroll data and analyses to support reported recommendations.**
- D. Provide documentation to support payroll taxes due.

1.4 An internal auditor's working paper should support the observations, conclusions and recommendations to be communicated. One of the purposes of this requirement is to...

- A. Provide support for the internal audit activity's financial budget.
- B. Provide control over working papers.
- C. Permit the audit committee to review observations, conclusions and recommendations.
- D. Facilitate quality assurance reviews.**

1.5 An organisation's directors, management, external auditors and internal auditors all play important roles in creating a proper control environment. Senior management is primarily responsible for...

- A. Establishing a proper organisation culture and specifying a system of internal control.**
- B. Ensuring that external and internal auditors adequately monitor the control environment.
- C. Implementing and monitoring controls designed by the board of directors.
- D. Designing and operating a control system that provides reasonable assurance that established objectives and goals will be achieved.

1.6 There are certain types of IT risks that tend to be common across organisations and industries. Which one of the following risks can be defined as unauthorised disclosure of business partners' proprietary information or individual's personal information that may result in loss of business, lawsuits and reputation impairment?

- A. Access risk.
- B. B. Availability risk.
- C. Confidentiality and privacy risk.**
- D. System reliability and information integrity risk

1.7 The internal audit activity customarily has a dual relationship with management and the audit committee. This means that...

- A. Management should help the internal audit activity by revising and forwarding engagement communications to the audit committee.
- B. The accuracy of engagement communications should be verified with management and the internal audit activity should then report to management and the audit committee.**

- C. The internal audit activity should report directly to the audit committee without corroborating engagement communications with management.
- D. Ideally, the internal audit activity works under the audit committee but reports to the chief operating officer on all engagement relating to operations.

1.8 When planning an attribute sampling application, the difference between the expected error rate and the maximum tolerable error rate is the planned...

- A. Skewness.
- B. Dispersion.
- C. Reliability.
- D. Precision.**

1.9 In preparing a sampling plan for an inventory pricing test, which of the following describes an advantage of statistical sampling over non-statistical sampling?

- A. Requires non quantitative expression of sample results.
- B. Provides a quantitative measure of sampling risk.**
- C. Minimises non-sampling risk.
- D. Reduces the level of tolerable error.

1.10 A specified range is based on an estimate of a population characteristic calculated from a random sample. The probability that the range contains the true population value is the...

- A. Error rate.
- B. Confidence level.**
- C. Standard error of the mean.
- D. Lower precision limit.

## **2014 S2 A1**

1.1 Which one of the following alternatives violates the integrity principle of the Code of Ethics?

- 1. In loyalty to her organisation which is experiencing financial difficulty, a chief audit executive (CAE) ignores the scheduled audit of the final tax return for the current tax year, knowing that management is understating taxable income.**

2. While auditing controls over wage pay-outs, an auditor finds that some controls have been circumvented. She discusses her finding of a possible fraud with her colleague in the canteen over lunch.
3. An internal auditor is assigned to an audit of controls in the procurement section, which is headed by his father.
4. While auditing controls over wage pay-outs, an auditor finds that some controls have been circumvented. She discusses her finding and the possibility of fraud with the internal audit manager in his office.

1.2 When reviewing the average collection period of the debtors' accounts of the company, the internal auditor observes an increase from 30 to 60 days in the collection period for the current financial year.

Which one of the following alternatives is the most likely cause of this happening?

- 1. Slackening of the organisation's credit control.**
2. Rising of the profit margin on sales.
3. An increase in the organisation's sales volume.
4. A smaller incidence of slow-moving inventory.

1.3 Due professional care implies reasonable care and competence, not infallibility or extraordinary performance. Thus, which of the following is unnecessary?

1. The conduct of examinations and verifications to a reasonable extent.
- 2. The conduct of extensive examinations.**
3. The reasonableness assurance that compliance does exist.
4. The consideration of possibility of material irregularities.

1.4 An internal auditor observes that a receivables clerk has physical access to and control of cash receipts. This has alerted him but he worked with the clerk several years before and has a high level of trust in the individual. Therefore, the auditor notes in the working papers that controls over receipts are adequate. Has the auditor exercised due professional care?

1. Yes, reasonable care has been taken.
- 2. No, irregularities were not noted.**
3. No, alertness to conditions most likely indicative of irregularities was not shown.
4. Yes, the working papers were annotated.

1.5 In evaluating the effectiveness and efficiency with which resources are employed, an internal auditor is responsible for...

1. Verifying the existence of assets.
- 2. Determining the extent to which adequate operating criteria have been established.**
3. Reviewing the reliability of operating information.
4. Verifying the accuracy of asset valuation.

1.6 Controls should be designed to ensure that...

1. Management's plans have not been circumvented by worker collusion.
2. Management's planning, organising and directing processes are properly evaluated.
- 3. Operations are performed efficiently.**
4. The internal audit activity's guidance and oversight of management's performance is accomplished economically and efficiently.

1.7 Developing engagement observations, conclusions and recommendations involves comparing the condition with the relevant standard or criterion. Which of the following choices best represents an appropriate standard or criterion to support engagement observations, conclusions and recommendations?

1. An internal accounting control principle cited and copied from a public accounting reference.
2. A sound industry practice, based on the internal auditor's knowledge and experience obtained during many engagement assignments within the organisation.
3. A quality standard operating procedure (number and date) for the department.
- 4. All the answers represent an appropriate standard or criterion to support engagement observations, conclusions and recommendations.**

1.8 According to King III Report, which of the following is not the audit committee's responsibility regarding combined assurance?

1. Monitoring the appropriateness of the company's combined assurance model.
2. Ensuring all the significant risks facing the company are adequately dealt with.
3. Monitoring the relationship between the external assurance providers and the organisation.
- 4. Providing an independent assurance on risk management and systems of internal control.**

1.9 In combined assurance, which of the following is not an external assurance provider?

1. Sustainability assurance providers.
2. External auditors.
- 3. The risk management function.**
4. Regulators.

1.10 For good internal control in the revenue and receipts cycle, company policy should clearly indicate that defective merchandise returned by customers is to be delivered to the...

1. Sales clerk.
2. Inventory control clerk.
- 3. Goods receiving clerk.**
4. Accounts receivable clerk.

1.11 The use of incorrect audit procedures in a sample for a given internal audit objective is an example of....

1. Alpha risk.
2. Sampling risk.
- 3. Non-sampling risk.**
4. Beta risk.

1.12 Which one of the following analytical trends indicates the possibility of an increase in obsolete inventory on hand?

1. A decrease in the ratio of inventory to accounts payable.
- 2. A decrease in the inventory turnover rate.**
3. A decrease in the ratio of inventory to accounts receivable.
4. A decrease in the ratio of gross profit to sales.

1.13 The cash receipts function should be separated from the related recordkeeping function in an organisation in order to...

- 1. Physically safeguard the cash receipts.**
2. Minimise undetected misappropriations of cash receipts.

3. Prevent paying cash disbursements from the cash receipts.
4. Establish accountability when cash is first received.

1.14 Which one of the following situations represents an internal control weakness in the payroll department?

- 1. Pay cheques are distributed by employees' immediate supervisors.**
2. Payroll department personnel are rotated in their duties.
3. Payroll records are reconciled with quarterly tax reports.
4. The timekeeping function is independent of the payroll department.

1.15 Select the correct option to complete the following sentence:

Controls are only effective and useful if ...

- 1. They are developed and implemented in order to achieve a specific objective.**
2. They are recommended by internal and external auditors.
3. They are applied to financial transactions of an organisation.
4. They eliminate the possibility that irregularities can occur.

1.16 Which one of the following statements is an appropriate internal audit objective?

- 1. To determine whether inventory on hand is sufficient to meet the projected sales targets.**
2. To observe the physical inventory count.
3. To include information about stock-out situations in the internal audit report.
4. To search for the existence of obsolete inventory by computing inventory turnover by product line.

1.17 Which one of the following activities may be performed by an internal auditor?

1. Drafting procedures for systems of control.
2. Designing systems of control.
- 3. Reviewing systems of control before implementation.**
4. Installing systems of control.

1.18 The International Standards for the Professional Practice of Internal Auditing, Standard 2420 states seven qualities for good communications. Avoiding unnecessary technical language is best associated with which of the following qualities of communication?

1. Concise.
2. Complete.
- 3. Clear.**
4. 4 Accurate.

1.19 During an audit of the receiving operations of a manufacturing organisation, an internal auditor will be most concerned with the risk that the function has...

1. Received goods that were ordered.
2. An insufficient staff complement to perform all the tasks.
- 3. Failed to detect the receipt of goods of poor quality**
4. Paid inflated prices for goods from related parties.

1.20 An internal auditor is observing cash sales to determine if customers are given written receipts. The objective of this test is to ensure that...

1. Cash received equals the total of the receipts.
2. Customers are charged authorised prices.
3. Cash balances are correct.
- 4. All cash sales are recorded.**

## **2014 S2 A2**

1.1 When sampling methods are used, the concept of sufficiency of information means that the sample selected provides \_\_\_\_\_.

- A. Reasonable assurance that the sample is representative of the sampled population.**
- B. Reasonable assurance that the evidence has a logical relationship with the internal audit objective.
- C. Absolute assurance that the sample is representative of the population.
- D. The best evidence that is reasonably obtained.

1.2 Which of the following are elements included in the control environment described in the COSO internal control framework?

- A. Integrity and ethical values, management's philosophy and operating style, and strategic alignment.**
- B. Organisational structure, commitment to competence and planning.
- C. Commitment to competence, backup facilities, board of directors or audit committee.
- D. Management's philosophy and operating style, assignment of responsibility and human resource practices.

1.3 The attitudes and actions of the board and management regarding the significance of control within the organisation describes...

- A. Risk assessments.
- B. Control environments.**
- C. Control activities.
- D. Monitoring.

1.4 When an internal auditor uses monetary-unit statistical sampling to examine the total value of invoices, each invoice...

- A. Has an equal probability of being selected.
- B. Has an unknown probability of being selected.
- C. Can be represented by no more than one monetary unit.
- D. Has a probability proportional to its monetary value of being selected.**

1.5 An organisation's directors, management, external auditors and internal auditors all play important roles in creating a proper control environment. Senior management is primarily responsible for...

- A. Establishing a proper organisation culture and specifying a system of internal control.**
- B. Ensuring that external and internal auditors adequately monitor the control environment.
- C. Implementing and monitoring controls designed by the board of directors.
- D. Designing and operating a control system that provides reasonable assurance that established objectives and goals will be achieved.

1.6 Which of the following represents the best statement of responsibilities for risk management?

- |                                       |                               |                         |
|---------------------------------------|-------------------------------|-------------------------|
| A. Management Responsibility for risk | Internal Audit Oversight role | Board Advisory role     |
| B. Oversight role for risk            | Responsibility                | Advisory role           |
| <b>C. Responsibility for risk.</b>    | <b>Advisory role</b>          | <b>Oversight role</b>   |
| D. Oversight role                     | Advisory role                 | Responsibility for risk |

1.7 The internal audit activity customarily has a dual relationship with management and the audit committee. This means that...

- A. Management should help the internal audit activity by revising and forwarding engagement communications to the audit committee.
- B. The accuracy of engagement communications should be verified with management and the internal audit activity should then report to management and the audit committee.**
- C. The internal audit activity should report directly to the audit committee without corroborating engagement communications with management.
- D. Ideally, the internal audit activity works under the audit committee but reports to the chief operating officer on all engagement relating to operations.

1.8 In a sampling application, the group of items about which the auditor wants to estimate some characteristic is called the...

- A. Attribute of interest.
- B. Population.**
- C. Sample.
- D. Sampling unit.

1.9 Monetary-unit sampling (MUS) is most useful when the internal auditor...

- A. Is concerned with overstatements.**
- B. Is testing the accounts payable balances.
- C. Expects to find several material misstatements in the sample.
- D. Cannot cumulatively arrange the population items.

1.10 One payroll audit objective is to determine whether segregation of duties is proper. Which of the following activities is incompatible?

- A. Hiring employees and authorising changes in the pay rates.
- B. Preparing the payroll and filling payroll tax forms.
- C. Signing and distributing the payroll cheques.
- D. Preparing attendance data and preparing the payroll.**

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1.1 Vouching entails verifying recorded amounts by examining the underlying documents from the \_\_\_\_\_ documents to the \_\_\_\_\_ documents.

- 1. Final; original.**
- 2. Final; previous.
- 3. Original; final.
- 4. Original; subsequent.

1.2 The proper organisational role of internal auditing is to

- 1. Assist the external auditor to reduce external audit fees.
- 2. Perform studies to assist in the attainment of more efficient operations.
- 3. Serve as the investigative arm of the Board.
- 4. Serve as an independent, objective assurance and consulting activity that adds value to operations.**

1.3 An internal auditor discovered some material inefficiencies in a purchasing function. The purchasing manager is the internal auditor's next door neighbour and best friend. In accordance with the IIA Code of Ethics, the internal auditor should

- 1. Objectively include the facts of the case in the engagement communications.**
- 2. Not report the incident because of loyalty to the friend.
- 3. Include the facts of the case in a special communication submitted only to the friend.
- 4. Not report the friend unless the activity is illegal.

1.4 A recommendation in a final engagement communication should address what attribute?

1. **Cause.**
2. Statement of condition.
3. Criteria.
4. Effect.

1.5 Which of the following engagement procedures provides the best information about the collectability of notes receivable?

1. Confirmation of notes receivable balances with the debtors.
2. Examination of notes for appropriate debtor's signatures.
3. Reconciliation of the detail of notes receivable and the provision for uncollectible amounts to the general ledger accounts.
4. **Examination of cash receipts records to determine the promptness of interest and principal payments.**

1.6 An internal auditor performed a formal consulting engagement for ABC Limited on June 1, Year 1. When is the earliest time the auditor can perform assurance services for ABC Limited and be considered independent and objective?

1. January 1, Year 2.
2. **June 1, Year 2.**
3. July 1, Year 1.
4. June 2, Year 2.

1.7 In sampling application, the group of items about which the auditor wants to estimate some characteristics is called the

1. **Population.**
2. Attribute of interest.
3. Sample.
4. Sampling unit.

1.8 An internal auditor is planning to use attribute sampling to test the effectiveness of a specific internal control relating to approvals for cash disbursements. In attribute sampling, decreasing the estimated occurrence rate from 5% to 4% while keeping all other sample size planning factors exactly the same would result in a revised sample size that would be

1. Larger.

2. **Smaller.**

3. Unchanged.

4. Indeterminate.

1.9 When an internal auditor uses monetary-unit statistical sampling to examine the total value of invoices, each invoice

1. Has an equal probability of being selected.

2. Can be represented by no more than one monetary unit.

3. Has an unknown probability of being selected.

4. **Has a probability proportional to its monetary value of being selected.**

1.10 An internal auditor has set an engagement objective of determining whether the planned rate of return on investment in international operations has been achieved. Which of the following engagement procedures will best meet this objective?

1. Inspection of documents.

2. Observation.

3. Inquiry.

4. **Analytical review.**

1.11 Which of the following is most likely an internal audit role in a less structured governance process?

1. Designing specific governance processes.

2. Playing a consulting role in optimizing governance practices and structure.

3. **Providing advice about basic risks to the organization.**

4. Evaluating the effectiveness of specific governance processes.

1.12 The requirement that purchases be made from suppliers on an approved vendor list is an example of a

1. **Preventative control.**

2. Detective control.

3. Corrective control.

4. Monitoring control.

1.13 Inherent risk is

1. A potential event that will adversely affect the organization.
2. Risk response risk.
3. The risk after management takes action to reduce the impact or likelihood of an adverse event.
4. **The risk when management has not taken action to reduce the impact or likelihood of an adverse event.**

1.14 Which of the following controls would prevent the ordering of quantities in excess of an organization's needs?

1. **Review of all purchase requisitions by a supervisor in the user department prior to submitting them to the purchase department.**
2. Automatic reorder by the purchasing department when low inventory is indicated by the system.
3. A policy requiring review of the purchase order before receiving a new shipment.
4. A policy requiring agreement of the receiving report and packing slip before storage of new receipts.

1.15 A utility with large investment in repair vehicles would most likely implement which internal control to reduce the risk of vehicle theft or loss?

1. Review insurance coverage for adequacy.
2. Systematically account for all repair work orders.
3. Physically inventory vehicles and reconcile the results with the accounting records.
4. **Maintain vehicles in a secured location with release and return subject to approval by a custodian.**

1.16 To minimise the risk that agents in the purchasing department will use their positions for personal gain, the organization should

1. **Rotate purchasing agent assignments periodically.**
2. Request internal auditors to confirm selected purchases and accounts payable.
3. Specify that all items purchase must pass value-per-unit-of-cost reviews.

4. Direct the purchasing department to maintain records on purchase prices paid, with review of such being required each 6 months.

1.17 Which of the following statements is an engagement objective?

1. Observe the deposit of the day's cash receipts.
2. Analyse the pattern of any cash shortages.
- 3. Evaluate whether cash receipts are adequately safeguarded.**
4. Recalculate each month's bank reconciliation.

1.18 Which of the following is a risk that is higher when electronic funds transfer (EFT) system is used?

1. Improper change control procedures.
- 2. Unauthorized access and activity.**
3. Insufficient online edit checks.
4. Inadequate backups and disaster recovery procedures.

1.19 The purposes of the Standards include all the following except

1. Establishing the basis for the measurement of internal audit performance.
- 2. Guiding the ethical conduct of internal auditors.**
3. Stating basic principles that represent the practice of internal auditing.
4. Fostering improved organizational processes and operations.

1.20 To verify the proper value of costs charged to real property records for improvements to the property, the best source of information is

1. Inspection by the internal auditor of real property improvements.
2. A letter signed by the property manager asserting the propriety of costs incurred.
- 3. Original invoices supporting entries into accounting records.**
4. Comparison of billed amounts with contract estimates.

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1.1 Which one of the following controls could be used to detect bank deposits that are recorded but never made?

- A. Having bank reconciliations performed by a third party**
- B. Consolidating cash receiving points
- C. Establishing accountability for receipts at the earliest possible stage in the process
- D. Linking receipts to other internal accountabilities such as accounts receivable or sales

1.2 Which one of the following analytical trends indicates the possibility of an increase in obsolete inventory on hand?

- A. A decrease in the inventory turnover rate**
- B. A decrease in the ratio of gross profit to sales
- C. A decrease in the ratio of inventory to accounts receivable
- D. A decrease in the ratio of inventory to accounts payable

1.3 Which one of the following represents an internal control weakness in the payroll department?

- A. Pay-cheques are distributed by the employees' immediate supervisor.**
- B. The timekeeping function is independent of the payroll department.
- C. Payroll records are reconciled with quarterly tax reports.
- D. Payroll department personnel are rotated in their duties.

1.4 Which one of the following is least likely to be placed on the agenda for discussion at a pre-engagement meeting?

- A. The required records and input from client personnel
- B. The sampling plan and audit programmes**
- C. The expected starting and completion dates
- D. The purpose and scope of the engagement

1.5 When sampling methods are used, the concept of sufficiency of information means that the sample selected provides ...

- A. Reasonable assurance that the sample is representative of the sampled population.**
- B. Reasonable assurance that the evidence has a logical relationship with the internal audit objective.

- C. Absolute assurance that the sample is representative of the population.
- D. The best evidence that is reasonably obtained.

1.6 Indicate the alternative that correctly completes the following phrase:

The internal auditor uses analytical procedures to evaluate information provided by the auditee. Analytical procedures ...

- A. May provide the best available information for the completeness assertion.
- B. Involve tests such as confirmation of receivables.
- C. Are never sufficient on their own to support management assertions.
- D. Are regarded as direct information about the assertion being evaluated.**

1.7 An internal auditor would primarily rely on which type of audit evidence when evaluating the collectability of accounts receivable?

- A. Positive confirmation.
- B. An age analysis of accounts receivable.**
- C. Negative confirmation.
- D. Management's representations.

1.8 When reviewing the average collection period of the company's debtors' accounts, the internal auditor observes an increase from 30 to 60 days in the collection period for the current financial year.

Which one of the following alternatives is the most likely cause of this phenomenon?

- A. An increase in the organisation's sales volume
- B. A slackening of the organisation's credit control**
- C. A smaller incidence of slow-moving stock
- D. An increase in the profit margin on sales

1.9 Despite the fact that management principles can be taught to everyone, not everyone who learns these principles can manage successfully. Successful management depends mostly on ...

- A. Excellent people skills.
- B. An ability to control and direct the work performed in the organization.**

C. Making correct decisions for every occasion.

**D. An ability and inclination to move other towards desired goals and a sense for making reasonable decisions.**

1.10 When reviewing a factory that manufactures body parts for vehicles, the internal auditors would be most concerned if they were to identify a risk that the factory has ...

A. received goods that were not ordered

B. accepted goods in excess of current needs

C. paid inflated prices for goods from related parties

**D. failed to detect the receipt of substandard raw materials**

## 2015 S2 A1

1.1 To determine whether refunds granted to customers were properly approved, the internal auditor should vouch accounts receivable entries to...

1. Sales invoices.

2. Remittance advices.

3. Shipping documents.

**4. Credit memos.**

1.2 A major reason for establishing an internal audit activity is to...

1. Relieve overburdened management of the responsibility of establishing effective controls.

2. Safeguard resources entrusted to the organization.

3. Ensure the reliability and integrity of financial and operational information.

**4. Evaluate and improve the effectiveness of control processes.**

1.3 An internal auditor engages in the preparation of income tax forms during the tax season. For which of the following activities will the internal auditor most likely be in violation of the IIA Code of Ethics?

1. Writing a tax guide intended for publication and sale to the general public.

**2. Preparing the personal tax return, for a fee, for one of the organization's division managers.**

3. Teaching an evening tax seminar, for a fee, at a local University.

4. Preparing tax returns for elderly citizens, regardless of their associations, as a public service.

1.4 Engagement observations and recommendations emerge by a process of comparing what should be and what is. In determining “what should be” during an engagement to review an organization’s treasury function, which of the following is the least desirable criterion against which to judge current operations?

1. **The operations of the treasury function as documented during the last engagement.**
2. Organizational policies and procedures delegating authority and assigning responsibilities.
3. Finance textbook illustrations of generally accepted good treasury function practices.
4. Codification of best practices of the treasury function in relevant industries.

1.5 An engagement to review payroll is least likely to include...

1. Tests of computations for gross and net wages.
2. Comparison of payroll costs to budget.
3. Tracing a sample of employee names to employment records in the personnel department.
4. **Observing the physical distribution of pay checks.**

1.6 Internal auditors should design the scope of work in a consulting engagement to ensure that all the following will be maintained except...

1. **Independence.**
2. Integrity.
3. Credibility.
4. Professionalism.

1.7 A specified range is based on an estimate of a population characteristic calculated from a random sample. The probability that the range contains the true population value is the...

1. Error rate.
2. Lower precision limit.
3. **Confidence level.**

4. Standard error of the mean.

1.8 If all other sampling size planning factors were exactly the same in attribute sampling, changing the confidence level from 95% to 90% and changing the desired precision from 2% to 4% would result in a revised sample size that would be...

1. Larger
- 2. Smaller.**
3. Unchanged.
4. Indeterminate.

1.9 Monetary-unit sampling is most useful when the internal auditor...

1. Is testing the accounts payable balance.
2. Cannot cumulatively arrange the population items.
3. Expects to find several material misstatements in the sample.
- 4. Is concerned with overstatements.**

1.10 Which technique is most appropriate for testing the quality of the preliminary survey of payment vouchers described in an internal control questionnaire?

1. Analysis.
2. Evaluation.
- 3. Verification.**
4. Observation.

1.11 Which of the following is not a role of the internal audit activity in best practice governance activities?

1. Support the board in enterprise-wide risk assessment.
- 2. Ensure the timely implementation of audit recommendations.**
3. Monitor compliance with the corporate code of conduct.
4. Discuss areas of significant risks.

1.12 Controls may be classified according to the function they perform, for example, as detective, preventative, or directive. Which of the following is a directive control?

1. Monthly bank statement reconciliations.

2. Dual signatures on all disbursements over a specific amount.
3. Recording every transaction on the day it occurs.
- 4. Requiring all members of the internal audit activity to be CIAs.**

1.13 Enterprise risk management.....

1. Guarantees achievement of organizational objectives.
2. Requires establishment of risk and control activities by internal auditors.
- 3. Involves the identification of events with negative impacts on organizational objectives.**
4. Includes selection of the best risk response for the organization.

1.14 The manager of a production line has the authority to order and receive replacement parts for all machinery that requires periodic maintenance. The internal auditor received an anonymous tip that the manager ordered substantially more parts than were necessary from a family member in the parts supply business. The unneeded parts were never delivered. Instead, the manager processed receiving documents and charged the parts to machinery maintenance accounts. The payments for the undelivered parts were sent to the supplier, and the money was divided between the manager and the family member. Which of the following internal controls would have most likely prevented this fraud from occurring?

1. Established predefined spending levels for all vendors during the bidding process.
- 2. Segregating the receiving function from the authorization of parts purchases.**
3. Comparing the bill of lading for replacement parts to the approved purchase order.
4. Using the company's inventory system to match quantities requested with quantities received.

1.15 Which of the following controls could be used to detect bank deposits that are recorded but are never made?

1. Establishing accountability for receipts at the earliest possible time.
2. Linking receipts to other internal accountabilities, for example, collections to either accounts receivable or sales.
3. Consolidating cash receiving points.
- 4. Having bank reconciliations performed by a third party.**

1.16 Management can best strengthen internal control over the custody of inventory stored in an off-site warehouse by implementing...

1. Reconciliations of transfer slips to/from the warehouse with inventory records.
2. Increases in insurance coverage.
- 3. Regular reconciliation of physical inventories to accounting records.**
4. Regular confirmation of the amount on hand with the custodian of the warehouse.

1.17 Which of the following is an appropriate statement of an engagement objective?

1. To observe the physical inventory count.
- 2. To determine whether inventory stocks are sufficient to meet projected sales.**
3. To search for the existence of obsolete inventory by computing inventory turnover by product line.
4. To include information about stock outs in the final engagement communication.

1.18 All of the following are potential security issues for e-commerce except...

1. Correct identification of transacting parties.
- 2. Proliferation of computer viruses.**
3. Determining who may rightfully make transaction decisions.
4. Verification of payment data.

1.19 One of the purposes of the International Standards for the Professional Practice of Internal Auditing ("the Standards") is to...

1. Encourage the professionalization of internal auditing.
2. Establish the independence of the internal audit activity and emphasize the objectivity of internal auditing.
3. Encourage external auditors to make more extensive use of the work of internal auditors.
- 4. Establish the basis for evaluating internal audit independence.**

1.20 Ordinarily, what source of information should most affect the internal auditor's conclusions?

- 1. External.**
2. Inquiry.
3. Oral.

4. Written.

**2015 S2 A2**

1.1 An engagement objective to verify that the correct goods or services are received on time, at the right price and in the right quantity. Based on this objective, the function to be reviewed is the...

- A. Receiving department.
- B. Manufacturing department.
- C. Purchasing department.**
- D. Payroll department.

1.2 For good internal control in the revenue and receipts cycle, company policy should clearly indicate that defective merchandise returned by customers is to be delivered to the ...

- A. Goods receiving clerk.**
- B. Sales clerk.
- C. Inventory control clerk.
- D. Accounts receivable clerk

1.3 The annual internal audit plan is normally compiled on the basis of...

- A. What was done in the previous year.
- B. The organisation's overall risk assessment.**
- C. Special requests from management and the audit committee.
- D. The availability of resources.

1.4 The major difference between statistical and non-statistical sampling is that, within statistical sampling,

- A. The internal auditor can always get a smaller sample size.
- B. The internal auditor can always express an opinion at 100% confidence level.
- C. The internal auditor can direct the sample towards those items that carry greater risk.
- D. The internal auditor can explicitly quantify the likelihood of the sample being non-representative.**

1.5 Select the alternative that correctly completes the following sentence:

A prerequisite for a risk analysis is...

- A. The establishment of an internal audit activity.
- B. The establishment of organisational objectives.**
- C. The establishment of control procedures and/or control activities.
- D. Establishing that a monitoring system exists.

1.6 To properly control working papers, the internal auditor should not....

- A. Share the results of an audit with the auditee.
- B. Permit access to auditors from the South African Revenue Service if and when required.
- C. Make them available to people who do not have the authority to use them.**
- D. Permit access to external auditors.

1.7 Which one of the following irregularities will probably not be detected by a system of internal control?

- A. Duplicate payments to suppliers.
- B. Theft by an employee.
- C. Theft by a group of employees who collaborate.**
- D. Unauthorised payments.

1.8 Which one of the following alternatives is a key issue to consider in developing audit objectives?

- A. The qualifications of the audit staff selected for the engagement.
- B. The auditee's objectives and control structure.**
- C. Recommendations of the auditee's employees.
- D. The recipient of the internal audit report.

1.9 In order to identify the amount of obsolete inventory that may exist in an organisation, the internal auditor probably would collect evidence using all of the following procedures except:

- A. Inspection.

**B. Confirmation.**

C. Re-computation.

D. Analytical review.

1.10 Which one of the following alternatives is a primary advantage of an internal control questionnaire?

**A. It reduces the risk of overlooking important aspects in the system.**

B. It provides a clear picture of the relationships that exist between the various controls.

C. It forces the internal auditor to acquire a full understanding of the system.

D. The negative responses indicate the only areas needing further internal audit attention.

#### **2016 S1 A1**

1.1 Which one of the following is not a component of the International Professional Practices Framework (IPPF)?

1. The definition of internal auditing

**2. Internal audit methodology**

3. The International Standards for the Professional Practice of Internal Auditing

4. The Code of Ethics

1.2 Risk management is the responsibility of management. The role of the internal audit activity in the risk management process may include which of the following?

**1. Evaluating the risk management process as part of the engagement plan.**

2. Appointing consultants to assist the management with the risk management process.

3. Managing the risk management process.

4. All of the above.

1.3 Adequate internal controls are most likely to be present in an organisation where...

**1. Management has planned and organised in a manner which provides reasonable assurance that the organisation's objectives and goals will be achieved efficiently and economically.**

2. Management has exercised due professional care in the design of operating and functional systems.
3. Operating and functional systems are designed, installed and implemented in compliance with applicable laws.
4. Management has designed, installed and implemented efficient operating and functional systems.

1.4 Which one of the following options is not an example of a detective control?

1. Review of exception reports
2. Smoke detectors
- 3. Insurance**
4. Physical stock counts

1.5 Which of the following principles does not form part of the Institute of Internal Auditors (IIA) Code of Ethics?

1. Integrity
2. Confidentiality
- 3. Compliance**
4. Competency

1.6 What kind of audit evidence is obtained from reviewing a signed purchase order?

- 1. Documentary evidence**
2. Primary evidence
3. Secondary evidence
4. Hearsay evidence

1.7 Which one of the following alternatives would constitute a violation of the Institute of Internal Auditors (IIA) Code of Ethics?

1. Janice accepted an assignment to audit the electronic manufacturing division. Janice has recently joined the internal auditing department. She worked as a senior auditor for an external auditing firm and audited many electronic companies during the past two years.
2. George has been assigned to do an internal audit of the warehousing function six months from now. George has no experience in that area but decides to accept the

assignment anyway. He has signed up for continuing education course in warehousing, which he will complete before his assignment commences.

3. **Jane is content with her career as an internal auditor and has come to look at it as a regular 8-to-5 job. She has not engaged in continuing professional education or other activities to improve her effectiveness during the last three years. However, she feels that she is delivering the same quality work she has always delivered.**
4. John discovered internal financial fraud during the year. The accounting books were adjusted to properly reflect the loss associated with the fraud. John discovered the fraud with the external auditor when the external auditor reviewed the working papers detailing the incident.

1.8 A major reason for establishing an internal audit activity is to ...

1. Relieve overburdened management of the responsibility for establishing effective controls.
2. Safeguard resources entrusted to the organisation.
3. Ensure the reliability and integrity of financial and operational information.
4. **Evaluate and improve the effectiveness of control processes.**

1.9 Which of the following activities is not presumed to impair the objectivity of an internal auditor?

- I. Recommending standards of control for a new information system application.
  - II. Drafting procedures for running a new computer application to ensure that proper controls are installed.
  - III. Performing reviews of procedures for a new computer application before it is installed.
1. I only.
  2. III only.
  3. III only.
  4. **I and III.**

1.10 Which of the following is most likely an internal audit role in a less structured governance process?

1. Designing specific governance processes.
2. Playing a consulting role in optimising governance practices and structure.
3. **Providing advice about basic risks to the organisation.**

4. Evaluating the effectiveness of specific governance processes.

1.11 When assessing a risk associated with an entity, an internal auditor should do which one of the following?

1. Determine how the risk should best be managed.
- 2. Provide assurance on the management of the risk.**
3. Update the risk management based on risk exposures.
4. Design controls to mitigate the identified risks.

1.12 Controls should be designed to ensure which one of the following?

- 1. Operations are performed efficiently.**
2. Management's plans have not been circumvented by worker collusion.
3. The internal audit activity's guidance and oversight of management's performance is accomplished economically and efficiently.
4. Management's planning, organising and directing processes are properly evaluated.

1.13 Which risk response reflects a change from acceptance to sharing?

1. An insurance policy on a manufacturing plant was not renewed.
- 2. Management purchased insurance on previously uninsured property.**
3. Management sold a manufacturing plant.
4. After employees stole numerous inventory items, management implemented mandatory background checks on all employees.

1.14 Cheques from customers are received in the organisation's mail room each day. What controls should be in place to safeguard them?

1. Establishing a separate post office box for customer payments.
2. Forwarding all cheques to the cashier upon receipt.
- 3. Requiring a specific mail clerk to list and restrictively endorse each cheque.**
4. Providing bonding protection for mail clerks.

1.15 One payroll engagement objective is to determine whether segregation of duties is proper. Which of the following activities is incompatible?

1. Hiring employees and authorising changes in pay rates.
2. Preparing the payroll and filing payroll tax forms.
3. Signing and distributing payroll cheques.
- 4. Preparing attendance data and preparing the payroll.**

1.16 In preparing a sampling plan for an inventory pricing test, which of the following describes an advantage of statistical sampling over non-statistical sampling?

1. Requires non-quantitative expression of sample results.
- 2. Provides a quantitative measure of sampling risk.**
3. Minimise non-sampling risk.
4. Reduces the level of tolerable error.

1.17 If all other sample size planning factors were exactly the same in attribute sampling, changing the confidence level from 95% to 90% and changing the desired precision from 2% to 5% would result in a revised sample size that would be ...

1. Larger.
- 2. Smaller.**
3. Unchanged.
4. Indeterminate.

1.18 An internal auditor found that the supervisor does not properly approve employee time records in one department. Which one of the following errors can result from this?

1. Duplicate pay cheques might be issued.
2. The wrong hourly rate could be used to calculate gross wages.
- 3. Employees might be paid for hours they did not work.**
4. Payroll cheques might not be distributed to the appropriate payees.

1.19 Statistical sampling differs from other sampling methods in the sense that ...

1. An auditor does not have to exercise professional judgement when applying statistical sampling as he or she must when applying other sampling methods.
2. A statistical sampling produces representative samples, whereas the other methods do not.

3. A statistical sampling can deliver absolute assurance, which is not possible with other sampling methods.
4. **A statistical sampling is based on the theory of probability, which is not the case with other sampling methods.**

1.20 Which one of the following is the best source for an internal audit team to use in identifying common external risks faced by a company?

1. Questionnaires
2. **Current research reported in professional journals and textbooks**
3. Flowcharts
4. Review lists or reminder lists

### 2016 S1 A2

1.1 Ordinarily, what source of information should most affect the internal auditor's conclusions?

- A. Inquiry
- B. Oral
- C. Informal
- D. **External**

1.2 Which one of the following alternatives describes a control weakness?

- A. The purchasing agent invests in a publicly traded mutual fund that lists the stock of one of the company's suppliers in its portfolio.
- B. Pre-numbered blank purchase orders are secured within the purchasing department.
- C. Normal operational purchases fall within the range of R500 to R1 000, with two cheque signatories required for purchases over R1 000.
- D. **Purchasing procedures are well designed and followed unless otherwise directed by the purchasing supervisor.**

1.3 Which one of the following alternatives is an audit objective?

- A. Observe the deposit of the day's cash receipts.
- B. Re-compute each month's bank reconciliations.
- C. **Ensure that cash receipts are adequately safeguarded.**

D. Analyse the pattern of any cash shortages.

1.4 The cash receipts' function should be separated from the related record keeping function in an organisation in order to...

**A. Physically safeguard the cash receipts.**

B. Prevent paying cash disbursements from the cash receipts.

C. Minimise undetected misappropriations of cash receipts.

D. Establish accountability when cash is first received.

1.5 A 90% confidence interval for the mean of a population based on the information in a sample always implies that there is a 90% chance that the...

**A. True population mean lies within the specified confidence interval.**

B. Estimate is equal to the true population mean.

C. True population mean is no larger than the largest end point of the interval.

D. Standard deviation will not be any greater than 10% of the population mean.

1.6 The standard deviation of a sample usually decreases with...

**A. A decrease in sample size.**

B. An increase in desired precision.

C. The use of stratification.

D. An increase in confidence level.

1.7 For good internal control in the revenue and receipts cycle, company policy should clearly indicate that defective merchandise returned by customers is to be delivered to the ...

A. Sales clerk.

**B. Goods receiving clerk.**

C. Inventory control clerk.

D. Accounts receivable clerk.

1.8 Which one of the following analytical trends indicates the possibility of an increase in obsolete inventory on hand?

A. A decrease in the ratio of inventory to accounts payable

B. A decrease in the ratio of inventory to accounts receivable

**C. A decrease in the inventory turnover rate**

D. A decrease in the ratio of gross profit to sales

1.9 Which one of the following statements is an appropriate internal audit objective?

A. To observe the physical inventory count.

**B. To determine whether inventory on hand is sufficient to meet the projected sales targets.**

C. To include information about stock-out situations in the internal audit report.

D. To search for the existence of obsolete inventory by computing inventory turnover by product line.

1.10 An internal auditor prepares income tax forms during the tax season. For which of the following activities will the internal auditor most likely be in violation of the IIA Code of Ethics?

A. Writing a tax guide intended for publication and sale to the general public.

**B. Preparing the personal tax return, for a fee, for one of the organisation's division managers.**

C. Teaching an evening tax seminar, for a fee, at a local university.

D. Preparing tax returns, for elderly citizens, regardless of their associations, as a public service.

## **2016 S2 A1**

1.1 The policies and procedures helping to ensure that management directives are executed and actions are taken to address risks to the achievement of the objectives describes ...

**1. Control activities.**

2. Risk assessments.

3. Control environments.

4. Monitoring.

1.2 Identifying damaged and obsolete inventory is important when valuing inventory. The best auditing procedure to discover damaged inventory included in closing inventory is to ...

1. Compare the physical quantities of slow-moving items with corresponding quantities of the previous year.
2. Review management's inventory certificate for accuracy.
3. Test the overall fairness of the inventory values by comparing the company's inventory turnover ratio with the industry average.
- 4. Inspect inventory during the physical inventory count.**

1.3 Which one of the following options violates the objectivity principle of the Code of Ethics?

1. The internal audit activity publishes an informative article on the organisation's intranet, setting out the advantages of introducing a time-management clock-in system for the administrative staff.
- 2. Since everyone in the organisation is aware of the IT department's inability to arrange suitable back-up facilities for the financial systems of the organisation, the internal auditor makes no mention of the fact in his report following an audit of the general IT controls.**
3. An internal audit activity appoints a chartered accountant who has recently completed her articles with an auditing firm and assigns her to lead an audit of control of the purchasing and implementing new IT systems.
4. While auditing controls over wage pay-outs, an auditor finds that some controls have been circumvented. She discusses her finding of a possible fraud with the internal audit manager in his office.

1.4 When planning an attribute sampling application, the difference between the expected error rate and the maximum tolerable error rate is the planned ...

1. Skewness.
2. Dispersion.
3. Reliability.
- 4. Precision.**

1.5 A specified range is based on an estimate of a population characteristic calculated from a random sample. The probability that the range contains the true population value is the ...

1. Error rate.
- 2. Confidence level.**
3. Standard error of the mean.
4. Lower precision limit.

1.6 Due professional care implies reasonable care and competence, not infallibility or extraordinary performance. Thus, which of the following is unnecessary?

1. The conduct of examinations and verifications to a reasonable extent

**2. The conduct of extensive examinations**

3. The reasonableness assurance that compliance does exist

4. The consideration of possibility of material irregularities

1.7 In combined assurance, which of the following is not an external assurance provider?

1. Sustainability assurance providers

2. External auditors

**3. The risk management function**

4. Regulators

1.8 Which one of the following activities may be performed by an internal auditor?

1. Drafting procedures for systems of control.

2. Designing systems of control.

**3. Reviewing systems of control before implementation.**

4. Installing systems of control.

1.9 During an audit of the receiving operations of a manufacturing organisation, an internal auditor will be most concerned with the risk that the function has ...

1. Received goods that were ordered.

2. Insufficient staff complement to perform all the tasks.

**3. Failed to detect the receipt of goods of poor quality.**

4. Paid inflated prices for goods from related parties.

1.10 An internal auditor is observing cash sales to determine if customers are given written receipts. The objective of this test is to ensure that ...

1. Cash received equals the total of the receipts.

2. Customers are charged authorised prices.

3. Cash balances are correct.

**4. All cash sales are recorded.**

1.11 Independence permits internal auditors to render impartial and unbiased judgements. The best way to achieve independence is through ...

1. Individual knowledge and skills.

**2. Dual reporting relationship.**

3. Supervision within the organisation.

4. Organisational knowledge and skills.

1.12 Which of the following is not a role of the internal audit activity in best practice governance activities?

1. Support the board in enterprise wide risk assessment.

**2. Ensure the timely implementation of audit recommendations.**

3. Monitor compliance with the corporate code of conduct.

4. Discuss areas of significant risk.

1.13 Many organisations use electronic funds transfer to pay their suppliers instead of issuing cheques. Regarding the risks associated with issuing cheques, which of the following risk management techniques does this represent?

1. Controlling

2. Accepting

3. Transferring

**4. Avoiding**

1.14 An internal auditor noted that the accounts receivable department is separate from other accounting activities. Credit is approved by a separate credit department. Control accounts and subsidiary ledgers are balanced monthly. The accounts receivable manager writes off delinquent accounts after one year, or sooner if a bankruptcy or other unusual circumstances are involved. Credit memoranda are pre-numbered and must correlate with receiving reports. Which of the following areas could be viewed as an internal control weakness of the above organisation?

**1. Writing off of delinquent accounts.**

2. Approving of credit.

3. Monthly aging of receivables.
4. Handling of credit memos.

1.15 Which of the following activities performed by a payroll clerk is a control weakness rather than a control strength?

- 1. The payroll clerk has custody of the cheque signature stamp machine.**
2. The payroll clerk prepares the payroll register.
3. The payroll clerk forwards the payroll register to the chief accountant for approval.
4. The payroll clerk draws the pay cheques on a separate payroll cheque account.

1.16 Which of the following controls could be used to detect bank deposits that are recorded but never made?

1. Establishing accountability for receipts at the earliest possible time.
2. Linking receipts to other internal accountabilities, for example collections to either accounts receivable or sales.
3. Consolidating cash receiving points.
- 4. Having bank reconciliations performed by a third party.**

1.17 The chief audit executive was reviewing recent reports that had recommended additional engagements because of risk exposures to the organisation. Which of the following represents the greatest risk and should be the next assignment?

1. Three pre-numbered receiving reports were missing.
2. There were several purchase orders issued without purchase requisitions.
- 3. Payment had been made for routine inventory items without a purchase order or receiving report.**
4. Several times cash receipts had been held over an extra day before depositing.

1.18 While planning an engagement, an internal auditor establishes engagement objectives to describe what is to be accomplished. Which of the following is a key issue to consider in developing engagement objectives?

1. The qualifications of the internal auditing staff selected for the engagement
- 2. Risks associated with the activities to be reviewed**
3. Recommendations of the engagement client's employees

4. The recipients of the final engagement communication

1.19 When faced with an imposed scope limitation, the chief audit executive needs to ...

1. Refuse to perform the engagement until the scope limitation is removed.
- 2. Communicate the potential effects of the scope limitation to the board.**
3. Increase the frequency of engagements concerning the activity in question.
4. Assign more experienced personnel to the engagement.

1.20 An internal auditor discovered some material inefficiencies in a purchasing function. The purchasing manager is the internal auditor's next-door neighbour and best friend. In accordance with the IIA, Code of Ethics, the internal auditor should ...

- 1. Objectively include the facts of the case in the engagement communications.**
2. Not report the incident because of loyalty to the friend.
3. Include the facts of the case in a special communication submitted only to the friend.
4. Not report the friend unless the activity is illegal.

## **2016 S2 A2**

1.1 During an engagement to evaluate the organisation's accounts payable function, an internal auditor plans to confirm balances with suppliers. What is the source of authority for such contacts with units outside the organisation?

- A. The internal audit activity policies and procedures
- B. The Standards
- C. The Code of Ethics
- D. The internal audit activity's charter**

1.2 Objectivity is most likely impaired by an internal auditor's ...

- A. Continuation on an engagement at a division for which he or she will soon be responsible as the result of a promotion.**
- B. Reduction of the scope of an engagement due to budget restrictions.
- C. Participation on a task force that recommends standards for control of a new distribution system.
- D. Review of a purchasing agent's contract drafts prior to their execution.

1.3 A chief audit executive may use risk analysis to prepare work schedules. Which of the following is not considered in performing a risk analysis?

- A. Issues relating to organisational governance
- B. Skills available on the internal audit staff**
- C. Results of prior engagement
- D. Major operating changes

1.4 Which of the following is not implied by the definition of control?

- A. Measurement of progress towards goals
- B. Uncovering of deviations from plans
- C. Assignment of responsibility for deviations**
- D. Indication of the need for corrective action

1.5 The function of the chief risk officer (CRO) is most effective when the CRO ...

- A. Manages risk as a member of senior management.
- B. Shares the management of risk with line management.
- C. Shares the management of risk with the chief audit executive.
- D. Monitors risk as part of the enterprise risk management team.**

1.6 An adequate system of internal controls is most likely to detect a fraud perpetrated by a...

- A. Group of employees in collusion.
- B. Single employee.**
- C. Group of managers in collusion.
- D. Single manager.

1.7 The use of incorrect audit procedures in a sample for a given internal audit objective is an example of...

- A. Alpha risk.
- B. Sampling risk.

**C. Non-sampling risk.**

D. Beta risk.

1.8 An internal auditor is observing cash sales to determine if customers are given written receipts. The objective of this test is to ensure that...

A. Cash received equals the total of the receipts.

B. Customers are charged authorised prices.

C. Cash balances are correct.

**D. All cash sales are recorded.**

1.9 In a sampling application, the group of items about which the auditor wants to estimate some characteristic is called the...

A. Attribute of interest.

**B. Population.**

C. Sample.

D. Sampling unit.

1.10 An internal auditor has set an engagement objective of identifying the existence of personality conflicts that are detrimental to productivity. Which of the following engagement techniques will best meet this objective?

A. Inspection of documents

B. Observation

**C. Inquiry**

D. Analytical review

### **2015 S1 Exam**

1.1 An internal auditor has recently conducted an audit of the human resources function. The auditor was previously a manager in this function. Which of the following principles, from the code of ethics, has the internal auditor violated

A. Integrity

**B. Objectivity**

- C. Confidentiality
- D. Has not violated any principle

1.2 Which of the following is required of the internal audit function according to the Standards?

- A. Evaluate the effectiveness of the audit committee annually
- B. Issue an overall opinion on the adequacy of the organisation's system of internal controls annually**
- C. Obtain an annual representation from management acknowledging management's responsibility for the design and implementation of internal controls to prevent illegal acts
- D. Assess whether the information technology governance of the organisation sustains and supports the organisation's strategies and objectives

1.3 Inherent risk can be defined as

- A. the probability of loss arising out of certain circumstances or existing in an environment in the absence of any action to control or modify the circumstances**
- B. the probability of loss arising out of certain circumstances or existing in an environment, taking the relevant controls into account as well
- C. the level of risk that an organisation is willing to accept
- D. the acceptable levels of risk size and variation relative to the achievement of objectives, which must align with the organisation's risk appetite

1.4 In organisations, a combined assurance plan needs to be established in order for risks to be controlled. This plan should indicate the level of assurance required, the frequency of such assurance, and how and by whom assurance should be provided. Which of the following is an objective of a combined assurance plan?

- A. Identify and specify the sources of assurance over the organisation's risks
- B. Provide risk management with a framework of the various assurance parties
- C. Link risk management activities with assurance activities**
- D. All of the above

1.5 All employees in XYZ Corporation have to obtain authorisation from their senior managers before placing an order. This type of control is classified as

- A. preventive control**

- B. detective control
- C. corrective control
- D. directive control

1.6 ABC company has the following control inscribed in its revenue and receipts policy “before processing the order, checks should be carried out by the credit controller to establish that the customer is creditworthy and did not surpass his credit limit ” Which of the following risks is this control most mitigating

- A. Orders may be accepted from non-account holders.
- B. Inaccurate or incomplete orders may be recorded which will result in a loss of sales and customer goodwill.
- C. Orders may not be acted upon timeously.
- D. A sale will be made to a customer who is not creditworthy, resulting in bad debts for the company.**

1.7 The objective of an audit procedure in the procurement cycle states “To ensure that all the goods received from suppliers are recorded as purchases in the purchase journal”. Which assertion does the objective refer to?

- A. Accuracy
- B. Cut-off
- C. Completeness**
- D. Classification

1.8 The acceptable error rate is the total number of errors which the auditor is prepared to accept within a given population. All of the following factors must be taken into account for the acceptable error rate except

- A. scope of the test**
- B. materiality
- C. the purpose of the test
- D. the effectiveness of the system of internal control

1.9 Statistical sampling for values includes the following sample method

- A. Estimation sampling

**B. Monetary unit sampling**

C. Acceptance sampling

D. Discovery sampling

1.10 The following statement was included as part of an audit report: "Currently the average stockholding of Branches A and B is 20% of their annual turnover. This is significantly above the industry average". This statement forms part of which key factor in a finding?

A. Criteria

B. Cause

**C. Condition**

D. Effect

1.11 Shipments are made from the warehouse based on customer purchase orders. The matched shipping documents and purchase orders are then forwarded to the accounts department for sales invoice preparation. The shipping documents are neither accounted for nor pre-numbered. Which of the following procedures should be executed as a result of this control weakness?

A. Select sales invoices from the sales register and examine the related shipping documents

**B. Select bills of lading from the warehouse and trace the shipments to the related sales invoices**

C. Balance the sales register and trace the total to the general ledger

D. Trace quantities and prices on the sales invoice to the customer purchase order and test extensions

1.12 When reviewing the average collection period of a company's debtors' accounts, the internal auditor observes an increase from 30 to 60 days for the current financial year. Which one of the following alternatives is the most likely cause of this increase?

A. A smaller incidence of slow moving inventory

**B. A slackening of the organisation's credit control**

C. The raising of the profit margin on sales

D. An increase in the organisation's sales volume

1.1 When testing controls, the internal auditor must be free from interference when determining the scope of such testing, the procedures, etc. In order to accomplish this, the internal auditor should report to levels in the organisation that allows it to accomplish its responsibilities. The best reporting structure for internal audit will be...

- A. Functionally to the audit committee and administratively to the chief executive officer.**
- B. Administratively to the audit committee and functionally to the chief executive officer.
- C. Functionally to the chief audit executive and administratively to the audit committee.
- D. Functionally to the audit committee and administratively to the chief audit executive.

1.2 The requirement that purchases be made from suppliers on an approved vendor list is an example of a \_\_\_\_\_ control.

- A. Detective
- B. Corrective
- C. Preventative**
- D. Monitoring

1.3 The purpose of the combined assurance model is to provide a coordinated approach to all assurance activities that will optimise the assurance coverage obtained. A report from a regulator on management's internal processes can be regarded as assurance from

- A. An internal assurance provider.
- B. An external assurance provider.**
- C. Management as an assurance provider
- D. A first line of defence.

1.4 Residual risk can be defined as...

- A. The amount of risk an organisation is willing to accept in pursuit of its business objectives.
- B. The portion of risk that remains after management executes its risk responses.**
- C. The acceptable levels of risk size and variation relative to the achievement of objectives.
- D. The combination of internal and external risk factors in their pure, uncontrolled state, assuming there are no internal controls in place.

1.5 During a review of the audit files, the senior internal auditor finds an audit file that contains an audit programme, specifically designed for an audit, where a third of the procedures have been left undone without any further explanation. This is a violation of which of the principles of the code of ethics?

- A. Objectivity
- B. Integrity
- C. Confidentiality
- D. Competency**

1.6 An internal auditor's procedure states the following "Inspect that invoices are numbered in sequence to confirm that all sales transactions are recorded." Which if the following assertions are being tested in the above audit procedure?

- A. Validity
- B. Completeness**
- C. Classification
- D. Authorisation

1.7 When determining the acceptable error rate, when selecting a sample, which of the following factors needs to be taken into account?

- A. Materiality.
- B. The purpose of the test.
- C. The effectiveness of the system of internal control.
- D. All of the above.**

1.8 Which of the following procedures would provide the best evidence of the effectiveness of the credit granting function?

- A. Observe the credit granting process.
- B. Ask the credit manager about the effectiveness of the function.
- C. Review the trend in receivables write-offs.**
- D. Check for evidence of credit approval on a sample of customer orders.

1.9 A 90% confidence interval for the mean of a population based on the information in a sample always implies that there is a 90% chance that the...

- A. **True population mean lies within the specified confidence interval.**
- B. Estimate is equal to the true population mean.
- C. True population mean is no larger than the largest end point of the interval.
- D. Standard deviation will not be any greater than 10% of the population mean.

1.10 During an audit of the receiving operations of a manufacturing organisation, an internal auditor will be most concerned with the risk that the function has ...

- A. Received goods that were ordered.
- B. **Failed to detect the receipt of substandard goods.**
- C. Accepted goods in excess of current needs.
- D. Paid inflated prices for goods from related parties.

#### **2014 S1 Exam**

1.1 Select the alternative that correctly completes the following sentence. Controls are only effective and useful if:

- A. They are recommended by internal or external auditors.
- B. **they are developed and implemented in order to achieve a specific objective**
- C. they are applied to the financial transactions of an organisation
- D. they eliminate the possibility that irregularities can occur

1.2 An internal auditor's preliminary analysis of accounts receivable revealed that the accounts receivable turnover rate had increased. Why would this information be important to the manager?

- A. Relaxation of credit policy should be considered
- B. It will influence cash flow which should be taken into consideration for transactions
- C. The cash discount offered had increased
- D. **The increase was due to an increase in cash sales**

1.3 During the performance of an audit, audit risk can best be described as the risk that the internal auditor:

- A. may fail to detect a significant error or weakness during the performance of the audit**
- B. may not be able to adequately evaluate a section due to a poor internal control system
- C. may not have the expertise required to perform the specific audit
- D. may miss testing faulty documents due to the use of sampling techniques

1.4 According to the COSO Internal Control - Integrated Framework, a precondition for risk assessment is the:

- A. appointment of a risk manager
- B. organisational independence of the internal audit activity
- C. establishment of organisational objectives**
- D. implementation of control procedures over activities

1.5 Which one of the following is an audit objective?

- A. To determine whether inventory on hand is sufficient to meet the projected sales targets**
- B. To observe the physical inventory count
- C. To include information about stock-out situations in the internal audit report
- D. To search for the existence of obsolete inventory by computing inventory turnover by product line

1.6 The most persuasive evidence to test the existence of newly acquired delivery trucks would be

- A. certificate received from specialist third party
- B. confirmation letters from management
- C. observation of the auditee's procedures
- D. a physical examination**

1.7 Which one of the following documents would provide the best evidence that a purchase transaction has actually occurred?

- A. The supplier's invoice for the procured goods
- B. The ordering department's original requisition for the goods

- C. The cancelled cheque issued in payment of the procured goods.
- D. The receiving memorandum (goods received note) documenting the receipt of the goods**

1.8 Which one of the following alternatives is a key issue to consider when developing audit objectives?

- A. The qualifications of the audit staff selected for the engagement
- B. The auditee's objectives and control structure**
- C. The recommendations of the auditee's employees
- D. The recipient of the internal audit report

1.9 Which one of the following activities may be performed by an internal auditor?

- A. A Drafting procedures for systems of control
- B. Designing systems of control
- C. Reviewing systems of control before implementation**
- D. Installing systems of control

1.10 In an internal audit report, which attribute should the recommendation address?

- A. Effect
- B. Condition
- C. Cause**
- D. Criteria

### **2014 S2 Exam**

1.1 Which of the following conduct violates the integrity principle of the Code of Ethics.

- A. The internal auditors perform a detailed risk assessment and identify the key controls relating to credit sales before they decided on the tests to be performed
- B. An internal auditor is assigned to an audit of controls in the procurement section, which is headed by his father

- C. While auditing the controls over wage pay-outs, an auditor finds that some controls have been circumvented She discusses her finding as a possibility of fraud with her colleague in the canteen over lunch
- D. The internal auditor uses an unrevised audit programme, which was used three years ago, to conduct an organisation-wide audit on credit sales**

1.2 Which of the following are elements included in the control environment described in the COSO internal control framework?

- A. Integrity and ethical values, management's philosophy and operating style, and human resource policies**
- B. Organisational structure, commitment to competence and planning.
- C. Competence of personnel, backup facilities, laws and regulations
- D. Risk assessment, assignment of responsibility and human resource practices

1.3 There are certain types of IT risks that tend to be common across organisations and industries. The unauthorised disclosure of business partners' proprietary information or individual's personal information may result in loss of business, lawsuits and reputation impairment, describes

- A. access risk
- B. availability risk
- C. confidentiality and privacy risk**
- D. system reliability and information integrity risk

1.4 According to the King III Report on Corporate Governance, which of the following is not the audit committee's responsibility regarding combined assurance?

- A. Monitoring the appropriateness of the company's combined assurance model
- B. Ensuring all the significant risks facing the company are adequately dealt with
- C. Monitoring the relationship between the external assurance providers and the organisation
- D. Providing an independent assurance on risk management and systems of internal control**

1.5 In combined assurance, which of the following is not an external assurance provider?

- A. Sustainability assurance providers
- B. External auditors

**C. The risk management function**

D. Regulators

1.6 A major distinction between statistical and non-statistical sampling is that

A. non statistical sampling allows the quantification of the sampling error

B. statistical sampling virtually eliminates sampling risk

**C. statistical sampling provides an objective means of determining sample size**

D. non statistical sampling results in smaller sample sizes

1.7 One payroll control objective is to ensure that there is adequate segregation of duties. Which of the following activities is incompatible?

A. Hiring employees and authorising changes in pay rates

B. Preparing the payroll and filing payroll tax forms

C. Signing and distributing payroll cheques

**D. Preparing attendance data and preparing the payroll**

1.8 Which of the following controls would help prevent overpaying a supplier?

**A. Reviewing and cancelling supporting documents when a cheque is issued**

B. Requiring the cheque signatory to mail the cheque directly to the supplier

C. Approving the purchase before ordering from the supplier

D. Reviewing the accounting disclosure for the expenditure

1.9 During an audit of the receiving operations of a manufacturing organisation, an internal auditor will be most concerned with the risk that the function has

A. received goods that were ordered

**B. failed to detect the receipt of goods of poor quality**

C. an insufficient staff complement to perform all the tasks

D. paid inflated prices for goods from related parties

1.10 Which of the following statements is an audit objective?

A. Observe the deposit of the day's cash receipts

**B. Determine whether cash receipts are adequately safeguarded**

C. Analyse the pattern of any cash shortages

D. Re-perform each month's bank reconciliation

1.11 Which one of the following activities may be performed by an internal auditor as an assurance service?

A. Drafting procedures for systems of control

B. Designing systems of control

**C. Reviewing systems of control before implementation**

D. Installing systems of control

1.12 A working paper is complete when it...

A. Complies with the internal audit activity's format requirements

B. Contains all the attributes of an observation

C. Is clear, concise and accurate

**D. Satisfies the audit objective for which it was developed**

1.13 When an internal auditor uses monetary-unit statistical sampling to examine the total value of invoices, each invoice

A. Has an equal probability of being selected

B. Has an unknown probability of being selected

**C. Has a probability of being selected proportional to its monetary value**

D. Can be represented by no more than one monetary unit

1.14 An internal auditor decides to perform an inventory turnover analysis for both raw materials and finished goods inventory. The analysis would be potentially useful in

A. Identifying products for which management has not adjusted to changes in market demand

B. Identifying obsolete inventory

C. Identifying potential problems in purchasing activities

**D. All the answers are correct**

## Reding Multiple Choice Answers

### Study Guide MCQ

#### Chapter 2

1. A primary purpose of the Standards is to:

- A. Promote coordination of internal and external audit efforts
- B. Establish a basis for evaluating internal audit performance.**
- C. Develop consistency in internal audit practices.
- D. Provide a codification of existing practices.

**2. Which of the following are "mandatory guidance" in the IIA's IPPF?**

- i. practice advisories
- ii. The code of ethics
- iii. The definition of internal auditing
- iv. The standards.

- A. i, ii, and iv
- B. ii and iv
- C. ii, iii and iv**
- D. i, ii, iii and iv

- c. ii, iii and iv
- ii. the code of ethics
- iii. the definition of internal auditing
- iv. the standards.

**3. An internal auditor provides income tax services during the tax season. For which of the following activities would the auditor most likely be considered in violation of the IIA's Code of Ethics?**

- A. Preparing, for a fee, a division manager's personal tax returns.**
- B. Appearing on a local radio show to discuss retirement planning and tax issues.
- C. Receiving a stipend for teaching an evening tax class at the local junior college.
- D. Working on weekends for a friend who has a small CPA firm.

**4. An internal auditor is auditing a division in which the division's CFO is a close personal friend. The auditor learns that the friend is to be replaced after a series of**

**critical contract negotiations with the Department of Defence. The auditor relays this information to the friend. Which principle of the IIA's Code of Ethics has been violated?**

- A. Integrity
- B. Objectivity
- C. Confidentiality**
- D. Privacy

5. The IIA's Standards require internal auditors to exercise due professional care while conducting assurance engagements. Which of the following is not something an internal auditor is required to consider in determining what constitutes the exercise of due care in an assurance engagement of treasury operations?

- A. The audit committee has requested assurance on the treasury function's compliance with a new policy on use of financial instruments.
- B. Treasury management has not instituted any risk management policies.
- C. The independent outside auditors have requested to see the engagement report and working papers.**
- D. The treasury function just completed implementation of a new real-time investment tracking system.

**6. In which of the following situations does the internal auditor potentially lack objectivity?**

- A. A payroll accounting employee assists an internal auditor in verifying the physical inventory of small motors.
- B. An internal auditor discusses a significant issue with the vice president to whom the auditee reports prior to drafting the audit report.
- C. An internal auditor recommends standards of control and performance measures for a contract with a service organization for the processing of payroll and employee benefits.
- D. A former purchasing assistant performs a review of internal controls over purchasing four months after being transferred to the internal audit department.**

7. Which of the following is/are components of the Standards?

- I. Statements
- II. Interpretations
- III. The glossary

- A. I only
- B. I and II
- C. I and III
- D. I, II, and III**

**8. According to the standards, which of the following must the internal audit manager think about when considering appropriate due care while planning an assurance engagement?**

- A. The opportunity to cross train internal audit staff
- B. The cost of assurance in relationship to potential benefits.**
- C. Job openings in the area that may be of interest to internal auditors assigned to the engagement
- D. The potential to delivery consulting services to the auditee

9. Which of the following types of IPPF guidance require(s) an exposure to the various IIA national institutes prior to issuance?

- i. A new Practice Advisory
- ii. A new Standard
- iii. A new Position Paper
- iv. A new definition in the Standards glossary

- A. iii only**
- B. ii and iv
- C. ii, iii, and iv
- D. i, ii, iii and iv

**10. Which of the following are required of the internal audit function per the Standards?**

- A. Evaluate annually the effectiveness of the audit committee
- B. Issue annually an overall opinion on the adequacy of the organization's system of internal controls**
- C. Obtain an annual representation from management acknowledging management's responsibility for the design and implementation of internal controls to prevent illegal acts.

- D. Assess whether the information technology governance of the organization sustains and supports the organization's strategies and objectives.

### Chapter 3

#### 1. Which of the following is not an appropriate governance role for an organization's board of directors?

- A. Evaluating and approving strategic objectives.
- B. Influencing the organization's risk-taking policy.
- C. Providing assurance directly to third parties that the organization's governance processes are effective.**
- D. Establishing broad boundaries of conduct, outside of which the organization should not operate.

#### 2. Which of the following are typically governance responsibilities of senior management?

- i. Delegating risk tolerance levels to risk managers.
  - ii. Monitoring day-to-day performance of specific risk management activities
  - iii. establishing a governance committee of the board.
  - iv. Ensuring that sufficient information is gathered to support reporting to the board.
- A. i and iv.
  - B. ii and iii
  - C. i, ii, and iv.**
  - D. i, ii, iii and iv.

3. ABC utility company sells electricity to residential customers and is a member of an industry association that provides guidance to electric utilities, lobbies on behalf of the industry and facilitates sharing among its members. From ABC's perspective, what type of stakeholder is the industry association?

- A. Directly involved the operation of the company.
- B. Interested in the success of the company.
- C. Influences the company**
- D. Not a stakeholder.

#### 4. Who is responsible for establishing the strategic objectives of an organization?

- A. The board of directors**

- B. Senior management
- C. Consensus among all levels of management
- D. The board and senior management jointly.

**5. Who is ultimately responsible for identifying new or emerging key risk areas that should be covered by the organization's governance process?**

- A. The board of directors
- B. Senior management**
- C. Risk owners
- D. The internal audit function

6. The Internal Audit function should not:

- A. Assess the organization's governance and risk management processes.
- B. Provide advice about how to improve the organization's governance and risk management processes.
- C. Oversee the organization's governance and risk management processes.**
- D. Coordinate its governance and risk management-related activities with those of the independent outside auditor.

7. Which of the following would not be considered a first line of defense in the Three Lines of Defense model?

- A. A divisional controller conducts a peer review of compliance with financial control standards.**
- B. An accounts payable clerk reviews supporting documents before processing an invoice for payment.
- C. An accounting supervisor conducts a monthly review to ensure all reconciliations were completed properly.
- D. A production line worker inspects finished goods to ensure the company's quality standards are met.

## **Chapter 5**

1. In assessing organization risk in a manufacturing organization, which of the following would have the greatest long-range impact on the organization?

- A. Advertising budget

- B. Production scheduling
- C. Inventory policy
- D. Product quality**

2. Internal auditors often prepare process maps and reference portions of these maps to narrative descriptions of certain activities. This an appropriate procedure to:

- A. Determine the ability of the activities to produce reliable information.
- B. Obtain the understanding necessary to test the process.**
- C. Document that the process meets internal audit standards.
- D. Determine whether the process meets established management objectives.

3. If a risk appears in the bottom right of quadrant II in the above risk control map, it means that:

- A. There is an appropriate balance between risk and control
- B. the controls may be excessive relative to the risk**
- C. the controls may be inadequate relative to the risk
- D. there is not enough information to make a judgment

4. If a risk appears in the middle of quadrant IV in the above risk control map, it means that:

- A. There is an appropriate balance between risk and control**
- B. the controls may be excessive relative to the risk
- C. the controls may be inadequate relative to the risk
- D. there is not enough information to make a judgment

5. Which of the following circumstances would concern the internal auditor the most?

- A. A risk in the lower left corner of quadrant I
- B. A risk in the lower right corner of quadrant II
- C. A risk in the upper left corner of quadrant III**
- D. A risk in the upper right corner of quadrant IV

6. Which of the following are business processes?

I. strategic planning

II. Review and write off of delinquent loans.

III. Safeguarding of assets

IV. Remittance of payroll taxes to the respective tax authorities

A. I and III

**B. II and IV**

C. I, II and IV

D. I, II, III and IV

7. Which of the following symbols in a process map will most likely contain a question?

A. Rectangle

**B. Diamond**

C. Arrow

D. Oval

8. After business risks have been identified, they should be assessed in terms of their inherent:

**A. impact and likelihood**

B. likelihood and probability

C. significance and severity

D. significance and control effectiveness

9. In a risk by process matrix, a process that helps to manage a risk indirectly would be shown to have:

A. a key link

**B. a secondary link**

C. an indirect link

D. no link at all

10. A major upgrade to an important information system would most likely represent a high:

A. external risk factor

- B. **internal risk factor**
- C. other risk factor
- D. likelihood of future systems problems

**11. Which of the following is true regarding business process outsourcing?**

- A. Outsourcing a core, high-risk business process business process reduces the overall operational risk.
- B. Outsourced processes should not be included in the internal audit universe.
- C. The independent outside auditor is required to review all significant outsourced business processes.
- D. **Management's controls to ensure the outsourcing provide meets contractual performance requirements should be tested by the internal audit function**

**Chapter 6**

**1. Which of the following best describes an internal auditor's purpose in reviewing the organization's existing governance, risk management, and control processes?**

- A. To help determine the nature, timing, and extent of tests necessary to achieve engagement objectives.
- B. To ensure that weaknesses in the internal control system are corrected.
- C. **To provide reasonable assurance that the process will enable the organization's objectives and goals to be met efficiently and economically.**
- D. To determine whether the processes ensure that the accounting records are correct and that financial statements are fairly stated

**2. What is residual risk?**

- A. Impact of risk.
- B. Risk that is under control.
- C. **Risk that is not managed.**
- D. Underlying risk in the environment.

**3. The requirement that purchases be made from suppliers on an approved vendor list is an example of a:**

- A. Preventive control.**
  - B. Detective control.
  - C. Compensating control.
  - D. Monitoring control.
4. An effective system of internal controls is most likely to detect a fraud perpetrated by a:
- A. Group of employees in collusion.
  - B. Single employee.**
  - C. Group of managers in collusion.
  - D. Single manager.
5. The control that would most likely ensure that payroll checks are written only for authorized amounts is to:
- A. Conduct periodic floor verification of employees on the payroll.
  - B. Require the return of undelivered checks to the cashier.
  - C. Require supervisory approval of employee timecards.**
  - D. Periodically witness the distribution of payroll checks.
6. An internal auditor plans to conduct an audit of the adequacy of controls over investments in new financial instruments. Which of the following would not be required as part of such an engagement?
- A. Determine whether policies exist that describe the risks the treasurer may take and the types of instruments in which the treasurer may invest.
  - B. Determine the extent of management oversight over investments in sophisticated instruments.
  - C. Determine whether the treasurer is getting higher or lower rates of return on investments than treasurers in comparable organizations.**
  - D. Determine the nature of monitoring activities related to the investment portfolio.
7. Appropriate internal control for a multinational corporation's branch office that has a department responsible for the transfer of money requires that:
- A. The individual who initiates wire transfers does not reconcile the bank statement.**

- B. The branch manager must receive all wire transfers.
- C. Foreign currency rates must be computed separately by two different employees.
- D. Corporate management approves the hiring of employees in this department.

**8. Who has primary responsibility for the monitoring component of internal control?**

- A. The organization's independent outside auditor.
- B. The organization's internal audit function.
- C. The organization's management.**
- D. The organization's board of directors.

9. Reasonable assurance, as it pertains to internal control, means that:

- A. The objectives of internal control vary depending on the method of data processing used.
- B. A well-designed system of internal controls will prevent or detect all errors and fraud.
- C. Inherent limitations of internal control preclude a system of internal control from providing absolute assurance that objectives will be achieved.**
- D. Management cannot override controls and employees cannot circumvent controls through collusion.

10. Which of the following best exemplifies a control activity referred to as independent verification?

- A. Reconciliation of bank accounts by someone who does not handle cash or record cash transactions.**
- B. Identification badges and security codes used to restrict entry to the production facility.
- C. Accounting records and documents that provide a trail of sales and cash receipt transactions.
- D. Separating the physical custody of inventory from inventory accounting.

11. The risk assessment component of internal control involves the:

- A. Independent outside auditor's assessment of residual risk.
- B. Internal audit function's assessment of control deficiencies.

- C. **Organization's identification and analysis of the risks that threaten the achievement of its objectives.**
- D. Organization's monitoring of financial information for potential material misstatements.

## Chapter 7

1. **The software that manages the interconnectivity of the system hardware devices is the:**

- A. Application software.
- B. Utility software.
- C. **Operating system software**
- D. Database management system software

2. An internet firewall is designed to provide protection against:

- A. Computer viruses
- B. **Unauthorized access from outsiders.**
- C. Lightning strikes and power surges
- D. Arson

3. Which of the following best illustrates the use of EDI?

- A. purchasing merchandise from a company's internet site
- B. **computerized placement of a purchase order from a customer to its supplier**
- C. transfer of data from a desktop computer to a database server
- D. withdrawing cash from an ATM

4. The possibility of someone maliciously shutting down an information system is most directly an element of:

- A. availability risk
- B. **access risk**
- C. confidentiality risk
- D. deployment risk

5. An organization's IT governance committee has several important responsibilities. Which of the following is not normally such a responsibility?

- A. aligning investments in IT with business strategies
- B. overseeing changes to IT systems
- C. monitoring IT security procedures
- D. designing IT application-based controls**

6. If a sales transaction record was rejected during input because the customer account number entered was not listed in the customer master file, the error was most likely detected by a:

- A. completeness check
- B. limit check
- C. validity check**
- D. reasonableness check

7. The purpose of logical security controls is to:

- A. restrict access to data**
- B. limit access to hardware
- C. record processing results
- D. ensure complete and accurate processing of

**8. Which of the following statements regarding an internal audit function's continuous auditing responsibilities is/are true?**

**I. the internal audit function is responsible for assessing the effectiveness of management's continuous monitoring activities.**

**II. In areas of the organization in which management has implemented effective monitoring activities, the internal audit function can conduct less stringent continuous assessments of risk and controls.**

- A. Only I is true
- B. Only II is true
- C. Both statements I and II are true**
- D. Neither statement I nor statement II is true

## Chapter 10

**1. Professional scepticism means that internal auditors beginning an assurance engagement should:**

- A. Assume client personnel are dishonest until they gather evidence that clearly indicates otherwise.
- B. Assume client personnel are honest until they gather evidence that clearly indicates otherwise.
- C. Neither assume client personnel are honest nor assume they are dishonest ineffectively.**
- D. Assume that internal controls are designed inadequately and/or operating ineffectively.

2. Which of the following statements regarding audit evidence would be the least appropriate for an internal auditor to make?

- A. I will consider the level of risk involved when deciding the kind of evidence I will gather.
- B. I do not perform procedures that provide persuasive evidence because I must obtain convincing evidence.**
- C. I evaluate both the usefulness of the evidence I can obtain and the cost to obtain it.
- D. I am seldom absolutely certain about the conclusions I reach based on the evidence I examine.

3. Audit evidence is generally considered sufficient when:

- A. It is appropriate
- B. There is enough of it to support well-founded conclusions**
- C. It is relevant, reliable, and free from bias.
- D. It has been obtained via random sampling

4. Documentary evidence is one of the principal types of corroborating information used by an internal auditor. Which one of the following examples of documentary evidence generally is considered the most reliable?

- A. A vendor's invoice obtained from the accounts payable department.**
- B. A credit memorandum prepared by the credit manager.
- C. Receiving report obtained from the receiving department.

D. A copy of a sales invoice obtained from the sales department.

**5. An internal auditor must weigh the cost of an audit procedure against the persuasiveness of the evidence to be gathered. Observation is one audit procedure that involves cost-benefit trade-offs. Which of the following statement regarding observation as an audit procedure is/are correct?**

**I. Observation is limited because individuals may react differently when being watched.**

**II. Observation is more effective for testing completeness than it is for testing existence.**

**III. Observation provides evidence about whether certain controls are operating as designed.**

A. I only

B. II only

**C. I and III**

D. I, II, and III

6. An internal auditor gathered the following accounts receivable trend and ratio analysis information: Which of the following is the least reasonable explanation for the changed observed by the auditor?

	Year		
	3	2	1
Net accounts receivable as % of total assets	30.8%	27.3%	23.4%
Accounts receivable turnover (net sales/avg accts rec)	5.21	6.05	6.98

Which of the following is the least reasonable explanation for the changes observed by the auditor?

A. Fictitious sales may have been recorded in years 2 and 3

B. The effectiveness of credit and collection procedures deteriorated over the 3year period

**C. Sales returned for credit were overstated in years 2 and 3**

D. The allowance for bad debts was understated in years 2 and 3

7. Your audit objective is to determine that purchases of office supplies have been properly authorized. If purchases of office supplies are made through the purchasing department, which of the following procedures is most appropriate?

**A. Vouch purchase orders to approved purchase requisitions.**

- B. Trace approved purchase requisitions to purchase orders.
- C. Inspect purchase requisitions for proper approval.
- D. Vouch receiving reports to approved purchase orders.

8. A Production manager of MSM Company ordered excessive raw materials and had the materials delivered to a side business he operated. The manager falsified receiving reports and approved the invoices for payment. Which of the following procedures would most likely detect this fraud?

- A. Vouch cash disbursements to receiving reports and invoices.
- B. Confirm the amounts of raw materials purchased, purchase prices, and dates of shipment with vendors.
- C. Perform ratio and trend analysis compare the cost of raw materials purchased with the cost of goods produced.**
- D. Observe the receiving dock and count materials received. Compare the counts with receiving reports completed by receiving personnel.

9. An internal auditor is concerned that fraud, in the form of payments to fictitious vendors, may exist. Company purchasers, responsible for purchases of specific product lines, have been granted the authority to approve expenditures up to \$10,000. Which of the following applications of generalized audit software would be most effective in addressing the auditor's concern?

- A. List all purchases over \$10,000 to determine whether they were properly approved.
- B. Take a random sample of all expenditures under \$10,000 to determine whether they were properly approved.
- C. List all major vendors by product line. Select a sample of major vendors and examine supporting documentation for goods or services received.
- D. List all major vendors by product line. Select a sample of major vendors and send negative confirmations to validate that they actually provided goods or services.**

10. Which of the following most completely describes the appropriate content of internal audit assurance engagement working papers?

- A. Objectives, procedures, and conclusions.
- B. Purpose, criteria, techniques and conclusions.
- C. Objectives, procedures, facts, conclusions and recommendations.**
- D. Subject, purpose, sampling information, and analysis.

11. Internal audit engagement teams prepare working papers primarily for the benefit of the:

- A. Auditee
- B. Internal audit function**
- C. Board and senior management
- D. Independent outside auditor.

### Chapter 13

1. Which of the following is not likely to be an assurance engagement objective?

- A. Evaluate the design adequacy of the payroll input process.
- B. Guarantee the accuracy of recorded inventory balances.**
- C. Assess compliance with health and safety laws and regulations.
- D. Determine the operating effectiveness of fixed asset controls.

2. A process objective stating "all contracts must be approved by an officer of the company before being consummated" is an example of what type of objective?

- A. Strategic
- B. Operations
- C. Reporting
- D. Compliance**

3. Analytical procedures can be applied during which phase(s) of an assurance engagement?

- A. Plan phase
- B. Perform phase
- C. Communicate phase
- D. Plan and perform phases**

4. Which of the following auditee-prepared documents will likely be of greatest assistance to the internal auditor in their assessment of process design adequacy?

- A. Policies and procedures manual

B. Organization charts and job descriptions

**C. Detailed flowcharts depicting the flow of the process**

D. Narrative memoranda listing key tasks for portions of the process

5. Which of the following controls is not likely to be an entity-level control?

A. All employees must receive ongoing training to ensure they maintain their competence.

**B. All cash disbursement transactions must be approved before they are paid.**

C. All employees must comply with the Code of Ethics and Business Conduct.

D. An organization-wide risk assessment is conducted annually.

6. Which of the following is not typically a key element of flowcharts or narrative memoranda?

**A. Overall process objectives.**

B. Key inputs to the process.

C. Key outputs from the process.

D. Key risks and controls.

**7. Which of the following external risks is least likely to impact the accuracy of financial reporting?**

A. The standard setting body in the organization's country issues a new financial accounting standard.

B. A recent judicial court case increases the likelihood that pending litigation will result in an unfavourable outcome.

C. Changes in standard industry contracts now allow for netting of payables and receivables.

**D. Competitor pressures cause the organization to pursue new sales channels.**

**8. Which of the following groups' risk tolerance levels are least relevant when conducting an assurance engagement?**

A. Senior management

B. Process-level management

C. The internal audit function

**D. Vendors and customers**

**9. Which of the following controls is likely to be least relevant when evaluating the design adequacy of a cash collections process?**

- A. Calculating the amount of cash received.
- B. Documenting the rationale for selecting the bank account into which the deposit will be made.**
- C. Matching the total deposits to the amounts credited to customers' accounts receivable balances.
- D. Segregating the preparation of deposit slips from the adjustment of customer account balances.

10. An internal auditor determines that the process is not designed adequately to reduce the underlying risks to an acceptable level. Which of the following should the internal auditor do next?

- A. Write the audit report, there's no reason to test the operating effectiveness of controls that are not designed adequately.
- B. Test compensating controls in other (adjacent) processes to see if the impact of the design inadequacy is reduced to an acceptable level.**
- C. Test the existing key controls anyway to prove that, despite the design inadequacy, the process is still meeting the process objectives.
- D. Postpone the engagement until the design inadequacy has been rectified.

11. If an internal auditor identifies an exception while testing, which of the following may be appropriate?

- A. Test additional items to determine whether the exception is an isolated occurrence or indicative of a control deficiency.
- B. Gain an understanding of the root cause, that is, the reason the exception occurred.
- C. Draft an observation for the audit report.
- D. All of the above.**

12. Which of the following is appropriate conclusion that can be drawn when the internal auditor identifies an observation from testing controls?

- A. The process objectives cannot be achieved**
- B. The area may be vulnerable to fraud**

**C. Certain risks are not effectively mitigated**

D. Overall, the process is not operating effectively.

13. Once an observation is identified by the internal auditor, it should be:

**A. Documented in the working papers**

B. Discussed with the audit committee

C. Included in the final audit report

D. Scheduled for follow-up.

### **CIA Part 1**

1. The CAE is preparing the engagement work schedule for the next budget year and has limited resources. In deciding whether to schedule the purchasing or the personnel department for an engagement, which of the following is the least important factor?

A. Major changes have occurred in one of the department.

**B. The internal audit staff has recently added an individual with expertise in one of the areas.**

C. More opportunities to achieve operating benefits are available in one of the departments than in the other.

D. Updated assessed risk is significantly greater in one department than in another.

2. Which of the following best defines control?

**A. Control is the result of proper planning, organizing, and directing by management.**

B. Controls are statements of what the organization chooses to accomplish.

C. Control is provided when cost-effective measures are taken to restrict deviations to a tolerable level

D. Control accomplishes objectives and goals in an accurate, timely, and economical fashion.

3. Which of the following situations does an internal auditor potentially lack objectivity:

A. An internal auditor reviews the procedures for a new electronic data interchange (EDI) connection to a major customer before it is implemented.

- B. A former purchasing assistant performs a review of internal controls over purchasing 4 months after being transferred to the internal audit department.**
  - C. An internal auditor recommends standards of control and performance measure for a contract with a service organization for the processing of payroll and employee benefits.
  - D. A payroll accounting employee assists and internal auditor in verifying the physical inventory of small motors.
4. The proper organizational role of internal auditing is to:
- A. Assist the external in order to reduce external audit fees.
  - B. Perform studies to assist in the attainment of more efficient operations.
  - C. Serve as the investigate arm of the board.
  - D. Serve as independent, objective assurance and consulting activity that adds value to operations.**
5. Ordinarily, those conducting internal quality program assessments should report to:
- A. The board
  - B. The CAE**
  - C. Senior management
  - D. The internal auditing staff
6. The audit committee may serve several important purposes, some of which directly benefit the internal auditing activity. The most significant benefit provided by the audit committee to the internal audit activity is:
- A. Protecting the independence of the internal audit activity from undue management influence**
  - B. Reviewing engagement work schedules and monitoring engagement results.
  - C. Approve engagement work schedules, scheduling, staffing, and meeting with the internal auditors as needed
  - D. Compare engagements completed with engagements planned
7. A CAE's activity report should:
- A. List the material engagement observations of major engagements
  - B. List uncorrected reported conditions

C. Report the weekly activities of the individual internal auditors

**D. Compare engagements completed with engagements planned**

8. The internal audit activity can perform an important role in preventing and detecting significant fraud by being assigned all but which one of the following tasks?

A. Review large, abnormal, or unexplained expenditures

B. Review sensitive expenses such as legal fees, consultant fees, and foreign sales commissions

**C. Review every control feature pertaining to petty cash receipts**

D. Review contributions by the organization that appear to be unusual

9. Which of the following communication activities should the CAE provide to the audit committee?

**I. Keep the audit committee informed of emerging trends and successful practices in internal auditing**

**II. Issue periodic reports to the audit committees and management summarizing results of audit activities**

**III. Confirm there is effective and efficient work coordination of activities between internal and external auditors.**

10. "Due care implies reasonable care and competence, not infallibility more extraordinary performance." This statement makes which of the following unnecessary:

A. The conduct of examination and verifications to a reasonable extent.

**B. The conduct of detailed examinations.**

C. The reasonable assurance that compliance does exist.

D. The consideration of the possibility of material irregularities.

11. A certified IA is found to have committed a violation of the code of ethics of the institute of internal auditors. The violation is not serious enough to warrant the maximum disciplinary action. The most likely result is that the CIA will:

A. Be required to take up to 24 hours of appropriation continuing professional education courses.

B. Lose his or her CIA designation permanently unless subsequent reinstatement is approved by the BOD of the institute.

C. Be prohibited from engaging in the practice of IA for a period not to exceed 60 days.

**D. Receive from the institute's BOD a written censure with outlines the consequence of repeated similar actions.**

12. A certified internal auditor is in violation of the code of ethics when accepting a gift from a company employee unless the gift is:

- A. Smaller in dollar value.
- B. Approved by senior management.**
- C. Reciprocated by the auditor.
- D. Reported as income.

13. A certified internal auditor who is a member of the institute of internal auditors does not perform any of the activities that qualify as continuing professional development. Such an individual is in violation of the:

- A. Code of ethics.**
- B. Statement of responsibilities.
- C. AICPA standards relative to proficiency.
- D. SEC regulations to the competence of IAs.

14. A certified internal auditor who is found by the IIA BOD to have violated the code of ethics will:

- A. Be discharged by his employer.
- B. Forfeit the CIA designation.**
- C. Pay a fine to the appropriate court.
- D. Receive an official reprimand

15. A certified internal auditor who is judged by the BOD of the institute to be in violation of the provisions of the code of ethics shall be subjected to:

- A. Suspension of a certified internal auditor for a minimum of one year.
- B. Completion of additional continuing professional development hours to retain the certified internal auditor designation.
- C. Suspension as a certified internal auditor indefinitely until reinstatement by the board.
- D. Forfeiture of the certified internal auditor designation.**

16. A certified internal auditor, working for a chemical manufacturer, believed that toxic waste was being dumped in violation of the law. Out of loyalty of the company, no evidence regarding the dumping was corrected. The auditor:

- A. Violated the code of ethics by knowingly becoming a party to an illegal act.**
- B. Violated the code of ethics by failing to protect the well-being of the general public.
- C. Did not violate the code of ethics. Loyalty to the employer in all matters is required.
- D. Did not violated the code of ethics. Conclusive evidence of wrongdoing was not gathered.

17. A particular assignment would place an auditor in a situation where a conflict of interest could be inferred. However, the director of internal auditing is confident that the particular auditor has enough character and objectivity that this would not be a problem. The director should:

- A. Give the auditor the assignment but perform a close review of all work papers.
- B. Obtain audit committee approval of the assignment.
- C. Reassign the auditor.**
- D. Give the auditor the assignment but explain the conflict of interest in the report.

18. According to the standards, due professional care calls for:

- A. Detailed audits of all transactions related to a particular function.
- B. Infallibility and extraordinary performance when the system of internal controls is known to be weak.
- C. Consideration of the possibility of material irregularities during every audit assignment.**
- D. Testing in sufficient detail to give absolute assurance that noncompliance does not exist.

19. An auditor discovers some material inefficiencies in a purchasing function. The purchasing manager happens to be the auditor's next door neighbour and best friend. In accordance with the code of ethics, the auditor should:

- A. Objectively include the facts of the case in the audit report.**
- B. Not report the incident because of loyalty to the friend.
- C. Include the face of the case in a special report.
- D. Not report the friend unless the activity is illegal.

20. An internal auditor suspects that a mail room clerk is embezzling funds. In exercising due professional care, the auditor should:

- A. Reassign the clerk to another department.
- B. Institute stricter controls over mail room operations.
- C. Inform the appropriate authorities in the company.**
- D. Confront the clerk with his suspicions.

21. As an internal auditor, you have been assigned to a pre-acquisition audit. Coincidentally, a significant portion of your personal investment portfolio is comprised of the target company's stock. Select the preferable course of action to take in this situation based on your knowledge of the code of ethics.

- A. Acquaint the director of IA with the situation and ask to be assigned to another audit.**
- B. Acquaint the director of IA with the situation and offer assurance that it will have no impact on your objectivity.
- C. Proceed with the audit since your personal investments are not an issue.
- D. Proceed with the audit since your investment is insignificant to the whole target of the company's stock.

22. Certified internal auditors who fail to maintain their proficiency through continuing education could be found to be in violation of:

- A. The statement of responsibilities of IA
- B. The standards for professional practice of internal auditing.
- C. The institute of internal auditors code of ethics.
- D. Both the standards and the professional practice of IA and the institute of internal auditors code of ethics.**

23. For an internal auditor of an insurance company, which of the following activities would probably constitute a conflict of interest and thus be a violation of the CIA code of ethics?

- A. Working in the evenings as an assistant to a general agent of the insurance company.**
- B. Working an evening college course which identifies and evaluates alternative investment programs.
- C. Purchasing a whole life insurance policy from the insurance company.
- D. Entering into a partnership engaged in real estate development.

24. For which of the activities listed below could an internal auditor for ABC Life Insurance Company be held in violation of the code of ethics with respect to "conflict of interest"?

- A. Designing an accounting system for a general agent of ABC Life Insurance Company.
- B. Entering into a partnership engaged in land development.
- C. Assisting members of a fraternal organization, of which the internal auditor is a member, in planning their life insurance coverage.
- D. None of the above.**

25. In which of the following situations would a certified internal auditor be considered to have violated an article of the certified internal auditor code of ethics?

- A. Refusing the request of the corporation to deliver a packet of money to an official of a country with which the corporation is attempting to negotiate a serge contract.
- B. Taking 2 weeks off from work in order to attend an intensive advance course in dollar unit sampling.
- C. Accepting a gift from an executive who was portrayed favourable in an audit report.**
- D. Refusing to issue a report on an audit assignment without conducting extended tests.

26. Independence of the internal auditing department could be compromised if:

- A. The board of directors participates in the appointment or removal of the internal auditing department.
- B. The purpose, authority, and responsibility of the department of internal auditing are defined in a charter.
- C. The director of internal auditing submits annual activity reports to management and to the board.
- D. The director of internal auditing reports directly to the head of the accounting division.**

27. Objectivity for internal auditors is achieved through:

- A. The organizational status of the auditing department
- B. An attitude favourable to the auditee's personnel
- C. Not developing operating procedures for the activity being audited

**D. An independent mental attitude while performing the said audit.**

28. The appropriate authority responsible for determining unethical conduct in accordance with the certified internal auditor code of ethics is:

- A. The Securities and Exchange Commission.
- B. The board of directors of the institute of internal auditors.**
- C. The judicial system.
- D. Statutory boards of accountancy.

29. The auditor schedule to perform the next audit was recently transferred for the department to be reviewed and had operating responsibilities there. As director of internal auditing identify the appropriate action to take in this situation.

- A. Limit the scope of the audit.
- B. Assign the audit to someone else.**
- C. Qualify the audit opinion.
- D. Cancel the audit completely.

30. The best reason for establishing a code of conduct within an organization is that such codes:

- A. Are required by the foreign corrupt practices act.
- B. Express standard of individual behaviour for members of the organization.**
- C. Provides a quantifiable basis for personnel evaluations.
- D. Have tremendous public relations potential.

31. The internal auditor should maintain an independent mental attitude which is commonly called objectivity. Which of the following would compromise objectivity?

- A. Reviewing the results of internal auditing work before the related report is released.
- B. Periodically rotating the internal auditors' assignments.
- C. Forming conclusions on audit matters based on consultation with auditees.**
- D. Obtaining from the internal audit staff info concerning potential conflicts of interest and bias.

32. Under the code of ethics' provision with respect to gifts and fees, which of the following would be acceptable for an internal auditor to receive?

- A. A pen received from the sales manager of a subsidiary with the imprinted name of the company's product and a phone number.**
- B. A dinner and baseball tickets for the manager of a department being audited. The tickers are usually made available to employees of the audited department.
- C. A dinner and baseball tickets for the manager of a department that has never been audited and for which there are no plans in the future to audit.
- D. A bottle of whiskey for the corporate treasurer.

33. Which of the following actions by a certified internal auditor is a violation of the certified internal auditor code of ethics?

- A. Accepting a payment for teaching auditing at a local university.
- B. Owning a significant amount of stock in a public company which is a competitor.
- C. Accepting a moderate gift from a customer of his employer and subsequently informing a manager of the internal auditing department.**
- D. Allowing use of the certified internal auditor designation in a context not involving his employment.

34. Which of the following actions by an auditor would violate the code of ethics?

- A. An audit activity managed by the auditor's spouse.**
- B. A material financial investment in the company.
- C. Use of a company car.
- D. A significant ownership interest in anon-related business.

35. Which of the following actions by an internal auditor would violate the code of ethics?

- A. Attendance at an educational program offered by an auditee to all employees.
- B. Acceptance of airline tickets from an auditee.**
- C. Disclosure, in an audit opinion, of all material facts relevant to the audit area.
- D. Disposal of stock in the company prior to learning of a business downturn.

36. Which of the following actions taken by a director of internal auditing could be considered professionally ethical under the certified internal auditor code of ethics?

- A. The director decides to delay the audit of a branch so that his nephew, the branch manager, will have time to "clean things up".
- B. In order to save company resources the director cancels all staff training for the next 2 years on the basis that all staff are too new to benefit from training.
- C. In order to save company resources, the director limits the audit of foreign branches to confirmations from branch managers that no major personnel changes have occurred.
- D. The director refuses to provide info about company operation to his father who is a stockholder.**

37. Which of the following actions would constitute a violation of the certified internal auditor code of ethics?

- A. Purchasing stock in a corporation which was proposed for acquisition in a report to the executive committee.**
- B. Discussion of an employer's data processing control procedures at a trade convention.
- C. Omission of sensitive info from the written audit report after receiving approval from senior management.
- D. Investigation of executive expense reports after hearing rumours of expense account padding.

38. Which of the following activities would be acceptable under the certified internal auditor code of ethics?

- A. Late arrivals and early departures from work because this practice is common in the organization.
- B. Frequent luncheons and other socializing with major suppliers of the company w/o consent of sr. Management.
- C. Conducting an unrelated business outside of office hours.**
- D. Acceptance of a material gift from a supplier w/o the employer's knowledge.

39. Which of the following is a violation of the certified internal auditor code of ethics?

- A. Receiving a gift with the consent of senior management.
- B. Using confidential information for personal gain.**
- C. Part ownership in a small business unrelated to the internal auditor's employer.
- D. Disclosing confidential information in the court of law.

40. Which of the following policies is least likely to affect the internal auditor's interdependence?

- A. Prohibiting internal auditors from owning stock in the companies they audit.
- B. Periodically rotating assignments of auditors.
- C. Providing continuing professional development opportunities.**
- D. Reporting to the CEO.

41. Which of the following situations is a violation of the certified internal auditors' code of ethics?

- A. A CIA, with the knowledge and consent of management, accepted a material fee for services rendered to a customer of his employer.
- B. Knowing the management was aware of the situation, a CIA purposefully left a description of an unlawful practice at the top of the report.**
- C. A CIA shared audit techniques with auditors from another company.
- D. Based upon knowledge of the probable success of the employer's business, a CIA invested in a mutual fund that specializes in the same industry.

42. Which of the following statements does not describe one of the purposes of the IIA code of ethics?

- A. Outline criteria of acceptable professional behaviour.
- B. Charges IIA members to maintain high standards of conduct, honour, and character.
- C. Explains the internal audit profession's responsibility to society at large.**
- D. Assists internal auditors in advancing the interests of their company organization.

43. The interpretation related to quality assurance given by the standards is that:

- A. Quality assurance reviews can provide senior management and the audit committee with an assessment of the internal auditing function.**
- B. Appropriate follow up to an external review is the responsibility of the internal auditing director's immediate supervisor.
- C. The internal auditing department is primarily measured against the institute's code of ethics.
- D. Continual supervision is limited to the planning, examination, evaluation report and follow up processes.

44. To properly evaluate the operations of an internal auditing department, a quality assurance program should include:

- A. Periodic supervision of the internal audit work on a sample bases.
- B. Internal review, by other than the internal audit staff, to appraise the quality of department operations.
- C. External reviews every 5 years by qualified person who are independent of organization.**
- D. Periodic rotation of audit managers.

45. The standards require that the director of the internal auditing department establish quality assessment. A quality assessment program should include:

- A. Required supervisory review of all audit programs, work papers and draft audit reports including compliance w/ code of ethics.**
- B. Require coordination with external auditors.
- C. Required compliance with the code of ethics of the institute of internal auditors.
- D. Required educational standards for all members of professional audit staff.

46. The standards require that that internal audit director establish and maintain a quality assurance program to evaluate the operation of the internal auditing department. All of the following are considered elements of a quality assurance program except:

- A. Annual appraisals of individual internal auditors' performances.**
- B. Internal reviews of audit work.
- C. Supervision of audit work.
- D. External reviews to assess compliance w/ standards.

47. According to the standards, quality assurance and improvement performance should be designed to help the internal activity:

- I) Add value to the organization**
- II) Improve the organization's operations**
- III) Provide assurance that the internal audit activity is in conformity with the code of ethics.**

48. A quality assurance and improvement program should be developed by the organizations:

- A. External auditors.

B. Senior management.

**C. CAE**

D. Senior management and CAE.

49. According to the standards, disclosure of non-compliance of internal auditors with the standards and the code of ethics should occur:

A. When discovered by the CAE.

**B. When non-compliance impacts the overall scope or operations of the internal audit activity.**

C. Immediate, before beginning or continuing any internal audits.

D. At the discretion of the CAE.

50. According to the standards, internal assessment should include:

A. Annual reviews performed through self-assessment.

B. Reviews by other persons within the organization.

C. Reviews by senior management.

**D. Ongoing review of the performance of the internal audit activity.**

51. Which of the following are reasons to involve employees in the control self-assessment process?

I. Employees are more motivated to do their jobs correctly

**II. Employees are objective about their jobs**

III. Employees can provide an independent assessment of internal control

**IV. Managers want feedback from their employees**

52. A university finds it impractical to have a centralized receiving function of department purchases of books, supplies, and equipment. Which of the following controls would most effectively prevent payment for goods not received?

A. Vendor invoices should be matched with dept. purchase orders

B. Names and addresses on vendor invoices should be compared to a list of department authorized vendors.

**C. Vendor invoices should be approved by a department supervisor other than the employee ordering the goods.**

D. Invoices over a specified amount should be approved by the vice president of finance.

53. A utility company with a large investment in repair vehicles would most likely implement which internal control to reduce the risk of vehicle theft or loss:

- A. Review insurance coverage for adequacy.
- B. Systematically account for all repair work orders.
- C. Physically inventory vehicles and reconcile the results with the accounting records.
- D. Maintain vehicles in a secure location with release and return subject to approval by a custodian.**

54. A company's management accountant prepared a set of reports for top management. These reports detail the funds expended and the expenses incurred by each department for the current reporting period. The function of internal auditing would be to:

- A. Ensure against any and all noncompliance of reporting procedures.
- B. Review the expenditure items and match each item with the expenses incurred.
- C. Determine if there are any employees expending funds without authorization.
- D. Identify inadequate controls that increase the likelihood of unauthorized expenditures.**

55. Adequate internal controls are most likely to be present if:

- A. Management has planned and organized in a manner which provides reasonable assurance that the organization's objectives and goals will be achieved efficiently and economically.**
- B. Management has exercised due professional care in the design of operating and functional systems.
- C. Operating and functional systems are designed, installed and implemented in compliance with law.
- D. Management has designed, installed, and implemented efficient operating and functional systems.

56. An audit of the payroll function revealed several instances where a payroll clerk has added fictitious employees to the payroll and deposited the checks in accounts of close relatives. What controls should have prevented such actions?

- A. Using time cards and attendance records in the computation of employee gross earnings.
- B. Establishing a policy to deal with close relatives working in the same department.
- C. Having the treasurer's office sign payroll checks.

**D. Allowing changes to the payroll to be authorized only by the personnel department.**

57. An audit of a company's payroll department has revealed various control weaknesses. These weaknesses along with recommendations for corrective actions were addressed in the internal audit report. This report should be most useful to the company's:

- A. Treasurer.
- B. Audit committee of the board of directors.
- C. Payroll manager.**
- D. President.

58. An adequate system of internal control is most likely to detect an irregularity perpetrated by a:

- A. Group of employees in collusion.
- B. Single employees.**
- C. Group of managers in collusion.
- D. Single manager.

59. Assuming that the internal audit staff possesses the necessary experience and training, which of the following is appropriate for a staff auditor to undertake?

- A. Substitute for the accounts payable supervisor while he is out on sick leave.
- B. Determine the profitability of alternative investment acquisitions and select the best alternative.
- C. As a part of an evaluation team, review vendor accounting software internal controls and rank according to exposure.**
- D. Participate in an internal audit of the accounting department shortly after transferring from the accounting department.

60. Audit programs testing internal controls should:

- A. Be tailored for the audit of each operation.**
- B. Be generalized to fit all situations without regards to departmental lines.
- C. Be generalized so as to be usable at all locations of a particular department.
- D. Reduce costly duplication of effort by ensuring that every aspect of an operation is examined.

61. Bank tellers might use authorized teller terminals to conceal overdrafts in their personal checking accounts by transferring funds to and from customers' accounts. The best control is to detect the tellers unauthorized actions is requiring:

- A. Integrated test facility.
- B. Overnight balancing of all accounts on-line teller system.
- C. Periodic examination of accounts of employees with access to teller functions.**
- D. Annual vacations for employees with access to teller functions.

62. Corporate management has a role in the maintenance of internal control. In fact, management sometimes is a control. Which of the following involves managerial functions as a control device?

- A. Supervision of employees.**
- B. Use of corporate policies manual.
- C. Maintenance of a quality control department.
- D. Internal auditing.

63. Internal controls are designed to provide reasonable assurance that:

- A. Material errors or irregularities would be prevented or detected and corrected within a timely period by employees in the course of performing their assigned duties.**
- B. Management's plans have not been circumvented by worker collusion.
- C. The IA department's guidance and oversight of management's performance is accomplished economically and efficiently.
- D. Managements planning, organizing, and directing processes are poorly evaluated.

64. Maintaining a file of purchase orders in the receiving department for merchandise ordered but not yet received helps ensure that:

- A. Goods are delivered to the appropriate department in a timely manner.
- B. Only authorized shipments are accepted.**
- C. Goods are properly counted when they arrive.
- D. Good received are not misappropriated.

65. One risk associated with the purchasing cycle is the possibility that quantities in excess of organizational needs may be ordered. Which of the following controls would address this exposure:

- A. **Using department supervisor reviewing each purchase requisition prior to its being forwarded to the purchasing department.**
- B. The purchasing department placing all orders when the computer indicates a low inventory level.
- C. The receiving department delaying the unloading of each shipment present for receipt until an originating purchase order is available.
- D. The warehouse delaying the shortage of all good until the inspection. Department provides a receiving report that is consistent with the packing slip provided by the vendor.

66. One operating department of a company does not have adequate procedures for inspecting and verifying the quantities of goods received. To evaluate the materiality of this control deficiency, the auditor should review the department's:

- A. Year-end inventory balance.
- B. **Annual inventory purchases.**
- C. Year-end total assets.
- D. Annual operating expenses.

67. Shipments are made from the warehouse based on customer purchase orders. The matched shipping documents and purchase orders are then forwarded to the billing department for sales invoice preparation. The shipping documents are neither accounted for nor renumbered. Which of the following substantive tests should be extended as a result of control weakness?

- A. Select sales invoices from the sales register and examine the related shipping documents
- B. **Select bills of lading from the warehouse and trace the shipments to the related sales invoices**
- C. Foot the sales register and trace the total to the general register.
- D. Trace quantities and prices on the sales invoice to the customer purchase order and test extensions and footings.

68. The cash receipts function should be separated from the related record keeping function in an organization in order to:

- A. Physically safeguard the cash receipts.

- B. Establish accountability when the cash is first received.
- C. Prevent paying cash disbursement from cash receipts.
- D. Minimizes undetected misappropriation of cash receipts.**

69. The accountant who prepared a spreadsheet model for workload forecasting left the company and the person's successor was unable to understand how to use the spreadsheet. The best control for preventing such situations from occurring to ensure that:

- A. Use of end user computing resources is monitored.
- B. End user computing afforest are consistent with strategic plans.
- C. Documenting standards exist and are followed.**
- D. Adequate backups are made for spreadsheet models.

70. The purpose of a programmed balancing control is to mitigate the risk of:

- A. Lost transaction after a restart.
- B. Missing or improper transactions.
- C. Processing the wrong file.**
- D. Recording transactions in the wrong period.

71. The results of an audit of cash indicate the bookkeeper signs expense checks and reconciles the checking account, the cash account was properly reconciles and no shortages were detected. Select the appropriate overall audit opinion:

- A. In our opinion the systems of internal control over cash is adequate.
- B. Based on the audit results, it is out opinion that the system of internal control over cash is inadequate.**
- C. The results of the audit indicate reconciliations have been properly completed.
- D. In our opinion the physical cash handing procedures are adequate.

**A bank auditor is interested in estimating the average account balance of its depositors based on a sample. The substantive test is an example of:**

Variable Sampling

**A bank auditor wishes to confirm liability demand deposits. The bank has excellent internal control. The auditor might efficiently use all of the following sampling techniques in confirming demand deposits except:**

Discovery sampling

**A rental agency has branches located throughout the world that are essentially small scale representations of the entire population. What is the appropriate sampling method for determining the average net revenue per vehicle in inventory?**

Cluster sampling

**A confidence level of 95 percent for a variable sampling application can be interpreted as a 95% possibility that:**

Results of repeated samples will not vary from population characteristics by more than a specified amount.

**An internal auditor who believes the occurrence proportion of a certain characteristic in a population being examined is 3% and who has established a maximum acceptable occurrence proportion at 5% should use an:**

Attribute sampling

**A major distinction between statistical and non - statistical sampling is that:**

Statistical sampling provides an objective means of determining sample size

**A major problem in using a systematic sampling plan as opposed to a random selection plan is:**

To be sure there is not a coinciding pattern in the population

**A multistage sampling plan is most appropriate for evaluating ending inventory when:**

Inventory locations are geographically dispersed.

**A population that is physically separated into two or more groups based on the sample variation being less than that for the entire population is called:**

Stratified sampling

**A sampling method that can be used to estimate overstatement error of an account balance but is not based on normal curve mathematics is:**

Dollar - unit sampling

**A simple random sample requires that:**

Every item in the population has an equal chance of being selected.

**An attribute sampling plan would be useful in determining the estimate of the:**

Percentage of customers more than 30 days late in making payments

**An auditor applying a discovery - sampling plan with a five percent risk of over reliance may conclude that there is:**

A 95% probability that the actual rate of occurrence in the population is less than the critical rate if no exceptions were found.

**An auditor desired a sample of 50 items from a population of 5,000 items. The auditor initially planned to select a random number between 1 and 100 and to then systematically sample every 100th item from the random point. Later, evidence was found which related to the characteristic being measured or tested. The internal auditor should have:**

Use random number table to select items

**An auditor discovered that discounts for prompt payment were frequently not being taken. About 30% of the supplier's invoices offered discounts ranging from 2-5% of the invoice amount. To estimate the amount lost from not taking these discounts during the year, the most efficient and effective sampling technique would be:**

Ratio Estimation

**An auditor desires to select a statistically representative sample from a large population of unnumbered documents. Which sampling method would provide the best opportunity for a representative sample?**

Systematic sampling based on multiple random starting points in the population.

**An auditor desires to use a table of random digits to select a sample from a population of documents which have the following broken # sequences: 0001-1000, 2000-5000, and 8000-11000. Which of the following is the most efficient approach to overcome the problem of broken number sequences?**

Deduct 4 digit constant values from the second and third sequences, choose the appropriate random numbers, and add the constants back to the individual numbers.

**An auditor draws a random sample of invoices and computes the mean invoice amount. The auditor then computes the standard error of the mean. The information can be used to:**

- Determine the standard deviation of the sample AND
- Measure the variability that exists among all the possible invoice samples of the same size

**According to COSO, which of the following components of enterprise risk management addresses an entity's integrity and ethical values?**

Internal Environment

**Which of the following are included in the control environment described in the COSO internal control framework?**

Integrity & Ethical Values, Assignment of Authority, Human Resource Policies

**In regard to the IIA's Electronic System Assurance and Control study, which of the following is not a business assurance objective?**

Recordability

**When an internal auditor followed up on a significant increase in maintenance supplies during the past year, a purchasing agent explained to the internal auditor that the primary reason for the increase was painting services and supplies. The internal auditor found a blanket purchase order without the normal bid or quote documentation. The blanket purchase order had been signed by the general manager and named the general manager's father as the sole contractor for painting services on the organization's projects. The auditor also found a number of large invoices, authorized for payment by the general manager, that showed the general manager's father as the person who signed for the receipt of the material at the supplier. Which is not a symptom of fraud as described in this situation?**

The use of blanket purchase orders

**When comparing perpetrators who have embezzled an organization's funds with perpetrators of financial statement fraud (falsified financial statements), those who have falsified financial statements are less likely to**

Be living beyond their obvious means of support

**Internal auditing is responsible for assisting in the prevention of fraud by**

Examining and evaluating the adequacy and effectiveness of control, commensurate with the extent of the potential exposure or risk in the various segments of the organization's operations

**The function of the chief risk officers (CRO) is most effective when the CRO**

Monitors risk as part of the enterprise risk management team

**An expected decrease in which of the following ratios could indicate that fictitious inventory has been recorded?**

Total asset turnover

**Which of the following statements is correct regarding corporate compensation systems and related bonuses?**

**I. A bonus system should be considered part of the control environment of an organization and should be considered in formulating a report on internal control.**

**II. Compensation systems are not part of an organization's control system and should not be reported as such.**

**III. An audit of an organization's compensation system should be performed independently of an audit of the control system over other functions that impact corporate bonuses.**

I Only

**Many organizations use electronic funds transfer to pay their suppliers instead of issuing checks. Regarding the risks associated with issuing checks, which of the following risk management techniques does this represent?**

Avoiding

**"He made the books balance. Because of these activities, John was able to purchase an expensive car and take his family on several trips each year."**

**Symptoms of fraud are also studied. Number 5, "he made the books balance," is an example of a(n)**

Document Symptom

**Management has a role in the maintenance of control. In fact, management sometimes is a control. Which of the following most likely involves managerial functions as a control?**

Monitoring performance

**Inherent Risk**

The risk when management has not taken action to reduce the impact or likelihood of an adverse event

**A manufacturing firm identified that it would have difficulty sourcing raw materials locally, so it decided to relocate its production facilities. According to COSO, this decision represents which of the following responses to the risk?**

Risk Reduction

**Which of the following is not a component of the CoCo model?**

Control Environment

**Under the COSO's ERM framework, which of the following most accurately describes risk management responsibilities?**

In practice, management has primary responsibility.

**According to COSO, the position or internal entity that is best suited, as part of the enterprise risk management process, to devise and execute risk procedures for a particular department is**

A manager within the department

**One factor that distinguishes fraud from other employee crimes is that fraud involves**

Intentional Deception

**The components of ERM should be present and functioning effectively. What does "present and functioning effectively" mean?**

No material weaknesses exist.

Risk is within the risk appetite

**The COSO model for internal control lists seven specific areas encompassed by the control environment component. Which of the following are elements of the control environment?**

Organizational Structure

Integrity and Ethical Values

Assignment of Authority and Responsibility

**Which of the following wrongful acts committed by an employee constitutes fraud?**

Embezzlement

**In the risk management process, management's view of the internal audit activity's role is likely to be determined by all of the following factors except**

Preferences of the independent auditor

**An international non-profit organization finances medical research. The majority of its revenue and support comes from fundraising activities, investments, and specific grants from an initial sponsoring corporation. The organization has been in operation over 15 years and has a small internal audit department. The organization has just finished a major fundraising drive that raised US \$500 million for the current fiscal period. Auditors must always be alert for the possibility of fraud. Assume the controls over each risk listed below are marginal. Which of the following possible frauds or misuses of organization assets should be considered the area of greatest risk?**

Grants are made to organizations that might be associated with the president or are not for purposes dictated in the organization's charter

**After noting some red flags, an internal auditor has an increased awareness that fraud may be present. Which of the following best describes the internal auditor's responsibility?**

Expand activities to determine whether an investigation is warranted

**A company's new time clock process requires hourly employees to select an identification number and then choose the clock-in or clock-out button. A video camera captures an image of the employee using the system. Which of the following exposures can the new system be expected to change the least?**

Errors in employees' overtime computation

**Which of the following best describes an auditor's responsibility after noting some indicators of fraud?**

Expand activities to determine whether an investigation is warranted

**Which of the following is not a responsibility of the chief audit executive?**

To oversee the establishment, administration, and assessment of the organization's system of risk management processes

**Limitations of ERM may arise from all of the following except:**

Failure to achieve objectives

**Internal control can provide only reasonably assurance that the organization's objectives will be met efficiently and effectively. One factor limiting the likelihood of achieving those objectives is that**

The cost of internal control should not exceed its benefits

**"He also joined an expensive country club." Symptoms of fraud are also studied. Number 6, "He also joined an expensive country club," is an example of a**

Lifestyle symptom

**Which of the following is an indicator of increased risk of fraud? The treasurer**

Takes no vacations and has refused promotion to vice president of finance

**Which risk response reflects a change from acceptance to sharing?**

Management purchased insurance on previously uninsured property

**"John was trusted completely and handled all financial functions. No one checked his work." Symptoms of fraud are also studied. Number 1, "John was trusted completely . . .," is an example of a(n)**

Opportunity to commit

**The internal audit activity has been assigned to perform an engagement involving a division. Based on background review, the internal auditor knows the following about management policies: Organizational policy is to rapidly promote divisional managers who show significant success. Thus, successful managers rarely stay at a division for more than 3 years. A significant portion of division management's compensation comes in the form of bonuses based on the division's profitability. The division was identified by senior management as a turnaround opportunity. The division is growing but is not scheduled for a full audit by the external auditors this year. The division has been growing about 7% per year for the past 3 years and uses a standard cost system. During the preliminary review, the internal auditor notes the following changes in financial data compared with the prior year:**

- a. Sales have increased by 10%.**
- b. Cost of goods sold has increased by 2%.**
- c. Inventory has increased by 15%.**
- d. Divisional net profit has increased by 8%.**

**Which of the following items might alert the internal auditor to the possibility of fraud in the division?**

A significant portion of management's compensation is directly tied to reported net profit of the division.

**Each of the following is a method to evaluate internal controls based on the framework set by the Committee of Sponsoring Organizations (COSO), except**

Distinguishing economy risk from industry risk and enterprise risk

**Auditors are more likely to detect fraud by developing/strengthening their ability to**

Recognize and question changes that occur in organizations

**Internal auditors should review the means of physically safeguarding assets from losses arising from**

Exposure to the elements

**Which of the following threatens the independence of an internal auditor who had participated in the initial establishment of a risk management process?**

Managing the identified risks

**Which of the following goals sets risk management strategies at the optimum level?**

Maximize shareholder value

**Which of the following policies is most likely to result in an environment conducive to the occurrence of fraud?**

Unreasonable sales and production goals

**Which of the following are elements of the control environment?**

Integrity and ethical values

Organization structure

Assignment of authority and responsibility

**Company management completes event identification and analyses the risks. The company wishes to assess its risk after management's response to the risk. According to COSO, which of the following types of risk does this situation represent?**

Residual risk

**Bank management suspects that a bank loan officer frequently made loans to fictitious entities, disbursed loan proceeds to personally established accounts, and then let the loans go into default. Some pertinent facts about the loan officer include:**  
a. A high standard of living, explained as the result of sound investments and not

taking vacations

- b. An expensive personal car obtained through business contracts
- c. Gasoline and repair bills submitted for a car assigned by the bank that are higher than the organization's average (mileage logs were submitted on a quarterly basis)
- d. Marked annoyance with questions from internal auditors

In this situation, typical indicators of the suspected fraud include all of the following except

Submitting gasoline and repaired bills that are higher than the company average

**The Enterprise Risk Management - Integrated Framework of the committee of sponsoring organizations (COSO) is best defined as a**

Process effected by an entity's board of directors, management, and other personnel

**The following are facts about a subsidiary:**

- a. The subsidiary has been in business for several years and enjoyed good profit margins although the general economy was in a recession, which affected competitors
- b. The working capital ratio has declined from a healthy 3:1 to 0.9:1.
- c. Turnover for the last several years has included three controllers, two supervisors of accounts receivable, four payable supervisors, and numerous staff in other financial positions
- d. Purchasing policy requires three bids. However, the supervisor of purchasing at the subsidiary has instituted a policy of sole-source procurement to reduce the number of suppliers.

**When conducting a financial audit of the subsidiary, the internal auditor should**

Consider 1, 2, 3, and 4 as warning signals of fraud

**The most common motivation for management fraud is the existence of**

Financial pressures on the organization

**What is residual risk?**

Risk that is not managed

**An organization's directors, management, external auditors, and internal auditors all play important roles in creating a proper control environment. Senior management is primarily responsible for**

Establishing a proper organizational culture and specifying a system of internal control

**An organization's directors, management, and internal auditors all have important roles in creating a proper control environment. Senior management is primarily responsible for**

Establishing a proper ethical culture

**According to COSO, which of the following is a compliance objective?**

To maintain a safe level of carbon dioxide emissions during production

**To minimize the risk that agents in the purchasing department will use their positions for personal gain, the organization should**

Rotate purchasing agent assignments periodically

**The internal auditor recognizes that certain limitations are inherent in any system of internal controls. Which one of the following scenarios is the result of an inherent limitation of internal control?**

A security guard allows one of the warehouse employees to remove assets from the premises without authorization

**Which of the following situations will cause an internal auditor to question the adequacy of controls over a purchasing function?**

Receiving reports are forwarded to purchasing when they are matched with purchase orders and sent to accounts payable

**The manager of a production line has the authority to order and receive replacement parts for all machinery that requires periodic maintenance. The internal auditor received an anonymous tip that the manager order substantially more parts than were necessary from a family member in the parts supply business. The unneeded parts were never delivered. Instead, the manager processed receiving documents and charged the parts to machinery maintenance accounts. The payments for the undelivered parts were sent to the supplier, and the money was divided between the manager and the family member. Which of the following internal controls would have most likely prevented this fraud from occurring?**

Segregating the receiving function from the authorization of parts purchases

**Of the following, which is the most efficient source for an auditor to use to evaluate a company's overall control system?**

Control Flowcharts

**Which of the following symbolic representations indicates that new payroll transactions and the old payroll file have been used to prepare payroll checks, prepare a printed payroll journal, and generate a new payroll file?**

The new payroll transactions and the old payroll file are represented by the magnetic tape symbols. These files are entered into the process function (the rectangle). The output is a new payroll file on magnetic tape and payroll checks and a printed payroll journal represented by the document symbols.

**If employee paychecks are distributed by hand to employees, which one of the following departments should be responsible for the safekeeping of unclaimed paychecks?**

Cashier departments

**Which of the following is not a type of control?**

Reactive

**Upon receipt of purchased goods, receiving department personnel match the quantity received with the packing slip quantity and mark the retail price on the goods based on a master price list. The annotated packing slip is then forwarded to inventory controls and goods are automatically moved to the retail sales area. The most significant control strength of this activity is**

Using a master price list for marking the sale price

**An advantage of using system flowcharts to document information about internal control instead of using internal control questionnaires is that system's flowcharts**

Provide a visual depiction of clients' activities

**A control likely to prevent purchasing agents from favouring specific suppliers is**

Rotating buyer assignments periodically

**Which of the following ensures that all inventory shipments are billed to customers?**

Shipping documents are pre-numbered and are independently accounted for and matched with sales invoices

**Which of the following controls could be used to detect bank deposits that are recorded but never made?**

Having bank reconciliations performed by a third party

**To control purchasing and accounts payable, an information system must include certain source documents. For a manufacturing organization, these documents should include**

Purchase requisitions, purchase orders, receiving reports, and vendor invoices

**Which of the following best defines control?**

Control is the result of proper planning, organizing, and directing by management.

**An organization has grown rapidly and has just automated its human resource system. The organization has developed a large database that tracks employees, employee benefits, payroll deductions, job classifications, ethnic code, age, insurance, medical protection, and other similar information. Management has asked the internal audit activity to review the new system.**

**Human resources and payroll are separate documents.**

**Which of the following combinations provides the best segregation of duties?**

Human resources adds employees, and payroll processes hours and enter employee bank account numbers. Paychecks are automatically deposited in the employee's bank account.

**The operations manager of a company notified the treasurer of that organization 60 days in advance that a new, expensive piece of machinery was going to be purchased. This notification allowed the treasurer to make an orderly liquidation of some of the company's investment portfolio on favourable terms.**

**What type of control was involved?**

Feedforward

**One payroll engagement objective is to determine whether segregation of duties is proper. Which of the following activities is not incompatible?**

Preparing attendance data and preparing the payroll

**A rental car agency's fleet maintenance division uses a different code for each type of inventory transaction. A daily summary report lists activity by part number and transaction code. The report is reconciled by the parts room supervisor to the day's material request forms and is then forwarded to the fleet manager for approval. The reconciliation of the summary report to the day's material request forms by the parts room supervisor**

Ensures the accuracy and completeness of data input

**Specific airline ticket information, including fare, class, purchase date, and lowest available fare options, as prescribed in the organization's travel policy, is obtained and reported to department management when employees purchase airline tickets from the organization's authorized travel agency. Such a report provides information for**

Quality of performance in relation to the organization's travel policy

**Managerial control can be divided into feedforward, concurrent, and feedback controls. Which of the following is an example of a feedback control?**

Variance analysis

**Which of the following describes the most effective preventive control to ensure proper handling of cash receipt transactions?**

One employee issues a pre-numbered receipt for all cash collections; another employee reconciles the daily total of pre-numbered receipts to the bank deposits.

**The actions taken to manage risk and increase the likelihood that established objectives and goals will be achieved are best described as**

Control

**One of two office clerks in a small organization prepares a sales invoice; however, the invoice is incorrectly entered by the bookkeeper in the general ledger and the accounts receivable subsidiary ledger for a smaller amount resulting from a transposition of digits. The customer subsequently remits the amount on the monthly statement. Assuming only three employees are in the department, the most effective control to prevent this type of error is**

Using predetermined totals to control posting routines

**Which of the following control procedures provides the greatest assurance that all donations to a not-for-profit organization are immediately deposited in its account?**

Use a lockbox to receive all donations

**Which of the following describes a control weakness?**

Purchasing procedures are well designed and are followed unless otherwise directed by the purchasing supervisor

**The use of financial statement analysis, quality control procedures, and employee performance evaluations are all examples of**

Feedback controls

**Which one of the following situations represents a strength of internal control for purchasing and accounts payable?**

Vendors' invoices are matched against purchase orders and receiving reports before a liability is recorded

**A recent inventory shortage at XYZ Corp., an unaffiliated supplier, contributed to production failures at OPS Corp. in the current period. To avoid future production failures because of supplier inventory shortages, the most appropriate method is for OPS to**

Inform XYZ about its risk appetite regarding supply failures

**This figure could be expanded to show the**

Details of the preparation of purchase orders

**Graphical notations that show the flow and transformation of data within a system or business area are called**

Data flow diagrams

**When a supplier of office products is unable to fill an order completely, it marks the out-of-stock items as back ordered on the customer's order and enters these items in a back order file that management can view or print. Customers are becoming disgruntled with the supplier because it seems unable to keep track of and ship out-of-stock items as soon as they are available. The best approach for ensuring prompt delivery of out-of-stock items is to**

Match the back order file to goods received daily

**Management is concerned with the potential for unauthorized changes in the payroll. Which of the following is the proper organizational structure to prevent such unauthorized changes?**

The personnel department authorizes the hiring and pay levels of all employees

**Which one of the following situations represents an internal control weakness in accounts receivable?**

Delinquent accounts are reviewed only by the sales manager

**The requirement that purchases be made from suppliers of an approved vendor list is an example of a**

Preventive control

**Appropriate internal control for a multinational corporation's brand office that has a monetary transfer unit requires that**

The individual who initiates wire transfers not reconcile the bank statement

**Which of the following observations made during the preliminary survey of a local department store's disbursement cycle reflects a control strength?**

The treasurer's office prepares checks for suppliers based on vouchers prepared by the accounts payable department

**An internal auditor is assigned to perform an engagement to evaluate the organization's insurance program, including the appropriateness of the approach to minimizing risks. The organization self-insures against large casualty losses and health benefits provided for all its employees. The organization is a large national firm with over 15,000 employees located in various parts of the country. It uses an outside claims processor to administer its healthcare program. The organization's medical costs have been rising by approximately 8% per year for the past 5 years, and management is concerned with controlling these costs. The healthcare processor wishes to implement controls that would help prevent fraud by dentists who are submitting billings for services not provided. Assume further that all the claims are submitted electronically to the healthcare processor. Which of the following control procedures would be the most effective?**

Develop a program that identifies procedures performed on an individual in excess of expectations was performed recently, or the average cost per claim

**Which of the following policies and procedures is consistent with effective administration of the insurance function?**

Final settlements are negotiated after claims are developed and submitted

**A preliminary survey of the purchasing function indicates that**

- Department managers initiate purchase requests that must be approved by the plant superintendent
- Purchase orders are typed by the purchasing department using pre-numbered and controlled forms
- Buyers regularly update the official vendor listing as new sources of supply become known
- Rush orders can be placed with a vendor by telephone but must be followed by a

**written purchase order before delivery can be accepted**

**- Vendor invoice payment requests must be accompanied by a purchase order and receiving report**

**One possible fault of this system is that**

Purchases could be made from a vendor controlled by a buyer at prices higher than normal

**Symbol X could represent**

An error report

**Auditors document their understanding of internal control with questionnaires, flowcharts, and narrative descriptions. A questionnaire consists of a series of questions concerning controls that auditors consider necessary to prevent or detect errors and fraud. The most appropriate question designed to contribute to the auditors' understanding of the completeness of the expenditure (purchases-payables) cycle concerns the**

Use and accountability of pre-numbered checks

**An organization has grown rapidly and has just automated its human resource system. The organization has developed a large database that tracks employees, employee benefits, payroll deductions, job classifications, ethnic code, age, insurance, medical protection, and other similar information. Management has asked the internal audit activity to review the new system. The automated system contains a table of pay rates matched with the employee job classifications. The best control to ensure that the table is updated correctly for only valid pay changes is to**

Require a supervisor in the department, who does not have the ability to change the table of pay rates, to compare the changes with a signed management authorization

**When documenting internal control, the independent auditor sometimes uses a systems flowchart, which can best be described as a**

Symbolic representation of a system or series of sequential processes

**Which of the following controls would help prevent overpaying a vendor?**

Reviewing and cancelling supporting documents when a check is issued

**Controls may be classified according to the function they are intended to perform, for example, as detective, preventive, or directive. Which of the following is a directive control?**

Requiring all members of the internal audit activity to be CIAs

An internal auditor noted that the accounts receivable department is separate from other accounting activities. Credit is approved by a separate credit department. Control accounts and subsidiary ledgers are balanced monthly. Similarly, accounts are aged monthly. The accounts receivable manager writes off delinquent accounts after 1 year, or sooner if a bankruptcy or other unusual circumstances are involved. Credit memorandum are pre-numbered and must correlate with receiving reports. Which of the following areas could be viewed as an internal control weakness of the above organization?

Write-offs of delinquent accounts

An internal auditor noted that several shipments were not billed. To prevent the recurrence of such nonbilling, the organization should

Numerically sequence and independently account for all controlling documents (such as packing slips and shipping orders) when sales journal entries are recorded

During an engagement involving a purchasing department, an internal auditor discovered that many purchases were made (at normal prices) from an office supplier whose owner was the brother of the director of purchasing. Controls were in place to restrict such purchases and no fraud appears to have been committed. In this case, the internal auditor should recommend

The initiation of a conflict-of-interest policy

Which one of the following situations represents an internal control weakness in the payroll department?

Paychecks are distributed by the employees' immediate supervisor

#### CIA Exam Question Bank - Part 1

#### Questions 1 - 100

##### 1. Which of the following is not true with regard to the internal audit charter?

- a. It defines the authorities and responsibilities for the internal audit activity.
- b. It specifies the minimum resources needed for the internal audit activity.
- c. It provides a basis for evaluating the internal audit activity.
- d. It should be approved by senior management and the board.

**b. Correct. The internal audit manual and annual audit plan help in determining the resource requirements.**

##### 2. The function of internal auditing, as related to internal financial reports, would be to

- a. Ensure compliance with reporting procedures.

- b. Review the expenditure items and match each item with the expenses incurred.
- c. Determine if there are any employees expending funds without authorization.
- d. Identify inadequate controls that increase the likelihood of unauthorized expenditures.

**d. Correct. Internal auditors are responsible for identifying inadequate controls, for appraising managerial effectiveness, and the pinpointing common risks.**

**3. The status of the internal audit activity should be free from the effects of irresponsible policy changes by management. The most effective way to assure that freedom is to**

- a. Have the internal audit charter approved by the board.
- b. Adopt policies for the functioning of the internal audit activity.
- c. Establish an audit committee as a subcommittee of the board.
- d. Develop written policies and procedures to serve as standards of performance for the internal audit activity.

**a. Correct. The purpose, authority, and responsibility of the IAA should be formally defined in the charter, which is approved by management and the board.**

**4. As part of a company-sponsored award program, an internal auditor was offered an award of significant monetary value by a division in recognition of the cost savings that resulted from the auditor's recommendations. According to the International Professional Practices Framework (IPPF), what is the most appropriate action for the auditor to take?**

- a. Accept the gift since the engagement is already concluded and the report issued.
- b. Accept the award under the condition that any proceeds go to charity.
- c. Inform audit management and ask for direction on whether to accept the gift.
- d. Decline the gift and advise the division manager's superior.

**c. Correct. Even though the gift is of significant value, since it is part of a company-sponsored program, it might be acceptable for the internal auditor to accept the gift; however, in these cases, it is recommended for the internal auditor to first confirm the acceptance with the CAE.**

**5. If a department's operating standards are vague and thus subject to interpretation, an auditor should**

- a. Seek agreement with the departmental manager as to the criteria needed to measure operating performance.
- b. Determine best practices in the area and use them as the standard.
- c. Interpret the standards in their strictest sense because standards are otherwise only minimum measures of acceptance.
- d. Omit any comments on standards and the department's performance in relationship to those standards, because such an analysis would be inappropriate.

**a. Correct. Based on Implementation Standard 2210.A3, if control criteria are inadequate, then internal auditors must work with management to develop appropriate evaluation criteria.**

**6. In which of the following would an internal auditor potentially lack objectivity?**

- a. The internal auditor reviews the procedures for a new electronic data interchange (EDI) connection to a major customer before it is implemented.
- b. A former purchasing assistant performs a review of the internal controls over purchasing four months after being transferred to the internal audit activity (IAA).
- c. An internal auditor recommends standards of control and performance measures for a contract with a service organization for a processing of payroll and employee benefits.
- d. A payroll accounting employee assists an internal auditor in verifying the physical inventory of small motors.

**b. Correct. According to the Standards, persons transferred to the internal audit activity (IAA) should not be assigned to audit those activities they previously performed until a reasonable period of time (at least one year) has elapsed.**

**7. Which of the following would not be considered a stated purpose of the IIA (as listed in the organization's articles of incorporation)?**

- a. To cultivate, promote, and disseminate knowledge and information concerning internal auditing and subjects related to internal auditing.
- b. To establish and maintain high standards of integrity, honor, and character among internal auditors.
- c. To publish the technical journal, The Internal Auditor.
- d. To promote social intercourse among the IIA's members.

**c. Correct. According to the articles of incorporation, the objectives of The IIA are: (1) to cultivate, promote, and disseminate knowledge and information concerning internal auditing and subjects related to internal auditing; (2) to establish and maintain high standards of integrity, honor, and character among internal auditors; (3) to promote social intercourse among its members; (4) to furnish information regarding internal auditing and the practice and methods thereof to its members, to other persons interested therein, and to the general public, and (5) to cause the publication of articles related to internal auditing and practices and methods thereof; and others (review all of the stated objectives). Publishing the technical journal, The Internal Auditor, is a method to promote the professionalism of internal auditing, but it is not a specific stated purpose.**

**8. An auditor's objectivity could be compromised in all of the following situations except**

- a. A conflict of interest.
- b. Auditee familiarity with auditor due to lack of rotation in assignment.
- c. Auditor assumption of operational duties on a temporary basis.
- d. Reliance on outside expert opinion when appropriate.

**d. Correct. It is highly likely that an auditor at some time will have to rely on the opinion of an outside expert.**

**9. An auditor, nearly finished with an engagement, discovers that the director of marketing has a gambling habit. The gambling issue is not directly related to the existing engagement and there is pressure to complete the current engagement. The auditor notes the problem and forwards the information to the chief audit executive but performs no further follow-up. The auditor's actions would**

- a. Be in violation of the IIA Code of Ethics for withholding meaningful information.
- b. Be in violation of the Standards because the auditor did not properly follow up on a red flag that might indicate the existence of fraud.
- c. Not be in violation of either the IIA Code of Ethics or Standards.
- d. Both a and b.

**c. Correct. There is no violation of either the Code of Ethics or the Standards.**

**10. Independence is most likely impaired by an internal auditor's**

- a. Continuation on an engagement at a division for which (s)he will soon be responsible as the result of a promotion.
- b. Reduction of the scope of an engagement due to budget restrictions.
- c. Participation on a task force that recommends standards for control of a new distribution system.
- d. Review of a purchasing agent's contract drafts prior to their execution.

**a. Correct. When the IAA or individual internal auditor is responsible for, or management is considering assigning, an operation that it might audit, the internal auditor's independence and objectivity may be impaired.**

**11. One of the purposes of the Standards for the International Professional Practice of Internal Auditing as stated in the Introduction to the current version of the Standards is to**

- a. Encourage the professionalization of internal auditing.
- b. Establish the independence of the internal audit activity and emphasize the objectivity of internal auditing.
- c. Encourage external auditors to make more extensive use of the work of internal auditors.
- d. Establish the basis for evaluating internal auditing performance.

**d. Correct. According to the IIA, the Standards are intended to: (1) State basic principles for the practice of internal auditing; (2) Provide a framework for performing and promoting value added internal audit activities; (3) Establish the basis for evaluating internal auditing performance; and (4) Improve organizational processes and operations.**

**12. The Standards require that the chief audit executive (CAE) seek the approval of management and the board of a formal, written internal audit charter. The purpose of the internal audit charter is to**

- a. Protect the internal auditing activity from outside influence.

- b. Establish the purpose, authority, and responsibility of the internal auditing activity.
- c. Define the internal auditor's relationship with the external auditor.
- d. Define the role of the chief audit executive as a member of the audit committee.

b. Correct. The purpose, authority and responsibility of the IAA must be formally defined in the charter.

**13. The best means for the internal auditing activity (IAA) to determine whether its goal of implementing broader audit coverage of functional activities has been met is through**

- a. Accumulation of audit findings by auditable area.
- b. Comparison of the audit plan to actual audit activity.
- c. Surveys of management satisfaction with the internal audit activity.
- d. Implementation of a quality assurance and improvement program.

d. Correct. Implementing a quality assurance and improvement program (QAIP) can assist the CAE in determining whether the IAA's audit coverage goals are being met. The QAIP evaluates and analyzes the effectiveness and efficiency of IAA operations, which has to do with understanding whether stated IAA goals and objectives are being achieved.

**14. Quality program assessments may be performed internally or externally. A distinguishing feature of an external assessment is its objective to**

- a. Provide independent assurance.
- b. Set forth the recommendations for improvement.
- c. Determine whether internal auditing services meet professional standards.
- d. Identify tasks that can be performed better.

a. Correct. External assessments of an IAA should appraise and express an opinion as to the IAA's compliance with the Standards for the International Professional Practice of Internal Auditing and, as appropriate, should include recommendations for improvement. External assessment should be conducted at least once every five years (PA 1312-1).

**15. During an engagement to evaluate the organization's accounts payable function, an internal auditor plans to confirm balances with suppliers. What is the source of authority for such contacts with units outside the organization?**

- a. Internal audit activity policies and procedures.
- b. The Standards.
- c. The Code of Ethics.
- d. The internal audit activity's charter.

d. Correct. The purpose, authority and responsibility of the internal audit activity should be defined in the charter. The charter should establish the internal audit activity's position within the organization; authorize access to records, personnel, and physical properties relevant to the performance of engagements; and define the scope of internal audit activities (PA 1000-1).

**16. External assessment of an internal audit activity is not likely to evaluate**

- a. The tools and techniques employed by the internal audit activity.
- b. Detailed cost-benefit analysis of the internal audit activity.
- c. Compliance with the Standards for the International Professional Practice of Internal Auditing.
- d. Adherence to the internal audit activity's charter.

b. Correct. The external assessment should consist of a broad scope of coverage that includes: (1) Conformance with the Definition of Internal Auditing, Standards, The Code of Ethics and the internal audit activity's charter, plans, policies, procedures, practices, and applicable legislative and regulatory requirements; (2) the expectations of the IAA expressed by the board, executive management and operational managers; (3) the integration of the IAA into the organization's governance process, including the relationships between and among the key groups involved in the process; (4) tools and techniques employed by the IAA; (5) the mix of knowledge, experience, and disciplines within the staff, including staff focus on process improvement; and (6) the determination as to whether or not the IAA adds value and improves the organization's operations (PA 1312-1.10). A detailed cost-benefit analysis of the IAA would not be part of the external assessment.

**17. During an internal audit, the internal auditor should exercise due professional care. Due professional care means that the internal auditor should consider**

- I. The extent of work needed to achieve the engagement's objectives.
- II. The relative complexity and materiality to which assurance procedures are applied.

- III. The probability of significant errors, irregularities, or noncompliance.
- IV. The engagement procedures necessary to ensure that all significant risks have been identified.
- a. I and II only.
- b. I, II and IV only.
- c. I, II, III and IV.
- d. I, II and III only.

d. Correct. Only items I, II and III are correct. The internal auditor can only provide reasonable assurance that significant risks will be identified, not a guarantee.

**18. Internal auditors need have an understanding with respect to which discipline?**

- a. Internal auditing procedures and techniques.
- b. Accounting principles and techniques.
- c. Management principles.
- d. Marketing techniques.

c. Correct. The internal auditor needs to have an understanding of management principles.

**19. If a department outside of the internal audit activity (IAA) is responsible for reviewing a function or process, the internal auditor should**

- a. Consider the work of the other department when assessing the function or process.
- b. Ignore the work of the other department and proceed with an independent audit.
- c. Reduce the scope of the audit since the work has already been performed by the other department.
- d. Yield the responsibility for assessing the function or process to the other department.

a. Correct. Review and testing of the other department's procedures may reduce necessary audit coverage of the function or process.

**20. Independence from outside pressure is an important factor for the internal audit activity (IAA) to work freely and objectively. Which of the following contributes to the internal auditor's independence?**

- a. Management should assist the IAA by reviewing, revising and forwarding engagement communications to the audit committee.
- b. The IAA reports directly to the audit committee, without corroborating engagement communications with management.
- c. Ideally, the IAA functionally reports to the audit committee but reports to the chief operating officer on all engagements relating to operations.
- d. The accuracy of the engagement communications should be verified with management, and the IAA should then report to management and the audit committee.

d. Correct. Internal auditors should first discuss conclusions and recommendations with management so management is able to verify the accuracy of the engagement communications. Final engagement communications would then be sent to the audit committee.

**21. The Standards require that internal auditors possess which of the following skills?**

- I. Internal auditors should understand human relations and be skilled in dealing with people.
- II. Internal auditors should be able to recognize and evaluate the materiality and significance of deviations from good business practices.
- III. Internal auditors should be experts on subjects such as economics, commercial law, taxation, finance, and information technology.
- IV. Internal auditors should be skilled in oral and written communication.
- a. I and II only.
- b. I, II and III only.
- c. I, II, III and IV.
- d. I, II and IV only.

I. Correct. Internal auditors need to understand human relations and be skilled in dealing with people.

II. Correct. Internal auditors need to be able to understand what constitutes materiality and significance of deviations from good business practice.

IV. Correct. Internal auditors should be skilled in oral and written communication.

**22. You were appointed the chief audit executive (CAE) of an organization one week ago. An engagement client has come to you complaining vigorously that one of your internal auditors is taking up an excessive**

**amount of the client's time on an engagement that seems to be lacking a clear purpose. In handling this conflict with the client, you should consider**

- a. Promising the client that you will have the internal auditor finish the work within 1 week.
- b. Whether existing procedures within the internal audit activity provide for proper planning and quality assurance.
- c. Presenting an immediate defense of the internal auditor based upon currently known facts.
- d. Discounting what is said, but documenting the complaint.

b. Correct. In this situation the CAE would have a responsibility to review the existing procedures to determine whether the IAA had provided for proper planning and quality assurance. Not doing so would jeopardize the authority of the CAE.

**23. According to the Standards, the internal audit activity's goals should specify**

- a. Policies and procedures to guide the internal audit staff.
- b. Engagement work schedules and activities to be reviewed.
- c. Measurement criteria and target dates for completion.
- d. Staffing plans and financial budgets.

c. Correct. The goals of the IAA should be capable of being accomplished within specified operating plans and budgets and, to the extent possible, should be measurable. They should be accompanied by measurement criteria and targeted dates of accomplishment.

**24. Which of the following best describes an internal auditor's purpose in reviewing the organization's existing risk management, control and governance processes?**

- a. To help determine the nature, timing, and extent of tests necessary to achieve engagement objectives.
- b. To ensure that weaknesses in the internal control system are corrected.
- c. To provide reasonable assurance that the processes will enable the organization's objectives and goals to be met efficiently and economically.
- d. To determine whether the processes ensure that the accounting records are correct and that financial statements are fairly stated.

c. Correct. As described by the IIA, the internal auditors' primary purpose in reviewing an organization's existing risk management, control, and governance processes is to provide reasonable assurance that these processes are functioning as intended and will enable the organization's objectives and goals to be met.

**25. Periodic external assessments of an internal audit activity's quality assurance and improvement program should be undertaken. On completion of such an assessment, a formal report or other communication should be issued expressing an opinion as to the**

- a. Adequacy of internal control.
- b. Effectiveness of the internal auditing coverage.
- c. Conformance with the internal audit activity's charter.
- d. Internal audit activity's compliance with the Standards.

d. Correct. The external assessment should consist of a broad scope of coverage that includes conformance with the Definition of Internal Auditing; the Code of Ethics; and the Standards (PA1312-1.10).

**26. During review of a construction contract, the chief audit executive (CAE) suspects that a construction company was given an unfair advantage in bidding on the contract. After learning that the chief executive officer (CEO) of the company is a member of the construction company's board of directors, how should the CAE proceed?**

- a. Submit a draft report to senior management, excluding the CEO.
- b. Contact the organization's external auditors for assistance.
- c. Obtain supporting documentation and present the finding to the chairperson of the audit committee.
- d. Immediately notify the board of directors.

c. Correct. A draft of the proposed report on fraud or conflict of interest situations should be submitted to the chairperson of the audit committee as a next step in light of the CEO's position in the company.

**27. Of the following activities, which ones are within the scope of internal auditing?**

- I. To assess an operating department's effectiveness in achieving stated organizational goals.
- II. To safeguard assets.
- III. To evaluate controls over compliance with laws and regulations.
- IV. To ascertain the extent to which objectives and goals have been established.

- a. I and III only.
- b. I and IV only.
- c. I, III and IV only.
- d. I, II and IV only.

I. Correct. Internal auditing should assess an operating department's effectiveness in achieving its stated goals.  
 III. Correct. Internal auditors should evaluate controls over compliance with laws and regulations.  
 IV. Correct. Internal auditors should ascertain the extent to which objectives and goals have been established.

**28. Which of the following represents the best governance structure?  
 Executive Management Board and Audit Committee Internal Auditing**

- a. Responsibility for risk Oversight role Advisory role
- b. Oversight role Responsibility for risk Advisory role
- c. Responsibility for risk Advisory role Oversight role
- d. Oversight role Advisory role Responsibility for risk

a. Correct. Executive management is responsible for risk management, board and audit committee provide an oversight function and internal auditor serve in the capacity of oversight and advisory roles.

**29. Assessments of the performance of the organization's external auditors should**

- a. Be carried out only when the external auditor is appointed.
- b. Not include any participation by the internal audit activity.
- c. Include the internal audit activity only when the external auditor is appointed.
- d. Include the internal audit activity at the time of the appointment and regularly thereafter.

d. Correct. Management and the board might request the IAA to participate in the performance of the external auditor, and this may include assessment of the external auditor's independence. In addition, this assessment should be carried out at least annually.

**30. A new chief audit executive (CAE) for a major retail company is questioning the audit activity's extensive use of store compliance testing, stating that the approach is not responsive to materiality concepts. Which of the following statements are valid in response to the CAE's claims?**

- I. Materiality is not based only on the size of individual stores; it is also based on the control structure that affects the whole organization.
  - II. Any deviation from a prescribed control procedure is, by definition, material.
  - III. The only way to ensure that a material amount of the company's control structure is reviewed is to comprehensively audit all stores.
- a. I only.
  - b. III only.
  - c. I and II only.
  - d. I, II and III.

I. Correct. Materiality is defined by the potential impact of an item on the organization and is not limited to items that can be assessed only in qualitative terms.

**31. Which of the following is the best means of aiding an internal audit activity (IAA) in determining whether its goals are being met?**

- a. Having external auditors review and evaluate the work of the internal audit activity.
- b. Having the board periodically review the quality of the internal audit activity's work.
- c. Developing measurement criteria to accompany its goals.
- d. Scheduling an external assessment every 3 years.

c. Correct. The goals of the IAA should be capable of being accomplished within specified operating plans and budgets and, to the extent possible, should be measurable. They should be accompanied by measurement criteria and targeted dates of accomplishment.

**32. The interpretation related to quality assurance given by the Standards is that**

- a. The IAA is primarily measured against the Institute's Code of Ethics.
- b. External assessments can provide senior management and the board with independent assurance about the quality of the IAA.
- c. Continual supervision is limited to the planning, examination, evaluation, communication, and follow-up process.
- d. Appropriate follow-up to an external assessment is the responsibility of the chief audit executive's immediate supervisor.

b. Correct. External assessments of an internal audit activity appraise and express an opinion as to the IAA's compliance with the Standards of the Professional Practice of Internal Auditing and, as appropriate, should include recommendations for improvement.

**33. The consultative approach to internal auditing emphasizes**

- a. Participation with engagement clients to improve methods.
- b. Imposition of corrective measures.
- c. Fraud investigation.
- d. Implementation of policies and procedures.

a. Correct. Consultation with the engagement client helps to facilitate good relations. This is important since the engagement client will be more likely to accept recommendations.

**34. As part of the process to improve internal auditor-engagement client relations, it is very important to deal with how the internal audit activity is perceived. Certain types of attitudes in the work performed will help create these perceptions. From a management perspective, which attitude is likely to be the most conducive to a positive perception?**

- a. Interrogatory.
- b. Investigative.
- c. Consultative.
- d. Objective.

c. Correct. A consultative attitude leads to two-way communication.

**35. Procedures describing how the supervisory review of staff auditors will be accomplished should be fully documented so that the internal audit activity will**

- a. Have a basis for promotions, pay raises, or disciplinary actions, if required.
- b. Have substantiation of its quality program.
- c. Comply with the Standards.
- d. Have a consistent framework for evaluating staff performance.

d. Correct. The IAA's quality program should provide reasonable assurance that the internal auditing work conforms to the Standards, the Code of Ethics, the IAA's charter, and other applicable standards

**36. An internal auditor often faces special problems when performing an engagement at a foreign subsidiary. Which of the following statements is true with respect to the conduct of internal international engagements?**

- a. The IIA Standards do apply outside the United States.
- b. The internal auditor should determine whether managers are in compliance with local laws.
- c. There may be justification for having different organizational policies in force in foreign branches.
- d. All of the above are true.

d. All of the above are true.

**37. The CAE of a fast growing software company wanted to promote the value added capabilities of internal auditing within the company. In order to achieve this goal the CAE instituted several initiatives. Which of the following initiatives would be considered appropriate?**

- I. The CAE promised that before the release of the final report, the auditor would review the findings with the client manager.
  - II. The CAE also promised that if the client manager disagreed with the conclusions of the report, the final report would contain the client manager's disagreements.
  - III. The CAE promised the client manager that if control deficiencies were in fact found, internal auditing has the capability to take care of the deficiencies.
- a. I only
  - b. II and III only
  - c. I and II only
  - d. I, II and III

I. Correct. Internal auditing should review findings with the client before release of the final report.

II. Correct. If the client disagrees with the conclusion of the report then the final report should contain any and all disagreements the client manager may have with the report.

**38. During an engagement to evaluate the organization's accounts payable function, an internal auditor plans to confirm balances with suppliers. What is the source of authority for such contracts with units outside the organization?**

- a. The internal audit activity policies and procedures.
- b. The Standards.
- c. The Code of Ethics.
- d. The internal audit activity's charter.

d. Correct. The charter is what gives the IAA the authority to confirm balances with suppliers

**39. Internal auditors must distinguish carefully between a scope limitation and other limitations. Which of the following is not considered a scope limitation?**

- a. The divisional manager of an engagement client has indicated that the division is in the process of converting a major computer system and has indicated that the information systems portion of the planned engagement will have to be postponed until next year.
- b. The board reviews the engagement work schedule for the year and deletes an engagement that the CAE thought was important to conduct.
- c. The engagement client has indicated that certain customers cannot be contacted because the organization is in the process of negotiating a long-term contract with the customers and do not want to upset the customers.
- d. None of the answers are correct.

b. Correct. The board has the right to delete an engagement from the annual IAA work schedule. Therefore, this is not considered to be a scope limitation.

**40. Which of the following combinations best illustrates a scope limitation and the appropriate response by the CAE?**

Nature of limitation internal audit action

- a. Engagement client limits scope based upon proprietary information.  
Report only to the controller
- b. Engagement client will not provide access to records needed for approved work schedule.  
Report to the board.
- c. Engagement client requests that the engagement be delayed for 2 weeks to allow it to close its books.  
Report directly to the CEO and controller.
- d. Engagement client will not allow internal auditor to contact major customers as part of an engagement to evaluate the efficiency of operations.  
No reporting is required because the operational engagement concerns operational efficiency.

b. Correct. This is the best combination. If the internal auditor does not have access to records then this fact needs to be reported to the board.

**41. Your organization has selected you to develop an IAA. Your approach will most likely be to hire**

- a. Internal auditors each of whom possesses all the skills required to handle all engagements.
- b. Inexperienced personnel and train them the way the organization wants them trained.
- c. Degreed accountants because most internal audit work is accounting related.
- d. Internal auditors who collectively have the knowledge and skills needed to perform the responsibilities of the IAA.

d. Correct. Collectively, the IAA should have necessary skills, knowledge and experience to carry out its activities. The IAA may use both internal and external resources that are qualified in such disciplines as accounting, tax, engineering, law, environmental, and IT.

**42. The consultative approach to internal auditing emphasizes**

- a. Imposition of corrective measures.
- b. Participation with engagement clients to improve methods.
- c. Fraud investigation.
- d. Implementation of policies and procedures.

b. Correct. Internal auditors need to maintain a satisfactory relationship with engagement clients. In order to enhance this relationship, it is good policy to involve the client on all engagements. Developing a positive relationship produces a more favorable environment for the engagement effort.

**43. An internal auditor issues a final report which had to do with evaluating the client's procedures for increasing the diversity of the organization's work force. In this regard, the internal auditor made several recommendations for changes in hiring and retaining practices. Regarding due professional care, the internal auditor would conduct a follow up to ensure which of the following actions by the client?**

- a. To ascertain whether the client has carried out the internal auditor's recommendations.
- b. To ascertain whether the organization is in line with the organization's diversity policies.
- c. To ascertain whether the client has considered the audit findings and has taken action to improve diversity within the organization.
- d. All of the following are true.

c. Correct. Exercise due professional care includes following up to see that the client has taken appropriate action. This does not mean that the client has to implement every recommendation submitted by the auditor but it is expected that the client would/should consider the recommendations.

**44. Which of the following persons might be considered when conducting a periodic external review of the internal auditing activity (IAA) in an organization's regional office?**

- I. An auditor from headquarters.
  - II. An internal audit "peer" from another organization's IAA.
  - III. A tax consultant who has no audit experience but will review only technical matters related to tax audits.
  - IV. An external chartered accountant with internal auditing experience who has been an external auditor of the organization's external financial reports.
- a. I and II only.
  - b. II and III only.
  - c. I, II, III and IV.
  - d. I, II and IV only.

d. I, II and IV only.

I. Correct. An auditor from the company's headquarters could be part of the external review of an organization's regional office's IAA.

II. Correct. An internal audit "peer" from another organization's IAA could be part of the external review of an organization's regional office's IAA.

IV. Correct. A chartered accountant with internal auditing experience and who had been an external auditor of the organization's external financial reports could be part of the external review of an organization's regional office's IAA.

**45. The IIA Standards require internal auditors to have the knowledge, skills and disciplines essential to performing an audit. Which of the following is true considering the level of knowledge or skill required by the Standards? Internal auditors must**

- I. Be proficient in the application of auditing standards and procedures to specific situations without extensive recourse to technical research and assistance.
  - II. Be proficient in accounting principles when auditing the financial records and reports of the organization.
  - III. Be proficient in applying knowledge of accounting and computerized information systems to specific or potential problems.
- a. I only.
  - b. I and II only.
  - c. II and III only.
  - d. I, II and III.

I. Correct. Internal auditors have to be proficient in applying the Standards.

II. Correct. Internal auditors must be proficient in accounting principles if auditing an organization's financial statements.

**46. A CIA, working as the purchasing director, signs a contract to procure a large order from the supplier with the best price, quality, and performance. Shortly after signing the contract, the supplier presents the CIA with a gift of significant monetary value. Which of the following statements regarding the acceptance of the gift is correct?**

- a. Acceptance of the gift would be prohibited only if it were non-customary.
- b. Acceptance of the gift would violate the IIA Code of Ethics and would be prohibited from a CIA.
- c. Since the CIA is not acting as an internal auditor, acceptance of the gift would be governed only by the organization's code of conduct.
- d. Since the contract was signed before the gift was offered, acceptance of the gift would not violate either the IIA Code of Ethics or the organization's code of conduct.

b. Correct. As long as the individual has the CIA designation, then he or she should be guided by the profession's Code of Ethics in addition to the organization's code of conduct. Rule of conduct 2.2 precludes such gifts because it could be presumed to have influenced the individual's decision.

**47. A review of an organization's code of conduct revealed that it contained comprehensive guidelines designed to inspire high levels of ethical behavior. The review also revealed that employees were knowledgeable of its provisions. However, some employees still did not comply with the code. What element should a code of conduct contain to enhance its effectiveness?**

- a. Periodic review and acknowledgment by all employees.
- b. Employee involvement in its development.
- c. Public knowledge of its contents and purpose.
- d. Provisions for disciplinary action in the event of violations.

d. Correct. Provisions for disciplinary action in the event of violations would be the most affect method to deter employees from conducting misconduct.

**48. Which of the following statements is not appropriate to include in a manufacturer's conflict of interest policy? An employee shall not**

- a. Accept money, gifts, or services from a customer.
- b. Participate (directly or indirectly) in the management of a public agency.
- c. Borrow from or lend money to vendors.
- d. Use organizational information for private purposes.

b. Correct. A person has the right to participate in the management of a public agency (a government agency). Thus, it would not be included in a manufacture's conflict of interest policy.

**49. An internal auditor, during the course of evaluating the policies & procedures for capitalizing fixed assets, uncovered some information that indicated that management had capitalized some general maintenance costs that should have been expensed. The amount is considered to be material. If the internal auditor failed to disclose this information to senior management or the Audit Committee, the internal auditor would be in violation of which rule of conduct?**

- a. Integrity.
- b. Objectivity.
- c. Confidentiality.
- d. Competence.

b. Correct. The internal auditor would be in violation of the objectivity rule of conduct. According to rule 2.3, internal auditors shall disclose all material facts known to them, that if not disclosed, may distort the reporting of activities under review. In this case, capitalizing general maintenance cost would distort the financial statements.

**50. Which of the following concurrent occupations could appear to subvert the ethical behavior of an internal auditor?**

- a. Internal auditor and a well-known charitable organization's local in-house chairperson.
- b. Internal auditor and part-time business insurance broker.
- c. Internal auditor and adjunct faculty member of a local business college that educates potential employees.
- d. Internal auditor and landlord of multiple housing that publicly advertise for tenants in a local community newspaper listing monthly rental fees.

b. Correct. According to the Code, an "Internal auditor shall not participate in any activity or relationship that may impair or be presumed to impair their unbiased assessment." Thus, an internal auditor and part-time business broker would be considered to be incompatible.

**51. Which of the following is not implied by the definition of control?**

- a. Measurement of progress toward goals.
- b. Uncovering of deviations from plans.
- c. Assignment of responsibility for deviations.
- d. Indication of the need for corrective action.

c. Correct. The basic process of control is to set objectives, measure performance and take corrective action is deficiencies are found. Assigning responsibility is not part of the controlling function.

**52. Which of the following different types of controls is often difficult to evaluate because it may lack established criteria or standards?**

- a. Operating controls.
- b. Financial controls.
- c. Directive controls.
- d. Preventive controls.

a. Correct. Operating controls are those applicable to production and support activities. In some cases, an operating activity, like customer service, or security, is difficult to measure because there is no set control standard.

**53. Which of the following operating controls relate to the organizing function?**

- a. Formal procedures for selecting potential suppliers.
- b. Procedures providing for clear levels of purchase order approvals based on the value of the requisition.
- c. Written objectives and goals for the department.
- d. Timely materials reporting to buyers.

b. Correct. Organizing is the intentional design and structuring of tasks and roles to accomplish organizational goals. An organizational arrangement whereby purchases of greater value require authorization at higher management levels is an example of an organizational control.

**54. Controls should be designed to ensure that**

- a. Operations are performed efficiently.
- b. Management's plans have not been circumvented by worker collusion.
- c. The IAA's guidance and oversight of management's performance is accomplished economically and efficiently.
- d. Management's planning, organizing, and directing processes are properly evaluated.

a. Correct. The purpose of the control process is to support people of the organization in the management of risks and the achievement of its established and communicated objectives. Control processes are expected to ensure that operations are performed efficiently and achieve established objectives (PA 2130).

**55. Enterprise risk management**

- a. Guarantees achievement of organizational objectives.
- b. Requires establishment of risk and control activities by internal auditors.
- c. Involves the identification of events with negative impacts on organizational objectives.
- d. Includes selection of the best risk response for the organization.

c. Correct. ERM is a process affected by entity's board, management, and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of objectives.

**56. Requests for purchases beyond those initially budgeted must be approved by the marketing manager. This procedure**

- I. Should provide for the most efficient allocation of scarce organizational resources.
  - II. Is a detective control procedure.
  - III. Is unnecessary because each product manager is evaluated on profits generated.
- a. I only.
  - b. III only.
  - c. II and III only.
  - d. I, II, III.

I. Correct. The marketing manager is high enough in the organization to coordinate this allocation.

**57. Which of the following control procedures does an internal auditor expect to find during an engagement to evaluate risk management and insurance?**

- a. Periodic internal review of the in-force list to evaluate the adequacy of insurance coverage.
- b. Required approval of all new insurance policies by the organization's CEO.
- c. Policy of repetitive standard journal entries to record insurance expense.
- d. Cutoff procedures with regard to insurance expense reporting.

a. Correct. Periodically reviewing the adequacy of the insurance policy is a risk assessment function. Insurance coverage should be sufficient to ensure that the relevant assessed risks are managed in accordance with the entity's risk appetite.

**58. Management can best strengthen internal control over the custody of inventory stored in an off-site warehouse by implementing**

- a. Reconciliations of transfer slips to/from the warehouse in inventory records.
- b. Increases in insurance coverage.

- c. Regular reconciliation of physical inventories to accounting records.
- d. Regular confirmation of the amount on hand with the custodian of the warehouse.

c. Correct. The best control would be to reconcile inventory on hand at the off-site warehouse with the company's accounting records. Discrepancies would be investigated.

**59. Which of the following describes a control weakness?**

- a. Purchasing procedures are well designed and are followed unless otherwise directed by the purchasing director.
- b. Prenumbered blank purchase orders are secured within the purchasing department.
- c. Normal operational purchases fall in the range from US \$500 to US \$1,000 with two signatures required for purchases over US \$1,000.
- d. The purchasing agent invests in a publicly traded mutual fund that lists the stock of one of the organization's suppliers in its portfolio.

a. Correct. Management override of controls is considered to be a control weakness.

**60. An internal auditor is conducting an audit of the use of corporate credit cards. Which of the following are major audit concerns regarding the use of credit cards?**

- I. Segregation of duties is insufficient.
  - II. The purchasing function is impaired.
  - III. Cards may be used for personal benefit.
  - IV. The company is required to make one large payment instead of many small ones.
- a. I and III only.
  - b. II and IV only.
  - c. III only.
  - d. I, II, III, and IV.

I. Correct. Cardholders effectively approve and execute purchasing transactions. Therefore, there is a lack of segregation of duties.

III. Correct. In the absence of effective monitoring, cards could easily be used for personal benefit.

**61. Which of the following are true concerning responsibility for maintaining a sound system of internal control?**

- I. The board of directors are responsible for the company's system of internal control.
  - II. The role of management is to implement board policies on risk and control.
  - III. All employees have some responsibility for internal control as part of their accountability for achieving objectives.
  - IV. Internal auditing has the primary responsibility to establish and maintain the internal control system.
- a. I and II only.
  - b. I, II and III only.
  - c. II, III and IV only.
  - d. I, II, III and IV.

I. Correct. The board is ultimately responsible for the company's system of internal control.

II. Correct. The board delegates authority and responsibility to management to implement board policies on risk and control.

III. Correct. All employees do have some responsibility to make sure that controls are operating as they should.

**62. A control likely to prevent purchasing agents from favoring specific suppliers is**

- a. Requiring management's review of a monthly report of the totals spent by each buyer.
- b. Requiring buyers to adhere to detailed material specifications.
- c. Rotating buyer assignments periodically.
- d. Monitoring the number of orders placed by each buyer.

c. Correct. Periodic rotation of buyer assignments will limit the opportunity for any buyer to show favoritism to a particular supplier.

**63. The results of an audit of cash controls indicated that the bookkeeper signed expense checks and reconciled the checking account. If the cash account reconciliations were current and no cash shortages were found, an internal auditor should conclude that the system of internal controls over**

- a. Recording of cash receipts is adequate.
- b. Accounting for cash is inadequate.
- c. Reconciliations of the cash account are adequate.
- d. Physical safeguards of cash are adequate.

b. Correct. The bookkeeper should not sign the checks and reconcile the checking account. These functions should be segregated. Therefore, the accounting for cash is inadequate.

**64. Which of the following exemplifies an inherent limitation of internal control?**

- a. A controller makes and records cash deposits.
- b. A security guard allows a warehouse employee to remove company property from the premises without authorization.
- c. The company sells to customers on credit without proper credit approval.
- d. An employee who is unable to read is assigned custody of the company's tape library and run manuals.

b. Correct. This is an example of collusion, where the security guard let the employee steal company property. Collusion is an inherent limitation of internal control because no matter how tight controls are, if two or more people get together to circumvent the control, controls aren't going to work.

**65. Which of the following controls would help an organization from ordering quantities in excess of the organization's needs?**

- I. User department supervisor reviews all purchase requisitions prior to submitting them to the purchasing department.
  - II. Automatic reorder by the purchasing department when low inventory is indicated by the system.
  - III. A policy requiring the accounts payable department to match the receiving report with the vendor's invoice.
- a. I only.
  - b. I and II only.
  - c. I and III only.
  - d. I, II and III.

I. Correct. Supervisory review at the originating department level is one means of control over the number of items ordered.

**66. The receiving department maintains a purchase orders file. Purchase orders are kept in the file until goods are received. The main purpose of this control function is meant to ensure that**

- a. Received goods are released to the appropriate department in a timely manner.
- b. Only approved shipments are accepted.
- c. Goods are accurately counted upon receipt.
- d. Goods are not stolen or lost after receipt.

b. Correct. A shipment should be rejected if it is not documented by a purchase order in the open file.

**67. The cash receipts function should be separated from the related record-keeping function in an organization to**

- a. Physically safeguard the cash receipts.
- b. Establish accountability when cash is first received.
- c. Prevent paying cash disbursements from cash receipts.
- d. Minimize undetected misappropriations of cash receipts.

a. Correct. The purpose of separating the functions is to prevent theft of the cash receipts.

**68. Which of the following is an example of an effectiveness measure?**

- a. The rate of absenteeism.
- b. The goal of becoming a leading manufacturer.
- c. The number of insurance claims processed per day.
- d. The rate of customer complaints.

b. Correct. Effectiveness has to do with meeting goals.

**69. Budgets are generally classified as both planning documents and control devices. An important difference between the budget planning information needed and the budget control information needed is that planning information is more**

- a. Likely to be generated using external data.
- b. Detailed.
- c. Likely to be quantifiable.
- d. Likely to be more accurate.

a. Correct. Because planning is impacted more strongly by the organization's environment, the planning information is more likely to be generated using external data.

**70. Appropriate internal control for a multinational corporation's branch office that has a monetary transfer unit requires that**

- a. The individual who initiates wire transfers not reconcile the bank statement.
- b. The branch manager receives all wire transfers.
- c. Foreign currency rates are computed separately by two different employees.
- d. Corporate management approves the hiring of monetary transfer unit employees.

a. Correct. Independent reconciliation of bank accounts is necessary for good internal control.

**71. The following are steps in a typical control process.**

1) Select the times or points at which to collect information about the activities that are being measured and controlled.

2) Set the standards.

3) Observe the process, or collect the samples.

4) Report any significant deviations or problems.

5) Review and revise the standards.

6) Record the information that was collected.

7) Implement whatever corrections to the system or processes are necessary.

8) Evaluate if the performance is satisfactory.

What is the correct order of these steps?

a. 2, 1, 6, 3, 8, 7, 4, 5.

b. 1, 2, 3, 6, 5, 7, 8, 4.

c. 2, 1, 3, 6, 8, 4, 7, 5.

d. 1, 3, 2, 6, 7, 5, 8, 4.

The correct order is:

1. Set the standards.

2. Select the times or points.

3. Observe the process.

4. Record the information.

5. Compare and measure the results against the standard.

6. Evaluate if performance is satisfactory.

7. Report any significant deviations.

8. Implement whatever corrections are necessary.

9. Follow-up to see if the corrections are effective.

10. Review and revise the standards.

**72. A warehouse employee of a retail company was able to conceal the theft of items of inventory by entering adjustments to the computer-based perpetual inventory records indicating that the items had been damaged or lost. The control that would have prevented the adjustments from being recorded is**

- a. Including a check digit in the inventory part number.
- b. Requiring separate authorization for input of adjustment transactions.
- c. Including a parity check on the inventory part number.
- d. Providing an edit check for the validity of the inventory part number.

b. Correct. All adjusting transactions have to have proper segregation of duties. This means that the warehouse employee having custody of inventory should not have authority to initiate or process entries to the inventory records.

**73. Which of the following internal control procedures would minimize the misuse of corporate credit cards?**

- a. Establishing a restrictive policy regarding the issuance of the cards.
- b. Reviewing the continued need for each card periodically.
- c. Reconciling the company's monthly credit card statements with cardholder charge slips.
- d. Subjecting credit card charges to the same controls applied to other expenses.

d. Correct. Credit card expenses should be subjected to the same controls used in processing similar expense reports for currency. In this way, per diems and authorization limits would be reviewed.

**Use the following information to answer questions 74 and 75. The following information applies to an organization's project. The numbers in the table are the expected times (in days) to perform each activity in the project.**

Activity	Time (days)	Immediate Predecessor
AB	6	None
AC	5	None
BE	6	AB
CD	2	AC
CE	5	AC
DF	6	CD
EF	2	CE

**74. The expected time to complete the project is**

- a. 13 days.
- b. 11 days.
- c. 14 days.
- d. 18 days.

c. Correct. ABEF is the longest path (6 + 6 + 2). Therefore, this is the critical path.

**75. The process of adding resources to shorten selected activity times on the critical path in project scheduling is called**

- a. Crashing.
- b. The Delphi technique.
- c. ABC analysis.
- d. A branch-and-bound solution.

a. Correct. Crashing is the process of adding resources to shorten activity times on the critical path in project scheduling.

**76. A bank is designing an on-the-job training program for its branch managers. The bank would like to design the program so that participants can complete it as quickly as possible. The training program requires that certain activities be completed before others. For example, a participant cannot make credit loan decisions without first having obtained experience in the loan department. An appropriate scheduling technique for this training program is**

- a. PERT/CPM.
- b. Linear programming.
- c. Queuing theory.
- d. Sensitivity analysis.

a. Correct. PERT/CPM is a network technique for scheduling interrelated time series activities and identifying any critical paths in the series of activities. The critical path is the longest path through the network.

**77. A Gantt chart**

- a. Shows the critical path for a project.
- b. Is used for determining an optimal product mix.
- c. Shows only the activities along the critical path of a network.
- d. Does not necessarily show the critical path through a network.

d. Correct. A Gantt or bar chart is sometimes used in conjunction with PERT or CPM to show the progress of a special project. Time is shown on the horizontal axis, the length of a bar equals the length of an activity, and shading indicates the degree of completion. However, the Gantt chart is not as sophisticated as PERT or CPM in that it does not reflect the relationships among the activities or define a critical path.

**78. Customer checks are received on a daily basis. What controls should be in place to safeguard against theft of the checks.**

- a. Establishing a separate post office box for customer payments.
- b. Forwarding all checks to the cashier upon receipt.
- c. Requiring a specific mail clerk to list and endorse each check.
- d. Providing bonding protection for mail clerks.

c. Correct. Requiring an authorized mail clerk to list and endorse each check is the strongest control procedure.

**79. Which of the following activities performed by a payroll clerk is a control weakness rather than a control strength?**

- a. Has custody of check signature stamp machine.
- b. Prepares the payroll register.
- c. Forwards the payroll register to the chief accountant for approval.
- d. Draws the paychecks on a separate payroll checking account.

a. Correct. In this case there is a segregation of duties issue. The payroll clerk should not have custody of the check signature stamp.

**80. Which of the following observations made during a preliminary survey of a local department store's disbursement cycle reflects a control strength?**

- a. Individual department managers use prenumbered forms to order merchandize from vendors.
- b. The receiving department is given a copy of the purchase order complete with a description of goods, quantity ordered, and extended price for all merchandize ordered.
- c. The treasurer prepares checks/EFT for suppliers based on vouchers prepared by the accounts payable department.
- d. Individual department managers are responsible for the movement of merchandize from the receiving dock to storage or sales areas as appropriate.

c. Correct. This is control strength. The treasure should prepare checks/EFT based on vouchers prepared by the accounts payable department.

**81. Which of the following situations would cause an internal auditor to question the adequacy of controls over a purchasing function?**

- a. The original and one copy of the purchase order are mailed to the vendor. The copy on which the vendor acknowledges acceptance is returned to the purchasing department.
- b. Receiving reports are forwarded to purchasing where they are matched with the purchase orders and send to accounts payable.
- c. The accounts payable section prepares documentation for payments.
- d. Unpaid voucher files and perpetual inventory records are independently maintained.

b. Correct. This is a control weakness. The receiving reports are forwarded to accounts payable department, where they are matched the purchase order.

**82. Which of the following are elements of the control environment as described by COSO's internal control framework?**

- a. Commitment to competence, strategic planning, and management philosophy.
- b. Integrity and ethical values, assigning authority, and maintaining backup facilities.
- c. Risk assessment, monitoring, and organizational structure.
- d. Management's philosophy, organizational structure, and commitment to competence.

d. Correct. The control environment includes the attitude and actions of the board and management regarding the significance of control within the organization. According to COSO, the control environment includes the following seven elements:

- Integrity and ethical values.
- Commitment to competence.
- Human resource policies and practices.
- Assigning authority and responsibility.
- Management's philosophy and operating style.
- Board of directors or audit committee.
- Organizational structure.

**83. Which of the following best describes an auditor's responsibility after noting some indicators of fraud?**

- a. Expand activities to determine whether an investigation is warranted.
- b. Report the possibility of fraud to top management and ask how to proceed.
- c. Consult with external legal counsel to determine the course of action to be taken.
- d. Report the matter to the audit committee and request funding for outside specialists to help investigate the possible fraud.

a. Correct. If an internal auditor notes that there is a possibility of fraud, then the internal auditor needs to expand activities to determine whether an investigation is warranted.

**The following information is for questions 84 and 85.**

**The manager of a production line has the authority to order and receive replacement parts for all machinery that require periodic maintenance. The internal auditor received an anonymous tip that the manager ordered substantially more parts than were necessary from a family member in the parts supply business. The unneeded parts were never delivered. Instead, the manager processed receiving documents and charged the parts to machinery maintenance accounts. The payments for the undelivered parts were sent to the supplier, and the money was divided between the manager and the family member.**

**84. Which of the following internal controls would have most likely prevented this fraud from occurring?**

- a. Establishing predefined spending levels for all vendors during the bidding process.
- b. Segregating the receiving function from the authorization of parts purchases.
- c. Comparing the bill of lading for replacement parts to the approved purchase order.
- d. Using the company's inventory system to match quantities requested with quantities received.

b. Correct. Additional authorization would be the most likely choice in preventing the fraud.

**85. Which of the following tests would best assist the auditor in deciding whether to investigate this anonymous tip further?**

- a. Comparison of the current quarter's maintenance expense with prior-period activity.
- b. Physical inventory testing of replacement parts for existence and valuation.
- c. Analysis of repair parts charged to maintenance to review the reasonableness of the number of items replaced.
- d. Review of a test sample of parts invoices for proper authorization and receipt.

c. Correct. An analysis of repair parts charged to maintenance would quantify the excessive number of items and detect that abuse may be occurring.

**86. Which of the following fraudulent entries is most likely to be made to conceal the theft of an asset?**

- a. Debit expenses, and credit the asset.
- b. Debit the asset, and credit another asset account.
- c. Debit revenue, and credit the asset.
- d. Debit another asset account, and credit the asset.

a. Correct. Most fraud perpetrators would attempt to conceal their theft by charging it against an expense account.

**87. Which of the following would not be considered a condition that indicates a higher likelihood of fraud?**

- a. Management has delegated the authority to make purchases under a certain dollar limit to subordinates.
- b. An individual has held the same cash-handling job for an extended period without any rotation of duties.
- c. An individual handling marketable securities is responsible for making the purchases, recording the purchases, and reporting any discrepancies and gains/losses to senior management.
- d. The assignment of responsibility and accountability in the accounts receivable department is not clear.

a. Correct. This is an acceptable control procedure, which is aimed at limiting risk while promoting efficiency. It is not, by itself, considered a condition that indicates a higher likelihood of fraud (a red flag).

**88. Which of the following statements is (are) true regarding the prevention of fraud?**

- I. The primary means of preventing fraud is through internal control established and maintained by management.
  - II. Internal auditors are responsible for assisting in the prevention of fraud by examining and evaluating the adequacy of the internal control system.
  - III. Internal auditors should assess the operating effectiveness of fraud-related communication systems.
- a. I only.
  - b. II only.
  - c. I and II only.
  - d. I, II and III.

I. Correct. Fraud is best prevented when management establishes and maintains strong internal controls.  
II. Correct. Internal auditors are responsible for assisting management in the prevention and detection of fraud.  
III. Correct. Internal auditors should assess the operating effectiveness of fraud related communication systems.

**89. Internal auditors are more likely to detect fraud by developing and strengthening their ability to**

- a. Recognize and question changes that occur in organizations.
- b. Interrogate fraud perpetrators to discover why fraud was committed.
- c. Develop internal controls to prevent the occurrence of fraud.
- d. Document computerized operating system programs.

a. Correct. The responsibility of internal auditors for detecting fraud include having sufficient knowledge of fraud to be able to identify indicators that fraud may have been committed. Fraud may be indicated by negative organizational changes; thus, recognizing and questioning changes can help in the detection of fraud.

**90. Which of the following best describes a preliminary survey?**

- a. A standardized questionnaire used to obtain an understanding of management objectives.
- b. A statistical sample of key employee attitudes, skills, and knowledge.
- c. A "walk-through" of the financial control system to identify risks and the controls that can address those risks.
- d. A process used to become familiar with activities and risks in order to identify areas for engagement emphasis.

d. Correct. A preliminary survey is used to become familiar with the activities, risks and controls; to identify areas for engagement emphasis; and to invite comments and suggestions from engagement clients (PA 2210.A1-1.3). A preliminary survey might include the use of standard questionnaires, statistical sampling, and a walk-through.

**91. During a preliminary survey of the accounts receivable function, an internal auditor discovered a potentially major control deficiency while preparing a flowchart. What immediate action should the internal auditor take regarding the weakness?**

- a. Perform sufficient testing to determine its cause and effect.
- b. Report it to the level of management responsible for corrective action.
- c. Schedule a separate engagement to evaluate that segment of the accounts receivable function.
- d. Highlight the weakness to ensure that procedures to test it are included in the engagement work program.

d. Correct. The internal auditor would highlight the weakness to ensure that procedures to test it are included in the engagement work program.

**92. Which of the following would not aid in the effectiveness of the preliminary survey?**

- a. Read all relevant background information.
- b. Identify the risk implicit in the areas under review.
- c. Identify people who could provide additional and needed information.
- d. Review the adequacy and effectiveness of controls.

d. Correct. Reviewing the adequacy and effectiveness of controls is part of the fieldwork, which is done after the planning stage.

**93. Which of the following procedures is the least effective in gathering information about the nature of the processing and potential problems?**

- a. Interview supervisors in the claims department to find out more about the procedures used, and the rationale for the procedures, and obtain their observations about the nature and efficiency of processing.
- b. Send an electronic mail message to all clerical personnel detailing the alleged problems and request them to respond.
- c. Interview selected clerical employees in the claims department to find out more about the procedures used, and the rationale for the procedures, and obtain their observations about the nature and efficiency of processing.
- d. Distribute a questionnaire to gain a greater understanding of the responsibilities for claims processing and the control procedures utilized.

b. Correct. Sending emails to clerical staff is the least effective method of gathering information. Emails are impersonal and the clerical staff might take offense to the alleged inefficiencies. Thus, the responses back might not be as truthful had another method been used.

**94. Many organizations use electronic funds transfer (EFT) to pay their vendors instead of issuing a check. Regarding the risks associated with issuing checks, which of the following risk management techniques does this represent?**

- a. Controlling.
- b. Accepting.
- c. Transferring.
- d. Avoiding.

d. Correct. Risk responses include avoidance, acceptance, transferring and reduction (TARA). By eliminating checks, the organization avoids all risk associated with them.

**95. Risk appetite is the level of risk an organization is willing to pursue or retain or take. Factors that could influence an organization's risk appetite might include**

- Viewpoints of the major stakeholders.
- The complexity of the organization's accounting system.
- External factors, such as changing economic considerations, changes in technology, changes in the industry, etc.
- All of the above.

d. Correct. The following are factors which could influence an organization's risk appetite, including:

- The viewpoints of the major stakeholders, including the views of the company's major shareholders, bondholders, lenders, analyst and many others. Each stakeholder might have a different opinion as to how much risk a company should take on.
- Accounting factors, such as the volume of transactions, the complexity of the accounting system, changing rules and regulations.
- The opportunity for fraud to be committed.
- External factors, such as changing economic considerations, changes in industry, changes in technology, etc.
- Governmental restrictions.
- Entity-level factors, such as the quality and quantity of hired personnel, quality for training courses, changes in key personnel, etc.

**96. In internal auditing sampling applications, there are four types of errors that may occur. These four errors are divided into two categories of risks. These risks**

- Result directly from the chance that the sample obtained by the internal auditor is unrepresentative of the population.
- Can be decreased by using more reliable, albeit more expensive, audit procedures.
- Have a magnitude based only on the economic consequences of incorrect sample-based conclusions.
- Refer respectively to the risks that (1) internal controls will fail, and (2) the resultant error will go undetected.

a. Correct. Sampling risk is the risk that the sample will not be representative of the population. Alpha and Beta risk are types of risks inherent in the practice of sampling. Alpha risk will cause the auditor to do additional and unnecessary work in coming to the correct conclusion. This makes the audit less efficient. Beta risk will cause the auditor to come to the wrong conclusion. This reduces audit effectiveness.

97. An auditor is conducting a survey of perceptions and beliefs of employees concerning an organization's health-care plan. The best approach to selecting a sample would be to

- Focus on people who are likely to respond so that a larger sample can be obtained.
- Focus on managers and supervisors because they can also reflect the opinions of the people in their departments.
- Use stratified sampling where the strata are defined by marital and family status, age, and salaried/hourly status.
- Use monetary-unit sampling according to employee salaries.

c. Correct. Because different employees probably have different situations, needs, and experiences, stratified sampling would best ensure that a representative sample would result.

The following information is for questions 98 and 99.

An internal auditor works for a car rental agency that operates a fleet of 75,000 vehicles in 1,000 cities throughout North America. As a part of an operational audit, the auditor tested the impact of vehicle age on the incidence of major repairs. A computer program showed that 20% of the fleet has been in service for more than 12 months. A sample of 375 is drawn based on:

- Confidence level = 95%
- Expected rate of occurrence = 10%
- Precision =  $\pm 3\%$

**98. If 30 of the vehicles tested had received major repairs after being in service for more than 12 months, which is the sample rate of occurrence?**

- 8%.
- 0.2%.
- 2.5%
- 20%.

a. Correct. The sample rate of occurrence is the proportion of items in a population that has a certain characteristic or attribute of interest. The sample rate of occurrence is calculated by dividing the number of items with major repairs by the sample population ( $30 \div 375$ ). Therefore, the rate of occurrence is 8%.

**99. Assuming that all other factors remain constant, how would sample size and achieved precision be affected by a change in confidence level from 95% to 99%?**

- a. Sample size would be smaller; achieved precision would be larger.
- b. Both sample size and achieved precision would be larger.
- c. Both sample size and achieved precision would be smaller.
- d. Sample size would be larger; achieved precision would be smaller.

d. Correct. Because the confidence coefficient is a numerator, increasing the confidence coefficient from 95% up to 99% will make the numerator value larger, thereby, sample size is larger. Also, since sample size is a denominator when calculating precision, a smaller precision would result from using a larger sample.

**100. An auditor applying a discovery-sampling plan with a 5% risk of overreliance may conclude that there is a. A 95% probability that the actual rate of occurrence in the population is less than the critical rate if only one exception is found.**

- b. A 95% probability that the actual rate of occurrence in the population is less than the critical rate if no exceptions are found.
- c. A 95% probability that the actual rate of occurrence in the population is less than the critical rate if the occurrence rate in the sample is less than the critical rate.
- d. Greater than a 95% probability that the actual rate of occurrence in the population is less than the critical rate if no exceptions are found.

b. Correct. Discovery sampling is when the auditor is looking for that one critical error or irregularity. If no exceptions are found, the correct conclusion is that the occurrence rate is less than the critical rate.