



Audit, Assurance and Related Services

Instructions to examinees:

- (i) Answer all **SEVEN** questions.
- (ii) Answer in **black** pen only.

Q.1 You are the audit manager at Haroon Rahim and Company, Chartered Accountants responsible for the audit of Fit Bit Limited (FBL) for the year ended 30 November 2020. FBL is a listed company and is engaged in the manufacturing of fitness equipment and related accessories. FBL sells its products all over the country through a chain of distributors.

The extracts from the draft financial statements for the year ended 30 November 2020 are as follows:

	2020	2019
	----- Rs. in million -----	
Revenue from sale of fitness equipment	71,000	70,000
Revenue from subscription of plans	30,000	-
Profit before tax	500	400
Property, plant and equipment	6,600	6,900
Intangible assets	1,000	250
Advance from customers	10,000	200
Stock in trade	16,000	15,800

During the month of October 2020, due to faulty pad used in a newly manufactured fitness equipment, 60 accidents were reported where FBL had paid compensation aggregating Rs. 30 million. Upon identification of fault, the sale of this equipment was immediately suspended until the matter was resolved in a month's time. The entire compensation amount paid to customers has been reported in the financial statements as receivable from a supplier who had supplied such faulty pads.

On 1 January 2020, FBL launched a mobile application that generates personalized exercise and diet plans considering an individual user's physical and medical conditions. The application has received an overwhelming response as large number of domestic and foreign customers have subscribed for it. Following information is available in this respect:

- (i) The application was developed in-house with the support of a leading software house.
- (ii) Each customer has an option to subscribe biannual or annual plan.
- (iii) All the subscription plans are paid in advance; however, each subscriber has an option to cancel the plan within 30 days and claim the refund of the entire subscription amount.

Required:

Discuss the audit risks that exist in the above scenario and suggest the key audit procedures to be performed in respect of the identified risks.

Q.2 You are the audit manager at HTC and Company, Chartered Accountants. Following matters relating to a joint audit of Petro Oil Limited are brought into your attention by audit team:

- (a) The joint auditors have agreed upon an audit strategy through which they have segregated audit areas for both the firms.

Required:

Discuss how your firm can ensure before finalization of the audit report that the work carried out by the other joint auditor has been in accordance with the agreed audit strategy. (05)

- (b) There is a difference of opinion on impairment of intangible assets. Your firm wants to issue a qualified report whereas the joint auditor is convinced with the management's explanation and intend to issue an unmodified report.

Required:

Discuss the course of action available to your firm. (04)

Q.3 You are the audit manager at Moosa and Company, Chartered Accountants responsible for the audit of Beta Bank Limited (BBL). While planning the audit for the year ending 31 December 2020, you come across a news published in a national newspaper that BBL has suffered a cyber-attack which has resulted in theft of depositors' confidential data.

Required:

Discuss the course of action you should plan in response to cyber-attack. (12)

Q.4 You are the audit manager responsible for the audit of Kekra Pakistan Limited (KPL). KPL has various production facilities across the country. Your audit team has brought the following matters to your notice which require your guidance:

- (i) KPL is required to decommission its production facilities and restore the site at the end of their economic life. Notes to the financial statements for the year ended 30 September 2020 contain the following disclosures related to decommissioning provision:

	Rs. in million
Balance at the beginning of the year	7,126
Provision made during the year	371
Reversal due to changes in estimates	(1,471)
Unwinding of discount	720
Balance at the end of the year	6,746

- (ii) As a result of decrease in demand, the management adjusted its medium-term and long-term price assumptions and discount rates, which had a significant impact on asset valuation. At 30 September 2020, KPL recognized an impairment of Rs. 2,184 million against the carrying value of cash generating unit.

Required:

Brief the audit team regarding the significance of the above matters and the audit procedures to be performed in this respect. (15)

Q.5 Salman Qasim is an audit senior of Ibrahim & Company, Chartered Accountants. He joined the ongoing audit of Kalam Limited (KL) which was under completion stage. During the audit, he came to know that the newly appointed Chief Financial Officer (CFO) is a close friend of the audit manager which was not disclosed by him to the firm. He decided to disclose this matter to the engagement partner; however, he came to know that the engagement partner has been out of country for last one month and has not yet discussed the progress of the audit with the audit team. He then wrote an email to the firm's quality control partner and brought all such observations in his knowledge.

Required:

Discuss the professional and ethical issues arising in the above situation and advise the course of action that the firm's quality control partner should take.

(13)

Q.6 You are the audit manager of Zafar Iqbal & Company, Chartered Accountants. You have asked one of the team members assigned on the audit of Brown Sugar Limited to draft the Key Audit Matter section of the audit report for the year ended 30 June 2020. The extracts from the draft report are as follows:

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the Basis for Adverse Opinion section, we have determined the matter described below to be the key audit matter to be communicated in our report.

Key audit matter	How our audit addressed key audit matter
<p>In the course of conducting a sales tax audit for the period from January 2019 to December 2019, FBR raised certain issues with respect to the company's sales. On May 2020, the company received an order in which demand of Rs. 100 million was raised. The company has filed an appeal with the appellant board and is confident that it would be decided in company's favour.</p> <p>Due to the materiality and significance of the above matter we have considered this tax contingency as a key audit matter.</p>	<p>Our key audit procedures in this area included amongst others were:</p> <ul style="list-style-type: none"> ▪ We reviewed the correspondence of the company with relevant tax authorities and tax advisors including judgements or orders passed by the competent authorities. ▪ We also obtained and reviewed confirmations from the company's external tax advisor for the latest status of the case. ▪ We involved internal tax experts to assess and review the management's conclusion on this matter. ▪ We verified all the journal entries posted in the ledgers related to legal expenses. ▪ We obtained representation from the management regarding the favourable outcome of the matter. <p>Based on the procedures performed, we concluded that there is no material misstatement and contingency has been adequately disclosed.</p>

Required:

Critically analyse the Key Audit Matter section of the audit report.

(13)

- Q.7 (a) You are employed as an audit manager in Bashir and Company, Chartered Accountants. One of your clients, Davidsons Pharma Limited (DPL), is considering to acquire 60% shareholding in Sehat Healthcare (Pvt.) Ltd. (SHPL) and has requested your firm to carry out a due diligence.

During the fieldwork of due diligence exercise, your team has brought the following matters to your attention:

- (i) A major customer which accounts for 10% of SHPL's annual sales has refused to place further sale orders. On inquiry, it was revealed that competitor has offered significant discount of 12% to increase its market share.
- (ii) DPL has central distribution model where single distributor has non-exclusive rights countrywide with commission rate of 5%. All sales made to the distributor on 30 days' credit. On the Other hand, SHPL has a regional distribution model where multiple distributors are involved country wide with commission rates ranging from 2% to 4%. Under this model, all sales are made on cash.

Required

Discuss how the above matters are to be investigated for due diligence review and also recommend the additional procedures to be performed in this respect. (12)

- (b) Your firm has been approached by Agar Products Limited for audit of accounts receivable and accounts payable reported in the financial statements. The financial statements were prepared in accordance with the general purpose framework and is audited by another firm of chartered accountants.

Required:

Discuss the matters you would consider before accepting the above assignment. (04)

(Ignore the ethical considerations for the acceptance of the audit)

(THE END)