



Audit and Assurance

Instructions to examinees:

- (i) Answer all **EIGHT** questions.
- (ii) Answer in **black** pen only.

- Q.1 (a) Alia recently completed her Chartered Accountancy qualification and training from Rumi Iqbal and Company, Chartered Accountants. During her training, Alia was mainly engaged in audits of fast moving consumer goods (FMCG) companies.

She is currently working with an audit client who approached her for reporting manager position. One of the main reasons for her selection was her audit experience in the FMCG sector. The audit client, who wants to employ her, expects that she will help prepare a comparative analysis of certain financial aspects of the company using the data from the sector that she may have obtained during the course of her audits.

Required:

In light of the Code of Ethics for Chartered Accountants, identify and explain the threats to the fundamental principles. (08)

- (b) You have been appointed as the Engagement Quality Control Reviewer for POM Limited, a listed company.

Required:

Mention any **six** procedures that you will perform during the review. (06)

- Q.2 Consider the following information of two companies:

Particulars	Company A (Listed Textile Company)			Company B (Unlisted Cement Company)		
	2023	2022	2021	2023	2022	2021
	----- Rs. in million -----			----- Rs. in million -----		
Financial information						
Net assets	4,645	4,008	3,998	571	665	566
Revenues	15,877	16,119	12,566	1,014	1,810	979
Profit before tax	864	768	690	(16)	145	71
Other information						
Uncorrected misstatements in prior years	-	9	-	-	-	-
Debt equity ratio	10:90	Not relevant		85:15	Not relevant	

Required:

Using the information provided above:

- (a) calculate the materiality at the financial statements level for each company separately for the year ended 30 June 2023. (02)
- (b) discuss the reasons for selection of appropriate benchmark for calculation of materiality in (a) above. (07)
- (c) briefly discuss how the performance materiality will be calculated for Company A. (02)

- Q.3 (a) During the audit of CCN Limited for the year ended 30 June 2023, the audit team circularized direct confirmations to trade debtors. The details are as follows:

Trade debtor's name	Year-end balance ----- Rupees -----	Balance confirmed	Confirmation received date	Comments
AAB	12,336,990	10,556,990	28 July 2023	None
BBC	50,997,000	-	Not received	None
CCD	20,234,565	20,234,565	20 July 2023	Received through email
DDE	1,678,000	1,678,000	Not received	Confirmed over phone on 15 July 2023

Required:

Analyze each of the above debtors' responses and recommend further course of action to be adopted by the auditor. (11)

- (b) The audit junior was assigned the task of verifying rent expense for a chain of retail stores based on the following data:

	2023	2022
Rent expense – stores	Rs. 21,990,120	Rs. 19,875,890

Certain facts about the rent of stores are as under:

- There is an annual rent increase of 10%.
- The number of new stores opened during the year is 2.
- The number of stores closed during the year is 10.

The audit junior prepared a working detailing substantive analytical procedures in the following manner:

	Rupees
Rent expense for 2022	19,875,890
Add: 10% annual increase as per agreement	1,987,589
Expected rent expense for 2023	21,863,479
Actual rent expense for 2023	21,990,120
Difference – Immaterial	126,641

Required:

- (i) Analyze the working prepared by the audit junior and identify deficiency(ies) in above procedure, if any. (03)
- (ii) State any **three** substantive audit procedures to verify rent expense. (03)

- Q.4 ABC & Co, Chartered Accountants, has been appointed as the auditor of FoodPro Limited (FPL). While obtaining an understanding of accounting and financial reporting process, the audit semi senior has documented the following for the review of audit senior:

- (i) FPL utilizes an off-the-shelf accounting system for recording and processing its transactions. The general ledger and trial balance are extracted from the system, while draft financial statements are manually prepared on spreadsheets by the accountant.
- (ii) Transactions are initially recorded on manual vouchers. Manual vouchers are reviewed, checked, and approved by the chief accountant. Once the voucher is approved, it is sent for data entry.
- (iii) Data entry is carried out by junior accountants from various terminals, based on information received from data owners such as sales, purchases, and payments. Data entered by junior accountants is automatically processed by the system without any further manual intervention.
- (iv) Inventory valuation sheets are provided by the warehouse manager at month-end to be posted in the system as balancing entries to calculate monthly consumption of materials and cost of sales.

Required:

Identify any **five** control weaknesses and suggest a related control to strengthen the system. (10)

- Q.5 (a) Your firm is the auditor of MAB Limited (MAB), a company listed on Pakistan Stock Exchange, for the year ended 30 June 2023. MAB had issued its financial statements on 1 September 2023 in which a profit before tax of Rs. 1,700 million was disclosed.

On 10 September 2023 an ongoing litigation at the appellate forum was decided against MAB, resulting in a liability of Rs. 500 million to the taxation authorities. This was previously disclosed as a contingent liability in MAB's financial statement. MAB's legal team is of the view that the liability would amount to Rs. 150 million, and they have decided to file an appeal to a higher judicial forum. Considering the legal team's advice, MAB's management has decided to amend its previously issued financial statements by recognizing a provision of Rs. 150 million and disclosing the remaining Rs. 350 million as a contingent liability in its amended financial statements for the year ended 30 June 2023.

Required:

Discuss the implications on the audit report.

(07)

- (b) Aslam has been assigned the role of audit manager for the audit engagement of Exploration Limited (EL). While reviewing the draft financial statements, Aslam has identified significant increase in the value of specialized assets used in the drilling of wells due to a recent revaluation conducted by EL. The revalued amount of these assets is Rs. 4,000 million. Owing to the significance of the matter, Aslam engaged an independent valuation company "the Valuers" for the valuation of specialized assets. After completing their work, the Valuers submitted their valuation report, according to which the value of these assets should be Rs. 3,500 million.

The draft financial statements show a profit before tax of Rs. 2,500 million.

Required:

- (i) State any **five** key audit procedures which may be performed by the audit team to address the difference in the fair value of the assets. (05)
- (ii) Discuss the possible impact on the audit report if the difference is not adjusted. (03)

- Q.6 The audit team has started planning for the audit of Rustam Limited (RL), a sports product manufacturer, for the year ended 30 June 2023.

RL holds contracts with two well-known international sports brands, Sportify and Xcelerate, for manufacturing their sports equipment. The majority of RL's sales comprise export to these two brands. The audit team has observed and documented the following matters for the review of the audit manager:

(I) **Sportify's Sponsorship and Production Impact**

Sportify served as the main sponsor of a top-ranked football team associated with a German football club, a partnership that came to an end on 31 December 2022. Consequently, one of RL's production units remained non-operational for six months during the year and at the year-end. This unit was established in 2020 with the specific intention of meeting Sportify's product demand. RL intends to sell the inventory produced for Sportify within the local market. However, there is a prevalence of cheaper counterfeits of RL products available in the market.

(II) **Xcelerate's Production Outsourcing and Industry Developments**

Xcelerate specializes in selling sports kit and protective gear for high-impact sports. Xcelerate has outsourced its production to various manufacturers, one of which is RL. Recent injuries have prompted increased awareness and regulations concerning the reliability of such protective gear. Xcelerate has recently issued a press release that five severe injury incidents occurred which involved its products and they are investigating it. Further, Xcelerate is expected to undergo an acquisition by another company operating within the same segment, with the transaction likely to finalize by November 2023.

Required:

Discuss the business risks and the related audit risks from the above scenario.

(09)

Q.7 Yasin is an audit junior in a firm of chartered accountants. He has recently been assigned to an audit client where he was allocated the area of bank borrowings. Yasin performed the following audit procedures at the assertion level:

Assertion verified	Audit procedures performed
Completeness	<ul style="list-style-type: none"> ▪ Obtained a list of the schedule of bank borrowings from the client. ▪ Traced the amounts specified in the schedule of borrowings with the figures included in the trail balance. ▪ Conducted an inspection of assets provided as security.
Accuracy and valuation	<ul style="list-style-type: none"> ▪ Checked the accuracy of calculations in the schedule provided by the client. ▪ Reviewed loan agreements concerning new facilities received.
Rights and obligations	<ul style="list-style-type: none"> ▪ Obtained schedule of bank charges from the client. ▪ Checked the recorded amounts (both received and repaid) in the ledgers, cross-referencing them with bank statements.
Existence	<ul style="list-style-type: none"> ▪ Obtained bank borrowing ledgers and traced the recorded amounts received and repaid with bank statements. ▪ Obtained management representation.
Presentation and disclosure	<ul style="list-style-type: none"> ▪ Inquired from the management about relevant disclosures. ▪ Reviewed loan agreements, identifying terms and conditions such as interest rates, repayment terms, and securities/ mortgages/liens.

Required:

Identify the procedures that lack relevance to the above-mentioned assertions. Also, recommend any **two** additional procedures to be performed for each assertion.

(12)

Q.8 (a) Briefly discuss ‘Non-sampling risk’ and ‘Anomaly’ in respect of audit sampling. Also, provide an example for each of them.

(04)

(b) In certain circumstances, an entity may ask the auditor to change the terms of the audit engagement. What should the auditor do in such a situation?

(03)

(c) Discuss the impact on the key audit matter section of the audit report when the auditor expresses an adverse opinion.

(05)

(THE END)