



UNIVERSITI KUALA LUMPUR BUSINESS SCHOOL

FINAL EXAMINATION

JANUARY 2016 SEMESTER

SUBJECT CODE : EAB21103
SUBJECT TITLE : AUDIT 1
LEVEL : BACHELOR
TIME / DURATION : 2.00 PM - 5.00 PM / 3 HOURS
DATE : 26th MAY 2016

INSTRUCTIONS TO CANDIDATES

1. Please read the instructions given in the question paper CAREFULLY.
 2. This question paper is printed on both sides of the paper.
 3. This question paper consists of FIVE (5) questions. Answer ALL questions.
 4. Please write your answers in the answer booklet provided.
 5. All questions must be answered in English (any other language is not allowed).
 6. This question paper must not be removed from the examination hall.
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THERE ARE SIX (6) PAGES OF QUESTIONS, EXCLUDING THIS PAGE.

(Total: 100 marks)

INSTRUCTION: Answer ALL questions

Please use the answer booklet provided

Question 1

A. Each of the following situations involves a possible violation of MIA's By-Laws on Professional Independence.

- (1) On 20th August 2015, Ali, Ahmad & Co., was offered and accepted the engagement to audit the annual financial statements of Jerneh Insurance Berhad for the year ended 31st December 2015. Preliminary work began on the audit on 15th September 2015 and the engagement ended on 7th March 2016. Ali served as financial controller of Jerneh Insurance Bhd from 1st December 2002 until 10th April 2016.
- (2) The accounting firm of Halim & Lee provides bookkeeping and tax services for Ramli Food Industries Sdn Bhd, a privately held company. Mr. Halim also performs the annual audit of Ramli Food Industries Sdn. Bhd.
- (3) Ahmad is an auditor, but not a partner, with 3 years professional experience with Sammy & Co. He owns 15% shares in an audit client of the firm, but he does not take part in the audit of client, and the amount of shares is not material in relation to his total wealth.
- (4) Halimah Appliance has not paid Peter Chong & Co, the audit fee for the past two years. Peter Chong is starting work on the current year's audit of Halimah Appliance.

Required:

For each situation (1) to (4) above:

(a) State whether it is a violation of MIA By-Laws.

(4 marks)

(b) Briefly explain how the situation violates (or does not violate) the MIA By-Laws on Professional Independence.

(8 marks)

B. Briefly explain the difference between **audit failure** and **audit risk**.

(4 marks)

C. Explain **TWO (2)** ways the practicing auditors should positively respond to and reduce the liability in auditing.

(4 marks)

20 marks

Question 2

A. A system of internal control consists of policies and procedures designed to provide management with reasonable assurance that the company achieve its objectives and goals.

Required:

(a) Briefly explain **THREE (3)** objectives in designing an effective internal control system.

(6 marks)

(b) Separation of duties is essential in preventing errors and intentional misstatements on the financial statements. List **THREE (3)** general guidelines for adequate separation of duties.

(3 marks)

B. The following internal control questionnaire is used by an audit firm for assessing control risk in the sales and collection cycle:

- (1) Credit is approved automatically by computer; by comparison to authorized credit limits.
- (2) Sales transactions are internally verified.
- (3) Shipping documents are pre-numbered and accounted for weekly.
- (4) Different persons are assigned to do different task; billing, recording of sales and handling of cash receipts.
- (5) Cash received from customers are stored in safe deposit box before deposited to bank on daily basis.

Required:

For each of the internal control questions above, identify the control activity involved.

(5 marks)

C. Three conditions for fraud arising from fraudulent financial reporting and misappropriation of assets are referred to as **fraud triangle**. Briefly explain each of the conditions.

(6 marks)

[20 marks]

Question 3

A. Management assertion is implied or expressed representations by management about classes of transactions and the related accounts and disclosures in the financial statements. Briefly explain **THREE (3)** types of management assertion.

(6 marks)

B. Hannan is the junior auditor in charge to audit Munzir Sdn. Bhd. The following audit procedures are from different transaction cycles:

- (1) Compute inventory turnover for each major product and compare it with the previous year's amount.
- (2) Compare the dates in receiving reports and vendor invoices with the dates in acquisitions journal.

- (3) Send confirmation letter to Maybank Berhad to confirm the outstanding balance of loan, interest rate and collateral with lender.
- (4) Examine whether the time card has proper authorization from Factory Manager.
- (5) Inquire Credit Manager on the likelihood to collect account receivables with balances outstanding for over 120 days.
- (6) Compare monthly sales amounts to identify any unusual transaction.

Required:

For each procedure (1) to (6) above, identify:

- (a) The **financial statement cycle** being audited.
- (b) The type of **audit procedure**, whether it is test of control, substantive test of transaction, analytical procedures or test of details of balances.
- (c) The **audit objective** or objectives being satisfied.

(9 marks)

- C. Distinguish between existence and completeness in balance related audit objectives. State the effect on the financial statements due to an overstatement or an understatement in the audit of account receivables.

(5 marks)

20 marks

Question 4

- A. ISA 320 *Materiality in Planning and Performing an Audit* emphasizes the need for the auditor to consider the materiality element and its relationship with audit risk during planning and designing the audit approach. However, the assessment of what is material is a matter of auditor's professional judgment.

Required:

- (a) Define materiality.

(2 marks)

(b) What is the relationship between materiality and the phrase **obtain reasonable assurance** used in the auditor's report?

(2 marks)

(c) There are several factors that affect an audit firm's business risk and, therefore, acceptable audit risk. Discuss **TWO (2)** of these factors.

(4 marks)

B. Explain the following:

(a) Planned detection risk

(b) Control risk

(c) Inherent risk

(6 marks)

C. Distinguish between **test of control** and **substantive test of transactions**. Provide **ONE (1)** example each for sales and collection cycle.

(6 marks)

20 marks

Question 5

A. Planning involves developing an overall audit strategy and an audit plan which include the nature, timing and extent of the audit procedures that should be carried out during the audit.

Required:

(a) Explain the purpose of an engagement letter. List **FOUR (4)** matters that should be covered in engagement letter?

(4 marks)

(b) List **THREE (3)** types of comparison which are useful when performing preliminary analytical procedure.

(3 marks)

B. ISA 500 *Audit Evidence* defines audit evidence as the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based.

Required:

- (a) Explain why external evidence is more reliable than internal evidence? (2 marks)
- (b) Explain the terms 'relevant' and 'reliable' that determine the persuasiveness of evidence. (4 marks)

C. For each of the following audit procedures, identify which type of audit evidence is applicable.

No.	Audit Procedures	Type of Evidence
1	Discussing the adequacy of provision of doubtful debt with credit manager.	
2	Check arithmetical accuracy of depreciation expenses prepared by personnel.	
3	Evaluate reasonableness of account receivables by calculating ratio.	
4	Examine a newly bought plant and machinery to make sure that the assets were actually received and are in operation.	
5	Perform a surprise count of petty cash to ensure that the amount is correct.	
6	Send letter to client's customers to ensure that the account receivables balances are accurately recorded.	
7	Observe warehouse staffs carried out stock taking at the end of financial year end.	

(7 marks)

20 marks

END OF QUESTION PAPER

