

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

**EXAMINATION FOR THE AWARD OF DEGREE OF MASTER OF BUSINESS
ADMINISTRATION**

MBAD 814: AUDITING

STREAMS: MBA Y2S1

TIME: 2 HOURS

DAY/DATE: MONDAY 12/07/2021

8.30 A.M. – 10.30 A.M.

INSTRUCTIONS:

- **Answer question ONE and any other THREE**
- **Do not write on the question paper.**

QUESTION ONE

- (a) Mazao Mema Limited is a large manufacturing company producing fertilizers and other agro-chemicals. It employs about 3,000 workers. Attendance by factory workers and payment of wages in evidence by use of clock card, whereby each worker clocks in and out of the factory. Time keeper man the clocking machine and at the end of each week a summary is prepared of recorded attendance of each employee. These weekly summaries serve as the input for the preparation of payrolls at the end of the month.

During the course of your audit of the company's wages expenditure, you discovered that fraud had taken place and the management has commissioned you to investigate it.

Required:

- (i) Clearly state and describe six possible ways in which wages fraud can be committed in an organization. (6 marks)
- (ii) Detail the areas and audit tests you will conduct to assess the extent of fraud in Mazao Mema Limited. (8 marks)

- (b) Critically discuss the concept of evidence in auditing in auditing. In your discussion show the impact of custom, convention and auditing standards on what constitute evidential matter in Kenya today. (8 marks)
- (c) With reference to appropriate International Standards on auditing, discuss the extent to which the auditor can rely on representation made by management which are not capable of independent verification by the auditor. (8 marks)
- (d) Discuss whether it is practical and desirable within the limits of procedures and costs, for the auditor to accept a general responsibility to detect fraud and other irregularities. (10 marks)

QUESTION TWO

- (a) The expressions “management audit, operational audit, and efficiency audit” are very often used these days. Do they differ from internal audits? If so, to what extent? Discuss. (5 marks)
- (b) Audit planning is a critical component of successful audit preparation, execution, reporting and follow up.

REQUIRED

- (a) Critically, discuss the benefits of planning the audit engagement. (4 marks)
- (b) Elucidate how the auditor would incorporate the following task in the audit planning stage.
 - (i) Assessment of risk (3 marks)
 - (ii) Determination of materiality (3 marks)
 - (iii) Audit evidence (3 marks)
 - (iv) Post balance sheet events and post audit review (2 marks)

QUESTION THREE

You are the auditor of Chuka drinks Ltd., a company which imports and distributes pombe Asili to a wide range of customers in the country. In recent years the company has experienced low profitability as the popularity of pombe Asili has declined. The draft accounts as at 30th April 2021 show net liabilities of Sh. 16,000,000. The company’s major source of finance is a bank loan of Sh. 40,000,000 which is due for repayment in full on 30th September 2021. The company is negotiating with its bankers for a replacement with long term loan of Sh. 80,000,000 and intended to use these additional funds to finance and expansion of its activities into the potentially more profitable business of importing and distributing wines.

The directors are optimistic that the bank will agree to make the loan available in view of the profit forecast for the year to 30th April 2022 which they submitted with their loan application. However, they do not expect negotiations to be completed before the Annual General Meetings on 23 August 2021.

The detailed audit work has been completed with the exception of obtaining the necessary confirmation from the bank and no other audit problems have been noted. The directors have asked you not to approach the bank because of the negotiations.

Required

- (a) State the enquiries you would make and the procedures you would perform with regard to establishing the status of Chuka drinks Ltd. as a going concern. (8 marks)
- (b) Discuss the alternative audit opinions which may be relevant to the accounts of Chuka drinks Ltd. together with the circumstances in which each would be appropriate.(8 marks)
- (c) Taking into account the audit standards and companies Act Cap 486 comment on directive given that the auditor should not approach the bank. (4 marks)

QUESTION FOUR

- (a) What precautions are necessary before undertaking an investigation? State the procedure that you would adopt in an investigation on behalf of a bank proposing to advance a loan to a private limited company. (10 marks)
- (b) There are those who put forward the theory that an auditor should not in any circumstance become involved, even as an adviser, in the management function of decision-making within a business. I do not subscribe to this view and indeed in my opinion it is the auditors' duty to point out weaknesses, to offer constructive advice and to help the business in every possible way that he can." Discuss this statement. (10 marks)

QUESTION FIVE

You have been in partnership with a fellow Certified Public Accountant for a number of years. Due to old age and ill-health your partner has suddenly resigned.

Unfortunately, some of the clients of your practice have also suddenly left you, thereby leaving you with few personal clients and only one large client which, on departure of your partner, will represent 30% of your total audit fee income.

While reviewing your business plan and your ethical position, you realize that in order to make the practice profitable and viable you will need to expand your client base considerably.

Required

- (a) In the light of the Accountant's Act (CAP. 531) and the Ethical Guidelines issued by the Institute, state with reasons whether you will have to resign as auditor of the large client. (7 marks)

- (b) Explain the steps you are entitled to take in order to bring in more clients. (7 marks)
 - (c) Discuss the actions which are specifically prohibited by the Ethical Guidelines for a practice which wishes to bring in more clients. (6 marks)
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