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ACCA – Paper F8 Audit and Assurance September 2015 to June 2016 Interim Assessment

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Notice to Markers

- 1 When commenting about the script performance, please ensure on individual questions and on overall assessment your comments cover areas of examination technique including:

<ul style="list-style-type: none">• Time management	<ul style="list-style-type: none">• Handwriting	<ul style="list-style-type: none">• Presentation and layout	<ul style="list-style-type: none">• Use of English
<ul style="list-style-type: none">• Points clearly and concisely made	<ul style="list-style-type: none">• Relevance of answers to question	<ul style="list-style-type: none">• Coverage and depth of answer	<ul style="list-style-type: none">• Accuracy of calculations
<ul style="list-style-type: none">• Calculations cross-referenced to workings	<ul style="list-style-type: none">• All parts of the requirement attempted	<ul style="list-style-type: none">• Length of answers equates to marks available	<ul style="list-style-type: none">• Read the question carefully

- 2 For each question, please provide suitable constructive comments

Question Number	General Comments	Exam Technique Comments

ACCA INTERIM ASSESSMENT

Audit and Assurance

September 2015 to June 2016

Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

This paper is divided into two sections:

Section A – ALL TWELVE questions are compulsory and MUST be attempted

Section B – ALL SIX questions are compulsory and MUST be attempted

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall

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Paper F8

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Section A – All TWELVE questions are compulsory and MUST be attempted

- 1 Which of the following correctly identifies the three parties involved in an assurance engagement?**
- A Practitioner, audit committee, responsible party
 - B Practitioner, intended user, regulator
 - C Practitioner, intended user, responsible party
 - D Practitioner, intended user, subject matter **(2 marks)**
- 2 Which TWO of the following are reasons why auditors can never provide absolute assurance?**
- (i) Auditors do not test all transactions and balances
 - (ii) Financial statements contain subjective estimates and other judgemental matters
 - (iii) Auditors need to make a profit on each audit
 - (iv) Audit evidence is inherently biased
- A (i) and (ii)
 - B (ii) and (iii)
 - C (ii) and (iv)
 - D (iii) and (iv) **(2 marks)**
- 3 Which TWO of the following people are eligible to act as an external auditor of a company?**
- (i) Member of ACCA
 - (ii) Group Financial Controller of the company
 - (iii) Member of the ACCA who has been allowed by their rules to act
 - (iv) Someone authorised by the state to act as external auditor
- A (i) and (ii)
 - B (ii) and (iii)
 - C (ii) and (iv)
 - D (iii) and (iv) **(2 marks)**

4 Which TWO of the following are statutory rights of auditors?

- (i) To speak at the monthly board meetings on financial matters
- (ii) To receive information and explanations necessary for the audit
- (iii) To receive notice of any general meetings of the members
- (iv) Access to the company's online banking facilities at any reasonable time

- A (i) and (ii)
- B (ii) and (iii)
- C (ii) and (iv)
- D (iii) and (iv)

(2 marks)

5 Which TWO of the following are identified in the ACCA Code of Ethics as threats to objectivity?

- (i) Advocacy
- (ii) Conflict of interest
- (iii) Insider dealing
- (iv) Self interest

- A (i) and (ii)
- B (ii) and (iv)
- C (i) and (iv)
- D (iii) and (iv)

(2 marks)

6 Sterling & Co have recently been appointed as the auditors of Anfield Co, an unlisted company. Anfield have asked if Sterling & Co would assist with the preparation of the financial statements. Which of the following statements, if any, are correct?

- (i) Sterling & Co could not adopt any safeguards that would adequately manage the self review threat.
- (ii) Sterling & Co could only accept this work if the preparation involved processing a very small number of year end journals.

- A (i) only
- B Both (i) and (ii)
- C (ii) only
- D Neither (i) or (ii)

(2 marks)

- 7 Tate & Co are the external auditors of Liberty Co. Liberty have asked if Tate & Co would represent them in a legal dispute with the tax authorities. Which of the following statements are correct?**
- (i) Tate & Co should accept this work as it is unlikely to generate recurring fee income and therefore will not result in fee dependency.
 - (ii) This would represent an advocacy threat and Tate & Co should politely decline the offer to act as legal representatives.
- A (i) only
B Both (i) and (ii)
C (ii) only
D Neither (i) or (ii) **(2 marks)**
- 8 Which TWO of the following are sections that would appear in an engagement letter?**
- (i) Responsibilities of management
 - (ii) Materiality level for the audit
 - (iii) Significant audit risks
 - (iv) Basis of the fees
- A (i) and (ii)
B (ii) and (iii)
C (i) and (iv)
D (iii) and (iv) **(2 marks)**
- 9 The auditor must test the controls of every audit client. True or false?**
- A True
B False **(1 mark)**
- 10 Which of the following is a financial statement assertion relevant to account balances?**
- A Rights and obligations
B Classification
C Cut-off
D Accuracy **(1 mark)**
- 11 Which of the following is not a procedure as stated in ISA 500 Audit Evidence?**
- A Recalculation
B Inspection
C Analytical procedures
D Review **(1 mark)**

12 Which of the following is an example of a general IT control?

- A Back ups
- B Reconciliation
- C Batch total
- D Exception report

(1 mark)

Section B – ALL six questions are compulsory and MUST be attempted.

- 1 (a) **Define ‘independence’ and explain the need for an assurance provider to be independent. (2 marks)**
- (b) The fundamental principle of objectivity requires that members do not allow bias, conflicts of interest or undue influence of others to override professional or business judgements.

Required:

Explain the fundamental principles in the IFAC and ACCA Codes of Ethics, other than objectivity. (4 marks)

- (c) ISA 240 *the Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements* describes the responsibilities of both management and the auditor with regard to preventing and detecting fraud.

Required:

Explain the responsibilities of both management and auditors with regard to the prevention and detection of fraud. (4 marks)

(Total: 10 marks)

- 2 You work for a firm of auditors which has seven offices throughout England and Wales. The firm's largest client, in terms of fee income, is Mart Co, a listed company which has grown steadily through a mixture of organic growth and acquisition of companies in the same industry sector.

Your firm has acted for this client since its incorporation 20 years ago and, in addition to the statutory audit, provides a range of non-audit services including tax planning (for the company and its individual directors) and consultancy work in respect of Mart's acquisition policy.

Earlier this year, the finance director of Mart retired and was succeeded by a former member of your firm's staff who had managed the audit of Mart for the preceding four years.

Required:

- (i) Explain FIVE ethical threats which may affect the auditor of Mart Co. (5 marks)
- (ii) For each threat, explain how it might be reduced to an acceptable level. (5 marks)

(Total: 10 marks)

- 3** You are a senior manager at Midway Co, a busy medium-sized audit firm with three offices in the central counties of England and over 100 employees. Following the unexpected resignation of their previous auditor part way during the financial year, the firm has been asked to tender for the provision of statutory audit and other services to Border Travel.

Border Travel is an unlisted company based on the south coast that provides package coach holidays and short breaks in Scotland.

Border Travel has proven to be popular with pensioners but has also gained success in promoting group trips to stag and hen parties and corporate outward bounds clients.

As a result the company is growing fast and would, if the tender is successful, provide a significant source of fee income for the firm. The finance director has explained that the company would like the successful firm to provide statutory audit services and assistance with the preparation of the financial statements. The company is also keen to improve its internal risk assessment procedures and would welcome an IT systems review. Your firm does not have much experience in the travel sector.

Required:

Describe the steps an audit firm should perform prior to accepting a new audit engagement. For each step, explain the relevance to Midway Co in relation to the audit of Border Travel.

(Total: 10 marks)

- 4 The directors of Lopit, a newly-formed company, have written to you with a view to securing your services as auditor. Within their letter, you note the following comments:

'Your duties and rights as auditor will be determined by the board of our company. In the main, these duties are in line with the usual legal requirements, but in the event of conflict or exclusion we will indemnify you against any legal action brought as a consequence of the position adopted. The board also retains the right to dismiss you at any time without necessarily disclosing the reasons for their action.

The letter also addresses the matter of fees. The directors wish to keep costs as low as possible in the early stages of the business. As a result, they have expressed interest in opting for a limited assurance report which they understand will require only a simple review of their financial statements and therefore warrant a reduced fee.

Required:

- (a) In accordance with *ISA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, describe the overall objectives of the auditor. (3 marks)
- (b) State the legal rights of an auditor of a limited company. (2 marks)
- (c) Discuss whether directors have the authority to dismiss auditors and explain the appropriate procedures required to remove an auditor. (5 marks)

(Total: 10 marks)

- 5 (a) ISA 500 *Audit Evidence* states that 'the objective of the auditor is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base an audit opinion.'

Required:

Explain what is meant by 'sufficient appropriate' audit evidence. (4 marks)

- (b) Collins Cosmetics is a long-established family company that manufactures perfumes. These are sold to customers who re-package and market them under their own brand names. The company has five manufacturing units spread across its home country. The machinery in two of these units has recently been upgraded to improve the speed of the production line.

Fred Goodwin, who had been managing director for 21 years, died just over a year ago. Mike Barlow has been promoted from sales director to take over as managing director, and a new sales director has been brought in from outside the company. The new sales director recently increased the credit period offered to customers from 30 to 90 days in an attempt to encourage new business and improve sales to existing customers.

The finance director, Ben Vashilli, has recently moved from a full-time to a part-time role as he wishes to spend more time with his family. He has announced his intention to leave within the next 12 months, and the company is seeking a full-time replacement.

Profit has been falling over the last three years. The company wishes to gain a listing on the stock exchange, and all efforts are being focused on reversing the alarming profit trend. A bonus scheme has recently been introduced, where certain managers and directors are paid a lump sum if production exceeds a certain level.

You are the auditor of Collins Cosmetics, and are about to commence the planning for the forthcoming audit.

Required:

Define the following terms:

- (i) **Inherent risk**
 - (ii) **Control risk**
 - (iii) **Detection risk. (3 marks)**
- (c) **Using the information provided, identify and describe FIVE audit risks, and explain the auditor's response to each risk, in planning the audit of Collins Cosmetics. (10 marks)**
- (d) **Explain how an audit strategy might be affected if the auditor concluded the level of inherent risk was high. (3 marks)**

(Total: 20 marks)

- 6** You are an audit supervisor of Fisher & Co and are currently reviewing documentation for Voyager Co's sales system and purchases system in preparation for the interim audit.

Voyager is a small company that manufactures and sells high quality knitwear. Its customers are mainly fashion boutiques. Voyager has two directors, one of whom is an executive, involved in the day-to-day administration of the business. The other is non-executive. The accounts team includes Mr Jones, who is responsible for processing revenue and receivables, and Mrs Singh, who is the purchases and wages clerk.

- (a) The company has one sales representative, who visits shops throughout the region. He is responsible for finding new clients and for generating orders from all customers. Orders are recorded on an order form which is referenced with the date and time the order was placed and the first letter of the customer's name. He passes the completed forms to the warehouse.

The completed order is despatched from the warehouse by courier, accompanied by one copy of a despatch note. The other copy is sent to Mr Jones, who prepares an invoice based on the information it contains and on the company's price list. He sends one copy of the invoice to the customer, and a second copy of the invoice is retained.

Each Friday, Mr Jones inputs the week's invoices into the computerised revenue ledger. He then files the invoices alphabetically by customer name. Despatch notes are not retained because filing space is limited.

Mr Jones opens the post daily and lists remittances received from receivables. Every Friday, he inputs the information listed to the receivables ledger. Cheques received are banked daily by the executive director.

Mr Jones reviews the accounts receivables ledger balances every month and writes to customers who have not paid within 90 days of receiving goods. Mr Jones reviews the receivables ledger on the computer screen, no hard copy is printed.

The company's computer package includes the facility to produce a day book and accounts receivables ledger control account. These are not used because Mr Jones considers that the low volume of transactions (10 to 15 invoices per week) makes them unnecessary.

Required:

For FOUR of the deficiencies already identified in the sales system of Voyager:

- (i) **explain the possible implication of the deficiency** (5 marks)
- (ii) **suggest a recommendation to address each deficiency** (5 marks)
- (b) During the audit you also identify the following significant points:
- (i) Amendments to the payables master file can only be made by the executive director. Access to the master file is restricted to the executive director by password protection.
- (ii) A current printout of the master file is kept by the director and compared to the underlying system data periodically to ensure that it has not been amended without authorisation.

- (iii) The payables ledger balances are reconciled to the supplier statements by Mr Jones. All reconciliations are retained on file to assist with the preparation of year-end accruals and in times of disputed payments.
- (iv) At the month end Mr Jones prints off an aged payables ledger and writes cheques to all suppliers with amounts in the 60 days or older column. He then presents the cheques to the executive director with a copy of the aged payables ledger who scrutinises the cheques and checks the payables back to the authorised list of suppliers on the master file. The executive director then signs the cheques, before Mr Jones mails them to suppliers.
- (v) All expense claims are supported by receipts as required by company policy. All claims are authorised by the director, who checks that the receipts are sufficient evidence and that claims are relevant to the business.

Required:

In respect of the purchases and wages control system of Voyager Co:

- (i) Identify and explain SIX strengths. (5 marks)
- (ii) Describe a test of control the Fisher & Co would perform to assess if each of these controls is operating effectively. (5 marks)

(Total: 20 marks)

