

December 12, 2002

ADVANCED AUDITING
[PE-1 Paper 2] & [Module "E" Paper E-14]

(MARKS 100)
(3 hours)

- Q.1 (a) List the type of information that may come to the auditor's attention that may indicate that Non-compliance with laws or regulations has occurred. **(05)**
- (b) With reference to the Acceptance procedures in respect of prospective clients, discuss the procedures, which you would include in your evaluation. **(05)**
- Q.2 One of your clients is implementing an IT system for its cash management function. List five key IT controls which you would suggest to include in the system. **(10)**
- Q.3 During the course of the audit of the accounts of Zafar Corporation Limited for the year ended June 30, 2002, you have decided to use the work of an Expert as audit evidence. However, before proceeding with the same, you need to discuss this matter with the management of the Corporation, and for that, you are expected to make a small presentation thereto which should include such matters as:
- (a) circumstances under which you would consider the need to use the work of an expert
- (b) consideration which you will have in determining the need to use the work of an expert
- (c) consideration which you will have in assessing the professional competence of the expert
- Address these matters in your presentation. **(10)**
- Q.4 During your audit of the accounts of Imran Manufacturing Co. (Private) Limited for the year ended June 30, 2002, you are in the process of briefing your staff about transactions which might appear unusual in the circumstances and wish to give them some examples that may indicate the existence of previously unidentified Related Parties. What examples would you give them in this regard? **(05)**
- Q.5 Your firm has been appointed as an auditor of a commercial bank which has recently commenced operations in Pakistan. The Audit Committee of the Bank has also asked your firm to carryout a special review, in addition to the statutory audit, to evaluate the bank control procedures for the prevention of money laundering. Highlight significant anti-money laundering control procedures which you would expect. **(12)**

- Q.6 (a) At the conclusion of the audit of XYZ (Private) Limited for the year ended June 30, 2002, you have decided to express a reservation in your report on the accounts of the above-referred company as a result of your disagreement with the management in respect of its failure to record depreciation on its building and equipment, using annual rates of 5% and 20% respectively. You have determined that a Qualified opinion would be issued. Draft your reservation, along with the opinion paragraph, to be included in your report in accordance with the requirements of related International Standard on Auditing. Do not draft the entire report pursuant to the requirements of the Companies Ordinance, 1984. (04)
- (b) Usman, an Audit Manager, is toying up with the idea of expressing a disclaimer of opinion in his report on the accounts of ABC Corporation for the year ended June 30, 2002 due to his inability to observe physical inventories and confirm trade debts on account of certain limitations placed by management of the company. Assist him in drafting the Scope paragraph, a paragraph discussing the scope limitation and the concluding paragraph of the report. You are expected to follow the requirements of related International Standard on Auditing in your drafting of the above. (04)
- (c) State the basic elements and the lay out of the auditor's report on a special purpose audit engagement. (05)
- Q.7 (a) The work performed by each assistant needs to be reviewed by personnel of at least equal competence. Why? (05)
- (b) State the functions performed by personnel carrying out supervisory responsibilities. (05)
- Q.8 (a) Identify the two categories in which fraud risk factors relating to misstatements resulting from misappropriation of assets may be grouped. (02)
- (b) For each of the above two categories, identified in (a) above, list examples of fraud risk factors which relate to misstatements that results from misappropriation of assets. (08)
- Q.9 While reviewing the notes, prepared for you by your Audit Manager, before the Closing meeting with the Chief Executive Officer of NY Corporation in respect of the financial statements for the year then ended June 30, 2002, you noted the following:
- (a) The management of the Corporation is not willing to reverse an accrual of Rs.350.00 million it made in the above-referred financial statements on account of certain rebates, the Corporation claims, are due from a Telecommunication company, as a result of a law suit filed by the corporation against the Telecommunication company, in the local High Court. These rebates relate to the period commencing July 1, 1998 to June 30, 2000. The Telecommunication company, in turn, filed a counter lawsuit against the Corporation. Legal proceedings in both cases are currently in the initial stages of hearing. Realization of amount accrued by the Corporation, therefore, appeared uncertain to you, as well as to the legal advisor of the Corporation. All your efforts failed to persuade the management that the accrual in question should be reversed.

(03)

- (b) The Corporation during the current year transferred a sum of Rs. 27.00 million, representing the cost of a Project, from capital work-in-progress to fixed assets and claimed depreciation and investment tax credit thereon, even though the said project had not resulted in the production of intended products in commercially feasible quantities by the end of the current year. Whilst your Audit Manager agreed with the management that the said project commenced production, he regards the production to be in trial run period and, as such, is of the firm view that commencement of commercial production had not taken place and, hence, is of the view that all expenditure of revenue nature should continue to be capitalized up to the date of commencement of commercial production. The management of the Corporation, however, is not willing to listen to your Audit Manager who has determined that due to the above-referred transfer, profit for the year is overstated by Rs.27.00 million.
- (c) The Corporation during the current year advanced a sum of Rs.287.00 million to one of its associated undertakings. The above sum was extended with complete disregard to the approval of the shareholders as a result of which your Audit Manager noted that the advance in question had been given without arranging for a Special resolution and that the said advance was, in fact, in excess of thirty percent of the paid up capital and free reserves of the Corporation at the time when the same was given. The management of the Corporation had not made any disclosures in this regard in its financial statements.

Required:

As Engagement Partner of the audit of NY Corporation, you are expected to:

- Give a convincing reason to the CEO as to why the views of your Audit Manager may be correct in respect of each of the above matters. (06)
- Identify the circumstances why it may not be possible for you to render an unqualified opinion if the CEO insists on his point of view in each of the above matters. (02)
- Assuming that it is not possible for you to render an unqualified opinion, draft your reservations in respect of each of the above matters. (12)

(THE END)