

**UNIVERSITY OF BOLTON**

**GREATER MANCHESTER BUSINESS SCHOOL**

**BA(HONS) ACCOUNTANCY**

**SEMESTER TWO EXAMINATIONS 2022/2023**

**AUDITING AND ASSURANCE**

**MODULE NO: ACC5004**

Date: Tuesday 9 May 2023

Time: 2.00 – 5.00

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**INSTRUCTIONS TO CANDIDATES:**

There are 5 questions on this paper.

Answer BOTH questions from section A and TWO questions from section B.

This is a closed book examination.

You must hand in this exam paper with your answer booklet.

Use of calculators is allowed.

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**Section A - Answer Both Questions**

**Question 1**

You are a manager in the audit department of Simmons and Stevens. A potential new client, Delta Co, an aircraft obstruction lighting company, has approached your firm to perform the external audit in addition to some other non-audit services for the year ending 30 October 20X3. Your audit firm was recommended to Delta Co by an existing client, B&L, a telecommunication company who is also a major customer of Delta Co.

You have been chosen to lead the engagement as you have experience of auditing such organisations and also manage the audit of B&L.

Whilst arranging the initial meeting with the directors of Delta Co, you realise that you studied accountancy with the finance director at university.

Delta Co has not made a profit for the last two years. The directors explain it is largely due to increased costs within the industry including rising prices of fuel. They are confident they have now controlled their costs for the current year. They have also been approached to tender for a large profitable contract which would improve the company's financial performance in future. They would like you to help them for preparing this tender and present with them on the day.

The prior year financial statements are being audited by another audit firm. The finance director tells you that the current auditors have identified material misstatements but the board of directors are refusing to make these adjustments. If adjusted it would turn the break-even into a loss.

The current auditors have replied to your professional clearance letter and have informed you that they are still owed fees relating to the prior year.

You calculate the potential fees from Delta Co would amount to approximately 15% of your firm's total fee income.

**Required:**

**(a) Explain the following fundamental principles in the code of ethics:**

**Integrity**

**Professional competence and due care**

**Objectivity**

**(5 Marks)**

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**Question 1 continued**

**(b) Identify and explain two threats and recommend a possible safeguard to objectivity if Simmons & Stevens accept Delta Co as a new client.**

**(Prepare your answer using two columns headed ethical threat and possible safeguard respectively)**

**(10 Marks)**

**(c) Explain matters that should be considered before accepting the engagement, other than ethical threats.**

**(5 Marks)**

**Total (20 Marks)**

**Question 2**

Your firm Rose & Co has recently been accepted appointment as auditor of Marcy Co (Manufacturer in fashion garments).

Having sold your shares in Marcy Co, you have been assigned as audit manager and you have started planning the audit (although you were an employee of Marcy Co many years ago, you were not involved in preparation of the financial statements). You have had a meeting with the client and have ascertained the following:

Marcy Co manufacture fashion garments. Most items of garments such as trousers and shirts and blouses take less than a day to manufacture. Marcy Co's largest revenue generating product, fashion coats take up to one week to manufacture. Marcy Co refurbished the assembly line for the coats during the year. Marcy Co stores its finished coats at a third-party warehouse and approximately a quarter of its other manufactured garments.

To date, Marcy Co has only sold to retailers. For the first time this year, Marcy Co has made sales directly to consumers online. Their website is directly linked to their finance system, recording sales automatically. Online customers pay upon ordering. The online development costs have been capitalised. Due to the dramatic decline in retailer sales, it was decided to implement online sales as per market demand. Some of Marcy Co's retail customers are struggling to pay their outstanding debt. Several employees from sales team were made redundant last month as a result in declined retailer sales.

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**Question 2 continued**

<b>Marcy Co - Draft Statement of Financial Position as at 31 December 20X3</b>		
	<b>20X3</b>	<b>20X2</b>
<b>Non-current assets</b>		
Property plant and equipment	5350	4900
Website development	150	0
	5500	4900
<b>Current Assets</b>		
Inventory	2109	1300
Trade Receivables	2040	1050
Cash & Cash equivalents	48	38
	4197	2388
	9697	7288
<b>Equity</b>		
Share Capital (50p shares)	2100	2100
Retained Earnings	2959	2156
	5059	4256
<b>Non current liabilities</b>		
Long term loan	2800	1500
<b>Current Liabilities</b>		
Provisions	240	195
Trade payables	1400	1205
Accruals	18	12
Bank Overdraft	180	120
	1838	1532
	9697	7288

**Question 2 continued over the page  
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**Question 2 continued**

<b>Draft Statement of Profit or Loss for The Year Ended 31 December 20X3</b>		
	<b>20X3</b>	<b>20X2</b>
Revenue	21960	19580
Cost of Sales	-18560	-17080
Gross Profit	3400	2500
Operating expenses	-2012	-2012
Operating Profit	1388	488
Finance Costs	-340	-240
Profit before Tax	1048	248
Taxation	-245	-24
Profit for the period	803	224

**Required:**

(a) Describe SIX audit risks, and explain the auditor's response to each risk in planning the audit for Marcy Co.

(18 Marks)

(b) Perform analytical procedures on the draft financial statements of Marcy Co.

(8 Marks)

(c) Define materiality and explain how the level of materiality is assessed

(4 Marks)

**Total (30 Marks)**

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**Section B - Answer Two Questions Only**

**Question 3**

A golf centre (JRK) set in the heart of Bolton offers a range of top-class facilities. It has 50 undercover bays, power tee technology across all bays, 6 target greens spread over 250 yards. The centre has 430 members from the start of the financial year to 31<sup>st</sup> December 2023. Each member is required to pay an annual membership fee £110 per annum.

You are the auditor of JRK and have been provided with the following information:

It has been noted that approximately 10% of members do not renew their memberships when they fall due. New members are only required to pay half of the annual membership fee. 30 new members joined during the month of October and members are not required to pay their fees in advance.

Non-members can hire a bay at the rate of £10.00 per hour and are required to sign a log sheet. All cash is collected and placed in a cash tin in the administration office. It is collected and banked by the JRK secretary regularly. The secretary prepares a paying-in slip which they then pass to the treasurer. This slip shows the relationship between bay hire and membership fees. The secretary also provides the treasurer with a list of those members who have paid their fees. These amounts are then recorded in the cash book.

JRK incurs expenses related to the running of the centre, including the maintenance of the golf centre, electricity for the lights on the bay. The centre also hosts championship golf competitions. It supplies the bowl for the competitors to ensure there is no possibility for the bowl to be tampered with, in order to gain competitive advantage. Each competition uses 20 bowls.

All expenses are paid for by the treasurer who uses the centre's debit card. The receipts for these expenses are filed in chronological order. The treasurer is also responsible for preparing the annual financial statements, which are subsequently audited by an independent auditor as required by the centre's rules.

**Required:**

**a) Assess the audit work required to ensure the completeness of income for JRK golf centre.**

**(10 Marks)**

**Question 3 continued over the page  
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**Question 3 continued**

**(b) Explain the audit procedures that should be performed to check the completeness and accuracy of expenditure at the centre.**  
**(10 Marks)**

**(c) Write an email to the audit partner explaining why testing of internal controls would not assist you in your audit work for the annual audit of JRK golf centre.**  
**(5 Marks)**

**(Total 25 Marks)**

**Question 4**

Egypto is an airline company. The company owns some of its fleet of aircraft, whilst others are leased from third parties. The company's board of directors are ethical and follow rules and regulations stringently. The company has an internal audit function that has recently been expanded. Your firm is the external auditor of Egypto. Your firm has been asked to investigate the extent to which it may be able to rely on the work of internal audit in the following areas:

- Sales and Ticketing
- Fleet acquisition and maintenance
- Trade payables and long-term debt financing (borrowings).

**Required:**

**(a) Explain why the work of the internal auditors, in the three areas noted above is likely to be useful to you as the external auditor.**  
**(10 Marks)**

**(b) Explain the matters that should be considered by the external auditor when evaluating the internal audit function and whether reliance can be placed on its work.**

**(10 Marks)**

**Question 4 continued over the page  
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**Question 4 continued**

**(C) Evaluate the use of adopting an audit software such as Computer Assisted Auditing Techniques (CAATs).**

**(5 Marks)**  
**(Total 25 marks)**

**Question 5**

**(a) Examine the following statements and explain the extent to which you agree to them:**

**(i) Inherent risk is the risk that can be ignored whilst assessing audit risk.**

**(5 marks)**

**(ii) Professional scepticism is an area that can be ignored when assessing audit evidence.**

**(5 marks)**

**(b) In order to identify risks to material misstatements in the financial statements it is important for the auditor to understand the entity and its environment. According to ISA 315, what would this generally include?**

**(7 marks)**

**(c) Discuss the audit risk model.**

**(8 marks)**

**(Total 25 marks)**

**END OF QUESTIONS**