

**ZIMBABWE EZEKIEL GUTI UNIVERSITY**



**DEPARTMENT OF ACCOUNTING AND FINANCE**

**B. COM ACCOUNTING**

**COURSE: ADVANCED THEORY AND PRACTICE OF AUDITING I**

**COURSE CODE: CAC404**

**DURATION: 3 HOURS**

**19 JUNE 2017**

**INSTRUCTIONS TO CANDIDATES**

1. No cell phones are allowed in the examination venue.
2. Answer all questions.
3. Begin each question on a new page.
4. The number of marks for each question or part question is shown in brackets.



### Question One

Tony Pvt Ltd assembles fridges, microwaves, washing machines and other similar domestic appliances from parts procured from a large number of suppliers. As part of the interim audit work two weeks prior to the company year-end, you are testing the procurement and purchases systems and attending the inventory count.

#### **Procurement and purchases system**

Parts inventory is monitored by the stores manager. When the quantity of a particular part falls below re-order level, an e-mail is sent to the procurement department detailing the part required and the quantity to order. A copy of the e-mail is filed on the store manager's computer.

Staff in the procurement department check the e-mail, allocate the order to an authorised supplier and send the order to that supplier using Electronic Data Interchange (EDI). A copy of the EDI order is filed in the order database by the computer system. The order is identified by a unique order number.

When goods are received at Tony, the stores clerk confirms that the inventory agrees to the delivery note and checks the order database to ensure that the inventory were in fact ordered by Tony. (Delivery is refused where goods do not have a delivery note.)

The order in the order database is updated to confirm receipt of goods, and the perpetual inventory system updated to show the receipt of inventory. The physical goods are added to the parts store and the paper delivery note is stamped with the order number and is filed in the goods inwards department.

The supplier sends a purchase invoice to Tony using EDI; invoices are automatically routed to the accounts department. On receipt of the invoice, the accounts clerk checks the order database, matches the invoice details with the database and updates the database to confirm receipt of invoice. The invoice is added to the purchases database, where the purchase day book (PDB) and suppliers individual account in the payables ledger are automatically updated.

#### **Required:**

- (a) List six audit procedures that an auditor would normally carry out on the purchases system at Tony Pvt Ltd, explaining the reason for each procedure. **(12 marks)**
- (b) On the day of the inventory count, you attended depot nine at Tony Pvt Ltd. You observed the following activities:
- Pre-numbered count sheets were being issued to client's staff carrying out the count.

The count sheets showed the inventory ledger balances for checking against physical inventory.

- All count staff were drawn from the inventory warehouse and were counting in teams of two.
- Three counting teams were allocated to each area of the stores to count, although the teams were allowed to decide which pair of staff counted which inventory within each area. Staff was warned that they had to remember which inventory had been counted.
- Information was recorded on the count sheets in pencil so amendments could be made easily as required.
- Any inventory not located on the pre-numbered inventory sheets was recorded on separate inventory sheets – which were numbered by staff as they were used.
- At the end of the count, all count sheets were collected and the numeric sequence of the sheets checked; the sheets were not signed.

**Required:**

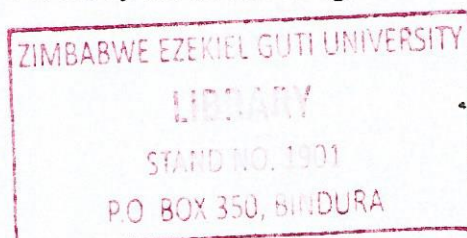
List the weaknesses in the control system for counting inventory at depot nine and explain how these weaknesses can be overcome. (13 marks)

**[Total: 25 marks]**

**Question Two**

- a. State the auditor's responsibility in relation to going concern. (5 marks)
- b. You are a partner of Hillary & Partners in charge of the audit of Chaffy Ltd, a public listed company; the audit manager has completed the audit for the financial year October 2015 to September 2016 and has given you the draft financial statements and audit file containing all the working papers. You are conducting your final review prior to signing the audit report and have identified that Chaffy Ltd currently has borrowings of \$10 million which are due for repayment on 1 November 2016 but it is currently trying to extend the due date; in addition it also has an overdraft of \$250,000 which is \$50,000 over the authorized limit; this was not identified as a cause for concern by the audit manager.

**Required:**



- i. Identify and explain ten issues that you think the audit manager should have considered when assessing whether or not Chaffy is a going concern. (10 marks)
- ii. Recommend typical types of evidence that you would have expected the audit manager to consider when performing her going concern review. (10 marks)

[Total: 25 marks]

### Question Three

The objectivity of the external auditor may be threatened or appear to be threatened where:

- a. There is undue dependence on any audit client or group of clients; (6 marks)
- b. The firm, its partners or staff have any financial interest in an audit client; (6 marks)
- c. There are family or other close personal or business relationships between the firm, its partners or staff and the audit client; (7 marks)
- d. The firm provides other services to audit clients. (6 marks)

#### Required:

For each of the four examples given above, explain why the objectivity of the external auditor may be threatened, or appear to be threatened, and why the threat is important and identify the safeguards that can be applied for each. [Total: 25 marks]

#### **Question Four**

Amigo is a charity whose constitution requires that it raise funds for educational projects. These projects seek to educate children and support teachers in certain countries. Charities in the country from which Amigo operates have recently become subject to new audit and accounting regulations. Charity income consists of cash collections at fund raising events, telephone appeals, and bequests (money left to the charity by deceased persons). The charity is small and the trustees do not consider that the charity can afford to employ a qualified accountant. The charity employs a part-time bookkeeper and relies on volunteers for fund raising. Your firm has been appointed as accountants and auditors to this charity because of the new regulations. Accounts have been prepared (but not audited) in the past by a volunteer who is a recently retired Chartered Certified Accountant.

#### **Required**

- a. Outline the three components of audit risk. **(15 marks)**
- b. Describe the risks associated with the audit of Amigo under the headings inherent risk, control risk and detection risk and explain the implications of these risks for overall audit risk. **(10 marks)**

**[Total: 25 marks]**

**End of Paper**

