

UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING

SUPPLEMENTARY EXAMINATION QUESTION PAPER

DEGREE/YEAR OF STUDY : B COM IV

TITLE OF PAPER : AUDITING 2

COURSE CODE : AC 418

TOTAL MARKS : 100 MARKS

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

**(a) Describe external auditor's responsibilities and the work that the auditor should perform in relation to the going concern status of companies.** (6 marks)

**(b) Describe the possible audit reports that can be issued where the going concern status of a company is called into question; your answer should describe the circumstances in which they can be issued.** (6 marks)

Corsco is a large telecommunications company that is listed on a stock exchange. It is highly geared because, like many such companies, it borrowed a large sum to pay for a licence to operate a mobile phone network with technology that has not proved popular. The company's share price has dropped by 50% during the last three years and there have been several changes of senior management during that period. There has been considerable speculation in the press over the last six months about whether the company can survive without being taken over by a rival. There have been three approaches made to the company by other companies regarding a possible takeover but all have failed, mainly because the bidders pulled out of the deal as a result of the drop in share prices generally.

The company has net assets, but has found it necessary to severely curtail its capital investment program. Some commentators consider this to be fundamental to the future growth of the business, others consider that the existing business is fundamentally sound. It has also been necessary for the company to restructure its finances. Detailed disclosures of all of these matters have always been made in the financial statements. No reference has been made to the going concern status of the company in previous auditor's reports on financial statements and the deterioration in circumstances in the current year is no worse than it has been in previous years.

### Required:

**(c) On the basis of the information provided above, describe the audit report that you consider is likely to be issued in the case of Corsco, giving reasons.** (6 marks)

**(d) Explain the difficulties that would be faced by Corsco and its auditors if Corsco's audit report made reference to going concern issues.** (7 marks)

**(25 marks)**

## QUESTION 2

Fizzipop manufactures and distributes soft drinks. Its inventories are controlled using a real-time system which provides accurate records of quantities and costs of inventories held at any point in time. This system is known within the company as the 'Stockpop' system and it is integrated with the purchases and sales system. Fizzipop has an internal audit department whose activities encompass inventories.

No year-end inventory count takes place. Inventories are held in several large warehouses where non-stop production takes place.

Your firm is the external auditor to Fizzipop and you have been asked to perform the audit of inventories. Inventories include finished goods and raw materials (water, sugar, sweeteners, carbonating materials, flavourings, cans, bottles, bottle tops, fastenings and packaging materials).

Your firm, which has several offices, wishes to rely on the 'Stockpop' system to provide the basis of the figure to be included in the financial statements for inventories. Your firm does not wish to ask the company to conduct a year-end inventory count.

**Required:**

**(a) Describe the audit tests that you would perform on the 'Stockpop' system during the year in order to determine whether to rely on it as a basis for the raw materials and finished goods figures to be included in the financial statements.** (13 marks)

NB: You are not required to deal with work in progress.

**(b) Describe the audit tests you would perform on the records held by Fizzipop at the year-end to ensure that raw materials and finished goods are fairly stated in the financial statements.** (12 marks)

**(25 marks)**

**QUESTION 3**

Towards the end of an audit, it is common for the external auditor to seek a letter of representation (written representations) from the management of the client company.

**Required:**

**(a) Explain why auditors seek letters of representation.** (6 marks)

**(b) List the matters commonly included in the letter of representation.** (8 marks)

**(c) Explain why it is important to discuss the content of the letter of representation at an early stage during the audit.** (4 marks)

**(d) Explain why management is sometimes unwilling to sign a letter of representation and describe the actions an external auditor can take if management refuses to sign a letter of representation.** (7 marks)

**(25 marks)**

**QUESTION 4**

ISA 500 *Audit Evidence* (Revised) states that management implicitly or explicitly makes assertions relating to the various elements of financial statements including related disclosures. Auditors may use three categories of assertions to form a basis for risk assessments and the design and performance of further audit procedures. The three categories suggested by ISA 500 relate to (i) classes of transactions, (ii) account balances, and (iii) presentation and disclosure.

One assertion applicable to all three categories is *completeness*: that all transactions, events, assets, liabilities, equity interests and disclosures that should be included, are included in the financial statements.

**Required:**

**(a) List and describe SIX financial statement assertions, other than completeness, used by auditors in the audit of financial statements.** (6 marks)

**(b)** Boulder is a small company that manufactures hosiery products. It employs approximately 150 staff, all of whom are paid by bank transfer.

Temporary factory staff are hired through an agency and are paid on piece rates (i.e. for the number of items that they produce or process) on a weekly basis. Supervisors at Boulder authorise documentation indicating the number of items produced or processed by agency staff. The agency is paid by bank transfer and it, not Boulder, is responsible for the deduction of tax and social insurance.

Permanent factory staff are paid on a weekly basis on the basis of hours worked as evidenced by clock cards.

Administration and sales staff are paid a monthly salary. The two directors of the company are also paid a monthly salary.

Sales staff are paid a quarterly bonus calculated on the basis of sales. Directors are paid an annual bonus based on profits.

You will be performing the audit of the financial statements for the year ending 31 March 2018 and you will be responsible for the figures in the financial statements relating to payroll.

**Required:**

**Describe the substantive audit procedures you will perform on:**

**(i) the payroll balances in the statement of financial position of Boulder;** (12 marks)

**(ii) the payroll transactions in the statement of comprehensive income of Boulder.**

(7 marks)

**End of Question Paper**