

**INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS  
OF PAKISTAN**

PROFESSIONAL III EXAMINATION-SPRING (SUMMER), 2004

Friday, the 28th May, 2004

574

**AUDITING**

*Time Allowed* 3 Hours

*Maximum Marks* 100

- (i) Attempt SIX questions, including question No. 4, which carries 20 marks. All other questions carry 16 marks each.
- (ii) Answers must be neat, relevant and brief.
- (iii) In marking paper, the examiners take into account clarity of exposition, logic of arguments, effective presentation and language.
- (iv) Read the instructions printed on the top cover of answer script CAREFULLY before attempting the paper.
- (v) DO NOT write your Name, Reg. No. or Roll No. anywhere inside the answer script.

Marks

**Special instructions for Q. 1:**

- An overwritten reply will carry no mark.
- Present your answer in the format given below:

S. No.	Your choice	Rationale (Brief reason for your answer)
ii		
iii		
and so on		

Q. 1 (a) Select the correct answer :

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- (i) The term "testing" implies:
  - (a) A guarantee.
  - (b) A certificate.
  - (c) Accuracy.
  - (d) Sampling.
- (ii) The risk that the auditor will conclude, based on audit tests, that a material misstatement does not exist in an account balance, whereas, in fact such a misstatement exists, is referred to as:
  - (a) Sampling risk.
  - (b) Detection risk.
  - (c) Non-sampling risk.
  - (d) Inherent risk.

P.T.O.

- (iii) Which one of the following is ordinarily included in the letter of representation. **Marks**
- Terms of engagement.
  - Weakness of internal control.
  - Introduction of audit staff.
  - Transactions with related parties.
- (iv) The primary objective of analytical procedures at the final review stage is to:
- Obtain evidence of details tested to corroborate particular assertions.
  - Assist in assessing the validity of the conclusions reached.
  - Identify areas that represent specific risks relating to audit.
  - Satisfy doubts when questions arise about client's ability to continue in existence.
- (v) In verifying contingent liabilities which one of the following is least relevant:
- Letter from lawyer.
  - Comparison with last year.
  - Inquiry of management.
  - Bank confirmation.
- (vi) Which one of the following subsequent events would require adjustment to financial statements:
- Issue of shares and debentures.
  - Loss of inventories as a result of fire.
  - Receipt of evidence that previous estimate of profit on long term contract was inaccurate.
  - Government action such as nationalization.
- (b) Match the following term or terms that relate to each description. **4**

<u>Description</u>	<u>Term</u>
1. The confirmation of the Auditor's responsibility for audit.	a. System flow chart.
2. The work is to be adequately planned and assistants are to be properly supervised.	b. Going concern.
3. Documenting understanding of accounting and internal control system.	c. Engagement letter.
4. Consider management's plans for generating adequate cash flow.	d. Requirement of International Standards on Auditing.

- |   | Marks                               |
|---|-------------------------------------|
| Q. 2 (a) Discuss significant inherent limitations of an audit.  | 8                                   |
| (b) Under what circumstances a person cannot be appointed as auditor of a company?  | 8                                   |
| Q. 3 (a) Enumerate any four cut off procedures that you would apply relating to Inventories at December 31, 2003. The relevant data is:   | 8                                   |
| <i>Audit Period :</i>   | <i>Year ended December 31, 2003</i> |
| <i>Date of physical stocktaking :</i>   | <i>December 31, 2003</i>            |
| <i>Last GRN # :</i>   | <i>117</i>                          |
| <i>Last suppliers' invoice # (unique number assigned by the client) :</i>   | <i>645</i>                          |
| <i>Last delivery note # :</i>   | <i>945</i>                          |
| <i>Last sales invoice # :</i>   | <i>3450</i>                         |
| <i>The client uses periodic inventory system.</i>   |                                     |
| (b) How would you verify liability under <i>Finance Lease</i> ?   | 8                                   |
| Q. 4 Due to the recent pronouncements of Securities and Exchange Commission of Pakistan, the role of Internal Audit Department of a listed company has been substantially upgraded. Keeping in view the requirements of Code of Corporate Governance: |                                     |
| (a) Briefly state the terms of reference of the Audit Committee recommended by the Code of Corporate Governance.  | 8                                   |
| (b) State the frequency of meetings of an Audit Committee as prescribed by the Code of Corporate Governance. Can the Head of Internal Audit request for holding meeting of Audit Committee?   | 4                                   |
| (c) Who approves appointment of Head of Internal Audit in a listed Company? State to whom does the internal auditor submit its report in a listed company?  | 4                                   |
| (d) What is the reporting procedure of an Audit Committee?  | 4                                   |
| Q. 5 (a) Enumerate some arguments whether or not the auditor should be liable for negligence in a claim by third party, and give your conclusion.   | 12                                  |
| (b) Explain your understanding of the phrase "scope of an audit".   | 4                                   |
| Q. 6 (a) One of the basic principles governing an audit as set out in ISA-200 is confidentiality. Explain what do you understand by confidentiality. Under what circumstances the principle of confidentiality may be violated.                       | 8                                   |
| (b) What are the differences between analytical procedures and detailed tests?  | 8                                   |

			Marks
Q. 7	(a)	(i) Briefly state the main objectives of control over fixed assets.	4
		(ii) State the main aspects of internal control which you would expect to find in operation in a listed company to control fixed assets.	4
	(b)	The strengths and weaknesses in the system of Internal Control are measured with reference to the degree to which functions of authorizing, custody and record-keeping are segregated. Based on this principle, you are required to draft two questions suitable for inclusion in a standard internal control questionnaire (ICQ) for:	
		(i) Purchases and creditors.	4
		(ii) Sales and Debtors.	4
Q. 8	(a)	The inspection of Board Minutes is considered an integral part of an auditor's examination of a listed company's financial statements.	
		(i) Explain why examination of Minutes of Board meetings is important for an auditor?	2
		(ii) State five Board Resolutions required to be verified by the auditor under Section 196 of the Companies Ordinance, 1984.	8
	(b)	What normal audit procedures would be applied to detect misappropriation of monies received from debtors by "Teeming and Lading".	6

THE END