



**MASINDE MULIRO UNIVERSITY OF  
SCIENCE AND TECHNOLOGY  
(MMUST)**

MAIN/BUNGOMA/WEBUYE/KAPSABET/NAIROBI CAMPUS

UNIVERSITY EXAMINATIONS  
2017/2018 ACADEMIC YEAR

THIRD YEAR SEMESTER ONE EXAMINATIONS

FOR THE DEGREE  
OF  
BACHELOR OF COMMERCE

**COURSE CODE:** BCA 320

**COURSE TITLE:** PRINCIPLES OF AUDITING

**DATE:** FRIDAY 2<sup>ND</sup> MARCH 2018

**TIME:** 3-5 PM

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**INSTRUCTIONS TO CANDIDATES**

Answer QUESTION ONE and any other two questions

**TIME:** 2 Hours

MMUST observes ZERO tolerance to examination cheating

This paper consists of 4 printed pages. Please turn over

### **QUESTION ONE (30 MARKS)**

(a) You are an audit senior in a firm of practicing accountants and your manager has gone out for an urgent meeting with a partner. Mr. Charo, a manager with Charo and Company, a wholesale business has come to your office with a request that your firm becomes their auditors.

**Required:**

(i) Describe to Mr. Charo the legal, ethical and practical factors your firm would consider before accepting the appointment. (10 marks)

(ii) Explain to Mr. Charo the qualifications and disqualifications of an accounting firm under the provisions of the Companies Act to become auditors. (10 marks)

(b) While auditing the financial statements of Apple Green Ltd, the certified public accounting firm of Onyango and Kamau CPA discovered that its client's legal expense account was abnormally high. Further investigation of the records indicated the following: Since the beginning of the year, several disbursements totaling to sh 150000 had been to the law firm of Kibet and Wafula Associates. Kibet and Wafula Associates were not Apple Green's attorneys. A review of the canceled checks showed that they had been written and approved by Mwakuterekwa, the cash disbursement clerk. Mwakuterekwa's other duties included performing the end-of-month bank reconciliation. Subsequent investigation revealed that Kibet and Wafula Associates are representing Mwakuterekwa in an unrelated embezzlement case in which he is the defendant. The checks had been written in payment of his personal legal fees.

**Required (10 marks)**

(i) What control procedures could Apple Green Ltd have employed to prevent this unauthorized use of cash?

(ii) Classify each control procedure in accordance with the COSO framework (authorization, segregation of functions, supervision, and so on)

(iii) Comment on the ethical issues in this case

### **QUESTION TWO (20 MARKS)**

In the course of audit of ABC Stationers Ltd for the year ended 30 June 2001, you have noted and recorded in the audit working papers, the following evidential matters:

1. Flowcharts of the company's payroll prepared by your audit assistant backed up by tests of controls.
2. An oral statement by the production director that the expected working life of plant acquired during the year is ten years.
3. A letter to the managing director from the company's bank manager indicating that the bank intends to extend overdraft facilities for a period of one year.
4. A list of items of inventory counted by a member of your audit team during the observation of the company's annual stock count.
5. A letter from a customer to your firm in reply to a confirmation request indicating agreement with the balance recorded in the books of ABC Stationers Ltd.

**Required**

a) With respect to each matter listed above, explain its relevance to the overall audit objectives of forming an opinion and reporting on the financial statements. (10 marks)

b) Explain your judgment on the reliability of the audit evidence obtained in five ways listed above. (10 marks)

### **QUESTION THREE (20 MARKS)**

The auditor's operational standards states, "The auditor should obtain relevant and reliable audit evidence sufficient to enable him to draw conclusion thereon."

#### **Required:**

- a) What factors would influence the judgment of the auditor with regard to sufficiency of the audit evidence? (10 marks)
- b) What factors would influence the auditor to accept third party certificates as audit evidence? (7 marks)
- c) State the important factors that must be considered when assessing the reliability of audit evidence. (3 marks)

### **QUESTION FOUR (20 MARKS)**

Inspection and monitoring of quality control by a firm of auditors involves both in-house and external procedures. The internal procedures include the post-audit review, sometimes known as a "cold review". The external procedures are sometimes known as "external practice inspections" or "peer reviews".

#### **Required:**

- a) Write explanatory notes on the "cold-review". (10 marks)
- b) Explain the advantages and disadvantages of "peer review". (10 marks)

### **QUESTION FIVE (20 MARKS)**

- a) State and briefly explain an auditor's responsibilities with regards to the detection of errors and frauds. (8 marks)
- b) In the context of the audit of a computerized accounting system;
  - i). State and explain internal control objectives generally associated with the processing of data in a computerized accounting environment. (6 marks)
  - ii). Identify the program controls which should be in built in a computerized accounting system. (6 marks)