



UNIVERSITY OF ESWATINI

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING AND FINANCE

MAIN EXAMINATION

AUGUST 2020

TITLE OF PAPER : ADVANCED AUDITING

COURSE CODE : ACF632

TOTAL MARKS : 100 MARKS

TIME ALLOWED : THREE (3) HOURS

- INSTRUCTIONS**
- 1 There are six (6) questions, answer any five (5)
 - 2 Begin the solution to each question on a new page.
 - 3 The marks awarded for a question are indicated at the end of each question.
 - 4 Show the necessary working.
 - 5 Calculations are to be made to zero decimal places of accuracy, unless otherwise instructed.

Note: You are reminded that in assessing your work, account will be taken of accuracy of the language and general quality of expression, together with layout and presentation of your answer.

THIS PAPER IS NOT TO BE OPENED UNTIL PERMISSION HAS BEEN GRANTED BY THE INVIGILATOR OR SUPERVISOR.

SPECIAL REQUIREMENTS: NONE

QUESTION 1

a) *ISA: 505 External Confirmations* states that 'the auditor should determine whether the use of external confirmations is necessary to obtain sufficient appropriate audit evidence at the assertion level'. An Auditor may obtain external confirmations from third parties to corroborate the audit evidence already available with the auditor. The Auditor shall determine whether positive or negative request is appropriate given the condition.

Responses or events of non-responses are required to be evaluated. Responses may be unreliable if they are served indirectly to the auditor, not served by the intended person or transmission is compromised and the auditor may have to perform additional procedures to resolve doubts and suspicion. In events of non-responses or management refusal to permit the auditor to seek confirmations, the auditor shall assess if modification in the auditor's report is necessary.

Required:

Explain **FOUR (4)** examples of external confirmations and for each one identify: an audit assertion that the external confirmation supports; and an audit assertion that the external confirmation does NOT support. **(10 marks)**

b) Mfundo & Co., a firm of Auditors with a number of clients listed on the Eswatini Stock Exchange, recently held a staff training session on quality control. During the session, staff raised matters from their experience relating to the ethical code on independence. Some of these matters are outlined below:

i) Shortly before commencing the final audit of a large listed company, a Junior Staff member on the audit team inherited a substantial number of shares in that company. No action was taken because, although representing a large investment for the staff member concerned, the number of shares was totally immaterial with respect to the company. Moreover, the partner knew that if the company's results is announced, there will be a rise in the share price and he did not think it was fair to require the staff member to sell them beforehand.

ii) The Management Accountant of another listed client company had an accident and was away from work for three months. At the time of the accident, the audit senior was winding up the prior year's audit. Given his familiarity with the company's management accounting system, it was agreed that he would take over as Management Accountant for the three months.

Required:

Discuss whether Mfundo & Co had complied with the IFAC's Code of Ethics or had acted unprofessionally in any other way with respect to each of the above scenarios. **(10 marks)**

[Total: 20 marks]

QUESTION 2

The information in the financial statements of your client, Honesty Company Limited, represents claims by management in relation to its responsibility to prepare financial statements which gives a true and fair view of the company's state of affairs and results of operations for the year under review. These claims are referred to as financial statements assertions.

Required:

As a member of the engagement team charged with the audit of the client's financial statements for the year ended October 31, 2019:

- a) Outline the audit objectives for the audit of stock (inventories) in the financial statements. Your answer should relate to the financial statement assertions. (8 marks)
- b) Discuss **FOUR (4)** sources from which evidence can be obtained to confirm the quantities and value of stocks. (8 marks)
- c) Explain why stocks present high audit risk (4 marks)

(Total: 20 marks)

QUESTION 3

ISA 315 requires the auditor to perform risk assessment procedures to provide a basis for identifying and assessing the risk of material misstatement. These risk assessment procedures should include appropriate analytical procedures. You are an audit team leader at an audit firm undertaking an external audit of the financial statements of a large public hospital. As part of your planning you are designing some analytical procedures to perform prior to the first visit to the hospital to begin the on-site audit. Public hospitals are subject to a funding system called "Income by Outcome" under which a set fee is paid for each procedure performed according to a nationally determined tariff. Currently your focus is on the revenue and costs from providing surgical services as this area is particularly closely regulated by central government and the focus of ever more stringent efficiency requirements. Your audit objectives in this area include the following;

To verify that all the relevant costs of the provision of surgical procedures have been included in the financial statements;

To verify that the hospital's costs of providing surgical services are sustainable in the context of the fees received for providing the different types of surgical procedure; and

To verify that appropriate management control has been exercised over the costs of the provision of surgical procedures.

ISA 700, *Forming an Opinion and Reporting on Financial Statements*, contains a number of requirements that must be met before an unmodified opinion on the financial statements may be provided.

Required

- (a) Formulate and describe an appropriate analytical procedure to meet **each** of the audit objectives listed above, clearly explaining what further action you would take after undertaking the procedure.

(10 marks)

- b) Briefly describe the areas auditors are required to consider under ISA 700. (6 marks)
- c) Explain why ISA 320, *Materiality in Planning and Performing an Audit*, makes a distinction between planning and performance materiality. (4 marks)

[Total 20 marks]

QUESTION 4

You are the audit manager of an audit firm where the purpose of an external audit and its role are not well understood. You have been asked to write some material for inclusion in your firm's training materials dealing with these issues in the audit of large companies.

Required:

- a). In your paper explain the purpose of an external audit and its role in the audit of large companies, for inclusion in your firm's training materials. (10 marks)

The IFAC international Ethics Standards Board for Accountant (IESBA) Code of Ethics for Professional Accountants set out the five fundamental principles of professional ethics and provides a conceptual framework for applying those principles. Professional Accountants must apply this conceptual framework to identify threats to compliance with the principles, evaluate their significance and apply appropriate safeguards to eliminate or reduce them so that compliance is not compromised.

Required:

- b). Identify **FIVE** major threats identified in the code of ethics giving examples of each. (5 marks)

- c) Briefly explain **FIVE** duties and **FIVE** rights of an auditor Companies Act, 2009, (Act 8). (5 marks)

[Total: 20marks]

QUESTION 5

- a) BDE Company Limited operates a hotel providing accommodation, leisure facilities and restaurants. Its year ends on 31 March. You are the senior associate of ABC and Associates and are currently preparing the audit programmes for the year-end audit of BDE Company Limited. You are reviewing the notes of last week's meeting between the audit manager and finance director where two material issues were discussed.

Depreciation

BDE Company Limited incurred significant capital expenditure during the year for refurbishing the restaurant facilities for the hotel.

The finance director has proposed that the new leisure equipment should be depreciated over 10 years using the straight-line method.

Food poisoning

BDE's directors received correspondence in January from a group of customers who attended a wedding at the hotel. They have alleged that they suffered severe food poisoning from food eaten at the hotel and are claiming substantial damages. BDE's lawyers have received the claim and believe that the lawsuit against the company is unlikely to be successful.

Required:

- i) Describe *substantive procedures* to obtain *sufficient and appropriate audit evidence* in relation to the above two issues. (6 marks)
- ii) List and explain the purpose of three items that should be included on every working paper prepared by the audit team during the audit of depreciation and food poisoning of BDE Company Limited. (3 marks)
- b)
- i) Identify and explain two financial statement assertions relevant to account balances at the year-end; and (2 marks)
- ii) For each identified assertion, describe a substantive procedure relevant to the audit of year-end inventory. (4 marks)
- c)
- i) *International Standard on Auditing 560: Subsequent Events* deals with auditor's responsibility towards events that occur after reporting date and especially before the auditor's report is issued.

The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in the financial statements have been identified.

Required:

Explain **FIVE** audit procedures to test subsequent events. (5 marks)

(Total: 20 marks)

QUESTION 6

a. *ISA 265 Communicating deficiencies in internal control with those charged with Governance and Management*. Auditors must report deficiencies in internal control with those charged with governance and management.

Required:

- a. Explain clearly what is *management letter*, indicating the contents of such a letter. (5 marks)
- b. Briefly explain what is meant by the '*Going Concern Concept*' and describe the test and procedures that the auditor needs to perform to form an opinion on management's conclusion that the company is a going concern as specified by *ISA 570 Going Concern*. (6 marks)
- c. Distinguish the three types of modified opinions that the auditor may issue on financial statements audited by him. (6 marks)
- d. State with details **TWO** circumstances under which an auditor may issue a qualified opinion.

(3 marks)

[Total: 20 marks]