Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Hong Kong's
CPA Qualification
香港會計師專業資格

Qualification Programme

Associate Module 8
Principles of Auditing

Pilot Examination Paper

Time Allowed	2 hours 30 minutes
Examination Assessment Allocation Objective Type / Scenario-based Questions	100 Marks All questions are compulsory

This pilot examination paper simulates a typical examination paper that assesses candidates' core foundational technical knowledge of the subject matters, and their skills in applying the knowledge to tackle routine professional problems, including computations. Mark(s) for each question is set in accordance with its level of difficulty.

The sample questions in this paper are to help candidates familiarise themselves with the form and style of questions which they may see in the Module 8 examination. The sample questions and answers are for reference only, and the content may not have been updated to reflect any changes in relevant standards or legislation.

You should answer **all questions** in this paper and allocate approximately 1.5 minutes for each mark.

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OBJECTIVE TYPE QUESTIONS (Total: 74 marks)

Answer **ALL** questions in this section. Together they are worth 74% of the total marks for this examination.

1 Determine whether the statement is true or false based on your knowledge and choose the appropriate option. Answer all sub-questions as required. *(2 marks)*

Answer area

(a) In a test of control, an increase in the tolerable rate of deviation would increase the sample size. *(1 mark)*

- A. True
- B. False

(b) An anomalous error is an one-off error for which the auditor must obtain sufficient appropriate audit evidence that such error is not representative of the population. *(1 mark)*

- A. True
- B. False

2 Determine whether the statement is true or false based on your knowledge and choose the appropriate option. Answer all sub-questions as required. *(2 marks)*

Answer area

(a) If general controls are ineffective, then application controls will generally be ineffective. *(1 mark)*

- A. True
- B. False

(b) The system rejects a sales order which takes the customer over its agreed credit limit is an example of a logical access control. *(1 mark)*

- A. True
- B. False

3 Determine whether the statement is true or false based on your knowledge and choose the appropriate option. Answer all sub-questions as required. *(2 marks)*

Answer area

(a) An audit procedure of agreeing total payroll expense per the payroll system with the trial balance and financial statements would test the occurrence assertion for payroll. *(1 mark)*

- A. True
- B. False

(b) Tracing physical inventory to the count sheets would verify the existence of inventory during the inventory count. *(1 mark)*

- A. True
- B. False

4 Substantive procedures are designed to _____ material misstatements at the assertion level. *(2 marks)*

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5 An inherent advantage of using audit software as it reduces [ ] risk. *(2 marks)*

6 Auditors are required to attend the year-end inventory count where inventory is material to the financial statements to [ ] management's instructions and procedures for the count. *(2 marks)*

7 The audit senior has calculated average trade receivable days and compared this with the prior year. This substantive analytical procedure addresses the [ ] assertion of trade receivables. *(2 marks)*

8 If the auditor concludes that uncorrected misstatements, [ ], this must be brought to the attention of management and/or those charged with governance as soon as possible. *(2 marks)*

- -Please Select-
- either individually or in aggregate, are material
- either individually or in aggregate, are not material
- both individually and in aggregate, are material
- both individually and in aggregate, are not material

9 Identify which of the following is/ are the auditor's responsibility relating to fraud. *(2 marks)*

- A. The auditor is required to detect all fraud during an assurance engagement.
- B. The auditor shall maintain professional skepticism throughout the audit and recognise the possibility that a material misstatement due to fraud could exist.
- C. When fraud is identified, a qualified audit opinion is a must for such assurance engagement unless the client provides adequate undertaking to protect the auditor.
- D. Both B and C are true.

10 Identify which of the following is true regarding internal auditors. *(2 marks)*

- A. Internal auditors report to the board of directors, or other people charged with governance.
- B. Internal auditors must be qualified members of the Hong Kong Institute of Certified Public Accountants.
- C. Internal auditors are employed by all business entities.
- D. Internal auditors generally report to the accounting department.

11 Identify which of the following assertions is NOT relevant in respect of sending confirmations to trade receivables. *(2 marks)*

- A. Existence.
- B. Completeness.
- C. Valuation.
- D. Rights and obligations

12 Identify which of the following condition(s) has/ have to be met such that a stratified sampling approach is most effective for auditing trade receivables. *(2 marks)*

- A. Stratifies the trade receivables population into discrete sub-populations by dividing them according to the outstanding balance.
- B. The variability between strata is maximised.
- C. The variability of items within each stratum is minimised.
- D. All of the above.

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13 The audit senior has obtained a valuation of a significant investment which has been carried out by a professional valuer. Identify which of the following audit procedures should be carried out by the audit senior. *(2 marks)*

- A. None, as the valuation has been carried out by a professional valuer.
- B. Assess the independence and objectivity of the professional valuer.
- C. Discuss with management why they have used a professional valuer.
- D. Refer to the professional valuer in the auditor's report.

14 Identify which of the following is NOT explicitly stated in the auditor's report with a standard unmodified audit opinion. *(2 marks)*

- A. The financial statements are the responsibility of the management.
- B. The audit was conducted in accordance with the Hong Kong Standards on Auditing.
- C. The audit includes the evaluation of the effectiveness of the company's internal controls.
- D. The audit includes the evaluation of the reasonableness of accounting estimates and related disclosures.

15 Determine which of the following audit procedures is appropriate to test the completeness assertion for trade receivables. *(2 marks)*

- A. Select samples from the trade receivables ledger and examine the goods delivery notes and invoices.
- B. Understand, ascertain and evaluate the effectiveness of the internal controls over credit policy and control.
- C. Trace a sample of goods delivery notes to the sales journal and into the sales ledger and trade receivables ledger.
- D. None of the above.

16 For sales of specialty products, determine which of the following balance-related audit objectives is affected by the occurrence of a transaction-related audit objective. *(2 marks)*

- A. Existence.
- B. Completeness.
- C. Rights and obligations.
- D. Accuracy.

17 After Christmas 2024, the Hong Kong Department of Health announced that it was investigating 25 clusters of suspected food poisoning related to Company A's products purchased by customers in one of its cake shops. The management of Company A informed the auditor that they have discussed with the company's lawyer and considered that there is no need to make any provision for such claims and to account for it in its financial statements for the year ended 31 December 2024. Identify which of the following is considered as the most appropriate audit procedure for substantiating the amount of litigation claims that may exist. *(2 marks)*

- A. Obtain a management representation letter from the management.
- B. Review all board minutes for the year 2025.
- C. Review all the correspondence with customers.
- D. Send an enquiry letter to the lawyer of Company A for their opinion regarding the probability of the claim being successful and the estimated amount of possible compensation, if any.

18 You are planning the audit of XYZ Co Ltd for the year ended 31 December 2024. Identify which of the following is an example of a fraud in XYZ Co Ltd. *(2 marks)*

- A. An unintentional overstatement of revenue.
- B. Omitted narratives in the accounting entries.
- C. A harmful act to society.
- D. Intentional wrongful act to manipulate the accounting records.

19 Computer-assisted auditing techniques (CAATs) allow the auditor to perform a variety of audit procedures. Identify which of the following is an example of an audit procedure using CAATs. *(2 marks)*

- A. Tracing disposal proceeds for a non-current asset to the cash book.
- B. Reviewing a non-current asset for indicators of impairment.
- C. Calculating trade receivables days.
- D. Ensuring that a provision for a liability has been adequately disclosed.

20 Identify which of the following would not be a key consideration when evaluating audit evidence at the completion stage. *(2 marks)*

- A. The reliability of the audit evidence obtained.
- B. The timing of the audit testing.
- C. The relevance of the evidence obtained to forming the auditor's opinion.
- D. The accumulation of audit evidence in accordance with Hong Kong Standards on Auditing.

21 Identify in which of the following circumstances a Disclaimer of Opinion would not be appropriate. *(2 marks)*

- A. The auditor was unable to attend the year-end inventory count or apply alternative audit procedures.
- B. The auditor is unable to determine the amounts associated with illegal acts committed by management.
- C. The financial statements fail to contain adequate disclosures in relation to related-party transactions.
- D. Management refuses to permit their lawyer from answering the auditor's legal confirmation process.

22 Identify which of the following actions would be appropriate when the auditors discover a related party which they were previously unaware of. *(2 marks)*

A. Resign from the audit.
B. Report the matter to the Hong Kong Institute of Certified Public Accountants.
C. Inform the rest of the engagement team as soon as possible.
D. Modify the auditor's opinion.

23 State when subsequent events audit procedures should always be carried out. *(2 marks)*

A. From period-end date until the date of the release of the financial statements.
B. From the auditor's report date until the release of the financial statements.
C. From period-end date until the date of the auditor's report.
D. From period-end date and for the following months until the end of the following accounting period.

24 Identify which of the following situation(s) would require auditor's audit work to evaluate potential misstatements. *(2 marks)*

(1) Discovery of the inclusion of a material amount of after year-end sales.
(2) Discovery of the inclusion of a material amount of consignment goods from consignors as inventory at the year-end date.
(3) Discovery of the omitted recognition for loss of inventories caused by a fire occurred right before the year-end date.
(4) Discovery of the management's intent to increase luxury product lines.

A. (1) only.
B. (2) and (3) only.
C. (1) and (4) only.
D. (1), (2) and (3) only.

25 Identify which of the following are assertions about classes of transactions and events. *(2 marks)*

(1) Rights and obligations
(2) Completeness
(3) Accuracy
(4) Existence
(5) Valuation and allocation

A. (1) and (2).
B. (2) and (3).
C. (3) and (4).
D. (4) and (5).

26 The audit junior is carrying out initial planning work on the trade receivables for the year ending 31 December 2024. The audit junior has asked you what factors must be considered when designing the sampling plan to test the existence and valuation of trade receivables. Identify which of the following would be factors the auditor must consider. *(2 marks)*

(1) The nature of the client's industry.
(2) Management's attitude to internal controls.
(3) The purpose of the procedure.
(4) The nature of the audit evidence sought.
(5) The law and regulation applicable to the client's industry.

A. (1) and (2).
B. (2) and (3).
C. (3) and (4).
D. (4) and (5).

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27 Determine which of the following audit procedures is/ are appropriate to test the completeness assertion for trade payables and accruals. *(2 marks)*

(1) Examine files for any unmatched purchase orders and suppliers' invoices for any unrecorded liabilities.
(2) Vouch selected amounts from the trade payables and accruals schedule to the suppliers' invoices.
(3) Compare the current year balance of trade payables and accruals to that of the previous year.

A. (3) only.
B. (1) and (2) only.
C. (1) and (3) only.
D. (2) and (3) only.

28 You are the audit senior designing the audit programmes for the payroll cycle for the year ending 31 December 2024. The audit engagement partner has requested that a combination of substantive procedures and tests of control be carried out. Determine which of the following are tests of control audit procedures over the entity's payroll cycle. *(2 marks)*

(1) Review source data (such as clock cards or time sheets) for evidence of review by a senior official to ensure that employees are only paid for hours worked.
(2) Test the calculation and agree the total payroll expense per the payroll system with the general ledger and the financial statements.
(3) Review payroll reports for evidence that they have been authorised by a responsible official (this verifies adequate segregation of duties).
(4) Confirm that payroll master file data is only able to be changed by the human resources department and not the payroll department by reviewing a log of amendments to payroll master file data.
(5) Recalculate the gross and net pay for a sample of employees and agree with the payroll records.
(6) Perform a proof in total of the payroll expense, incorporating joiners and leavers and the annual pay increase. Compare this expectation with the actual payroll expense per the financial statements and investigate any significant differences.
(7) Review Board minutes for evidence that bonuses and/or annual pay increases have been agreed by the directors.
(8) Observe the payroll process in operation, ensuring that adequate review processes are in place (e.g. a senior member of the finance department authorises the ban transfer to employees and that the payroll is reviewed by a senior official prior to it being finalised).

A. (1), (3), (4) and (8).
B. (1), (3), (4), (7) and (8).
C. (1), (4), (5), (7) and (8).
D. (1), (3), (4), (6) and (8).
E. All of the above.

29 Identify which of the following are substantive analytical procedures. *(2 marks)*

(1) Casting the inventory valuation and agreeing the total with the financial statements.
(2) Obtaining a breakdown of standard cost calculations and agreeing a sample of costs with invoices.
(3) Calculating the gross profit margin, comparing to prior year and investigating any significant differences.
(4) Calculating the inventory holding period, comparing to prior year and investigating any significant differences.
(5) Inspecting inventory for evidence of damage or obsolescence.

A. (1) and (2).
B. (2) and (3).
C. (3) and (4).
D. (4) and (5).

30 When designing substantive analytical procedures, there are four elements which comprise distinct steps in the process. Identify which of the following are the correct elements. *(2 marks)*

(1) Develop an independent expectation.
(2) Define a significant difference or threshold.
(3) Perform recalculation.
(4) Compare the expectation against performance materiality.
(5) Discuss the outcome with the engagement team.

A. (1) and (2).
B. (2) and (3).
C. (3) and (4).
D. (4) and (5).

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31 An audit client has refused to provide certain representations to the auditor. Identify which of the following are not the suggested responses by the auditor under the above circumstance. *(2 marks)*

(1) Immediately resign.
(2) Re-evaluate the integrity of management.
(3) Issue a disclaimer of opinion.
(4) Insist that the client provides the representation.

A. (1) and (2).
B. (3) and (4).
C. (1) and (3).
D. None of the above.

32 During the planning phase of the audit, the auditor will carry out preliminary analytical procedures which include ratio analysis. Identify which of the following ratios are profitability ratios: *(2 marks)*

(1) Current ratio.
(2) Quick ratio.
(3) Gross profit margin.
(4) Net profit margin.
(5) Gearing ratio.

A. (1) and (2).
B. (2) and (3).
C. (3) and (4).
D. (4) and (5).

33 Identify which of the following factor(s) is/ are NOT correct when an auditor is designing a sample. *(2 marks)*

(1) State the objectives of audit procedures and the period covered.
(2) Ensure the population is not one for which the audit engagement partner does not require sampling to be applied.
(3) Determine the projected misstatement.
(4) Consider the possibility of any anomalous error.

A. (1) only.
B. (1), (2) and (3).
C. (2), (3) and (4).
D. All of the above.

34 Identify which of the following organisation structure setup could serve a better corporate governance practices of a Hong Kong listed company. *(2 marks)*

(1) Board of Directors.
(2) Remuneration committee.
(3) Executive committee.
(4) Nomination committee.
(5) Audit committee.
(6) Risk committee.

A. (1), (2), (3) and (4).
B. (2), (3), (4) and (5).
C. (2), (4), (5) and (6).
D. All of the above.

35 A professional accountant shall comply with the fundamental principles of the HKICPA's Code of Ethics for Professional Accountants. Identify three fundamental principles of the HKICPA's *Code of Ethics for Professional Accountants*. *(2 marks)*

A. Independence.
B. Integrity.
C. Conflicts of interest.
D. Professional Competence and Due Care.
E. Confidentiality.
F. Compliance with laws and regulations.
G. Honesty.
H. Professional scepticism.
I. Duty to shareholder.

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36 Identify which of the THREE items below are NOT the basic elements of an unmodified auditor's report of an unlisted Hong Kong company according to HKSA 700 (Revised) *Forming an Opinion and Reporting on Financial Statements.* *(2 marks)*

- [ ] A. Title of the report.
- [ ] B. Addressee.
- [ ] C. Basis for opinion.
- [ ] D. Key audit matters.
- [ ] E. Other information.
- [ ] F. Responsibilities of Directors and Those Charged with Governance for the financial statements.
- [ ] G. Auditor's responsibilities for the audit of the financial statements.
- [ ] H. Director's name and signature.
- [ ] I. Auditee's address.
- [ ] J. Date of the report.

37 Identify three general controls out of the answers. *(2 marks)*

- [ ] A. Adding up the total of a batch of supplier invoices to ensure the total agrees to the value inputted into the system (Batch total checks).
- [ ] B. Preventing and detecting unauthorised access to the IT system.
- [ ] C. Ensuring that changes to the IT system are appropriate, carried out by authorized individuals and are logged and have appropriate access rights.
- [ ] D. Matching master files to transaction records – for example inspecting the number of documents processed to ensure there have been no deletions.
- [ ] E. Ensuring controls are in place to prevent business interruption in case of failure of the IT system.
- [ ] F. Inspecting the output of numerical sequence checks for any exception reports and inquiring as to how these have been resolved (Sequence checks).
- [ ] G. Ensuring that sales invoices are mathematically correct in terms of amounts invoiced and that sales taxes are correctly calculate (Arithmetic checks).

* * * END OF SECTION A * * *

SECTION B –SCENARIO-BASED QUESTIONS (Total: 26 marks)

Answer **ALL** questions in this section. Together they are worth 26% of the total marks for this examination.

For Questions 38, 39 and 40

You are required to complete three questions based on the following scenario.

PHD & Co has been the auditor of a Hong Kong listed company – Good Health Limited ("GHL") for seven years. The partner in charge of this audit has always been Kelvin over this seven year period. Same as the prior years, GHL plans to celebrate the completion of the audit by arranging a party for their staff and the audit team. In order to enhance the atmosphere of the party, a lucky draw is arranged every year and everyone can get a piece of gold of a different weight. The chairman of GHL believes that the money is well spent as such an arrangement can enhance the audit efficiency of each year.

Close to the end of the audit team's field work for the financial year ended 31 December 2024, Kelvin was approached by the chairman of GHL discussing the continuation of the assurance engagement for the next year. The only condition was that the bank loan of GHL could be renewed after the current year's audit with an unmodified auditor's report. The renewal of the bank loan is critical for GHL's continuation of business.

After evaluating all the audit evidence, Kelvin concluded that there was a material uncertainty regarding the renewal of the bank loan of GHL and such material uncertainty has been adequately disclosed in its 2024 financial statements. He also concluded that the management's use of the going concern basis of accounting to prepare GHL's 2024 financial statements is appropriate. The auditor's report was issued on 31 March 2025.

* * * END OF SCENARIO * * *

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38 39 40

Analyse the situation of GHL for PHD & Co and identify which three of the potential threats and the ethical principle that may be breached. *(2 marks)*

- [ ] A. Familiarity threat.
- [ ] B. Self-review threat.
- [ ] C. Advocacy threat.
- [ ] D. Self interest threat.
- [ ] E. Intimidation threat.

38 39 40

Based on the situation outlined in the third paragraph of the case, explain what types of auditor's opinion should be issued by PHD & Co. *(2 marks)*

- ( ) A. Unmodified opinion.
- ( ) B. Qualified opinion.
- ( ) C. Adverse opinion.
- ( ) D. Disclaimer opinion.
- ( ) E. Unmodified opinion with a separate section under the heading "Material Uncertainty Related to Going Concern".

38 39 40

Subsequent to the issuance of auditor's report, GHL reappointed PHD & Co as it's auditor for the financial year ending 31 December 2025. Identify the duration of cooling-off period that Kelvin has to be followed? *(2 marks)*

- ( ) A. 2 consecutive years.
- ( ) B. 4 consecutive years.
- ( ) C. 5 consecutive years.
- ( ) D. 7 consecutive years.
- ( ) E. Cooling off is not required.

For Questions 41, 42, 43, 44 and 45

You are required to complete five questions based on the following scenario.

AEC Limited is a retail company with more than 20 physical stores in Hong Kong, which sold books, VCDs, DVDs, Blue-rays, and CDs in the past. The company has gone through a significant transformation last year and has become an e-commerce trading company. It closed majority of its physical shops and is now an internet-based retailer selling books, VCDs, DVDs, Blue-rays, CDs, video downloads/ streaming, MP3 downloads/ streaming, audiobook downloads/ streaming, software, video games, electronics, apparel, furniture, food, toys and jewellery.

AEC Limited has separate retail websites for different countries and it offers international shipping to those countries for most of its products. All the goods are priced and transactions are settled in the customers' local currencies. Inventory counts take place at the end of the year for all the stores and for the warehouse by the teams of warehouse staff. However, subject to the availability of staff, inventory counts are conducted within one week before or after the year end date.

PF & Co has been the auditor of AEC Limited for five years. In the past years' audits, the audit team noticed that many VCDs were slow-moving items. However, the management explained that those VCDs could be sold more quickly after the online selling platform is ready.

During the current year's audit, the following issues are identified:

- The inventory count was conducted two weeks after the year end date as the management explained that a material number of inventories originally kept in the physical stores were in transit back to the warehouse.
- After the online store has been set up, it is found that those VCDs are still slow moving and even no movement for many of the items.

From AEC Limited's draft financial statements for the current year's audit, the amount of total assets of the company at the end of the year is HK$120 million, net amount of current assets is HK$5 million and the profit for the year is HK$1.2 million.

* * * END OF SCENARIO * * *

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41 42 43 44 45

List three main category of business risks: *(2 marks)*

- [ ] A. Operational risks.
- [ ] B. Concentration risks.
- [ ] C. Financial risks.
- [ ] D. Compliance risks.
- [ ] E. Geographic risks.

41 42 43 44 45

Evaluate any information technology risks faced by AEC Limited in the new business model by the expansion of the company's e-commerce trading business. *(2 marks)*

- [ ] A. The loss of adequate audit trails in either paper or electronic form regarding the e-commerce retailing trading transactions.
- [ ] B. The e-commerce security risks such as virus attack or fraud by customers, employees and others through unauthorised access to the e-commerce trading system of the company.
- [ ] C. Non-compliance with the laws and regulations of other countries due to the absence of knowledge.
- [ ] D. Non-compliance with the tax rules of other countries due to the absence of knowledge.
- [ ] E. Risks of systems and infrastructure failures due to poor system development and implementation as well as hacking.
- [ ] F. Foreign currency risks as the purchase of goods and sales of goods are denominated in different currencies.
- [ ] G. International shipping risks.
- [ ] H. Risks associated with the e-payment system.

41 42 43 44 45

Determine three internal controls (including General IT Controls) that could mitigate the information technology risks in AEC Limited's e-commerce trading system. *(2 marks)*

- [ ] A. Controls over the development and implementation of systems used to support the e-commerce retailing trading transactions and the keeping of business records for financial reporting and other purposes.
- [ ] B. Using unencrypted websites and electronic shopping carts.
- [ ] C. Store sensitive consumer information in the online system.
- [ ] D. Grant employees' access to all information.
- [ ] E. Using fire walls and virus protection software to protect the e-commerce trading system of the company.
- [ ] F. Maintaining foreign currency hedging procedures to address the foreign currency risks from the expansion of the business.
- [ ] G. Updating knowledge on the new technologies that give rise to the risk exposed to the internet security and keeping up to date the effective use of technology for the protection of the e-commerce trading system.
- [ ] H. Maintaining a compliance department to ensure compliance with tax rules, law and regulations.

41 42 43 44 45

Determine which of the followings are NOT the appropriate audit procedures to address the valuation assertion regarding the slow-moving VCDs of AEC Limited. *(2 marks)*

- [ ] A. Reconcile the inventory movement between the inventory count date and year end date.
- [ ] B. Check whether there are any sales of the VCD items subsequent to the year end date.
- [ ] C. Obtain understanding of the inventory impairment policy of the company.
- [ ] D. Ascertain the inventory balance at the beginning of the financial year.
- [ ] E. Conduct substantive audit procedures to ascertain the existence of sales transactions during the year.
- [ ] F. For inventory items with movement during the year and after the year end date, check whether the selling price is lower than the cost.
- [ ] G. Check the reasonableness of the impairment of inventory estimated by the management for the current year.
- [ ] H. For inventory items without movement during the year and after the year end date, discuss with the management and request evidence of the realisable value.

41 42 43 44 45

Based on the audit evidence obtained, the audit team concluded that the value of VCDs at year end should be written down by HK$300,000. An audit adjustment on inventory balance is proposed by PF & Co but the management insisted to keep the current book value as they considered AEC Limited has a broad market and selling platforms.

Assume the audit team did not satisfy with the explanation and no additional evidence could be provided by AEC Limited to support the value of VCDs, determine what type of auditor's opinion would be expressed by PF & Co. *(2 marks)*

- A. Unmodified opinion.
- B. Qualified opinion.
- C. Adverse opinion.
- D. Disclaimer opinion.
- E. Unmodified opinion with a separate section under the heading "Material Uncertainty Related to Going Concern".

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For Questions 46, 47 and 48

You are required to complete three questions based on the following scenario.

You are the audit senior of Dan & Co. Certified Public Accountants auditing an existing client, Stan Ltd. A customer is suing Stan Ltd for HK$2 million for damage to property and breach of contract. The court case took place after the financial year-end date and management believe they have a 35% chance of success. The finance director of Stan Ltd has informed you that he intends to include a provision for a liability of HK$2 million and they are suing their contractor for the damage because it was his company that caused the damage. The finance director said that the financial statements will also recognise a receivable of HK$2 million in respect of the claim against their contractor. Based on the audit evidence obtained, an unmodified audit opinion is expected to be expressed.

* * * END OF SCENARIO * * *

46 47 48

Determine which of the following are NOT the substantive procedures which Dan & Co. could be performed to obtain sufficient and appropriate audit evidence in respect of the litigation claim from Stand Ltd's customer. *(2 marks)*

- [ ] A. Review correspondence from the customer to assess whether a present obligation as a result of a past event has taken place and also with the contractor to assess whether they accept liability for the damage caused.
- [ ] B. Inquire of the company's lawyers to obtain their view as to the probability of the claim from customer and the likely amounts involved.
- [ ] C. Review Board minutes to understand whether the directors believe that the claim from customer will be successful or not.
- [ ] D. Review the post-year-end cash book to assess whether cash has been received from the supplier.
- [ ] E. Discuss with management why they believe a reimbursement receivable is appropriate as this is likely to be a contingent asset and should only be recognised if the receipt of cash is virtually certain. If probable, the amount should be disclosed as a contingent asset.
- [ ] F. Obtain a written representation confirming management's view that the claim from customer is likely to be successful and therefore a provision for a liability is to be included.
- [ ] G. Ensure that the reimbursement receivable is properly accounted in the statement of financial position.
- [ ] H. Review the adequacy of the disclosures in the financial statements and ensure the disclosure comply with Hong Kong Accounting Standard 37 Provisions, Contingent Liabilities and Contingent Assets.

46 47 48

If Dan & Co. concluded that the provision for a liability did not fulfill the recognition criteria (i.e. it is not probable to have an outflow of economic benefit to satisfy the obligation; and the obligation cannot be reliably measured). Stan Ltd. agreed to reverse the provision in its financial statement and disclose the legal case as a contingent liability. Identify which of the following is the potential implications for the auditor's opinion. *(2 marks)*

- ( ) A. No change to the auditor's opinion.
- ( ) B. Express a qualified 'except for' opinion.
- ( ) C. Express an adverse opinion.
- ( ) D. Expressed a disclaimer opinion.

46 47 48

If the chance of claiming the damage from the contractor found to be remote (i.e. less than 5% of success chance as estimated by the auditor's external lawyer) but Stan Ltd. insisted to keep the receivable in its financial statement. Identify which of the following is the potential implications for the auditor's opinion. *(2 marks)*

- ( ) A. No change to the auditor's opinion.
- ( ) B. No change to the auditor's opinion if Dan & Co. agreed to disclose the fact.
- ( ) C. Express a qualified 'except for' opinion if the misstatement found to be material but not pervasive.
- ( ) D. Express an adverse opinion.

For Questions 49 and 50

You are required to complete two questions based on the following scenario.

You are the audit senior of Malick Limited whose year-end is 31 December 2024. The company has a number of related parties who are either fellow subsidiaries or companies under common control. The audit junior has noted that the audit engagement partner has confirmed that there is a higher risk of material misstatement where related-party transactions are concerned and is unsure what she means by this comment. In addition, the audit engagement partner has also requested that audit procedures be developed at the risk assessment stage which address the specific requirements of Hong Kong Standards on Auditing 550 *Related Parties*, keeping in mind the high-risk nature of related parties.

* * * END OF SCENARIO * * *

49 50

Identify which of the following is NOT the reason to support a higher risk of material misstatement in respect of transactions with related parties. *(2 marks)*

- A. Related parties may operate through an extensive and complex range of relationships and structures, with a corresponding increase in the complexity of related-party transactions.
- B. The transaction volume of related-party transactions is normally large.
- C. Information systems may be ineffective at identifying or summarising transactions and outstanding balances between an entity and its related parties.
- D. Related-party transactions may not be conducted under normal market terms and conditions.

49 50

Determine which of the audit procedures the auditor should carry out at the risk assessment stage of the audit in respect of related parties. *(2 marks)*

(1) Verify the list of related parties provided by management.
(2) Discuss among the engagement team the susceptibility of the financial statements to material misstatement due to related parties or transactions with them.
(3) Inquire of management as to the identity of related parties, including any changes from the previous year.
(4) Conduct company search to related parties to ascertain the adequacy of information provided by management.
(5) Apply professional scepticism at all times throughout the course of the audit, recognising the possibility that there may be related parties or related-party transactions which the auditors may not be aware of.
(6) Review the related-party transactions disclosed in the company's financial statement.
(7) Obtain the written representation from management to confirm the related parties' relationship.

- A. (1), (2), (3) and (5).
- B. (1), (2), (3) and (6).
- C. (2), (3) and (5).
- D. (2), (3), (4), (5) and (7).
- E. All of the above.

* * * END OF EXAMINATION PAPER * * *

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Associate Module 8 Principles of Auditing Pilot Paper

Answers

The purpose of the suggested answers is meant to help candidates in their revision and learning.

Questions	Answers	Marks Allocation
1a	False	2
1b	True	
2a	True	2
2b	False	
3a	False	2
3b	False	
4	detect	2
5	detection	2
6	observe	2
7	valuation	2
8	either individually or in aggregate, are material	2
9	B	2
10	A	2
11	C	2
12	D	2
13	B	2
14	C	2
15	C	2
16	A	2
17	D	2
18	D	2
19	C	2
20	B	2
21	C	2
22	C	2
23	C	2
24	D	2
25	B	2
26	C	2
27	C	2
28	B	2
29	C	2
30	A	2
31	C	2

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Questions	Answers	Marks Allocation
32	C	2
33	C	2
34	C	2
35	B, D, E	2
36	D, H, I	2
37	B, C, E	2
38	A, D, E	2
39	E	2
40	C	2
41	A, C, D	2
42	B, E, H	2
43	A, E, G	2
44	A, D, E	2
45	B	2
46	D, E, G	2
47	A	2
48	C	2
49	B	2
50	C	2

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