



Certificate in Accounting and Finance Stage Examination

8 September 2025

3 hours – 100 marks

Additional reading time – 15 minutes

Audit and Assurance

Instructions to examinees:

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

Q.1 You are the audit manager in Khan & Company, Chartered Accountants, and are currently involved in the audit of Lahore Electronics Limited (LEL) for the year ending 30 September 2025. LEL is a listed company engaged in the import and distribution of consumer electronics.

The following information has been obtained during the planning stage:

- (i) Due to significant currency depreciation, the prices of imported goods have increased sharply. LEL's management is concerned about a potential decline in sales volume and has introduced a "buy now, pay later" scheme for retailers, offering extended credit terms of up to 180 days.
- (ii) In the prior year, a fraud was uncovered in which a warehouse supervisor colluded with a retailer to misappropriate inventory. Management claims to have strengthened internal controls over warehouse dispatches but has not provided documentation to support the changes in internal controls.
- (iii) LEL has recently expanded its supply network by importing products from multiple overseas suppliers. These goods are stored in third-party warehouses near the port before being delivered to LEL's facilities. Records of these goods are maintained separately by the warehouse operator and are manually integrated into LEL's records.

Required:

Identify and explain the audit risks from the above scenario and link each risk to the relevant component(s) of audit risk.

(10)

Q.2 You are the audit senior for Noor Engineering Limited (NEL), a listed manufacturing company. The audit for the year ended 30 June 2025 is at the finalisation stage.

During the audit, following matters have been noted:

- (i) Management has prepared a cash flow forecast for the next 12 months, showing sufficient liquidity despite incurring losses for the past three years. NEL also has renewed its major bank loan after the year-end.
- (ii) Inventory includes a significant quantity of slow-moving products. Management asserts that the net realisable value exceeds cost, based on expected sales during the next six months.
- (iii) During the year, NEL sold goods worth Rs. 45 million to a company owned by the CEO's spouse.
- (iv) NEL incurred marketing expenses of Rs. 500 million during the year, a substantial rise compared to prior periods.

Required:

For each of the above matters, discuss the need for obtaining a written representation.

(08)

- Q.3 You are the audit supervisor for Metro Plastics (Pvt.) Limited, a mid-sized manufacturer of plastic packaging materials. The audit for the year ended 30 June 2025 is currently in progress.

The audit senior has proposed using analytical procedures as substantive tests for payroll costs related to production, as these costs have increased sharply as compared to the previous year. The following information has been obtained from the client's records:

	2025	2024
Total payroll cost (Rs. in million)	142	109
Number of employees	140	132
Total overtime hours	12,500	8,000
Production volume (units)	4.6 million	4.5 million

Payroll is processed monthly through an internally developed payroll system, based on input provided by the human resource and production departments.

Required:

- (a) Explain the factors that should be considered when using analytical procedures as substantive audit evidence for payroll. (04)
- (b) Using analytical procedures, identify and explain the potential audit risks in payroll costs. (04)
- (c) Recommend further audit procedures the team should perform to address the specific risks identified in part (b). (04)

- Q.4 You are the audit manager for Atlas Textiles Limited (ATL), a company engaged in the manufacture and export of home textile products to various customers in the United States of America (USA). The audit for the year ending 30 September 2025 is currently in the planning stage.

The following matters have come to your attention:

- (i) ATL has 35 major overseas customers, accounting for Rs. 900 million and representing 60% of total receivables. At the end of each month, ATL translates all foreign currency balances at the closing exchange rate and records the translated balances in the receivables ledger.
- (ii) For several USA customers, ATL's sales are routed through agents who collect payments on behalf of ATL and deduct their commission therefrom before remitting the balance. The agents send monthly statements to ATL, but these are reconciled only on need basis.
- (iii) The audit senior has proposed using negative confirmations for balances below Rs. 10 million.

Required:

- (a) Identify and explain the key factors to be considered when planning and designing the external confirmation process for ATL's receivables. (04)
- (b) Discuss whether it would be appropriate to use negative confirmations for balances below Rs. 10 million in ATL's circumstances. (04)

During preliminary work, the audit team observed that one confirmation reply received directly from a USA customer showed a balance significantly lower than that recorded in ATL's ledger. The customer explained that part of the goods had been returned in early October 2025 due to quality issues.

Required:

- (c) State any **four** key audit procedures in response to the confirmation reply showing a lower balance than ATL's ledger. (04)

- Q.5 (a) You are the audit manager for Techno Pharma Limited (TPL), a listed company manufacturing pharmaceutical products. TPL uses an integrated ERP system (PharmaERP) for its sales, inventory, procurement, payroll and other functions. The audit for the year ending 30 September 2025 is currently in the planning stage.

From your preliminary review of IT controls, you noted the following:

- (i) A new inventory valuation module was deployed in July 2025. Test data was entered directly in the live environment for testing the system processing.
- (ii) Daily automated backups run at midnight and are saved to a network drive. The IT department confirmed that the backup location is separate from the live database but is located on the same premises.
- (iii) In PharmaERP, sales orders exceeding Rs. 1 million trigger an on-screen warning if the customer's outstanding balance plus the order amount exceeds the credit limit. The sales team leader has an override option to proceed without reducing the order quantity.
- (iv) For high-value items, warehouse staff are required to scan each item before dispatch. In case of scanner downtime, supervisors can process shipments by manually entering item codes into the PharmaERP.
- (v) The IT department maintains the master list of all active PharmaERP users. The list is updated based on monthly staff movement reports received from HR department.

Required:

For each of the above points, identify whether it relates to a General IT Control or an Application Control, and discuss the control weakness.

(07)

- (b) You are the audit manager of Karim Foods Limited (KFL), a manufacturer of spices and sauces for the year ended 31 March 2025. On 2 April 2025, a fire broke out in one of KFL's warehouses. Upon investigation, it was revealed that this warehouse primarily contained damaged, slow-moving and expired inventory, which had been carried at cost. Inventory records indicate that these goods had a cost of Rs. 105 million. The building, along with furniture, fixture and equipment, had a carrying value of Rs. 300 million.

Required:

Discuss the effect of the fire incident at KFL on the audit and state the substantive audit procedures to be performed.

(10)

- Q.6 You are the quality control partner at a chartered accountancy firm. The following two independent scenarios have arisen in relation to two of your audit clients:

- (i) Your firm is the auditor of Delta Elevators (Pvt.) Limited (DEL). Due to recent business losses and liquidity issues, DEL's management has requested a 25% reduction in the current year's audit fee, asserting that the reduced scale of operations justifies a lower level of audit effort. Furthermore, management has proposed that the audit fee may be increased in future years if the company returns to profitability.
- (ii) The engagement partner for Royal Furniture (Pvt.) Limited (RFL) has proposed purchasing furniture worth Rs. 4 million for the firm's office and Rs. 1 million for his residence from RFL. These purchases would be made under RFL's ongoing promotional scheme, which offers a 30% discount.

Required:

In light of the ICAP's Code of Ethics for Chartered Accountants, discuss the threat(s) involved and the fundamental principle(s) affected due to these threats. Also, evaluate the significance of these threat(s).

(13)

- Q.7 You are the audit manager at Almas & Company, Chartered Accountants, appointed as the external auditor of Shifa Diagnostics (Private) Limited (SDL) for the year ended 30 June 2025. This is the first time your firm is auditing SDL.

During the audit, following matters came to your attention:

- (i) SDL capitalized Rs. 40 million incurred on renovating leased laboratory premises. The lease agreement for these premises is for five years. The amount includes Rs. 10 million related to decorative and branding expenses.
- (ii) SDL is currently involved in a legal case concerning the alleged use of expired chemicals. Management has disclosed this matter in the notes to the financial statements. However, it has been widely covered in the national media and has resulted in the temporary closure of the branch by the health regulator.

SDL's profit before tax for the year ended 30 June 2025 is Rs. 90 million.

Required:

Evaluate the above situations and discuss their implications for the audit report. (12)

- Q.8 (a) Differentiate between the overall audit strategy and the audit plan. (05)
- (b) A client requests that the engagement letter should not include management's responsibility for internal control. Discuss, how the auditor should respond. (03)
- (c) List **five** operational events or conditions that may indicate a going concern problem for an audit client. (05)
- (d) Explain the effect of a disclaimer of opinion and an adverse opinion on the reporting of Key Audit Matters in the auditor's report. (03)

(THE END)