



ZIMBABWE EZEKIEL GUTI UNIVERSITY

FACULTY OF LAW, BUSINESS INTELLIGENCE AND ECONOMICS

**DEPARTMENT OF ACCOUNTING, FINANCE AND HUMAN
CAPITAL MANAGEMENT**

EXAMINATION PAPER

COURSE CODE : CAC 412
COURSE TITLE : AUDIT THEORY, SKILLS AND PRACTICE
SPECIAL REQUIREMENTS : NONE
DURATION : 3 Hours
LEVEL : 4.1
DATE : 10 APR 2024

INSTRUCTIONS TO CANDIDATES:

1. No cell phones are allowed in the examination venue
2. Use of silent, non-programmable calculators is allowed
3. Answer **ALL** questions in both Section A and Section B.
4. Begin each question on a new page.
5. The number of marks for each question or part question is shown in brackets []

Section A - compulsory question which carries 25 marks

Question 1

The firm for which you work, is the auditor of STEP Manufacturing Ltd, and you have been asked by the senior in charge to describe how you can use computer assisted audit techniques to audit the company's computerized sales and sales ledger system. STEP Manufacturing Ltd. will allow you to use your data on test files to check the correct operation of the accounting computer programs and to use computer audit programs to interrogate the sales ledger file. You have already satisfied yourself that controls over access to the sales ledger system are effective. You have established the following details pertaining to the computerized sales system:

1. Details of goods to be dispatched are input into the computer and after approval by the credit controller, dispatch notes are printed in the dispatch department who send the goods to the customers.
2. The computer department prepares the sales invoices using prices from the price file. It posts the invoices to the sales ledger and the sales and VAT to the nominal ledger. The invoices are then sent to the customers.
3. Cash received and discounts allowed are posted to the sales ledger by the accounts department
4. The system allows posting of credit notes, adjustments (to correct errors) and writing off bad debts
5. At monthly intervals, statements are sent to customers.
6. The computer may print out the following information at any time:
 - Details of transactions on any account.
 - An age analysis of sales ledger accounts.
 - The total of the balances on the sales ledger.
 - Details of transactions posted during the month

- An analysis of sales income for the month.
7. The information required when inputting dispatch note details is as follows:
- Customer account number
 - Date of dispatch (if different from the current date)
 - Part number and quantity of each item dispatched.
 - Any special discounts allowed to a customer.

Required:

(a) Describe the test data you would enter into the computerized sales system to check the correct processing of dispatch notes and sales invoices. **(8 marks)**

(b) Explain how a computer audit program may assist you in

- i. Carrying out a circularization of accounts receivable including selecting the accounts to circularize. **(5 marks)**
- ii. Verifying the year end receivables in the sales ledger. **(7 marks)**

Notes:

- In part (a) you are not required to describe how you would check the correct processing of cash discounts, credit notes and adjustments to correct errors.
- You are not required to describe in detail how you would carry out a circularization of accounts receivable. You are only required to consider the aspects of a circularization required by part (b) of the questions.

(c) Describe the inherent limitations facing auditors in undertaking their work. **(5 marks)**

Total **[25 marks]**

Section B – Answer ALL questions, each carries 25 marks

Question 2

Big Manufacturing is a large manufacturing group which operates from several locations around the world. It has recently announced plans to expand its operations in a large developing country where it will manufacture a new car model. This model will be small, cheap, and basic and will be marketed to lower-to-middle income individuals and families, for whom owning a car has never previously been a possibility. These cars will not have many standard features such as radios, heaters/coolers, electronic windows and the like. They will have basic safety features such as seat belts, but not more advanced ones like air bags.

Many western environmentalists have expressed concern that the extensive use of this car model will cause a great deal of damage to the environment, particularly through carbon emissions. Traffic congestion will also be greatly worsened. This will increase the clamour for the building of new roads and, hence, reinforce the environmental damage. This new model will also exacerbate the already very poor road safety record that this country experiences. Additionally, environmentalists believe that the cars themselves will have relatively short useful lives at the end of which they will be dumped in a disorganised and unregulated manner.

Big Manufacturing has responded by claiming that this new model will not use a great deal of fuel because they are lightweight and have small and efficient engines. It points out that this car model is designed to be much safer than car models that were marketed in Europe, a comparatively short time ago. Also many of the target customers would otherwise ride motorbikes that are more inefficient, more polluting, and much less safe than the proposed new car.

Big Manufacturing has also stated that cars will not be dumped at the end of their lives. All of the dealers who sell the new model will be required to collect any cars that are no longer roadworthy from each customer's home and will be required to return them to the manufacturer's recycling centre. The car has a simple design which makes it easy to dismantle and separate into different categories of material for recycling. The recycling

centre has not been built yet because it will be at least three years before there are significant numbers of scrap cars.

Big Manufacturing has asked your firm, as its auditors, to conduct an environmental audit of its claims. It wishes to publish your report on its corporate website in order to address the concerns of the environmental movement.

REQUIREMENT:

(a) There is some skepticism in the professional and business community and amongst outside commentators as to environmental and social reporting. Discuss the extent to which the auditing of such reports could help to allay the skeptics' concerns in this regard. Use the scenario presented above to illustrate your argument. **(10 marks)**

(b) Assess critically the particular difficulties you would experience in auditing Big Manufacturing claim that:

(i) The new car is efficient and that its use will not adversely affect the environment compared with existing forms of transport; **(5 marks)**

(ii) The new cars will operate to an acceptable standard of safety; **(5 marks)**

(iii) It will be capable of recycling all scrap cars. **(5 marks)**

Total **(25 marks)**

Question 3

It is 1 July 2023. You are a manager in the audit department of Tama & Co Accountants.

You are assigned to the audit of the Rhodes bout Group, which has a financial year ending 30 September 2023, and is listed on ZSE. Tama & Co was appointed auditor to the Group in January 2023. The Group operates in the travel industry, and has a fleet of 20 cruise bouts. The Group operates three brands which provide different types of cruise experience.

You are provided with the following information which you should use to help you with planning the audit of the new client, the Rhodes Group, for the financial year ending 30 September 2023.

Background information

Group operations

The Group, which is headquartered in Bulawayo, operates cruise bouts in Victoria Falls under three brands.

The brands are internally generated and therefore are not recognised as intangible assets within the Group financial statements.

Business developments in the year

Sunseeker bouts

In this financial year, the Group will spend \$75 000 on upgrading and maintenance of these bouts.

These luxury bouts have to adhere to a very high standard, so the Group regularly incurs high expenditure on their maintenance. As well as refurbishment, several bouts have been enhanced by the installation of new entertainment facilities.

Explorer bouts

The Explorer bouts, while still luxurious, are the oldest bouts in the fleet, and the Group is gradually replacing these with new ones. During this financial year, two new bouts with a total cost of \$110 000 will come into use.

The bouts took three years to build, and were constructed by Toyota boat builders Ltd, a company which is not owned by the Group. However, the chairman of the Group, Peter Zimbo, is also the chairman of Toyota boat builders Ltd, and his son is the company's chief executive officer. The purchase of the ships was financed through a \$110 000 loan with a fixed interest rate of 6% per annum. A further three bouts are currently under construction by Toyota Ltd.

The Group has taken out a loan of \$180 000 with a 6.5% fixed interest rate to finance this capital expenditure.

Pioneer bouts

These cruises are growing in popularity. In order to visit certain destinations on these specialist cruises, the Group has to acquire operating licences from the local authorities. The cost of licence acquisition is capitalised as an intangible asset.

Selected financial information

		Projected to	Actual to
		30 Sept 2023	30 Sept 2022
	Note	\$ 000	\$ 000
Group revenue	1	764	670
Operating profit		145	101
Profit before tax		81	65
Total assets		1 800	1 780
Included in total assets:			
Intangible assets – operating licences	2	56	57
Property, plant and equipment	3	1 520	1 510

Note 1

Revenue includes passenger ticket sales, which accounts for approximately 85% of revenue. When customers book a cruise they are required to pay a refundable 20% deposit, which is initially recognised as deferred revenue. The balance of 80% is paid at least six weeks before the cruise commences and at that point it is also recognised as deferred revenue. The full amount of the ticket price is transferred to revenue when the cruise starts irrespective of the duration of the cruise.

The remaining 15% of revenue is derived from on-board sales of food, drinks, entertainment and other items to passengers. Management monitor this revenue stream closely as it achieves a high gross profit margin, and staff are encouraged to maximise these sales to customers.

Revenue is presented on a segmental basis in the notes to the financial statements, with segments based on the three brands of the Group:

Revenue per operating segment

	Projected to	Actual to
	30 Sept 2023	30 Sept 2022
	\$ 000	\$ 000
Sunseeker Cruises	320	288
Explorer Cruises	180	190
Pioneer Cruises	<u>264</u>	<u>192</u>
Total	<u>764</u>	<u>670</u>

Note 2

Operating licences are required for the Pioneer Cruise ships to visit certain destinations. Licences are amortised over the specific period to which each licence relates.

Note 3

Property, plant and equipment is comprised as follows:

Property, plant and equipment	Projected to	Actual to
	30 Sept 2023	30 Sept 2022
	\$ 000	\$ 000
Ships in use	2,041	2,010
Ships under construction	83	62
Other property, plant and equipment	<u>180</u>	<u>173</u>
	2,304	2,245
Accumulated depreciation	<u>(784)</u>	<u>(735)</u>
Carrying amount	<u>1,520</u>	<u>1,510</u>

Extract from Audit team meeting notes

A meeting took place yesterday in which the audit engagement partner discussed several issues:

Recent development affecting Pioneer Cruises

Last week, the local authorities withdrew their operating licences with immediate effect, stating that this is likely to be a temporary measure being put in place to limit the number of tourists visiting areas of natural beauty, but they did not confirm when they can resume operations.

Cyber-security attack

Last month, the Group suffered a cyber-security attack in which the personal information of 1,400 customers, including their credit card details, were stolen. According to a representative of the Group audit committee, the Group's internal audit team had not properly assessed the risks relating to cyber-security, which is a requirement of recently introduced data protection legislation. The issue which led to the cyber-security attack has now been resolved.

Social and environmental information

The Group audit committee has enquired whether Tama & Co Accountants can provide an additional service, to advise management on how to measure certain social and environmental information which is to be published on the Group's website and is required by new regulations in the industry and is required to be submitted to regulatory authorities. The social and environmental information relates to matters such as water efficiency, energy consumption, charitable donations and initiatives which support diversity in the workplace. In recognition that this work is quite urgent, as the deadline for submission to the regulatory authorities falls within the next month, the Group audit committee has stated it is willing to pay an 'enhanced fee' for this service.

Audit data analytics

The increased use of audit data analytics by many audit firms to provide several benefits including more efficient and effective audit work and enhanced audit quality was

discussed. The audit engagement partner asked the team to prepare information describing how the use of data analytics can bring these benefits to an audit like that of the Rhodes Bouts Group.

Required

(a) Using the information above, evaluate the audit risks to be considered in planning the Group audit. (12 marks)

(b) Design the principal audit procedures to be performed on the segmental information relating to the Group's revenue, using the information in the meeting notes. (4 marks)

(c) Evaluate the matters to be considered in deciding whether Pegasus & Co should accept the engagement to provide advice on the Group's social and environmental information. (6 marks)

(d) Comment on the use of audit data analytics to enhance audit efficiency, effectiveness and quality in the Group audit. (3 marks)

Total (25 marks)

QUESTION 4

(i) Profeeds is a fast-growing company in the animal feed industry. It is quoted on the ZSE but the founder, Bobby Ncube, and his family still control about 60% of the voting shares. He personally makes all the major decisions and the Board of Directors just 'rubber stamps' them. There is a nomination committee of the board but, notwithstanding this, a majority of the board are either members of Mr. Helen's extended family or have some connection to him.

(ii) Store-It Ltd is a private company engaged in the development and manufacture of versatile computer storage devices. The industry is very competitive and subject to rapid changes in technology. The company is usually third or fourth in the market in which it operates and its products are typically slightly behind the market leaders in terms of performance.

REQUIREMENT:

For each of the above situations, evaluate how the risk of material misstatement should be assessed and what effect that assessment will have on detection risk. (12 marks)

(b) (i) Farm Supply Ltd. is a manufacturer of light agricultural and horticultural equipment. Important details from its financial statements are as follows:

	\$ million
Net Profit	22
Total Assets	560
Total Revenues	780

During the course of the audit of the company, the audit firm detected two misstatements that aggregated to \$1.3m.

(ii) Sliotar Investments Ltd. provides a group of mutual funds for investors. Important details from its financial statements are as follows:

	\$ million
Net Profit	41
Total Assets	4 500
Total Revenues	905

During the course of the audit of the company, the audit firm detected two misstatements that aggregated to \$ 5.86m.

REQUIREMENT:

For each of the above situations, appraise and justify materiality. (13 marks)

[Total: 25 Marks]

END OF EXAMINATION QUESTION PAPER