



Auditing

Intermediate Examinations – Autumn 2010
Module D

August 30, 2010
100 marks - 3 hours

- Q.1 You are the Audit Manager on the audit of Al-Salam Pakistan Limited (ASPL) for the year ended June 30, 2010. ASPL is engaged in the manufacture of a wide range of plastic products. While reviewing the initial work performed by the audit team, the following matters have come to your notice:
- The quantity of material scrapped during the year is materially different from the quantity of scrap sold. The company's records show nil balance both at the beginning and at the close of the year. No reconciliation for the difference has been provided by the company.
 - Sales for the year have increased by 7% over the previous year. However, it has been noted that sales in the last two weeks of June 2010 have been exceptionally high and represent 15% of the annual sales. The audit working papers carry the following observations in respect of the above:
 - 70% of the sales in the last two weeks of June were made to two new customers whose credit assessment has not been formally documented;
 - a significant portion of the goods sold to the above referred customers were returned in the first week of July 2010; and
 - management bonuses are linked to the operating performance of the company.
 - During the year, ASPL purchased a machine for Rs. 25 million. The payment voucher is duly supported by the invoice from the supplier. However, the fixed assets schedule provided by the client shows the amount capitalized as Rs. 2.5 million. Depreciation has been charged on this amount. The difference of Rs. 22.5 million is appearing in the Bank Reconciliation Statement.

Required:

- Analyze each of the above situations and assess whether it represents a fraud or an error. *(06 marks)*
- What action would you take to deal with the above matters? *(09 marks)*

- Q.2 During the course of the audit, effective consultation helps to address the difficult or contentious matters that may arise within the engagement team or between the engagement team and others, within or outside the firm.

Required:

- What are the responsibilities of an audit engagement partner in this regard? *(04 marks)*
- How can an auditor ensure that consultations involving difficult or contentious matters have been appropriately documented? *(03 marks)*

- Q.3 The analytical procedures which are carried out near the end of the audit usually assist the auditor in forming an overall conclusion on the financial statements.

Required:

- State the objectives which an auditor expects to achieve while applying analytical procedures at the end of an audit. *(04 marks)*
- Discuss the course of action an auditor should adopt when results of analytical procedures identify inconsistent relationships or differ from expected values by significant amounts. *(04 marks)*

Q.4 Al-Shams Limited is an unquoted public company. A large part of its business is carried out with persons / organisations who are related to the management or the shareholders.

Required:

- (a) State any *eight* procedures which an auditor may perform for determining the existence of related parties or related party transactions. (08 marks)
- (b) Give four examples of situations that may be indicative of dominant influence exerted by a related party. (04 marks)

Q.5 Al-Madad Foundation (AMF) is a charitable organization. It receives donations which are utilized to help the destitute persons in accordance with the rules and regulations prescribed by the AMF's Trust Deed.

The donations are received from the following sources:

- (i) Cash collected from the general public through charity boxes placed at key points in hospitals, airports, superstores etc.,
- (ii) cash and cheques received from individuals and institutions at AMF's office; and
- (iii) cash from generous individuals who prefer to remain anonymous.

Donations received in case of (ii) and (iii) above, often contain specific instructions for utilisation of the donated amount for specific purposes e.g. for education of orphan children.

Required:

- (a) Identify the inherent risks in the operations of AMF. (03 marks)
- (b) Briefly discuss the effect of each of these risks on the audit of AMF. (03 marks)

Q.6 (a) What is the difference between audit strategy and audit plan? (04 marks)

- (b) You have been appointed as the auditor of a company which was previously audited by another auditor. Being a new client, what additional considerations would you take into account while performing the preliminary engagement activities prior to commencement of the audit? (05 marks)

Q.7 (a) Explain the term "Sufficient and Appropriate Audit Evidence". (04 marks)

- (b) You are the Audit Senior on the audit of Al-Haq Limited. The company is a trading concern and 70% of its business relates to imported goods. The chief accountant has provided you the bank reconciliation statements of all the bank accounts alongwith the bank statements.

Required:

- (i) State the substantive procedures that you would carry out for the verification of bank balances. (06 marks)
- (ii) Identify any *eight* types of information which you would verify from the confirmations received directly from the bank. (08 marks)

Q.8 When expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence, the auditor has to determine whether to use the work of an auditor's expert.

Required:

List down the sources from where the auditor may get the information regarding the expert's competence, capabilities and objectivity. (06 marks)

Q.9 In the light of ISA-700 “Forming an opinion and reporting on financial statements”, discuss the auditor’s responsibilities with regard to un-audited supplementary information presented with the audited financial statements. **(07 marks)**

Q.10 Al-Badr & Company, Chartered Accountants, have conducted the statutory audit of the financial statements of Al-Qasim Limited, a listed company, for the year ended June 30, 2010 under the requirements of the Companies Ordinance, 1984. The job in charge has drafted the following audit report:

Auditors’ Report to the Directors

We have audited the annexed balance sheet of Al-Qasim Limited as at June 30, 2010 and the related profit and loss account and statement of changes in equity together with the notes forming part thereof, for the year then ended and we state that we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purposes of our audit.

We conducted our audit in accordance with the auditing standards. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the above said statements are free of any material misstatement. An audit includes examining evidence supporting the amounts and disclosures in the above said statements. An audit also includes assessing the accounting policies and all estimates made by management, as well as, evaluating the overall presentation of the above said statements. We believe that our audit provides a reasonable basis for our opinion and, after due verification, we report that:

- (a) in our opinion:
 - (i) the balance sheet and profit and loss account together with the notes thereon have been drawn up in conformity with the Companies Ordinance, 1984, and are in agreement with the books of account and further in agreement with accounting policies consistently applied;
 - (ii) the expenditure incurred during the year was for the purpose of the company’s business; and
 - (iii) the business conducted, investments made and the expenditure incurred during the year were in accordance with the objects of the company;
- (b) in our opinion and to the best of our information and according to the explanations given to us, the balance sheet, profit and loss account and statement of changes in equity together with the notes forming part thereof conform with International Financial Reporting Standards, and give the information required by the Companies Ordinance, 1984, in the manner so required and respectively give a true and fair view of the state of the company’s affairs as at June 30, 2010 and of the profit and changes in equity for the year then ended; and
- (c) in our opinion, no zakat was deductible at source under the Zakat and Ushr Ordinance, 1980 (XVIII of 1980).

Al-Badr & Company
Chartered Accountants
Karachi

Dated: September xx, 2010

Required:

Identify and explain (where necessary) the errors in the above audit report.

(Note: You are not required to redraft the report.)

(12 marks)

(THE END)