



**CPA PART II SECTION 4**  
**AUDITING AND ASSURANCE**

**FRIDAY: 27 November 2020.**

**Time Allowed: 3 hours.**

**Answer ALL questions. Marks allocated to each question are shown at the end of the question.**

**QUESTION ONE**

- (a) International Standard on Auditing (ISA) 505 – External confirmations, considers a number of different types of external confirmations including accounts receivable confirmations.

**Required:**

- (i) Distinguish between a “positive confirmation” and a “negative confirmation”. (4 marks)
- (ii) Evaluate four circumstances, other than the confirmation of accounts receivable, where external confirmations might be used by the auditor to obtain audit evidence. (4 marks)

- (b) International Standard on Auditing (ISA) 315 – Identifying and assessing the risks of material misstatement through understanding the entity and its environment, sets out matters that should be documented during the planning stage of an audit.

**Required:**

Highlight six matters that should be documented when developing an audit plan. (6 marks)

- (c) International Standard on Auditing (ISA) 230 – Audit Documentation, provides guidance to auditors in respect of audit working papers.

**Required:**

Summarise six factors which could affect the form and content of audit working papers. (6 marks)

**(Total: 20 marks)**

**QUESTION TWO**

- (a) An overall audit strategy guides the auditor in developing an audit plan.

**Required:**

Examine four matters that might be taken into consideration by an auditor when developing the overall audit strategy. (8 marks)

- (b) Describe five motives for fraudulent financial reporting by the management of an entity. (5 marks)

- (c) Other than in fraud detection, suggest four other areas where forensic accounting and auditing might be applied. (4 marks)

- (d) Evaluate three approaches used in performance auditing in the Public Sector. (3 marks)

**(Total: 20 marks)**

**QUESTION THREE**

- (a) (i) Distinguish between “tests of control” and “substantive tests”. (4 marks)

- (ii) Describe six tests of control that an auditor might carry out in the course of his audit assignment. (6 marks)

- (b) Any work delegated to audit assistants should be directed, supervised and reviewed in a manner which provides reasonable assurance that such work is performed competently.

**Required:**

Examine four matters that might be taken into consideration when reviewing the work performed by audit assistants in an audit engagement. (4 marks)

- (c) Your audit firm is currently engaged in the audit of Zed Ltd. for the financial year ending 30 November 2020. You are considering whether to perform certain tests manually or with the assistance of computer assisted audit techniques (CAATs).

**Required:**

Discuss three factors that could influence your decision on whether to perform the tests manually or with CAATs. (6 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

- (a) Your friend James Nyakemincha has recently purchased some shares from ABC Ltd., a listed company at the Securities Exchange. You questioned him on whether he had investigated the company before purchasing the shares. He replied: "Not really, I chose ABC Ltd.'s shares because I read in the newspaper that ABC is externally audited, of which not all companies are, and that their auditors are an international auditing firm hence it must be a good investment".

**Required:**

Citing five reasons, justify why you would agree or disagree with James' view with regard to his purchase of shares. (10 marks)

- (b) Discuss five mechanisms that the management of an audit firm could use to ensure compliance with the professional code of ethics by members of staff. (10 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

- (a) In terms of International Standard on Auditing (ISA) 700 - Forming an opinion and reporting on financial statements; in evaluating whether the financial statements are presented fairly in the context of the financial reporting framework, the auditor should evaluate important aspects of the financial statements.

**Required:**

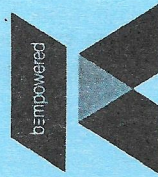
Identify five aspects of the financial statements which the auditor should evaluate. (5 marks)

- (b) Describe five audit assertions you would test in the conduct of an audit of office furniture and equipment. (10 marks)

- (c) Explain five reasons why directors might decide not to correct a material misstatement in the financial statements. (5 marks)

**(Total: 20 marks)**

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CPA PART II SECTION 4  
AUDITING AND ASSURANCE

WEDNESDAY: 27 November 2019.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

QUESTION ONE

- (a) Lingo Ltd. was recently incorporated. It will be operating in the retail sector. The company has five directors and is currently in the process of setting-up in order to commence business on 1 January 2020. The directors of the company are considering outsourcing the internal audit function in the interim period instead of recruiting their own staff.

**Required:**

Analyse six advantages to Lingo Ltd. of outsourcing the internal audit function. (6 marks)

- (b) In relation to audit investigations:

(i) Highlight six characteristics of audit investigations. (6 marks)

(ii) Evaluate eight reasons why audit investigations might be conducted. (8 marks)

(Total: 20 marks)

QUESTION TWO

- (a) The completeness assertion is always the most difficult for the auditor to assess, particularly in relation to provisions and contingent liabilities.

**Required:**

Describe six steps that might be undertaken by the auditor to confirm unrecorded liabilities. (6 marks)

- (b) You work as an audit senior for Kamau Mengo and Associates. You have been appointed to be the lead auditor of Tamu Tamu Ltd. for the financial year ended 31 October 2019. Tamu Tamu Ltd. specialises in the production of biscuits and cakes.

During preliminary audit work, you noted that the profitability of the company declined, costs increased and prices charged were higher than those of competitors. This was due to low levels of output. In recent years, Tamu Tamu Ltd. has been financing its operations using a bank overdraft facility. This issue was raised during a meeting between the auditors and Tamu Tamu Ltd.'s management.

During this meeting, a discussion took place which focused on actions that could be taken by the management to improve the liquidity of the company. The management team informed you of a plan to expand facilities for producing biscuits, as this line of production had maintained its market share. Tamu Tamu Ltd. has applied for a bank loan to finance this expansion and also maintain the present level of working capital.

To support its request for a loan, the company has prepared a cash flow forecast for the two years from the end of the reporting period. The internal audit department has submitted a report on this forecast to the board of directors. However, the bank has said it would like a report from the external auditors, to confirm the reasonableness of the forecast.

Following this request, the company has requested you to examine the cash flow forecast and write a report to the bank.

**Required:**

(i) Describe three levels of assurance that could be included in your response to the bank's request. (6 marks)

(ii) Assess eight procedures that could be adopted to examine the cash flow forecast. (8 marks)

(Total: 20 marks)

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### QUESTION THREE

- (a) Your firm, JM and Associates, has just concluded an external audit on Familia Medical Services Ltd. Based on the audit findings, JM and Associates issued an unqualified report to the company.

**Required:**

- (i) Explain the term “unqualified opinion”. (2 marks)
- (ii) Suggest five matters that could be included in your unqualified report to the company. (5 marks)
- (b) In relation to auditing in a computerised environment:
- (i) Explain the term “test data”. (2 marks)
- (ii) Analyse two uses of test data when auditing a computerised environment. (2 marks)
- (c) Distinguish between “tolerable error” and “expected error”. (4 marks)
- (d) (i) Explain the term “inherent risk”. (1 mark)
- (ii) Highlight four factors that could result in an increase in inherent risk of a business. (4 marks)

**(Total: 20 marks)**

### QUESTION FOUR

- (a) In the context of International Standard on Auditing (ISA) 560 – Subsequent Events:

- (i) Distinguish between “adjusting events” and “non-adjusting events” giving an example in each case. (4 marks)
- (ii) Analyse the relationship between “going concern” and “non-adjusting event”. (2 marks)
- (b) The financial reporting year of Kipengo Ltd., ends on 31 October. The financial statements of the company for the year ended 31 October 2019 are due to be approved on 15 December 2019. You were appointed to carry out the audit assignment and arising from your audit work, the following events have come to your attention:
1. On 5 November 2019, Kipengo Ltd. sold inventory for a price which was less than its cost price. (The inventory had been recorded in the financial statements as closing inventory).
  2. Kipengo Ltd. issued new shares on 7 November 2019.
  3. A fire in the warehouse destroyed all of Kipengo Ltd.’s inventory on 10 November 2019.
  4. A major customer who owed Kipengo Ltd. Sh.3,000,000 as at 31 October 2019 was declared bankrupt on 12 November 2019.
  5. On 23 November 2019, Kipengo Ltd. Purchased an asset worth Sh.1,600,000.

**Required:**

Review each of the events above. Advise, with reasons, if the event is an adjusting or non-adjusting event and the action to be taken (if any) on Kipengo Ltd.’s financial statements. (10 marks)

- (c) Describe four objectives of public sector auditing. (4 marks)

**(Total: 20 marks)**

### QUESTION FIVE

- (a) You have recently been appointed as the auditor of Sugo Ltd. for the financial year ended 30 June 2019.

**Required:**

Examine eight reasons why it is important for your audit firm to review Sugo Ltd.’s internal control system prior to undertaking verifications of transactions. (8 marks)

(b) Kaka Kimenju & Co. is an international audit firm with a number of clients listed on the securities exchange. Recently, the firm held a staff training session on quality control. During the meeting, the members of staff were invited to raise matters from their past experiences relating to the ethical code on independence. Some of the matters raised are outlined below:

1. Shortly before commencing the final audit of AKZ Ltd., a listed company, a junior staff member on the audit team inherited a substantial number of shares in that company. No action was taken because, although representing a large investment for the staff member concerned, the number of shares were totally immaterial with respect to the company. Moreover, the partner knew that when the company's results would be announced, the share price would rise and he did not think it was fair to require the staff member to sell them before hand.
2. The management accountant of ABC Ltd., a listed client, had an accident and was away from work for three months. At the time of the accident, the audit senior was winding up the prior year's audit. Given his familiarity with the company's management accounting system, it was agreed that he would take over as the management accountant for the three months.
3. Kaka Kimenju & Co. warned its client, MKN Ltd., that its computer system lacked essential controls. Subsequently, MKN Ltd., decided to install a totally new system and Kaka Kimenju and Co.'s management consultancy department was appointed to design the new system.

**Required:**

Evaluate whether Kaka Kimenju & Co. had complied with the ethical code on independence or had acted unprofessionally in any other way with respect to each of the above scenarios. (12 marks)

(Total: 20 marks)

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CPA PART II SECTION 4  
AUDITING AND ASSURANCE

THURSDAY: 23 May 2019.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

**QUESTION ONE**

The Finance Director of Usonga Ltd. has informed you that some fraud took place during the year in the company's payroll department. A number of fictitious employees were set up on the payroll and wages were paid into one bank account that belonged to two supervisors who have recently resigned. One of the supervisors had the sole responsibility for setting up new entrants in the payroll system, while the other supervisor processed and authorised bank transfer requests for wages and supplier payments.

The finance director has requested your audit firm for recommendations on how to improve controls in this area to prevent this type of fraud recurring. Usonga Ltd. has recently established a Human Resources department.

**Required:**

- (a) Explain three types of control that Usonga Ltd. could put in place to reduce the risk of the above fraud recurring. For each control, describe how it would mitigate the risk. (12 marks)
- (b) Describe four procedures which you would perform to assess whether Usonga Ltd. is a going concern. (8 marks)
- (Total: 20 marks)**

**QUESTION TWO**

- (a) Describe three responsibilities of an auditor in the audit of general purpose financial statements. (6 marks)
- (b) The Finance Director of Kijanj Industries has requested your firm to undertake a non-audit assurance engagement later in the year. Part of your team includes an audit assistant who has not been involved in such an assignment before and has asked you to explain what an assurance engagement involves.

**Required:**

Explain three key elements of an assurance engagement. (6 marks)

- (c) In the context of modifying an audit opinion, the auditor might either conclude that:
- (i) Based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement;
- Or
- (ii) As a result of being unable to obtain sufficient and appropriate audit evidence, the financial statements as a whole are not free from material misstatement.

**Required:**

Differentiate between the two audit conclusions above. (4 marks)

- (d) Outline four safeguards that an audit firm could implement to address potential conflicts of interest when auditing two competing clients. (4 marks)
- (Total: 20 marks)**

**QUESTION THREE**

- (a) In the context of International Standard on Auditing (ISA) 620 relating to reliance on the work of an expert:
  - (i) Describe two situations where an auditor might need to rely on the work of an expert. (2 marks)
  - (ii) Explain three factors taken into consideration by an auditor when placing reliance on the work of an expert. (6 marks)
- (b) Examine four contents of working papers in circumstances where the auditor has used analytical procedures as substantive tests in carrying out his audit engagement. (4 marks)
- (c) As an audit assistant engaged in the audit of Samawati Ltd., you have been assigned the audit of non-current assets. The company has a substantial number of items of plant and machinery in its books of account.

**Required:**

- (i) Summarise two objectives of an internal control system over the company's non-current assets. (2 marks)
- (ii) Discuss three internal control procedures you would recommend to the company to safeguard its investments in non-current assets. (6 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

- (a) With reference to an auditor's report, examine the matters that are included in the following paragraphs:
  - (i) Basis for opinion. (3 marks)
  - (ii) Key audit matters. (3 marks)
- (b) Citing two examples, explain the term "fraudulent financial reporting". (3 marks)
- (c) Discuss four circumstances which might cause an auditor to change his risk assessment of a client company. (8 marks)
- (d) Examine the importance of materiality assessment to an auditor. (3 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

- (a) Describe three components of an entity's internal control system. (6 marks)
- (b) (i) Explain the term "reasonable assurance" as used in auditing. (2 marks)
- (ii) The internal audit function of an entity should have an internal audit charter approved by the Board to govern its activities:

**Required:**

As an internal auditor of Zed Ltd., discuss six matters contained in an internal audit charter of an entity. (12 marks)

**(Total: 20 marks)**

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CPA PART II SECTION 4  
AUDITING AND ASSURANCE

THURSDAY: 29 November 2018.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

**QUESTION ONE**

- (a) Analyse two types of threats that might arise from an audit firm accepting to undertake non-audit related services to its client. (4 marks)
- (b) In the context of the Companies Act, outline four statutory rights of an auditor. (4 marks)
- (c) Explain the term “negative assurance” as used in auditing. (2 marks)
- (d) With reference to an auditor’s report, discuss five matters that should be included in the “auditor’s responsibilities for the audit of the financial statements” paragraph. (10 marks)

**(Total: 20 marks)**

**QUESTION TWO**

- (a) Auditors should obtain written confirmation of representations from management on matters material to the financial statements.

**Required:**

- (i) Explain four reasons why an auditor should discuss the contents of the letter of representation with the directors of a client at an early stage in the audit. (8 marks)
- (ii) Analyse three responsibilities of an auditor on receipt of written representations from management. (6 marks)
- (b) Some companies have a substantial portion of their total assets comprising investments in stocks and shares of other entities.

**Required:**

- Outline three audit objectives sought by an auditor when examining a client’s investments in stocks and shares. (6 marks)
- (Total: 20 marks)**

**QUESTION THREE**

- (a) Describe the process that an auditing firm should undertake to assess whether pre-conditions for an audit are present when accepting an audit assignment. (4 marks)
- (b) Identify three main areas, other than audit risk, which should be included within the audit strategy document for an audit of a client and for each area, provide a relevant example. (6 marks)
- (c) International Standard on Auditing (ISA) 510, “Initial Audit Engagements - Opening Balances” requires auditors to undertake additional audit procedures for confirming opening balances for new audit engagements. In addition, the ISA gives guidance on audit report implications if auditors are unable to confirm opening balances or if they contain misstatements.

**Required:**

- (i) Describe the procedures the auditor should undertake to confirm opening balances for a new audit engagement. (3 marks)



- (ii) Explain the impact on the audit report if the auditor is unable to confirm the opening balances or if the opening balances contain misstatements. (3 marks)
- (d) Citing two areas and with relevant examples in each case, explain the purpose of a value for money audit. (4 marks)
- (Total: 20 marks)**

**QUESTION FOUR**

- (a) During the audit of Health Care Limited, the audit team discovers that intangible assets balance includes Sh.4,000,000 related to one of their ten development projects. This expenditure does not meet the criteria for capitalisation. As this project is ongoing, the finance director has suggested that no adjustment should be made in this year's financial statements. He is confident that the project will meet the criteria for capitalisation in the following year.

Materiality considerations have established that the amount represents 7% of profit before tax and 1.2% of net assets.

**Required:**

Discuss the audit issues applicable in the above case. (6 marks)

- (b) The finance director of your client, ABC Ltd., has read about review engagements and is interested in the possibility of ABC undertaking these in future. However, he is unsure how these engagements differ from an external audit and how much assurance would be gained from these types of engagement.

**Required:**

(i) Explain the purpose of review engagements and how they differ from external audits. (4 marks)

(ii) Describe the level of assurance provided by external audits and review engagements. (4 marks)

- (c) Explain three ethical threats which might affect the independence of audit practitioners and for each threat, explain how it might be reduced to an acceptable level. (6 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

- (a) With reference to International Standard on Auditing (ISA) 520 - "Analytical Procedures", explain four different types of analytical procedures available to the auditor. (8 marks)

- (b) With respect to information technology (IT) audits, explain the following terms:

(i) Social media risk assessment. (2 marks)

(ii) Software licence review. (2 marks)

(iii) IT governance audit. (2 marks)

(iv) IT risk assessment audit. (2 marks)

- (c) Describe two types of errors that could arise from sampling risk. (4 marks)

**(Total: 20 marks)**

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**CPA PART II SECTION 4**  
**AUDITING AND ASSURANCE**

**THURSDAY: 24 May 2018.**

**Time Allowed: 3 hours.**

**Answer ALL questions. Marks allocated to each question are shown at the end of the question.**

**QUESTION ONE**

- (a) Describe the procedures you would apply in detecting fraud where employees create non-existent suppliers and then divert payments to themselves. (8 marks)
- (b) International Standard on Review Engagements (ISRE) 2400 “Engagements to review Financial Statements” sets out the objective, general principles and procedures to be applied for a review engagement.

**Required:**

Explain six main procedures which an auditor should perform when conducting a review engagement. (12 marks)  
**(Total: 20 marks)**

**QUESTION TWO**

- (a) You are considering deploying an audit software to undertake substantive testing of data files in the sales and inventory system.

**Required:**

Discuss five challenges you might encounter while using the audit software. (10 marks)

- (b) Explain the following terms as used in contemporary audit:

- (i) Cyber insurance. (2 marks)
- (ii) Social engineering. (2 marks)
- (iii) Data protection. (2 marks)
- (iv) Remediation procedures. (2 marks)
- (v) Forensic accounting. (2 marks)

**(Total: 20 marks)**

**QUESTION THREE**

- (a) You have been appointed the lead auditor of CBC Ltd. and you have held a meeting with management where certain representations were orally given and others implied.

**Required:**

With reference to International Standard on Auditing (ISA) 580 “Written Representations”, discuss the circumstances that might lead you to require management to confirm in writing the oral and implied representations. (8 marks)

- (b) Highlight the substantive procedures that might be performed by an auditor to verify the payroll. (8 marks)
- (c) In the context of public sector auditing, distinguish between “performance audits” and “compliance audits”. (4 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

(a) Explain the internal control objectives in each of the following cases relating to credit sales:

- (i) Credit approval. (2 marks)
- (ii) Receipt of sales order. (2 marks)
- (iii) Invoicing of goods dispatched. (2 marks)
- (iv) Entry into the debtor's ledger. (2 marks)

(b) Your firm has been appointed the auditor for Musoni Ltd., a company that distributes computer equipment. During the audit, the following matters came to your attention:

1. The depreciation rates had been reviewed and adjusted resulting in an increase in asset lives and a reduction in depreciation amounts.
2. Stock take across all the warehouses could not be undertaken due to lack of staff.
3. One of the warehouses caught fire and goods worth Sh.50 million got damaged. A claim had been lodged with the insurance company but the incident was still under investigation. The amount had however been included in the financial statements as expected income.
4. Bank reconciliation had not been completed even though there were material balances.

**Required:**

Describe four audit risks arising from the issues above and the proposed auditor's response. (8 marks)

(c) Distinguish between "assurance engagements" and "non-assurance engagements". (4 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

(a) A suitable criteria is the benchmark used to evaluate a subject matter for the purpose of presentation and disclosure.

**Required:**

Describe three characteristics of a suitable criteria. (6 marks)

(b) Explain the three components of the fraud triangle. (6 marks)

(c) Discuss four reasons why an auditor might decide not to seek for re-election. (8 marks)

**(Total: 20 marks)**

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CPA PART II SECTION 4  
AUDITING AND ASSURANCE

THURSDAY: 30 November 2017.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

**QUESTION ONE**

- (a) Auditors carry out various audit assignments.

In relation to the above statement, explain four non-assurance assignments that auditors undertake. (4 marks)

- (b) Describe three circumstances in which the management of an organisation might request the auditor to change the terms of an audit engagement. (6 marks)
- (c) Kisomo Kizuri is a charity organisation that raises funds for educational projects. Charities in the country from which Kisomo Kizuri operates have recently become subject to new audit and accounting regulations.

Your firm has been appointed as Kisomo Kizuri's new auditors.

**Required:**

Analyse five audit tests you might carry out on the income and expenditure from fund raising events. (10 marks)  
**(Total: 20 marks)**

**QUESTION TWO**

- (a) Explain the following terms as used in contemporary audit:

- (i) Environmental audit. (2 marks)
- (ii) Corporate governance. (2 marks)
- (iii) Enterprise risk management (ERM). (2 marks)

- (b) Citing a relevant example in each case, explain the following control procedures:

- (i) Segregation of duties. (3 marks)
- (ii) Authorisation and approval. (3 marks)
- (iii) Physical controls. (3 marks)

- (c) Analyse five circumstances that might lead to qualification of financial statements. (5 marks)  
**(Total: 20 marks)**

**QUESTION THREE**

- (a) Explain six benefits an auditor might derive from using computerised audit software. (6 marks)
- (b) Citing a relevant example in each case, distinguish between "adjusting events" and "non-adjusting events". (6 marks)
- (c) International Standard on Auditing (ISA) 620 "Using the work of an expert" contains guidance to an auditor on using the work of an expert to provide knowledge relevant to the audit which the audit firm does not possess.

Evaluate four procedures that an audit firm might apply before relying on such an expert. (8 marks)  
**(Total: 20 marks)**

**QUESTION FOUR**

- (a) Examine six factors that might influence inherent risk at the organisational level. (6 marks)
  - (b) Discuss the importance of the following provisions of professional ethics:
    - (i) Audit fees. (2 marks)
    - (ii) Conflict of interest. (2 marks)
    - (iii) Due care and skill. (2 marks)
  - (c) You are the audit manager in charge of the audit of Lenga Ltd. You have come across the following matters which you consider to be material. Explain how you would report each matter in the audit report:
    - (i) A major customer owing the company a substantial amount, has filed for bankruptcy. No provision for this has been made in the financial statements. (2 marks)
    - (ii) Some of the company's inventory is of a special nature. The expert you were relying on to value them might not be available to carry out the valuation in time for issuance of an audit report. You have to rely on management representation. (2 marks)
    - (iii) A major supplier has gone out of business and there is no immediate alternative for the raw material in question. (2 marks)
    - (iv) After the financial year end, a major fire broke out destroying machinery that had been purchased at the end of the year. (2 marks)
- (Total: 20 marks)**

**QUESTION FIVE**

- (a) Highlight six reasons why an auditor might need to understand the entity and its environment before undertaking an audit assignment. (6 marks)
  - (b) Explain the following terms:
    - (i) Reasonable assurance. (2 marks)
    - (ii) Opinion shopping. (2 marks)
  - (c) Discuss five stages that might be followed in carrying out a forensic audit. (10 marks)
- (Total: 20 marks)**
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# KASNEB

## CPA PART II SECTION 4

### AUDITING AND ASSURANCE

THURSDAY: 25 May 2017.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

#### QUESTION ONE

(a) Discuss five disclosure requirements that should be made in an audit report as specified in the Companies Act. (10 marks)

(b) Your firm has been appointed as the auditor of Fanaka Limited for the year ended 31 December 2016.

Explain why each of the following matters which you have noted during the audit should or should not be included in the letter to the management and those charged with governance:

(i) The company upgraded the accounting system which upon testing you noted that the system did not carry over all the balances accurately. The differences in credit and debit balances considered separately were material to the financial statements but when offset against each other, they were immaterial. (2 marks)

(ii) The new accounting system had a functionality that allows online approval of transactions by the various signatories but it had not been activated. The signatories continued to approve transactions manually and all the transactions sampled were duly approved. (2 marks)

(iii) The company supplying stationery to Fanaka Limited was owned by the wife of the procurement manager. However, you confirmed that the appropriate procurement procedures were followed. (2 marks)

(iv) The bank reconciliations were required to be signed by the preparer (Financial Accountant) and approved by the finance manager. You noted that 6 out of the 12 bank reconciliation statements were not signed by the Financial Accountant but had been approved by the Finance Manager. However, you confirmed that the reconciliation statements were accurate. (2 marks)

(v) The company was involved in a restructuring exercise that resulted in the discharge of 25% of the staff. You got to learn that the affected staff had filed a suit in court to challenge their dismissal but the matter had not been heard. However, the management was keen to have the suit heard in order for them to present the issue for reporting in the next financial year when it would be possible to establish if there was a reputable contingent liability. (2 marks)

**(Total: 20 marks)**

#### QUESTION TWO

(a) Describe five roles you would expect the internal audit staff to perform. (10 marks)

(b) Discuss four capabilities and competencies expected of the engagement team as espoused in the International Standards of Auditing (ISA) 220 "Quality Control for Audit of Financial Statements". (8 marks)

(c) Outline two benefits of the auditor communicating with those charged with governance. (2 marks)

**(Total: 20 marks)**

#### QUESTION THREE

(a) Explain the following terms as used in auditing:

(i) Emphasis of matter paragraph. (2 marks)

(ii) Contingent liability. (2 marks)

(iii) Audit committee. (2 marks)

(iv) Assurance engagement risk. (2 marks)

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- (b) Your audit firm was recently appointed the auditor of Baraka Ltd. The company has a subsidiary based in Mombasa and its auditor had retired the previous year.

**Required:**

- (i) Enumerate six factors that would influence you in determining whether or not to send a separate engagement letter to the subsidiary. (6 marks)
- (ii) If the audit of Baraka Ltd. was a recurring audit, suggest six factors that would make it appropriate for you to send a new engagement letter. (6 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

- (a) Explain three factors to consider while designing an effective system of internal control. (6 marks)
- (b) In the context of auditing, define the following:
- (i) Operational audit. (2 marks)
- (ii) Financial audit. (2 marks)
- (iii) Agreed upon procedures engagement. (2 marks)
- (iv) Positive assurance. (2 marks)
- (c) Discuss three responsibilities of the external auditor in relation to prevention and detection of fraud. (6 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

- (a) State the opinions you would give in each of the following situations:
- (i) The books of the client were taken away by the regulator for investigations and were not available for audit. (2 marks)
- (ii) The provision for doubtful debts was not adequate. The debtors in the financial statement were misstated but the financial statements gave a true and fair view. (2 marks)
- (iii) There was no provision for depreciation and the directors were unwilling to provide for any amounts during the financial year. The amount if provided for would reduce the reported profit by 30%. (2 marks)
- (iv) There was a legal suit filed by a customer who was unsatisfied with the goods supplied but no provisions were made in the books. The assessment of the case by the company lawyers indicate that the customer has very slim chances of success. (2 marks)
- (b) Discuss four factors that might influence the extent of substantive tests carried out during an audit. (8 marks)
- (c) Highlight four substantive procedures you would perform on the year end trade payables. (4 marks)

**(Total: 20 marks)**

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# KASNEB

## CPA PART II SECTION 4

### AUDITING AND ASSURANCE

THURSDAY: 24 November 2016.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

#### QUESTION ONE

- (a) In the context of International Standards of Auditing (ISA) 210 "Agreeing the Terms of Audit Engagements", discuss six steps the auditor should undertake to establish whether the pre-conditions for an audit were present. (12 marks)
- (b) In the context of International Standards of Supreme Audit Institutions (ISSAI) 100 "Fundamental Principles of Public Sector Auditing", discuss four principles relating to planning an audit. (8 marks)

(Total: 20 marks)

#### QUESTION TWO

- (a) You have been appointed the lead auditor in charge of the audit of Sky Computer Limited. The financial year ended on 31 January 2016 and the audit was concluded on 1 March 2016. The audit report was signed on 15 May 2016 and the financial statements issued on 20 June 2016. The following material events occurred between the balance sheet date and 30 June 2016:

- 25 February 2016 - A sudden flood resulted in damage of an uninsured equipment worth Sh.12 million.
- 1 May 2016 - A customer owing Sh.4 million was declared bankrupt and no recovery of the amount was expected.
- 15 June 2016 - The company lost a law suit amounting to Sh.6 million which was filed in 2013 by a customer due to a defective computer software.
- 25 June 2016 - The Board of directors approved the closure of a division that had been making losses consistently for the last four years.

#### Required:

- (a) Explain the appropriate treatment of each of the above events. (8 marks)
- (b) Describe four audit procedures necessary to aid in obtaining evidence relating to subsequent events. (8 marks)
- (c) Explain the responsibility of an auditor with regard to events occurring between the date the financial statements are signed and the annual general meeting. (4 marks)

(Total: 20 marks)

#### QUESTION THREE

- (a) Examine five possible frauds in the area of purchases that an Internal Control System should be designed to prevent and detect. (10 marks)
- (b) Discuss five input validity checks you would expect to find in a computerised financial system. (10 marks)

(Total: 20 marks)

#### QUESTION FOUR

- (a) Explain four factors which might influence an auditor while assessing the reliability of evidence gathered during an audit. (8 marks)
- (b) For financial reporting purposes, the entity's risk assessment process includes how management identifies business risks relevant to the preparation of financial statements in accordance with the applicable financial reporting framework.

#### Required:

- Discuss six circumstances in which risks in an entity might arise or change. (12 marks)

(Total: 20 marks)

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**QUESTION FIVE**

- (a) Describe four types of assurance engagements. (8 marks)
  - (b) Summarise four substantive procedures that you would perform in respect of bank overdraft. (8 marks)
  - (c) Highlight four matters that an auditor is likely to include in a management letter. (4 marks)
- (Total: 20 marks)**
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# KASNEB

## CPA PART II SECTION 4

### AUDITING AND ASSURANCE

THURSDAY: 26 May 2016.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

#### QUESTION ONE

- (a) In the context of International Standards of Supreme Auditing Institutions 3100, "Performance Audit Guidelines - Key Principles":
- (i) Define the term "performance auditing". (2 marks)
  - (ii) Discuss the three approaches that might be taken in examining the performance of the audited entity. (6 marks)
- (b) During the audit of Bamboo Ltd., you suspect that there might have been some irregularities in the procurement department based on the discussions you had with some of the staff members.

**Required:**

Explain six audit steps you would undertake to help you in arriving at an appropriate audit opinion. (12 marks)  
(Total: 20 marks)

#### QUESTION TWO

- (a) Highlight two limitations of external audits. (2 marks)
- (b) Describe the type of assurance report a practitioner would issue in each of the following engagements:
- (i) Reasonable assurance engagement. (2 marks)
  - (ii) Limited assurance engagement. (2 marks)
- (c) Describe four types of audit opinions that an auditor could issue. (8 marks)
- (d) In the context of International Standard on Auditing (ISA) 260 - "Communicating with those charged with governance", describe three matters that the auditor should communicate to those charged with governance in relation to auditor independence. (6 marks)  
(Total: 20 marks)

#### QUESTION THREE

- (a) (i) Define the term "sampling risk". (2 marks)
- (ii) Discuss two types of errors that could arise from sampling risk. (4 marks)
- (b) Describe the impact of each of the following situations on the sample size:
- (i) An increase in the extent to which the auditor's risk assessment takes into account relevant controls. (2 marks)
  - (ii) An increase in the use of other substantive procedures directed at the same assertion. (2 marks)
  - (iii) An increase in the auditor's assessment of the risk of material misstatement. (2 marks)
- (c) Explain four purposes of an audit program. (8 marks)  
(Total: 20 marks)

**QUESTION FOUR**

- (a) Describe the following Computer Assisted Audit Techniques (CAATs):
  - (i) Embedded audit facilities. (2 marks)
  - (ii) Integrated test facilities. (2 marks)
- (b) List four audit procedures that could be carried out using computer assisted audit techniques. (4 marks)
- (c) Shujaa Ltd. is in the process of implementing a computer based accounting system. As their auditor, you have been requested to advise on the appropriate controls to be implemented to prevent unauthorised changes to the data files.

**Required:**

Suggest six controls that the management of Shujaa Ltd. should consider. (12 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

- (a) In the context of International Standards on Auditing (ISA) 560 - "Subsequent Events":
  - (i) Define the term "subsequent event". (2 marks)
  - (ii) Discuss two objectives of the auditor in relation to subsequent events. (4 marks)
- (b) Explain four ways in which the auditor might minimise risk during a particular audit. (8 marks)
- (c) You have been appointed the auditor of Fadhili Ltd. and as part of the audit, you have requested management to provide you with a letter of representation.

**Required:**

Discuss three matters you would expect to find in the letter in relation to management's responsibilities. (6 marks)

**(Total: 20 marks)**

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# KASNEB

## CPA PART II SECTION 4

### AUDITING AND ASSURANCE

THURSDAY: 26 November 2015

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

#### QUESTION ONE

- (a) (i) Define the term "forensic accounting". (1 mark)  
(ii) Explain a situation in which forensic accounting might be applied. (1 mark)
- (b) Discuss the three E's of value for money auditing as used in public sector auditing. (6 marks)
- (c) In the context of International Standard on Auditing (ISA) 220-Quality Control for an Audit of Financial Statements, discuss the quality control procedures the engagement partner might consider in each of the following:
- (i) Client acceptance. (4 marks)  
(ii) Engagement team. (4 marks)  
(iii) Direction. (4 marks)

**(Total: 20 marks)**

#### QUESTION TWO

- (a) Explain four assertions relevant to accounts payable at year end. (8 marks)
- (b) You are the auditor responsible for the audit of Yummy Foods Ltd., a company that operates a chain of fast food outlets. It has come to your attention that a customer has sued the company claiming an amount of ten million shillings for food poisoning. The amount is material, but management believes there is good defence against the claim and thus no provision or disclosure has been made in the books.

##### Required:

- (i) Evaluate five items of evidence that might enable you form a conclusion on the likelihood of the claim being successful. (10 marks)  
(ii) Describe how the matter could be reported in the financial statements if your conclusion is that there is a possibility, but not a probability that the claim would be successful. (2 marks)

**(Total: 20 marks)**

#### QUESTION THREE

- (a) (i) Explain the meaning of the term "going concern". (2 marks)  
(ii) State eight factors that might indicate doubt in the ability of an entity to continue as a going concern. (8 marks)
- (b) Discuss five factors that could influence the extent to which an auditor might use analytical review to collect audit evidence. (10 marks)

**(Total: 20 marks)**

#### QUESTION FOUR

- (a) In the context of International Standard on Auditing (ISA) 315-Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and its Environment, describe five components of an entity's internal control system. (10 marks)
- (b) Explain the following terms as used in auditing:
- (i) Audit risk. (2 marks)  
(ii) Inherent risk. (2 marks)  
(iii) Control risk. (2 marks)  
(iv) Attest engagement. (2 marks)  
(v) Direct reporting engagement. (2 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

(a) Your audit firm was recently appointed the auditor of ABC Ltd. for the first time. ABC Ltd. requires that the audit be concluded within two months after the end of the financial year.

Describe the steps your audit firm would take prior to accepting this appointment. (10 marks)

(b) During the audit of Faida Ltd., you noticed the following:

1. There were material deposits in the bank just before the year end and subsequent withdrawals thereafter.
2. Many debtors disputed the amount alleged by management after circularisation. There were also inconsistencies between the dates when the debtors made their payments and the dates when the records were updated, noting that all the payments were in cash.

**Required:**

- (i) Explain the impact of each of the two aspects above. (2 marks)
- (ii) Examine four audit procedures that could help you in arriving at an audit opinion in each of the two aspects above. (8 marks)

**(Total: 20 marks)**

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# KASNEB

## CPA PART II SECTION 4

### AUDITING AND ASSURANCE

#### PILOT PAPER

September 2015.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

#### QUESTION ONE

You are an audit manager in Ujima & Co. One of the your audit clients, Shangilia Africa Ltd. is a specialist supplier of African literature books with over 120,000 customers. The company owns one large warehouse which holds about 1 million books of up to 80,000 different titles. Customers place orders for books either over the internet, or by mail order. Books are dispatched on the day of receipt of the order.

Returns are allowed up to 30 days from the dispatch date provided the books look neat and unread.

Due to high inventory turnover, Shangilia Africa Ltd. maintains a perpetual inventory system using standard purchased software. Ujima Co. has audited the system for the last five years and has found no error within the software.

Continuous inventory checking is carried out by Shangilia Africa Ltd.'s internal audit department.

You are currently reviewing the continuous inventory checking system with an audit junior. The audit junior needs experience in auditing continuous inventory checking systems and some basic knowledge on the code of ethics for professional accountants.

#### Required:

- (a) Explain four advantages of using a perpetual inventory system. (4 marks)
- (b) Summarise the audit procedures you would perform to confirm the accuracy of the continuous inventory checking at Shangilia Africa Ltd. Justify each of the procedures. (7 marks)
- (c) Explain five fundamental principles set out in the Code of Ethics for professional accountants. (5 marks)
- (d) During preliminary audit planning you note that the engagement letter has been returned unsigned by the directors of Shangilia Africa Ltd. When asked to explain their action, the directors indicate that they cannot allow you access to information on the company's new website development as this contains various trade secrets. You would not, therefore, be able to perform audit procedures on the research and development expenditure incurred on the website and included in non-current assets.

Briefly explain four actions you would take as a result of directors not signing the engagement letter. (4 marks)

**(Total: 20 marks)**

#### QUESTION TWO

- (a) Outline the meaning of the following terms:
  - (i) Audit risk. (1 mark)
  - (ii) Inherent risk. (1 mark)
  - (iii) Control risk. (1 mark)
  - (iv) Detection risk. (1 mark)
- (b) My-family Car Hire Limited has a large fleet of cars for hire. The firm operates from twelve separate depots providing national car hire services around the country. It offers car hire services to corporate customers on credit payment terms, including payment by cash.

In addition to the car hire revenue, the company categorises income from the sales of excess damage waiver insurance premiums, the hire of child seats and satellite navigation systems as car hire income.

**Required:**

Explain three factors that would contribute to the assessment of high inherent risks applying to car hire income as reported in the financial statements of My-family Car Hire Limited. (6 marks)

- (c) (i) A Junior colleague working at your firm is uncertain as to why on every audit all of the work carried out by the audit team is regularly reviewed by the audit manager.

**Required:**

Explain the purpose of the review carried out by the audit manager. (5 marks)

- (ii) List two examples of subsequent events that may provide confirming evidence when auditing the financial statements of a large manufacturing company. (2 marks)

- (iii) State the auditor's responsibility for reporting on the going concern assumptions of a company. (3 marks)

**(Total: 20 marks)**

**QUESTION THREE**

- (a) Smiling Windows Co. (SW) is a window cleaning company. Customers windows are cleaned monthly. The window cleaner then posts a stamped addressed envelope for payment through the customer's front door.

SW has a large number of receivables balances. These customers pay by cheque or cash which is received in the stamped addressed envelopes through the post. The following procedures are applied to the cash received cycle:

1. A junior clerk from the accounts department opens the posts and if any cheques or cash have been sent, she records the receipts in the cash received log and then places all the monies into the locked small cash box.
2. The content of the cash box are counted each day and every few days these sums are banked by whichever member of the finance team is available.
3. The cashier records the details of the cash received log into the cash received day books and also updates the sales ledger.
4. Usually on a monthly basis the cashier performs bank reconciliation which he then files. If he misses a month then he catches this up in the following months' reconciliation.

**Required:**

- (i) Explain three deficiencies in the system. (3 marks)

- (ii) Suggest controls to address each of these deficiencies. (3 marks)

- (b) Describe the steps an audit firm should perform prior to accepting a new audit engagement. (5 marks)

- (c) Explain the term "International Standards on Auditing". (4 marks)

- (d) Outline how an audit committee may be of assistance in the relationship between the internal auditor and external auditor. (5 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

- (a) XYZ Ltd.'s directors have expressed an interest in your audit firm Tato & Co. to perform other review engagements in addition to the external audit. However, they are unsure how much assurance would be gained via these engagements and how these differ compared to the assurance provided by an external audit.

**Required:**

Identify and explain the level of assurance provided by an external audit and other review engagements. (4 marks)

- (b) Discuss the legal responsibilities of an auditor to shareholders and third parties during the course of their normal professional engagement and the mitigation measures that auditors may institute. (8 marks)

- (c) Knowledge of the business is crucial in determining the most effective and efficient audit strategy of an entity using the internet for electronic commerce. Any auditor needs to have an indepth understanding of the related risks and the measures to minimise them.

**Required:**

Discuss the impact of e-commerce on the audit process.

(8 marks)

(Total: 20 marks)

**QUESTION FIVE**

Fitness Ltd. (fitness) is a client of your firm and runs both fitness and leisure centres all over your country. You are the audit senior on assignment and the audit field work for the year ended 31December 2015 has just been completed. The following figures have been extracted from the draft financial statements:

	Year ended 31 December	
	2014	2013
	Sh."000"	Sh."000"
Revenue	5,000	5,300
Profit before tax	300	320
Taxation	(96)	(102)
Profit after tax	<u>204</u>	<u>213</u>

1. Fitness received fees from customers in November 2014 as they ran a special gym offer for the four months period from 1 November 2014 to 28 February 2015. The fees collected amounted to Sh.20,000 and the full amount had been recorded in revenue for the year ended 31 December 2014.
2. One of the directors is unwilling to disclose her interests in the shares of the company and currently this amount is not shown in the draft financial statements. The director holds 400 ordinary shares of the 200,000 issued ordinary shares of the company.
3. During the audit test of control performed on the revenue cycle, it was noted that the monthly prepared bank reconciliation had not been reviewed on a consistent basis by management.

**Required:**

- (a) Set an appropriate materialist level for fitness, showing your calculation. (4 marks)
- (b) Outline the testing you should perform on the revenue figure which arises from the gym membership fees. (4 marks)
- (c) Draft a memorandum to the audit partner in which you evaluate the potential implications for the audit report of fitness for the year ended 31 December 2014 arising from each of the three issues (1) to (3) described above. (12 marks)

(Total: 20 marks)

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