**MAKERERE UNIVERSITY BUSINESS SCHOOL**

**FINAL EXAMINATION**

**FOR THE DEGREE OF BACHELOR OF SCIENCE IN ACCOUNTING OF MAKERERE UNIVERSITY ACADEMIC YEAR 2023/2024**

**COURSE NAME:** Audit Theory & Practice  **YEAR OF STUDY:** Three

**COURSE CODE:** BSA 3204 **DATE:** Tuesday, April 23, 2024

**SEMESTER :** Two **TIME:** 2:00 Pm – 5:00 Pm

***Instructions:***

1. *Section A has one compulsory question carrying 25 marks.*
2. *Section B has five questions and only three are to be answered. Each question carries 25 marks.*
3. *Write all your answers in the answer booklet provided.*
4. *Please, read further instructions on the answer booklet before answering any question.*

**SECTION A (*Compulsory*)**

**Question One**

It is April 2024. You are an audit assistant with BKKB and Co CPAs and are responsible for the final audit of your existing client Bugolobi Co Ltd, which is due to commence in June 2024. Bugolobi Co Ltd is a listed company which manufactures furniture. Its draft financial statements for the year ending 30April 2024 show revenue of Shs 65.1 million and profit before tax of Shs 18.2 million. The following matters have been brought to your attention:

**Revenue**

Bugolobi Co Ltd.’s revenue is generated through sales to individual customers via its website and also to wholesale customers such as garden centres and stores. Price increases in line with inflation were applied across all products in June 2023. Bugolobi Co Ltd successfully launched three new product lines in November 2023. Whole sale customers place their orders on credit via Bugolobi Co Ltd.’s sales ordering department, individual customers place their orders online and immediately pay full amount owing. The goods are normally dispatched within seven days of the customer placing the order.

**Issue of share capital**

The company is looking to expand its operations by securing an additional factory site in October 2024. In order to raise sufficient capital to fund the factory purchase, Bugolobi Co Ltd issued ordinary shares at a premium in March 2024, raising a sum of Shs 4.3 million

**Bank balances**

The bank and cash figure included in Bugolobi Co Ltd.’s draft financial statements is comprised of a number of bank account balances: an overdraft of Shs 5.1 million which is the company's main current account and Shs 0.2 million relating to several savings accounts. The finance director has informed the audit manager that all accounts have been reconciled as at the year end. The overdraft of Shs 5.1 million has increased significantly since the prior year (2023: Shs 1.2 million). The directors have informed you that the overdraft facility, which the company requires in order to operate on a daily basis, is due for renewal in October 2024 and that they are confident it will be renewed.

**Required:**

1. Describe substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in relation to Bugolobi Co Ltd.’s revenue. [8 Marks]
2. Explain the steps the auditor should perform in undertaking a positive receivables circularisation for Bugolobi Co Ltd. [4 marks]
3. Elaborate on the substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in relation to Bugolobi Co Ltd.’s issue of share capital. [8 Marks]
4. Develop substantive audit tests to obtain evidence in relation to Bugolobi Co Ltd.’s bank balances. [5 marks]

**SECTION B *(Answer any THREE questions)***

**Question Two**

BSA Door Glass Co (BSA) is a glass manufacturer which operates from a large production facility. In the facility, BSA undertakes continuous production for 24 hours a day and 7 days a week. Also, on this site are two warehouses, where the company's raw materials and finished goods are stored. BSA's year end is 30 April.

BSA is finalising the arrangements for the year-end inventory count, which is to be undertaken on 30 April 2024. The finished Doors are stored within 20 corridors of the first warehouse. The second warehouse is for large piles of raw materials, such as sand, used in the manufacture of glass. The following arrangements have been made for the inventory count. The warehouse manager will supervise the count as he is most familiar with the inventory. There will be ten teams of counters and each team will contain two members of staff, one from the finance and one from the manufacturing department. None of the warehouse staff, other than the manager, will be involved in the count.

Each team will count a corridor of finished goods by counting up and then down each corridor. As this process is systematic, it is not felt that the team will need to flag areas once counted. Once the team has finished counting a corridor, they will hand in their sheets and be given a set for another corridor of the warehouse. In addition to the above, to assist with the inventory counting, there will be two teams of counters from the internal audit department and they will perform inventory counts.

The count sheets are sequentially numbered, and the product codes and descriptions are printed on them but no quantities. If the counters identify any inventory which is not on their sheets, then they are to enter the item on a separate sheet, which is not numbered. Once all counting is complete, the sequence of the sheets is checked and any additional sheets are also handed in at this stage. All sheets are completed in ink.

Any damaged goods identified by the counters will be too heavy to move to a central location, hence they are to be left where they are but the counter is to make a note on the inventory sheets detailing the level of damage.

As BSA undertakes continuous production, there will continue to be movements of raw materials and finished goods in and out of the warehouse during the count. These will be kept to a minimum where possible.

The level of work in progress in the manufacturing plant is to be assessed by the warehouse manager. It is likely that this will be an immaterial balance. In addition, the raw materials quantities are to be approximated by measuring the height and width of the raw material piles. In the past this task has been undertaken by a specialist; however, the warehouse manager feels confident that he can perform this task.

**Required:**

1. Identify and explain five deficiencies in BSA’s internal control system, and provide a control recommendation to address each of these deficiencies. [15 Marks]
2. Describe a test of control the external auditors should perform to assess if each of these controls, if implemented, is operating effectively to reduce the identified deficiency. [5 Marks]
3. As an Audit Assistant at Nanyonjo & Co CPAs responsible for the audit of inventory for BSA. You will be attending the year-end inventory count on 30 April 2024. In addition, your manager wishes to utilise substantive testing in auditing BSA Door Glass Co's inventory.

**Required:** Describe the procedures you will undertake DURING the inventory count of BSA Door Glass Co in order to gain sufficient appropriate audit evidence. [5 marks]

***Note:*** *Use a table to answer sub-questions a & b. The table should have the following columns: control deficiency and its effect, control recommendation and test of control.*

**Question Three**

Your Audit firm, Okello Akello & Co. (OAC) CPAs, has been re-appointed as auditors of Kololo Courier Services Limited (KLS) for the year ended 31 March, 2024. OAC has been auditing KLS for 5 years. KLS’s financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). You are the audit senior in charge of the audit of KLS and you have to ensure, among other things, that the audit is conducted in accordance with International Standards on Auditing (ISAs).

As part of planning, you and the audit manager attended a pre-audit meeting with KLS’s management. The following brief notes were prepared during that meeting:

* KLS finance manager Mr. Emmanuel Odur joined the company on 1 July, 2023. He previously worked at St. Agnes Primary School as a Bursar.
* KLS carried out a restructuring exercise in December 2023 and 50 employees were laid off. A provision of Shs 50 million has been included in the financial statements for compensation. Some employees have, however, sued the company claiming the compensation to be given to them is too small.
* KLS’s trade and other receivables amount to Shs 5 billion as at 31 March, 2024. KLS made a general provision of 5% of the total trade and other receivables. Some clients have written to KLS about the financial difficulties they are facing but the Finance Manager is sure that they will be able to pay. No specific provision has been made in respect of this.
* The Finance Department is under staffed. It has only three staff instead of the required six.
* Sandra, a former employee of KLS, joined OAC on 1 March, 2023. She is slated to be part of the audit team because, it is felt, that her experience of working with KLS will be of great value to the audit team.
* An analytical review carried out on KLS’s financial statements showed a material variance which was due to an increase in finance costs by over 50% in the current year.
* KLS intends to list on the Uganda Securities Exchange. However, one of the requirements is to have an independent Board in place. OAC is tasked with the responsibility of recommending to KLS members to serve on the board.
* KLS has significant outstanding audit fees but OAC is not worried as KLS has always endeavoured to pay.

**Required:**

1. Discuss, with the Audit Manager:
2. The possible financial statements risks the audit team is likely to face during the audit of KLS. [5 marks]
3. How the financial statements risks in (a) (i) above can be mitigated to an acceptably low level. [5 marks]
4. Examine the actual and possible ethical threats that may arise in relation to the audit of KLS, and the safeguards to reduce them. [6 marks]
5. Describe the assertions made by KLS’s management in relation to the trade and other receivables balance. [4 marks]
6. Explain the substantive audit procedures the audit team should perform on trade and other receivables. [5 marks]

**Question Four**

Nakaazi & Co CPAs., where you work as an audit assistant is the auditor for BSA Saving Association Limited (BSAL) for the year ended 31st March 2024. BSAL is a registered Savings and Cooperative Society (SACCO) with over 1,500 members. Nakaazi & Co. has been auditing BSAL for the last 3 years. They gave a “Qualified opinion except for” for the first two years. In 2023, they gave an “Unqualified audit opinion”. The members have expressed concern about the change of audit opinion and desire to know why this is the case.

BSAL members have also expressed their concern why the auditors have never communicated to them throughout their three years of audit of BSAL. ISA 260, however, requires that the auditor determines the appropriate persons within the organisation governance structure with whom to report relevant audit matters concerning the organisation. Nakaazi & Co. is, therefore, under no obligation to communicate with all the members of BSAL. However, being a socially responsive audit, which serves public interest, Nakaazi & Co is considering a response to concerns raised by BSAL members.

**Required:**

1. Explain the circumstances under which Nakaazi & Co CPAs may issue:
2. Unqualified audit opinion. [6 Marks]
3. Qualified opinion-except for. [6 Marks]
4. Adverse audit opinion [3 Marks]
5. Disclaimer of opinion [2 Marks]
6. Describe the objectives, the auditor seeks to achieve in determining the appropriate persons within BSAL to communicate to during an audit. [8 Marks]

**Question Five**

1. Explain the benefits and limitations of an external audit. [10 Marks]
2. Describe the overall objectives of the audit of financial statements. [4 Marks]
3. Elaborate on the functions of the Board Audit Committee in a commercial bank. [6 Marks]
4. What factors should the Auditor consider while assessing the reliability of audit evidence? [5 Marks]

**Question Six**

1. What are the four major types of public sector audits in Uganda. [8 Marks]
2. Describe any five internal audit activities in an organisation of your choice. [5 Marks]
3. Describe the auditor’s responsibility for subsequent events occurring between: the year-end date and the date the auditor’s report is signed. [5 Marks]
4. Nakawa Cereals Ltd produces wheat flour and bread in Kampala. The audit for the year ended 31 December 2023 is nearly complete and the financial statements and audit report are due to be signed shortly. Profit before taxation is Shs 710 million. The following event occurred in 2024 and no amendments or disclosures have been made in the financial statements.

On 5 February 2024, a fire gutted one of the company’s warehouses for wheat and the estimated damage was Shs 60 million. The company’s operations have not greatly been affected by the fire. PPEI, the entity’s insurance company is already investigating the fire to assess the likelihood and level of payment. Its preliminary findings indicate that the fire was started deliberately at night by disgruntled company guards and the confirmation of this information would invalidate any insurance cover.

**Required:** For the subsequent event described above:

1. Explain whether the financial statements require amendment. [3 Marks]
2. Describe audit procedures which should be performed to form a conclusion on any required amendment. [4 Marks]

***End of the examination paper***