



Audit and Assurance

- Q.1 You have been assigned the audit of Sukkur Limited (SL), a listed company, for the year ended 31 December 2016. The company engaged in the business of manufacturing security equipment for the local market. During the planning phase, while reviewing the previous year's audit file, you have noted that in 2015, due to introduction of many new equipment in the market and changes in technology, SL faced stiff competition and its market share reduced from 45% to 35%. However, the management has now informed you that SL has made significant investment in technology which has helped the company to increase the market share to 38% in 2016.

The following information has been extracted from the draft financial statements:

Extracts from the statement of comprehensive income

	2016 (draft)	2015 (audited)	2014 (audited)
----- Rs. in million -----			
Revenue	10,742	9,703	9,650
Cost of sales	8,050	7,177	6,740
Financial charges	750	600	350
Profit before tax	1,550	1,601	2,260

Extracts from the statement of cash flows

	2016 (draft)	2015 (audited)	2014 (audited)
----- Rs. in million -----			
Cash flows from operations	(3,361)	(1,948)	(585)
Cash flows from financing activities	4,000	3,500	1,500

Required:

- (a) Identify any **four** fraud risk factors in the above scenario. (04)
- (b) Identify **four** audit risks which the auditor should consider while planning the audit. (06)

- Q.2 (a) During the audit of Shahbaz Chemicals Limited (SCL) for the year ended 31 December 2016, the audit team had noticed that sales of SCL has declined due to various reasons and SCL is facing difficulties in selling the existing stock of inventory at current price levels.

Required:

Explain the steps which the auditor should perform to ensure that carrying value of inventories is based on lower of cost and net realisable value. (04)

- (b) Express Limited is a medium size entity engaged in trading of electronic appliances. After the issuance of financial statements and audit report for the year ended 30 June 2016, a major debtor was declared bankrupt by the Court. No recovery has been made from the debtor after year-end.

Required:

Evaluate the above situation and state the procedures which the auditor would need to perform. (08)

- Q.3 You are the audit partner in a firm of chartered accountants. Some of the audits are in the finalization stage and presently the following matters are under your consideration:
- (a) The management of Sohni Limited has changed its revenue recognition policy. As the audit engagement partner you are satisfied with the accounting and disclosures related to change in accounting policy. Further, the impact of the change is significant. (04)
 - (b) There is a legal dispute between Marvi Limited and one of its customers. In this regard, the legal advisor has confirmed the stance of the management in a meeting with you. However, he has refused to provide a written confirmation thereon. (02)
 - (c) The management of Laila Limited is not willing to make certain disclosures. The management is of the view that these disclosures will not add any value to the financial statements. Further, the information required to make these disclosures cannot be compiled before the deadline for completion of the audit. (04)

Required:

Discuss the possible impact on the audit report and specify the procedures (if any) which you would undertake in the above situations.

- Q.4 Discuss the categories of threats and related safeguards in each of the following situations:
- (a) An unlisted audit client which has recently been incorporated has requested your firm to assist the finance department in the preparation of financial statements. (03)
 - (b) Saleem has recently been promoted as a partner and the audit of TTL has been assigned to him. TTL owns and operates a chain of restaurants. The following matters are under his consideration:
 - (i) Asif has been involved in the audit of TTL as audit senior for the last three years. He has recently qualified as chartered accountant and Saleem wants to appoint him as audit manager.
 - (ii) TTL's management has requested Saleem to include Rashid, a semi-senior, in the audit team. Rashid is the son of TTL's Marketing Director.
 - (iii) The firm has long cordial relationship with the management of TTL. Saleem has noticed that the firm often uses the restaurants run by TTL for conducting its internal functions. (07)

- Q.5 You are the audit senior on the audit engagement of Farhan Foods Limited and assigned to attend the inventory count.

Required:

- (a) State what matters you would consider while observing the inventory count. (05)
 - (b) State the procedures to be performed during the final audit in relation to the cut-off assertions for sales and purchases. (03)
- Q.6
- (a) List any **four** situations that may require revision in the terms of audit engagement letter. (04)
 - (b) Discuss the concepts of stewardship and accountability in the context of a limited company and fair presentation (true and fair view) in relation to the financial statements. (06)
 - (c) Discuss the course of action which may be adopted by the auditor if pre-conditions of audit are not present. (04)
 - (d) State the factors which determine the extent to which an auditor may use Analytical procedures as a form of substantive audit evidence. (04)

- Q.7 You are currently in the planning phase of the audit of Fresh Dairies Limited (FDL) for the year ended 31 December 2016. The information available to you in respect of the company's debtors includes the following:

Customer category	Number of customers	Balance outstanding (Rs. in '000)	Percentage of customers who confirmed the balance last year
Distributors	20	30,500	90%
Wholesalers	2,250	12,750	70%
Restaurants	12	20,400	83%
Individual customers	5,700	9,800	20%
		73,450	

FDL is a low risk client and therefore you are assessing whether to send negative confirmation requests.

Required:

In respect of each of the above categories of customers, discuss the appropriateness of sending negative confirmation requests. (09)

- Q.8 (a) Briefly state the course of action which should be adopted by a firm if the requested written representations are not provided by the client. (02)
- (b) You are the audit manager at Afzal Textile Mills Limited (ATML). While reviewing the draft financial statements and the working paper file, the following matters have come to your attention:
- There is a significant decline in the number of related parties and related party transactions.
 - During the year, ATML has acquired 15% shareholding in Bashir Textiles Limited, a listed company.
 - ATML owns six buildings out of which four have been revalued during the current year while the remaining buildings would be revalued next year.

Required:

Discuss whether it would be necessary to obtain management representation in respect of the above matters. (06)

- Q.9 (a) Differentiate between General IT controls and Application controls. Also give two examples of each type of control. (06)
- (b) Discuss the effects on Application controls where General IT controls are ineffective. (03)

- Q.10 Comment on each of the following situations with reference to the appointment of external auditors in accordance with the requirement of the Companies Ordinance, 1984.

- (a) Bilal and Company, Chartered Accountants has received an offer for appointment as auditor of Dawood Limited (DL). Ghalib, a partner in Bilal and Company holds 100,000 Term Finance Certificates of DL. (03)
- (b) Zain and Company, a firm of Chartered Accountants, has received an offer for appointment as auditor of Haris Limited (HL). Imran, a partner in Zain and Company is also a partner in Pure Investment Associates, a partnership firm, which owns 100,000 shares in HL. (03)

(THE END)