
Answer ALL questions. Marks allocated to each question are shown at the end of the question.

QUESTION ONE
(a) Discuss five disclosure requirements that should be made in an audit report as specified in the Companies Act.  
(10 marks)

(b) Your firm has been appointed as the auditor of Fanaka Limited for the year ended 31 December 2016.

Explain why each of the following matters which you have noted during the audit should or should not be included in the letter to the management and those charged with governance:

(i) The company upgraded the accounting system which upon testing you noted that the system did not carry over all the balances accurately. The differences in credit and debit balances considered separately were material to the financial statements but when offset against each other, they were immaterial.  
(2 marks)

(ii) The new accounting system had a functionality that allows online approval of transactions by the various signatories but it had not been activated. The signatories continued to approve transactions manually and all the transactions sampled were duly approved.  
(2 marks)

(iii) The company supplying stationery to Fanaka Limited was owned by the wife of the procurement manager. However, you confirmed that the appropriate procurement procedures were followed.  
(2 marks)

(iv) The bank reconciliations were required to be signed by the preparer (Financial Accountant) and approved by the finance manager. You noted that 6 out of the 12 bank reconciliation statements were not signed by the Financial Accountant but had been approved by the Finance Manager. However, you confirmed that the reconciliation statements were accurate.  
(2 marks)

(v) The company was involved in a restructuring exercise that resulted in the discharge of 25% of the staff. You got to learn that the affected staff had filed a suit in court to challenge their dismissal but the matter had not been heard. However, the management was keen to have the suit heard in order for them to present the issue for reporting in the next financial year when it would be possible to establish if there was a reputable contingent liability.  
(2 marks)

(Total: 20 marks)

QUESTION TWO
(a) Describe five roles you would expect the internal audit staff to perform.  
(10 marks)

(b) Discuss four capabilities and competencies expected of the engagement team as espoused in the International Standards of Auditing (ISA) 220 “Quality Control for Audit of Financial Statements”.  
(8 marks)

(c) Outline two benefits of the auditor communicating with those charged with governance.  
(2 marks)

(Total: 20 marks)

QUESTION THREE
(a) Explain the following terms as used in auditing:

(i) Emphasis of matter paragraph.  
(2 marks)

(ii) Contingent liability.  
(2 marks)

(iii) Audit committee.  
(2 marks)

(iv) Assurance engagement risk.  
(2 marks)
Your audit firm was recently appointed the auditor of Baraka Ltd. The company has a subsidiary based in Mombasa and its auditor had retired the previous year.

**Required:**

(i) Enumerate six factors that would influence you in determining whether or not to send a separate engagement letter to the subsidiary. 

(ii) If the audit of Baraka Ltd. was a recurring audit, suggest six factors that would make it appropriate for you to send a new engagement letter.

**QUESTION FOUR**

(a) Explain three factors to consider while designing an effective system of internal control. 

(b) In the context of auditing, define the following:

(i) Operational audit.

(ii) Financial audit.

(iii) Agreed upon procedures engagement.

(iv) Positive assurance.

(c) Discuss three responsibilities of the external auditor in relation to prevention and detection of fraud.

**QUESTION FIVE**

(a) State the opinions you would give in each of the following situations:

(i) The books of the client were taken away by the regulator for investigations and were not available for audit.

(ii) The provision for doubtful debts was not adequate. The debtors in the financial statement were misstated but the financial statements gave a true and fair view.

(iii) There was no provision for depreciation and the directors were unwilling to provide for any amounts during the financial year. The amount if provided for would reduce the reported profit by 30%.

(iv) There was a legal suit filed by a customer who was unsatisfied with the goods supplied but no provisions were made in the books. The assessment of the case by the company lawyers indicate that the customer has very slim chances of success.

(b) Discuss four factors that might influence the extent of substantive tests carried out during an audit.

(c) Highlight four substantive procedures you would perform on the year end trade payables.