

BINDURA UNIVERSITY OF SCIENCE EDUCATION

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTANCY

EXAMINATION PAPER

15 OCT 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 II (AC 206)

**DURATION: 3 HOURS
MARKS)**

(100

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 (30 MRKS)

1. Due to storm damage Morrison Ltd lost all its accounting records for the current year and back-ups are not available. Which audit opinion is most likely to be issued?
 - A. Unmodified
 - B. Qualified (except for)
 - C. Adverse
 - D. Disclaimer.
2. Which of the following is correct in respect of 'going concern'?
 - A. Financial statements must be prepared on the 'going concern' basis for all companies.
 - B. If there are material uncertainties regarding 'going concern', the financial statements must be prepared on the break up basis.
 - C. Going concern means the company is no longer profitable.
 - D. The directors of the company must disclose material uncertainties regarding going concern in the notes to the financial statements.
3. Which of the following audit procedures provides evidence of valuation and existence of receivables at the year end?
 - A. External confirmation from the customer of the amount outstanding.
 - B. Recalculation of the receivables listing.
 - C. Enquiry with management regarding the adequacy of an allowance for receivables.
 - D. Inspection of post year end bank statements to identify payments by customers of balances outstanding at the year-end.
4. As provided for in terms of IAS10- Events after the reporting date and ISA560- Subsequent events, which of the following is not an adjusting event?
 - A. Amounts received or receivable in respect of insurance claims which were under negotiations at the reporting date.
 - B. Decline in market value of investments between the end of the reporting period and the date when the financial statements are authorised for issue

- C. Valuation of a property which provides evidence of permanent diminution in value
 - D. Discovery of errors or frauds which show the financial statements were incorrect
5. From the following, how does an audit firm achieve quality control for individual audits?
- A. Ensuring all audit work is fully reviewed
 - B. Ensure that all partners and staff are aware of and adhere to the principles of independence, objectivity, integrity and confidentiality
 - C. Developing procedures for evaluating prospective clients with consideration of the firm's ability to meet the client's needs and for making the decision on acceptance which may be made by an individual partner, or by a committee
 - D. none of the above
6. Which one of the following sampling methods is not considered in ISA530 Audit sampling?
- A. Block selection
 - B. Systematic selection
 - C. Convenience selection
 - D. Random selection
7. ISA 570 Going concern requires the auditor to evaluate management's assessment of their enterprise's going concern status. Which one of the following is a financial indicator of going concern challenges?
- A. Indications of withdrawal of financial support by lenders
 - B. Arrears or discontinuance of dividends
 - C. Negative operating cash flows in historical or prospective financial statements
 - D. All of the above
8. Which of the following is not one of the basic elements of an auditor's report?
- A. Scope paragraph
 - B. Auditor's opinion paragraph
 - C. Summary paragraph

- D. Date of the report
9. Which one from the following is not a type of audit report?
- A. Adverse opinion
 - B. Unqualified report with an 'emphasis of matter' paragraph
 - C. Unqualified report
 - D. Qualified report
10. Which one from the following is not part of a systems-based audit approach?
- A. Identification of the key controls to assess the extent to which the auditors may rely on them
 - B. Tests of control on identified key controls
 - C. Using tests of control to draw conclusions concerning the internal control system
 - D. A maximum number of substantive testing procedures on the transactions
11. Which of the following is not an objective of the audit planning?
- A. To set out the way in which the objectives and other priorities will be achieved
 - B. To define how the audit evidence necessary to achieve the objectives will be obtained
 - C. To perform data analysis to identify major weaknesses
 - D. To identify the resources that will be needed and actually employed in audits
12. Materiality threshold is defined as the maximum tolerance level of errors identified after verification of a sample. Audit risk is the probability of existing errors not being identified by the auditors. Which one of the following statements is not correct?
- A. The higher the materiality threshold, the lower the audit risk
 - B. Materiality and audit risk are inversely proportional
 - C. The lower the materiality threshold, the higher the audit risk
 - D. Materiality and audit risk are not related
13. Which one of the following statements is correct?
- A. Audit risk is the risk of a material misstatement in the financial statements.
 - B. The risk of a material misstatement in the financial statements consists of control risk.

- C. Audit risk is the risk that the auditor will not detect a material misstatement that exists in the financial statements.
 - D. Audit risk is the risk of a material misstatement in the financial statements and that the auditor did not detect the material misstatement.
14. Which one of the following does not impact on inherent risk?
- A. The auditor has reduced the sample sizes for testing of purchases for the entity.
 - B. The entity has purchased its raw materials from the United States at discounted prices.
 - C. During the year, the entity converted its computer system to a new improved online system.
 - D. Management has introduced a new bonus scheme for sales employees who meet their monthly target.
15. What is not included under the audit phrase "substantive procedures"?
- A. Tests made to obtain evidence of material errors
 - B. A general strategy and detailed approach concerning the nature, programming and extent of the audit
 - C. Analytical procedures to analyse trends and fluctuations
 - D. Tests of the details of the transactions

SECTION B :70 MARKS

QUESTION 1

- (a) Explain the purpose of a value for money audit. (4 marks)
- (b) Bluesberry hospital is located in a country where healthcare is free, as the taxpayers fund the hospitals which are owned by the government. Two years ago management reviewed all aspects of hospital operations and instigated a number of measures aimed at improving overall 'value for money' for the local community.

Management have asked that you, an audit manager in the hospital's internal audit department, perform a review over the measures which have been implemented. Bluesberry has one centralised buying department and all purchase requisition forms for medical supplies

must be forwarded here. Upon receipt the buying team will research the lowest price from suppliers and a purchase order is raised. This is then passed to the purchasing director, who authorises all orders. The small buying team receive in excess of 200 forms a day.

The human resources department has had difficulties with recruiting suitably trained staff. Overtime rates have been increased to incentivise permanent staff to fill staffing gaps, this has been popular, and reliance on expensive temporary staff has been reduced. Monitoring of staff hours had been difficult but the hospital has implemented time card clocking in and out procedures and these hours are used for overtime payments as well. The hospital has invested heavily in new surgical equipment, which although very expensive, has meant that more operations could be performed and patient recovery rates are faster. However, currently there is a shortage of appropriately trained medical staff.

A capital expenditure committee has been established, made up of senior managers, and they plan and authorise any significant capital expenditure items.

Required:

i Identify and explain four strengths within Bluesberry's operating environment; and

(6 marks)

ii For each strength identified, describe how Bluesberry might make further improvements to provide best value for money.

(4 marks)

(c) Describe two substantive procedures the external auditor of Bluesberry should adopt to verify each of the following assertions in relation to an entity's property, plant and equipment:

(i) Valuation

(ii) Completeness; and

(iii) Rights and obligations. Note: Assume that the hospital adopts International Financial Reporting Standards.

(6 marks)

[Total 20 marks]

QUESTION 2

Clarinet Co (Clarinet) is a computer hardware specialist and has been trading for over five years. The company is funded partly through overdrafts and loans and also by several large shareholders; the year end is 30 April 2022.

Clarinet has experienced significant growth in previous years; however, in the current year a new competitor, Drums Design Co (Drums), has entered the market and through competitive pricing has gained considerable market share from Clarinet. One of Clarinet's larger customers has stopped trading with them and has moved its business to Drums.

In addition, a number of Clarinet's specialist developers have left the company and joined Drums. Clarinet has found it difficult to replace these employees due to the level of their skills and knowledge. Clarinet has just received notification that its main supplier who provides the company with specialist electrical equipment has ceased to trade. Clarinet is looking to develop new products to differentiate itself from the rest of its competitors.

It has approached its shareholders to finance this development; however, they declined to invest further in Clarinet. Clarinet's loan is long term and it has met all repayments on time. The overdraft has increased significantly over the year and the directors have informed you that the overdraft facility is due for renewal next month, and they are confident it will be renewed. The directors have produced a cash flow forecast which shows a significantly worsening position over the coming 12 months. They are confident with the new products being developed, and in light of their trading history of significant growth, believe it is unnecessary to make any disclosures in the financial statements regarding going concern.

At the year end, Clarinet received notification from one of its customers that the hardware installed by Clarinet for the customers' online ordering system has not been operating correctly. As a result, the customer has lost significant revenue and has informed Clarinet that they intend to take legal action against them for loss of earnings. Clarinet has investigated the problem post year end and discovered that other work-in-progress is similarly affected and inventory should be written down.

The finance director believes that as this misstatement was identified after the year end, it can be amended in the 2023 financial statements.

Required:

- (a) Describe the procedures the auditors of Clarinet Co should undertake in relation to the uncorrected inventory misstatement identified above. (4 marks)
- (b) Explain six potential indicators that Clarinet Co is not a going concern. (6 marks)
- (c) Describe the audit procedures which you should perform in assessing whether or not Clarinet Co is a going concern. (6 marks)
- (d) The auditors have been informed that Clarinet's bankers will not make a decision on the overdraft facility until after the auditor's report is completed. The directors have now agreed to include some going concern disclosures.

Required:

Describe the impact on the auditor's report of Clarinet Co if the auditor believes the company is a going concern but that this is subject to a material uncertainty. (4 marks)

[Total = 20 marks]

QUESTION 3

Part (a)

ISA 260 Communication with those charged with governance provides guidance to auditors in relation to communicating with those charged with governance on matters arising from the audit of an entity's financial statements.

Required

- (i) Explain why it is important that auditors communicate throughout the audit with those charged with governance; and (2 marks)
- (ii) Describe THREE examples of matters that the auditors may communicate to those charged with governance. (3 marks)

Part (b)

Fox Industries Co (Fox) manufactures engineering parts. It has one operating site and a customer base spread across Europe. The company's year end was 30 April 2022. Below is a description of the purchasing and payments system.

Purchasing system: Whenever production materials are required, the relevant department sends a requisition form to the ordering department.

An order clerk raises a purchase order and contacts a number of suppliers to see which can despatch the goods first. This supplier is then chosen. The order clerk sends out the purchase order. This is not sequentially numbered and only orders above \$5,000 require authorisation. Purchase invoices are input daily by the purchase ledger clerk, who has been in the role for many years and, as an experienced team member, he does not apply any application controls over the input process.

Every week the purchase day book automatically updates the purchase ledger, the purchase ledger is then posted manually to the general ledger by the purchase ledger clerk.

Payments system: Fox maintains a current account and a number of saving (deposit) accounts. The current account is reconciled weekly but the saving (deposit) accounts are only reconciled every two months. In order to maximise their cash and bank balance, Fox has a policy of delaying payments to all suppliers for as long as possible. Suppliers are paid by a bank transfer.

The finance director is given the total amount of the payments list, which he authorises and then processes the bank payments.

Required:

As the external auditors of Fox Industries Co, write a report to management in respect of the purchasing and payments system described above which:

- (i) Identifies and explains FOUR deficiencies in the system (4 marks)
- (ii) Explains the possible implication of each deficiency. (4 marks)
- (iii) Provide a recommendation to address each deficiency. A covering letter is required. (6 marks)
- (c) Identify and explain FOUR application controls that should be adopted by Fox Industries Co to ensure the completeness and accuracy of the input of purchase invoices. (4 marks)
- (d) Describe substantive procedures the auditor should perform to confirm the bank and cash balance of Fox Industries Co at the year end. (7 marks)

[Total = 30 marks]

END OF QUESTION PAPER