

QUESTION 1

- A. Section 267 and 271 of the Companies Act 2016 respectively require for the private and public companies to appoint an auditor for each financial year. An auditor should ensure that the financial statements of the company are prepared in accordance with the relevant accounting standards. An auditor is guided by the auditing standards in order to obtain reasonable assurance that the financial statements are free from material misstatements.

Required:

- i. Explain two (2) benefits of a financial statements audit performed by an approved company auditor. (4 marks)
 - ii. Explain the term 'reasonable assurance'. (3 marks)
 - iii. Explain two (2) importance of auditing standards to an auditor in performing the assigned duties. (3 marks)
- B. Auditors are required to adhere to the Fundamental Principles of the Malaysian Institute of Accountants (MIA) By-Laws (on Professional Ethics, Conduct and Practice) to safeguard the profession.

Required:

In the context of the MIA By-Laws, briefly define the following:

- i. Integrity
 - ii. Objectivity
 - iii. Professional competence and due care
 - iv. Confidentiality (6 marks)
- C. For the following scenarios, explain whether the MIA By-Laws (on Professional Ethics, Conduct and Practice) has been violated:
- i. Sakinah is an accounting graduate who has just been admitted as a new MIA member. During a recent taxation seminar, she distributed her business cards to prospective clients. Besides her name and contact number, the business card also indicates the name of the firm she is attached to, her designation as a chartered accountant as well as particulars relating to her professional qualification.

- ii. Hamizah & Co, a public accounting firm based in Johor Bharu, has been offered to provide IT services to an existing client, Utama Budi Bhd. Nevertheless, the partner of Hamizah & Co has declined the offer due to shortage of staff. The partner then introduced the prospective client to Karim & Co, another public accounting firm in Johor Bharu, who then accepted the appointment. For the referral, the partner of Hamizah & Co received RM1,000 as a token of appreciation and this is acknowledged by Utama Budi Bhd.

(4 marks)

(Total: 20 marks)

QUESTION 2

Katarana Sdn Bhd operates a business in the wholesale distribution of consumer products. You are one of the auditors attached with Vijay Salleh & Associates who has been appointed to audit Katarana Sdn Bhd's financial statements for the financial year ended 31 December 2018. Your team leader has assigned you to review the company's sales system. Your observations are as follows:

Sales Department

The sales department directly receives order from both regular and new customers. For regular customers, Encik Faizal, who is the sales department assistant processes the order and immediately prepares the delivery order in four copies. The first copy is sent to the customer, second copy to the store, third copy to the accounts department and the fourth copy is retained in the sales department's file. For new customers, the sales manager grants the credit and processes the order after the approval by the higher management.

Warehousing Department

Encik Khairil is the only storekeeper handling the stores department. On receipt of the delivery order from the sales department, he makes the necessary arrangement to deliver the goods to the customers. He prepares the delivery notes in quadruplicate with the customer's details, quantity, specification and rates of the goods delivered. Goods will be delivered to the customers either at the stores or at their site based on the terms in the delivery order. The original copy of the delivery note is given to the customer at the time of delivery. The second copy is given to accounts department, third copy is sent to the sales department and the fourth copy is kept in the store's file.

Accounts Department

The accounts department is headed by Puan Amirah and assisted by a clerk, Encik Muthu and a cashier. On receipt of a copy of the delivery order and delivery note, Encik Muthu raises the invoice and forwards the original copy to the customer. The second copy is sent to the sales department while the third copy is retained in his department's file. All cheques received by the company are handed over to the cashier who will issue serially numbered receipts and the cashier, then, deposits the cheques into the bank.

Encik Muthu, who maintains the sundry debtors' ledger, posts the transactions and prepares monthly schedules of outstanding debtors. If the customer delays payment or made short payment, he will write to them. If the short payment is due to shortage in supply or poor quality of product, Encik Muthu will credit the customer's account with suitable rebate or allowances. Encik Muthu also prepares the bank reconciliation statement once in every three months.

Required:

- a. Identify any six (6) internal control weaknesses of the existing sales system of Katarana Sdn Bhd and describe the potential impact that could occur due to the weaknesses that have been identified.

Present your answers in the following format:

Internal control weaknesses	Impact of the weaknesses

(10 marks)

- b. Suggest three (3) improvements that can be made to the internal control system of Katarana Sdn Bhd that could prevent any potential irregularities in the company. (6 marks)
- c. Differentiate between 'internal controls' and 'test of controls'. (4 marks)

(Total: 20 marks)

QUESTION 3

A review engagement is carried out in accordance with the International Standard for Review Engagements (ISRE) 2400. During review engagement, the auditor should apply the same materiality considerations as would be applied if an audit opinion on the financial statements were being given. Although there is a greater risk that misstatements will not be detected in a review than in an audit, the judgment as to what is material is made by reference to the information on which the auditor is reporting and the needs of those relying on that information, not to the level of assurance provided.

Required:

- a. Differentiate between 'audit engagement' and 'review engagement' in respect of their objective and comparative level of assurance. (4 marks)
- b. Justify the need for a review of financial statements. (3 marks)
- c. Explain the reason why 'there is a greater risk that misstatements will not be detected in a review than in an audit'. (3 marks)

(Total: 10 marks)

QUESTION 4

Energy Bhd (Energy) manufactures energy drinks made from dates and peaches. The financial year end is 31 December 2018. You are the audit manager of Meor & Associates and are currently planning the audit of Energy. You had attended the planning meeting with the engagement partner and finance director and the minutes from the meeting are shown below.

Minutes of planning meeting for Energy

Energy's trading results have been strong this year and the company is forecasting revenue of RM85 million, which is an increase from the previous year. The company has invested significantly in the production of dates and peaches drinks at the factory. This resulted in expenditure of RM5 million on upgrading, repairing and replacing a significant amount of machinery used in the production process.

As the level of production has increased, the company has expanded the number of warehouses it uses to store inventory. It now utilises 15 warehouses; some are owned by Energy and some are leased from third parties. There will be inventory counts taking place at all 15 warehouses at the year end.

A new accounting general ledger has been introduced at the beginning of the year, with the old and new systems being run in parallel for a period of two months as a pilot run.

As a result of the increase in revenue, Energy has recently recruited a new credit controller to follow up on the outstanding receivables. The finance director thinks it is not necessary to continue to maintain an allowance for receivables and so has released the opening allowance of RM1.5 million as it is no longer required. In addition, Energy has incurred expenditure of RM4.5 million on developing a new brand of energy drinks. The company started this process in January 2016 and is due to launch their new product into the market.

The finance director stated that there was a problem in November in the mixing of raw materials within the production process which resulted in a large batch of dates products tasting differently. A number of these products were sold, however, due to complaints by customers about the flavour, no further sales of these goods have been made. No adjustment has been made to the valuation of the damaged inventory, which will still be held at cost of RM1 million at the year end.

As in previous years, the management of Energy is due to be paid a significant annual bonus based on the value of year-end total assets.

Required:

- a. Explain audit risk and the components of audit risk. (8 marks)
 - b. Using the minutes provided, identify and describe six (6) audit risks, and explain the auditor's response to each risk, in planning the audit of Energy Bhd. (12 marks)
- (Total: 20 marks)

QUESTION 5

ISA 500 explains what constitutes audit evidence in an audit of financial statements, and deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.

Required:

Describe substantive procedures that the auditor should perform in order to obtain sufficient and appropriate audit evidence in relation to:

- a. Research and development expenditure. (5 marks)
 - b. Depreciation of property, plant and equipment. (5 marks)
- (Total: 10 marks)

QUESTION 6

You are the audit manager in Nazatul & Associates and nearly completing the audit of BMS Bhd. The team leader has produced the extracts from the draft audit report for BMS Bhd as shown below.

Auditor's responsibility

1. Our responsibility is to express an opinion on all pages of the financial statements based on our audit. We conducted our audit in accordance with most of the International Standard of Auditing.
2. Those standards required that we comply with ethical requirements and plan; and perform the audit to obtain maximum assurance as to whether the financial statements are free from all material misstatements whether caused by fraud or error.
3. We have a responsibility to prevent and detect fraud and error; and to prepare the financial statements in accordance with the Malaysian Financial Reporting Standards.
4. An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statement. The procedures selected depends on the availability and experience of audit team members. We considered internal controls relevant to the entity; and express an opinion on the effectiveness of these internal controls.
5. We did not evaluate the overall presentation of the financial statements, as this is the management's responsibilities. We considered the reasonableness of any accounting estimates made by management. We did not review the appropriateness of accounting policies as these are the same as last year.

Required:

For the above audit report extracts, identify and explain ten (10) elements of this report which require amendment.

(Total: 20 marks)

END OF QUESTION PAPER