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**COURSE CODE: ACF 416/AC 418 (S) 2019**

**UNIVERSITY OF ESWATINI**

**DEPARTMENT OF ACCOUNTING**

**SUPPLEMENTARY EXAMINATION QUESTION PAPER**

**DEGREE/YEAR OF STUDY : B COM IV**

**TITLE OF PAPER : AUDITING II**

**COURSE CODE : ACF 416/AC 418**

**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**

Amber 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 'Comms' system and it is integrated with the purchases and sales system. Amber 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 Amber 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 'Comms' 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 SIX audit tests that you would perform on the 'Comms' 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 SIX audit tests you would perform on the records held by Amber at the year-end to ensure that raw materials and finished goods are fairly stated in the financial statements.**

(12 marks)

(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;**
  - (iii) **List the reconciling items highlighted by external confirmation of accounts receivable.**

(8 marks)

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

(5 marks)

(c) Puppies (Pty) Ltd is a small company which manufactures high quality shoes and sells them to small retailers. This is your first year as auditor. Puppies 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 E750, 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 key audit work you will perform on accounts receivable and bad debts at Puppies.**

(12 marks)

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

(25 marks)

**QUESTION 3**

**(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)

Camtha Co 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 Camtha, giving reasons.** (6 marks)

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

**(25 marks)**

**QUESTION 4**

**(a) Describe the auditor's responsibility for subsequent events occurring between:**

**(i) The year-end date and the date the auditor's report is signed; and**

**(ii) The date the auditor's report is signed and the date the financial statements are issued.** (7 marks)

**(b)** Savemore Co operates a chain of food wholesalers across the country and its year end was 31 March 2019.

The final audit is nearly complete and it is proposed that the financial statements and audit report will be signed on 13 June 2019. Revenue for the year is E78 million and profit before taxation is E7.5 million. The following events have occurred subsequent to the year end.

**Receivable**

A customer of Savemore Co has been experiencing cash flow problems and its year-end balance is E0.3 million.

The company has just become aware that its customer is experiencing significant going concern difficulties.

Savemore believe that as the company has been trading for many years, they will receive some, if not full, payment from the customer; hence they have not adjusted the receivable balance.

**Lawsuit**

A key supplier of Savemore Co is suing them for breach of contract. The lawsuit was filed prior to the year end, and the sum claimed by them is E1 million. This has been disclosed as a contingent liability in the notes to the financial statements; however correspondence has just arrived from the supplier indicating that they are willing to settle the case for a payment by Savemore Co of E0.6 million. It is likely that the company will agree to this.

**Warehouse**

Savemore Co has three warehouses; following extensive rain on 10 May 2019 significant rain and river water flooded the warehouse located in Bass. All of the inventory was damaged and has been disposed of. The insurance company has already been contacted. No amendments or disclosures have been made in the financial statements.

**Required:**

**For each of the three events above:**

**(i) discuss whether the financial statements require amendment;**

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**(ii) describe audit procedures that should be performed in order to form a conclusion on the amendment; and**

**(iii) explain the impact on the audit report should the issue remain unresolved.** (18 marks)

*Note: The total marks will be split equally between each event.*

**(25 marks)**

**End of Question Paper**