

EXAMINATION NO. _____



2016 EXAMINATIONS

ACCOUNTING TECHNICIAN PROGRAMME

PAPER TC 7: AUDITING

WEDNESDAY 30 NOVEMBER 2016

**TIME ALLOWED : 3 HOURS
2.00 PM – 5.00 PM**

INSTRUCTIONS

1. You are allowed **15 minutes** reading time **before the examination begins** during which you should read the question paper and, if you wish, make annotations on the question paper. However, you are **not** allowed, **under any circumstances**, to open the answer book and start writing or use your calculator during this reading time.
2. Number of questions on paper – 7.
3. **FIVE** questions **ONLY** to be answered.
4. The paper is divided into Sections **A** and **B**. **Question one** is compulsory, and the candidates are required to answer **ANY FOUR** questions from Section **B**.
5. Each question carries 20 marks.
6. Begin each answer on a fresh page.
7. **DO NOT OPEN THIS PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR**

This question paper contains 6 pages

This question paper must **not** be removed from the examination hall.

SECTION A

This question is compulsory and MUST be attempted

1. Pompano Ltd operates an integrated computerized accounting system controlled from its head office in Lilongwe. Data is captured at various terminals within the accounts departments and various reports are produced. Printouts are sometimes produced for various ledgers or reports when hard copies are needed.

You are also informed that the programs have been designed with a number of internal checks in order to eliminate erroneous inputs and restrict access to the system by unauthorised users.

Required:

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|---------|--|----------------------------------|
| (a) (i) | Define the term “audit trail”. | 2 Marks |
| (ii) | Give an example of an audit trail. | 1 Mark |
| (b) | State three reasons why an audit trail may easily get lost in a computerized accounting system. | 3 Marks |
| (c) | What is the meaning of the terms “audit through the computer” and “audit around the computer” and state when each one is suitable. | 6 Marks |
| (d) | Define the following terms:

(i) General controls
(ii) Application controls | 1 Mark
1 Mark |
| (e) | Give three examples of each of the following terms:

(i) General controls
(ii) Application controls | 3 Marks
3 Marks |

(TOTAL : 20 MARKS)

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SECTION B

FOUR questions ONLY to be answered from this section

2. Lengwe CA have been approached by Nyala Ltd, a newly incorporated company, to be appointed as their auditors for the coming financial year.

In a briefing meeting, in response to the directors' request to understand what exactly an audit involves, the partner explains that it involves designing and conducting an audit to obtain sufficient appropriate evidence to state whether the financial statements of a client show a true and fair view.

When one of the directors asked for further clarification on what is meant by *true and fair view*, the partner responded in short: *whether the financial statements are credible or represent the entity's true results and reflect its state of affairs in a certain period*. He felt short of saying: to certify whether the financial statements are accurate.

This led to some dissatisfaction by the directors of Nyala Ltd.

Required:

- (a) Define the term "audit expectation gap". **3 Marks**
- (b) Give any **four** reasons why it would be inappropriate for the auditor to offer a stronger assurance, such as to certify that the financial statements are accurate. **8 Marks**
- (c) Give any **two** suggestions on how the auditor can reduce the expectation gap. **4 Marks**
- (d) Despite the existence of the expectation gap, an audit is still useful to an entity.

Required:

State any **five** benefits that may be accrued from an audit. **5 Marks**
(TOTAL: 20 MARKS)

3. Mr Kampango, Managing Director of Chembe Ltd, has approached the partner of your audit firm expressing his intention to appoint the firm as auditors of his company. In return for giving you business, he says he will expect your firm to waive 50% of your normal fees for the first year's audit. The existing auditors have not resigned, but the managing director has informed you that they will not be reappointed at the next annual general meeting of the company.

Required:

- (a) Explain the procedure that you should follow before accepting or declining the appointment as auditors of Chembe Ltd. **5 Marks**

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- (b) What action should your firm take in response to Mr Kampango's request to reduce the normal fees by 50% for the first year? **5 Marks**
- (c) Explain the **two** general procedures of appointing a new audit firm from the current audit firm as stipulated in the Companies Act (1984). **5 Marks**
- (d) Is the current audit firm acting within its right not to resign when it knows that the managing director wishes to replace it? Give **five** reasons for your argument. **5 Marks**
(TOTAL: 20 MARKS)

4. Your firm has been auditors of Kwaela Ltd for the past three years. You have just finalized the audit of their financial statements for the year ended 31 March 2016, and you have indicated in your audit report that their financial statements show a true and fair view, which you are to present in their annual general meeting to be held on 30 June.

Meanwhile, you have read from the media that Kwaela has been taken over by new shareholders, a holding company with a number of subsidiaries. They want to standardize Kwaela with other subsidiaries by introducing the latest integrated organizational performance, financial management and reporting information system programmed in a high level programming language known as the common business oriented language (COBOL).

You are currently faced with two main uncertainties:

- Firstly, whether the new holding company will reappoint your firm in the coming annual general meeting for the coming year's audit.
- Secondly, if reappointed, whether you will be able to successfully obtain sufficient appropriate evidence to arrive at a reasonable conclusion on the company's financial statements in the new system.

Required:

- (a) State the professional ethical provisions with regard to competence and due skill. **5 Marks**
- (b) State the **four** courses of action that the auditor can take in the above scenario. **4 Marks**
- (c) State and explain the **four** other key principles contained in the code of ethics. **8 Marks**
- (d) An auditor uses judgment in a number of circumstances in the course of his/her audit work.

Required:

State any **three** issues in which the auditor uses professional judgment. **3 Marks**
(TOTAL: 20 MARKS)

5. ISA 300 on audit evidence requires that the auditor should obtain sufficiently appropriate evidence to arrive at a reasonable conclusion on the financial statements of an entity.

Required:

- (a) Define the term “audit evidence”. **2 Marks**
- (b) State **five** reasons why documented audit evidence is important to the firm. **5 Marks**
- (c) Define the term “audit sampling”. **2 Marks**
- (d) State the **four** factors that the auditors should consider when deciding to rely on:
- (i) an internal auditor’s work; **4 Marks**
- (ii) expert work. **4 Marks**
- (e) (i) Define the term “internal controls”. **2 Marks**
- (ii) State any **two** types of controls in an entity. **1 Mark**
- (TOTAL : 20 MARKS)**

6. You are a member of an audit team that is currently conducting a final audit of Mbenje Ltd, a company engaged in retail trade.

Required

Explain how the following items, appearing in the financial statements of the company, can be verified:

- (a) Payables **8 Marks**
- (b) Wages and salaries **6 Marks**
- (c) Prepayments and accrued expenses **6 Marks**
- (TOTAL: 20 MARKS)**

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7. Kangachepe Ltd, one of your audit clients, is involved in retail trade of a wide range of products. Its annual audit is nearly complete. As audit senior, you have reported to the engagement partner that the company is having financial difficulties. Income has fallen due to the adverse effects of two high-profile court cases, where the company's products were found to be defective but the company had initially refused to compensate its customers. Not only did this provide adverse publicity for the company, but a number of clients stopped buying from the company. The Chief Executive Officer (CEO) and the Finance Manager have since resigned from the company and are yet to be replaced.

A cash flow forecast prepared internally shows that the company requires significant additional cash within the next 12 months to maintain even the current level of services. You have also sought assurances from the directors about the possible recovery from the current situation.

Required:

- (a) (i) Define the term "going concern". **2 Marks**
- (ii) Mention any **two** responsibilities of the auditor in respect of going concern. **2 Marks**
- (b) State any **four** audit procedures that may be carried out to try to determine whether or not Kangachepe Ltd is a going concern. **8 Marks**
- (c) Explain the **four** audit procedures that the auditor may take where the auditor has concluded that Kangachepe Ltd is unlikely to continue trading as a going concern. **8 Marks**
- (TOTAL : 20 MARKS)**

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