INTERNATIONAL UNIVERSITY OF EAST AFRICA
'Learning to Succeed'

FACULTY OF BUSINESS MANAGEMENT

END OF SEMESTER EXAMINATIONS - AUGUST 2025

PROGRAMME: BBA
YEAR/SEM: YEAR 3/SEMESTER 2
COURSE CODE: ACC 3203
NAME: AUDIT PRINCIPLES AND PROCEDURE

DATE:
TIME:

INSTRUCTIONS TO CANDIDATES:

SECTION A

Section A is Compulsory

Question 1:

Your firm, WLS & Co. (WLS), has been re-appointed as auditors of Magana Light Ltd (MLS) for the year ended 30 June, 21. WLS has-been auditing MLS for 6 years. MLS's financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). You are the audit senior in charge of the audit of MLS and you have to ensure, among other things, that the audit is conducted in accordance with International Standards on (ISAs).As part of planning; you and the audit manager attended a pre-audit meeting with MLS's management. The following brief notes were prepared during that

1. MLS finance manager Mr. Bob Musoke joined the company on 1 July, 2020. He previously worked at Uganda Martyrs University as a university finance officer

2. MLS carried out a restructuring exercise in December 2020 and 50 employees were laid off. A provision of Shs 60 million has been included the financial statements for compensation. Some employees have, however, sued the company claiming the compensation to be given to them is too small.

3. MLS's trade and other receivables amount to Shs 6 billion as at 30 June, 2021. MLS made a general provision of 5% of the total trade and other receivables. Some clients have written to MLS about the financial difficulties they are facing but the Finance Manager is sure that they will be able to pay. No specific provision has been made in respect of this.

4. The Finance Department is under staffed. It has only three staff instead of the required six.

5. Jane, a former employee of MLS, joined WLS & Co on 1 March, 2020. She is
slated to be part of the audit team because, it is felt, that her experience of with MLS will be of great value to the audit team.

6. An analytical review carried out on MLS's financial statements showed a material variance which was due to an increase in finance costs by over 50% in the current year.

7. MLS intends to list on the Uganda Securities Exchange. However, one of the requirements is to have an independent Board in place. WLS is tasked with the responsibility of recommending to MLS members to serve on the board.

8. MLS has significant outstanding audit fees but WLS & Co is not worried as
MLS has always endeavored to pay.

Required:

(a) Discuss, with the Audit Manager:

(i) The possible financial statements risks the audit team is likely to face
during the audit of MLS.
(10 marks)
(ii) How the financial statements risks in (a) (i) above can be mitigated
to an acceptably low level.
(6 marks)

(b) Examine the actual and possible ethical threats that may arise in relation
to the audit of MLS, and the safeguards to reduce them.
(10 marks)

(c) Describe the assertions made by MLS' management in relation to the trade and other receivables balance.

(4 marks)

(d) Explain the substantive audit procedures the audit team should perform on:

(i) trade and other receivables.

(6 marks)

(ii) bad debts.

(4 marks)

(Total 40 marks)

Question 2:

Your client, Mapema Ltd, sells and distributes computers and accessories on a wholesale basis. The company was taken over by a holding company which brought in a manager to run it on their behalf about two years ago. In that period of time, the business has seen massive expansion.

The company has since reached an agreement with one of the major producers of computers in Asia, Peng Ltd, to be their representative in Uganda and they are thus opening up outlets in all the major towns and municipalities in the country. The number of customers served by Mapema Ltd has risen rapidly and thus the company has also had to employ many more staff to cope with this rapid expansion.

Because of this rapid expansion, some of the departments have had to be transferred away from the head office to another location. The departments transferred include the stores and servicing departments. Being representatives of a manufacturer, the company also has a duty to deal with any defects that may arise from the machines distributed before the expiry of the warranty period.

Due to the entry of a new competitor in the market, sales of Mapeam Ltd which had risen rapidly in the past two years have started declining and yet they make up most of the sales of the company and for this reason,

management has opted to make an acquisition of another company, Mwisho Ltd, a company dealing in the software used by numerous other service provision companies to try and shore up their fortunes. Mwisho Ltd is owned by three individuals who are also the core technical staff of the company and there are no other staff employed apart from a secretary who also manages the office reception desk.

In addition to your work as auditors of Mapema Ltd, the directors have also requested your firm to advise them on their plan to purchase Mwisho Ltd and it has been decided that this would need you to carry out a due diligence exercise on the potential acquisition.

You are an audit manager with the audit firm responsible for the audit of Mapema Ltd. You have been assigned the task of heading the audit of the financial statements of the company for the year ended 30 June 2011. You would also be responsible for undertaking the due diligence exercise on Mwisho Ltd that the directors would want to be done.

a) Describe the principal audit risks arising from the scenario outlined above. ***[10 marks]***

b) Explain how the audit strategy would be prepared in order to take into account the risks you have identified. ***[10 marks]***

c) Examine the matters to be considered by Mapema Ltd when deciding whether to acquire Mwisho Ltd. ***[10 marks]***

d) Define the term 'due diligence' and explain the nature and purpose of a due diligence review exercise. ***[5 marks]***

e) Explain the matters that need to be taken into consideration before accepting an engagement to carry out a due diligence review of Mwisho Ltd. ***[5 marks]***

SECTION B

Attempt any Three Questions From Section B

Question 1:

PKL Microfinance Limited (PKL) offers financial services to small and medium-sized Enterprises (SMEs). PKL intends to upgrade its status from microfinance to a Commercial bank regulated by Bank of Uganda in order to be competitive in the financial services industry characterized by information technology (IT) environment. One of the requirements of Bank of Uganda is for PKL to have an audit committee to oversee both internal and external audits. PKL has subsequently instituted an audit committee to meet the requirements of Bank of Uganda. Your firm GKS & Co. (GKS) has been invited by PKL to train their (PKL's) audit committee on matters relating to external and internal auditing. The audit manager will be carrying out the training next week assisted by you, the audit senior.

Required:
Prepare brief notes for your audit manager in relation to the training covering
the following:
(a) (i) Composition of an audit committee.
(2 marks)
(ii) Objectives of an audit committee.
(6 marks)
(b) Differences between internal and external audit reports.
(8 marks)
(c) Reasons why auditing in an IT environment may lack visible audit trail.

(4 marks)

(Total

20 marks)

Question 2:

You are an audit supervisor at ZY & Co. Your firm has been appointed to audit
ABCA Pharmactical Limited (ABCA) for the year ending 31 December, 2021 ABCA
Pharmactical is the main supplier to hospitals and pharmacies within country. The previous auditors would send trainee accountants for the assignments. The partners never had face to face meetings with then of ABCA. Some partners became suppliers of ABCA products. They would obtain drugs on credit and fail to pay. Eventually their services were terminated. In the pre-audit meeting, the Head of Finance at ABCA cautioned ZY & Co. about the uniqueness of the sector in which the company operates. Therefore the engagement partner concluded that there will be need to approach the audit with professional skepticism, and deployment of staff that are able to apply professional judgment during an audit. The company operates in a computerized environment and most of the controls are automated. The company has material levels of inventory and ZY & Co. will be invited to witness the inventory count after year end. You are the audit senior for this engagement.

Required:

(a) Explain to the audit team the meaning of:

(i) Professional skepticism
(2 marks)

(ii) Professional judgment
(2 marks)

(b) With examples, explain to your audit team thecircumstances that give rise
to self-interest threats during the audit of an entity
(2 marks)

(c) Explain to the audit team the:

(i) Circumstances under which the auditor may be held liable to third parties for professional negligence.
(2 marks)

(ii) Ways the auditor can use to minimize potential liability arising from professional negligence
(5 marks)

(d) Explain the audit procedures ZY & Co will apply during the count of ABCA's
Inventory **(7 marks)**

(Total 20 marks)

Question 3:

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pre-audit meeting, the Head of Finance at ABCA cautioned ZY & Co. about the uniqueness of the sector in which the company operates. Therefore the engagement partner concluded that there will be need to approach the audit with professional skepticism, and deployment of staff that are able to apply professional judgment during an audit. The company operates in a computerized environment and most of the controls are automated. The company has material levels of inventory and ZY & Co. will be invited to witness the inventory count after year end. You are the audit senior for this engagement.

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(5 marks)

(d) Explain the audit procedures ZY & Co will apply during the count of ABCA's Inventory **(7 marks)**

(Total 20 marks)

Question 4:

You are an audit senior in KLB & Co., a firm that has been appointed to audit the books of Jojo for the first time. In the pre-audit meeting with the client, the following issues were discussed:

§ Management does not understand the difference between audit and accountancy work.
§ Management has neither read the engagement letter nor signed it off.
§ Some of the information may not be readily availed to the team.
§ The finance director threatened that if the audit team did not tread carefully their payment would not be forthcoming.

Required:

(a) Explain the terms 'engagement letter' and 'letter of representation'.

(5 marks)

(b) Discuss the importance of using an engagement letter to the auditor as highlighted in ISA 210: Terms of an Audit Engagement. **(10 marks)**

(c) Explain the rights of an auditor. **(5**

marks)

(Total 20 marks)

Question 5:

ISA 700: forming an opinion and reporting on financial statement, deals with the auditors' responsibility to form an opinion on the financial statement based on an evaluation of the conclusions drawn from the audit evidence obtained

Required

1. Describe the types of modified audit opinions **(4marks)**
2. Explain the circumstances where modification of auditor's opinion would be required **(4marks)**
3. There are two types of reports, qualified and unqualified. Describe the circumstance under which each of these reports should be issued (**8marks)**
4. Identify the qualities of a good audit report **(4marks)**

(Total mark 20)

Question 6:

People are the most important elements in any business. It is the people who buy the products of a business. Without customers, no business would survive for long. Businesses exist because they can make profit by supplying goods and services that are highly demanded. Before establishing any business, an entrepreneur should first assess the market potential of his products. Failure to carry out market survey and consider other factors leads to business failure.

Required:

(a) Explain reasons for business failure of many enterprises in Uganda.

(10 marks)

(b) Discuss the factors that are considered when assessing the market potential of a product.

(10 marks)

(Total 20 marks)

Question 7:

The venture life cycle shows the stages through which a business goes up to the time it is wound up. In order to achieve its major goal of profit maximization, a business depends on the society for inputs like money, workers and skills for its existence and growth. Likewise, the society depends on business for meeting its needs and welfare. This kind of interdependence requires businesses to be socially responsible. However, some people believe that the concept of social responsibility is against the profit motive and most of the classical economists are against the idea of social responsibility.

Required:

(a) Describe the stages of the 'venture life cycle'.

(8 marks)

(b) Explain reasons why some businessmen are opposed to the notion of social responsibility.

(12 marks)

(Total 20 marks)

Question 8:

Given the preparations for the forthcoming International Conference on HIV/AIDS, the Partners of Grace & Co. are anticipating a number of audit assignments from companies which have won numerous contracts from government for this memorable event. In fact, the Managing Partner has held several meetings with the prospective companies which have expressed willingness to hire the services of Grace & Co., a firm of Certified Public Accountants to audit their Financial Statements for the year ended 31 December 2022.

The Partners have particularly reached a compromise with two companies namely Courtesy International Limited (CIL) and Munyonyo Works Limited (MWL). The former company (CIL) deals in hospitality services and has been contracted to manage the International Conference on HIV/AIDS event. CIL is a highly computerized company both in accounting and operations, for example booking hotel reservations and tours for the delegates will be done online.

Munyonyo Works Limited (MWL) is a construction company specializing in grading roads. It has so far won a major contract to construct and tarmac the main road leading to the venue of the meeting.

CIL has got qualified accountants in addition to an efficient internal audit function. Given the highly computerized environment of CIL, you intend to use an Information Technology (IT) expert.

MWL on the other hand is using a part-time unqualified accountant as a book- keeper. In fact you have to rely on verbal representations for most of the assertions, since management of MWL does not find it necessary to write a formal letter of representation. MWL employs a few permanent staff and 500 casual workers. MWL management suspects there could be dummy workers in the company given the high wage bill beyond the budget. There is a current dispute where six employees have taken MWL to court over injuries sustained during the course of work due to lack of protective gears.

As the Audit Manager in the firm, you have been assigned the duty to make preparations for these two prospective audits and the Partners are expecting you to play a major role during these two impending assignments. The Partners in particular want to put more emphasis on t

he aspect of "audit evidence". You are aware that "the auditor should obtain relevant and rel iable audit evidence sufficient to enable him to draw reasonable conclusions therefrom".

Required:

a) Critically evaluate the basic techniques for collecting audit evidence ***[3 marks]***

b) Outline the audit objectives for non-current assets. Recommend an audit programme which your firm will use in the audit of non-current assets for MWL. ***[5 marks]***

c) Discuss the audit procedures you would design to detect dummy workers in MWL. ***[5 marks]***

d) Illustrate the characteristics of Computer Information Systems which would create problems both for management of CIL and the auditor in his risk analysis ***[3 marks]***

e) Describe the audit procedures that you may design to verify the pending legal disput e. Advise MWL about the preventive measures to safeguard against law suits in future ***.[4 marks]***

Question 9:

You are an audit senior with a firm of certified public accountants. You have been assigned to head the team of auditors for XY limited which runs many supermarkets in the country with the brand name Pay for Quality supermarkets. The company is owned by a group of families who raised the initial capital to start it up and many of whom have continued to be involved in the day-to-day management of the company. One of the difficulties being faced by XY limited is the loan repayment. Currently XY limited is servicing 3 loans from three different commercial banks. After the monthly loan repayments the company is left with very little money to sustain its daily operations. Employees have not been paid for the last three months while suppliers have started demanding cash on delivery since they have big outstanding balances with XY limited. Further, Capital shoppers, a bigger supermarket has established a one stop shopping center in the same location of XY limited, which has resulted into a decline in the daily sales revenues of XY.

Required:

a) Using the information in the case above, highlight the factors that indicate that XY may not be a going concern**.** ***[5 marks]***

b) Explain the audit procedures you would carry out to give further assurance that the company can indeed continue trading as a going concern. ***[7 marks]***

c) In case you concluded that the company was indeed unable to continue trading for the foreseeable future, explain briefly the audit opinion that you would give if management refuses any disclosure to be made on going concern. ***[8 marks]***

Question 10:

Victoria Supermarkets Ltd (VSL) operates supermarkets in 20 municipalities in Uganda. The company's year-end is 31 December 2021. The audit manager and partner recently attended a planning meeting with the finance director and have provided you with the planning notes below.

You are the audit senior and this is your first year on this audit. In order to familiarize yourself with VSL, the audit manager has asked you to undertake some research in order to gain an understanding of the company, so that you are able to assist in the planning process. He has then asked that you identify relevant audit risks from the notes below and also consider how the team should respond to these risks.

VSL has spent Shs 600 million in refurbishing all of its supermarkets. As part of this refurbishment programme their central warehouse has been extended and a smaller warehouse, which was only occasionally used, has been disposed of at a profit. In order to finance this refurbishment, a sum of Shs 500 million was borrowed from the bank. This is due to be repaid over five years.

The company will be performing a year-end inventory count at the central warehouse as well as at all 20 supermarkets on 31 December 2021. Inventory is valued at selling price less an average profit margin as the finance director believes that this is a close approximation to cost.

Prior to 2021, each of the supermarkets maintained their own financial records and submitted returns monthly to head office. During 2021 all accounting records have been centralized within head office. Therefore at the beginning of the year, each supermarket's opening balances were transferred into head office's accounting records. The increased workload at head office has led to some changes in the finance department and in November 2021 the financial controller resigned. His replacement will start in late December 2021.

Required:

a) Using the information provided, describe **FIVE** audit risks and explain the auditor's response to each risk in planning the audit of VSL. ***[15 marks]***

b) It is the duty of an Auditor to obtain and evaluate evidence against the assertions made in the financial statements. State and explain five assertions made in the Financial

Statement. ***[5marks]***

Question 11:

ISA.610: DEFINES INTERNAL AUDIT AS; "AN APPRAISAL OR MONITORING ACTIVITY ESTABLISHED BY MANAGEMENT AND THE DIRECTORS, FOR THE REVIEW OF THE ACCOUNTING AND INTERNAL CONTROL SYSTEMS AS A SERVICE TO THE ENTITY".

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a) Discuss the scope of the internal Audit as may be set by Management of a manufacturing entity ***[3*** marks]

b) Explain the key aspects which the external auditor will have to assess before relying on the work of internal auditors ***[3 marks]***

c) Your firm is the auditor of Leisure limited , a company operating three large centers which sell wooden furniture (such as garden benches, seats and playhouses) to the general public. You are involved in the audit of the company's Non-current assets. The main categories of Non-current assets are as follows:

- Land and buildings (all of which are owned outright by the company)
- Computers (on which an inventory control and sales system is operated)
- A number of large and small vans, mostly used for the delivery of inventory to customers
- Equipment for packaging and pricing products**.**

Required:

i) Explain the main risks associated with financial statement assertions relating to Non Current assets*. [3 marks]*

ii) List the sources of evidence available to verify the ownership and cost of land & buildings, computers and motor vehicles. ***[6 marks]***

iii) As an auditor, describe the substantive procedures you would carry out to confirm completeness in relation to the Non-current assets above. ***[5marks]***

Question 12:

a) Explain the concepts of materiality and its performance in accordance with ISA 320 ***[4 marks]***

b) Explain factors that are used by the auditor in determining what is considered material.

[4 marks]

c) Define a ‘test of control’ and give an example of a test of control in relation to the audit of revenue.

[4 marks]

d) Define a ‘substantive procedure’ and provide an example of a substantive procedure in relation to

the audit of non-current assets. ***[4 marks]***

e) ISA 230 *Audit Documentation* deals with the auditor’s responsibility to prepare audit documentation for an audit of financial statements. State FOUR benefits of documenting audit work. ***[4 marks]***