

INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS OF PAKISTAN



Spring (August) 2012 Examinations

Friday, the 31st August 2012

RISK MANAGEMENT AND AUDIT (S-503)

STAGE - 5

Time Allowed: 02 Hours 45 Minutes

Maximum Marks: 80

Roll No.:

- (i) Attempt all questions.
- (ii) Answers must be neat, relevant and brief.
- (iii) In marking the question paper, the examiners take into account clarity of exposition, logic of arguments, effective presentation, language and use of clear diagram/ chart, where appropriate.
- (iv) Read the instructions printed inside the top cover of answer script CAREFULLY before attempting the paper.
- (v) Use of non-programmable scientific calculators of any model is allowed.
- (vi) DO NOT write your Name, Reg. No. or Roll No. anywhere inside the answer script.
- (vii) Question No.1 – “Multiple Choice Question” printed separately, is an integral part of this question paper.
- (viii) **Question Paper must be returned to invigilator before leaving the examination hall.**

- | | Marks |
|--|--------------|
| Q. 2 (a) An experienced risk manager working with Decent Contractors (Pvt.) Limited, a company engaged in various constructions projects carrying out at different locations. You have recently joined the company as deputy risk manager. Your risk manager asked you some common methods of identifying possible risks as the nature of operation has posed various potential risks? Explain. | 05 |
| (b) After satisfactory response of the question (a) above, your manager further asked you that in measuring risks we may take a number of factors into account. What types of such risk factors may be commonly found? Give at least two examples each. | 06 |
| (c) Your manager has further asked you that if you have to perform a brainstorming session in the capacity of a leader, what rules of participation will you likely to observe there? | 04 |
| Q. 3 (a) Prime Bank Limited, a bank with over hundred branches all over the country, has completed one year of its successful operation. The directors of the bank in their board meeting have appointed Raja & Co., as auditors to perform audit of its head office and all branches. What kind of audit is this? (Give reasons) | 02 |
| (b) In the same year Prime Bank Limited, in their annual general meeting has appointed Kalam & Co., as auditors to perform audit of its head office and all branches. The auditors are required to visit all branches throughout the year, therefore, auditors agreed to pay monthly visit. What kind of audit is this? (Give reasons) | 02 |
| (c) (i) At the same year directors of Prime Bank Limited, appointed Raza & Co., to perform audit procedures concerning to current assets, revenues, and expenses only which is duly agreed between both parties (i.e., auditor and auditee). What kind of service is this? (Give reasons) | 02 |
| (ii) What important contents Raza & Co., have to include in their report which are necessary under the said engagement? (No need to mention those contents which are common in other form of engagement) | 09 |

PTO

Q. 4 Manager finance of Popular Hotels Management Limited (PHML) came across dual payment of same bill by avoiding placing paid stamp on the bill. So, he took all previous vouchers and revealed that such kind of fraud may be committed by the cashier. He further learned that such fraud has been committed in past years as well which have already been audited. He informed director finance who then contacted auditors and asked them why PHML shouldn't sue auditors. Should auditors be held responsible if:

- (i) Auditors proved that they have performed their duties with professional competence, professional skepticism, and due care? Elaborate. **02**
- (ii) Auditors failed to prove that they did not commit negligence in order to detect the fraud mentioned in (i) above. Elaborate. **02**
- (iii) Auditors failed to prove that they did not commit negligence, however, they proved that such fraud was never committed during the year audited by them. Elaborate. **02**
- (iv) Auditors proved that they have detected such fraud and the same has been mentioned in the management letter as well as in the notes to the accounts, however, instead of its materiality they have delivered unqualified report. Elaborate. **02**
- (v) Auditors proved that such fraud was never committed in the current audited year, however, it was committed three years before where they had committed negligence to detect such fraud, and therefore they are not liable after such long period. Elaborate. **03**

Q. 5 (a) Assume you have been working as an assistant manager of Furqan & Co., a chartered accountants firm. A team of your firm was engaged in the audit of Happy Home (Pvt.) Limited, a fast moving consumer goods company. Due to your university exams you met your audit team when they were near to conclusion. During review of working papers you asked audit supervisor (who was leading the engagement team), why they did not get representation letter. Audit supervisor replied that management provided verbal representations several times, moreover, that they did not imply any restriction on access to any record or books of accounts. He further argued that auditors are responsible to apply audit procedures in order to express their opinion about correctness of books of accounts; therefore auditors cannot take management representation as sufficient appropriate audit evidence. Company will also provide us signed financial statements which may itself be deemed as a written representation by the management.

Required:

- (i) What may be your comments in order to guide audit supervisor about his concerns? **06**
- (ii) Further guide him what actions should an auditor carry out if:
 - Management refused to provide written representations. **04**
 - Auditor has doubts about the reliability of written representations provided by the management. **03**
- (b) (i) Define 'test of controls'. **01**
- (ii) Define 'substantive procedures'. **01**

(iii) What may be the effect (i.e., increase, decrease, or negligible) of the following factors on the sample size for test of controls?

02

Factor	*Effect on Sample Size
• An increase in the extent to which the auditors' risk assessment takes into account relevant control.	
• An increase in the tolerable rate of deviation.	
• An increase in the expected rate of deviation of the population to be tested.	
• An increase in the auditors' desired level of assurance that the tolerable rate of deviation is not exceeded by the actual rate of deviation in the population.	

(iv) What may be the effect (i.e., increase, decrease, or negligible) of the following factors on the sample size for tests of details?

02

Factor	*Effect on Sample Size
• An increase in the auditors' assessment of the risk of material misstatement.	
• An increase in the use of other substantive procedures desired at the same assertion.	
• An increase in the auditors' desired level of assurance that tolerable misstatement is not exceeded by actual misstatement in the population.	
• An increase in the tolerable misstatement.	

Q. 6 (a) Standard Wheels Limited, have its head office in Karachi while its production units are situated at Hub. The company has been engaged in manufacturing and distributing wheels of different vehicles to all over the country. After several requests from general manager finance to get cost accounts audited whether from an employee of the company or as outsource service of any audit firm. Director finance has appointed Mr. Akmal, as cost auditor, who at the commencement of cost audit asked management for necessary information which may be helpful to him in performing cost audit of the company effectively. Identify and list down such information.

07

(b) Enlist areas at a broad category where Mr. Akmal should perform cost audit procedures.

06

(c) How should Mr. Akmal examine "Sales" of the company in the capacity of a cost auditor?

07

THE END