

**MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY**

**P.O. Box 972-60200 – Meru-Kenya.**

**Tel: 020-2069349, 061-2309217. 064-30320 Cell phone: +254 712524293, +254 789151411**

**Fax: 064-30321**

**Website:** [**www.must.ac.ke**](http://www.must.ac.ke) **Email:** [**info@must.ac.ke**](mailto:info@must.ac.ke)

**University Examinations 2016/2017**

FIRST YEAR SECOND SEMESTER EXAMINATION FOR THE DEGREE OF MASTER IN BUSINESS ADMINISTRATION

**BFA 5227: AUDITING & FORENSIC ACCOUNTING**

**DATE: DECEMBER 2016 TIME: 3HOURS**

**INSTRUCTIONS:** *Answer question* ***one*** *and any other* ***three*** *questions*

**QUESTION ONE (15 MARKS)**

The following financial information shows the financial performance of the national airline for the period to 30th November 2016

**2012 2013 2014 2015 2016**

**Particulars shs. Billion shs. Billion shs. Billion shs.Billion shs.Billion**

Sales turnover 120 135 138 140 145

General administration

Expenses 80 90 100 114 125

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**2012 2013 2014 2015 2016**

**Particulars shs. Billion shs. Billion shs. Billion shs.Billion shs.Billion**

Salaries & wages 18 18 20 20 20

Finances costs 5 5 5 5 5

Directors fee& allowances 0.5 0.8 1 2 3

Profit before tax 16.5 21.2 12 (1) (8)

Taxation (5) (6) (3.6) 0 0

11.5 15.2 8.4 (1) (8)

General reserve (5) (5) (5) - -

Profits for distribution 6.5 10.2 3.4 (1) (8)

Dividends (5.0) (5.00) (5.0) - -

Retention for the year 1.5 5.2 (1.6) (1) (8)

Profit balance b/f - 1.5 6.7 5.1 4.1

Profit balance c/f 1.5 6.7 5.1 4.1 3.9

With the above financial information and data, the corporation directors hold a plan to restructure the firm and significantly boost the net incomes or operating profits. Restructuring proposal are:

1. Lay off non cores staff and from the layoffs save 10 billion annually
2. Sale of obsolete and non core assets and raise shs. 12 billion at 10% from international finance corporation combine the funds and acquire two modern state of the art of air craft that are efficient, high speed and have low fuel consumption.

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This is projected to increase net earnings by shs. 5 billion annually.

However, their exist serious dispute and likely shown down from workers union who have threatened to all quit if any one of them is retrenched. Union is of the view that cost of operations have increased due to corruption in procurements of supplies, pilferages and wastages and expensive lifestyles of managers and directors, and are of view that some managers and their portfolios need to be reduced, and directors should cut their high fees that have no justification. 30 managers take shs. 4.5 billion as wages annually while 1500 other staff take the balance of salaries and wages account and this has demotivated and demoralized staff. Workers are selling airline products but managers are misusing and abusing the revenues.

With additional borrowing of shs. 12billion the exiting lenders who have loaned the airline shs. 50billion are considering calling the loan if the airline go for additional loan. To trench staff it will cost the airline about 30 billion immediately in additional to legal costs should the matter go to courts of law.

The transport committee of parliament has engaged you have the experts/consulting firm to arbitrate on the despite and advise the way forward.

**Required:**

1. Discuss the methods you would use to collect evidence of the above assertions by the workers union on corruption and malpractices in the airline. (4 marks)
2. How different will be methods used in (a) above from those of investigating and collecting evidence on account of directors proposals for restructuring. (3 marks)
3. Advise management on the best option, either to eradicate corruption in the airline structures and systems or retrench and borrow and face loan calls and strikes. Put up a clear memorandum or basis for the choice you have obtained. (4 marks)
4. Discuss the merit of alternative dispute resolution such as mediation or arbitration, other than courts litigations and settlement. (4 marks)

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**QUESTION TWO (15 MARKS)**

The international standard on auditing ISA 300 planning an audit of financial statements requires the auditors to plan audit work so that the audit is performed in an efficient and effective manner.

**Required**:

1. Discuss the benefits of audit planning on the part of the auditors before marking on the execution of the audit assignment. (4 marks)
2. Elucidate some of the activities to be included in the audit plan (3 marks)
3. Illustrate clearly. Why it is necessary for the audit to have an audit strategy and the factors he or she should consider in designing an audit strategy (4 marks)
4. Why is it importance and of critical significance for the audit or to incorporate assessment of risk in the audit plan (4 marks)

**QUESTION THREE (15 MARKS)**

ISA 240 requires auditors to consider frauds on financial statements as most frauds have to do with books of account by those entrusted to keep them. Recently a firm of prominent lawyers lost a total seven cheque leaves plucked out with counter foils and led to a loss of shs.10 million. Cheque payment to a consultant firm was made with excess of almost 12 million by the national youth service, recently a bank lost 5 million through computer fraud and a petrol station was milked dry as revenues accountants raised invoices by use computer and later cancelling the invoices after the products had been loaded into awaiting tanker and left the depot.

**Required:**

1. Discuss the factors behind this state of affairs in our corporate financial environment.

(4 marks)

1. Explain the measures that government and corporate entities can employ to curb the increasing frauds and embarrassments to the accounting profession (3 marks)

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1. With regard to corporate business areas of :
2. Fixed assets
3. Sales and stocks
4. Cash
5. Salaries and wages

Show how the above can fraudulently be manipulated and the measures you would take as the in charge to stop and curb the menace in the enterprise. (8 marks)

**QUESTION FOUR (15 MARKS)**

The duty of accountability arises through out the private and public sectors whenever resources are entrusted to stewards by their owners. This duty is discharged by furnishing the owners with annual statements of accounts and audit report. Auditing therefore becomes a vital elements in the relationship of accountability.

**Required:**

1. To what extent is the internal auditing a vital element in the accountability relationship in a corporate entity (3 marks)
2. Do accounts and annual financial statements provide the overall utility of accountability? Explain (3 marks)
3. Discuss the limitations of accounts and reporting by the financial statements in the public sector with regard to determining financial responsibility (3 marks)
4. Explain the reasons behind low levels of accountability in the public sector in Kenya

(6 marks)

**QUESTION FIVE (15 MARKS)**

In a well economically endowed rural/county health facility and in the financial year ended June 30th 2016 the patients of the hospital in the wards were being given one meal per day i.e a breakfast of thin tea and a half plate of rice and beans as supper, from a period of 4 months.

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At times the Hospital matron would rebuke the patients mockingly that they are not sick and only suffering from hunger and loneliness in their homes especially those in age of 60-100years. However, forensic audit and examinations of financial transactions items showed that in the four months under review the hospital paid shs.2million for food stuffs consumed in the wards for an average of 200 patients per month in wards, money that would by far be more than adequate to provide food in the wards with breakfast, lunch and supper and with tea for 10a.m and 4pm daily for 4 months.

However forensic investigations, showed that food:

1. Supplies would be delivered by contracted firms but the same would be sneaked out at night under the orders of the hospital matron and be supplied to a nearby girls high school
2. The hospital security system new what was happening but they had taken oath not to make disclosure and were paid for overseeing the plunder of the patients food
3. Internal audit had made several observations and raised several queries but the matron who was a close confident of the county governor was not moved chief internal auditor of the county had opted to resign other than watch the malpractices. Complaints by the local MCA were fruiters. During a harambee for MCA’s son who was proceeding to United Kingdom further studies the matron gave shs. 500,000 as her contribution
4. Upon collection of overriding evidence by the forensic experts under the courtesy of county assembly, the forensic report was tabled before the assembly and by a majority vote the hospital matron, the procurement assistant together with security guards were all dismissed from employment with the county service board

Required:

1. Discuss the financial and administrative crimes, that were committed at county health facility as indicated above

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1. As a forensic experts and in your own wards illustrate the methods you would use to collect and gather evidence pertaining to the embezzlement of the patients food evidence that would admissible in a court of law
2. Explain the factors that have brought the county health facility to the state it is in, and what should be done by the county assembly to stop further financial crime occurring again.

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