Certificate in Accounting and Finance Stage Examination

Audit and Assurance Essentials

18 August 2026
100 marks
3 hours and 15 minutes (including 15 minutes' reading time)

ICAP

Instructions to examinees:
(i) Answer all **NINE** questions.
(ii) Answer in **black** pen only.
(iii) Use the first page of the answer script to answer the Multiple-Choice Questions.

SECTION A

QUESTION 1

Select the most appropriate answer from the options provided for each of the following Multiple-Choice Questions.

(i) Solar Components Limited operates the following controls over procurement, invoice processing and supplier master data:

- Procurement officers initiate requests to create new suppliers and issue purchase orders;
- Accounts-payable staff record supplier invoices after a successful system-based three-way match;
- Requests to amend an existing supplier's bank account details are forwarded by procurement officers to accounts-payable staff together with an email received from the supplier; and
- The procurement manager reviews a monthly report of changes to supplier master data to confirm that newly created suppliers were appropriately authorised.

Which of the following controls would most effectively reduce the risk of payments being redirected to fraudulent bank accounts?

(a) Require accounts-payable staff to compare the amended bank details with the supplier's invoice and request forwarded by the procurement officer.
(b) Require procurement officers to retain screenshots of all amendments made to supplier records.
(c) Restrict bank detail changes to authorised personnel independent of the procurement function, require dual approval and perform an independent review of master-data change logs.
(d) Prohibit all amendments to supplier bank account details after a supplier has been created in the system. **(02 marks)**

(ii) While testing the operating effectiveness of purchase-authorisation controls, the auditor selects a sample of 80 purchase order numbers. During testing, the auditor identifies the following matters:

- One selected purchase order was properly cancelled before it was issued and therefore was not subject to the purchase authorisation control.
- The documentation relating to another selected purchase order cannot be located, and no alternative evidence of authorisation is available.

How should the auditor treat these two matters?

(a) Treat the properly cancelled purchase order as an anomaly and exclude it from the sample evaluation, but treat the missing purchase order documentation as a control deviation.
(b) Treat both matters as control deviations because the supporting documents were not available.
(c) Select replacements for both purchase orders so that the originally planned sample size is maintained.
(d) Select a replacement for the properly cancelled purchase order, but treat the missing purchase order as a control deviation. **(02 marks)**

(iii) The auditor of Apex Limited has identified the following uncorrected misstatements:

- Inventory overstated by Rs. 12 million;
- Operating expenses understated by Rs. 9 million;
- A legal provision understated by Rs. 6 million; and
- Revenue understated by Rs. 15 million.

Materiality for the financial statements as a whole is Rs. 20 million.

Which of the following is the most appropriate evaluation?

(a) The gross misstatements are Rs. 42 million, which exceeds materiality and therefore requires further evaluation both individually and in aggregate.
(b) The net effect is an overstatement of profit by Rs. 12 million, which is below materiality; therefore, no further evaluation is required.
(c) Each misstatement is individually below materiality and is therefore immaterial, regardless of their combined effect.
(d) As the net effect of Rs. 12 million is below materiality, the auditor should obtain a written representation from management and remove the misstatements from the summary of uncorrected misstatements. **(02 marks)**

(iv) The shareholders of Orbit Foods Limited passed a special resolution on 10 March 2026 to remove the company's existing auditors before the expiry of their term. On 15 March 2026, the board appointed another audit firm to fill the resulting vacancy.

Which of the following correctly describes the legal position under the Companies Act, 2017?

(a) The removal through a special resolution is valid; however, the appointment is not valid as it requires the prior approval of the Commission.
(b) Both the removal and the appointment are valid because the board filled the vacancy within 30 days.
(c) The removal is invalid because auditors appointed by members cannot be removed before the conclusion of the next annual general meeting.
(d) The removal is valid; however, the replacement auditor must be appointed directly by the Commission rather than by the board. **(01 mark)**

(v) Shortly before year-end, Urban Distribution Limited (UDL) purchased a warehouse for Rs. 320 million from a newly incorporated company introduced by its operations director. UDL normally uses third-party warehouses and had not previously planned to acquire its own warehouse. The transaction is material and outside UDL's normal course of business.

Which inquiry is specifically required under ISRE 2400 in relation to this transaction?

(a) Whether the acquisition was authorised by the board, legal title had transferred by year-end and depreciation commenced when the warehouse became available for use.
(b) Whether the purchase price was supported by an independent valuation, the consideration was paid through UDL's bank account and the warehouse was correctly classified as a fixed asset.
(c) The nature and business rationale of the transaction, including whether a related party may be involved.
(d) Whether the acquisition was included in the capital expenditure budget, how management intends to use the warehouse and whether it was adequately disclosed in the financial statements. **(01 mark)**

(vi) Coastal Traders Limited opened eight new branches during the year and extended credit to selected wholesale customers. Customer credit limits are set centrally. However, after the credit controller resigned, reports of customers exceeding approved limits were not reviewed for three months. A replacement was appointed shortly before year-end.

Despite the expansion in branch network, the audit senior intends to use the same sample sizes for revenue and receivables as in the prior year. Which option correctly classifies the resulting audit risk components?

	Issue 1: Expansion and extended credit	**Issue 2: Unreviewed reports**	**Issue 3: Unchanged sample size**
(a)	Increase control risk	Increase inherent risk	Increase detection risk
(b)	Increase inherent risk	Increase control risk	Increase detection risk
(c)	Increase control risk	Increase control risk	Increase detection risk
(d)	Increase inherent risk	Increase control risk	Increase control risk

(01 mark)

(vii) River Transport Limited has incurred recurring losses and is unable to meet liabilities falling due within the next twelve months unless its major bank loan is renewed. Although renewal negotiations are progressing satisfactorily, no binding agreement has been signed by the date of the auditor's report. Management's cash-flow forecast shows that the company can continue operating if the loan is renewed, and the financial statements adequately disclose the uncertainty and management's plans.

What is the appropriate reporting treatment?

(a) A qualified opinion because renewal of the loan remains uncertain.
(b) An adverse opinion because the company cannot presently meet its liabilities.
(c) An unmodified opinion with an Emphasis of Matter paragraph.
(d) An unmodified opinion with a separate Material Uncertainty Related to Going Concern section. **(01 mark)**

QUESTION 2

You are the audit manager responsible for the audit of Electronics Limited (EL), a consumer electronics retailer, for the year ended 30 June 2026.

The consumer electronics sector is experiencing market saturation, intense price competition and rapid technological change. The depreciation of the Pakistani Rupee has also increased the cost of imported products. Despite these concerns, EL placed substantial orders during the final quarter to meet purchase targets agreed with its major foreign suppliers to qualify for volume rebates. Consequently, EL's closing inventory increased by 38%. At year-end, approximately 25% of the inventory comprises models that have been held for more than six months.

EL's profit before tax margin increased from 2% in the previous year to 6% in the current year. The CFO attributes the improvement mainly to volume rebates of Rs. 180 million expected from foreign suppliers. EL recognised the entire amount as a reduction in cost of sales and recorded a corresponding receivable.

Rebate arrangements with suppliers are generally documented through electronic correspondence, while supplier discounts are normally reflected on individual purchase invoices. At year-end, EL had not received a separate rebate statement or a credit note from the relevant suppliers confirming the amount recognised.

Despite reporting a profit, EL generated a negative operating cash outflow of Rs. 150 million during the year. EL's principal bank facility requires it to maintain a minimum profit before tax margin of 5%.

Required:
Identify and discuss the business risks faced by EL and the related risks of material misstatement arising from the above scenario. **(10 marks)**

QUESTION 3

Salman is the audit supervisor assigned to the external audit of Nexus Appliances Limited (NAL) for the year ended 30 June 2026. He is responsible for reviewing the work performed by the audit team.

During the review, Salman uploaded NAL's complete receivables ageing report and selected customer contracts to a newly launched, freely available generative artificial intelligence (AI) platform using his personal account. The information uploaded included customer names, addresses, outstanding balances and contractual terms. Salman did not obtain NAL's consent or the firm's approval before uploading the information.

The platform identified potentially doubtful balances and generated explanations and suggested conclusions relating to those balances. Without independently evaluating the reliability and appropriateness of the output, Salman relied on these generated information when completing his review and concluded on the adequacy of NAL's allowance for doubtful debts. He completed the working papers using his usual review sign-off but did not document the use of the AI platform.

Required:
In light of the ICAP Code of Ethics for Chartered Accountants, identify and explain the threats to compliance with the fundamental principles arising from the above circumstances and evaluate their significance. **(11 marks)**

QUESTION 4

(a) Explain the factors that influence the auditor's selection of an appropriate benchmark for determining materiality. Also discuss why entities may require different materiality benchmarks. **(04 marks)**

(b) Explain the meaning of the term 'true and fair view'. Why does the auditor express an opinion on whether the financial statements give a true and fair view rather than certify that they are completely accurate? **(05 marks)**

SECTION B

QUESTION 5

You are the audit manager responsible for the audit of Sun Pharma Limited (SPL), a listed pharmaceutical manufacturer, for the year ended 30 June 2026. The draft financial statements show profit before tax of Rs. 600 million.

During the year, SPL incurred Rs. 90 million on laboratory investigations and the screening of compounds for a potential new medicine. At the reporting date, management was assessing the test results for several possible compounds. Further testing was planned to determine whether any compound should be selected and taken forward for product development and regulatory approval.

Management capitalised the entire expenditure as an intangible asset and recognised amortisation of Rs. 9 million during the year. Management believes that the medicine's anticipated commercial prospects justify capitalisation and has referred to a feasibility study prepared by an independent external advisor in support of its treatment.

Required:
Evaluate the capitalisation of expenditure incurred on the potential new medicine and discuss its implications for the auditor's report. ***(Audit procedures are not required)*** **(06 marks)**

QUESTION 6

You are the audit manager at Bilal & Company, Chartered Accountants. You are reviewing the working papers of Star Streaming Pakistan (Pvt.) Limited (SSP) for the year ended 30 June 2026.

SSP provides a prepaid, subscription-based video-streaming service. Subscribers are charged a standard monthly fee of Rs. 900. Subscription revenue is recognised over the relevant monthly subscription period.

SSP has reported subscription revenue of Rs. 950 million for the year ended 30 June 2026. Yasir, an audit junior, performed a substantive analytical procedure to obtain audit evidence regarding subscription revenue. He performed the following analysis:

Active subscribers at 30 June 2026, according to the Marketing Department's monthly promotional report	89,000
Standard monthly subscription fee	Rs. 900
Expected annual revenue (89,000 × Rs. 900 × 12 months)	Rs. 961.2 million
Recorded subscription revenue	Rs. 950.0 million
Difference	Rs. 11.2 million

In response to Yasir's inquiries, the Marketing Director explained that:

- the monthly promotional report includes users benefiting from a one-month free trial; and
- the number of subscribers increased gradually during the year.

Yasir concluded that the difference of Rs. 11.2 million was below the materiality of Rs. 15 million determined for the financial statements as a whole. He also considered the explanations provided by the Marketing Director to be reasonable and, therefore, concluded that no further audit work was required.

Required:

(a) Evaluate whether the substantive analytical procedure performed by Yasir provides sufficient appropriate audit evidence regarding subscription revenue. **(07 marks)**

(b) Based on your evaluation in part (a), state the audit procedures that the audit team should perform to obtain sufficient appropriate audit evidence regarding subscription revenue. **(08 marks)**

QUESTION 7

You are the audit manager responsible for the audit of Delta Limited (DL) for the year ended 30 June 2026. DL's financial statements show a profit before tax of Rs. 600 million.

On 10 June 2026, a fire damaged inventory stored at one of DL's warehouses. DL appropriately wrote-off the damaged inventory. In addition, management recognised an insurance claim as other income and a corresponding insurance receivable of Rs. 120 million in respect of a claim submitted under DL's fire insurance policy.

On 15 August 2026, the insurer rejected the claim because DL's electrical safety certificate had expired on 5 June 2026, which was a necessary condition of the insurance policy for a valid claim. Management intends to initiate legal proceedings against the insurer. They argue that DL had applied to renew the certificate on 31 May 2026 and that the renewal was delayed by the relevant regulatory authorities. Therefore, management believes that the insurer's rejection is unjustified and does not intend to amend the financial statements.

Management has finalised the financial statements, and the audit team has prepared a draft auditor's report for discussion with management and those charged with governance.

Required:

(a) Evaluate the above matter and discuss its effect on DL's financial statements for the year ended 30 June 2026. Also state the audit procedures that the auditor should perform in respect of this matter. **(09 marks)**

(b) Based on your evaluation in part (a), discuss the implications for the auditor's report. **(05 marks)**

QUESTION 8

You are the audit manager in a firm of Chartered Accountants responsible for the audit of Eagle Industries Limited (EIL) for the year ended 30 June 2026. The audit is at the finalisation stage.

You provided the draft written representation letter to EIL's Chief Executive Officer (CEO) for approval and signature. The CEO returned the signed representation letter but deleted the following paragraph:

> "We have disclosed to you our knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others."

The CEO informed that, EIL cannot provide this representation because EIL has received anonymous whistle-blower emails alleging possible fraud within the procurement department. EIL is investigating the matter internally and considers it confidential.

Management has not provided the audit team with any details of the allegations or the internal investigation.

Required:

(a) Evaluate the CEO's refusal to provide the specific written representation and discuss the auditor's course of action. **(06 marks)**

(b) In accordance with ISA 240 – The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements, discuss how the auditor should respond to the risk of material misstatement arising from the whistle-blower allegations. **(05 marks)**

(Implications on audit report are not required)

QUESTION 9

You are the audit senior assigned to the statutory audit of Super Core Industries Limited (SCIL), a listed company that manufactures steel components for the construction and energy sectors, for the year ended 30 June 2026.

The following is a summary of the responses received in respect of positive external confirmation requests sent to selected customers:

Customer	Balance per SCIL's ledger	Balance confirmed by the customer	Remarks
	------------- Rs. in million	-------------	
AA Builders (Pvt.) Limited, which is also a supplier of SCIL	41.00	41.00	Signed PDF document received through SCIL's finance manager. Balance agreed.
Star Steel Distributors (Pvt.) Limited	24.00	14.00	Direct response from customer received. Goods of Rs. 10 million are held on consignment and payable only when sold.
Mega Contractors Limited	36.00	39.50	Direct response from customer received. Additional SCIL invoice of Rs. 3.50 million relates to goods received on 30 June 2026.
Malik & Co.	0.30	-	Direct response from customer received. No purchases made from SCIL.

Required:

Evaluate the results of the external confirmation exercise for each customer listed above and recommend **three** audit procedures in respect of each customer balance. **(14 marks)**

(THE END)