

UGANDA MARTYRS UNIVERSITY

FACULTY OF BUSINESS ADMINISTRATION AND MANAGEMENT

BSC ACCOUNTING YEAR 111

FINAL ASSESSMENT

CPA LEVEL TWO

AUDITING & PROFESSIONAL ETHICS AND VALUES-PAPER 12

THURSDAY: 14TH JULY, 2022

INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours 15 minutes**.

The first 15 minutes of this examination have been designated for reading time. You may not start to write your answer during this time.

2. Section **A** has one compulsory case study question carrying 30 marks.
3. Section **B** has **four** questions and only **three** are to be attempted. Each question carries 20 marks.
4. Section **C** has **two** questions and only **one** is to be attempted. Each question carries 10 marks.
5. Write your answer to each question on a fresh page in your answer booklet.
6. Please, read further instructions on answer book before attempting any question.
7. Please, read further instructions on the answer booklet, before attempting any question.

SECTION A

This section has one compulsory question to be attempted

Question 1

Your firm, WLS & Co. (WLS), has been re-appointed as auditors of Magana Light Ltd (MLS) for the year ended 30 June, 21. WLS has been auditing MLS for 6 years. MLS's financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). You are the audit senior in charge of the audit of MLS and you have to ensure, among other things, that the audit is conducted in accordance with International Standards on (ISAs). As part of planning; you and the audit manager attended a pre-audit meeting with MLS's management. The following brief notes were prepared during that

1. MLS finance manager Mr. Bob Musoke joined the company on 1 July, 2020. He previously worked at Uganda Martyrs University as a university finance officer
2. MLS carried out a restructuring exercise in December 2020 and 50 employees were laid off. A provision of Shs 60 million has been included in the financial statements for compensation. Some employees have, however, sued the company claiming the compensation to be given to them is too small.
3. MLS's trade and other receivables amount to Shs 6 billion as at 30 June, 2021. MLS made a general provision of 5% of the total trade and other receivables. Some clients have written to MLS about the financial difficulties they are facing but the Finance Manager is sure that they will be able to pay. No specific provision has been made in respect of this.
4. The Finance Department is under staffed. It has only three staff instead of the required six.
5. Jane, a former employee of MLS, joined WLS & Co on 1 March, 2020. She is slated to be part of the audit team because, it is felt, that her experience of with MLS will be of great value to the audit team.
6. An analytical review carried out on MLS's financial statements showed a material variance which was due to an increase in finance costs by over 50% in the current year.

7. MLS intends to list on the Uganda Securities Exchange. However, one of the requirements is to have an independent Board in place. WLS is tasked with the responsibility of recommending to MLS members to serve on the board.

8. MLS has significant outstanding audit fees but WLS & Co is not worried as MLS has always endeavored to pay.

Required:

(a) Discuss, with the Audit Manager:

(i) The possible financial statements risks the audit team is likely to face during the audit of MLS. **(5 marks)**

(ii) How the financial statements risks in (a) (i) above can be mitigated to an acceptably low level. **(5 marks)**

(b) Examine the actual and possible ethical threats that may arise in relation to the audit of MLS, and the safeguards to reduce them. **(6 marks)**

(c) Describe the assertions made by MLS' management in relation to the trade and other receivables balance. **(4 marks)**

(d) Explain the substantive audit procedures the audit team should perform on:

(i) trade and other receivables. **(6 marks)**

(ii) bad debts. **(4 marks)**

(Total 30 marks)

SECTION B

Attempt three of the four questions in this section

Question 2

PKL Microfinance Limited (PKL) offers financial services to small and medium-sized Enterprises (SMEs). PKL intends to upgrade its status from microfinance to a Commercial bank regulated by Bank of Uganda in order to be competitive in the financial services industry characterized by information technology (IT) environment. One of the requirements of Bank of Uganda is for PKL to have an audit committee to oversee both internal and external audits. PKL has subsequently instituted an audit committee to meet the requirements of Bank of Uganda. Your firm GKS & Co. (GKS) has been invited by PKL to train their (PKL's) audit committee on matters relating to external and internal auditing. The audit manager will be carrying out the training next week assisted by you, the audit senior.

Required:

Prepare brief notes for your audit manager in relation to the training covering the following:

- (a) (i) Composition of an audit committee. **(2 marks)**
 - (ii) Objectives of an audit committee. **(6 marks)**
 - (b) Differences between internal and external audit reports. **(8 marks)**
 - (c) Reasons why auditing in an IT environment may lack visible audit trail. **(4 marks)**
- (Total 20 marks)**

Question 3

You are an audit supervisor at ZY & Co. Your firm has been appointed to audit ABCA Pharmaceutical Limited (ABCA) for the year ending 31 December, 2021 ABCA Pharmaceutical is the main supplier to hospitals and pharmacies within country. The previous auditors would send trainee accountants for the assignments. The partners never had face to face meetings with then of ABCA. Some partners became suppliers of ABCA products. They would obtain drugs on credit and fail to pay. Eventually their services were terminated. In the pre-audit meeting, the Head of Finance at ABCA cautioned ZY & Co. about the uniqueness of the sector in which the company operates. Therefore the engagement partner concluded

that there will be need to approach the audit with professional skepticism, and deployment of staff that are able to apply professional judgment during an audit. The company operates in a computerized environment and most of the controls are automated. The company has material levels of inventory and ZY & Co. will be invited to witness the inventory count after year end. You are the audit senior for this engagement.

Required:

(a) Explain to the audit team the meaning of:

(2 marks)

(i) Professional skepticism

(2 marks)

(ii) Professional judgment

(b) With examples, explain to your audit team the circumstances that give rise to self-interest threats during the audit of an entity

(2 marks)

(c) Explain to the audit team the:

(i) Circumstances under which the auditor may be held liable to third parties for professional negligence.

(2 marks)

(ii) Ways the auditor can use to minimize potential liability arising from professional negligence

(5 marks)

(d) Explain the audit procedures ZY & Co will apply during the count of ABCA's Inventory

(7 marks)

(Total 20 marks)

SECTION C

Attempt one of the two questions in this section

Question 6

People are the most important elements in any business. It is the people who buy the products of a business. Without customers, no business would survive for long. Businesses exist because they can make profit by supplying goods and services that are highly demanded. Before establishing any business, an entrepreneur should first assess the market potential of his products. Failure to carry out market survey and consider other factors leads to business failure.

Required:

- (a) Explain reasons for business failure of many enterprises in Uganda. **(5 marks)**
- (b) Discuss the factors that are considered when assessing the market potential of a product. **(5 marks)**

(Total 10 marks)

Question 7

The venture life cycle shows the stages through which a business goes up to the time it is wound up. In order to achieve its major goal of profit maximization, a business depends on the society for inputs like money, workers and skills for its existence and growth. Likewise, the society depends on business for meeting its needs and welfare. This kind of interdependence requires businesses to be socially responsible. However, some people believe that the concept of social responsibility is against the profit motive and most of the classical economists are against the idea of social responsibility.

Required:

- (a) Describe the stages of the 'venture life cycle'. **(4 marks)**
- (b) Explain reasons why some businessmen are opposed to the notion of social responsibility. **(6 marks)**

(Total 10 marks)