

Implementing Audit Procedures (International Stream)

ACCA CERTIFIED ACCOUNTING TECHNICIAN EXAMINATION

ADVANCED LEVEL

MONDAY 11 DECEMBER 2006

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 Rhodes Co provides entertainment for holidaymakers in a large resort, by staging local culture evenings at its indoor arena. The entertainment is provided every evening throughout the holiday season and comprises members of the local community performing dance routines in traditional costume and others demonstrating acrobatic skills.

The arena forms part of a building which houses Rhodes Co's administrative and accounting functions together with a snack bar used by customers attending the culture evenings.

The company accepts only cash payment from culture evening customers and, in addition to staff who carry out specific tasks, a manager and three assistant managers are in attendance nightly to supervise activity at the arena.

The following controls are exercised over the income from the culture evenings:

Entry Charges

The company does not issue entry tickets. Customers gain entry into the arena's audience area through a turnstile located alongside the arena cashier's kiosk in the foyer of the arena building. As customers pay and enter through the turnstile, a meter connected to it and located inside the kiosk, automatically counts the number of entrants. The kiosk does not have a cash register but it is furnished with a cash drawer, containing a small permanent cash float, for use by the cashier. At the end of each night the cashier ensures that the total cash takings in the drawer equate to the entrants counted on the turnstile meter multiplied by the standard entry charge as set by the directors of Rhodes Co. After zeroing the turnstile meter for future use she then e-mails, for the next day attention of the company's accounts department, confirmation of the number of customer entrants and the total kiosk takings. Prior to finishing her work the cashier puts the takings into a designated cash wallet and deposits the wallet in the secure night safe of Rhodes Co. The safe is of a hole in the wall design, located in a secure room inside the company's premises and allows 'deposit only' access to arena employees with full access being granted to specified accounts department employees of Rhodes Co who are responsible for the removal of deposits from the safe.

Snack Bar Income

This comprises snack bar sales and income from vending machines located in the snack bar area. The bar's automated cash register (till), containing a permanent small cash float, is operated by the snack bar manager and his staff, all of whom have had training in its use. At the end of each night the snack bar manager obtains a listing from the till of all transactions registered and compares the total to the actual cash takings, which he counts without assistance, writing a note on the listing to explain any differences between the totals. He then empties the takings from the vending machines and puts these together with those from the snack bar sales and the till listing into a designated wallet, prior to depositing the wallet in the night safe of Rhodes Co.

Required:

- (a) **State THREE objectives of the internal controls that should be exercised over cash sales.** (3 marks)
- (b) **With regard to the controls exercised over sales income received from the culture evenings:**
 - (i) **Explain why the auditors of Rhodes Co could not rely on the controls as a basis for verifying completeness of sales income;** (7 marks)
 - (ii) **Recommend SIX improvements to address specific weaknesses in the controls over entry charges and the snack bar income.** (9 marks)
- (c) **State FOUR controls that Rhodes Co should employ over the subsequent access to and recording and banking of the sales income from the culture evenings as deposited into the company's night safe.** (6 marks)

Note: You should assume that there are a sufficient number of employees to implement any required controls, in (b) and (c) above.

(25 marks)

- 2** The auditors of Malaga Co, a large engineering company are now in the course of auditing the company's financial statements for the year ended 31 October 2006.

At the audit briefing meeting, the audit manager made the following statements:

- (i) 'whilst we are all aware of the benefits that Malaga Co should have gained from using a computer-based accounting system, we need to be alert to the specific risks that a computer-based accounting system poses to an entity's internal controls.'
- (ii) 'we will be using audit software.'

Required:

- (a) **State FOUR benefits that Malaga Co should have gained from using a computer-based accounting system.**
(4 marks)
- (b) **State SIX specific risks that the use of a computer-based accounting system poses to an entity's internal controls.**
(9 marks)
- (c) **Explain the term 'audit software'.**
(2 marks)
- (d) **Describe FIVE functions performed by audit software and for each function suggest how it could be used for a specific task by the external auditors of Malaga Co.**
(10 marks)

(25 marks)

- 3** Paphos Co trades as a department store. It has 85 employees, some of whom are hourly paid, and a large administration and accounts department with appropriate segregation of duties, supervisory controls and authorisation levels throughout the various accounting functions.

Your firm is auditing the company's financial statements for the year ended 30 September 2006 and, together with an inexperienced audit junior, you have been assigned to the audit of wages. The company pays all employees on a weekly basis, using a computerised payroll system to process wages, prior to making payment directly into employees' bank accounts. Wages costs are reported as \$1.62 million in the financial statements of Paphos Co for the year ended 30 September 2006.

You are about to commence tests of control on the wages system. However, from discussions with the audit junior, it is apparent that he does not understand the concept of obtaining evidence to verify the assertions made implicitly or explicitly by management and contained in a company's financial statements. Similarly, he does not understand that there are several recognised methods that an auditor may adopt when selecting a sample of items to be tested from a population.

Required:

- (a) **State FOUR financial statement assertions made by the directors of Paphos Co, in reporting wages costs of \$1.62 million in the financial statements of the company for the year ended 30 September 2006.** (6 marks)
- (b) **Explain the following terms as applied to audit sampling methods and contained in ISA 530 *Audit Sampling and Other Means of Testing*:**
- (i) **Random selection;** (2 marks)
 - (ii) **Haphazard selection;** (2 marks)
 - (iii) **Systematic selection.** (3 marks)
- (c) **Identify SIX tests of control that you should carry out in connection with the audit of the reported wages costs in the financial statements of Paphos Co for the year ended 30 September 2006.** (12 marks)

(25 marks)

4 'The auditors of a company operating a supermarket chain, could be more effectual by making use of appropriate analytical procedures, and by using the work of internal auditors and the work of an expert.'

Required:

- (a) Identify the stage or stages of an audit, during which an audit firm should use analytical procedures and explain the purpose of the use at each stage, as stated in ISA 520 *Analytical Procedures*. (6 marks)
- (b) For each of the efficiency measures listed below, set out the accounting ratio that should be used by a firm of auditors when analysing the financial statements of a company operating a supermarket chain:
- (i) Working capital turnover;
 - (ii) Average inventory turnover;
 - (iii) Payment period for trade payables;
 - (iv) Total assets turnover;
 - (v) Non-current assets turnover. (5 marks)
- (c) (i) Identify FOUR activities in which the internal audit department of a company, operating a supermarket chain, may be typically involved;
- (ii) For each activity identified above, provide a practical example. (8 marks)
- (d) (i) Identify THREE areas in the financial statements of a company, operating a supermarket chain, where an audit firm may need to rely on the work of an expert;
- (ii) For each area identified above, provide a practical example. (6 marks)

(25 marks)

End of Question Paper