



CPA PART III SECTION 6

ADVANCED AUDITING AND ASSURANCE

FRIDAY: 3 September 2021.

Time Allowed: 3 hours.

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

QUESTION ONE

- (a) Maisha Bora Welfare Group was established in the year 2015. The organisation's aim is to provide support to children from disadvantaged backgrounds who wish to take part in athletics.

The organisation has a detailed constitution which explains how the income of the welfare group can be spent. The constitution also notes that administration expenses should not exceed 10% of income in any year.

The income of the organisation is derived wholly from voluntary donations. The sources of income include:

- Cash collected by volunteers seeking donations from the public.
- Cheques sent to the welfare group's head office.
- Donations from generous individuals. Some of these donations have specific clauses attached to them indicating that the initial amount donated (capital) cannot be spent and that the interest income from the donation must be spent on specific activities, for example, provision of sports shoes.

Required:

In the context of the above information:

- (i) Explain the term "audit risk", clearly indicating three elements of risk that contribute to total audit risk. (4 marks)
- (ii) Explore the areas of inherent risk in Maisha Bora Welfare Group, explaining the effect of each of these risks on the audit approach to be adopted. (6 marks)
- (b) Suggest the procedures that an auditor should perform in order to gain understanding of a client's business. (4 marks)
- (c) You are a senior audit manager in M and M Associates Certified Public Accountants. Recently, you were assigned specific responsibility for undertaking annual reviews of existing clients. The following situation has arisen in connection with one of the clients, Reward Ltd., an exporter of specialist equipment.

The Chief Executive Officer of Reward Ltd. has requested for advice on the accounting treatment and disclosure of payments being made for security consultancy services. The payments, which aim to ensure that consignments are not impounded in the destination country of a major customer, may be material to the financial statements for the year ending 31 December 2021. Reward Ltd. does not treat these payments as tax deductible.

Required:

Explore the ethical and other professional issues raised by the above matter and indicate the action, if any, that your firm should now take. (6 marks)

(Total: 20 marks)

QUESTION TWO

- (a) You are a manager at Dundee Associates, a firm of Certified Public Accountants. Your specific responsibility is for the quality of audits.

Your firm was appointed the auditor of Taka Ltd., a provider of waste management services, in January 2020. You have visited the audit team at Taka Ltd.'s head office. The team comprises an audit senior, an audit assistant and two trainees.

Taka Ltd.'s draft accounts for the year ended 31 December 2019 show revenues of Sh.118 million (2018 Sh.8.3 million) and total assets of Sh.40 million (2018 Sh.30 million). During your visit, a review of the audit working papers revealed the following:

- (i) On the planning checklist, the audit senior has crossed through the analytical procedures section and written "Not applicable-New client". The audit planning checklist has not been signed off as having been reviewed.
- (ii) The audit senior last visited Taka Ltd.'s office when the final audit commenced two weeks earlier on 1 February 2020. The audit senior has since completed the audit of tangible non-current assets including property and service equipment which amount to Sh.8 million as at 31 December 2019 (2018 Sh.8 million). The audit senior spends most of his time at your firm's office and is currently allocated three other assignments in addition to the audit of Taka Ltd.

Required:

Discuss the implications of the two findings above for Dundee Associate's quality control policies and procedures. (8 marks)

- (b) Explain the role of support/comfort letters as evidence in the audit of group financial statements. (6 marks)
 - (c) Discuss how horizontal groups (non-consolidated entities under common control) affect the scope of an audit and the audit work undertaken. (6 marks)
- (Total: 20 marks)**

QUESTION THREE

- (a) Following the outbreak of the Covid-19 pandemic with its associated uncertainty and crisis management requirements, internal audit is now in an interesting position to guide organisations through a completely new landscape of risk. It is evident that new trends have emerged in internal audit that will change the way audit is perceived for years to come.

Required:

In the context of the above statement, explain how the following recent trends are transforming the audit landscape:

- (i) Artificial intelligence. (3 marks)
 - (ii) Soft controls and company culture. (3 marks)
- (b) Describe how the following factors are posing risks to internal audit in the new dispensation:
 - (i) Cyber security in the remote world of work. (3 marks)
 - (ii) Changing regulatory risks. (3 marks)
 - (c) Most auditing practitioners agree that legal liability is part of the risk associated with their work. However, they argue that practising auditors may also take specific action to minimise their liability.

Required:

Evaluate the measures that auditors may take to minimise the possibilities of legal liability. (8 marks)

(Total: 20 marks)

QUESTION FOUR

- (a) You are the auditor of Benrose Ltd. which undertakes construction contracts on behalf of its clients.

Last year, you qualified the auditor's report due to lack of evidence to support the client's schedules of estimated costs to completion. During the year, a quantity surveyor joined the management team of Benrose Ltd. His main role is to prepare year end schedules, by contract, of total costs to completion. This includes:

- Direct costs incurred to the balance sheet date.
- Attributable overheads.
- Estimated costs to completion.

You are satisfied that the quantity surveyor is appropriately qualified and experienced.

Required:

- (i) Explain the nature and extent of the reliance which you would seek to place on the work of the quantity surveyor. (4 marks)
 - (ii) Describe the audit work you would perform in respect of total costs to completion. (8 marks)
- (b) Describe the audit work that you would carry out in respect of the following:
- (i) Segment information. (3 marks)
 - (ii) Transfer of shares. (3 marks)
 - (iii) Dividends. (2 marks)
- (Total: 20 marks)**

QUESTION FIVE

- (a) Discuss the nature and purpose of the following:
- (i) E-Commerce audits. (3 marks)
 - (ii) Value for money audits. (3 marks)
 - (iii) Social audits. (3 marks)
- (b) Discuss the practical challenges that professional bodies might face in trying to conduct audit quality assurance (AQA) activities in member audit firms. (6 marks)
- (c) Identify the practical steps that auditors might take to ensure independence and objectivity in their work. (5 marks)
- (Total: 20 marks)**
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