

## **WARNING**

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Family Name					
Given Name/s					
Student Number					
Teaching Period	Semester 2, 2017				

ACT504 – Auditing	<b>DURATION</b>	
	Reading Time:	<b>10 minutes</b>
	Writing Time:	<b>180 minutes</b>

### INSTRUCTIONS TO CANDIDATES

The examination has 3 sections:

<b>Section A:</b> Suggested Time:	<b>Multiple Choice Questions:</b> Answer ALL questions, 20 marks 45 minutes
<b>Section B:</b> Suggested Time:	<b>Short Answer Questions:</b> Answer ALL questions, 40 marks 90 minutes
<b>Section C:</b> Suggested Time:	<b>Case Study Questions:</b> Answer ALL questions, 20 marks 45 minutes

**Section A** must be answered on the Multiple Choice Answer Sheet provided in this examination paper and must be handed in with your answer booklet. Please ensure that your name and student number are clearly indicated on your Answer Sheet and at the top of this examination paper.

**Section B and Section C** are to be answered in the Answer Booklet provided.

Note that questions **ARE NOT** of equal value.

### EXAM CONDITIONS

You may begin writing from the commencement of the examination session. The reading time indicated above is provided as a guide only.

This is a RESTRICTED OPEN BOOK examination

Any non-programmable calculator is permitted

No handwritten notes are permitted

Hard copy, unannotated English translation dictionary only

ADDITIONAL AUTHORISED MATERIALS	EXAMINATION MATERIALS TO BE SUPPLIED
No additional printed material is permitted	1 x 16 Page Book 1 x 4-Multiple Choice Answer Sheet

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DOUBLE-SIDED.**

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LEFT BLANK.**

**Section A**  
**Multiple Choice Questions**  
**Total No of Marks for this section: 20**

This section should be answered on the Multiple Choice Answer Sheet provided. Please ensure that your name and student number have been written on the Answer sheet and place in the completed answer Booklet.  
Each question carries 1 mark. Suggested Time allocation for Section A: 45 mins

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## Section B

### Short Answer Questions

**Total No of Marks for this section: 40**

This section should be answered in the Answer Booklet provided.

Marks for each question are indicated. Suggested Time allocation for Section B: 90 mins

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#### **Question 1: (10 marks)**

Your client is DarwinCorp Pty Ltd (“DarwinCorp”), a diversified business operating throughout Australia. Year-end was 30 June 2016, the auditor’s report was signed on 31 July 2016 and the financial statements were mailed to shareholders on 14 August 2016.

During your subsequent events review, you noted the following independent and *material* items:

1. DarwinCorp has been involved in a legal dispute with a competitor for a number of years. The dispute relates to alleged breaches of copyright by DarwinCorp. On 27 July, you discovered that DarwinCorp had settled the legal action out of court on terms more favourable than expected.
2. As for (1) above, except that the legal action was settled on 5 August.
3. On 10 July, one of DarwinCorp’s major product lines developed a fault that rendered the product unusable. DarwinCorp became aware of the fault on 30 July. Although the fault posed no safety risks to consumers, DarwinCorp decided to launch a full product recall on the following day.
4. On 30 July 2016, the Bureau of Meteorology issued a cyclone warning for parts of Far North Queensland. DarwinCorp has a large sugar cane plantation in this area. On 2 August, the cyclone hit, wiping out about 90% of the crop.
5. In early June, one of DarwinCorp’s largest debtors informed DarwinCorp that it was experiencing serious financial difficulties. On 5 July, DarwinCorp was informed that the debtor had gone into receivership. Preliminary reports suggest DarwinCorp will recover only 10 cents in the dollar of the outstanding debt.

#### **REQUIRED:**

- (a) Outline the key additional procedures you should have performed in relation to each of the above events.

(5 marks)
- (b) What actions should you have recommended to management in relation to each of the above events?

(5 marks)

**Question 2: (10 marks)**

You are a newly qualified accountant who works for the audit firm David David & Co. You have been approached by a potential new client, Slingshot Electronics Pty Ltd (“Slingshot”), who is looking for an audit firm to carry out an audit on its annual financial report prepared in accordance with the *Corporations Act 2001*. The managing director of Slingshot, Goliath, is not sure exactly what an audit involves and what are the responsibilities of the auditor.

**REQUIRED:**

Identify and explain to the managing director, Goliath, the responsibilities of the auditor and the responsibilities of management.

(10 marks)

**Question 3: (10 marks)**

Listed below are ten substantive procedures:

1. Ensure that interest paid on the bank loan is correct by multiplying the interest rate by the outstanding principal for each month of the year.
2. Send a letter to the bank to confirm a loan taken out by the company during the year.
3. Attend the year-end stocktake and perform test counts on a sample of stock items.
4. Review all invoices received for one month after the year-end to ensure that they do not relate to the current year.
5. Calculate the accounts receivable turnover and compare with previous year’s turnover.
6. Select a sample of non-current assets and sight them.
7. Review the income statement for unusual differences in the balances recorded for this year and last year.
8. Select a sample of invoices and ensure that they have been properly recorded in the sales ledger.
9. Trace the last inventory received before the year-end to the inventory listing.
10. Review the adequacy of the company’s allowance for doubtful debts.

**REQUIRED:**

- (a) For each test, indicate what type of substantive procedure to which it relates (analytical review, tests of details of balances or tests of details of transactions).

(5 marks)

- (b) Give an assertion (ONLY ONE) to which each test relates.

(5 marks)

#### **Question 4: (10 marks)**

Darwin Playtime Pty Ltd (DPPL) is a toy manufacturer. DPPL has factories across the country and its customer base includes retailers, as well as individuals, to whom direct sales are made through their website. You are an audit senior at Raul David & Associates and you are currently reviewing documentation of DPPL's internal controls in preparation for the interim audit.

DPPL's website allows individuals to order goods directly and full payment is taken in advance. Currently the website is not integrated into the inventory system and inventory levels are not checked at the time when orders are placed.

Goods are delivered via local couriers; however, the couriers do not always record customer signatures as proof that the customer has received the goods. Over the past year, there have been customer complaints about the delay between sales orders and receipt of goods. DPPL has investigated these complaints and found that, in each case, the sales order had been entered into the sales system correctly, but was not forwarded to the despatch department for fulfilling.

DPPL's retail customers undergo credit checks prior to being accepted and credit limits are set accordingly by sales ledger clerks. Neither the sales area managers nor the sales director are involved with this process. These customers place their orders through one of the sales team, who decides on sales discount levels.

Raw materials are purchased from a wide range of suppliers. As a result of staff changes in the purchase ledger department, supplier statement reconciliations are no longer performed. Additionally, changes to existing supplier details or inclusion of new supplier details in the purchase ledger master file can be undertaken by purchase ledger clerks, as well as supervisors.

In the past six months, DPPL has changed part of its manufacturing process and as a result some new equipment has been purchased. However, there are now considerable levels of plant and equipment that are now surplus to requirement. Purchase requisitions for all new equipment have been authorised by production supervisors and little has been done to reduce the surplus of old equipment.

#### **REQUIRED:**

- a) Identify five (5) deficiencies in the internal controls of DPPL. Explain how a business risk arises from each deficiency.

(10 marks)

## Section C

### Case Study Questions

**Total Number of Marks for this section: 20**

This section should be answered in the Answer Booklet provided.

Marks for the question is as indicated. Suggested Time allocation for Section C: 45 mins

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#### **Background information**

Clearview Pty Ltd (Clearview) is a manufacturer of glass fencing for swimming pools and balconies. Clearview operates from a large production facility, where it undertakes continuous production 24 hours a day, seven days a week. Also on this site are two warehouses, where the company's raw materials and finished goods are stored. Clearview's year end is 30 June. Clearview is finalising the arrangements for the year-end inventory count, which is to be undertaken on 30 June 2017.

The finished glass fence panels are stored within 25 aisles in the first warehouse. The second warehouse is for large piles of raw materials, such as sand, used in the manufacture of glass. The following arrangements have been made for the inventory count:

The warehouse manager will supervise the count, as he is most familiar with the inventory. There will be ten teams of counters and each team will contain two members of staff, one from the finance and one from the manufacturing department. None of the warehouse staff, other than the manager, will be involved in the count.

Each team will count an aisle of finished goods by counting up and then down each aisle. As this process is systematic, it is felt that the team will not need to flag areas once counted. Once the team has finished counting an aisle, they will hand in their sheets and be given a set for another aisle of the warehouse. In addition to the above, to assist with the inventory counting, there will be two teams of counters from the internal audit department and they will perform inventory counts.

The count sheets are sequentially numbered, and the product codes and descriptions are printed on them, but no quantities. If the counters identify any inventory which is not on their sheets, then they are to enter the item on a separate sheet, which is not numbered. Once all counting is complete, the sequence of the sheets is checked and any additional sheets are also handed in at this stage. All sheets are completed in ink.



Any damaged goods identified by the counters will be too heavy to move to a central location, hence they are to be left where they are located, but the counter is to make a note on the inventory sheets detailing the level of damage.

As Clearview undertakes continuous production, there will continue to be movements of raw materials and finished goods in and out of the warehouse during the count. These will be kept to a minimum where possible.

The level of work-in-progress in the manufacturing plant is to be assessed by the warehouse manager. It is likely that this will be an immaterial balance. In addition, the raw materials quantities are to be approximated by measuring the height and width of the raw material piles. In the past this task has been undertaken by a specialist; however, the warehouse manager feels confident that he can perform this task.

**REQUIRED:**

- (a) List four (4) sources of information that would be of use in gaining an understanding of Clearview, and for each source describe what information you would expect to obtain. (8 marks)
- (b) (i) Identify and explain five (5) internal control weaknesses in the inventory count arrangements of Clearview. (ii) Explain the impact of these weaknesses on the audit. (7 marks)
- (c) Describe a recommendation to address each internal control weakness identified in requirement (b)(i). (5 marks)

**\*\*\* End of Exam\*\*\***