



ZIMBABWE EZEKIEL GUTI UNIVERSITY

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FACULTY OF LAW, BUSINESS INTELLIGENCE AND ECONOMICS

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DEPARTMENT OF ACCOUNTING, FINANCE AND HUMAN  
CAPITAL MANAGEMENT

**EXAMINATION PAPER**

COURSE CODE : CAC412  
COURSE TITLE : AUDIT THEORY, SKILLS AND PRACTICE  
SPECIAL REQUIREMENTS : NONE  
DURATION : 3 Hours  
LEVEL : 4.1  
DATE : 26 SEP 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**

1 July 2023, you are an audit manager in Tavonga & Co Accountants. Your role includes performing post-issuance audit quality reviews, and you have been asked to review the audit work performed on Masimba Co, for the financial year ended 31 January 2023. You have gathered the following information from your review of the audit file:

**Audit team and fees**

Masimba Co is a listed company operating in the construction industry. The company has an audit committee. Masimba Co has been an audit client of Tavonga & Co for six years, and Brians has been the audit engagement partner during this time. Masimba Co's auditor's report was signed by Brians and issued last week. The report contained an unmodified opinion.

Tavonga & Co requires its staff to record each hour they spend working on each client in the firm's time management system. From reviewing the time records relating to the audit of Masimba Co, you are aware that Brians and the other audit team members recorded the following amount of time on the audit:

Brians– audit engagement partner	2 hours
A Chiyangwa – senior audit manager	6 hours
R Kimberly – audit manager	35 hours
Six audit assistants	<u>130 hours</u>
Total time spent on audit	<u>173 hours</u>

It is apparent from your review that almost all of the detailed review of the audit working papers was completed by R Kimberly, who has evidenced her review by stating 'final review' on each page of the audit file. She has recently been promoted to audit manager.

You are also aware that Brains booked a total of 40 hours to Masimba Co in respect of non-audit work performed. The only information you can find in the documentation is that the non-audit work related to a 'special investigation', and that Bob confirms that it does not create a threat to auditor objectivity. The total fee charged for the audit was \$250,000 and the fee for the 'special investigation' was \$890,000.

#### Going concern

From reviewing the audit working papers, you are aware that going concern was identified as a significant audit risk at the planning stage of the audit due to low profit margins or losses being made on many of the company's construction contracts and increasing economic uncertainty. The company typically has 20 contracts ongoing at any time.

Most of the audit work on going concern was performed by Mary Manyaza, an audit assistant who has just taken her last professional exam and is not yet qualified. The majority of the audit work performed on going concern focused on a review of five major contracts to determine their profitability. The management of Masimba Co identified the major contracts for review and provided Mary with forecasts indicating that the contracts would all make a small profit. Mary confirmed that the assumptions used in the forecasts agreed to assumptions used in previous years and concluded that the contracts which she had reviewed support the going concern status of the company.

Having reviewed these major contracts, Mary completed the conclusion on going concern, stating that there is no significant uncertainty over going concern.

#### Required:

- (a) Comment on the quality of the planning and performance of the audit of Masimba Co, discussing the quality control, ethical and other professional issues raised and recommending appropriate actions to be taken. **(15 marks)**
- (b) State the respective responsibilities of the directors and management of a company and its external auditors with respect to the financial statements. **(3 marks)**
- (c) Describe the inherent limitations facing auditors in undertaking their work. **(3 marks)**

**(Hint: Don not confuse inherent limitations with inherent risk)**

(c) Describe the significant types of judgments made by auditors in:

i. Gathering evidence (2 marks)

ii. Arriving at an opinion on the financial statements. (2 marks)

[Total 25 marks]

## Section B

Answer 3 questions, each carries 25 marks

### Question 2

'The International Federation of Accountants (IFAC) was established in 1977 to set international standards of auditing, ethics, education and training'

#### Required:

(a) Discuss the potential advantages of international harmonization of auditing standards. (15 marks)

(b) Discuss the difficulties that stand in the way of harmonization. (10 marks)

[Total 25 marks]

### Question 3

(a) IFAC's Code of Ethics for Professional Accountants states that a professional accountant is required to comply with five fundamental principles, one of which is the principle of 'professional competence and due care'.

#### Required:

Explain what is meant by the term 'professional competence and due care', and outline how Accounting firms can ensure that the principle is complied with. (8 marks)

(b) You are a senior manager in Ascending Ladder Accountants, and you are responsible for the audit of Zhing Ltd, a manufacturer of plastic toys which are exported all over the continent. The following matter has been brought to your attention by the audit senior, who has just completed the planning of the forthcoming audit for the year ending 30 June 2023:

During a discussion with the production manager, it was revealed that there have been some quality control problems with the toys manufactured between March and May 2023.

It was discovered that some of the plastic used in the manufacture of the company's products had been contaminated with a dangerous chemical which has the potential to explode if it is exposed to high temperatures. Zhing Ltd did not recall any of the products which had been manufactured during that time from customers, as management felt that the risk of any injury being caused was remote.

Your firm has been invited to tender for the provision of the external audit service to Zhuangin Ltd. You are aware that Zhuangin Ltd operates in the same industry as Zhing Ltd, and that the two companies often enter into highly publicised, aggressive advertising campaigns featuring very similar products. Zhuangin Ltd is a much larger company than Zhing Ltd, and there would be the opportunity to offer some non-audit services as well as the external audit.

Required:

Assess the ethical and professional issues raised, and recommend any actions necessary in respect of:

- (i) The contaminated plastic used by Zhing Ltd; and (9 marks)
- (ii) The invitation to audit Zhuangin Ltd. (8 marks)

[Total 25 marks]

#### Question 4

The ISA 240 'The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements' distinguishes fraud from error, sets out the auditor's responsibilities with respect to fraud, and provides additional guidance related to earnings management.

Required:

- (a) Compare and contrast the auditor's responsibility for the detection and reporting of fraud and of error.

Your answer should distinguish fraud from error. (10 marks)

- (b) Explain the term 'professional skepticism' and comment on its role in the detection of fraud. (5 marks)

(c) Comment on the difficulties which 'earnings management' presents to the auditor. (5 marks)

(d) What is meant by expectation gap? Is there any expectation gap relating to detection of fraud? How can it be reduced? (5 marks)

[Total 25 marks]

### Question 5

(a) Explain 4 reasons why a firm of auditors may decide not to seek re-election as auditor. (6 marks)

(b) Read the case study below and answer the following questions relating to it.

Croco Motors Ltd manufactures cars and Lorries in Zimbabwe. You are the manager responsible for the audit of Croco Motors Ltd, and you are reviewing the audit working papers for the year ended 28 February 2023. The draft financial statements show Revenue of \$10.5 million, profit before tax of \$3.2 million, and total assets of \$45 million.

Two matters have been brought to your attention by the audit senior, both of which relate to assets recognised in the balance sheet for the first time this year:

#### Leases

In July 2022, Croco Motors Ltd entered into five new finance leases of land and buildings. The leases have been capitalised and the balance sheet includes leased assets presented as tangible fixed assets at a value of \$3.6 million, and a total finance lease creditor of \$3.2 million presented as a creditor falling due after more than one year.

#### Financial assets

Fixed assets include financial assets recognised at \$1.26 million. A note to the financial statements describes these financial assets as investments classified as 'fair value through profit or loss', and the investments are described in the note as 'held for trading'. The investments are all shares in listed companies. A gain of \$350,000 has been recognised in net profit in respect of the revaluation of these investments.

Required:

In your review of the audit working papers, comment on the matters you should consider, and state the audit evidence you should expect to find in respect of:

(i) The leases; and (7 marks)

(ii) The financial assets. (7 marks)

(b) You are aware that Croco Ltd is seeking to list on the ZSE in September 2023. The listing rules require that interim financial information is published halfway through the accounting period, and that the information should be accompanied by a review report issued by the company's independent auditor.

**Required:**

Explain the principal analytical procedures that should be used to gather evidence in a review of interim financial information. (5 marks)

[Total 25 marks]

**END OF EXAMINATION QUESTION PAPER**

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