

COURSE CODE: IDE AC404 (M) 2013

UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING

MAIN EXAMINATION QUESTION PAPER

DEGREE/YEAR OF STUDY : B COM

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

You are the audit manager in DeCe & Co, an audit firm with ten national offices.

One of your clients, Rocks Forever, purchases diamond jewellery from three manufacturers. The jewellery is then sold from Rocks Forever's four shops. This is the only client your firm has in the diamond industry.

You are planning to attend the physical inventory count for Rocks Forever. Inventory is the largest account on the statement of financial position with each of the four shops holding material amounts. Due to the high value of the inventory, all shops will be visited and test counts performed.

With the permission of the directors of Rocks Forever, you have employed UJ, a firm of specialist diamond valuers who will also be in attendance. UJ will verify that the jewellery is, in fact, made from diamonds and that the jewellery is saleable with respect to current trends in fashion. UJ will also suggest, on a sample basis, the value of specific items of jewellery.

Counting will be carried out by shop staff in teams of two using pre-numbered count sheets.

Required:

- (a) **List and explain the reasons for the audit procedures used in obtaining evidence in relation to the inventory count of inventory held in the shops.**
(14 marks)
- (b) **Explain the factors you should consider when placing reliance on the work of UJ.**
(6 marks)
- (c) **Describe the audit procedures you should perform to ensure that jewellery inventory is valued correctly.**
(5 marks)

(25 marks)

QUESTION 2

You are the senior manager in the internal audit department of Octball, a limited liability company. You report to the chief internal auditor and have a staff of six junior auditors to supervise, although the budget allows for up to ten junior staff.

In a recent meeting with the chief internal auditor, the difficulty of staff recruitment and retention was discussed. Over the past year, five junior internal audit staff have left the company, but only two have been recruited. Recruitment problems identified include location of Octball's head office in a small town over 150 kilometres from the nearest major city and extensive foreign travel, often to cold climates.

Together with the chief internal auditor you believe that outsourcing the internal audit department may be a way of alleviating the staffing problems. You would monitor the new outsourced department in a part-time role taking on additional responsibilities in other departments, and the chief internal auditor would accept the post of Finance Director (FD) on the board, replacing the retiring FD.

Two firms have been identified as being able to provide the internal audit service:

- The NFA Partnership, a local firm specialising in provision of accountancy and internal audit services. NFA does not audit financial statements or report to members, and
- T&M, Octball's external auditors, who have offices in 75 countries and employ in excess of 65,000 staff.

Required:

- (a) **Discuss the advantages and disadvantages of appointing NFA as internal auditors for Octball.** (10 marks)
- (b) **Discuss the issues T&M need to consider before they could accept appointment as internal auditors for Octball.** (8 marks)
- (c) Assume that an outsourcing company has been chosen to provide internal audit services.
Describe the control activities that Octball should apply to ensure that the internal audit service is being maintained to a high standard. (7 marks)

(25 marks)

QUESTION 3

You are the auditor of BearsWorld, a limited liability company which manufactures and sells small cuddly toys by mail order. The company is managed by Mr Kyto and two assistants. Mr Kyto authorizes important transactions such as wages and large orders, one assistant maintains the payables ledger and orders inventory and pays suppliers, and the other assistant receives customer orders and despatches cuddly toys. Due to other business commitments Mr Kyto only visits the office once per week.

At any time, about 100 different types of cuddly toys are available for sale. All sales are made cash with order – there are no receivables. Customers pay using credit cards and occasionally by sending cash. Turnover is over\$5.2 million.

You are planning the audit of BearsWorld and are considering using some of the procedures for gathering audit evidence recommended by *ISA500* as follows:

- (i) Analytical Procedures
- (ii) Inquiry
- (iii) Inspection
- (iv) Observation
- (v) Re-calculation

Required:

(a) For EACH of the above procedures:

- (i) Explain its use in gathering audit evidence.** (5 marks)
- (ii) Describe one example for the audit of BearsWorld.** (5 marks)

(b) Discuss the suitability of each procedure for BearsWorld, explaining the limitations of each. (15 marks)

(25 marks)

QUESTION 4

You are the audit manager of Tela & Co, a medium sized firm of accountants. Your firm has just been asked for assistance from Jumper & Co, a firm of accountants in an adjacent country. This country has just implemented the internationally recognised codes on corporate governance and Jumper & Co has a number of clients where the codes are not being followed. One example of this, from SGCC, a listed company, is shown below. As your country already has appropriate corporate governance codes in place, Jumper & Co have asked for your advice regarding the changes necessary in SGCC to achieve appropriate compliance with corporate governance codes.

Extract from financial statements regarding corporate governance:

Mr Sheppard is the Chief Executive Officer and board chairman of SGCC. He appoints and maintains a board of five executive and two non-executive directors. While the board sets performance targets for the senior managers in the company, no formal targets or review of board policies is carried out. Board salaries are therefore set and paid by Mr Sheppard based on his assessment of all the board members, including himself, and not their actual performance.

Internal controls in the company are monitored by the senior accountant, although detailed review is assumed to be carried out by the external auditors; SGCC does not have an internal audit department.

Annual financial statements are produced, providing detailed information on past performance.

Required:

Write a memo to Jumper & Co which:

- (a) Explains why SGCC does not meet international codes of corporate governance**
- (b) Explains why not meeting the international codes may cause a problem for SGCC, and**
- (c) Recommends any changes necessary to implement those codes in the company.**

(25 marks)

End of Question Paper