



Auditing Module 7

Monday 20th June 2011
10am – 1pm

Instructions to Candidates:

1. Answer Question 1, and any other 4 questions.
2. All questions carry equal marks.
3. Include all workings with your answer.

Time Allowed: 3 Hours.

Question 1 (This question must be attempted).

Provide brief answers to each of the following short form questions:

- (a) Set out the purpose of a letter of representation and state what it should contain. **(4 Marks)**
- (b) In the audit of a credit sales system give examples of controls you would expect to find in such a system to ensure that all goods despatched are invoiced to the customer. **(4 Marks)**
- (c) State what is meant by a test of control and outline two examples of such tests that would be undertaken during the audit of a company. **(4 Marks)**
- (d) Explain what is meant by the term “substantive test” and give examples of a substantive test that you would use in the audit of trade debtors. **(4 Marks)**
- (e) Set out the audit procedures you would undertake to verify that all post balance sheet events were correctly accounted for in the financial statements of the auditee. **(4 Marks)**

Total marks 20

Question 2.

You were recently requested to give a presentation to a group of people who are attending a start their own business course run by the local County Enterprise Board. The course organiser has requested you to address the issue of accounting and auditing requirements of companies. He has asked you to set out for the attendees what is involved in a statutory audit and in particular to address in your presentation:

- What is an audit?
- Who can be appointed as auditor?
- Who is responsible for the appointment of the auditor?
- What is / are the duty / duties of the auditor?
- Who decides on the amount of audit work the auditor must undertake?
- Who will the auditor report to?
- What are the outputs of an audit?
- Why do some companies not require an audit?

Your answer should be presented in the form of a speech that you will make to the group and should refer to relevant sections of the Companies Acts or to relevant auditing standards.

Total marks 20

Question 3

You are currently working on the audit of the financial statements of "Applejack Limited" for the year ended 31 December 2010. Applejack Limited manufactures tin cans which are sold to Irish based customers. The schedule below sets out the amounts included under the debtors figure on the balance sheet of the company at 31 December 2010.

<u>Lead Schedule</u>	€
Trade debtors, net	1,125,000
Prepayments	10,000
Grant receivable	17,500
VAT recoverable	<u>11,650</u>
	<u>€1,164,150</u>

Trade debtors represent 15% of turnover. There are 60 customer accounts. Three customers account for 60% of the debtors as at 31 December 2010. The provision for doubtful accounts is € 414,750 and has been reduced by 50% from 2009. The gross debtors figure has increased by 1%. There were no bad debts written off.

Required:

- (a) Based only on the information provided, identify two key audit issues that would concern you when drafting the audit work programme for trade debtors. **(2 Marks)**
- (b) Draft the programme of audit work you would undertake as part of the substantive tests of trade debtors at the 31 December 2010. **(12 Marks)**
- (c) Describe appropriate substantive audit procedures to be undertaken in respect of:
- Prepayments,
 - Grant receivable and
 - VAT recoverable

(6 Marks)

Total Marks 20

Question 4

1. Explain each of the following terms using the sales / debtors receipts cycle to illustrate your answer:
 - a. Audit risk.
 - b. Control risk.
 - c. Inherent risk.
 - d. Detection risk.

(10 Marks)
2. Outline the relationship that exists between control risk, detection risk and inherent risk and how this relationship would impact your audit planning work on an audit assignment.

(5 Marks)
3. Briefly explain the difference between an audit strategy that proposes to test the operating effectiveness of internal controls as part of the audit assignment and an audit strategy that adopts a purely substantive based approach to the audit assignment.

(5 Marks)

Total Marks 20

Question 5.

You are auditor to Orange Juice Limited. At a recent meeting with the Board of Directors the vulnerability of the company to fraud was discussed in detail. Many of the board members appeared to be of the opinion that the external auditors principal role was to detect instances of fraud. You are concerned that the Board members have a mistaken opinion as to the role of the auditor in detecting fraud and you have decided to write to the Board to set out the actual role of the auditor in relation to fraud. You are required to draft the letter in which you should address the following matters:

1. Duty of the directors and auditors in relation to the prevention and detection of fraud.
2. The approach the auditor should take in discharging his responsibility in relation to fraud.
3. Steps the auditor should take where he becomes aware of suspected or actual instance of fraud.

Total Marks 20

Question 6.

You are auditor to Banana Limited. The company is engaged in the retail of men's clothing. An analysis of employee numbers and cost is as follows:

	Employee Numbers	Annual Cost
Salary staff	3 (paid monthly)	€398,000
Administration staff	4 (paid weekly)	€120,000
Retail staff	24 (paid weekly)	€679,098

Required:

1. Describe the controls you would expect to find in the payroll system of Banana Limited.

(8 Marks).
2. Discuss the role (if any) that segregation of duties would play in the design of effective controls in the payroll system.

(4 Marks).
3. Set out how you might test the operating effectiveness of two of the controls described in (1) above.

(4 Marks)
4. Describe analytical review procedures that could be applied in the audit of the payroll figures.

(4 Marks)

Total Marks 20

Question 7.

As part of the audit team assigned to the audit of Pineapple Limited, you are scheduled to attend the annual stock count of the company on the 30 June 2011. You are required to prepare a memorandum for the junior audit staff member setting out the following matters:

1. The purpose of the auditor attending the annual stock count. **(4 Marks)**

2. Set out the cut-off information you would gather during your attendance at the company's stock take and explain how this information would be used during the course of the final audit of the company's financial statements. **(4 Marks)**

3. Set out the audit procedures you will undertake:
 - a. before the stock count commences; **(4 Marks)**

 - b. during the stock count; **(4 Marks)**
 - c. after the physical count is completed on the day of the count; **(4 Marks)**

Total Marks 20