

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of the Council of ICPAU*

## CPA (U) EXAMINATIONS

### LEVEL ONE

#### AUDIT THEORY – PAPER 7

**WEDNESDAY, 28 NOVEMBER 2012**

#### INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours 15 minutes**.  
The first 15 minutes of this examination have been designated for reading time. You may not start to write your answer during this time.
2. This examination contains Sections **A**, **B** and **C**.
3. Section **A** is bound separately from Sections **B** and **C**.
4. Attempt all the 20 multiple-choice questions in Section **A**. Each question carries 1 mark.
5. Attempt the compulsory question in Section **B** carrying 30 marks.
6. Attempt **two** of the **three** questions in Section **C**. Each question carries 25 marks.
7. Write your answer to each question on a fresh page in your answer booklet.
8. Please, read further instructions on the answer booklet, before attempting any question.

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## SECTION B

*This section has one compulsory question to be attempted*

### Question 2

Adas Limited, based in Kabarole, employs a large number of staff who are paid based on the hours worked. Each staff, when appointed, is given a contract which clearly shows the fixed hourly rate. This rate is followed by the payroll accountant until such a time when there is a revision in the rate. Changes in the payroll rates are always approved by the Human Resource Manager who then communicates them to the payroll accountant.

You are a senior auditor in Armstrong Certified Public Accountants (ACPA) and have been assigned to head the audit team for Adas Limited. While reviewing the draft financial statements provided for audit, you realized that employment costs form part of the biggest costs in the statement of comprehensive income for the year ended 30 June 2012.

In your preliminary interview with the accounts assistant, she informs you that the rate at which staff join and leave the company is quite alarming but she prefers that this information is kept between the two of you.

You are further informed that National Social Security Fund and pay as you earn deductions are made but not remitted to the relevant authorities. Knowledge of this fact has tremendously angered the employees who are threatening to go to the offices of the local newspaper and expose the company.

#### Required:

- (a) Explain the audit work you would carry out on the payroll of Adas Limited.  
(12 marks)
  - (b) Briefly discuss why it is important for ACPA to plan for the impending audit of Adas Limited.  
(10 marks)
  - (c) Explain the actions to be taken by ACPA given that Adas Limited has not been complying with the relevant laws and regulations?  
(8 marks)
- (Total 30 marks)**

## SECTION C

*Attempt two of the three questions in this section.*

### Question 3

You are a senior auditor in J&J Associates, a firm which is located in Namanve. Your firm was appointed to audit the books of Bingo Estates Limited, a small sized company, for the first year which ended on 30 September 2012. You are a senior auditor in the firm and you chose an audit assistant to carry out the audit. The assignment was rated as low risk and for this matter, you prepared an audit programme for the assistant to follow while carrying out the duties allocated to him. While reviewing his working papers, it came to your attention that he did not do enough work. The audit fieldwork was carried out on a Friday yet he had promised the girlfriend an outing to watch a movie at Screenplex and was thus not concentrating. You had, however, insisted that he completes the assignment before going for the weekend.

#### Required:

- (a) Define the term 'audit risk'. (3 marks)
  - (b) Explain the:
    - (i) limitations that J&J Associates are likely to be faced with in using audit programmes. (12 marks)
    - (ii) advantages of using audit programmes. (10 marks)
- (Total 25 marks)**

### Question 4

Mable Max is a local firm which buys goods from a number of suppliers and normally pays them 30 working days after supplies are made. Mable max is not computerized and thus prepares its accounts manually. All the suppliers have individual ledgers which are maintained by the manager in charge of suppliers. The company policy is that each supplier invoice is settled in full and no payment on account is allowed.

Your firm has been appointed to carry out the audit of Mable Max. During your preliminary interview with management, it came to your knowledge that the trade payables are a very grey area and might need special attention.

**Required:**

- (a) Outline the substantive audit procedures you would carry out in relation to the audit of trade payables. (10 marks)
- (b) With regard to the audit of the trade payables of Mable Max, identify the kind of audit evidence that is expected to be found on the current audit file. (5 marks)
- (c) Discuss the matters that should be considered by your audit firm before accepting appointment as auditors. (10 marks)
- (Total 25 marks)**

**Question 5**

- (a) Briefly explain the following terms as used in auditing:
- (i) Detection risk. (3 marks)
  - (ii) Control risk. (3 marks)
  - (iii) Business risk. (3 marks)
- (b) Define the following audit opinions and, with examples, state the circumstances under which each one of them would be given:
- (i) unqualified opinion. (5 marks)
  - (ii) qualified opinion. (5 marks)
  - (iii) adverse opinion. (6 marks)
- (Total 25 marks)**