

COURSE CODE: AC 404/IDE AC404 (S) 2010

UNIVERSITY OF SWAZILAND
DEPARTMENT OF ACCOUNTING
SUPPLEMENTARY EXAMINATION QUESTION PAPER

DEGREE/YEAR OF STUDY : B COM IV
TITLE OF PAPER : AUDITING
COURSE CODE : AC 404
TIME ALLOWED : THREE (3) HOURS
INSTRUCTIONS

- 1. TOTAL NUMBER OF QUESTIONS ON THIS PAPER: FOUR (4)**
- 2. ANSWER ALL QUESTIONS**
- 3. WHERE APPLICABLE ALL WORKINGS SHOULD BE SHOWN**
- 4. ALL CALCULATIONS ARE TO BE MADE TO THE NEAREST LILANGENI.**

NOTE: YOU ARE REMINDED THAT IN ASSESSING YOUR WORK, ACCOUNT WILL BE TAKEN OF ACCURACY OF THE LANGUAGE AND THE GENERAL QUALITY OF EXPRESSION, TOGETHER WITH THE LAYOUT AND PRESENTATION OF YOUR FINAL ANSWER.

SPECIAL REQUIREMENT: NONE

THIS PAPER IS NOT TO BE OPENED UNTILL PERMISSION HAS BEEN GRANTED BY THE INVIGILATER.

QUESTION 1

There are similarities and differences between the responsibilities of internal and external auditors. Both internal and external auditors have responsibilities relating to the prevention, detection and reporting of fraud, for example, but their responsibilities are not the same. Both internal and external audit are part of an organisation's overall corporate governance arrangements. Sometimes, the responsibilities of internal auditors are outsourced to external organisations.

Required:

(a) Explain the difference between the responsibilities of internal auditors and external auditors for the prevention, detection and reporting of fraud and error.
(7 marks)

(b) Explain the role of internal audit in the context of: (i) corporate governance;

(ii) risk management;

(iii) organisational control.

(12 marks)

Your answer should include one example of how an internal audit department in a manufacturing company might fulfil its role under each of the headings above.

(c) Outline the issues that should be considered when an organisation decides to out source the internal audit function.
(6marks)

(25 marks)

QUESTION 2

ISA 505 External Confirmations. deals with a number of different types of external confirmation. External confirmation is a useful method of obtaining audit evidence in relation to accounts receivable.

Required:

(a) In relation to external confirmation of accounts receivable:

(i) explain the difference between a positive and a negative confirmation;

(ii) explain the two different types of positive confirmation and the advantages and disadvantages of each;

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(iii) list the reconciling items highlighted by external confirmation of accounts receivable. (9 marks)

(b) Describe the principal risks associated with financial statement assertions relating to receivables. (4 marks)

(c) Leatherfoot is a small company which manufactures high quality shoes and sells them to small retailers. This is your first year as auditor. Leather foot has a receivables ledger with approximately 750 accounts. A number of the receivables accounts are old, some have nil or credit balances and some should probably be written off. The company's client base is mixed. Bad debts have generally represented about 2% of the total receivables figure and

a general provision of 1.5% has been made in the past in addition to any specific provisions. Most of the bad debts relate to smaller customers but there are some very slow moving larger accounts in the current year. The total value of receivables is \$750,000, 60% of which comprises some thirty large accounts, and 40% of which comprises a large number of small accounts.

You have tested the system of internal controls over receivables and it appears to be working adequately. In your experience external confirmation of receivables in this sector generally have a response rate of just over 50%.

Required:

Describe the audit work you will perform on accounts receivable and bad debts at Leatherfoot. (13 marks)

Note: You are not required to perform numerical calculations in this question.

(25 marks)

QUESTION 3

a) Company A has a number of long and short-term payables, accruals and provisions in its balance sheet.

Required:

Describe the audit procedures you would apply to each of the three items listed below, including those relating to disclosure.

(i) A 10-year bank loan with a variable interest rate and an overdraft (a bank account with a debit balance on the bank statement), both from the same bank. (6 marks)

(ii) Expense accruals. (5 marks)

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(iii) Trade payables and purchase accruals. (7 marks)

(b) Company B has a provision in its balance sheet for claims made by customers for product defects under 1-year company warranties.

Required:

Describe the matters you would consider and the audit evidence you would require for the provision. (7 marks)

(25 marks)

QUESTION 4

IAS 2 'Inventories' requires that inventories are measured at the lower of cost and net realisable value.

Required:

- (a) Explain why the audit of inventory is important to auditors. (5 marks)**
- (b) Define 'cost' and 'net realisable value' according to IAS 2 'Inventories'. (6 marks)**
- (c) Describe the audit evidence that you would obtain for the cost and net realisable value of finished inventory in a company that manufactures household furniture. (9 marks)**

NB: You are not required to deal with inventory quantities.

(25 marks)

End of Question Paper