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CERTIFIED ACCOUNTING TECHNICIAN
STAGE 3 EXAMINATION
S3.4: AUDIT AND ASSURANCE
DATE: TUESDAY 27, FEBRUARY 2024
MARKING GUIDE AND MODEL ANSWERS

Question	Answers
1	D
2	B
3	B
4	C
5	A
6	A
7	D
8	C
9	B
10	D
11	B
12	A

Each question has 2 Marks.

Total marks for section A (20 Marks)

Model answers

QUESTION ONE

The correct answer is D

All the following factors plays a contributes to commission of fraud (i)Incentive to commit fraud(ii)Rationalization of the act(iii)Perceived opportunity to do so(iv)Individual leaving beyond their means (v)People believe that the accounting system can be overridden.

QUESTION TWO

The correct answer is B

(B) Circularize the debtors to confirm the amount of inventory sold to does not help in determining the value of stock but rather a method of confirming the debtors' balance. Test that can effectively be used to establish the value of inventory to be recognize therefore include(A)Reviewing and testing the client's system for identifying slow-moving, obsolete or damaged inventory to determine its effectiveness in identifying items which may be written down to NRV(C) Review quantities of good sold after the year end to determine that inventory at the year-end has been, or will be realized and (D) Observing whether correct cut-off procedures are being followed in the dispatch and receiving areas.

QUESTION THREE

The correct answer is B

Test of controls for inventory would include : (i) Select a sample of inventory movements records and reperform matching to goods received and dispatched notes, (iii) Confirm that movements of inventory have been authorized. **However**, test of control for expenditure, register, depreciation tests are done on non-current assets and therefore making choice A, C and D inappropriate

QUESTION FOUR

The Correct Answer is C

The control objectives over inventory are; (A) To ensure that all inventory movements are authorized and recorded, (B) To ensure that inventory is safeguarded against loss, pilferage or damage and (D) To ensure that the levels of inventory held are reasonable. However, to ensuring that inventory is classified as a current asset is an assertion management assertion relating to presentation and disclosure

QUESTION FIVE

The correct answer is A

The correct answer is **A**. The auditor has a right to require from the company's officers such information and explanations as the auditor thinks necessary for the performance of his duties as auditor; receive a copy of any written resolution proposed and receive all notices of and communications relating to such meetings which any member of the company is entitled to receive. He does not however, have a right to coordinate general meeting as stipulated in (ii) has a right of access at all times to the books, accounts and vouchers of the company contrary to (iv) that suggests limited times access.

QUESTION SIX

The correct answer is A

Test (iii) is for beneficial ownership while testing the completeness. Thus, test (i), (ii), (iv) apply to valuation.

QUESTION SEVEN

The correct answer is D

The duties of the auditor during the stock take are (i) Observe whether the client's staff are following instructions (ii) Record fully the work done and the impressions of stock take in the working papers and (iv) Take note of movement of inventory during the count. However, (iii) Review surrounding systems of internal control to identify areas of potential difficulty and Confirm that client's final valuation of inventory has been calculated correctly to confirm accuracy are done before and after the inventory count respectively.

QUESTION EIGHT

The Correct Answer is C

(i) Suppliers with material balances at the year-end, and(ii) Suppliers which have a high volume of business with Uwineza Ltd s and (iii) Major suppliers of Uwineza Ltd with nul balances at the year-end should selected for review to ensure correctness of the trade payables.

QUESTION NINE

The correct answer is B

While all procedures would be valid in the circumstance, only the written confirmation from the company's lawyer would allow the auditor to obtain an expert, third party confirmation on the likelihood of the case being successful. This would provide the auditor with the most reliable evidence in the circumstance.

QUESTION TEN

The correct answer is D

This all the following describes auditing procedures for the valuation of inventories.

1. Ensuring that allocation of overheads is appropriate
2. Confirming inventories are valued at lower of cost and net realizable value
3. Reviewing price changes near the year end
4. Ageing the inventory held

SECTION B

QUESTION 11

Marking guide

Maximum marks

- a) Describe the substantive procedures that will be performed to obtain sufficient and appropriate audit evidence about the acquisition and depreciation of the gym equipment. *(1 mark for each valid procedure, 3 marks Maximum on depreciation and the same on Additional equipment).* (6 Marks)
- b) List FOUR assertions relevant to the audit of tangible non-current assets and state one audit procedure which provides appropriate evidence for each assertion. *(0.5 marks for an assertion and 0.5 marks for a relevant audit procedure).* (4 Marks)

Total marks

(10 Marks)

Model answers

- a) **The substantive procedures that will be performed to obtain sufficient and appropriate audit evidence about the acquisition and depreciation of the gym equipment:**

Depreciation

- i. Review the reasonableness of the depreciation rates applied to the new gym facilities and compare to industry averages.
- ii. Review the capital expenditure budgets for the next few years to assess whether there are any plans to replace any of the new leisure equipment, as this would indicate that the useful life is less than 10 years.
- iii. Review profits and losses on disposal of assets disposed of in the year, to assess the reasonableness of the depreciation policies.
- iv. Select a sample of leisure equipment and recalculate the depreciation charge to ensure that the non-current asset register is correct.
- v. Perform a proof in total calculation for the depreciation charged on the equipment, discuss with management if significant fluctuations arise.
- vi. Review the disclosure of the depreciation charges and policies in the draft financial statements.

Additional gym equipment

- i. Inspect vendors' invoices to confirm valuation and ownership of the gym equipment.
- ii. Verify whether capitalization of expenditure is correct by considering for NCA additions and items in relevant expense categories (repairs, motor expenses sundry expenses): capital/revenue distinction correctly drawn and capitalization in line with consistently applied company policy to determine whether costs have been correctly classified.
- iii. Confirm purchases have been properly allocated to correct NCA account by inspecting a sample to confirm that all items of capital expenditure have been correctly classified.

- iv. verify that purchases have been authorized by directors/senior management by inspecting board Minutes
 - v. verify that additions recorded in NCA register have been recorded in the General ledger to confirm completeness.
- b) Four assertions relevant to the audit of tangible non-current assets and relevant audit procedure:**
1. Completeness – ensure that all non-current assets are recorded in the non-current asset register by agreeing a sample of assets physically verified back to the register.
 2. Existence – ensure non-current assets exist by taking a sample of assets from the register and physically seeing the asset.
 3. Valuation and allocation – ensure assets are correctly valued by checking the reasonableness of depreciation calculations.
 4. Rights and obligations – ensure the company owns the asset by seeing appropriate document of ownership for example, a purchase invoice.
 5. Presentation and disclosure assertions – ensure all necessary financial statements disclosures have been made by reviewing the financial statements and ensure non-current assets are correctly categorized in those financial statements

QUESTION 12

Marking guide

Maximum marks

- a) Describe Five matters Katuna CPAs should have considered before accepting to audit Majyambere Co. *(1 mark for each valid point).* (5 Marks)
- b) Calculate at any Two ratios, for both years, which would assist you in planning the audit of Majyambere Co. *(0.5 marks for each year's ratio; 2 ratios for two comparative years (2*2*0.5= 2 marks).* (2 Marks)
- c) From a review of the above information and ratios calculated, describe Three audit risks, and explain the auditor's response to each risk in planning the audit of Majyambere Co. *(0.5 marks for identifying audit risk, 0.5 marks for response to that risk).* (3Marks)

Total marks

(10 Marks)

Model answers

- (a) Matters Katuna cpas should have considered before accepting to audit Majyambere Co:**
- (i) Issues that could threaten compliance with ICPAR code of ethics or any local legislation, such fee charged on Majyambere Co, to ensure they are not dependent one client, as well as conflict of interest
 - (ii) They should consider their competence to do the job, and appropriate of resources, as well as any specialist skills or knowledge to audit Majyambere Co.

- (iii) Level of risk should also be considered to established whether it is within the firm's acceptable risk levels.
- (iv) Communication with outgoing auditor as matter of professional courtesy and to establish whether there are any ethical reasons why they should not accept the appointment.
- (v) Consider the reputation of directors and their integrity and where necessary obtain references on the directors if they are not personally known to them.

(b) Any two ratios, for both years, which would assist you in planning the audit of Majyambere Co:

Ratio	Formulae	2022	2021
Gross margin	Gross profit/sales*100	9390/25230= 37.2%	7165/21180= 33.8%
Operating margin	Operating profit/sales *100%	4487/25230= 17.8%	3980/25230= 18.5%
Inventory holding period	Inventory /cost of sales *365	2360/15840*365= 54 days	1800/14015*365 47 days
Inventory turnover	Cost of sales/inventory	15840/2360 6.7	14015/1800 7.8
Receivables collection period	Trade receivables/sales *365	1590/25230*365 =23 days	1250/1800= 22 days
Payables payment period	Trade payables/purchases*365	3500/15840* 365= 81 days	2800/14015= 73 days
Current ratio	Current assets/current liabilities	3950/4080= 0.97	2530/2800 =1.16
Quick ratio	Current assets- inventory /current liabilities	(3950- 2360)/4080= 0.39	(3530-1800)/2800= 0.62

(c) Three audit risks and the auditor's response to each risk in planning the audit of Majyambere Co:

Audit risk	Auditors' response
Since majyambere is a new client for Katuna CPAs there is increased detection risk	Get experience team, adequate time allocation to team members to gain a proper understanding of the client's business and the risk of material misstatement.
Use of perpetual inventory instead of full year end count. Under such a system, all inventory must be counted at least once a	The completeness of the perpetual inventory count should be reviewed and the controls

<p>year with adjustments made to the inventory record on a timely basis. inventory could be under or overstated if the perpetual inventory counts are not adequate.</p>	<p>over the counts and adjustment to record should be tested.</p>
<p>There were large number of exceptions where the inventory records were consistently higher than the physical inventory. This means the value of inventory could be overstated</p>	<p>The level of adjustment made to inventory should be considered to assess their significance. This should be discussed with management as soon as possible to place reliance on the inventory records at the year end, which could result in the requirement for a full year end count</p>
<p>During the count it was noted that some lines of inventory were at least 90 days old. Additionally, the inventory holding period has gone up from 47 days in 2021 to 54 days in 2022.this means that there is a possibility of an increase in slow moving stock.</p> <p>IAS 2 requires that inventory be valued at the lower of cost and net realizable amounts. There is risk of obsolete inventory which should be written down to its realizable amount to avoid overvaluing inventory</p>	<p>Ageing of inventory should be reviewed and discussed with management to identify slow moving goods.</p> <p>Analysis of cost and net realizable values should be done to assess any need for writing down some inventory.</p>
<p>There are four additional sites where some accounting records are maintained, and these sites were not visited during the interim audit. The records are incorporated monthly through an interface to the general ledger. Katuna CPAs need to obtain appropriate evidence for all site.</p> <p>There is increased detection risk if the audit team does not undertake testing of the records at this site.</p> <p>Also, if the interface to the general ledger does not occur as expected, there is a risk that accounting record are incomplete.</p>	<p>Discuss with the management the significance and materiality of the records maintained at the four sites. The team may visit some of these sites during the final audit to undertake testing of the records held there. CAATs could be used by the team to sample test the monthly interface of data from each site to head office to identify any errors.</p>
<p>A building was only sold in 2022 at a loss of FRW 825 million. There is risk that this disposal has not been properly accounted for. The loss on disposal could be an indicator of wrong application of the depreciation policy an indication that the depreciation policy for land and building may be inappropriate,</p>	<p>Agree that the asset has been removed from the non-current assets register, recalculate the loss on disposal calculation and agree all items to supporting documentation.</p>

<p>leading to understating of depreciation and overstatement of assets</p>	
<p>Gross profit margin has increased from 33.8% to 37.2% while operating margin has decreased from 18.5% to 17.8%. This movement in gross margin is significant and there is a risk that cost may have been omitted or included in operating expenses rather than cost of sales.</p>	<p>The classification of costs between cost of sales and operating expenses will be compared with the prior year to ensure consistency. Also increased cut-off testing should be performed at the year end to ensure costs are complete.</p>
<p>The overall liquidity of the company is in decline with the current and quick ratios decreasing from 1.26 to 0.97 and 0.62 to 0.39 respectively. In addition, the cash balances have decreased significantly over the year, and the company now has an overdraft of FRW 580,000 at the end of the year. Further, the trade payables payment period has increased from 73 to 81 days, implying the company is struggling to meet their liabilities as they fall due. All of these changes in key ratios could signal going concern difficulties.</p>	<p>Detailed going concern testing to be performed during the audit as there may be a doubt over going concern and the basis of accounting should be discussed with management to ensure that the going concern basis is reasonable.</p>

SECTION C

QUESTION 13

Marking guide

Maximum marks

- (a) Explain to Kigali Three things must exist for the company to bring a successful negligence claim against the auditors and state whether the case will be ruled in their favor. *(2 marks for well explained point otherwise 1 for stated point (3*2=6), 2 marks for correctly stating the expected outcome of the case* (8 marks)
- (b) Define a fraud and describe the auditor's responsibilities in relation to fraud and errors. *(2 marks for well definition of fraud ;1 mark for correctly describing auditor' responsibilities up to 1*3 =3 marks)* (5 marks)
- (c) Identify Five responsibilities for the directors in relation to the books of accounts. (5 marks)
- (d) Explain professional skepticism in light of auditor's responsibilities as far as detection of errors and frauds is concerned. *(2 marks for correctly explaining professional skepticism)* (2 marks)

Total Marks

(20 Marks)

Model Answers

(a) Three things must exist for the company to bring a successful negligence claim against the auditors and state whether the case will be ruled in their favor

- (i) Duty of care-there existed a duty of care enforceable at law
 - (ii) Negligence in a situation where duty of care exists the auditor were negligent in the performance of that duty, judged by the professional standard
 - (iii) Damages- the client has suffered some monetary loss a direct consequence of the negligence of the negligence by the auditors
- The case will not be successful since no duty of care was owed. There was no sufficient proximity between Kigali and the auditors since the auditors were not aware of the existence of Kigali nor the purpose for which the accounts were being used by them

(b) Define a fraud and describe the auditor's responsibilities in relation to fraud and errors

Fraud is an intentional act by an individual or management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unfair or unlawful advantage.

The auditor's responsibilities

- (i) The auditor is responsible for assessing material misstatements in the financial statements due to fraud, by obtaining sufficient appropriate audit evidence through the design and implementation of appropriate responses and responding to fraud or suspected fraud identified during the audit.

- (ii) In addition, the auditor should evaluate whether risk assessment procedures and other information or unusual or unexpected relationships that have been identified may indicate a risk of material misstatement due to fraud.
- (iii) obtain reasonable assurance that financial statements are free from material misstatement, whether due to error or fraud.

(c) Five responsibilities for the directors in relation to the books of account

- (i) To ensure that proper books of accounts are maintained
- (ii) To prepare the financial statements
- (iii) To ensure the balance sheet give a true and fair view
- (iv) To safeguard the company’s assets
- (v) To prevent and detect errors and frauds within the company

(d) Professional skepticism in light of auditor’s responsibilities as far as detection of errors and frauds is concerned

In accordance with ISA 2005, the auditor shall maintain professional skepticism throughout the audit, recognizing the possibility that a material misstatement due to fraud could exist, notwithstanding the auditor’s past experience of the honesty and integrity of the entity’s management and those charged with governance.

QUESTION 14

Marking guide

Maximum marks

- (a) Six tests of control that an auditor would normally carry out on the dispatch and sales system at Kivu electronica and explain the reason for each test. *(1 mark for stating the test of control, 1 mark for explaining the reason for the test; = 2*6 points).* (12 marks)
- (b) Identify Four control objectives and control activities that would help Kivu electronica sales system to become more efficient. *(1 mark for stating the Control objective, 1 mark for stating the Control activity , 2*4 points = 8 marks)* (8 marks)

Total marks

(20 Marks)

NB: any other valid point should be assessed and marked

Model Answers

a) Test of control and reason for each test

Test of Control	Reason for the Test
review a sample of goods dispatch notes (GDN) or signatures of the goods despatch staff and customer.	ensures that the goods dispatched are correctly recorded on the GDN
review a sample of (GDN) for signature of the accounts staff.	ensures that the (GDN) details have been entered onto the computer system.
observe despatch system ensuring Kivu electronica staff have seen the customers' identification card prior to goods being loaded into customers' vans.	ensures that goods are only despatched to authorised customers.
review the error report on numeric sequence of GDN produced in the accounts department and enquire action taken regarding omissions.	ensures that the sequence of GDN is complete
observe despatch process to ensure that the customers' credit limit is reviewed prior to goods being despatched.	ensures that goods are not despatched to poor/bad credit risks. <i>note: reviewing credit limits is not specifically stated in the scenario; however, most despatch/ Sales systems will have this control and most candidates who mentioned this in their should be awarded for this point.</i>
review a selection of invoices ensuring they have been signed by accounts staff.	ensures the accurate transfer of goods despatched information from the GDN to the invoice.

b) Identify four control objectives and control activities that would help kivu electronica sales system become more efficient

Control objective	Control activity
1) Goods are only supplied to customers with good credit ratings and who are within approved credit limits	<ul style="list-style-type: none"> ➤ Segregation of duties (credit control, invoicing and dispatching) ➤ Authorization of credit limits ➤ Credit limits confirmed before new orders are accepted
2) All dispatches of good are delivered	<ul style="list-style-type: none"> ➤ Authorization of goods dispatch ➤ Examination of goods outwards ➤ Recording of goods outward on timely basis

	<ul style="list-style-type: none"> ➤ Pre-numbering of dispatch note and delivery notes and regular check on sequences
3) All goods and services sold are correctly invoiced	<ul style="list-style-type: none"> ➤ Agreement of goods outwards records to customer redispach notes and invoice ➤ Preparation of invoice: preparation of selling price and verification
4) Credit notes are only given for valid reasons	<ul style="list-style-type: none"> ➤ Condition of return is reviewed ➤ Recording of goods returned notes ➤ Management approves credit notes issued

QUESTION 15

Marking guide

Maximum marks

(a) In respect of the purchases and payables system for GAKWETO:

- i. Identify and explain FIVE deficiencies; (1 mark for each deficiency). (5marks)
 - ii. Recommend a control to address each of these deficiencies (1mark for each Recommended control). (5marks)
 - iii. Describe a TEST OF CONTROL the auditor should perform to assess if each of these controls, if implemented, is operating effectively to reduce the identified deficiency. (1 mark for each test of control). (5marks)
- (b) Five most important control objectives of internal control relating to inventory. (1 mark for each valid point) (5marks)

Total marks (20 Marks)

Model Answers

a) **Control deficiency, Control recommendation and a relevant test of control**

Control deficiency	Control recommendation	Test of control
1. It is not possible for a store to order goods from other local stores for customers who request them. Instead, customers are told to contact the other stores or use the company website. Customers are less likely	An inter-branch transfer system should be established between stores, with inter-branch inventory forms being completed for store transfers. This should help stores whose inventory levels are low	During the interim audit, arrange to visit a number of the stores, discuss with the store manager the process for ordering of inventory items, in particular whether it is possible to order from other

<p>to contact individual stores themselves and this could result in the company losing valuable sales. In addition, some goods which are slow moving in one store may be out of stock at another; if goods could be transferred between stores, then overall sales may be maximized.</p>	<p>but are awaiting their deliveries from the suppliers.</p>	<p>branches. At each store, inspect a sample of completed inter-branch inventory forms for confirmation the control is operating.</p>
<p>2. Purchase orders below FRW 1,000 are not authorised and are processed solely by the purchase order clerk who is also responsible for processing invoices. This could result in no business -related purchases and there is an increased fraud risk as the clerk could place orders for personal goods up to the value of FRW 1,000, which is significant.</p>	<p>All purchase orders should be authorised by a responsible official. Authorised signatories should be established with varying levels of purchase order authorisation</p>	<p>Select a sample of purchase orders and review for evidence of authorisation, agree this to the appropriate signature on the approved signatories list.</p>
<p>3. Goods received notes (GRNs) are sent to the accounts department every two weeks. This could result in delays in suppliers being paid as the purchase invoices could not be agreed to a GRN and also recorded liabilities being understated. Additionally, any prompt payment discounts offered by</p>	<p>A copy of the GRNs should be sent to the accounts department on a more regular basis, such as daily. The accounts department should undertake a sequence check of the GRNs to ensure none are missing for processing.</p>	<p>Enquire of the accounts clerk as to the frequency of when GRNs are received to assess if they are being sent promptly. Undertake a sequence check of GRNs held by the accounts department and discuss any missing items with the accounts clerk.</p>

suppliers may be missed due to delayed payments.		
4. GRNs are only sent to the accounts department. Failing to send a copy to the ordering department could result in a significant level of unfulfilled orders leading to a loss of sales and stock-outs.	The GRN should be created in three parts and a copy of the GRN should be sent to the purchase order clerk, Pierre, who should agree this to the order and change the order status to complete. On a regular basis he should then review for all unfulfilled orders and chase these with the relevant supplier.	Review the file of copy GRNs held by the purchase ordering clerk, Pierre, and review for evidence that these are matched to orders and flagged as complete. Review the file of unfulfilled purchase orders for any overdue items and discuss their status with Oliver Dancer.
5. The purchase ordering clerk, Pierre, has responsibility for ordering goods below FRW1,000 and for processing all purchase invoices for payment. There is a lack of segregation of duties , and this increases the risk of fraud and nonbusiness related purchases being made.	The roles of purchase ordering and processing of the related supplier invoices should be allocated to separate members of staff.	Observe which member of staff undertakes the processing of purchase invoices and confirm this is not the purchase ordering clerk, Oliver Dancer. Inspect a copy of the company's organisation chart to identify if these tasks have now been allocated to different roles.
6. The finance director authorises the bank transfer payment list for suppliers; however, she only views the total amount of payments to be made. Without looking at the detail of the payments list, as well as supporting documentation, there is a risk that suppliers could be being paid an incorrect amount, or that	The finance director should review the whole payments list prior to authorising. As part of this, she should agree the amounts to be paid to supporting documentation, as well as reviewing the supplier names to identify any duplicates or any unfamiliar names. She should evidence her review by signing the bank transfer list.	Review the payments list for evidence of review by the finance director. Enquire of accounts staff what supporting documentation the finance director requests when undertaking this review.

sums are being paid to fictitious suppliers.		
7. Supplier statement reconciliations are no longer performed. This may result in errors in the recording of purchases and payables not being identified in a timely manner.	Supplier statement reconciliations should be performed on a monthly basis for all suppliers and these should be reviewed by a responsible official.	Review the file of reconciliations to ensure that they are being performed on a regular basis and that they have been reviewed by a responsible official. Re-perform a sample of the reconciliations to ensure that they have been carried out appropriately.

b) Five most important control objectives of internal control relating to inventory.

- (i) Recording to (ensure that): all inventory movements are authorized and recorded;
- (ii) inventory record only includes items that belong to the client, inventory records include inventory that exist and is held by the client, inventory quantities have been recorded correctly and cut-off procedures applied to inventory
- (iii) protection of inventory: to ensure that inventory is safeguarded against loss, pilferage or damage)
- (iv) valuation of inventory: to ensure that the costing system values inventory correctly and allowance is made for slow-moving, obsolete or damaged inventory
- (v) inventory holding: to ensure that levels of inventory held are reasonable

END OF MARKING GUIDE AND MODEL ANSWERS