

Implementing Audit Procedures (International Stream)

ACCA CERTIFIED ACCOUNTING TECHNICIAN EXAMINATION

ADVANCED LEVEL

MONDAY 12 DECEMBER 2005

QUESTION PAPER

Time allowed **3 hours**

ALL FOUR questions are compulsory and MUST be answered

Do not open this paper until instructed by the supervisor

This question paper must not be removed from the examination hall

The Association of Chartered Certified Accountants

Paper T8(INT)



ALL FOUR questions are compulsory and MUST be attempted

1 (a) **State the FIVE components of internal control set out in ISA 315 *Understanding the Entity and its Environment and Assessing the Risks of Material Misstatement*.** (5 marks)

(b) **State FOUR objectives of the internal control which should be exercised over a sales and trade receivables system.** (4 marks)

(c) Haydn Co is a limited liability company and wholesale supplier of stationery products. It commenced trading in 2001 and now has 60 employees with separate sales and accounts departments. However at a recent board meeting, concern was expressed at some aspects of the company's internal control, including those relating to sales and trade receivables.

Jon May, the sales director is an excellent salesman and has been largely responsible for the company's growth since 2001 and for the implementation of the control activities exercised over the company's sales and trade receivables system. The following policies and procedures form part of the control activities exercised over that system.

1. Haydn Co uses a networked integrated sales and general ledger accounts system. The company's accountant and assistant accountant, together with Jon May and the trade receivables department clerks (sales clerks) have full access to all sales ledger files including the master file.
2. Requests from potential customers to open a credit account are forwarded to Jon May, who carries out full credit checks before deciding whether to grant a credit facility. When credit facilities are granted a sales clerk updates the sales ledger master file with the new customer details. Credit limits are not applied to customer accounts as Jon May considers this to be a restricting factor in achieving sales targets. Slow or late paying customers are pursued for payment by Jon May.
3. Customer orders received, in writing or by telephone, are directed to a sales clerk. After establishing that a trade receivables ledger account exists, the clerk uses a sales invoicing programme to generate a pre-numbered sales invoice and accompanying goods despatch note addressed to customers for products as ordered. The programme prices sales invoices automatically using authorised prices stored in a standing data file. Full access to this file is restricted to Jon May and the sales clerks.
4. Sales clerks post invoices as prepared to Haydn Co's trade receivables ledger, and the automated accounting system immediately updates the company's general ledger with the trade receivables ledger postings. On a daily basis:
 - all invoices are mailed by the sales clerks to customers and the goods despatch notes are forwarded to the stores department to accompany goods as and when despatched.
 - a copy of each invoice is forwarded to the assistant accountant who is responsible for dealing with customers' invoice queries, the issue of sales credit notes, as he deems appropriate, and the posting of credit notes to the trade receivables ledger.

Required:

From the information provided on the sales and trade receivables system of Haydn Co:

- (i) **Identify FOUR weaknesses in the system;**
- (ii) **Describe the implication of each weakness identified;**
- (iii) **Recommend improvements to address the weakness.**

You should assume that there is an adequate number of employees to implement any recommendations you make.

(16 marks)

(25 marks)

- 2 You have been assigned to your firm's audit of the financial statements of Brahms Co for the year ending 31 December 2005.

At the planning meeting, attended by all members of the audit team, the audit manager confirmed that the firm would adopt a risk-based approach to the audit, and for the benefit of the junior members of the team he explained the use of the audit risk model comprising inherent risk, control risk and detection risk. The manager also explained the importance of preparing good audit working papers and confirmed that he expected the header of every working paper to be properly completed.

Required:

- (a) Explain what is meant by the term 'a risk-based approach' to an audit. Your answer should include commentary on the audit risk model. (14 marks)
- (b) Briefly explain the purpose of audit working papers and comment on the matters to be considered generally, in assessing the extent of working papers to be prepared. (7 marks)
- (c) List the information that should be included on the header of every working paper prepared in connection with the audit of the financial statements of Brahms Co for the year ending 31 December 2005.

(4 marks)

(25 marks)

- 3 (a) ISA 500 (Revised) *Audit Evidence* states that the reliability of audit evidence is influenced by its source and by its nature and is dependent on the individual circumstances under which it is obtained. The standard then states five generalisations about the reliability of audit evidence which may be useful.

Required:

State the FIVE generalisations about the reliability of audit evidence.

(10 marks)

- (b) ISA 500 (Revised) explains that the auditor should use management assertions to form a basis for the assessment of risks of material misstatement and the design and performance of further audit procedures.

Assertions about different classes of transactions and events for a period under audit are categorised as follows:

1. Occurrence.
2. Completeness.
3. Accuracy.
4. Cut-off.
5. Classification.

Required:

For FOUR of the above categories, state the implicit or explicit management assertions made about classes of transactions and events for the period under audit.

(6 marks)

- (c) Describe SIX typical substantive procedures the auditor of the financial statements of a manufacturing company may carry out to verify the completeness of different classes of transactions and account balances. You are required to describe only SIX procedures in total and should set out your answer in the following format:

Area of Financial Statements

Procedure to verify completeness

(9 marks)

(25 marks)

4 A university recently held a recruitment fair on its campus and invited local firms of auditors to attend, to interview students for audit junior positions. As an existing audit junior at your firm, you attended the recruitment fair to promote your firm and to talk informally to students. In conversation with you, students made several enquiries on audit matters.

Required:

In response to enquiries from students:

- (a) **State, with reasons, FOUR personal qualities which a qualified external auditor should possess.** (6 marks)
- (b) **Explain what is meant by the term 'materiality'.** (3 marks)
- (c) (i) **Identify FOUR different situations during the course of an audit, where an auditor may need to obtain audit evidence in the form of reports, opinions, valuations or statements from an expert;**
and
(ii) **For each situation identified (above), provide a practical example.** (6 marks)
- (d) (i) **Identify FOUR matters reflected in the financial statements of a limited company where management typically make accounting estimates;** (6 marks)
and
(ii) **Outline the approaches that an auditor should adopt in the audit of an accounting estimate.** (4 marks)
- (25 marks)**

End of Question Paper