



ZIMBABWE EZEKIEL GUTI UNIVERSITY

FACULTY OF BUSINESS, ECONOMICS AND ACCOUNTING

DEPARTMENT OF ACCOUNTING AND FINANCE

EXAMINATION PAPER

COURSE CODE : CAC408
COURSE TITLE : ADVANCED THEORY AND PRACTICE OF AUDITING II
SPECIAL REQUIREMENTS :
DURATION : 3 Hours
LEVEL : 4.2
DATE :

printed

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

Answer all questions in this section. Each question carries 2 marks.

Select the most appropriate answer

1. Which of the following is NOT a statutory right of the auditors of a limited liability company?

(1) A right to attend all directors' meetings and receive all notices and communications relating to such meetings.

(2) A right to speak at general meetings on any part of the business that concerns them as auditors.

(3) A right to attend any general meeting and receive all notices and communications relating to such meetings.

A (1) only

B (1) and (3)

C (2) only

D (2) and (3)

2. The PRIMARY purpose of an auditor evaluating and testing the internal controls of a limited liability company, is to enable the auditor to advise management of the deficiencies in the internal controls.

Is this statement true or false?

A True

B False

3. 'Audit risk' represents the risk that the auditor will give an inappropriate opinion on the financial statements when the financial statements are materially misstated. Which of the following categories of risk can be controlled by the auditor?

Category of risk:

(1) Control risk

(2) Detection risk

(3) Sampling risk

A (1) and (2)

B (2) only

C (1) and (3)

D (2) and (3)

4. Possible indications of the existence of irregularities include the following except:

- A. Missing vouchers or documents
- B. Falsified documents
- C. Absence of investment policy
- D. Evidence that internal control is not operating as it is intended

5. Which of the following is not a major cause of failure in the planning process

- A. Starting work before finishing planning
- B. Inadequate documentation
- C. Lack of understanding of the business
- D. None of the above

6. The appropriateness of audit evidence can be enhanced by the following except

- A. Independence of provider
- B. Effectiveness of client's internal controls
- C. Nature of the client industry
- D. Qualification of provider

7. Professional skepticism requires that the auditor assumes that management is

- A. Reasonably honest
- B. Neither honest or dishonest
- C. Not necessarily honest
- D. Dishonest unless proved otherwise

8. The IFAC Code of Ethics recognizes that the objectives of the accountancy profession are:

- A. To work to the highest standards of professionalism
- B. To attain the highest level of performance
- C. Generally, to meet the public interest requirement set out
- D. All of the above

9. All of the following are safeguards created by the audit profession except
- A. Educational, training and experience requirements for entry into the profession
 - B. Continuing education requirements
 - C. Allocation of complex tasks to competent audit firms
 - D. Professional standards and monitoring and disciplinary processes

10. Which of the following should be facilitated by the standardisation of substantive procedure working papers?

- (1) Meeting of specified audit objectives.
- (2) Communicating with the staff of the audit client.
- (3) Delegation of audit work.

A (1) only

B (1) and (3)

C (2) and (3)

D (3) only

11. Which of the following types of internal controls does a small limited liability company normally have particular difficulty in implementing satisfactorily?

- (1) Segregation of duties.
- (2) Performance reviews.
- (3) Information processing.

A (1) only

B (2) only

C (3) only

D (1) (2) and (3)

12. Which of the following is not a threat to auditor's independence

- A. Familiarity
- B. Self-interest
- C. Self-actualisation
- D. Self-review

13. Fraudulent financial reporting may be accomplished by the following except
- A. Manipulation, falsification (including forgery), or alteration of accounting records or supporting documentation from which the financial statements are prepared
 - B. Misrepresentation in, or intentional omission from, the financial statements of events, transactions or other significant information
 - C. Intentional misapplication of accounting principles relating to amounts, classification, manner of presentation or disclosure
 - D. None of the above
14. Which of the following is not a stage in the audit process
- A. Planning
 - B. Responding to assessed risks
 - C. Gathering audit evidence
 - D. Preliminary
15. Which of the following is not a component of internal controls
- A. The control environment
 - B. The entity's risk assessment process
 - C. Physical access controls
 - D. Control activities

[Total: 30 marks]

SECTION B

Answer all questions in this section

Question One

(a) Auditors have various duties to perform in their role as auditors, for example, to assess the truth and fairness of the financial statements.

Explain the auditor's rights as provided in the Companies and Other Companies Act (Chapter 24:31) which are meant to protect the auditor in carrying out statutory audit work. **[10 marks]**

(b) In order to achieve the objectives of the accountancy profession, professional accountants have to observe a number of prerequisites or fundamental principles.

Describe the SIX fundamental ethical principles that guide the audit profession **[15 marks]**

[Total: 25marks]

Question Two

You work in the audit department of Tarcs & Co. The Gomba Group (the Group) is an audit client of your firm and the audit for the financial year ended 31 December 2019 is in the completion stage.

The Group, which is not listed, installs and maintains security systems for businesses and residential customers.

Materiality for the audit of the Group financial statements has been determined to be \$400,000. You are reviewing the audit working papers, and have gathered the following information:

Fraud

The Group finance director has informed the audit team that during the year, a fraud was carried out by a manager, Tonde Zulu, in one of the Group's procurement departments. The manager had raised fictitious supplier invoices and paid the invoiced amounts into his personal bank account. When questioned by the Group's finance director, Tonde Zulu confessed that he had stolen \$40,000 from the Group.

The finance director asked the audit team not to perform any procedures in relation to the fraud, as the amount is immaterial. He also stated that the financial statements would not be adjusted in relation to the fraud.

The only audit evidence on file is a written representation from management acknowledging the existence of the fraud, and a list of the fictitious invoices which had been raised by the manager, provided by the finance director.

The audit working papers conclude that the fraud is immaterial and no further work is needed.

Development costs

In August 2019, the Group commenced development of a new security system, and incurred expenditure of \$600,000 up to the financial year end, which has been capitalised as an intangible non-current asset.

The only audit evidence obtained in relation to this balance is as follows:

- Agreement of a sample of the costs included in the \$600,000 capitalised to supporting documentation such as supplier invoices.
- Cash flow projection for the project, which indicates that a positive cash flow will be generated by 2021. The projection has been arithmetically checked.

A written representation from management stating that 'management considers that the development of this new product will be successful'.

You are aware that when the Group finance director was asked about the cash flow projection which he had prepared, he was reluctant to answer questions, simply saying that 'the assumptions underlying the projection have been agreed to assumptions contained in the Group's business plan'. He provided a spreadsheet showing the projection but the underlying information could not be accessed as the file was password protected and the Group finance director would not provide the password to the audit team.

Trade receivables

Trade receivables recognised in the Group's current assets includes a balance of \$500,000 relating to a specific customer, Hamlyn Co. Audit procedures indicate that at 31 December 2020, the balance was more than six months overdue for payment. In relation to this balance, the following procedures have been performed:

- Agreement of the balance to invoices and original customer order.
- Discussion with the Group credit controller who states that 'we are in discussions with Hamlyn Co and we are confident that some or all of the amount due to us will be paid. We have always allowed this customer extended credit terms and they have always paid eventually.'

- Hamlyn Co was included in the trade receivables direct confirmation audit procedure, whereby a sample of customers were asked to confirm the outstanding balance, but no reply was received.

Required:

(a) Discuss the implications of the fraud for the completion of the audit, and the actions to be taken by the auditor. **[10 marks]**

(b) In respect of the development costs and trade receivables:

(ii) Comment on the sufficiency and appropriateness of the audit evidence obtained **[8 marks]**

(iii) Recommend the actions to be taken by the auditor, including the further evidence which should be obtained. **[7 marks]**

**[Total
25marks]**

Question Three

a) Define what is meant by Audit risk and materiality and briefly explain their relationship **[5 marks]**

ISA 300: Planning an Audit of Financial Statements states that an auditor should plan the audit work so that the audit will be performed in an efficient and effective manner.

Required

(a) Which critical areas should an auditor take into consideration during the planning stage in order to make the audit efficient and effective? **[5 marks]**

(b) (i) identify and explain FOUR financial statement assertions relevant to account balances at the year end. **[5 marks]**

(ii) For each identified assertion, describe a substantive procedure relevant to the audit of year-end inventory. **[5 marks]**

[Total: 20 marks]

END OF EXAMINATION_QUESTION PAPER