



**CPA INTERMEDIATE LEVEL**  
**AUDITING AND ASSURANCE**

**THURSDAY: 6 January 2022.**

**Time Allowed: 3 hours.**

**Answer ALL questions. Marks allocated to each question are shown at the end of the question.**

**QUESTION ONE**

- (a) ABC Ltd. manufactures mineral water and has factories across the East African region. The company's customer base comprises individuals and retailers who make direct purchases through its website. You are the audit supervisor reviewing the documentation of the company's internal controls and you come across the following matters:
1. ABC Ltd.'s website allows customers to make orders directly and also pay in advance. The website is not integrated with the stock system. Goods are dispatched to the customers via courier service although the courier company does not file returns with ABC Ltd. to confirm delivery.
  2. Over the last 9 months, customers have been complaining about delayed deliveries. Investigations have revealed that sales orders are entered correctly, but not dispatched to the delivery department for action.
  3. Customers undergo credit checks prior to being given credit and the limits are set by the sales ledger clerks. Customers also place orders through the sales team who decide on the discount to be granted.
  4. There have been various complaints raised on the accuracy of supplier statements given that the accountant who used to handle this docket left the organisation.

**Required:**

With reference to the internal control system of ABC Ltd.:

- (i) Explain five deficiencies in the system. (5 marks)
  - (ii) Describe five tests of control required to assess if the controls are working effectively. (5 marks)
- (b) In line with ISA 220 "Quality Control for an Audit of Financial Statements", describe four responsibilities of an audit supervisor in relation to supervising and reviewing the audit assistant's work during an audit. (4 marks)
- (c) Describe six activities that an audit firm should perform prior to accepting a new audit engagement. (6 marks)
- (Total: 20 marks)**

**QUESTION TWO**

ISA 320 "Audit Materiality" states that "The auditor should consider materiality and its relationship with audit risk when conducting an audit".

**Required:**

- (a) Discuss the relationship between materiality and audit risk both when planning for an audit and when evaluating audit evidence. (10 marks)
  - (b) Explain the following terms:
    - (i) Peer review. (2 marks)
    - (ii) Hot review. (2 marks)
  - (c) Describe six substantive tests that you would undertake over accounts receivable. (6 marks)
- (Total: 20 marks)**

### QUESTION THREE

When auditing a computer accounting system, the independent auditor should understand how the use of computers affects the various characteristics of internal control. The independent auditor should be aware of those control procedures that are commonly referred to as “general” controls and those that are commonly referred to as “application” controls. General controls relate to all computer activities and application controls relate to specific accounting tasks.

#### Required:

- (a) Describe three general controls that should exist in computer-based accounting systems. (6 marks)
- (b) Explain four potential problems of using audit software indicating how each may be resolved. (4 marks)
- (c) Explain the concept of “auditing around the computer” and why it increases audit risk. (2 marks)
- (d) The directors of XYZ Enterprises Ltd. have prepared a cash flow forecast for submission to the bank. They have asked you as the auditor to provide a negative assurance report on this forecast.

#### Required:

- (i) Discuss two differences between “positive” and “negative” assurance. (4 marks)
- (ii) Explain two advantages to the directors of providing a negative assurance report on their cash flow forecast. (4 marks)

**(Total: 20 marks)**

### QUESTION FOUR

You are the manager responsible for the audit of Jamii Retail Ltd., a public quoted company, which has a number of stores that sell household products including; furniture, electrical equipment, iron sheets, cement, vehicle spare parts, cooking equipment and carpets to the general public. Jamii Retail Ltd. is highly respected by investors across East Africa.

The company has an average annual turnover of Sh.20 billion. In the previous year’s audit, there have been problems, some of which were highlighted in recent media coverage. The problems related to:

1. Pilferage of stock by employees and customers.
2. Slow moving and damaged stock which was worth less than cost.
3. Incomplete recording of sales when the customer pays in cash (these represent 65% of all sales).

The company has a small internal audit department. The internal audit staff occasionally visit branches and perform appropriate audit work at the head office.

#### Required:

- (a) Describe the work you would carry out and the matters you would consider in planning the audit prior to the commencement of the detailed audit work, including consideration of the timetable for the audit. (12 marks)
- (b) In the context of ISA 240 “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements”, explain the auditor’s responsibilities in relation to the prevention and detection of fraud and error in the course of an audit assignment. (8 marks)

**(Total: 20 marks)**

### QUESTION FIVE

(a) In the context of auditing in the public sector:

- (i) Describe four roles of Parliament and County Assemblies, or their equivalents, in public audit. (4 marks)
- (ii) Explain the salient features of “regulatory audits”, “forensic audits” and “performance audits”. (6 marks)
- (iii) Summarise four reasons for qualified audit reports in the public sector. (4 marks)

(b) With reference to the e-commerce environment, discuss three controls that an entity needs to put in place to safeguard the accuracy, completeness and integrity of financial information. (6 marks)

**(Total: 20 marks)**

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