



CPA INTERMEDIATE LEVEL

AUDITING AND ASSURANCE

WEDNESDAY: 26 April 2023. Afternoon Paper.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question. Do NOT write anything on this paper.

QUESTION ONE

- (a) Highlight **THREE** benefits that may be derived from independently audited financial statements. (3 marks)
- (b) International Standard on Auditing (ISA): 560 - Subsequent Event defines subsequent events as events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

Required:

Propose **FOUR** audit procedures that an auditor should perform as near as possible to the date of the Auditor's Report. (4 marks)

- (c) Elimu Yetu Trust is a charitable institution that sponsors needy students to seek tertiary education in Europe. The organisation raises finances from cash donations at annual fund-raising events, telephone and online appeals from well-wishers. Elimu Yetu Trust has employed a part-time bookkeeper since it is still at an early formative stage and the trustees cannot afford to hire a qualified accountant.

Following a recent review of the Finance Act, charitable institutions will be subjected to new audit and accounting regulations. Due to this, your firm has been appointed as first-time auditors of Elimu Yetu Trust. You have been informed by the trustees of Elimu Yetu Trust that the unaudited financial statements for the year have been prepared by a volunteer who is a recently retired qualified accountant.

Required:

- (i) Describe **TWO** examples of each of the following risks associated with the audit of Elimu Yetu:
- Inherent risks. (2 marks)
 - Control risks. (2 marks)
 - Detection risks. (2 marks)
- (ii) Propose **FOUR** audit tests that you could perform on income from fund raising events. (4 marks)
- (iii) Evaluate **THREE** substantive audit tests that you might undertake to verify the expenditure during the fund raising events. (3 marks)

(Total: 20 marks)

QUESTION TWO

- (a) Explain the following terms as used in computerised audit environment:
- (i) Cloud computing. (2 marks)
 - (ii) Encryption. (2 marks)
 - (iii) Embedded audit module. (2 marks)

- (b) During the annual audit evaluation exercise by the Internal Audit Committee of Limau Ltd., the Head of Internal Audit presented the internal audit plan for the upcoming financial year. He requested for additional members of staff to enhance the skill set in the audit team to match planned audit activities for the year. The committee, citing budgetary constraints of the company, resolved to adopt either co-sourcing or out-sourcing of the skills lacking in the current internal audit staff team.

Required:

- (i) Distinguish between “co-sourcing” and “out-sourcing” of the skills lacking in the current internal audit staff team. (4 marks)
- (ii) Outline **FOUR** matters that the Head of Internal Audit could ensure are included in the engagement letter with the outsourced service provider of the internal audit activity. (4 marks)
- (iii) Evaluate **SIX** areas that the Head of Internal Audit might review to ensure that the external service provider possesses the necessary knowledge, skills and competencies to undertake the task. (6 marks)

(Total: 20 marks)

QUESTION THREE

- (a) Contrast the responsibilities of the external auditors and internal auditors in detection of fraud. (4 marks)
- (b) Kezzia Karimi has recently been appointed as the head of internal audit function in one of the Government Entities. The entity has never had an internal audit function. In this regard, Kezzia has the responsibility of developing an audit charter for approval by the Audit Committee.

Required:

Advise Kezzia on four matters for inclusion to the audit charter to ensure independence of the internal audit function. (8 marks)

- (c) International Standard of Auditing (ISA) 315 - Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment, requires the auditor to perform risk assessment procedures which include obtaining an understanding of the entity and its environment, including its internal controls.

Required:

- (i) Citing a relevant example, explain the term “negative assurance”. (3 marks)
- (ii) Explain the purpose of undertaking risk assessment procedures. (2 marks)
- (iii) Outline **THREE** sources of audit evidence that the auditor can use as part of risk assessment procedures. (3 marks)

(Total: 20 marks)

QUESTION FOUR

- (a) An efficient wage system is important for most companies however, there is no single wage system which suits all companies. Some companies have a completely manual system, others a partially computerised system while others have a system which is completely computerised. Broadly speaking, a company with a completely manual system will use a clock and a clockcard system to record hours, prepare the payroll manually and conduct a physical wage payout. A fully computerised system may include biometric time keeping, processing of the payroll by the computer and payment of the amount owed to the employee by electronic funds transfer.

Required:

In the context of the above information:

- (i) Explain the major advantage of biometric scanning technology over other methods of recording hours worked. (2 marks)
- (ii) Discuss whether the use of biometric scanning technology to record hours worked, might eliminate the risk of fictitious employees being used to perpetrate wage fraud. (5 marks)
- (iii) Evaluate **FOUR** characteristics of an organisation which could influence the management in deciding on a suitable wage system. (8 marks)

- (b) Joyce Jamila runs an audit firm that recently completed the audit of SofaSeti Ltd., a manufacturer of exclusive home furniture. The audit fee amounted to Sh. 4,800,000. Having recently purchased a new house, Joyce proposed the following to SofaSeti Ltd. as a mode of settlement:
1. Instead of invoicing SofaSeti Ltd. a fee of Sh. 4,800,000, she would invoice the company an amount of Sh.2,800,000 for the audit fees.
 2. SofaSeti Ltd. would then supply Joyce Jamila with free furniture with a cost value of Sh.2,000,000 for her new house.
 3. SofaSeti Ltd. would not raise a sale in the company's accounting records and would write off the amount of Sh.2,000,000 off as part of the allowance for obsolete inventory.

Required:

Discuss **FIVE** issues in terms of the code of professional conduct applicable in the situation above. (5 marks)

(Total: 20 marks)

QUESTION FIVE

- (a) You are a senior auditor in the audit of Baisiko Ltd., a company which manufactures bicycles. The company has numerous suppliers due to the fact that its products are manufactured from a wide range of materials and components. During discussion with the audit team about further audit procedures to be adopted, one of the trainees raised the question of whether it would be appropriate to circularise creditors to confirm their balances.

Although your firm had not carried this procedure in prior years, you decide to perform a positive circularisation on creditors listed as at 31 December 2022.

Required:

Evaluate **FIVE** creditors that you could include in the sample of creditors to be positively circularised. (10 marks)

- (b) You have been auditing Fruitly Ltd., a large national grocery store chain for the first time. Towards the end of the audit, your audit manager demands that you seek a letter of representation from the management of the client company. Upon follow up with the client's management, you are informed that the management is unwilling to sign the letter of representation.

Required:

(i) Examine the need for seeking a letter of representation from the client's management. (2 marks)

(ii) Outline **SIX** matters that you expect the management of Fruitly Ltd. to include in the letter of representation. (6 marks)

(iii) Highlight **TWO** reasons for the management to be unwilling to sign a letter of representation. (2 marks)

(Total: 20 marks)

.....