



Advanced Auditing

Final Examination
Winter 2011
Module F

9 December 2011
100 marks - 3 hours
Additional reading time - 15 minutes

Q.1 Your firm has recently been appointed as the statutory auditor of Chaudhry Limited (CL) for the year ending 31 December 2011. The previous auditors, from whom your firm has received professional clearance, did not wish to be re-appointed as auditors.

CL is involved in the supply of imported consumer products. The company has its own retail outlets in all major cities. It also supplies goods to large retailers most of whom are allowed 45 days credit.

Time required to import the goods is approximately two months. 50% of the amount is paid at the time of booking of order and the remaining amount is paid at the time of receipt of goods. The goods are required to be insured by CL.

CL's suppliers are mainly based in Middle East. Due to political disturbances, a major supplier has recently ceased its operations.

All imported goods are initially placed in a warehouse in Karachi. Supplies are made against orders which are mostly received over telephone by the sales department. The warehouse in-charge prepares a summary of all dispatches which is approved by the sales manager, on a daily basis. Stock records are computerised. Physical stock taking is carried out on a regular basis, at the warehouse as well as retail outlets. Therefore, a 100% physical count is not undertaken at the year-end.

Day to day expenses of the retail outlets are paid out of cash receipts from customers. Balance cash is deposited into the bank on a daily basis.

The management accounts show that the company has not been able to achieve the sales target for the current year although the sales have increased by 12% as compared with the same period in 2010. Stocks and trade debtors have significantly increased and the management attributes this to be on account of increase in sales.

CL is planning to expand its business and intends to fund the expansion through a bank loan. CL's existing bankers have declined to increase the borrowing limits and therefore, the company has approached another banker for the loan. The management has requested you to complete the audit by 15 February 2012 to enable it to submit the audited financial statements to the new bankers.

Required:

Identify and evaluate the audit risks in the above situation and specify the audit procedures that you would perform to address those risks. *(22 marks)*

Q.2 You are the engagement partner on the audit of Faraz Industries Limited. The company has recently started using internet to carry out its business activities and the share of business conducted through e-commerce is growing rapidly.

Required:

(a) Identify the matters that you believe would be relevant while updating your knowledge of the company's business. *(04 marks)*

(b) Identify the business risks related to the company's e-commerce activities. *(09 marks)*

(c) Identify the matters that need to be addressed in order to ensure the integrity of the transactions carried out through the company's website. *(07 marks)*

Q.3 You are the quality control partner in Pirzada and Company, Chartered Accountants. The following matters are under your consideration:

- (i) Your firm has been approached for appointment as external auditors of Watto Limited (WL), a listed company. Your firm has been providing valuation services to WL.
- (ii) To evaluate the network security system of Babar Limited (BL), your firm had acquired the services of a Systems Auditor. The Finance Director of BL has accused the Systems Auditor for compromising information relating to the company's customers and providing their contact details to a competitor.
- (iii) Your finance department has issued an invoice to Qamar Software Services (QSS) against referral fees for recommending services of QSS to an assurance and a non-assurance client. Your permission has been sought before sending the bill to QSS.

Required:

Identify and evaluate the threats involved and explain what action would you take in the above circumstances including the steps required, if any, to reduce the risk to an acceptable level. *(16 marks)*

Q.4 As the audit partner responsible for the audit of Mubashar Limited (ML), you have recently issued an audit report on ML's annual financial statements.

The audit senior involved in the audit of another client Salman Limited (SL) has informed you that SL's records indicate that it has made purchases worth Rs. 37 million from ML. Since the same audit senior was also involved in the audit of ML he knows that SL and ML are associated companies and ML had not disclosed any related party transactions in its financial statements. This fact has also been confirmed from the working papers of both the companies. Payments against these purchases were made in the name of ML by way of crossed cheques.

Required:

Discuss the factors that you will consider with reference to above and specify the action that you would take in this regard. *(20 marks)*

Q.5 Ghulam Limited (GL) is a listed company. You have issued an audit report on GL's financial statements for the year ended 30 June 2011. In November 2011, the management of GL has approached your firm to provide a report on their summary financial statements for the year ended 30 June 2011.

Following information is available:

- (i) The audit report on the annual financial statements had been qualified on account of management's failure to capitalize borrowing costs of Rs. 15 million, on the construction of a building for GL's own use. The building is in use of the company since January 2011.
- (ii) Under a local regulation which has recently been introduced, you are required to issue a report on the summary financial statements. However, there are no established criteria for the preparation of summary financial statements. The management has developed the criteria but which is not acceptable to you.
- (iii) The summary financial statements include a note which explains the reasons for decline in the profitability of the company. You concur with the reasons given in the note but it did not form part of the annual audited financial statements.

Required:

Evaluate each of the above situations considering them to be independent of each other and discuss what measures would you take in each case. *(09 mark)*

Q.6 You are the manager responsible for the audit of Hafiz Limited (HL), a listed company, whose fieldwork in respect of the statutory audit is in progress. You are reviewing the following issues which were brought to your attention by the audit team:

- (i) HL's parent company is registered in a foreign country and has asked your firm to also provide an audit report on a separate set of financial statements which have been prepared under the accounting framework prevalent in that country.
- (ii) HL has paid a substantial amount of consultancy fee to a firm in another foreign country. The management of HL is unable to provide a convincing explanation for such a payment. An employee of HL has unofficially informed the audit senior that the amount was paid to avoid paying a fine. However, the management has denied this allegation.

Required:

Discuss how would you deal with each of the above issues and what may be the implications thereof on your audit report. *(13 marks)*

(The End)