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**CERTIFIED PUBLIC ACCOUNTANT  
INTERMEDIATE LEVEL EXAMINATIONS**

**I1.4: AUDITING**

**DATE: FRIDAY 29, NOVEMBER 2024**

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**INSTRUCTIONS:**

1. Time Allowed: **3 hours 15 minutes** (15 minutes reading and 3 hours writing).
2. This examination has **two** sections: **A & B**.
3. Section **A** has **Three Compulsory Questions** while section **B** has **three questions** to choose any **two**.
4. Five questions in total are to be attempted.
5. Marks allocated to each question are shown at the end of the question

## **SECTION A**

### **QUESTION ONE**

Gen Z Ltd is a listed company specialized in development, manufacturing, and selling of a range of pharmaceuticals with a significant customer-base across East Africa. M&C Associates has recently won the tender for the audit of Gen Z Ltd for the year ended on 31<sup>st</sup> December 2023. As the audit manager at M&C Associates, you are planning to carry out a discussive meeting with the finance director in order to develop the audit strategy.

From the meeting with the finance director noted the following information came your attention:

During the year the company has spent FRW 500 million in developing several new products. Some of these products are still at early stage of development whilst others are nearing completion stage. The finance director has confirmed that all product development projects are likely to be successful and so he plans to capitalize the full FRW 500 million project investment.

Once products have completed the development stage, Gen Z Ltd begins manufacturing them. At the year end it is anticipated that there will be significant levels of work in progress. In addition, the company uses a standard costing method to value inventory; the standard costs are set when a product is first manufactured and are not usually updated.

In order to fulfil customer orders promptly, Gen Z has warehouses for finished goods located across East Africa; one third of these are owned by third parties from whom Gen Z just rents space.

In September 2023, a new accounting system was introduced. This is a customized system developed by inhouse IT manager. The old and new system were not run in parallel as it was felt that this would be too burdensome for the accounting team. Two months after the system changeover the IT manager left the company; a new manager has been recruited but is yet to start his work till the time of the audit.

The reporting timetable for audit completion of Gen Z Ltd is quite short, and the finance director would like to report results even earlier this year.

In the kick off meeting, you presented the above information to the engagement team and in the presence of the engagement partner. The Audit Partner appreciated the preliminary work done and He also restated that carrying out risk assessment will help the team to gain a clear understanding of the entity and its environment and that it will eventually help the team to develop adequate and timely responses to the assessed risks.

**Required:**

- a) In accordance with ISA 315, *Identifying and assessing the risks of material misstatement through understanding the entity and its environment*, **Discuss on How the auditor would get an understanding of the entity and its environment.** (8 Marks)
- b) Using the information provided in the above case study, **discuss any SIX audit risks, and explain the auditor's response to each risk in planning the audit of Gen Z Ltd.** (12 Marks)

*Hint: Use a table to show and explain the audit risk and corresponding auditor's response*  
**(Total: 20 Marks)**

**QUESTION TWO**

Ebenezer tours and travels Ltd is a company that operates in transport industry with well-known extinguished transport services in the entire country. The company has ten booking offices in ten bus parks across different cities of the country. Due to the growing market and perceived risks by Ebenezer Tours and travels management, the company would like to carry out the extensive review of its internal control system to ensure that the all-possible control deficiencies are addressed. You are an auditor at ABG consultants and your firm has been approached by Ebenezer tours and travels Ltd management to carry out an ad hoc review of its internal control system at its booking offices.

During the engagement team discussion meeting, the audit manager has tasked with the review of cash receipts and payments system and from the information gathered during the assessment of risk of material misstatements over internal controls at booking offices, he presented you the below information for your consideration:

Each booking office is run by a booking manager and all bookings are done by cash whereby passengers pay directly to the cashier and the cashier issues the payment receipt together with bus ticket to the passenger who must present them to the bus driver before entering in the bus. The cashier then records the receipts in the cash register.

The company works hand in hand with agents in the bus parks who looks for passengers, once the agent brings a passenger at any of Ebenezer tours and travel ltd booking office, a 10% commission is immediately calculated and remitted in cash to the agent by the cashier after the ticket issue.

The cashier is responsible for weekly cash count and provide a report of all cash sales and remittances which is to be prepared every Friday and shared with the booking manager before the cashier takes the money to the bank. The bank deposit receipt is then returned and has to be stamped by the booking manager before the cashier files it.

Each booking office is allowed to maintain a petty cash facilitation to allow them settle small urgent payments, the threshold for any petty cash payment is Frw 50,000, the cashier is allowed to pay it and report all weekly petty transactions to the booking manager before she claims back to the head office for replenishment which is supposed to be Frw 500,000 maximum.

At the year end, to help head office finance department while preparing annual financial statements, each booking office is supposed to carry out a cash count exercise which is done by the cashier and the sales person at the booking office, they then produce and counter-sign a cash certificate which to be shared to the head office via email by the booking manager.

**Required:**

- a) In accordance with the information provided above, **develop an audit program that you will use to review the cash receipts and payments system at booking offices of Ebenezer tours and travels Ltd.** (20 Marks)

*Hint: Use a table to show the relevant assertion, control objective, control and a test of control*

**(Total: 20 Marks)**

**QUESTION THREE**

Corporate governance is a crucial aspect of ensuring the effective management, accountability, and transparency of companies. A series of high-profile corporate scandals and fraudulent activities in the 1980s and 1990s, such as those involving Enron, WorldCom, and other major corporations, highlighted the need for enhanced corporate governance frameworks globally. These events prompted many countries to introduce voluntary codes of best practice to enforce sound governance, encourage ethical conduct, and protect shareholders' interests. Among these codes, the Cadbury Report (1992) and the Combined Code (1998) are two prominent frameworks that have been influential in shaping corporate governance practices worldwide.

**Required:**

- a) **Highlight how corporate scandals have influenced the development of governance codes.** (4 marks)
- b) **Analyze the key principles and recommendations of the Cadbury Report and the Combined Code, and evaluate their applicability in today's corporate landscape. In your answer, provide examples of how these codes have been implemented and their impact on improving transparency, accountability, and shareholder confidence.** (10 Marks)
- c) **Discuss the significance of sound corporate governance in the context of the global business environment.** (6 marks)

**(Total: 20 Marks)**

## **SECTION B**

### **QUESTION FOUR**

ISA 520 “*Analytical procedures*” define the term analytical procedures as evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

#### **Required:**

- a) In accordance with the above ISA, **Explain the factors to be considered by the auditor when deciding to use analytical procedures.** (6 marks)
- b) **Discuss on matters to consider when determining whether data is reliable for purposes of designing substantive analytical procedures.** (8 Marks)
- c) ISA 580 *written Representations*, states that with regards to the preparation of the financial Statements, the auditor shall request management to provide a written representation that it has fulfilled its responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation, as set out in the terms of the audit engagement.

#### **Required:**

In accordance to the ISA 580, **Discuss the auditor’s objectives with regards to written representations.** (6 Marks)

**(Total: 20 Marks)**

## QUESTION FIVE

Your firm is at nearly completion stage of the audit of NMG Ltd for the year ended 31<sup>st</sup> December 2023, NMG Ltd is a group of companies that deal with real estate business. The client would like the audited financial statements and the audit report to be signed urgently to secure source of funds for the government's green funding grants. The draft financials show that the revenue for the year is Frw 5,000 million and with a profit before tax of Frw 1,500 million.

The following information comes to your attention:

Two real estate projects that were underway were heavily damaged following the floods from an extensive rain on 15<sup>th</sup> January 2024. The management of group engaged the insurance company but no amendments or disclosures notes have been made in the financial statements.

A major supplier of NMG Ltd sued the group for breach of contract. The lawsuit was filed before the year end and the plaintiff claims the sum of Frw 1,000 million. The relevant disclosure was done in the notes to the financial statements as a contingent liability. However, the supplier has recently contacted the legal department that he is willing to settle the case for a payment of Frw 600 million by NMG Ltd.

The Chief Financial Officer of the group has recently informed the engagement partner that he was contacted by the bank that the overdraft facility that the group had will not be renewed. The group does not have any other source of finance apart from the targeted green grant which also not assured.

### Required:

- a) With the use of examples, **Differentiate adjusting from non-adjusting events.** (3 marks)
- b) In line with the above case study, **Explain the audit procedures you will perform to test the above subsequent events.** (10 marks)
- c) An auditor must perform and document an overall review of the financial statements before making an audit opinion. This review, along with the conclusions drawn from other audit evidence obtained, gives the auditor a reasonable basis for his opinion on the financial statements. It needs to be carried out by a senior member of the audit team, who has the appropriate skills and experience.

**Required:**

- i) In accordance with ISA 450 *Evaluation of Misstatements Identified during the Audit*, **Define the term “misstatement”**. (2 Marks)
  - ii) **Explain any five areas of consideration by the auditor to perform an overall review of the financial statements before making an audit opinion.** (5 Marks)
- (Total: 20 Marks)**

**QUESTION SIX**

You have been approached by a junior auditor in your audit team who has been tasked by the audit manager to audit the balance of trade receivables reported in the financial statements of Wilson & Sons Ltd. He had carried out internal controls review on sales and invoicing system of the client and decided that no reliance should be placed on them and hence he concluded to undertake substantive procedures. The audit manager has altered him that the key assertions for the audit of receivable are completeness, accuracy, existence, rights and obligations and valuation. He then seeks for your support to help him come up with proper substantive audit procedures that would help him gather enough and appropriate audit evidences on each of the above key assertions.

**Required:**

- a) In line with the above, **explain to the Junior auditor, the substantive audit procedures to be performed on each of the above key assertions for the audit of trade receivables reported in financial statements of Wilson & Sons Ltd.** (14 Marks)
- b) You are a senior auditor at B&D Consultants, you are in the process of reviewing the payroll cycle of Kamango Industries Co, as well as preparing the audit program for its final audit.

Below is a description of the payroll system along with deficiencies identified by the audit manager during the audit planning stage:

- ✓ The company operates three shifts every day with employees working eight hours each. They are required to clock in and out using an employee swipe card, which identifies the employee number and links into the hours worked report produced by the computerised payroll system.
- ✓ Employees are paid on an hourly basis for each hour worked. There is no monitoring of the clocking in/out process and an employee was recently witnessed clocking in for several employees using their employee swipe cards.
- ✓ The payroll department calculates on a weekly basis the cash wages to be paid to the workforce, based on the hours worked report multiplied by the hourly wage rate, with appropriate tax deductions. These calculations are not checked by anyone as they are generated by the payroll system. During the year the hourly wage was increased by the Human Resources department and this was notified to the payroll department verbally.

- ✓ Each Friday, the payroll department prepares the pay packets and physically hand them over to the workers who operate the morning and late afternoon shifts. However, for those who work night shift, the pay packets are given to the factory supervisor to distribute. If any night shift worker is absent on pay day, then the factory supervisor keeps his/her wage and returns it to the payroll department on Monday.

**Required:**

**Describe the substantive procedures you would perform to confirm the accuracy and completeness of Kamango industries Co's payroll system.**

(6 Marks)

**(Total: 20 Marks)**

**End of question paper.**