

TECHNICAL UNIVERSITY OF MOMBASA

SCHOOL OF BUSINESS

ACCOUNTING AND FINANCE DEPARTMENT

**COURSE/CLASS: BACHELOR OF BUSINESS ADMINISTRATION
BACHELOR OF COMMERCE**

UNIT : BAC 4302

UNIT NAME : AUDITING

SERIES : MAY 2016

TIME : 2 HOURS

INSTRUCTIONS TO CANDIDATES:

Answer Question One (Compulsory) and any other TWO questions.

QUESTION 1 (COMPULSORY)

- (a) International standard on auditing (ISA300), Planning an Audit of Financial Statements states that an auditor must plan the audit.
Explain why it is important to plan an audit. (6 marks)
- (b) The objectivity of the external auditor may be threatened or appear to be threatened where:
- There is undue dependence on any audit client or group of clients.
 - The firm, its partners or staff have any financial interest in an audit client.
 - There are family or other close personal or business relationships between the firm, its partners or staff and the audit client.
 - The firm provides other services to audit clients.

Required:

- For each of the four examples given above, explain why the objectivity of the external auditor may be threatened, or appear to be threatened, and why the threat is important. (7 marks)
 - Describe requirements that reduce the threats to auditor objectivity for each of the four examples given above. (7 marks)
- (c)
- What is audit sampling?
 - Distinguish between audit risk and sampling risk.
 - What conditions are necessary to carry out sampling?
 - What should the auditor consider before relying on the work of an expert?
 - List and explain the qualities of a good sample. (10 marks)

QUESTION 2

- (a) Describe the matters to consider within your firm and the other procedures that must be undertaken before accepting the appointment as auditor to a new client. (7 marks)
- (b) Explain why it would be inappropriate to commence the audit before consideration of the matters and the procedures referred to in (a) above have been completed. (4 marks)
- (c) Explain the purpose of an engagement letter and list its contents. (9 marks)

QUESTION 3

You are a recently qualified Certified Public Accountant in charge of the internal audit department of ZX co. Ltd., a rapidly expanding company. Turnover has increased by about 20% p.a. for the last five years, to the current level of Ksh.500 million. Net profits are also high, with an acceptable return being provided for the shareholders. The internal audit department was established last year to assist the board of directors in their control of the company and to prepare for a possible listing on the stock exchange. The Managing director is keen to follow the principles of good corporate governance with respect to internal audit. However, he is also aware that the other board members do not have complete knowledge of corporate governance or detailed knowledge of International Auditing Standards.

Required:

Write a memo to the board of ZX co. Ltd that:

- (a) Explains how the internal audit department can assist the board of directors in fulfilling their obligations under the principles of good corporate governance. (14 marks)
- (b) Explain the advantages and disadvantages to ZX of an audit committee. (6 marks)

QUESTION 4

The responsibilities of internal and external auditors in relation to the risk of fraud and error differ.

Required:

Discuss the responsibilities of external auditors in respect of the risk of fraud and error in an audit of financial statements. (20 marks)

QUESTION 5

The Auditors Operational Standard requires that the auditor to obtain relevant and reliable audit evidence sufficient to enable him to draw reasonable conclusions therefrom.

Required:

- (a) What is audit evidence?
- (b) Explain the meaning of the following terms:
 - Relevant audit evidence (3 marks)
 - Reliable audit evidence (3 marks)
- (c) Explain whether the following types of audit evidence meets the standards of relevancy, reliability and sufficiency as required by the auditor's operational standards regarding:
 - Written confirmation of a trade debtor circularized at year end. (3 marks)
 - Work-in-progress inventories identified during the annual physical stock count.
 - Solicitors letter confirming pending legal action. (3 marks)