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Conversion of the uniform CPA examination to computer-based examination, October 1998

Joint AICPA/NASBA Computerization Implementations Committee

American Institute of Certified Public Accountants

National Association of State Boards of Accountancy

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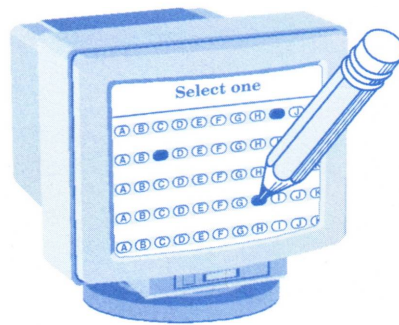
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Briefing Paper No. 1

Conversion of the Uniform CPA Examination to a Computer-Based Examination

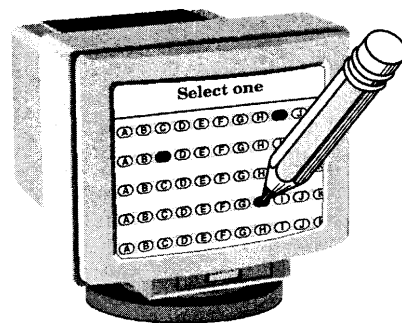


October 1998

Prepared by the Joint AICPA/NASBA
Computerization Implementation Committee

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PART 1

INTRODUCTION

Overview

The Uniform CPA Examination has a long and trusted history in the licensing of Certified Public Accountants (see Appendix A for details). To move forward with that track record and to incorporate advances available only in a technological environment, a group of individuals representing organizations currently involved in writing, grading, administering, and evaluating the examination have come together to create a model for a computer-based examination.

Comprised of members from the National Association of State Boards of Accountancy (NASBA) and the American Institute of Certified Public Accountants (AICPA), the Joint AICPA/NASBA Computerization Implementation Committee (CIC) has been charged with formulating a computer-based examination; eliciting advice and feedback on the technological and administrative viability of the proposed examination; testing a computerized model; and moving towards implementation of a computer-based examination by the year 2003.

Our Goals for the Examination

The vision of the CIC is to develop and implement a computer-based Uniform CPA Examination that will continue to assure protection of the public by providing a better mechanism for screening CPA candidates for entry-level competencies.

To this end, the Committee's goals are to provide a computer-based examination that will:

- *Provide reasonable assurance that candidates with the required knowledge and skills to protect the public continue to pass the Examination, and those without the required knowledge and skills do not pass the Examination.*
- *Provide reasonable assurance that successful candidates have the knowledge and skills needed to perform in the current business environment.*

The ongoing adherence to these goals will require changes in both the content and format of the current Uniform CPA Examination, the specifics of which will be discussed in detail throughout this *Briefing Paper*.

The Need for a Computer-Based Examination

The world is already technologically driven and will become even more so in the next century. Personal computers, e-mail, the Internet, and teleconferencing make it possible to transact business anywhere, anytime. Historic information is available not in days, not in hours, but with the click of a mouse. The business environment is becoming more complex, more demanding, more immediate, more global, and more knowledge-driven.

Key to the accountancy profession is the effects of these changes on the audit function. The emergence of technology has changed both the "what" (audit trail of financial information) and the "how" (audit tools) of the traditional audit. With the disappearance of paper records, it is no longer possible for CPAs to audit "around the computer" for some entities.

Consequently, the many arguments for a computer-based examination include:

- Testing an expanded range of knowledge and skills that more closely reflects the current practice environment (e.g., research skills in an electronic environment).

- Gathering more information about candidates and determining if there is bias towards any group of candidates.
- Measuring candidate performance more effectively on a question-by-question basis.
- Allowing questions to be more readily added, modified, or deleted.
- Reducing subjectivity in grading.
- Allowing candidates greater flexibility in sitting for the examination by offering the examination more frequently.

An Interactive Process

This *Briefing Paper* is intended as an update and a synopsis of our efforts to date. The following pages offer a look at the proposed components of the computerized examination and its potential structure.

Nothing in this Briefing Paper is set in stone. It is a synopsis of what at this point seems to be an ideal examination. Changes are invited, anticipated, and inevitable. Throughout the process of converting to a computer-based examination, the input of various interested parties will be crucial in ensuring that *the examination continues to do first and foremost what it has always done: protect the public interest.*

PART 2

THE PROPOSAL FOR THE COMPUTERIZED UNIFORM CPA EXAMINATION

Developing a Computerized Examination Model

The CIC began its work by defining the “ideal examination” after evaluating information obtained from the Boards of Accountancy and other parties (see Appendix B), holding discussions with organizations that develop computer-based examinations, and investigating other computerized examinations. Based on these processes and the information obtained, the CIC has made the tentative and preliminary decisions described below.

The proposed structure of the computer-based Uniform CPA Examination is a two-section examination. The first section (“fundamentals of knowledge”) would primarily test the basic *knowledge* needed by entry-level CPAs using multiple-choice questions; the second (“performance assessment”) would emphasize assessing the *skills* needed by entry-level CPAs using computer simulations. The content of each section would be clearly defined in the content specification materials for the Uniform CPA Examination provided to candidates.

Each section would serve to protect the public interest by evaluating whether candidates demonstrate a sufficient degree of the requisite knowledge and skills needed to become entry-level CPAs.

Section 1: Fundamentals of Knowledge

This section is presently envisioned as an all-objective, multiple-choice examination using a computer-mastery test. Computer-mastery testing aims at determining “masters” (those who should pass) and “nonmasters” (those who should not pass).

In this testing environment, questions are administered in groups known as *testlets*. Each testlet might comprise, for example, 25 to 30 questions and would cover a sample of the content specification outline (see Appendix C for an example of the possible content specifications of the testlets). Candidates would first be given a base test composed of multiple testlets that are selected at random from a pool of testlets. The base test would include pretest items. Based on our experience with the paper-and-pencil examination, we estimate that the base test would be completed in a morning testing session.

After the base test is administered, the computer would make a determination for each candidate as follows:

- Pass—Candidate has demonstrated mastery of the content;
- Fail—Candidate has demonstrated nonmastery of the content;
- Indeterminate—Candidate has not clearly demonstrated mastery or nonmastery.

If the candidate’s status is “pass” or “fail,” testing would end for this section. Candidates would be notified at the end of the morning session whether they need to come back for the afternoon session. If the candidate’s status is “indeterminate,” an additional testlet would be administered to obtain more information about the candidate’s level of knowledge, after which the candidate’s “pass/fail/indeterminate” status would be reassessed. Additional testlets, up to a maximum, would be administered during the afternoon session, until a pass or fail determination could be made for the candidate. Candidates would be assigned a score based on all the testlets administered to them.

Section 2: Performance Assessment

An ideal examination would include a second section, “Performance Assessments,” which would consist of a series of free-response scenarios/questions in which a candidate is provided with a situation and is required to

address a number of open-ended items involving accounting, auditing, tax, and other business issues. Performance assessments would more closely replicate the work actually performed by entry-level CPAs. Thus, by assessing a candidate's abilities to perform tasks in a manner that more closely resembles the work an entry-level CPA performs, protection of the public increases. The skills assessed in this section could be expected to include research skills, analytical reasoning, critical thinking, communication skills, and the ability to use electronic technology.

This section of the computer-based examination likely would last a full day (six to eight hours) and require each candidate to complete four simulations, with each accounting for 25% of the candidate's grade. Although the content for this section is not yet fully specified, it likely would include:

- Knowledge of and ability to apply generally accepted accounting principles (GAAP) to prepare financial reports.
- Knowledge of and ability to apply generally accepted auditing standards (GAAS) to audit financial statements.
- Ability to prepare and evaluate auditors' reports.
- Ability to develop effective audit procedures in an information technology environment.
- Ability to use financial and economic data to provide information for business decisions and to audit effectively.
- Ability to apply general business knowledge to evaluate situations and make recommendations and decisions.
- Knowledge of and ability to apply the income tax laws and regulations in various tax compliance and planning situations.

Appendix D presents two sample simulations. The first is presented in storyboard fashion, and the second in a narrative mode. The simulations actually included on the examination would be lengthier and more detailed than these examples.

Content

Relevant content is the single most critical component of the Uniform CPA Examination in both its current paper-and-pencil format and in the proposed computer-based model. In 1996, the AICPA Board of Examiners formed the Examination Content Oversight Task Force (COTF) "to provide reasonable assurance that the content of the Uniform CPA Examination reflects the knowledge and skills needed by entry-level CPAs to practice competently." This mission includes:

- Revising and updating the Examination's content specifications.
- Developing (and implementing) a process to keep the content specifications current.

In addition, the COTF was charged to obtain information and comments from Boards of Accountancy and other interested parties regarding the knowledge and skills that should be assessed on the Examination.

The COTF is composed of 10 members with diverse backgrounds as CPAs, who are predominately practitioners, with one academic and one representative of the NASBA Examinations Committee.

As part of revising and updating the content specifications, the COTF is currently focusing on the following:

- Identification of the skills necessary to protect the public interest, such as:
 - Analytical skills
 - Communication skills
 - Organizational skills
 - Research skills
 - Ability to recall information

- Increased testing of:
 - General business knowledge
 - Information technology

As the COTF revises the content of the Examination, the CIC will of course make full use of its findings and recommendations as the CIC moves forward to create a computer-based examination.

Feasibility Study

In late August, a "Request for Proposal" was issued to procure the services of a consultant to conduct a feasibility study on all aspects of the development and administration of the "ideal" examination. The selected consultant will be asked to determine the feasibility of the proposed model from the perspectives of time, cost, and technical implementation. If the "ideal" examination proves not to be feasible, the consultant is charged with providing viable alternatives. The feasibility study is expected to be completed by early 1999 and the findings of that study will be shared with key stakeholders in the Uniform CPA Examination process.

PART 3

FEATURES OF A TWO-PART COMPUTERIZED EXAMINATION

Non-Hierarchical Structure

The two examination sections would not depend on each other, resulting in an examination that is not hierarchical. Despite a slight preference for a hierarchical structure by the respondents to the *Invitation to Comment*, the CIC observed that a non-hierarchical examination would provide the candidates with optimum flexibility. Consequently, candidates who qualify to sit for the computerized examination would do so by making an appointment for each section at a computerized learning center. The examination sections could be taken in the order that the candidate preferred, and the sections could be, but would not have to be, taken on consecutive days.

In addition, a non-hierarchical structure would make the examination easier for Boards of Accountancy to administer.

Pass/Fail

Based on input received, the CIC has tentatively concluded that a pass/fail grading methodology should be used for the computerized Uniform CPA Examination. That position is based on the basic purpose of the examination and on practicalities. The computer will administer different numbers of multiple-choice questions to different candidates, depending on the individual's mastery. Assigning numerical grades would be meaningless under this structure. Also, a licensure examination should be designed to focus on whether candidates possess the level of technical knowledge and skills necessary for entry-level licensees—not on their exact scores. Pass/fail grade reporting is consistent with that design. The CIC will study the feasibility of developing a Candidate Diagnostic Report to provide candidates with information regarding their performance on the various content areas covered on the examination.

Grade Reporting

The computer would grade each section independently, i.e., a candidate passing one section would not be required to pass the other section at the same time. The computer would then transmit the grade (pass or fail) directly to the appropriate board of accountancy. The board of accountancy would inform the candidate of his or her grade.

Frequency of Delivery

One of the many benefits of computer-based testing is that the examination can be offered by appointment rather than just twice a year as with the current paper-and-pencil examination. This flexibility allows a candidate to take the examination when he or she is ready. After the research regarding the technological feasibility of the proposed structure, decisions will need to be made regarding the frequency with which the examination may be offered (e.g., all year long, two weeks per month).

Conditioning

Historically, the Boards of Accountancy have established conditioning and retake policies—not all of which are the same, which has presented problems to Boards of Accountancy, CPAs, and candidates. The proposed two-section computerized examination eliminates the need for many of these conditioning requirements.

The only conditioning requirement that should be necessary is that a candidate who passes one section of the examination would receive credit for it regardless of whether the candidate takes the other section or how the candidate does on it. The current requirement in most states to obtain a minimum score on sections failed to obtain credit for sections passed would not apply to the computerized examination because the two sections would be graded on a pass/fail basis.

Decisions will have to be made regarding how often a candidate may retake a failed section (e.g., every thirty days, every six months), and how long credit for one section may be retained until the other section is passed (e.g., three years). The CIC will recommend retake policies at a later date based upon input received from the State Boards and the results of the research regarding the technological feasibility.

The CIC acknowledges that each individual Board of Accountancy establishes its own conditioning and retake rules and that the CIC's tentative conclusions are advisory.

CURRENT AND IDEAL EXAMINATIONS: A COMPARISON

Feature	Current Uniform CPA Examination	Ideal Computerized Uniform CPA Examination
<i>Number of Sections</i>	Four sections	Two sections
<i>Criteria for Grading</i>	75% required on each section	Pass/Fail for each section
<i>Structure</i>	Non-Hierarchical	Non-Hierarchical
<i>Types of Questions</i>	Multiple-Choice, Other Objective Answer Format, and Essay/Problem	Multiple-Choice and Simulation
<i>Test Frequency</i>	Twice a year: May & Nov.	By appointment (appointment period and frequency to be determined)
<i>Length of Examination</i>	2 days—back-to-back	2 days—each section scheduled separately; may be back-to-back
<i>Reporting of Grades</i>	Approximately 90 days after Examination has been given	Potentially more quickly— exact timing to be determined

PART 4

EVIDENCE SUPPORTING A COMPUTER-BASED UNIFORM CPA EXAMINATION

Evidence Supporting Change to a *Computerized* Examination

In 1995, the Board of Examiners (BOE) began researching the possibility of converting the examination to a computer-based test. The responses to the BOE's *Invitation to Comment—Conversion of the Uniform CPA Examination to a Computer Based Examination* indicated that:

- 73% of the Boards of Accountancy favored conversion.
- 24% were unsure.
- 4% did not favor conversion.

Supported by the responses of the Boards of Accountancy and other interested parties, the CIC is now preparing for a computer-based Uniform CPA Examination.

Evidence Supporting Change to a *Two-Part* Examination

Five key factors indicate both the desirability and acceptability of changing from the current four-section examination to the proposed two-part examination:

First, the current structure limits the extent to which the knowledge and skills from separate sections can be integrated. Although the four-section structure provides reasonable assurance that candidates demonstrate competence in each section, questions involving the integration of information *across* sections do not easily fit within the current structure.

Second, changes within the accounting profession in recent years, and expected changes in the near future, suggest that the current four-section structure may not be the optimal structure for assessing the changing competency requirements of entry-level CPAs. These changes indicate that, to protect the public, accountants will need certain knowledge and skills that have not traditionally been needed (e.g., information technology), and that some of the traditional knowledge and skills have diminished, relatively, in importance (e.g., business law). These changes also suggest that entry-level CPAs will need to integrate their knowledge and skills to a greater degree than currently is assessed by the examination. The proposed two-part examination will provide the developers of the examination with greater flexibility in adapting the examination to changes in the requisite knowledge and skills.

Third, there is the issue of *face validity*: “how valid” the examination *appears* to members of Boards of Accountancy, current members of the profession, candidates, and the public. If the Uniform CPA Examination is to retain strong support from these constituencies, they must believe, based on the appearance of the examination, that it is adequate for making decisions on licensure for CPAs. Unless the examination's structure and content reflect the broad-based integrated knowledge and skills necessary for the practice of accounting, these groups may no longer have confidence in the examination for making licensing decisions.

Fourth, psychometric studies¹ currently being conducted are providing preliminary evidence that the current four-section examination structure may not reflect the underlying *dimensionality* of the examination. When investigating the dimensionality of an examination, the relationships among candidates' performances on all examination sections are evaluated. If candidates' performances on each examination section are not closely

¹ The AICPA is sponsoring several psychometric studies that are addressing the dimensionality of the current examination. These studies will be released to the boards of accountancy upon completion and review by the CIC, the COTF, and the Board of Examiners.

related to their performances on the other sections, the sections should remain independent. However, preliminary results from the psychometric studies show a strong correlation in candidates' performances across test sections, indicating that four distinct sections may be superfluous. The evidence indicates that the sections could be combined without negatively affecting the validity of the examination results.

Fifth, responses to *Invitation to Comment—Conversion of the Uniform CPA Examination to a Computer Based Examination* suggest that changing the current four-section structure would be acceptable. The respondents looked favorably upon a structure other than the current four-section structure. These results suggest that, within the context of computerization, the Boards of Accountancy and other interested parties would accept a structure other than the traditional four-section examination.

In addition, in responding to the Comment Form included in the *Invitation to Comment*, many respondents indicated a desire to assess candidates' critical thinking and other higher-level cognitive skills. Inclusion of performance assessment-type questions in the computer-based examination would permit this.

Based on this input, the CIC reached a tentative conclusion that a two-section examination would be ideal. One section would primarily test whether candidates demonstrate a sufficient degree of the requisite *knowledge* needed by entry-level CPAs, while the other section would emphasize assessing the *skills* needed by entry-level CPAs. Multiple-choice questions, generally used to cover a broad range of subject matter, would be used on the knowledge section of the computerized examination, whereas computer-administered simulations would be used on the other section. (See Pages 3–9 of this *Briefing Paper* for details.)

CONCLUSION

The CIC believes that a computer-based Uniform CPA Examination, with advancements achievable only in a technological environment, is an important step in the continued protection of the public interest. While many changes to the format and content are proposed, the examination will continue to cover much of the knowledge and skills that have always been tested.

The CIC feels that, based on its work to date, the structure proposed in this *Briefing Paper* provides the best level of public protection by focusing *both* on what entry-level CPAs need to know and on what they need to be able to do. This structure uses computerization effectively and provides the flexibility of accommodating future changes to the content of the examination without affecting the structure.

The Committee will also take the following steps to ensure the involvement of and input from all interested parties throughout the process of creating and implementing a computer-based Uniform CPA Examination:

- Incorporate the work of the COTF regarding an expanded range of knowledge and skills that more closely emulate the current practice environment.
- Define, along with the COTF, the structure of the examination.
- Develop a structure for the computerized examination that gains the acceptance of the Boards of Accountancy, NASBA, the AICPA, and other interested parties.
- Ensure that all legal and statutory issues have been resolved for its adoption.
- Develop a means to deliver a computerized examination and seek evaluation and feedback.
- Implement the computerized examination and seek evaluation and feedback.
- Evaluate and report on the initial administration of the computerized examination.
- Hand off evaluation and feedback to another responsible group following the creation and initial administration of a viable computer-based Uniform CPA Examination.

The CIC fully understands that the development and implementation of a truly viable computer-based examination cannot be achieved in a vacuum. Consequently, it has sought advice, comment, and direction from a variety of interested parties, including state regulators, state CPA societies, and educators. Through this *Briefing Paper* and other documents, the Committee will continue to seek input from those affected by the computerization of the Examination.

The CIC welcomes your advice and continued support as together we work towards a computerized Uniform CPA Examination by the year 2003.

APPENDIX A

THE UNIFORM CPA EXAMINATION

Background

Examinations to test the qualifications of public accountants were first used in New York State in 1896. As the country and profession grew, more states enacted accountancy laws that required individuals to pass an examination to qualify as certified public accountants. The American Institute of Certified Public Accountants (AICPA) has offered the Uniform CPA Examination as a tool for licensing CPAs since 1917. By the 1960s, all jurisdictions in the United States required new CPAs to have passed the Uniform CPA Examination prepared by the AICPA and graded by its Advisory Grading Service.

The current Uniform CPA Examination is delivered to candidates through agreements between the Boards of Accountancy and the accounting profession, represented by the AICPA. The Boards of Accountancy make licensure decisions based on two factors: (1) results of the Examination and (2) the fulfillment of educational and experience requirements, as applicable. The Boards also validate candidates' credentials, contract for administration of the Examination, and evaluate the advisory grades received from the AICPA. The AICPA develops and grades the Examination. The current examination is the primary tool in all 54 jurisdictions for assessing the qualifications of CPA candidates.

Objective of the Uniform CPA Examination

The objective of the Uniform CPA Examination is to provide reasonable assurance to Boards of Accountancy that candidates passing the Examination possess the level of technical knowledge, skills, and abilities necessary for initial licensure to protect the public interest.²

The Examination ensures that CPAs entering the profession have met appropriate minimum requirements and that they have passed an examination that has uniform content coverage, difficulty, and grading methodology.

Current Examination Structure and Format

The current Uniform CPA Examination is a two-day, paper-and-pencil linear examination where candidates receive questions in a predetermined sequence and record their answers manually on paper answer sheets. The Examination is offered semi-annually in May and November to thousands of CPA candidates. In 1997, over 120,000 candidates sat for the Examination.

The Examination covers four sections: Auditing; Financial Accounting & Reporting; Accounting & Reporting—Taxation, Managerial, and Governmental and Not-for-Profit Organizations; and Business Law & Professional Responsibilities. The Examination consists of both objective and essay questions and problems.

As of May 1996, the examination became nondisclosed, meaning that candidates were no longer allowed to retain or receive their question booklets after the Examination or to reveal questions on the Examination in any manner. All candidates taking the Examination agree to comply with this policy under penalty of possible invalidation of their grades or disqualification from future Examinations.

² *The Board of Examiners Uniform CPA Examination Annual Report* (AICPA, 1998), p. 17.

Grading

Each section of the Uniform CPA Examination is graded separately. All grades are reported to Boards of Accountancy on a scale ranging from 0 to 100, with a minimum grade of 75 required to pass each section. Conditional status may be granted to those candidates who receive a passing grade on at least two sections, with many Boards of Accountancy granting conditional status only if a candidate achieves a minimum grade on the sections failed.

Candidates receiving conditional status are generally allowed a limited number of additional opportunities to pass the remaining sections. If conditional credit lapses, candidates must be reexamined in all sections.

Grade Reporting

All 54 Boards of Accountancy mail grades approximately 90 days after the Examination is administered. This day is referred to as the Uniform Mailing Date. Boards of Accountancy may include with the candidate's grades information on how the candidate performed on each content area of the Examination and/or a Candidate Diagnostic Report, which may be helpful if a candidate must retake one or more sections.

APPENDIX B

BIBLIOGRAPHY

The structure and content of the computerized Uniform CPA Examination, as described in this report, are based on the following works:

- Computerization Task Force (1994–1997):
 - *Invitation to Comment—Conversion of the Uniform CPA Examination to a Computer Based Examination* (AICPA, Board of Examiners, September 1995).
 - *Status Report—Conversion of the Uniform CPA Examination to a Computer Based Examination* (AICPA, Board of Examiners, June 1997).
- Examination Content Oversight Task Force (1996–current):
 - *Invitation to Comment—Updating the Uniform CPA Examination Content Specifications* (AICPA, Board of Examiners, January 1997).
 - *Status Report—Updating the Uniform CPA Examination Content Specifications* (AICPA, Board of Examiners, November 1997).
- Practice Analysis Task Forces (1981–1983 and 1988–1991):
 - *Report of the Practice Analysis Task Force* (AICPA, Board of Examiners Practice Analysis Task Force, September 1983).
 - *Practice Analysis of the Certified Public Accountants in Public Accounting* (AICPA, Professional Examination Services, May 1991).

APPENDIX C

SAMPLE TESTLET

This example demonstrates how a testlet may be structured on a computerized Uniform CPA Examination.

Content Topic	Estimated Percentage
Assurance	30%
—Planning	
—Evidence	
—Report and review	
Professional responsibilities	4%
Financial accounting	30%
Governmental and not-for-profit accounting	6%
Taxation	14%
General business knowledge	16%
—Managerial accounting	
—Business law	
—Information technology	
—Other (finance, economics, etc.)	
Total content	100%

Appendix D

SIMULATION EXAMPLES

The following tools will be provided for all simulations:

Authoritative literature:

Financial Accounting and Reporting:

Financial Accounting Standards Board (FASB) Statements of Financial Accounting Standards and Interpretations

Accounting Principles Board Opinions

AICPA Accounting Research Bulletins

FASB Technical Bulletins

AICPA Statement on Auditing Standards No. 69, “The Meaning of *Present Fairly in Conformity With Generally Accepted Accounting Principles* in the Independent Auditor’s Report,” and Statement on Auditing Standards No. 62, “Special Reports”

AICPA Practice Bulletins

Emerging Issues Task Force: Abstracts

FASB Statements of Financial Accounting Concepts

AICPA Statements of Position

Auditing:

AICPA Statements on Auditing Standards

AICPA Statements on Standards for Accounting and Review Services

AICPA Statements on Quality Control Standards

AICPA Statements on Standards for Attestation Engagements

AICPA Accounting and Audit Guides

Tax:

Internal Revenue Code and Income Tax Regulations

Internal Revenue Service Circular 230

AICPA Statements on Responsibilities in Tax Practice

Business Law & Professional Responsibilities:

AICPA *Code of Professional Conduct*

AICPA Statement on Standards for Consulting Services

AICPA Statements on Responsibilities in Personal Financial Planning Practice

Uniform Commercial Code

Federal Bankruptcy Act (Statutes)

Uniform Partnership Act

Revised Model Business Corporation Act

Computational tools:

Spreadsheet program

Calculator

Present value tables

SIMULATION NO. 1
STORYBOARD FORMAT
ACCOUNTS RECEIVABLE SIMULATION

Objective

To test the candidate's ability to:

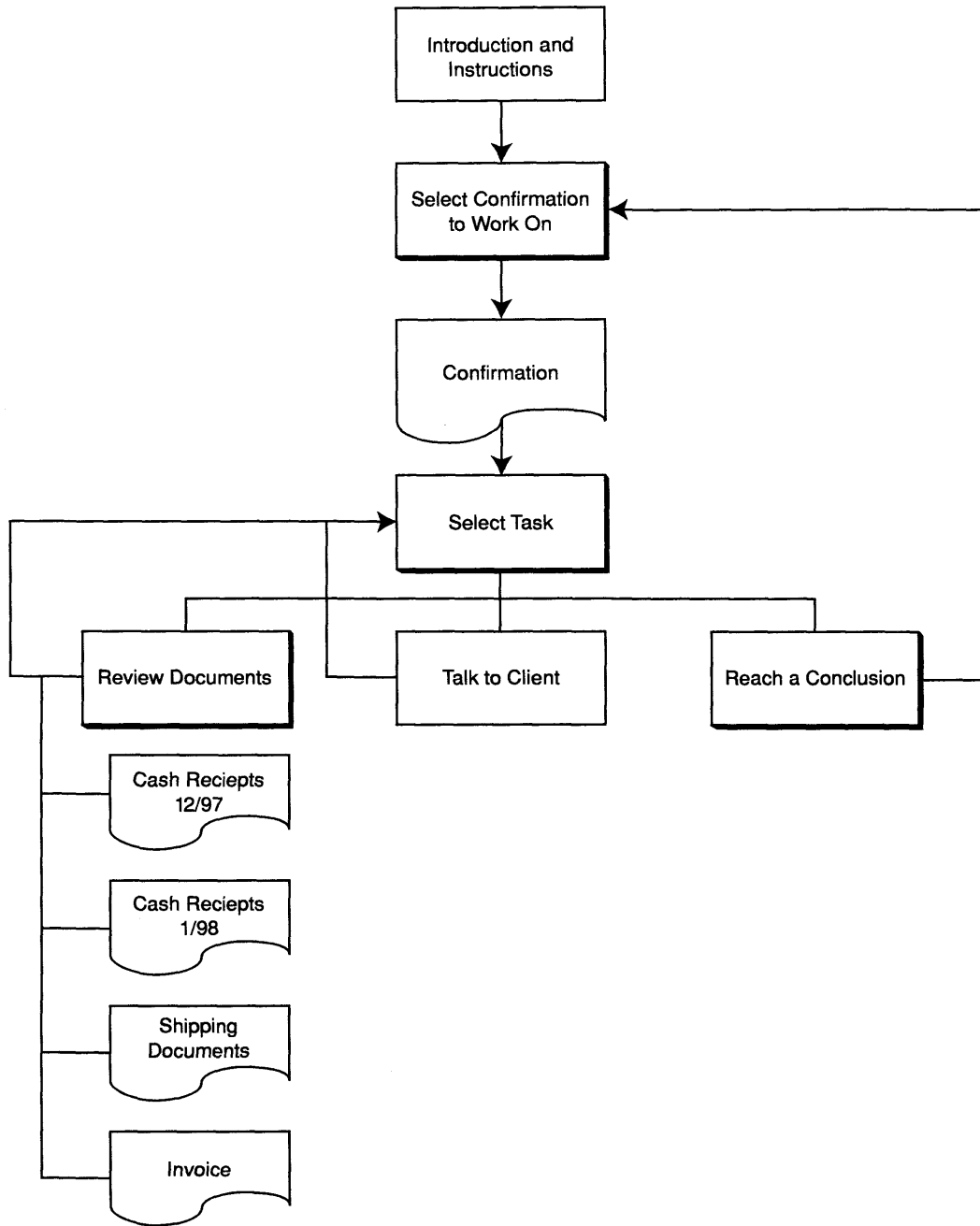
- Evaluate the relevance and relative strength of various types of audit evidence.
- Reach a proper audit conclusion regarding accounts receivable confirmation exceptions, given a variety of supporting documents.

Synopsis

After a brief series of screens that introduce the problem and provide instructions for completing the exercise, the candidate is presented with eight accounts receivable confirmation requests that have been returned by the client's customers. Each confirmation request has an "exception" noted by the customer, and the candidate must research and clear these exceptions. For each confirmation request, the candidate can choose from among five different sources of audit evidence (for example, make inquiries of client personnel, review the cash receipts journal, etc.). After reviewing the chosen supporting evidence, the candidate must then conclude either (a) no exception exists (the accounts receivable balance is fairly stated), or (b) the client's accounts receivable trial balance is in error and must be adjusted. If the candidate determines an adjustment is required, he or she must then prepare the adjusting entry. The candidate may be asked to justify his or her conclusion, depending on the audit evidence used and conclusion reached.

The candidate is required to document both the conclusion reached (including any adjusting entry) and the audit evidence used to reach the conclusion.

Organization of Material



Note: A rectangle set on a shadow indicates that this is a point where the candidate can make a choice. Additional documents are listed on page 27.

Script

Introduction and Instructions

Screen #1

Miller, CPA has been engaged to audit the financial statements of Superior Wholesaling for the year ended December 31, 1997. Miller obtained and documented an understanding of Superior's internal control relating to accounts receivable and assessed control risk relating to accounts receivable at the maximum level.

You are the staff accountant assigned to the engagement, auditing the accounts receivable area. To date, you have:

- Requested and obtained from Superior an aged accounts receivable schedule listing the total amount owed by each customer as of December 31, 1997.
- Sent positive confirmation requests to a sample of customers on January 15, 1998.
- Received from your client's customers eight replies to the confirmation requests that may be considered "exceptions."

Treatment: actions/interactions/effects

Candidate reads text. Each screen in this simulation has five navigational buttons:

- Review instructions (returns to screen #2)
- Review confirmation request exception worksheet
- Select another reply to a confirmation request for testing (Screen #8)
- Access authoritative literature
- Next screen

On this screen, only the "next screen" button is active.

Screen #2

You have received from your client's customers eight replies to the confirmation requests that may be considered "exceptions." Your job is to review these replies, obtain audit evidence relating to the potential "exceptions," and reach a conclusion for each.

Treatment: actions/interactions/effects

Candidate reads text. Only the "next screen" button is active.

Screen #3

Required. For each reply, the following documents are available for your use:

- Cash receipts journal, December 1997
- Cash receipts journal, January 1998
- Cash receipts documents
- Shipping documents
- Original invoices
- Bank statements
- Accounts receivable records

In addition, Superior's accounts receivable manager is available to answer questions.

You may choose to use as many of the sources of information as you wish to gather evidence to support your conclusion.

Treatment: actions/interactions/effects

Candidate reads text. Only the "next screen" button is active.

Screen #4

Document Your Conclusions. For each reply, you must state your conclusion about the item. You must determine that either:

- a) Superior's accounts receivable is properly stated. No exception exists, or
- b) The customer has identified a valid exception. Superior's accounts receivable is incorrect and must be adjusted.

If you conclude that Superior's accounts receivable must be adjusted, you will be asked to prepare a journal entry to make the adjustment.

Treatment: actions/interactions/effects

Candidate reads text. Only the "next screen" button is active.

Screen #5

Document the Basis for Your Conclusion. For each reply, you will be asked to document the audit evidence you used to reach your conclusion. For example, if you reviewed the original invoice sent to the customer and found this to be persuasive you should note this when prompted by the computer. You may rely on more than one source of evidence to reach your conclusion.

Treatment: actions/interactions/effects

Candidate reads text. Only the “next screen” button is active.

Screen #6

Once you have documented your conclusion and the audit evidence you used to reach your conclusion, the computer will automatically log your answers onto a worksheet. This worksheet summarizes your responses for all confirmation requests. You can review this worksheet and change your answers at any time by clicking this button.

Treatment: actions/interactions/effects

Candidate reads text. The “review worksheet” button becomes active and is circled in red.

Screen #7

Listed below are the names of Superior's customers that noted "exceptions" on their returned confirmation requests. Click on any name to review the returned confirmation request and resolve the exception.

Atom

Baker

Clark

Delta

Eagle

Franklin

Grove

Hall

Treatment: actions/interactions/effects

Candidate chooses a reply to a confirmation request. Once a reply has been chosen and a conclusion reached, the name of the customer is highlighted. From this point forward, the "next screen" button is inactive. The five other navigational buttons are all active.

Customer: Atom

Balance to be confirmed: \$15,000

Customer's Notation: "Mailed check for \$15,000 on 12/18/97"

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash receipts from Atom. Cash receipts journal indicates that the \$15,000 received from Atom on 12/29/97 was credited to Accounts Receivable-Adam.

Cash receipts journal, January 1998. No cash receipts from Atom.

Shipping documents. Items shipped on 10/20/97.

Invoice. Invoice dated 10/20/97 indicates nothing unusual.

Bank statement indicates that a check for \$15,000 was deposited on 12/29/97.

Speak to Client

Clicking this button plays an audio. Client says, "Maybe they think they mailed it in December, but sometimes companies hold checks a few days before they send them out. With the holidays and everything, I'm sure we didn't get it until January. As a matter of fact I'm positive. If it's still showing up as outstanding on our accounts receivable as of December 31, then I'm sure we didn't get the money until sometime in 1998."

Additional Interaction

Additional interaction may be required when candidate reaches a conclusion about this confirmation (see Screen to Document Conclusions, page 40).

If the candidate

- Checks the December 1997 cash receipts journal as a source of audit evidence AND
- Listens to the audio of the client AND
- Does *not* check the client representation as a source of audit evidence,

Then the candidate must answer the following free-response question.

I noticed that you listened to the client's representation but did not rely on this to reach your conclusion. In the box provided, explain why.

Customer: Baker

Balance to be confirmed: \$25,000

Customer's Notation: "\$25,000 of goods back-ordered; received 1/6/98"

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash received from Baker in December 1997.

Cash receipts journal, January 1998. No cash received from Baker in January 1998.

Shipping documents. Shipping documents indicate item was shipped (F.O.B. shipping point) via ground transportation on December 30, 1997.

Invoice. Invoice dated December 30, 1997 shows nothing unusual.

Speak to Client

Clicking this button plays an audio. Client says, "I don't know about this one. We ship everything to Baker the slowest, cheapest way possible—their choice. I'll bet we shipped it out on the last day of the year or something and they didn't get it until early January. December 31st was a Wednesday last year. I remember because we were closed Thursday and Friday."

Customer: Clark

Balance to be confirmed: \$24,000

Customer's Notation: "\$24,000 of merchandise was received on consignment 12/10/97; not sold as of 1/19/98"

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash receipts from Clark.

Cash receipts journal, January 1998. No cash receipts from Clark.

Shipping documents. Items shipped on 12/8/97.

Invoice. Invoice dated 12/8/97. Stamped on the face of the invoice is the following: "Items delivered on consignment. Payment not due until goods are sold." The word "consignment" has been highlighted with a yellow highlighter.

Speak to Client

Clicking this button plays an audio. Client says, "We ship stuff to Clark all the time on consignment. I'm pretty sure they're right about this order. We always stamp the invoice 'On Consignment' and we circle it in yellow for the accounting department, but they always end up recording a few as sales. It's a problem. I don't know what else we can do."

Customer: Delta

Balance to be confirmed: \$45,000

Customer's Notation: "Order canceled 12/12/98."

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash received from Delta.

Cash receipts journal, January 1998. \$45,000 received from Delta on 1/30/98.

Shipping documents. Items shipped 12/12/97.

Invoice: Invoice dated 12/12/97. In the memo section of the invoice is a handwritten notation, "Replacement order for PO#9779303."

Speak to Client

Clicking this button plays an audio. Client says, "I talked to my sales manager about this one. He told me Delta had an original order they canceled because they wanted more of the 4-inch elbow valves. He remembered it because he told them we would just add the new items to the existing order, but their computer system made them cancel the old order and issue a new one. That's what happened. They canceled their order and booked a new one the same day."

Customer: Eagle

Balance to be confirmed: \$59,000

Customer's notation: "Can't verify total, only individual invoices"

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. \$27,000 received from Eagle in December 1997. Notation in journal gives invoice number, which is not one of the invoices outstanding at year-end.

Cash receipts journal, January 1998. \$25,000 received from Eagle in January 1998. This is payment on one of the three invoices outstanding at December 31, 1997, which the candidate can verify by comparing the invoice number recorded on the journal to the copy of the invoice.

Shipping documents: Three separate shipments made 11/27, 12/15, and 12/21.

Invoice: Three separate invoices dated the same dates as the shipping documents. Invoices total \$25,000, \$14,000, and \$20,000.

Speak to Client

Clicking this button plays an audio. Client says, "They're one of our major customers. We ship them stuff all the time. I don't know why they can't verify the total. I can sort our receivables any way you want. Which one is best for you?"

Treatment: actions/interactions/effects

After audio plays, a dialogue box appears and gives the candidate the following options:

Check all of the printouts you would like to see

- All outstanding invoices at 12/31/97, sorted numerically with daily subtotals.
- All outstanding invoices at 12/31/97, sorted by customer number with customer subtotals.
- All outstanding invoices as of the date of fieldwork, 2/15/98, sorted numerically with daily subtotals.
- All outstanding invoices as of the date of fieldwork, 2/15/98, sorted by customer number with customer subtotals.
- No further documentation is required for me to reach a conclusion.

Clicking "No further documentation required" returns the candidate to screen #7. Otherwise, the checked document(s) are produced from the client's accounts receivable system. After reviewing the requested document(s), the candidate returns to screen #7.

Customer: Franklin

Balance to be confirmed: \$65,000

Customer's notation: None. Confirmation request was "Returned to sender—addressee unknown."

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash received in December.

Cash receipts journal, January 1998. No cash received in January.

Shipping documents. Shipment made February 20, 1997, to same address as listed in the confirmation.

Invoice. Invoice for \$65,000 dated February 20, 1997, sent to same address as listed in the confirmation.

Speak to Client

Clicking this button plays an audio. Client says, "Franklin? I'm not surprised you didn't get anything back from them. They declared bankruptcy just before Christmas. Their purchasing manager called me looking for a job. We had one big shipment to them about a year ago—\$60,000, something like that. Never collected a dime."

Customer: Grove

Balance to be confirmed: \$75,000

Customer's Notation: "\$75,000 check mailed 12/27/97"

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. \$23,000 received in December.

Cash receipts journal, January 1998. \$75,000 check received January 5, 1998.

Shipping documents. Shipping documents show nothing unusual. Items shipped December 18, 1997.

Invoice. Invoice shows nothing unusual. \$75,000 billed December 18, 1997.

Bank statement indicates that a deposit of \$75,000 was made on January 8, 1998.

Speak to Client

Clicking this button plays an audio. Client says, "I wish all our customers were like these guys. They always pay right away."

Customer: Hall

Balance to be confirmed: \$80,000

Customer's notation: "Amount closer to \$106,000."

Treatment: actions/interactions/effects

A dialogue box prompts candidate: "What would you like to do?" Three choices are offered: review documents, speak to the client, or reach a conclusion.

The candidate reviews the reply to the confirmation request and selects one of the three tasks.

Review Documents

Cash receipts journal, December 1997. No cash received in December.

Cash receipts journal, January 1998. No cash received in January.

Shipping documents. Two shipping documents, one dated 12/19/97 and a second one dated 1/19/98.

Invoice. Invoice dated 12/19/97 for \$80,000. A second invoice dated 1/19/98 for \$26,000.

Speak to Client

Clicking this button plays an audio. Client says, "I don't know why they have a problem with this. Maybe they do owe us more. If they pay us maybe we should adjust our records."

Additional Interaction

Additional interaction may be required when candidate reaches a conclusion about this confirmation (see Screen to Document Conclusion, page 40).

If the candidate

- Listens to the audio of the client AND
- Does *not* propose an adjustment,

Then the candidate must answer the following free response question.

I noticed that you listened to the client, who agreed that the customer might owe more, and therefore, the accounts receivable balance should be adjusted. You have not proposed an adjustment. In the box provided, describe why.

Screen to Document Conclusions

Conclusion (select one):

Not an exception

Exception. Adjustment required

Source(s) of audit evidence (check all that apply)

Cash receipts journal, December 1997

Cash receipts journal, January 1998

Cash receipts documents

Bank statements

Accounts receivable records

Shipping documents.

Original invoices

Client's representation

Other (describe) _____

Click here when you're finished and ready to work on another confirmation. (Note: You can always return to this page to change your answers by clicking on the review worksheet button.)

Treatment: actions/interactions/effects

Candidate clicks the appropriate box to document the conclusion reached. If the "exception" box is clicked, a dialogue box appears to allow the candidate to type in an adjusting journal entry, if any. Other answers are possible—send revised confirmation requests, adjust customer's records, but not general ledger, etc. When the candidate is finished, he or she is returned to screen #7.

Conclusion of the Simulation

After the candidate documents a conclusion for each reply, the candidate returns to screen #7 to select another reply to work on. Once all the replies to the confirmation requests have been completed, a dialogue box appears informing the candidate that all the replies to the confirmation requests have been completed. The candidate has the choice of reviewing the worksheet summarizing the conclusions or moving on to the next simulation, if any.

Worksheet

Note: at any point after screen #7, the candidate has the option to review the following worksheet, which summarizes the candidate's conclusions. Clicking on the name of a customer will return the candidate to that customer's reply to the confirmation request to make any desired changes.

Customer	Balance	Conclusion	Audit Evidence	Adjustment
Atom	\$ 15,000			
Baker	\$ 25,000			
Clark	\$ 24,000			
Delta	\$ 45,000			
Eagle	\$ 59,000			
Franklin	\$ 65,000			
Grove	\$ 75,000			
Hall	\$ 80,000			

SIMULATION No. 2
NARRATIVE FORMAT
FINANCIAL ACCOUNTING SIMULATION

Objective

To test the candidate's ability to:

- Format an income statement, balance sheet, and statement of cash flows.
- Calculate earnings per share.
- Calculate current and deferred income tax expense.
- Identify and describe financial statement note disclosure information.

Synopsis

This is a multiple part simulation that requires the candidate to perform two distinct tasks. In the first part, the candidate is given a trial balance and asked to prepare a basic set of financial statements, including the calculation of earnings per share and current and deferred taxes. The second part of the simulation begins with the financial statements just prepared and requires the candidate to outline the note disclosures that should be included with the financial statements.

Introduction and Instructions

A brief introduction explains that Miller, CPA, has been engaged to prepare the financial statements for Probe Co. The candidate is the staff accountant assigned to the engagement. The candidate is informed that the simulation requires the preparation of a set of financial statements, including the accompanying notes. The candidate has no option but to proceed with the first part of the simulation.

Part One: Prepare Basic Financial Statements**Introduction and Instructions**

The candidate is instructed that the purpose of this section of the simulation is to prepare an income statement, balance sheet, and statement of cash flows for Probe Co. for the year ended X1. There will be two parts to the exercise:

- First, the candidate will review the condensed trial balance for the company and assign accounts to one of the three financial statements.
- Second, once the trial balance accounts have been assigned to a financial statement, the candidate will be asked to prepare each of the three required financial statements. Preparation of the income statement requires calculation of earnings per share and deferred taxes.

Review Trial Balance and Assign Accounts

The candidate is presented with a condensed trial balance for the company. The trial balance lists the accounts (summarized for financial reporting purposes), together with the change in the account from the previous year. For example, the condensed trial balance might be formatted as follows:

	12/31/X1	12/31/X0	Net
	Balances	Balances	change
	<u>Dr.(Cr.)</u>	<u>Dr.(Cr.)</u>	<u>Dr.(Cr.)</u>
Cash	\$xxx,xxx	\$xxx,xxx	\$xxx,xxx
Accounts receivable, net	xxx,xxx	xxx,xxx	xxx,xxx
Property, plant and equipment, etc.	x,xxx,xxx	x,xxx,xxx	xx,xxx

The candidate is instructed to review each account listed on the condensed trial balance and determine whether it should flow to the balance sheet, the income statement, statement of cash flows, or none of the above. Once all the accounts have been designated, the candidate is ready to choose a financial statement to work on. Note: the candidate can return to the trial balance to make changes to the assignments at any time during the simulation.

Selecting the Financial Statement to Prepare

A dialogue box appears to inform the candidate that certain additional information, not included in the trial balance, is available to assist in preparing the financial statements. This information appears in a small scroll box to one side of the screen. The candidate has the option of keeping the scroll box open during the preparation of the financial statements or recalling it when necessary by clicking a button.

The additional information includes items that are necessary for the preparation of the financial statements or the notes. For example, information necessary to calculate earnings per share or deferred taxes might be included, along with “off-balance sheet” disclosure items such as related party transactions or concentrations of credit risk.

After the additional information has been displayed, the candidate has the option of choosing which of the financial statements to work on.

Financial Statement Utility

Each financial statement is prepared using a financial statement utility. The utility has the look and feel of a spreadsheet program, except that the available features have been severely limited to include only those necessary to complete the problem requirements. For example, the candidate could edit account descriptions, add captions, and foot columns, but the utility would not allow the candidate to perform unnecessary functions such as graphing or formatting.

The candidate has the option of observing a brief demonstration explaining the features of the utility program. This demonstration is animated with a voiceover explaining how the utility works. The animation demonstrates the features as they are being described. A separate dialogue box summarizes key points. The candidate can keep the summary of key points on the screen or can close it and recall it when necessary. Also, by highlighting a cell in the spreadsheet and clicking the right mouse button, the candidate is presented with a pull-down menu of available options for manipulating the contents of the cell.

Prepare the Financial Statements

Accounts and amounts previously designated from the condensed trial balance appear on the financial statement in the order in which they were selected. Using the financial statement utility, the candidate must order the accounts and amounts and add captions to create the required financial statement. The candidate may also need to use the “additional information” to properly prepare the statement.

Earnings per Share and Deferred Taxes Subroutine

The income statement contains three account descriptions that were not included in the condensed trial bal-

ance: earnings per share and current and deferred taxes. These account titles are highlighted. A dialogue box appears, reminding the candidate that the preparation of the income statement requires the calculation of earnings per share and current and deferred taxes. The dialogue box also explains that when the candidate is ready to make those calculations, he or she should click on the title of the item, and a worksheet will be provided to make the calculation.

Clicking on one of the highlighted titles launches the spreadsheet utility. This utility is smaller than the income statement the candidate is working on, which allows the candidate to use the utility while still looking at the income statement. (Note: the screen also must accommodate the additional information scroll box, which contains information necessary to make the calculations). The spreadsheet utility is a spreadsheet application that includes only the most basic arithmetic functions.

When the candidate is finished with the calculation, double-clicking the cell with the answer automatically links the answer to the income statement worksheet.

Conclusion of Part One

Once all three financial statements have been prepared, the candidate is ready to move on to part two of the simulation.

Part Two: Prepare Notes to the Financial Statements

Introduction and Instructions

The candidate is instructed that this part of the simulation will require describing the content of the notes to the financial statements that have just been prepared. The tasks required to complete the requirements are described.

Select Topics for Note Disclosure

The candidate reviews the captions from the financial statements just prepared and chooses the account descriptions that require financial statement disclosure. By highlighting these accounts, the candidate begins to build an outline for the notes to the financial statements. To indicate that all financial statement items requiring disclosure have been highlighted, the candidate clicks a button.

The outline for the notes appears. This outline contains all the accounts the candidate has just selected. A dialogue box appears and asks the candidate if there are any other items, not included in the financial statements, that require disclosure. If so, these items can then be entered into the outline.

Outline Note Disclosures

Once the topics for the notes have been determined, the candidate will describe the information to be included in each note.

BRIEFING PAPER NO. 1

**CONVERSION OF THE UNIFORM CPA EXAMINATION
TO A COMPUTER-BASED EXAMINATION**

COMMENT FORM

NAME _____

TITLE _____

ORGANIZATION _____

ADDRESS _____

Please take a few minutes to provide us with your feedback. Your advice, comments, and input will be carefully weighed and considered as the Joint AICPA/NASBA Computerization Implementation Committee moves forward. The Committee welcomes your frank evaluations throughout this detailed and complex process.

You may return the form in the envelope provided, or e-mail akendal@aicpa.org with your comments and suggestions.

1. Overall, to what degree do you believe the proposed computerized Uniform CPA Examination, as defined on Pages 3–9 of the *Briefing Paper*, is the best model for assessing the knowledge and skills required by newly-licensed CPAs to protect the public interest?

Check one:

- 5 The best model.
- 4 A very good model.
- 3 Not sure.
- 2 Not a very good model.
- 1 An unacceptable model.

Additional comments: _____

2. Please provide what you believe to be the two greatest advantages and the two greatest disadvantages of this model to the Public, to Board Members, to Board Administrators, and to CPA Candidates.

Two greatest ADVANTAGES of this model	Two greatest DISADVANTAGES of this model
Public (1) (2)	Public (1) (2)
Board Members (1) (2)	Board Members (1) (2)
Board Administrators (1) (2)	Board Administrators (1) (2)
CPA Candidates (1) (2)	CPA Candidates (1) (2)

3. Do the examples presented in Computer Simulations 1 and 2 meet your expectations of the concept of a simulation for the computer-based examination?

Check one:

- 5 Surpass my expectations.
- 4 Meet my expectations.
- 3 Not sure.
- 2 Do not meet my expectations.
- 1 Are unacceptable.

Additional comments: _____

4. Do you have any questions about the proposed computer-based examination that this *Briefing Paper* did not answer to your satisfaction?

Please specify: _____

5. Do you have any suggestions for topics that you would like to see covered in future *Briefing Papers* dealing with the computerized Uniform CPA Examination?

6. Additional comments and suggestions: _____

Please check all that apply to you:

- CPA
- Public Practice
- Business or Industry
- Individual Member of Board of Accountancy
- State Board Administrator
- Individual Member of NASBA
- CPA Candidate
- Educator
- Affiliated with a CPA Examination Review Course
- Other: _____

Thank you for your participation. We will continue to keep you informed and to seek your input in the months ahead.

**PLEASE RETURN YOUR
COMPLETED COMMENT FORM IN
THE ENVELOPE PROVIDED BY
JANUARY 15, 1999.**