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# Answers

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Section A

Question	Answer	See Note
1	B	1
2	D	2
3	C	3
4	C	4
5	C	5
6	B	6
7	A	7
8	D	8
9	A	9
10	B	10
11	B	11
12	D	12

Notes:

- 1 Results of previous audits and the need to maintain professional scepticism should be included in an audit strategy as opposed to an audit engagement letter.
- 2 In the case of situations 1 and 4, the auditor has an obligation to disclose details of their clients' affairs to third parties. Situations 2 and 3 are ones where voluntary disclosure should be made.
- 3 When the accounting records are unavailable, it is not acceptable to obtain a written representation as this represents an inability to obtain sufficient and appropriate audit evidence and if material would result in a modified audit report.
- 4 Substantive procedure 1 provides evidence over the assertion of completeness as the direction of the test is from source documents to accounting records. Substantive procedure 4 provides evidence over valuation and allocation rather than existence.
- 5 Auditors do not have a responsibility to formally report on the going concern status. ISA 570 *Going Concern* requires auditors to obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern.
- 6 Procedures 2 and 3 are substantive procedures rather than tests of control.
- 7 Costs may reduce if the internal audit function is outsourced; however, this would not always be the case as redundancies of the company's existing internal audit function may increase the overall costs.
- 8 Entering dummy data into the company's own computer system is a test data technique as it involves the use of the company's system rather than the auditor's own computer programs.
- 9 Internal control questionnaires can sometimes contain a large number of irrelevant controls; hence this is a disadvantage. B relates to disadvantages of using narrative notes and C is incorrect as questionnaires are quick to prepare.
- 10 Statement 1 is not correct as internal audit (IA) should not report to the finance director as this would impact on their independence. Some of the internal controls and functions IA review are the responsibility of the finance director and they may not act on any recommendations which appear to criticise their department. Statement 2 is correct as companies are not required to implement and maintain an IA function. Corporate governance principles recommend that listed companies maintain an IA function and annually consider the need for such a function; however, they do not require it.
- 11 Audit risk is made up of two components being risk of material misstatement; inherent risk and control risk and also the risk that the auditor will not detect material misstatements being detection risk.
- 12 If management are unwilling to make their assessment of going concern this would result in a modified opinion with a qualified or disclaimer opinion. If the going concern basis is not appropriate, then an adverse opinion should be provided rather than a qualified opinion as the matter is material and pervasive.

## Section B

### 1 (a) Importance of audit planning

- It helps the auditor to devote appropriate attention to important areas of the audit.
- It helps the auditor to identify and resolve potential problems on a timely basis.
- It helps the auditor to properly organise and manage the audit engagement so that it is performed in an effective and efficient manner.
- It assists in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks and the proper assignment of work to them.
- It facilitates the direction and supervision of engagement team members and the review of their work.
- It assists, where applicable, in the coordination of work done by experts.

### (b) Procedures due to increased risk of fraud

The audit senior should consider undertaking the following procedures as a result of the increased risk of the payroll fraud.

- Discuss with management and those charged with governance as to whether they are aware of any other payroll frauds or potential frauds.
- Review board minutes for evidence of management discussion of the materiality of the payroll fraud and to the existence of any additional frauds or suspected frauds.
- Discuss with the payroll manager the nature of the payroll fraud, how it occurred and the financial impact of amounts incorrectly paid into the payroll clerk's bank account.
- Review the supporting documentation to confirm the total of the fraudulent payments made and assess the materiality of this misstatement.
- Review and test the internal controls surrounding setting up of and payments to new joiners to assess whether further frauds may have occurred.
- Consider whether other information obtained by the audit team indicates risks of additional material misstatements with regards to payroll fraud.
- Obtain a written representation from management acknowledging that they have disclosed to the auditors all knowledge of actual and suspected payroll frauds.

## 2 Audit risks and responses

### Audit risk

Eagle Heating Co (Eagle) has decreased the selling price of products significantly since September 2014 and there are increased levels of inventory expected at the year end.

It is possible that the selling price may have fallen so that the net realisable value (NRV) of inventory is below cost. IAS 2 *Inventory* requires inventory to be stated at the lower of cost and NRV. Hence it is possible that inventory is overvalued.

A key customer of Eagle has been experiencing financial difficulties and Eagle has agreed a six-month payment break; however, the finance director does not believe an allowance is required.

If the customer is experiencing difficulties, there is an increased risk that the receivable is not recoverable and hence is overvalued.

In light of the increased competition, reduction in selling price and financial difficulties of a key customer, there is an increased risk that Eagle is facing going concern difficulties.

The financial controller of Eagle was dismissed in October and is threatening to sue the company for unfair dismissal.

If it is probable that Eagle will make payment to the financial controller, a provision for unfair dismissal is required. If the payment is possible rather than probable, a contingent liability disclosure would be necessary. If Eagle has not done this, there is a risk over the completeness of any provisions or contingent liabilities.

### Auditors response

The auditor should undertake detailed cost and NRV testing to assess whether inventory is overvalued and requires write down.

If the six-months payment break has now ended, review after date cash receipts for this customer to assess whether any payments have been made.

Discuss with the finance director why he feels an allowance is not required. Review whether any general allowance for uncollectable accounts is sufficient to cover the amount of this receivable.

The auditor should undertake detailed going concern testing. They should review the cash flow forecast for the foreseeable future to assess whether the going concern basis is appropriate or whether additional going concern disclosures are required in the financial statements.

The audit team should write to the company's lawyers to enquire of the existence and likelihood of success of any claim from the former financial controller.

### **Audit risk**

The financial controller has been dismissed and his tasks have been allocated between the finance department team, this has increased their workload.

This increases the inherent and control risk within Eagle as errors may have been made within the accounting records by the overworked finance team members and there is no one working in a supervisory capacity.

The purchase ledger supervisor left in August and no reconciliations of supplier statements and purchase ledger control account have been performed. There is an increased risk of errors within trade payables and the year-end payable may be under or overstated.

Preliminary analytical review of the draft statement of profit or loss has identified a significant fall in administration expenses.

Administration expenses tend to be fixed costs and hence would be unlikely to fluctuate significantly with changes in sales volumes. Hence there is a risk that administration expenses are understated.

### **Auditors response**

The team should remain alert throughout the audit for additional errors within the finance department.

In addition, discuss with the finance director whether he will be able to provide the team with assistance for any audit issues as there is no financial controller available.

The audit team should increase their testing on trade payables at the year end, with a particular focus on completeness of payables. A detailed review of the year-end purchase ledger control account reconciliation should be performed with a focus on any unusual reconciling items.

Update the analytical review with the full year results and if significant fluctuations on prior year remain, discuss these with management. Obtain supporting evidence to verify management explanations.

## **3 (a) Benefits of audit committee for Bluebird Enterprises Co**

Appointing an audit committee will benefit Bluebird in the following ways:

- Bluebird does not currently have any non-executive directors, hence once appointed, they will bring considerable external experience to the board as well as challenging the decisions of executive directors and contributing to independent judgements.
- The finance director will benefit in that he will be able to raise concerns and discuss accounting issues with the audit committee.
- It will help to improve the quality of the financial reporting of Bluebird; whilst the company already has a finance director, the audit committee will assist by reviewing the financial statements.
- The establishment of an audit committee can help to improve the internal control environment of the company. The audit committee is able to devote more time and attention to areas such as internal controls.
- If Bluebird has an internal audit (IA) department, then establishing an audit committee will also improve the independence of IA.
- The audit committee can also provide advice on risk management to the executive directors. They can create a climate of discipline and control and reduce the opportunity for fraud, and increase public confidence in the credibility and objectivity of the financial statements.
- The audit committee will assume responsibility for appointing and liaising with the external audit firm, thus ensuring the independence of the external auditor especially in cases of dispute with management.

## **(b) Advantages and disadvantages of potential non-executive directors (NEDs)**

### **Advantages**

- (i)** Antony Goldfinch already has experience of being a NED for another company and he has sat on an audit committee, hence he will be familiar with what the role entails and will be able to bring experience of being a NED to Bluebird. In addition, Antony Goldfinch has indicated he is agreeable to being paid a fixed fee which is not profit related; this is important as an independent NED's remuneration should be unrelated to the performance of the company.
- (ii)** Jacob Mallard is currently a finance director and so he possesses recent and relevant financial experience which is required for at least one member of the audit committee. In addition, he operates in the retail industry and so would be aware of key issues facing companies like Bluebird and so would have an appropriate mix of experience and knowledge.

### **Disadvantages**

- (i)** Appointing Antony Goldfinch as a NED has disadvantages as he works for a banking company and so would not have relevant experience of companies such as Bluebird; hence he could lack the critical skills and relevant experience needed to provide meaningful advice to the executive directors. In addition, Antony Goldfinch is already an executive director for a large multinational company and a NED for another company; it might be difficult for him to devote sufficient time to his role at Bluebird.
- (ii)** Jacob Mallard is the brother of the chief executive and therefore he is not an independent NED. He might be inclined to agree with the chief executive as he is his brother rather than providing the level of objective judgement required from a NED. Also he wants a contract as a NED for a period of seven years; all directors including NEDs must be subject to re-election at regular intervals not exceeding three years.

#### 4 (a) Audit report elements and why included

The following elements should be included within an auditor's report along with why:

**Title** – The auditor's report shall have a title which clearly indicates that it is the report of an independent auditor, this distinguishes this report from any other.

**Addressee** – The auditor's report shall be addressed as required by the circumstances of the engagement, this is determined by law or regulation but is usually to the shareholders. This clarifies who may rely on the opinion and who may not, such as third parties.

**Introductory paragraph** – The introductory paragraph in the auditor's report shall identify the entity whose financial statements have been audited, state that the financial statements have been audited, identify the title of each statement which comprises the financial statements, refer to the summary of significant accounting policies and other explanatory information and specify the date or period covered by each financial statement. This paragraph aims to clarify what time period the audit covers and which pages of the financial statement have been audited, as not every page is audited.

**Management's responsibility for the financial statements** – This section of the auditor's report describes the responsibilities of those in the organisation who are responsible for the preparation of the financial statements. This paragraph along with that of the auditor's responsibilities looks to make clear what the role of management is, as well as what the role of the auditor is. It seeks to reduce the expectation gap.

**Auditor's responsibility** – The auditor's report shall state that the responsibility of the auditor is to express an opinion on the financial statements based on the audit and that the audit was conducted in accordance with International Standards on Auditing and ethical requirements and that the auditor plans and performs the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. Along with the management's responsibility paragraph, it seeks to make clear the role of the auditor and also what management's role is. Also this paragraph seeks to explain what an audit involves and that only material misstatements are considered, as opposed to all errors.

**Opinion paragraph** – When expressing an unmodified opinion, the auditor's opinion shall either state that the financial statements 'present fairly' or 'give a true and fair view' in accordance with the applicable financial reporting framework. This paragraph details whether the financial statements are true and fair or not.

**Other reporting responsibilities** – If the auditor addresses other reporting responsibilities in the auditor's report, these shall be addressed in a separate section in the auditor's report titled 'Report on Other Legal and Regulatory Requirements'. This is important where there is local legislation which requires reporting on; this needs to be clearly identified in the report as this is in addition to the requirement of the ISAs.

**Signature of the auditor** – The auditor's report must be signed, this can be either the personal name of the auditor or, the signature is on behalf of the firm, depending on the jurisdiction in which the auditor is operating. This clarifies which firm or auditor has performed the audit engagement.

**Date of the auditor's report** – The auditor's report shall be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements. The date of the audit report is important in the case of subsequent events which impact the financial statements; the auditor's role is different depending on whether the audit report was signed or not when the subsequent event came to light.

**Auditor's address** – The auditor's report shall name the location where the auditor practises. This is useful in case shareholders need to contact the auditors.

#### (b) Subsequent event

A key customer of Bullfinch.com has just notified the company that they are experiencing cash flow difficulties and are unlikely to make any payments for the foreseeable future. This information was received after the year end but provides further evidence of the recoverability of the receivable balance at the year end. If the customer is experiencing cash flow difficulties just a few months after the year end, then it is highly unlikely that the year-end receivable was recoverable as at 31 October and hence is an adjusting event.

The receivables balance is overstated and consideration should be given to adjusting this balance, if material, through the use of an allowance for receivables or by being written off. The total amount outstanding at the year end was \$283,000 and is material as it represents 7.4% (0.283/3.8m) of profit before tax and 2.5% (0.283/11.2m) of revenue. Hence, the directors should amend the 2014 financial statements by writing down or writing off the receivable balance.

The following audit procedures should be applied to form a conclusion as to the level of the adjustment:

- The correspondence with the customer should be reviewed to assess whether there is any likelihood of payment.
- Discuss with management as to why they feel an adjustment is not required in the 2014 financial statements.
- Review the post year-end period to see if any payments have been received from the customer.

5 (a) Board of directors  
Hummingbird Co  
23 Buzzard Lane  
Peregrine City  
Hawk Country

4 December 2014

Dear Sirs,

**Audit of Hummingbird Scents Co (Hummingbird) for the year ended 30 September 2014**

Please find enclosed the report to management on deficiencies in internal controls identified during the audit for the year ended 30 September 2014. The appendix to this report considers deficiencies in the sales system and recommendations to address those deficiencies.

Please note that this report only addresses the deficiencies identified during the audit and if further testing had been performed, then more deficiencies may have been reported.

This report is solely for the use of management and if you have any further questions, then please do not hesitate to contact us.

Yours faithfully

An audit firm

**APPENDIX**

**Deficiency**

Brenda the sales clerk receives customer orders, raises sales invoices and processes payments for hotel customers. This is a lack of segregation of duties and could lead to a risk of fraudulent transactions or errors, as no one checks the work undertaken by this clerk.

Hotel customers have contracted sales prices; however, as online trade prices are automatically loaded into the sales invoices, Brenda has to manually amend the invoices.

This significantly increases the risk of error, as if Brenda incorrectly increases the sales prices, then this can lead to a loss of customer goodwill and if they are too low, this results in a loss of revenue for Hummingbird.

Credit limits are determined by the finance director when a new trade customer is set up in the system. However, these limits could be out of date, resulting in limits being too high and sales being made to poor credit risks or too low and Hummingbird losing potential revenue.

Customer orders and goods despatched notes (GDN) are given a number based on the customer account number and order number. These numbers are not sequential. Without sequential numbers, it is difficult for Hummingbird to identify missing orders and to monitor if all orders are being despatched in a timely manner, leading to a loss of customer goodwill.

Hummingbird has changed from a reliable national courier company to a cheaper local courier; as a result some orders have been delivered late. There is a risk that orders may be lost resulting in a loss of revenue for Hummingbird or orders arriving later than normal which would lead to a loss of customer goodwill.

Trade customers' sales invoices are automatically generated by the system at the same time that the online order is placed. However, if goods are not despatched straight away, then customers could be invoiced in advance of receipt of their goods. This is likely to lead to a loss of customer goodwill and the early recognition of revenue in the accounting records.

**Control**

Another sales ledger clerk should be involved in the processing of hotel customer transactions so that no one individual undertakes all elements of the sales cycle. The work could be split so that one clerk raises orders and invoices but a second clerk processes the payments.

As hotel customers account for 40% of revenue, consideration should be given to amending the sales system so that each customer's agreed prices are pre-loaded, therefore no manual amendment of invoices would be required.

If this is not feasible, then all sales invoices for hotel customers should be double checked by another member of the finance department prior to being sent out.

Customer credit limits should be regularly reviewed by the finance director and updated based on the level of sales transactions and credit risk.

Sales orders and goods despatched notes should be sequentially numbered. On a regular basis, a sequence check of orders should be undertaken to identify any missing orders. Upon despatch, the GDN should be matched to the order; a regular review of unmatched orders should be undertaken to identify any unfulfilled orders.

The courier company should be set targets with regards to timeliness of despatches. A review should be undertaken of target despatch times and actual times taken by the new courier company. If late delays continue, then consideration should be given to changing back to the original courier company.

The system should be amended so that it links into the despatch system. Sales invoices should not be raised until after goods have been despatched.

**Deficiency**

If Hummingbird makes special offers or discounts sales, the master file data for sales prices is amended by a senior sales ledger clerk. There is a risk that these amendments could be made incorrectly resulting in a loss of sales revenue or overcharging of customers.

In addition, the sales ledger clerk, although senior, is not senior enough to be given access to changing master file data as this could increase the risk of fraud.

Monthly statements are not sent to trade customers. If statements are not sent regularly, this increases the likelihood of errors and any disputed invoices not being quickly identified and resolved by Hummingbird.

The sales ledger control account is only reconciled at the end of September in order to verify the year-end balance. If the sales ledger is only reconciled annually, there is a risk that errors will not be spotted promptly.

**Control**

When special offers or discounted sales occur, the changes to master file data should be made by a supervisor and each change checked by a responsible official to reduce the risk of errors occurring.

Amendments to master file data should be restricted so that only supervisors and above can make changes.

Hummingbird should produce monthly customer statements for both hotel and trade customers and send them out promptly.

The sales ledger control account should be reconciled on a monthly basis to identify any errors. The reconciliations should be reviewed by a responsible official and they should evidence their review.

**(b) Substantive procedures for revenue**

- Compare the overall level of revenue against prior years and budget and investigate any significant fluctuations.
- Obtain a schedule of sales for the year broken down into the two categories of hotel and trade customers and compare this to the prior year breakdown and for any unusual movements discuss with management.
- Calculate the gross profit margin for Hummingbird and compare this to the prior year and investigate any significant fluctuations.
- Select a sample of sales invoices for hotel customers and agree the sales prices back to the contracted rates to ensure the accuracy of invoices.
- Select a sample of credit notes raised, trace through to the original invoice and ensure invoice correctly removed from sales.
- Select a sample of trade customer orders placed online and agree these to the despatch notes and sales invoices through to inclusion in the sales ledger to ensure completeness of revenue.
- Select a sample of despatch notes both pre and post year end; follow these through to sales invoices in the correct accounting period to ensure that cut-off has been correctly applied.

**6 (a) Reliance on the work of an independent valuer**

ISA 500 *Audit Evidence* requires auditors to evaluate the competence, capabilities including expertise and objectivity of a management expert.

This would include consideration of the qualifications of the valuer and assessment of whether they were members of any professional body or industry association. The expert's independence should be ascertained, with potential threats such as undue reliance on Jackdaw or a self-interest threat such as share ownership considered.

In addition, Puffin & Co should meet with the expert and discuss with them their relevant expertise, in particular whether they have valued similar land and buildings to those of Jackdaw Motor Cars Co (Jackdaw) in the past. Puffin & Co should also consider whether the valuer understands the accounting requirements of IAS 16 *Property, Plant and Equipment* in relation to valuations.

The valuation should then be evaluated. The assumptions used should be carefully reviewed and compared to previous revaluations at Jackdaw. These assumptions should be discussed with both management and the valuer to understand the basis of any valuations.

**(b) (i) Substantive procedures for land and buildings**

- Obtain a schedule of land and buildings revalued this year and cast to confirm completeness and accuracy of the revaluation adjustment.
- On a sample basis agree the revalued amounts to the valuation statement provided by the valuer.
- Agree the revalued amounts for these assets are included correctly in the non-current assets register.
- Recalculate the total revaluation adjustment and agree correctly recorded in the revaluation surplus.
- Agree the initial cost for the warehouse addition to supporting documentation such as invoices to confirm cost.
- Confirm through a review of the title deeds that the warehouse is owned by Jackdaw.
- Recalculate the depreciation charge for the year to ensure that for assets revalued during the year, the depreciation was based on the correct valuation and for the warehouse addition that the charge was for nine months only.
- Review the financial statements disclosures of the revaluation to ensure they comply with IAS 16 *Property, Plant and Equipment*.

**(ii) Substantive procedures for work in progress (WIP)**

- Prior to attending the inventory count, discuss with management how the percentage completions are attributed to the WIP, for example, is this based on motor cars passing certain points in the production process.
- During the count, observe the procedures carried out by Jackdaw staff in assessing the level of WIP and consider the reasonableness of the assumptions used.
- Agree for a sample that the percentage completions assessed during the count are in accordance with Jackdaw's policies communicated prior to the count.
- Discuss with management the basis of the standard costs applied to the percentage completion of WIP, and how often these are reviewed and updated.
- Review the level of variances between standard and actual costs and discuss with management how these are treated.
- Obtain a breakdown of the standard costs and agree a sample of these costs to actual invoices or payroll records to assess their reasonableness.
- Cast the schedule of total WIP and agree to the trial balance and financial statements.
- Agree sample of WIP assessed during the count to the WIP schedule, agree percentage completion is correct and recalculate the inventory valuation.

**(c) Audit report**

Discuss with the management of Jackdaw why they are refusing to make the amendment to WIP.

Assess the materiality of the error; if immaterial, it should be added to the schedule of unadjusted differences. The auditor should then assess whether this error results in the total of unadjusted differences becoming material; if so, this should be discussed with management; if not, there would be no impact on the audit report.

If the error is material and management refuses to amend the financial statements, then the audit report will need to be modified. It is unlikely that any error would be pervasive as although WIP in total is material, it would not have a pervasive effect on the financial statements as a whole. As management has not complied with IAS 2 *Inventory* and if the error is material but not pervasive, then a qualified opinion would be necessary.

A basis for qualified opinion paragraph would need to be included before the opinion paragraph. This would explain the material misstatement in relation to the valuation of WIP and the effect on the financial statements. The opinion paragraph would be qualified 'except for'.

	<i>Marks</i>
<b>Section A</b>	
Questions 1–12 multiple choice	<u><b>20</b></u>
<b>Section B</b>	
<b>1 (a)</b> Up to 1 mark per well explained point. <ul style="list-style-type: none"><li>– Important areas of the audit</li><li>– Potential problems</li><li>– Effective and efficient audit</li><li>– Selection of engagement team members and assignment of work</li><li>– Direction, supervision and review</li><li>– Coordination of work</li></ul>	<u>5</u>
<b>(b)</b> Up to 1 mark per well described procedure. <ul style="list-style-type: none"><li>– Discuss with management as to whether they are aware of any additional payroll frauds</li><li>– Review board minutes</li><li>– Discuss with the payroll manager the nature of the payroll fraud, how it occurred and the impact</li><li>– Review supporting documentation to confirm the total of the fraudulent payments made</li><li>– Review and test the internal controls surrounding setting up of and the payments to new joiners</li><li>– Consider if other information obtained indicates risks of material misstatement due to payroll fraud</li><li>– Obtain a written representation from management</li></ul>	<u>5</u>
	<u><b>10</b></u>
<b>2</b> Up to 1 mark per well explained risk and up to 1 mark for each well explained response. Overall max of 5 marks for risks and 5 marks for responses. <ul style="list-style-type: none"><li>– Inventory valuation</li><li>– Receivable valuation</li><li>– Going concern</li><li>– Unfair dismissal of financial controller</li><li>– Increased inherent risk of errors in finance department due to loss of financial controller</li><li>– Under or overstated trade payables</li><li>– Completeness of administration expenses</li></ul>	<u>10</u>
	<u><b>10</b></u>

3 (a) Up to 1 mark per well explained point.

- Non-executives will bring outside experience to the board
- The finance director will be able to raise concerns with the audit committee
- Improve the quality of the financial reporting
- Improve the internal control environment of the company
- Establishing an audit committee will improve the independence of internal audit
- Provide advice on risk management to the executive directors
- Responsibility for appointing and liaising with external auditors; reducing the work load of the finance director

4

(b) Up to 1 mark per well explained point, max of 3 marks for advantages and max of 3 marks for disadvantages. Max of 3 marks for each director, overall max of 6 marks in total.

**Advantages**

- Antony Goldfinch has experience as a NED and of audit committee role
- Antony Goldfinch has agreed to a non-profit related fee
- Jacob Mallard has relevant and recent financial experience as he is a finance director
- Jacob Mallard operates in the retail industry

**Disadvantages**

- Antony Goldfinch could lack critical skills and relevant experience of the retail industry
- Antony Goldfinch may not have sufficient time as he has a number of roles already
- Jacob Mallard is the brother of the chief executive and so is not independent
- Jacob Mallard wants a seven-year fixed contract which is contrary to corporate governance principles

6

**10**

4 (a) Up to 1 mark per well described element and explanation of why included.

- Title
- Addressee
- Introductory paragraph
- Management responsibility
- Auditor's responsibility
- Opinion paragraph
- Other reporting responsibilities
- Signature of the auditor
- Date of the auditor's report
- Auditor's address

4

(b) Up to 1 mark per valid point, max of 3 marks for whether financial statements require amendment and max of 3 marks for procedures.

- Provides evidence of conditions at the year end
- Adjusting event
- Calculation of materiality
- Receivable to be written down or an allowance for receivable used
- Customer correspondence reviewed
- Discuss with management why no adjustment in 2014 financial statements
- Review the post year-end period for payments

6

**10**

- 5 (a) Up to 1 mark each per well explained deficiency and recommendation. If not well explained, then just give ½ marks for each. Overall maximum of 7 marks each for deficiencies and recommendations.

2 marks for presentation: 1 mark for address and intro and 1 mark for conclusion.

- Lack of segregation of duties for sales ledger clerk processing hotel customer transactions
- Manual override of sales invoices for hotel customers
- Credit limits set up when trade customer established, limits not regularly reviewed
- Sales orders and goods despatch notes not sequentially numbered
- Change to a cheaper courier company to despatch goods increases risk of customer complaints
- Trade customers' sales invoices generated on order date, goods may not have been despatched at this stage
- Senior sales clerk amends master data file for special offers and discount sales
- Monthly statements not sent to trade customers
- Sales ledger control account only reconciled at the year end

16

- (b) Up to 1 mark per well explained procedure.

- Analytical review over revenue compared to budget and prior year
- Analytical review of two categories of sales compared to prior year
- Gross margin review
- Agree sales prices for hotel customers to contracted rates
- Review credit notes
- Follow trade online orders to goods despatched note to sales invoice to sales ledger
- Sales cut-off

4

20

- 6 (a)** Up to 1 mark per valid point.
- ISA 500 requires consideration of competence and capabilities of expert
  - Consider if member of professional body or industry association
  - Assess independence
  - Assess whether relevant expertise of type of properties as Jackdaw Motor Cars Co
  - Evaluate assumptions
- 5
- (b)** Up to 1 mark per well explained procedure, overall max 6 marks for land and buildings and max of 4 marks for work in progress.
- (i) Land and buildings**
- Cast schedule of land and buildings revalued this year
  - Agree the revalued amounts to the valuation statement provided by the valuer
  - Agree the revalued amounts included correctly in the non-current assets register
  - Recalculate the total revaluation adjustment and agree recorded in the revaluation surplus
  - Agree the initial cost for the warehouse to invoices to confirm cost
  - Confirm through title deeds that the warehouse is owned by Jackdaw
  - Recalculate the depreciation charge for the year
  - Review the financial statements disclosures for compliance with IAS 16 *Property, Plant and Equipment*
- 6
- (ii) Work in progress**
- Discuss with management how the percentage completions are attributed to WIP
  - Observe the procedures carried out in the count in assessing the level of WIP; consider the reasonableness of the assumptions used
  - During the count, agree a sample of percentage completions are in accordance with Jackdaw's policies
  - Discuss with management the basis of the standard costs
  - Review the level of variances between standard and actual costs
  - Obtain a breakdown of the standard costs and agree a sample of these costs to actual invoices
  - Cast the schedule of total WIP and agree to the trial balance and financial statements
  - Agree sample of WIP assessed during the count to the WIP schedule, agree percentage completion is correct and recalculate the inventory valuation
- 4
- (c)** Up to 1 mark per well explained valid point.
- Discuss with management why they are refusing to make the amendment
  - Assess the materiality of the error
  - If immaterial, add to the schedule of unadjusted differences and assess if total errors material
  - If material but not pervasive, modified audit report, material misstatement, qualified opinion
  - Basis for qualified opinion paragraph required
  - Opinion paragraph – except for
- 5

**20**