

BINDURA UNIVERSITY OF SCIENCE EDUCATION

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTANCY

EXAMINATION PAPER

NOV 2024

PROGRAMMES:

BACHELOR OF ACCOUNTANCY HONOURS DEGREE

BACHELOR OF BUSINESS ADMINISTRATION HONOURS DEGREE IN POLICE & SECURITY STUDIES

BACHELOR OF COMMERCE HONOURS DEGREE IN FINANCIAL INTELLIGENCE

AUDITING PRINCIPLES & PROCEDURES I (AC 205)

DURATION: HOURS 3 HOURS

(100 MARKS)

INSTRUCTIONS TO CANDIDATES

1. Answer all questions in Section A and Section B.
 2. All questions in Section A carry 2 marks each and marks for questions in Section B are given in brackets at the end of each question.
 3. Start each question on a new page.
 4. No cell phones are allowed in the examination room.
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SECTION A (30 MARKS)

The following scenario relates to questions 1 – 4

You are an audit senior of YHT & Co and have worked on the external audit of BJM Co (BJM), an unlisted company, since your firm was appointed external auditor two years ago. BJM owns a chain of nine restaurants and is a successful company. BJM has always been subject to national hygiene regulations, especially in relation to the food preparation process. Non-compliance can result in a large fine or closure of the restaurant concerned. Despite running a successful company, BJM's Board have often needed to be reminded of some fundamental principles and you often have to explain key concepts.

QUESTION 1

Which of the following statements best defines the external audit?

- A. The external audit is an exercise carried out by auditors in order to give an opinion on whether the financial statements of a company are fairly presented.
- B. The external audit is an exercise carried out in order to give an opinion on the effectiveness of a company's internal control system.
- C. The external audit is performed by management to identify areas of deficiency within a company and to make recommendations to mitigate those deficiencies.
- D. The external audit provides negative assurance on the truth and fairness of a company's financial

QUESTION 2

The Board has also struggled to differentiate between their responsibilities and those of the external auditor in circumstances such as the prevention and detection of fraud and error, and compliance with regulations.

Which of the following statements best describes YHT & Co's responsibility regarding BJM's compliance with hygiene regulations, in line with ISA 250 Consideration of laws and regulations in an audit of financial statements?

- A. YHT & Co should actively prevent and detect non-compliance with the regulations.
- B. YHT & Co should perform specific audit procedures to identify possible non-compliance.
- C. YHT & Co should obtain sufficient appropriate audit evidence about BJM's compliance with the regulations as they have a direct effect on the financial statements.
- D. YHT & Co does not have any responsibility as the hygiene regulations do not have a direct effect on the financial statements.

QUESTION 3

The Board of BJM have recently notified you that the national hygiene regulations have been updated and are now much more stringent and onerous than before. With this in mind, the Board have asked your firm to conduct a review of BJM's compliance with hygiene regulations, in order to allow the Board to assess whether the appropriate processes have been implemented at each of the nine restaurants. The review is not expected to include the provision of accounting advice or the preparation of figures in the financial statements.

This work is likely to be very lucrative. Your firm has sufficient experience to undertake the above review engagement. The partner responsible for this review has informed you that the engagement is an assurance engagement.

Which of the following would NOT have been relevant to the partner in forming this opinion?

- A. The existence of a three-party relationship
- B. The existence of suitable criteria
- C. The determination of materiality
- D. The subject matter

QUESTION 4

The audit partner has told you that the independence threats arising from YHT & Co performing the review engagement should be monitored carefully.

Which of the following is likely to cause the audit partner most concern?

- A. According to the Code of Ethics, YHT & Co is prohibited from providing other assurance services to an audit client.
- B. The review engagement is likely to give rise to a self-review threat, as the outcomes of the review could form the basis of the financial statements which the audit team will audit.
- C. The lucrative nature of the review engagement may make the external audit team less inclined to require management to make adjustments or to issue a modified audit opinion, for fear of losing the review engagement.
- D. If the new review engagement causes YHT & Co's fee income from BJM to exceed 15% of the firm's total fees, the Code of Ethics states that the new engagement must be turned down.

The following scenario relates to questions 5 - 7.

You are an audit manager of Ali & Co and have just been assigned the audit of Stark Co (Stark). Stark, a listed company, provides investment advice to individuals, and is regulated by the relevant financial conduct authority. Mr Day, a partner in Ali & Co, has been the audit engagement partner for Stark for the previous nine years and has excellent knowledge of the client. Mr Day has informed you that he would like his daughter Zoe to be part of the audit team this year; Zoe is currently studying for her first set of fundamentals papers for her qualification.

In an initial meeting with the finance director of Stark, you learn that the audit team will not be entertained on Stark's yacht this year, instead, he has arranged a balloon flight costing less than one-tenth of the expense of using the yacht and hopes this will be acceptable. Ali & Co has always carried out tax advisory work for Stark.

The tax advisory services do not have an impact on the figures reported in the financial statements. The finance director has stated that he feels strongly that the firm that offers taxation services this year should charge a fee which is based on a percentage of tax saved. He also trusts that your firm will accept a fixed fee for representing Stark in a dispute regarding the amount of sales tax payable to taxation authorities.

QUESTION 5

In relation to the audit team being offered a balloon ride:

Which of the following actions should be taken to ensure the firm complies with ACCA's Code of Ethics and Conduct?

- A. The gift may be accepted as Stark has taken appropriate measures to reduce the value of the gift compared to previous years.
- B. The value of the gift should be assessed to determine whether it is of material value to the financial statements.
- C. The gift should only be accepted if its value is trivial and inconsequential to the recipients.
- D. Only the audit partner and audit manager should accept the gift.

QUESTION 6

In relation to the audit engagement partner holding the role for nine years:

Which of the following safeguards should be implemented in order to comply with ACCA's Code of Ethics and Conduct?

- A. An independent review partner should be appointed to the audit.
- B. The audit engagement partner should be removed from the audit team but may serve as a quality control reviewer.
- C. Ali & Co should not audit Stark for a two year period.
- D. The audit engagement partner should be removed from the audit team.

QUESTION 7

Zoe is also concerned that Ali & Co might breach confidentiality were the audit firm to represent Stark in its dispute with the tax authorities.

Which of the following statements best reflects the auditor's duty of confidentiality?

- A. Auditors must never, under any circumstances, disclose any matters of which they become aware during the course of the audit to third parties, without the permission of the client.
- B. Auditors may disclose any matters in relation to criminal activities to the police or taxation authorities, if requested to do so by the police or a tax inspector.
- C. Auditors may disclose matters to third parties without their client's consent if it is in the public interest, and they must do so if there is a statutory duty to do so.
- D. Auditors may only disclose matters to third parties without their client's consent if the public interest or national security is involved.

QUESTION 8

The following scenario relates to questions 8 to 11.

You are an audit senior of IBN & Co and you are planning the audit of Mason Air Services (Mason) for the year ended 31 December 20X3. Mason is a company that provides specialist helicopter support to the police force, the ambulance service, the fire service and the coastguard. Each of Mason's four contracts is equal in value. Mason owns and maintains the helicopter fleet which is held at cost. Each aircraft carries specialist equipment and is operated by a highly skilled specialist pilot

Based on the above information, which of the following statements summarises a key audit risk?

- A. Mason's assets could be undervalued if the market value of the helicopter fleet exceeds its cost
- B. Mason could breach the terms of its contracts with its customers and be liable to pay penalties, so provisions may be understated
- C. Revenue may be overstated if it is recognised according to the contract date rather than over the relevant accounting period
- D. An expert valuer is required to value the helicopters in the financial statement

QUESTION 9

Mason has not purchased any new helicopters during the year to 31 December 2021; however there has been a lot of re-fitting, replacement and adding of specialist equipment to some of the existing aircraft. This has been necessary to keep up with the latest developments in search and rescue, and to maintain the aircraft to the high standard required under the contracts in place. This information has led you to be concerned that property, plant and equipment may be overstated in the financial statements.

Which of the following statements represents a valid response to this audit risk?

- A. Perform a proof in total calculation of the depreciation charge for the year and investigate any significant differences
- B. Review minutes of training meetings to determine whether the pilots have been trained how to use the specialist equipment
- C. Obtain a breakdown of the capitalised costs and agree a sample of items to invoices to determine the nature of the expenditure
- D. Discuss with directors how the acquisition of specialist equipment has been financed

QUESTION 10

From reading the prior year audit file you have just realised that Mason funded the original purchase of each aircraft with a secured loan carrying substantial interest charges. The loan is in the process of being renegotiated and the bank have indicated that finance costs will increase further. Furthermore, the directors have told you that Mason's contract with the police force expires in March 2021, at a time when the police are trying to substantially reduce the amount they pay in the wake of government cuts. It is thought that the contract will be put out to tender, and it is possible that another aircraft provider may also bid for the contract.

From the above information, which is the most important audit risk that should be documented in the detailed audit plan?

- A. Disclosure relating to the secured loan may be omitted from the financial statements
- B. Mason's going concern status may be at risk if the contract is not renewed

- C. That interest charges may be understated
- D. That the bank will rely on the audited financial statements when deciding whether to renew the loan

QUESTION 11

Mason also holds around \$2 million of aircraft spares which are included within inventory. Mason sells the aircraft spares to amateur flying associations. Aircraft spares which are not sold after three years are scrapped. Approximately a quarter of this value is made up of specialist equipment taken out of aircraft when it was replaced by newer or more advanced equipment. Such specialist equipment is transferred from non-current assets to inventory without adjustment, and continue to be recognised at amortised cost.

Which of the following summarises the key audit concern arising from the matter described?

- A. Accuracy, valuation and allocation of non-current assets
- B. Completeness of non-current assets
- C. Existence of inventory
- D. Accuracy, valuation and allocation of inventory

The following scenario relates to questions 12– 15.

You are an audit manager in the internal audit department of KLE Co, a listed retail company. The internal audit department is auditing the company's procurement system. KLE's ordering department consists of six members of staff: one chief buyer and five purchasing clerks.

QUESTION 12

All orders are raised on pre-numbered purchase requisition forms, and are sent to the ordering department. In the ordering department, each requisition form is approved and signed by the chief buyer. A purchasing clerk transfers the order information onto an order form and identifies the appropriate supplier for the goods. Part one of the two part order form is sent to the supplier and part two to the accounts department. The requisition is thrown away.

Which of the following is NOT a likely effect of the deficiencies in the internal control system described?

- A. Purchases may be made unnecessarily at unauthorised prices
- B. Subsequent queries on orders cannot be traced back to the original requisition
- C. The order forms may contain errors that are not identified
- D. Goods could be ordered twice in error or deliberately

QUESTION 13

When goods are received, the goods inwards department immediately raises a two-part pre-numbered Goods Received Note (GRN).

- Part one is sent to the ordering department, which then forwards the GRN to the accounts department
- Part two is filed in order of the reference number for the goods being ordered (obtained from the supplier's goods despatched documentation), in the goods inwards department.

Which of the following statements are valid recommendations with regards to improving the internal controls described?

- (1) The ordering department should match orders to GRNs and mark orders as closed once all goods have been received, to enable any outstanding orders to be chased up.
- (2) The first copy of the GRN should be sent directly to the accounts department, without first going through the ordering department, to prevent delays in recording the purchase.
- (3) The goods inwards department should review the goods for their condition, in order to identify and return any damaged goods.
- (4) GRNs should be filed in date order or by purchase order number, instead of by the supplier's reference number, to ensure that they can be matched easily to orders.

- A. 1 and 3
- B. 1, 2 and 3
- C. 1, 2 and 4
- D. 1, 3 and 4

QUESTION 14

As part of your audit of the procurement system, you have recommended that the goods inwards department should ensure that the goods received are valid business purchases, by matching all deliveries to an authorised order form before issuing a GRN.

Which of the following would be an appropriate test of control to confirm that the control is operating effectively?

- A. For a sample of orders, check that there is a matching goods received note
- B. Check that the numerical sequence of purchase orders is complete
- C. For a sample of goods received notes check that there is an authorised purchase order
- D. Check that the numerical sequence of goods received notes is complete

QUESTION 15

KLE Co's management is keen to increase the range of assignments that the company's internal audit undertake.

Which of the following assignments could the internal audit department be asked to perform by management?

- A. Undertake 'mystery shopper' reviews, where they enter the store as a customer, purchase goods and rate the overall shopping experience
- B. Assist the external auditors by requesting bank confirmation letters
- C. Provide advice on the implementation of a new payroll package for the payroll department
- D. Review the company's financial statements on behalf of the board.

SECTION B (70 MARKS)

QUESTION 1

You are the audit senior in charge of the audit of Advanced Office Equipment Suppliers plc (AOES) and are conducting the audit for the year ended 30 June 2018. AOES's provision for impaired receivables (doubtful debts) is calculated as a standard percentage based on historical collection experience. Specific provisions for impaired receivables have already been dealt with in a separate section of the file. Management uses the same process for estimating the provision for impaired receivables as in previous years. As part of its risk assessment procedures, the engagement team identified the following risk of material misstatement related to the valuation assertion: • The entity may not appropriately update its provision for impaired receivables for changes in circumstances.

The engagement team obtained the following evidence from the audit procedures performed to address this risk:

1. Although year-end receivables are higher than previously, the current year provision as a percentage of gross receivables is consistent with prior years.
2. The charge to the income statement in respect of specific impaired receivables written off remained consistent as a percentage of gross revenue over the past several years.
3. A retrospective review of receivable collections indicates that management's provisions have historically been accurate.
4. Economic conditions have been relatively stable and are predicted to remain so.
5. Revenues increased substantially year over year as a result of the introduction of a new product line.
6. The new product line is marketed towards customers in the education sector, especially private colleges and tuition providers, with which the entity does not currently have an established customer base.
7. The private college/tuition sector generally has a higher rate of business failure

than other customer segments.

8. The entity's collections experience has primarily been with customers in the legal services and accountancy sectors; the entity has very little collections experience with the new product line, given the recent launch.
9. Approved sales terms have not changed year to year (e.g. sales personnel may offer an extension of credit of up to 100 percent of the purchase price consistent with prior year, creditworthiness is determined in the same manner, and payment terms are consistent with prior year).
10. A greater percentage of sales is made on credit in the education/tuition market than in the traditional accountancy/legal market.
11. Competitors who supply similar office equipment products have higher provisions as a percentage of their trade receivables. [Note that the engagement team may have identified additional risks of material misstatement related to the valuation assertion as part of its risk assessment procedures; however, in this example you are required to consider this specific risk of material misstatement only. There is no evidence of any fraudulent behaviour in this case].

Requirements:

(a) For the case above:

- (i) Comment on the problem caused by contradictory evidence on an assurance assignment, and evaluate the corroborative and contradictory audit evidence in the scenario.

(9 marks)

(ii) On the basis of the case facts, determine whether the valuation of receivables is supportable, and recommend what additional information, if any, is needed to reach a conclusion. (9 marks)

(b) Critique the well-known method of obtaining audit evidence known as 'the trade receivables confirmation or circularisation'.

(7 marks)

[Total: 25 Marks]

QUESTION 2

(a)

Auditors are required to document a company's accounting and internal control systems as part of their audit process. Two methods available for documenting internal control systems are narrative notes and questionnaires.

Required:

For each of the two methods, narrative notes and questionnaires:

(i) Describe the method for documenting internal control systems; and (2 marks)

(ii) Explain advantages of using these methods. (2 marks)

(b)

Freesia Co is a company listed on a stock exchange. It manufactures furniture which it supplies to a wide range of retailers across the region. The company has an internal audit (IA) department and the company's year end is 30 June 20X9. You are an audit supervisor with Zinnia & Co, preparing the draft audit programmes and reviewing extracts from the internal controls documentation in preparation for the interim audit. Sales Freesia Co generates revenue through visits by its sales staff to customers'

premises. Sales ledger clerks, who work at head office, carry out credit checks on new customers prior to being accepted and then set their credit limits.

Sales staff visit retail customers' sites personally and orders are completed using a four-part pre-printed order form. One copy is left with the customer, a second copy is returned to the sales ordering department, the third is sent to the warehouse and the fourth to the finance department at head office. Each sales order number is based on the sales person's own identification number in order to facilitate monitoring of sales staff performance. Retail customers are given payment terms of 30 days and most customers choose to pay their invoices by bank transfer.

Each day Lily Shah, a finance clerk, posts the bank transfer receipts from the bank statements to the cash book and updates the sales ledger. On a monthly basis, she performs the bank reconciliation. Purchases and inventory Receipts of raw materials and goods from suppliers are processed by the warehouse team at head office, who agree the delivery to the purchase order, check the quantity and quality of goods and complete a sequentially numbered goods received note (GRN). The GRNs are sent to the finance department daily. On receipt of the purchase invoice from the supplier, Camilla Brown, the purchase ledger clerk, matches it to the GRN and order and the three documents are sent for authorisation by the appropriate individual. Once authorised, the purchase invoices are logged into the purchase ledger by Camilla, who utilises document count controls to ensure the correct number of invoices has been input.

The company values its inventory using standard costs, both for internal management reporting and for inclusion in the year-end financial statements. The basis of the standard costs was reviewed approximately 18 months ago. Payroll Freesia Co employs a mixture of factory staff, who work a standard shift of eight hours a day, and administration and sales staff who are salaried. All staff are paid monthly by bank transfer. Occasionally, overtime is required of factory staff. Where this occurs, details of overtime worked per employee is collated and submitted to the payroll department by a production clerk. The payroll department pays this overtime in the month it occurs. At the end of each quarter, the company's payroll department sends overtime reports

which detail the amount of overtime worked to the production director for their review. Freesia Co's payroll package produces a list of payments per employee which links into the bank system to produce a list of automatic bank transfer payments.

The finance director reviews the total to be paid on the list of automatic payments and compares this to the total payroll amount to be paid for the month per the payroll records. If any issues arise, then the automatic bank transfer can be manually changed by the finance director.

Required:

(b) In respect of the internal controls of Freesia Co:

(i) Identify and explain SIX deficiencies; (ii) Recommend a control to address each of these deficiencies. (9 marks)

(iii) 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. Note: Prepare your answer using three columns headed Control deficiency, Control recommendation and Test of control respectively.

The total marks will be split equally between each part.

(9 marks)

Freesia Co deducts employment taxes from its employees' wages and salaries on a monthly basis and pays these to the local taxation authorities in the following month. At the year end, the financial statements will contain an accrual for employment tax payable.

Required:

(c) Describe the substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in respect of Freesia Co's year-end accrual for employment tax payable (4 marks)

(d)

The listing rules of the stock exchange require compliance with corporate governance principles and the directors of Freesia Co are confident that they are following best practice in relation to this. However, the chairman recently received correspondence from a shareholder, who is concerned that the company is not fully compliant. The company's finance director has therefore requested a review of the company's compliance with corporate governance principles. Freesia Co has been listed for over eight years and its board comprises four executive and four independent non-executive directors (NEDs), excluding the chairman. An audit committee comprised of the NEDs and the finance director meets each quarter to review the company's internal controls.

The directors' remuneration is set by the finance director. NEDs are paid a fixed fee for their services and executive directors are paid an annual salary as well as a significant annual bonus based on Freesia Co's profits. The company's chairman does not have an executive role and so she has sole responsibility for liaising with the shareholders and answering any of their questions.

Required:

- (d) Describe TWO corporate governance weaknesses faced by Freesia Co and provide a recommendation to address each weakness to ensure compliance with corporate governance principles.

(4 marks)

(Total 30 marks)

QUESTION 3

Briefly explain the following five threats that could endanger an auditor's independence.

- Self-interest threat
- Intimidation threat

(3 marks)

(3 marks)

- Familiarity threat.
- Self-review threat.
- Advocacy threat.

(3 marks)

(3 marks)

(3 marks)

[Total 15 marks]

END OF QUESTION PAPER