CERTIFIED PUBLIC ACCOUNTANTS

INTERMEDIATE LEVEL EXAMINATIONS

I1.4: AUDITING

DATE: FRIDAY 30, AUGUST 2024

MARKING GUIDE & MODEL ANSWERS

QUESTION ONE

MARKING GUIDE

Q/NO	CRITERIA OF AWARDING MARKS	MARKS
Q1(a)	For each correct discussed responsibility, Award 1mark (max 5 marks)	5
Q1b(i)	For the correct definition of audit risk award 2marks	2
Q1b(ii)	For each correct component stated, Award 1mark & correct explanation 2marks (max 9)	9
Q1(c)	For the correct definition award 1 mark and for each correct reason stated award 1 mark (max 4)	4
Total marks		**20**

MODEL ANSWERS:

a) Responsibilities of an auditor in relation to errors and frauds and for the entity's compliance to laws and regulations:

The auditor does not have a specific responsibility to prevent errors and fraud, as it is the responsibilities of management to institute strong internal control systems that should prevent errors and fraud, but he must **consider** whether it has caused a material misstatement in the financial statements but generally, the following are the responsibilities:

1. **To test and examine the internal control systems of the client:** The auditor is responsibility is to employ audit tests to examine whether the ICS of the client is able to prevent errors and frauds.
2. **To employ audit test which are able to detect errors and frauds:** should employ reasonable audit tests capable to detect errors and frauds in client's financial statement.
3. **To report the error and frauds to the management:** it is the responsibility of an auditor to report errors and frauds discovered during an audit to the management.
4. **To recommend to management to correct the errors identified:** the auditor has the responsibility to request the management to correct the errors identified in the books of accounts through management letter.
5. **To qualify the report if the errors and frauds identified are material:** in case the material misstatements identified in the financial statements are material and management refuses to correct them, the auditor should consider qualifying the report.
6. **To exercise professional scepticism during the conduct of audit:** to conduct an in depth audit or risk based approach where there is suspicion of errors and frauds.

b)

i.

An audit risk: This is the risk that an auditor expresses an inappropriate opinion on the financial statement due biasness or due to the underlying circumstances.

ii. Components of an audit risk:

1. **Detection risk:** The risk that the audit tests employed by an auditor may fail to detect misstatement in **the financial statements of the client.**
2. **Control risk**: The risk that the clients internal control systems may fail to prevent perpetration of misstatements in financial statement.
3. **Inherent risk**: This is an audit risk due to the susceptibility of an account balance or class of transactions to material misstatement, due to the complexity of underlying transactions. It may be due to the characteristics of those items such as the fact they are estimates, complex calculations etc.

c) Materiality means where, misstatement or an omission in the financial statements could influence the economic decision of users taken on the basis of information available.

Reasons as to why an auditor should asses' materiality:

1. To determine which method to use in gathering audit evidence.
2. To determine which items to examine.
3. To determine how many items to examine.
4. To determine which Audit procedures to be employed to reduce audit risk.

QUESTION TWO

MARKING GUIDE

Q/NO	**CRITERIA OF AWARDING MARKS**	**MARKS**
Q2 (a)	For each correct deficiency identified award 0.5 mark per each valid point and brief explanation award 0.5 mark (max 1)	2
Q2 (b)	Stating the correct technique award 1 mark and to describe award 2 marks per each valid explanation (max 3 per technique)	12
Q2 (c)i.	For the correct definition of audit program award 2marks	2
Q2 (c)ii.	Stating the correct activity award 0.5 mark per each valid point and explaining award 0.5 mark (max 1 per activity)	4
Total marks		**20**

MODEL ANSWERS

a) Deficiencies in the purchasing system of PRT Rwanda Ltd:

1. The managing manager determines store inventory levels without consulting those the store's manager.
2. Store manager are responsible for reordering through the purchasing manager and it can take up to four weeks before goods are received.
3. Purchases orders reviewed and authorized by the purchasing director are aggregated at the districts,
4. Poor internal checks as records are matched manually

b) Techniques for recording and assessment of control systems:

1. **Narrative notes:** These are written descriptions of processes and procedures, which will help in understanding the client system.
2. **Internal control questionnaire:** These are short and clear, designed questions used to ask whether controls exist or not. They should be designed in a manner that short answers, such as yes and no are given.
3. **Flow charts:** This is a diagrammatic representation which shows the flow of a process through an accounting system. It represents the sequence of processes.
4. **Checklists:** This is in the form of the ICQ but the difference is that, instead of asking questions, statements are made to mark off and tick boxes are used to show where the statement is true.

c)

- **i)** **Audit program**: This is a prior action plan, which documents procedures to be followed by an auditor in examination of a particular component of financial statements.
- **ii)** **Accounting control activities in relation to audit program for purchases:**

1. **Examine the cut-off:** This involves checking as to whether all the purchases which relate to current period under review has been recorded.
2. **Authorization of payments:** Ensure as to whether there is proper authorization on payment of both cash purchases and credit purchases.
3. **Reconciliation of credit control accounts to the list of purchases ledger:** Check as to whether the creditors balances reconcile with purchases control accounts.
4. **Recording of purchases ledger and returns day book:** Ensure as to whether the recording of returns inwards has been made and properly recorded in the control accounts.
5. **Segregation of duties:** Check as to whether there is division of activities in processing of transactions

QUESTION THREE

MARKING GUIDE

Q/NO	**CRITERIA OF AWARDING MARKS**	**MARKS**
Q3(a)	For every correct stated assertion award 1mark and for explanation 1 mark (max 2 per point)	8
Q3(b)i.	For a correct definition award the 2 marks (max 2)	2
Q3(b)ii.	For the correct statement award 1 mark and explanation award 1.5 mark (max 2 per point)	10
Total marks		**20**

MODEL ANSWERS

a) Assertions used by an auditor during the audit of financial statements:

1. **Existence**: The auditor should ascertain that assets and equity interest exist
2. **To determine Completeness:** All assets, liabilities and equity that should have been recorded have been duly recorded and relevant disclosures.
3. **Classification**: That assets, liabilities and equity have been properly recorded in proper accounts.
4. **Accuracy, valuation and allocation**: That assets, liabilities and equity have been included in the financial statements in appropriate amounts.
5. **Presentations**: Assets, liabilities and equity components have been aggregated or disaggregated and clearly described in the context of applicable financial reporting framework.
6. **Rights and obligation**: The entity holds and controls the rights of assets and obligation of a liabity.
7. **Occurrence**: Transactions and events recorded in the financial statements have been occurred and relates to the entity.
8. **Cut-off**: Transactions and events have been recorded for the period which they belong.

b)

i) An audit report is a means of communication by which the external auditors express their opinion on the true and fair view of the financial statements of a company.

ii) **Effects of material misstatements on the financial statements on the audit reporting**:

1. If there are no issues or any uncorrected material misstatements, the auditor will probably issue a clean audit report (unmodified).
2. If there are uncorrected material misstatements and management agree to adjust the financial statements, the auditor will probably issue a clean audit report.
3. If management refuses to adjust the financial statements and the results of any extended audit procedures do not enable the auditor to conclude that the aggregate of the uncorrected misstatements is not material, then the auditor needs to consider a qualification in his audit report (modified).

4. If management refuses to adjust the financial statements but the results of any extended audit procedures enable the auditor to conclude that the aggregate of the uncorrected misstatements is not material, then the auditor may issue a clean audit report. However, the auditor would need to consider the actions of management in this case.
5. If management refuses to adjust the financial statements but the results of any extended audit procedures enable the auditor to conclude that the aggregate of the uncorrected misstatements is material, then the auditor may issue a modified audit report. However, the auditor would need to consider the actions of management before the issue of modified report.

QUESTION FOUR

MARKING GUIDE

Q/NO	CRITERIA OF AWARDING MARKS	MARKS
Q4 a.i	For each point correctly stated, award 0.5 mark and explanation 0.5 mark (max 1)	4
Q4 a.ii	For correct explanation award 2 marks for each	4
Q4 b.i	For correct definition award 2 marks (max 2)	2
Q4 b.ii	For each correctly stated audit evidence on opening balances by an auditor in regard to initial audit engagement award 1 mark (max 3) and max 3 for audit evidences audit evidences with regard to prior period audited by another auditor.	6
Q4 c.i	For correct description award 1 mark (max 1)	1
Q4 c.ii	To state a correct point award 0.5 mark and explanation 0.5 mark (max 3)	3
Total marks		**20**

MODEL ANSWERS:

a)

i) Circumstances in which sampling may be applicable as a means of gathering audit evidence:

1. **When items to be audited are homogeneous:** When the items which are to be examined contains common characteristics.

2. **When the internal control system of the client is strong:** When the auditor has tested and belief that the internal control systems of the client are strong, hence no chance of errors and frauds.

3. **When the population of items to be audited is too large:** If the items to be audited are too many and 100% audit cannot be ideal.

4. **Where the audit resources are limited:** In case where the audit resources are limited, such as time and audit staff.

5. Where the auditor has previous experience about the client business

ii) Audit sampling key terms

Sampling risk: This is the risk that the auditor makes a wrong audit opinion based on the results obtained from the sample or the conclusion reached on a sample may be different if the entire population was subjected to the same audit procedures.

Tolerable error: This is the maximum amount of an error an auditor is willing to accept in the sample and go on and conclude that the audit objectives were made.

b)

i) Opening balances are those balances of closing balances of the prior period and reflect transactions of and accounting policies applied to the prior period, it may include any relevant matters affecting balances that form part of disclosures at the end of the financial year.

ii) Audit evidence required on opening balances by an auditor in regard to initial audit engagement.

1. That the opening balances do not contain material misstatements that may affect the current period financial statements under review.
2. As to whether the prior periods closing balances have been brought forward correctly in the current period.
3. That appropriate accounting policies have been consistently applied or any change in accounting policy has been properly accounted for and disclosed.
4. As to whether any post balance sheet event in prior period are properly accounted for in the current period.

Audit evidence with regard to prior period audited by another auditor:

1. Reviewing the other auditors' working papers.
2. Consider professional competence and independence of the other auditor.
3. If the previous periods report was qualified, the auditor should seek reasons for qualification and particular attention of those matters which let to qualification in the current year.

c)

i) comparative financial statements: This are the amounts and other disclosures for the preceding period that are included for comparison with the financial statements of the current period but do not form integral part of the current year's financial statements.

ii) Responsibilities of an auditor in relation to corresponding figure in comparative financial statements:

1. To ensure that the accounting policies used for corresponding amounts are consistent with the current period and as to whether appropriate adjustments and disclosure have been made
2. Corresponding amounts agree with the amounts and disclosures presented in the preceding and that they are free from errors.
3. Whether any adjustment made in correspondence are in conformity with the relevant accounting standards and legislation and that there is proper disclosure.

QUESTION FIVE

MARKING GUIDE

Q/NO	CRITERIA OF AWARDING MARKS	MARKS
Q5 a)i.	For a correct responsibility stated award 1 mark and for correct explanation award 1 mark (max 8 for before the date of report and Max 6 for points on after date of report}	14
Q5 b)i.	For the correct point stated award 1 mark (max 1)	3
Q5 b)ii.	For correct audit stated award 0.5 mark and correct explanation award 0.5 mark (max 1)	3
Total marks		**20**

MODEL ANSWERS:

a) Responsibilities of an auditor before date of the report.

1. Perform additional audit procedures sufficient and appropriate to obtain additional evidence on these matters.
2. For those matters which require adjustments, the auditor should recommend to the management for such adjustments before issue of the final report.
3. For non-adjusting events the auditor should disclose those matter to financial statements
4. If the auditor considers the matters to be affecting financial statements materially, and the management fails to rectify them, he should consider qualifying the report but if the matters are corrected, he should consider revision of the financial statements
5. Obtain written representations from the management that all the subsequent events that need adjustment or disclosure have been adjusted or disclosed.
6. if the going concern of the company may be in doubt as a result of tank spillage, the auditor should gather sufficient evidence that such disclosure have been made and where possible provide an emphasis matter paragraph where a clean opinion is issued.

Responsibilities of an auditor after the date of the report:

1. Discuss the matter with management and those charged with governance
2. Determine as to whether the financial statements need amendment
3. If amendments are required, enquire how the management intends to address the matters in the financial statements.

b)

i) Matters to be taken into consideration by public sector auditors to achieve the objective of the audit:

1. Plan each audit with thorough understanding of entity to be audited

2. Work closely with the internal auditors

3. Consider proper timing of an audit

4. Consult with public sector bodies regarding their overall audit approach

5. Focus on key risk areas

6. Be accessible throughout the year to public sector entities.

ii. Types of public sector audits

1. **Financial Audit:** This is an audit which aims to ensure that the financial statements of audited entities present true and fair view during the reporting period. This means they are free from material misstament.
2. **Compliance audit:** This is an audit which is aimed to validate as to whether an entity's transactions have been undertaken in correspondence with the relevant laws and regulations.
3. **Performance audit:** It is also known as value for money audit, which looks at efficiency, effectiveness and economical usage of public resources.

QUESTION SIX

MARKING GUIDE

Q/NO	CRITERIA OF AWARDING MARKS	MARKS
Q6 a)i.	Award 1 mark for every correct stated point and 1 mark for correct explanation (max 2)	8
Q6 a)ii.	Award one mark for each correct stated point (max 1)	4
Q6 b)i.	For correct definition of an audit committee award 2 marks (max 2)	2
Q6 b)ii.	For each stated correct point award 0.5 mark and correct explanation award 0.5 mark (max 1)	6
Total marks		**20**

MODEL ANSWERS:

a)

i) Pillars **of corporate governance:**

1. **Transparency:** This mean openness and having nothing to hide. This enables necessary disclosures that allows information to freely flow to all stakeholders. This will allow all entity's activities can be observed and examined at any particular time.
2. **Responsibility:** This is the authority to act on behalf of the organization. Therefore, those charged with governance should accept full responsibility of the powers conferred to them. This requires them to act to the best interest of an organization.
3. **Fairness:** This means equal treatment of all stakeholders and ensure equitable distribution of resources.
4. **Accountability:** This is an obligation or willingness to accept responsibility or to account for one's actions.

ii) Characteristics of a good corporate governance:

1. Fair remuneration and benefits.

2. Fair performance appraisal

3. Fair financial reporting

4. Sound internal control systems

5. Oversight non-executive board of directors

6. Effective management

7. Good relationship with directors

b)

i) **An audit committee** is a sub-committee of independent non-executive directors which is responsible for the oversight of the financial reporting and disclosure process.

ii) **Specific roles of audit committee:**

1. Improve the quality of financial reporting by reviewing on behalf of the board
2. The strengthen the independence and reporting of both external and internal auditors
3. Increase public confidence on credibility and objectivity of financial statements.
4. Provide a channel of communication both for internal and external auditors
5. Strengthen the position of internal audit department6.Relief main board of directors to concentrate on more important matters
6. Create acclimate of discipline and controls, hence minimal errors and frauds.

End of Marking Guide and Model Answers.