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Family Name					
Given Name/s					
Student Number					
Teaching Period	Semester 1, 2018				

ACT504 – Auditing	DURATION	
	Reading Time:	10 minutes
	Writing Time:	180 minutes
INSTRUCTIONS TO CANDIDATES		
The examination has 3 sections:		
Section A: Suggested Time:	Multiple Choice Questions: Answer ALL questions, 20 marks 45 minutes	
Section B: Suggested Time:	Short Answer Questions: Answer ALL questions, 40 marks 90 minutes	
Section C: Suggested Time:	Case Study Questions: Answer ALL questions, 20 marks 45 minutes	
<p>Section A must be answered on the <u>Multiple Choice Answer Sheet</u> 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.</p> <p>Section B and Section C are to be answered in the <u>Answer Booklet</u> provided.</p>		
EXAM CONDITIONS		
<p><u>You may begin writing from the commencement of the examination session.</u> The reading time indicated above is provided as a guide only.</p>		
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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Section A
Multiple Choice Questions
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

Question 1: (10 Marks)

Moss Green Ltd is a wine grower and producer of medium- to high-quality wines located in Western Australia's Margaret River region. The company has recently listed on the Australian Securities Exchange. After listing, it changed auditors from Tickit Associates to your firm, Watson and Partners. You are an audit supervisor in Watson and Partners and you are planning the audit for 31 December 2017.

The managing director of Moss Green Ltd is Tom Green. He is the founder of the winery and has a very 'hands on' management style. He is a trained winemaker and has always focused more on the wine making and marketing side of the business than the financial side, which he leaves to Wendy Chong, the financial director, in whom he has great faith. He pays her a good base salary and provides an attractive bonus scheme based on growth in net profitability.

The company has been very successful in selling its medium-quality wine to the United Kingdom. This is mainly due to a very large contract with one of the leading supermarket chains there, Safeburys. Part of the success has been due to the low value of the Australian dollar compared with the British pound. However, the company manages its foreign exchange risk through hedging, which is controlled by Wendy. Tom has also been very happy with Wendy's performance in this area as she has made some healthy profits on her hedging contracts.

The wine production manager is Alfred Horndale. From discussions with Alfred, you become aware that the company has significant stock from the 2015 vintage in the Margaret River warehouse and in London (because it was rejected by Safeburys — payment for this stock is currently in dispute).

As is the standard practice, you contacted Tickit Associates before you accepted the engagement at the beginning of the year to see whether there were any matters you should have been aware of before accepting the engagement. They told you that they had only two main concerns. First, they had problems getting Tom Green to have any interest in the financial side of the business, and it was their view that he was not financially literate. Second, there had been a number of disputes over accounting policy with Wendy Chong, particularly over getting her to implement *AASB 141 Agriculture* and *AASB 137 Provisions, Contingent Liabilities and Contingent Assets*.

REQUIRED:

Prepare a memo to the audit partner outlining potential problem areas and their impact on the audit plan.

(10 marks)

Question 2: (10 Marks)

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) Identify and explain five (5) internal control weaknesses in the inventory count arrangements of Clearview. **Explain the impact of these weaknesses on the audit.** (5 marks)
- (b) Describe a recommendation to address EACH internal control weakness identified in requirement. (5 marks)

Question 3: (10 Marks)

Listed below are ten substantive procedures:

1. Review the company-prepared bank reconciliation.
2. Obtain the company's depreciation rates from the financial statements and check they have been applied correctly.
3. Perform accounts receivable circularisation.
4. Review a sample of repairs and maintenance expenditure for the year to ensure that it does not include any items that are capital in nature.
5. Ensure that all contingent liabilities have been included in the notes to the accounts.
6. Send a letter to the bank to confirm a loan taken out by the company during the year.
7. Review all invoices received for one month after the year-end to ensure that they do not relate to the current year.
8. Select a sample of non-current assets and sight them.
9. Select a sample of invoices and ensure that they have been properly recorded in the sales ledger.
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 and **explain why**.
(5 marks)

Question 4: (10 Marks)

Your client is NTCorp Pty Ltd (“NTCorp”), a diversified business operating throughout Australia. Year-end was 30 June 2017, the auditor’s report was signed on 31 July 2017 and the financial statements were mailed to shareholders on 14 August 2017.

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

1. NTCorp has been involved in a legal dispute with a competitor for a number of years. The dispute relates to alleged breaches of copyright by NTCorp. On 27 July, you discovered that NTCorp 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 2017.
3. On 10 July, one of NTCorp’s major product lines developed a fault that rendered the product unusable. NTCorp became aware of the fault on 30 July. Although the fault posed no safety risks to consumers, NTCorp decided to launch a full product recall on the following day.
4. On 30 July, the Bureau of Meteorology issued a cyclone warning for parts of Far North Queensland. NTCorp has a large sugar cane plantation in this area. On 2 August 2017, the cyclone hit, wiping out about 90% of the crop.
5. In early June, one of NTCorp’s largest debtors informed NTCorp that it was experiencing serious financial difficulties. On 5 July 2017, NTCorp was informed that the debtor had gone into receivership. Preliminary reports suggest NTCorp 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)

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

Background information:

You are the audit partner of David & Associates (“DA”), working on the audit of Australian Tourist Buses (“ATB”) for the 2017 financial year. ATB is a provider of luxury bus trips all around Australia, including both interstate capital city travel and conference and holiday packages.

The net profit before tax of ATB for the 2017 financial year is \$14,541,000 while net assets total \$231,982,000.

Part A (8 Marks)

You are reviewing the 2017 audit working papers and note that the assurance services senior has documented a number of situations that may lead to a breach of independence for DA.

Situation 1

It has been documented that the ATB Financial Controller has gifted the three audit team members with two free luxury holiday packages each. The audit manager has concluded that the key threat to independence in Situation 1 is ‘**self-interest**’.

Situation 2

The audit team has documented that ATB is intending to launch a new customer loyalty program. The CFO of ATB has guaranteed that if the audit team convince DA and five of its biggest clients to sign an exclusive corporate travel arrangement with ATB, the audit team will receive immediate platinum status (normally requiring a customer to have accumulated one million points), giving them a host of benefits. The audit manager has concluded that the key threat to independence in Situation 2 is ‘**familiarity**’.

Situation 3

The audit team has noted that DA has put forward a proposal to ATB to provide consulting services. The CFO of ATB has told the audit team that if they do not remove comments in the audit summary review memorandum to be provided to the audit committee about a weakness in the revenue and receivables process, he will not award DA the consulting work. The audit manager has concluded that the key threat to independence in Situation 3 is ‘**advocacy**’.

REQUIRED:

Explain whether the audit manager has correctly identified the key potential threat to independence for each of Situations 1, 2 and 3 above. Your answer should clearly identify what you believe is the key threat to independence in each situation. (8 marks)

Part B (12 Marks)

You are due to sign the auditor's opinion on 22 August 2017. ATB will issue the financial statements on 28 August 2017.

On 16 August 2017, the following situations come to your attention:

Situation 1

Happy Holidays, one of ATB's largest wholesale travel agents that purchased travel packages in bulk from ATB, went into liquidation on 3 July 2017. A letter from the liquidator dated 31 July 2017 indicates that creditors are likely to receive \$0.10 in the dollar. As at 30 June 2017, Happy Holidays owed ATB \$2,301,000.

Situation 2

On 15 August 2017, a bus travelling from Brisbane to Sydney crashed. It is alleged that the bus driver was distracted by a call on his mobile telephone. 5 passengers died and 17 were injured. The passengers had paid their fares during the 2017 financial year. (An account "Unearned Income" was credited in the prior year when monies were received). It is likely that a law suit will be brought against the company due to the driver's negligence.

REQUIRED:

Assume there are no issues other than those described in Situations 1 and 2, and that going concern is not an issue. Also, assume that in response to each material situation above, management could either adjust the amounts in the financial statements or take no action.

Treating Situations 1 and 2 independently when answering this question:

- (a) For Situation 1,
- (i) Identify the appropriate treatment in the financial statements. Justify your answer. (2 marks)
 - (ii) Identify the appropriate auditor's opinion if management adjusts the amounts in the financial statements. Justify your answer. (2 marks)
 - (iii) Identify the appropriate auditor's opinion if management takes no action. Justify your answer. (2 marks)
- (b) For Situation 2,
- (i) Identify the appropriate treatment in the financial statements. Justify your answer. (2 marks)
 - (ii) Identify the appropriate auditor's opinion if management adjusts the amounts in the financial statements. Justify your answer. (2 marks)
 - (iii) Identify the appropriate auditor's opinion if management takes no action. Justify your answer. (2 marks)

You may wish to present your answer in the form of the following table:

Situation	(i) Accounting treatment and justification.	(ii) Auditor's opinion if management adjusts financial statements and justification.	(ii) Auditor's opinion if management takes no action and justification.
1			
2			

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