

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA(U) EXAMINATIONS

LEVEL THREE

AUDITING & OTHER ASSURANCE SERVICES – PAPER 15

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. Section **A** has one compulsory case study question carrying 50 marks.
3. Section **B** has **four** questions and only **two** are to be attempted. Each question carries 25 marks.
4. Write your answer to each question on a fresh page in your answer booklet.
5. Please, read further instructions on the answer booklet, before attempting any question.

SECTION A

This section has one compulsory question to be attempted.

Question 1

Fast Telecom Ltd is an international company offering telecommunication services including mobile telephone, internet and the recently introduced mobile money services. It has been argued that the proliferation of mobile money services can increase access to formal financial services in many of the developing countries. It is also argued, however, that it also increases the risk of money laundering and terrorist financing.

Due to competition, another telecom outfit, Pride Telecom Ltd decided to close shop and its business was acquired 100% by Fast Telecom Ltd on 1 July 2012. With the new acquisition, the company is hoping to expand coverage to the far flung areas of the country with a view to getting even more clients and improving the revenue base.

Goodwill on the acquisition of the subsidiary was arrived at after employing the services of a consultant who prepared a due diligence report and produced the figures showing the net book value of the company's assets and the related goodwill with the sum of the two making up the ask price for Pride Telecom Ltd. It was agreed that the company would pay for the goodwill conditionally in instalments with the final instalment being paid off towards the end of a period of three years at which time the company would be expected to have achieved certain milestones specified in the acquisition document.

Fast Telecom Group of Companies Ltd has performed well this year, with forecast consolidated revenue for the year to 31 December 2012 of Shs 20 billion (2011 = Shs 15 billion), and profit before tax of Shs 2.5 billion (2011 = Shs 1.9 billion).

The most recent consolidated statement of financial position at 30 November 2012 recognises total assets of Shs 50 billion.

You are a senior audit manager in Bits, Samanya & Co., a firm of Certified Public Accountants based in Kampala. Your firm has been the auditors of Fast Telecom Ltd for a number of years. The firm has also been appointed to be the auditor of the recently acquired company, Pride Telecom Ltd. You are the engagement manager for this assignment.

Required:

- (a) Identify and describe the principal business risks faced by Fast Telecom Group of Companies Ltd.
(12 marks)
- (b) Identify and explain the implications of the acquisition of Pride Telecom Limited for the audit planning of both the individual and consolidated financial statements of Fast Telecom Group of Companies Ltd.
(14 marks)
- (c) Evaluate the risks of material misstatement to be considered in the audit planning of the individual and consolidated financial statements of Fast Telecom Group of Companies Ltd.
(10 marks)
- (d) Discuss the issues that the auditor would take into consideration before relying on the work of the consultant that prepared a due diligence report on Pride Telecom Ltd.
(10 marks)
- (e) Compare the scope of a due diligence investigation with that of an audit of financial statements, in respect to Fast Telecom Ltd.
(4 marks)

Total 50 marks

SECTION B

Attempt two of the three questions in this section.

Question 2

- (a) Okwa Limited is a company which is part of a group. The shareholders at their last annual general meeting appointed your firm, Tuwe & Co., Certified Public Accountants, to be their auditors for the financial year ended 30 September 2012.

You are a manager with Tuwe & Co. The partners recently appointed you to be the engagement manager for the audit of Okwa Limited. You communicated to the management of the company who indicated to you that the financial statements had been prepared and were ready for audit. You then arranged for and held a preliminary meeting with them to discuss various matters related to the audit. Among the matters discussed was the issue of related party transactions. Management, however, appeared not to be fully aware of all the related parties of the company.

You are in the process of preparing briefing notes for your team and you would like them to pay particular attention to related party transactions.

Required:

- (i) Identify and explain the nature of transactions which may indicate the existence of previously unidentified related parties.

(5 marks)

- (ii) Recommend the procedures you would advise the team to undertake in order to reduce the chances of risks of failure to identify and review related party transactions.

(10 marks)

- (b) One of your assistants has narrated to you that he studied about letters of representations during his CPA course but that he did not fully comprehend such documents.

Required:

- (i) Explain what an auditor needs to do in relation to matters in the letter of representations that the auditor considers material.

(3 marks)

- (ii) Explain the basic elements of a management representation letter.

(3 marks)

- (iii) What actions would you take in case management of the entity refused to provide the representations?

(4 marks)

(Total 25 marks)

Question 3

- (a) Kalungu Limited has appointed your firm of Certified Public Accountants as their auditors for the year ended 30 September 2012 and the audit is due to commence soon.

You are an audit manager within the firm and would like to guide members of the team assigned to this engagement on how to go about the engagement especially relating to the opening balances since they are not sure about how to audit the same.

Required:

- (i) Identify and explain the matters that you would take into consideration when determining the sufficiency and appropriateness of the audit evidence you need to obtain regarding opening balances.

(3 marks)

- (ii) Recommend the audit procedures that you would advise your team to undertake in order to obtain satisfaction that the opening balances were properly taken up and are reliable.

(10 marks)

- (b) In addition to the issue of the opening balances, one of the junior auditors has come to you stating that the managing director has provided a directors' report which has issues some of which are inconsistent with the financial statements. The managing director informed him that it does not really matter since the figures the firm is reporting on were duly audited and that there was no misunderstanding regarding them.

Required:

- (i) Distinguish between a material inconsistency and a material misstatement of fact.

(4 marks)

- (ii) Describe what you, as an auditor, would do when faced with each of the issues in (b) (i) above.

(8 marks)

(Total 25 marks)

Question 4

Kwes Ltd is a company that has been operating for a long period of time. The directors held a meeting at which they reviewed the management accounts and decided to invite the auditors to carry out the statutory audit of their financial statements for the year ended 31 October 2012.

You are an audit manager with one of the audit firms in the city. You assigned an audit senior to commence planning for this particular assignment. The audit senior has reported to you that the company might be facing going concern challenges following casual discussions held with some of the staff of Kwes Ltd though this has not been revealed by the management of the company. The company has a large overdraft from their bankers. They, however, expect to receive some funding from a related company to overcome this issue. Cashflows from customers are also expected to improve though sales reduced for the last few months due to competition from newcomers into the market. Shareholders' funds are also said to be negative. The audit senior has disclosed to you that he has never encountered any such situation before and would like you to assist him prepare for this particular assignment.

Having discerned this information, you advised the audit senior to request management to prepare a cashflow forecast in order to support their claim of trading as a going concern and they duly provided a cashflow forecast for six months after the accounting year end.

Required:

- (a) Identify and explain the matters which may indicate doubts about the company's ability to continue trading as a going concern that you would include in your discussions with the audit senior.
(11 marks)
- (b) Describe the evidence that you would expect to find on the audit file regarding the audit of the cash flow forecast for the six months ending 31 April 2013.
(14 marks)

(Total 25 marks)

Question 5

You are the audit senior manager in Fero & Co, Certified Public Accountants, and directly in charge of technical issues. The firm has taken on a new client who needs a review of their financial statements.

A new staff has been assigned this task but he is not sure on how to go about it. He is, however, aware of a standard relating to review of financial statements; ISA 2400: Review Engagements. He would like you to advise him on how to proceed with such an assignment.

Required:

- (a) Identify and explain the matters to be included in a letter of engagement for a review assignment. Please note that you are not required to draft the letter of engagement.
(4 marks)
- (b) Prepare a memorandum for the partner explaining the general procedures normally undertaken in carrying out a review of financial statements.
(15 marks)
- (c) Outline the format of the review report that is to be prepared.
(6 marks)

(Total 25 marks)