Solution Manual For

Auditing, 11th Edition by Alan Millichamp, John Taylor

Chapter 1-31

ANSWERS TO CASE STUDIES AND EXAMINATION QUESTIONS

Note

The answers to the chapter questions comprise

1) Suggested points from the Case Studies.

These are meant to be indicative and not exhaustive – other points may arise out of study and discussion.

2) Answers to examination questions

The answers to questions from ACCA examinations are those suggested by ACCA and are used by kind permission of the Association of Chartered Certified Accountants

The Answers to questions from ICAEW examinations are derived by the author as the ICAEW levies a charge for answers to individual examination questions! The questions have been used with kind permission of the Institute of Chartered Accountants in England & Wales

(Note: no suggested answers are given to student self test questions as these should be apparent from the text)

Chapter 1
Case Study

What benefits would the company get from employing an independent auditor?

Consider:

- Credibility of financial statements –particularly when borrowing money
- Financial statements correctly stated for taxation purposes
- Benefits when dealing with suppliers and employees – more reliable financial information creates increased confidence in reliability of company information
- Protection of minority shareholders
- Review of internal systems of control
- Increased likelihood of the prevention and detection of errors and fraud
- Improved risk management
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Where would they find a suitable auditor?

The company is below the threshold for a statutory audit so would not need to appoint a registered auditor. Consequently a suitably qualified accountant would suffice, however it is good practice to appoint an appropriately qualified person – particularly if the company is expected to grow.

Both ACCA and ICAEW (in England, ICAS in Scotland and ICAE in Ireland) have registers of appropriately qualified auditors who could be approached.

Would it benefit Bertha to have a proper audit?

Consider:

- Principles of agency theory – actions of Gibbs & Angelo
- Protection of minority shareholders
- Safeguard company value
- Disclosure of directors' remuneration and benefits
- Points made above re appointment of qualified auditor

Examination question

Key points

a) Key stakeholders in the company relevant to this issue principally comprise

- Shareholders – including minorities
- Directors
- Customers using the materials
- Members of the public coming into contact with the materials or consequences of it being used e.g. relative to toxic chemicals, pollutants etc
- Regulatory agencies/government bodies
- Employees – particularly overseas employees

b) The company is in a particularly sensitive market and simply providing the minimum information is not enough. It should disclose the environmental impact of its products, information about its health and safety record, its policies on sales of products overseas etc.

Environmental reporting would be a key issue as shareholders and the public expect a greater sense of corporate social responsibility from companies, particularly those where the ethics of their policies might be called into question

Consider

- Ethical position of the company with regard to overseas sales
- Actual environmental impact of use of banned products
- Consequences to the company of health and safety breaches and accidents to employees – financial and reputational
- Reputational risk could damage home market sales with adverse publicity

c) Directors have a duty to protect assets of the company and a wider duty to the public at large. They must review the policy of dumping and also consider what they need to do to correct the situation in the dangerous factory.

They must investigate all allegations. This could involve the non executive direct ors and the internal audit function as the investigation should be seen to be independent and thorough. The directors cannot ignore the revelations and must take steps to respond.

They should create clear policies and guidelines regarding overseas sales and the sale of banned materials and, if these constitute a hazard they should stop the practice.

Chapter 2

Case Study

What will Bolington need to do in order to start complying with some of the key aspects of corporate governance?

Consider

- Key aspects of Cadbury Report and subsequent reports incorporated into the Code of Corporate Governance which the company must comply with when shares are floated
- Compliance with the provisions of the Code on a 'comply or explain' basis
- Separation of roles of Chairman and Chief Executive
- Appointment of non-executive directors – perhaps three or four
- Appointment of non -executive Chairman
- Clear division of responsibilities of executive board
- Procedures for appointing directors so suitable persons appointed – especially Bill Stickers – *(Is he qualified? Does he have capacity for strategic planning, is he being promoted simply as a reward for long service rather than because he is a good financial director?)*

- Review of management information to ensure adequate for Board purposes
- Acceptance of increased disclosure in financial statements
- Procedures for evaluating performance of board collectively and individual directors
- Review of levels of directors' remuneration – possibly move to rewards linked to performance
- Appointment of Audit Committee of non executive directors
- Review of internal controls and possible creation of internal audit function
- Auditors to report on compliance with Combined Code provisions