

**THE PAPUA NEW GUINEA UNIVERSITY OF TECHNOLOGY**

**FIRST SEMESTER EXAMINATION 2022**

**DEPARTMENT OF BUSINESS STUDIES**

**BA 411 AUDITING**

**TUESDAY 5<sup>TH</sup> JUNE 2022**

**TIME ALLOWED: 3 HOURS**

**DIRECTIONS TO STUDENTS**

- 1. You have 10 minutes to read the examination paper. You must not begin writing during this time.**
- 2. PART A: You MUST Answer all Questions. Total Marks 50  
PART B: You MUST Answer only three (3) Questions. Total Marks 50  
  
IN TOTAL YOU SHOULD HAVE ANSWERED 5 QUESTIONS.**
- 3. Make sure that you read each question carefully. The number of marks for each question is given with each question.**
- 4. PRINT your name and student number on the answer booklet provided. PLEASE DO IT NOW.**
- 5. All answers must be written on the answer booklets provided. No other written material may be accepted. Please hand in every answer booklet provided to you whether used or unused.**
- 6. Notes and textbooks are not allowed in the exam hall.**

**This Examination is worth 50% of your Final Grade.**

**PART A – MULTIPLE CHOICE QUESTIONS (COMPULSORY)**  
**(50 Marks)**

1. Enterprise governance is perceived as a model that can be applied to:
  - a. corporations.
  - b. not-for-profit organisations.
  - c. the public sector.
  - d. all of the above.
  
2. The conformance aspect of enterprise governance covers all these issues except:
  - a. the roles of the chair of the board and top management.
  - b. inwardly focused entities.
  - c. internal control structures.
  - d. the adequacy and reasonableness of compensation schemes for executives.
  
3. Earnings management occurs when:
  - a. income and expenses are managed to influence the performance of the entity.
  - b. financial statements and transactions are manipulated to influence perceptions about the entity.
  - c. executive salaries are increased surreptitiously by including the raises in late night meetings.
  - d. earnings are manipulated to improve the company's tax position.
  
4. Incentives for earnings management are inherent in the management structure but are unlikely to originate from:
  - a. high positive cash flows.
  - b. political considerations.
  - c. executive remunerations.
  - d. situations including financial distress.
  
5. The COSO Enterprise Risk Management integrated framework has four categories of risk objectives which include:
  - a. strategic, operations, reporting and business unit.
  - b. strategic, control activities, reporting and business unit.
  - c. strategic, control activities, reporting and compliance.
  - d. strategic, operations, reporting and compliance.
  
6. There have recently been a number of developments which enhance the role of auditors in the corporate governance regime including:
  - a. the declaration by the auditor of the audit opinion.
  - b. the legal codification of auditing standards.
  - c. the creation of the *Auditing Competency Standard For Registered Company Auditors* by the ATO.
  - d. the change of the Code of Ethics for Professional Accountants to the CPA Australia/ICAA Code of Professional Conduct.

Formatted: Right: 0.63 cm

7. Audit quality is an overall concept covering all of the following except:
  - a. the adherence to ethical standards.
  - b. auditor competence.
  - c. due diligence.
  - d. quality control processes.
  
8. Following the corporate collapses of the early 2000s, firms are:
  - a. implementing more complicated modern audit techniques in order to minimise audit risks.
  - b. implementing simplified modern audit techniques in order to minimise audit risks.
  - c. reverting to complicated audit techniques such as substantive testing in order to minimise audit risks.
  - d. reverting to basic audit techniques such as substantive testing in order to minimise audit risks.
  
9. Investigation of Triple Bottom Line (TBL) assurance statements from the UK and Europe show that:
  - a. there is much variability and ambiguity within the statements.
  - b. there is conformity within the statements.
  - c. the TBL standards have been adhered to more closely than other statutory requirements.
  - d. the other statutory requirements have been adhered to more closely than TBL standards.
  
10. The SEC proposal on audit committees did not require:
  - a. the audit committee to be directly responsible for the hiring of an independent auditor.
  - b. the audit committee to be directly responsible for the oversight of an independent auditor.
  - c. the audit committee to be directly responsible for the internal auditor.
  - d. the names of the committee members to be disclosed in the annual report.
  
11. Under the Framework for Assurance Engagements, which of the following is one of the types of assurance engagements?
  - a. absolute assurance.
  - b. reasonable assurance.
  - c. no assurance.
  - d. partial assurance.

12. To become a certified internal auditor under the Institute of Internal Auditors – Australia, a person must:
  - a. have a minimum of 1 years' experience as an internal auditor.
  - b. pass an examination and have a minimum of 1 years' experience as an internal auditor.
  - c. have a minimum of 2 years' experience as an internal auditor.
  - d. pass an examination and have a minimum of 2 years' experience as an internal auditor.
  
13. The scope of internal auditing should not encompass the examination and evaluation of:
  - a. the adequacy and effectiveness of the organisation's governance and internal control structure.
  - b. the quality of performance in carrying out assigned responsibilities.
  - c. the independence of external auditors.
  - d. the mechanisms to ensure regulatory compliance.
  
14. The independent auditor:
  - a. can seek direct assistance during a financial statement audit from the internal auditor.
  - b. cannot seek direct assistance during a financial statement audit from the internal auditor due to the internal auditor's lack of independence.
  - c. cannot seek direct assistance during a financial statement audit from the internal auditor due to the internal auditor's lack of insurance.
  - d. cannot seek direct assistance during a financial statement audit from the internal auditor due to the Code Of Professional Conduct.
  
15. Following the introduction of CLERP 9, it is now prohibited for external auditors to provide internal audit services for audit clients in order to:
  - a. reduce year-end workloads.
  - b. enhance the self-review threat.
  - c. preserve independence in mind.
  - d. preserve independence in appearance.
  
16. Important criteria in assessing the performance of internal auditing by the external auditor do not include:
  - a. organisational status.
  - b. technical competence.
  - c. due professional care.
  - d. scope of the external audit.
  
17. Internal auditors reports are not usually distributed to:
  - a. the board of directors.
  - b. management.
  - c. members.
  - d. audit committee.

18. Operational auditing is used to evaluate a variety of activities that include all of these except:
- quality control systems.
  - planning control systems.
  - accurate classification of balance sheet items.
  - management's performance.
19. KPMG's fraud survey identified a number of factors which have given rise to the increase in electronic fraud including:
- restricted access.
  - the ease with which funds can be moved around the world.
  - the replacement of traditional internal controls with efficient electronic systems controls.
  - the denial of a certain level of fraud in business.
20. A forensic auditor will look for evidence concerning:
- internal control effectiveness.
  - the reliability of balance sheet items.
  - likelihood of fraud.
  - the appropriate application of accounting standards.
21. Which of the following is not among the characteristics of the procedures performed in **completing the audit**?
- they are optional since they have only an indirect impact on the opinion to be expressed.
  - they involve many subjective judgements by the auditor.
  - they do not relate to specific transaction cycles or accounts.
  - they are usually performed by audit managers or seniors.

A is correct

Feedback: Section 16.1 Completing the fieldwork

22. Which of the following is not among the specific auditing procedures the auditor performs to obtain additional audit evidence?
- making subsequent events review.
  - reviewing for contingent liabilities.
  - reviewing evidence already gathered concerning litigation, claims, and unrecorded or contingent liabilities.
  - obtaining management representation letter.

Formatted: Right: 0.63 cm

23. In working with the minutes of meetings of shareholders, those charged with governance, and their subcommittees, the auditor should:
- read the minutes of all important meetings.
  - scan the minutes of all meetings.
  - read the minutes of all meetings.
  - read the minutes of all members' meetings.
24. In regard to identifying and evaluating subsequent events, ASA560.10 (ISA 560) specifies that the auditor make inquiries of management. Which of the following is not an example of a specific inquiry?
- whether new commitments, borrowings or guarantees have been entered into.
  - whether sales of assets have occurred or are planned.
  - whether any unusual accounting adjustments have been made or are contemplated.
  - the current status of items previously accounted for on the basis of preliminary or inconclusive data.
25. Which of the following auditing procedures would not be useful for the auditor in discharging responsibilities under ASA560.10 (ISA 560)?
- read minutes of directors' meetings.
  - read the latest interim financial statements.
  - review management budgets.
  - review procedures the auditor used to ensure subsequent events were identified.
26. By definition, **subsequent events** occur between:
- interim and year-end.
  - year-end and the audit report date.
  - the audit report date and the date the financial statements are issued.
  - year-end and the date the financial statements are issued.
27. After the auditor's report has been signed, the auditor:
- does not have a responsibility to detect subsequent events.
  - does have a responsibility to detect subsequent events.
  - has provided absolute assurance that all significant events occurring up to that date have been identified.
  - will issue a bill to the client.

28. Financial statements are usually prepared on the going concern basis. The auditor is required by ASA 570 (ISA 570) to assess the risk of going concern problems at which stage(s) of the audit?
- ASA 570 (ISA 570) does not require the assessment of the risk of going concern problems.
  - during the final review.
  - the planning stage.
  - the planning stage and during the final review.
29. If the auditor discovers that management intends to liquidate the entity:
- the going concern basis is inappropriate.
  - it is irrelevant if they did not intend to liquidate the entity at reporting date.
  - it requires inclusion as a disclaimer of opinion.
  - it requires inclusion as an 'except for'.

A is correct

Feedback: Section 16.1 Completing the fieldwork

30. Which of the following events in a subsequent period is an example of a condition existing at the reporting date?
- casualty loss resulting from a flood.
  - discovery of fraud or errors.
  - purchase of a business.
  - issuance of preferred stock.
31. The account balance audit objective, "Accounts receivable represent gross claims on customers at balance date and agree with the sum of the accounts receivable subsidiary ledger", is derived from the assertion category of:
- existence or occurrence.
  - completeness.
  - rights and obligations.
  - valuation or allocation.
32. Which of the following is not a specific audit objective for sales and receivables?
- existence or occurrence.
  - completeness.
  - representation.
  - presentation and disclosure.

33. In a credit sales environment, which of the following documents usually initiates the activity in the sales cycle?
- customer order.
  - sales order.
  - dispatch note.
  - sales invoice.
34. Which of the following is not normally considered a step in the credit sales functions?
- accepting customer orders.
  - approving credit.
  - acquiring goods to fill the order.
  - billing customers.
35. In a credit sales environment, which of the following documents serves as the basis for internal processing of an order?
- customer order.
  - sales order.
  - dispatch note.
  - sales invoice.
36. In a credit sales environment, the best place to vest credit approval is in:
- accounts receivable.
  - the sales department.
  - the cashier area where receipts will eventually be sent.
  - an independent credit department.
37. Controls over approving credit relate to the:
- existence or occurrence assertion.
  - completeness assertion.
  - accuracy, valuation or allocation assertion.
  - rights and obligations assertion.
38. To enhance controls in the credit sales area, the warehouse should be instructed not to release (or dispatch) goods until:
- they received a faxed copy of the sales requisition.
  - they have a completed sales invoice.
  - they receive an approved sales order.
  - the shipping department requests the goods.



39. Accounting for the numerical sequence of dispatch notes used in tracing will primarily meet the:
- existence or occurrence assertion.
  - completeness assertion.
  - accuracy, valuation or allocation assertion.
  - presentation or disclosure assertion.
40. From the following which would not be an appropriate control procedure for the invoicing of customers?
- checking the existence of a dispatch note matching the approved sales order before an invoice is prepared.
  - using an authorised price list when preparing the invoice.
  - comparing totals for dispatch notes with totals for invoices.
  - segregating filling and dispatching sales orders.
41. Audit sampling is involved whenever an auditor:
- examines 100% of the population.
  - forms a conclusion about the population from which the sample is drawn.
  - performs tests of controls.
  - performs substantive tests.
42. Which of the following statements is most accurate about the terminology applied to errors identified when applying tests of controls or substantive testing to an audit sample?
- an error identified in substantive testing is referred to as an irregularity.
  - an error identified in substantive testing is referred to as a control deviation.
  - an error identified in a test of controls is referred to as a misstatement.
  - an error identified in a test of controls is referred to as a control deviation.
43. The justification for the wide use of non-statistical sampling in auditing is due to:
- cost/benefit considerations.
  - classical decision theory.
  - the concept of due care.
  - professional scepticism.
44. Which of the following is not a type of sampling risk?
- risk of overreliance.
  - risk of incorrect decision.
  - risk of sample size.
  - risk of underreliance.

45. Whenever sampling is used in an audit procedure, uncertainty will be present. The two sources of this uncertainty are:
- audit risk and detection risk.
  - inherent risk and control risk.
  - sampling risk and non-sampling risk.
  - detection risk and control risk.
46. The risk of concluding control risk is lower than it actually is, is also known as:
- risk of overreliance.
  - risk of underreliance.
  - risk of incorrect acceptance.
  - risk of incorrect rejection.
47. The risk of concluding a material error does not exist when in fact it does, is also known as:
- Risk of overreliance.
  - risk of underreliance.
  - risk of incorrect acceptance.
  - risk of incorrect rejection.
48. Which of the following would not be considered to be a source of non-sampling risk?
- human mistakes.
  - inappropriate audit procedures.
  - inappropriate sample size.
  - reliance on erroneous information.
49. Which of the following statements is inaccurate? The choice between non-statistical sampling and statistical sampling:
- does not affect the selection of auditing procedures to be applied to the sample.
  - does affect the appropriateness of the evidence obtained about individual sample items.
  - does not affect the appropriate response by the auditor to errors found in the sample.
  - does not impact on the need to exercise professional judgement.

50. The sample supports the conclusion that the recorded account balance is materially misstated when it is actually not materially misstated. This is the:
- a. risk of assessing control risk too low.
  - b risk of assessing control risk too high.
  - c .risk of incorrect acceptance.
  - d. .risk of incorrect rejection.

Formatted: Right: 0.63 cm

**PART B – ESSAY QUESTIONS (50 marks)**

**ATTEMPT ANY THREE QUESTIONS (All Questions carry equal marks)**

**QUESTION ONE (16.6 Marks)**

Following are a number of potential misstatements that might occur in sales and receivables. Also listed are a number of necessary controls for this cycle.

**Potential misstatements**

1. Cash may not be deposited intact daily.
2. Sales may be made without credit approval.
3. Sales invoices may have incorrect prices.
4. Cash sales may not be registered.
5. Mail receipts may be lost or misappropriated after receipt.
6. Invoices may be posted to wrong account.
7. Unauthorised shipments may be made.
8. Some shipments may not be billed.
9. Some receipts may not be recorded.
10. Fictitious sales transactions may be recorded.

**Necessary controls**

- A Sales invoices and matching documents required for all entries.
- B Independent check on pricing of invoices.
- C Credit department credit check on all new customers.
- D Matching sales invoice for each shipping document.
- E Mailing of monthly statements to customers.
- F Segregation of duties for filling and shipping orders.
- G Use of cash registers or point-of-sales devices.
- H Restrictive endorsement of cheques immediately on receipt.
- I Independent check of agreement of validated deposit slip with daily cash summary.
- J Check of agreement of amounts journalised and posted with daily cash summary.

**REQUIRED:**

For each potential misstatement, indicate, using the assigned letter, the necessary control that would most likely prevent or detect the misstatement.

**QUESTION TWO (16.6 Marks)**

The audit firm of Tindale & Partners (T & P) has lost a number of clients to larger competitor firms, and is anxious to rebuild its clientele. As part of its drive to expand services and attract new business, it recently acquired a computer system to network its office accounting and administrative functions from a local systems supplier - Turco Office Solutions.

The managing partner of T & P has just received a phone call from Alex Turco of Turco Computer Systems (TCS) requesting payment on the outstanding installation. At the moment T & P is strapped for cash, and is unable to make payment on the outstanding account. After explaining his firm's inability to pay the outstanding account, John Tindale has suggested a possible solution. Rather than borrow additional monies from the bank, TCS could re-invoice the account for the computer system from \$85,000 to \$30,000, and T & P could audit the accounts of TCS for a notional consideration of \$5,000 (last year's fees audit amounted to \$60,000).

Although T & P intend on having EDP audit capability for their clients, they do not as yet have those skills within the practice. Because T & P was very satisfied with the ease of installation and the suitability of the equipment supplied, John Tindale reasoned that it would largely be unnecessary to do any compliance testing of TCS' internal controls, and that a basic Balance Sheet audit would not take long to perform.

**REQUIRED:**

Outline any legal and ethical problems in connection with this audit, and in general terms, address the issues to legitimise the appointment of T & P as auditors of TCS.

Formatted: Right: 0.63 cm

**QUESTION THREE (16.6 Marks)**

Much has been written about the Audit Expectation Gap and the performance of auditors. Discuss the term "**Audit Expectation Gap**" giving consideration to the following matters:

Why is there an Audit Expectation Gap?

The claims or assertions made regarding audited financial statements by users.

Does Business failure = Audit failure?

**REQUIRED:**

Discuss the auditing profession's response in narrowing that gap.

**QUESTION FOUR (16.6 Marks)**

(a) Distinguish between:

Operational auditing;

Compliance auditing; and

External auditing.

(b) For both operational and compliance auditing, identify who might normally perform such audits, and give two examples of each type.

**QUESTION FIVE (16.6 Marks)**

Detail the basic sequence of facts of the Caparo vs Dickman case and summarise the requirements for a duty of care to exist to third parties expressed in this case.

To what extent has an auditor's liability to third parties changed since Caparo? Illustrate your answer with reference to at least three (3) post Caparo cases.

**QUESTION SIX (16.6 Marks)**

- A.** What are some reasons for the auditors to use a predominantly substantive approach audit approach?

Describe the three types of substantive procedures that an auditor might use and discuss when they might be used?

Explain some of the different circumstances when direct tests of details are necessary for the profit and loss accounts.

What is the auditor's objective in evaluating an accounting estimate?

**TOTAL MARKS (50 + 50 = 100 MARKS)**

**\*\*\*END OF EXAM\*\*\***

Formatted: Right: 0.63 cm

