THE UNIVERSITY OF NEW SOUTH WALES

Faculty of
Commerce and Economics

School of Accounting

ACCT 3708
AUDITING AND ASSURANCE SERVICES

COURSE OUTLINE

Session 2, 2003

CONTENTS

Workshop Program:

THE UNIVERSITY OF NEW SOUTH WALES

SCHOOL OF ACCOUNTING

ACCT3708 AUDITING AND ASSURANCE SERVICES

SESSION 2 2003

COURSE OUTLINE AND STUDY GUIDE

1. Description of Course:

This course examines the practice of auditing and the concepts which underlie the practice. Although the focus of attention is on audits carried out under the provisions of the Australian Corporations & Securities Legislation, reference is also made to other forms of audit. The course is intended to provide an overview of the audit process as it exists in Australia. Although the auditing course is broken into a number of segments, students should recognise that each segment forms part of the audit process.

2. Course Objectives:

(a) To develop students' understanding of the audit function and of the reasons for an audit.

(b) To familiarise students with the professional, legal, commercial and regulatory constraints within which audits are carried out.

(c) To examine techniques used by auditors including risk analysis, evidence collection and evaluation, and audit reporting.

(d) To familiarise students with current developments in audit practice and research.

3. Prescribed Textbooks, and References:

(a) Prescribed Textbooks:

CPA Australia and the Institute of Chartered Accountants in Australia, Auditing Handbook, 2003, Vol. 2 of the Accounting and Auditing Handbook, Prentice-Hall.

Gay G., & R. Simnett "Auditing and Assurance Services in Australia" (2nd Edition) McGraw-Hill, Sydney 2003. Note : This text is available as a package with the "MaxMark" student resource which includes a test bank of multiple choice questions.

P. Roebuck & N. Martinov "Case Studies in Auditing & Assurance" (3nd Ed.) Butterworths, 2003.

(b) Additional References:

Students will find many other auditing textbooks which will provide additional supplementary information. Some of these are available on closed reserve in the main library.

4. Course Arrangements:

Instruction in this course consists of a three-hour workshop each week. It should be emphasised that attendance at classes is a necessary but not sufficient condition for adequate examination preparation. All students should keep up to date with recommended references and participate in workshop discussions. (Note: Workshop solutions will not be made available either on the Web or in open reserve.)

5. Assessment:

Subject to a satisfactory result in the final examination, the weighting of the final (composite) mark will be as follows:

Workshop Quiz (Week 5)	5%
Mid-Session Test (Week 7)	25%
Assignment (Week 11)	20%
Final Examination	50%
	100%
	===

NB: Students who do not obtain a satisfactory result in the final examination may still obtain a composite mark in excess of 50 and fail the subject. In such instances a UF grade will be recorded - which means that there has been unsatisfactory performance in an essential component of the course.

Date of Mid-Session

The mid-session test will be held during Week 7 on Friday 12th September and will cover all material up to and including week 6 (workshop 5). Location and timing of the Exam will be finalised during session.

NO SUPPLEMENTARY TESTS WILL BE HELD FOR THE MID-SESSION TEST.

The final examination will cover the whole semester's work.

Except in exceptional circumstances, ***no supplementary examinations*** will be given if requests (for special consideration) are received more than ten days after the final examination in this subject.

Students should note that there will be only one supplementary examination. Note also that it is university policy to advise the granting of supplementary exams via your student email address.

6. Staff:

Staff participating in this course are:

	Room	Telephone
Wendy Green (Lecturer-in-charge and Honours Co-ordinator)	Quad Room 3092	9385 5805
Fiona Foster	Quad Room 3113	9385 5907
Tatjana Lovelady	Quad Room 3113	9385 5907

Staff consultation hours will be advised in workshops. Note that consultation in person is the recommended consultation mode. Any problems with the course should be directed in the first instance to your workshop leader.

7 In addition, a web site for prescribed text book Gay & Simnett "Auditing and Assurance Services in Australia" is available should you wish to use it (this is not mandatory):

The web site is accessible at http://www. mhhe.com/au/gay2e. The site contains information for students such as an On-line Learning Centre, Weblinks and an Auditing News Centre.

ACCT 3708/ACCT3718 AUDITING AND ASSURANCE SERVICES - Provisional Workshop Schedule

Week	Week Beginning		Topic
1	July	28	**Lecture -** Introduction to Audit Function, Assurance Framework, Professional Standards and Structure of the Profession.
2	August	4	**Workshop 1 -** Introduction to the Audit Process, Risk and Audit Planning.
3	August	11	**Workshop 2 -** Control Risk Evaluation and Tests of Controls.
4	August	18	**Workshop 3 -** Evaluation of Detection Risk and Substantive Testing.
5	August	25	**Workshop 4 -** Analytical Procedures. **Class Quiz**
6	September	1	**Workshop 5 -** Assessment of Materiality and Development of the Audit Strategy.
7	**September**	**8**	**MID-SESSION EXAM – 12h September**
8	September	15	**Workshop 6 -** Auditing in a CIS Environment — Internal Control.
9	September	22	**Workshop 7 -** Auditing in a CIS Environment — Substantive Testing.
	Sept 29 to	**Oct 5**	**RECESS**
10	October	6	**Workshop 8 -** Using the Work of Others/Internal Audit/Public Sector Auditing **Public Holiday Monday 6 October**
11	October	13	**Workshop 9 - ASSIGNMENT PRESENTATIONS**
12	October	20	**Workshop 10 -** Legal Liability/Ethics.
13	October	27	**Workshop 11 -** Completing the Audit Process and Audit Reporting.
14	November	3	**Workshop 12 –** Course Review and Current Issues

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Introduction to the Audit Function, Assurance Framework, Professional Standards and Structure of the Profession

LECTURE: Week beginning 28 July 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 1, Chapter 2 and Chapter 14

Standards:

AUS 106:	Explanatory Framework for Standards on Audit and Audit Related Services.
AUS 202:	Objective and General Principles Governing an Audit of a Financial Report.
AUS 206:	Quality Control for Audit Work.
AUS 210:	Fraud and Errors.

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Introduction to the Audit Process, Risk and Audit Planning

WORKSHOP 1: Week beginning 4 August 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 5 (pages 175-182, 190-213)
Gay and Simnett, Chapter 6 (pages 226-253)

Standards:

AUS 302: Planning.
AUS 304: Knowledge of the Business.
AUS 306: Materiality.
AUS 402: Risk Assessments and Internal Controls.

A REVISION QUESTIONS

MaxMark Topics 1, 2 and 14

B PREPARATION QUESTIONS

1. Roebuck & Martinov Case 1.3 Parts 1 – 3 Pages 13-15. Solution Page 206-208.
2. Roebuck & Martinov Mock Exam No. 1 Question 1 Part (i) pg 163 and Solution pg. 169.

C HOMEWORK QUESTIONS

1. Roebuck & Martinov
   Chapter 10, Question 5, Page 194.

2. Roebuck & Martinov
   Chapter 10, Question 6, Page 194.

D CLASS GROUP DISCUSSION QUESTIONS

1. Roebuck & Martinov Case 1.5 Part 1, Pages 19 –20.

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Control Risk Evaluation and Tests of Controls

WORKSHOP 2: Week beginning 11 August 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 8 (pages 321-349)
Gay and Simnett, Chapter 9 (pages 383-390)

Standards:

AUS 402 Risk Assessments and Internal Controls.

AGS 1006: Expression of an Opinion on Internal Control.

A REVISION QUESTIONS

MaxMark Topics 5 and 6

B PREPARATION QUESTIONS

1. Roebuck & Martinov Case 2.6 Parts 1 and 2 page 32 –34. Solution pages 209-210.

2. Roebuck & Martinov Mock Exam No. 1 Question 3 page 165. Solution Page 170.

C HOMEWORK QUESTIONS

1. The University recently opened a parking station on its lower campus area for the benefit of the students. A guard has been engaged to patrol the lot and to issue parking stickers to University students who submit an application for and show evidence of enrolment. When the sticker is affixed to the car, the student may park in the lot for six hours by placing a dollar in the parking meter. The guard inspects the stickers on all parked cars to determine that only students are parking in the lot and also looks at the time gauges to see that the meter reflects the necessary fee has been paid. The completed application forms are maintained in the guard's office.

   By using the master key, the guard empties the meters weekly and delivers the cash to the University central store department where a clerk opens it, manually counts the coins, puts the cash in a safe, and records the total on a weekly cash report. This report is sent to the University's accounting department. The day following the cash count, the University cashier picks up the cash and manually recounts it, prepares the deposit slip, and makes the deposit at the bank. The deposit slip, authenticated by the bank teller, is sent to the accounting department where it is filed with the weekly cash report.

Required:

Describe weaknesses in the existing system. Recommend for each weakness at least one improvement to strengthen the internal accounting control over the parking station cash receipts.

2. Roebuck & Martinov Mock Exam No 2 Question 2 page 174.

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 1, 2002, Exam Question 2**

Modern Ltd is a large manufacturing organisation which through seasonal trends occasionally has surplus funds available for investment in marketable securities. The following represents a brief description of its procedures in dealing with securities transactions.

Investments in marketable securities are acquired through banks and brokers. The company does not have any regular broker through which security dealings are normally negotiated.

The board has recently delegated general authority to the treasurer (a non-board member) for the dealings in all securities of a short term nature. All securities purchased are held in the treasurer's safe to which only the treasurer and the treasurer's secretary have access (note either person can access the safe without the knowledge of the other party).

The treasurer initiates all purchases and disposals by telephone. Payments are made by the treasurer submitting a cheque request to the disbursements clerk to initiate a manual cheque rather than putting a sensitive transaction through normal mechanical cheque producing facilities. A copy of the brokers' advise is given to the accounting clerk in order to record the transaction. This advice is usually delivered by the secretary who also collects and mails the cheque to the broker. The treasurer keeps no subsidiary records of security dealings, however a report is given yearly to the board for their approval.

Required:

2 **a) Identify five (5) internal control weaknesses for Modern Ltd.**

2 **b) Discuss the potential overall impact of the identified weaknesses on the Financial Statements of Modern Ltd.**

c) Discuss the role and responsibility of each of the following groups in relation to the internal control system of Modern Ltd:

3 **(i) Management**

(ii) Audit Committee (assuming that one exists)

(iii) External Auditor

2. Session 2, 2002, Exam Question 2

Everyday Supplies Pty Ltd is a single-store retailer that sells a variety of tools, garden supplies, timber, small appliances, and electrical fixtures to the public, although about half of Everyday Supplies' sales are to construction contractors on account.

Retail customers pay for merchandise by cash or credit card at cash registers when merchandise is purchased. A contractor may purchase merchandise on account, if approved by the credit manager. This approval is based only on the manager's familiarity with the contractor's reputation. After credit is approved, the sales assistant files a pre-numbered order form with the accounts receivable supervisor to set up the receivable.

The accounts receivable supervisor independently verifies the pricing and other details on the order form by reference to a management-authorised price list, corrects any errors, prepares the invoice, and supervises a part-time employee who mails the invoice to the contractor. The accounts receivable supervisor electronically posts the details of the invoice in the accounts receivable subsidiary ledger and at the end of the day the total is automatically posted to the general ledger. The accounts receivable supervisor also prepares a monthly computer-generated accounts receivable subsidiary ledger and a monthly report of overdue accounts. Because of the automatic posting the accounts receivable subsidiary ledger is not reconciled with the accounts receivable control account in the general ledger.

The cash receipts functions are performed by the cashier, who also supervises the cash register clerks. The cashier opens the mail, compares each cheque with the enclosed remittance advice, stamps each cheque "for deposit only", and lists cheques for deposit. The cashier then gives the remittance advices to the bookkeeper for recording. The cashier prepares two deposit slips, one for cheques received each day and one for daily cash register receipts. These are banked at the end of each day. The cashier retains the verified deposit slips to assist in reconciling the monthly bank statements, but forwards to the bookkeeper a copy of the daily cash register summary. The cashier does not have access to the journals or ledgers.

The bookkeeper receives the details of transactions from the accounts receivable supervisor and the cashier for journalising and posting to the general ledger. After recording the remittance advices received from the cashier, the bookkeeper electronically transmits the remittance information to the accounts receivable supervisor for subsidiary ledger updating. The bookkeeper sends monthly statements to contractors with unpaid balances upon receipt of the monthly report of overdue balances from the accounts receivable supervisor. The bookkeeper authorises the accounts receivable supervisor to write off accounts as uncollectible when six months have passed since the initial overdue notice was sent. At this time, the credit manager is notified by the bookkeeper not to grant additional credit to that contractor.

Required:

7.5 a) Describe five internal control weaknesses in Everyday Supplies' internal control structure for the cash receipts and billing functions. Explain briefly why each is a weakness.

NOTE: Provide your answer in the following format:

Internal Control Weakness	Explanation of Weakness

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Evaluation of Detection Risk and Substantive Testing

WORKSHOP 3: Week beginning 18 August 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 5 (pages 182-190)

Standards:

AUS 502: Audit Evidence.

A REVISION QUESTIONS

MaxMark Topics 8 and 9

B PREPARATION QUESTIONS

1. Roebuck & Martinov Mock Exam No 1 Question 1 page 163-4 and solution p169.
2. Roebuck & Martinov Case 9.3 Page 186 and Solution page 241-2.

C HOMEWORK QUESTIONS

1. Roebuck & Martinov Mock Exam No 2, Question 4 Page 177-8.

2. For each of the three (3) key audit risks described below complete the following:

   (i) provide a brief **explanation** as to why the situation constitutes an audit risk
   (ii) identify the **key** account balance affected
   (iii) identify the **prime** audit assertion to be tested
   (iv) for the account balance and the assertion listed in (ii) and (iii) describe in specific terms the **substantive audit procedure** which would best address the risk.

   The situations are independent of each other and are to be treated separately in your answers.

(a) Slim and Fit Limited is a manufacturer of sporting equipment. The majority of the merchandise is highly desirable, easily handled and of relatively high dollar value. Pilfering has been an ongoing problem.

(b) Cold and Frosty Limited is a manufacturer of refrigerators. The government has passed environmental legislation to become effective in the next eighteen months which will require Cold and Frosty to substantially modify and replace its current manufacturing process and equipment.

(c) Holford Limited is a manufacturer of cars. Their new range of sports coupe 'EAGLE' has been a great success with huge sales in the last twelve months. However, there has been a great number of customer complaints and a dramatic increase in the servicing and repairs of this model in the last three months. It appears that the material used in the brake linings which is unique to 'EAGLE' is defective after 8,000 kilometres. There is no stock of 'EAGLE' at year end due to a waiting list as a result of the popular demand for the car.

3. Roebuck & Martinov Case 9.4 Part A, page 187

D CLASS GROUP DISCUSSION QUESTIONS

1. Session 1, 2002 Exam Question 1 [20 Marks]

Your audit client ABC Limited (ABC) a listed company, has presented you with the following information:

	Unaudited (projected)	Audited	Industry
	2002	**2001**	**2001**
Liquidity ratio	0.84	0.69	1.02
Gearing ratio	0.70	0.48	0.60
No. of times interest earned	3.02	5.02	4.0
Earnings per share	85.42¢	54.29¢	63.25¢
Return on equity	0.38	0.28	0.35
Net tangible assets per share	$5.40	$4.80	$4.20
Share price	$7.82	$9.50	$9.50
Inventory turnover	4.8	5.0	6.0

Additional information:

- ABC is in an industry which manufactures and distributes stationery. It is a mature industry with traditional customer loyalty being eroded by the introduction of large warehouse style outlets.
- Demand for the product is "flat" within Australia. There is a trend towards discounted brands by customers. As a result ABC has embarked on an intensive advertising campaign.
- ABC has been attempting to move vigorously into the Asia/Pacific region due to the intense competition locally.
- As a result of the Prices Surveillance Authority, a recent press release stated that ABC's products would remain subject to price controls. Plans to build a new factory have been scrapped.

- A potential takeover by a US company was announced in the last three (3) months.

Required:

a) Based on the preliminary analytical procedures and the additional information provided:

4 **(i) Identify and describe four (4) risks which you would consider in planning the audit for the 2002 year end;**

4 **(ii) For each of the risks identified in (i), indicate which account is most at risk;**

4 **(iii) For the account identified in (ii), identify the relevant financial report assertion most affected;**

4 **(iv) Outline a specific substantive audit procedure to address the account and assertion at risk identified in (ii) and (iii) above.**

b) Your audit plan for sales for ABC places substantial reliance on the system of internal control and the use of analytical procedures. Your tests of control on the internal control system for sales has found a significant number of instances where customer's credit ratings have not been checked and abnormally large discounts have been given. The sales manager states that these changes have been the result of difficulties in maintaining past sales levels.

2 **(i) Identify the prime account other than sales, and the financial report assertion at risk in the above situation.**

2 **(ii) Considering that your control risk has now increased for the risky account and assertion identified in (i) above, and assuming inherent risk to be high, outline an audit strategy in terms of Tests of Control/Analytical Procedures/ Substantive Tests of Detail.**

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Analytical Procedures

WORKSHOP 4: Week beginning 25 August 2003

CLASS QUIZ TO BE HELD IN THIS WORKSHOP

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 6 (pages 254-265)

Standards:

AUS 512 Analytical Procedures.

A REVISION QUESTIONS

MaxMark Topic 5

B PREPARATION QUESTIONS

1. Roebuck & Martinov Case 4.1 parts 1 & 2 page 58-59 and solution page 217-218.

C HOMEWORK QUESTIONS

1. Session 2, 2002, Exam Question 1 (12 Marks)

You are the audit senior on the audit of EasyFit Pty Ltd, a large manufacturer of shoes. EasyFit Pty Ltd's main market lies with 18 to 24 year olds.

This is the first year in which your firm has performed the audit (2002). As part of the planning work, you have performed analytical procedures on an annualised basis and compared the results to industry averages and last year's (2001) audited financial information. The results are given below:

	Ratio	Industry average 2002	Industry average 2001	EasyFit Pty Limited 2002	EasyFit Pty Limited 2001
1	Current ratio	2.84	3.27	1.89	2.24
2	Receivables turnover ratio	4.9	4.6	6.3	7.0
3	Inventory turnover ratio	3.7	3.8	5.0	5.5
4	Return on total assets	7%	5%	13%	11%
5	Net profit ratio	0.06	0.06	0.04	0.04
6	Gross margin	0.20	0.26	0.20	0.18

Required:

6 a) Discuss the conclusions that the auditor can draw from the above ratios about EasyFit's financial position and performance.

6 b) Identify potential audit risks the auditor would need to investigate.

NOTE: Provide your answer in the following format:

a) Conclusion drawn	b) Potential risks indicated by ratio to further investigate

2. Roebuck & Martinov, Chapter 10, Question 35, Page 199

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 1 1998 Question 3 Part B [6 MARKS]**

WGRS Ltd manufactures electrical components. In the economy, inflation is coinciding with a recession, and interest rates for WGRS have increased from 8% at the beginning of the year to 14% at the end of the year. There has also been an increase in overseas competition due to recent government tariff reductions. The company has tried to boost sales by relaxing its credit polity.

Consider the following extracts from the financial statements of WGRS Ltd

	($'000s) 1998	($'000s) 1997	% change
Sales	2,000	1,700	+18%
Cost of goods sold	1,050	1,000	+5%
Gross margin	47.5	41.2	+15%
Interest expense	132	128	+3%
Long term liabilities	1,600	1,600	–
Interest rate (at 30 June)	14%	8%	n/a
Inventory	500	250	+100%
Accounts receivable	670	480	+40%
Provision for doubtful debts	14	10	+40%
Current ratio	1.94	2.39	-19%
Quick ratio	1.23	1.78	-31%
Inventory turnover (times per year)	2.1 times	4 times	-48%
Debtors turnover (times per year)	3.05	3.62	-16%

REQUIRED:

Identify the concerns (if any) you have with the following accounts or ratios, and their implications for the audit.

(a) **Interest Expense/Long-term Liabilities**

(b) **Accounts Receivable/Provision for Doubtful Debts**

(c) **Current Ratio/Quick Ratio and associated balances.**

2. **Session 1 2003 Question 2 [10 MARKS]**

Question 2 (10 marks)

Your audit senior has provided you, the audit partner, with a memo on the results of the preliminary analytical procedures analysis for your client. The highlights are as follows:

(a) Inventory turnover increased from 2.5 times to 3.75 times.
(b) Depreciation expense has been about 2% of total assets for several years. This year it was only 1% of total assets.
(c) Interest expense has been about 6% of total debt; this year it was 8%.
(d) The quick ratio has decreased from 1.45 to 0.95.
(e) Average days payable decreased from 35 days to 29 days.
(f) Average days receivable increased from 28 days to 35 days.
(g) Price/earnings has decreased from 10 times to 8 times.
(h) Return on assets increased from 2.5% to 4%.

Required:

8 **a) Assuming that each of these is considered material to the audit risk assessment, provide two (2) reasons that explain each change in the client's ratios: one that suggests a normal consequence of business and one that would suggest increased audit risk.**

Present your answer in the following format:

Normal business explanation	Audit risk explanation

2 **b) Indicate which of the increased audit risk scenarios noted in part (a) suggest the valuation assertion is at risk.**

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Assessment of Materiality and Development of the Audit Strategy

WORKSHOP 5: Week beginning 1 September 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 7

Standards:

AUS 306: Materiality.

AUS 402: Risk Assessments and Internal Controls.

AASB1031: Materiality.

A REVISION QUESTIONS

MaxMark Topic 6.

B PREPARATION QUESTIONS

1. None.

C HOMEWORK QUESTIONS

1. Roebuck & Martinov Mock Exam No. 2 Question 3 Parts A, B and C. Page 175.

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 1, 2003 Exam Question 1 (10 marks)**

Question 1 (10 marks)

During the planning stage of your current audit of Micro Ltd, a small computer manufacturer, you determine that due to declining sales volumes in the face of increased competition Micro has been unable to maintain minimum cash balances as required by a major loan agreement. Moreover, a significant fourth quarter loss appears likely, leading to an overall loss for the year. This will be the first time Micro Ltd has sustained a loss in its five-year history. Further investigation of the computer industry reveals that several small manufacturers have failed during the past five years. The management of Micro Ltd has assured you that they are prepared to compete actively with the increased competition. Further, as a means of dealing with its severe liquidity problems, the management has decided to issue additional share capital.

Required:

5 a) Based on the above information, list five (5) specific factors that would affect your assessment of risk.

Note: refer to suggested answer format presented below.

2.5 b) For each factor noted in (a) identify which component of the audit risk model it affects.

2.5 c) For each factor noted in (a) describe the impact on the audit plan.

Present your answer in the following format:

Risk Factor	Audit/Risk Model Component	Impact on Audit Plan

2. **Session 2, 1999 Exam Question 1 (16 Marks)**

You are the auditor of a medium sized fashion textile manufacturer, ABC Limited (ABC), that at the beginning of the year was listed on the Australian Stock Exchange. The major reason for the listing was to fund a significant expansion into the Japanese fashion market. Due to an economic recession and first time costs associated with the expansion, it appears that the company will be struggling to meet the forecast contained in the prospectus prepared as part of the listing requirements. Exchange rates against the YEN are steady, however the government has announced a cut in tariffs which is expected to have an adverse effect on demand for locally produced textiles. Already, a number of customers have asked that orders be held.

Your preliminary analytical procedures reveal the following:

	1998	**1999**
Current ratio	1.9	2.1
Liquid ratio	0.8	0.5
Days debtors outstanding	40	54
Inventory turnover	63 days	110 days
Share price	$ 5.00	$ 3.50
Net asset backing	$ 5.00	$ 5.00

Your review of the control environment suggests that key controls such as, authorisation and attitude of management, are satisfactory.

Your detailed review of the sales/accounts receivable system shows that a copy of the prenumbered sales invoice accompanied by a dispatch notice is sent to the accounts receivable clerk, who updates the accounts receivable subsidiary ledger. The sequence of sales invoices is independently accounted for each month and the subsidiary ledger is reconciled to the general ledger. A listing of accounts receivable is produced monthly and reviewed by the accountant, and analytical procedures including variance from budget, are produced for each salesperson and reviewed by the sales manager. The company has no formal follow-up procedure for debtors who do not pay within the required 30 days.

The controls over the cash receipts are regarded as satisfactory. On receipt of payment from a debtor a listing of receipts plus any supporting documentation is forwarded to the accounts receivable clerk who posts the entries to the subsidiary ledger. An independent computer reconciliation of the amount posted to the subsidiary ledger is sent to the accountant who reconciles this to the daily receipts shown on the bank deposit slip.

REQUIRED:

(a) Identify and discuss three (3) issues of significance which are highlighted by the preliminary analytical procedures (i.e. the ratios). Determine their effect on your overall risk assessment. [3 marks]

(b) From the information provided identify six (6) significant factors, other than those discussed in (a) above, and their impact (i.e. increase or decrease) on the evaluation of inherent risk. [3 marks]

(**c) In relation to the sales/accounts receivable system identify ALL the**

- **internal control strength(s)**
- **internal control weakness(es)**

and relate each to the relevant financial report assertion. [3 marks]

(d) For the valuation assertion in relation to ABC's 'Accounts Receivable' evaluate (high/medium/low):

- **Control Risk,**
- **Inherent Risk,**
- **Detection Risk.**

Justify your evaluation with reference to the information provided. [3 marks]

(e) Devise an audit strategy (Tests of Control/Analytical Procedures/Substantive Tests of Detail) for the valuation assertion in relation to 'Accounts Receivable' based on the evaluation of Inherent and Control Risk performed in (d) above. Explain your decision. [2 marks]

(f) From an audit point of view, verifying the existence of accounts receivable is relatively easier than verifying the valuation of this asset (accounts receivable).

Outline specific substantive audit procedures that enable the auditor to obtain a reasonable assurance about:

- **Valuation, and**
- **Existence**

of accounts receivable. [2 marks]

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MID-SESSION EXAMINATION

WEEK BEGINNING 8 September 2003

A Mid-Session Examination worth 25% will be held during this week, on Friday 12th September. No workshops will be conducted.

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Auditing in a CIS Environment – Internal Control

WORKSHOP 6: Week beginning 15 September 2003

READING GUIDE

Textbook Reference:
Gay and Simnett, Chapter 8 (pages 349-360)
Gay and Simnett Chapter 9 (pages 415-420)

Standards:

AUS 214: Auditing in a CIS Environment.

A REVISION QUESTIONS

MaxMark Topic 7

B PREPARATION QUESTIONS

1. Roebuck and Martinov Case 2.6 page 34 and solution page 209

C HOMEWORK QUESTIONS

1. You have been assigned to the audit of a private company which operates a plant nursery with a turnover of $2 million a year. The total number of full-time employees working for the company is 10, together with 3 to 5 casual employees as and when required on weekends. The company is run by a husband and wife team who are the directors and shareholders and a full time accounts clerk, Margaret, who is responsible for all accounting related tasks including debtors, stock, payroll and creditors. All accounting functions are performed on a stand alone PC which runs purchased software from a software house which specialises in the nursery industry. The access to various applications is controlled by passwords. Margaret records passwords to each application in her top drawer. Back up diskettes for all applications are done on a regular basis, appropriately labeled and maintained in a "back-up" case next to the PC.

   As a security measure, the keyboard to the microcomputer has a locking mechanism to control access to the on/off switch. Each night the machine is locked and the key left at reception in case the directors need to access the computer.

   The office of the company is located in a large mobile caravan inside the nursery which is well fenced. The company trades 7 days a week but Margaret only works Mondays to Fridays. The office is also used by various members of the staff to process sales invoices and dispatch documents.

Instructions on the use of various applications of software are maintained behind the desk on which the PC is located for ease of access by Margaret as she needs to refer to these on a regular basis.

A monthly profit and loss and balance sheet is prepared as part of the roll-forward procedure. Monthly reconciliations are also prepared by Margaret for all balances on the balance sheet, however the directors concentrate their review on the P&L account.

Required:

Identify major weaknesses in the general CIS control environment and suggest remedies for each weakness.

2. You have just been appointed auditor of A Limited (A). As part of the audit planning process you have visited the premises and noted the following issues:

   - A's CIS function is under the overall control of the Finance Director. However the day to day operations are the responsibility of the CIS Manager who has had significant CIS experience.

   - The key modules of A's Financial Management System (FMS) are currently undergoing significant modification. The Systems Analyst who initially implemented the FMS was recently dismissed as a result of a disagreement with the CIS Manager.

   - A few days after the dismissal, the Systems Analyst returned to A's CIS department and made some unauthorised changes to the FMS.

   - Subsequent to the dismissal of the Systems Analyst, the FMS development work lost direction. The programmers, who received their detailed instructions from the Systems Analyst, had no written instructions or documented system specifications for the FMS modifications. All such instructions and specifications had been given by the Systems Analyst verbally.

   - Only CIS department staff are allowed access to the CIS department. When you visited, however, you were able to enter the department, review existing FMS documentation, and make changes to a FMS program under development via a terminal which was logged on but not attended by a programmer. During this period you were not asked for identification and were left alone for long periods of time.

Required:

(a) **From the information above, identify four (4) key general control weaknesses.**

(b) **For each weakness identified in (a) above, specify your recommendation to overcome these problems**

You may wish to present your answer to parts (a) and (b) in your answer book in the form of a table, as indicated below.

Weakness	**Recommendation**

D CLASS GROUP DISCUSSION QUESTIONS

1. Session 2, 1997 Exam Question 2

In accordance with your firm's partner rotation policy you have been newly appointed as signing partner of Knocked Down Ltd, a building construction firm with a head office in Sydney. Following an extensive cost review during the year Knocked Down now gets 80% of its timber supplies from a Solomon Islands supplier of low cost rainforest timber. The audit manager has informed you that in previous years significant reliance was placed on the work performed by the client's internal audit staff. The client was required to make significant adjustments last year because your firm detected several errors concerning valuation of inventory. Your initial planning meeting with the client's financial controller has revealed the following information about the purchases and inventory system:

- When goods are received, the goods are counted and inspected and a pre-numbered Goods Received Note (GRN) is prepared. After counting and inspection, the goods are moved directly to a locked storage area. The storeman only releases the goods upon receipt of a materials requisition form signed by an authorised employee.

- The Goods Received Note is sent to the Purchasing Department where it is matched with a supplier's order and then batched and sent to the Computer Information Systems (CIS) Department for input and processing.

- The company has recently purchased a very advanced computer system and purchased software specially for the construction industry which has been developed by Bits'n'Bytes Pty Ltd, a small organisation headed by the General Manager's nephew.

- The CIS Department consists of manager, programmer and two data processing operators. The programmer is not involved in data entry and any programming changes are reviewed and approved by the Manager. A password system restricts the access of the data processing operators to only the applications software that they are using. The CIS department input the batch of transactions and update the Inventory Master File. The Inventory Master File contains inventory number, description, approved suppliers, quantity on hand, invoice price, total cost, sales price, sales year to date and last sale date.

- The updated inventory master file is reconciled to the old master file and the transaction data by the CIS Manager and is sent back to the user department for review. The system automatically produces a number of exception reports which are reviewed by the user department.

- The inventory balance has remained constant over the last year while the accounts payable balance has increased by 40% as the client is suffering from a severe cash shortage brought on by the recession. Many suppliers' accounts have remained unpaid for several months and the client is under pressure from several to pay.

- At the beginning of the year, the client decided to retrench its internal audit department as part of its cost cutting programme.

Required:

(a) From the information provided above, outline factors that would affect your assessment of inherent risk for Knocked Down. Assess this level of risk as Low/Medium/High.

(b) From the information provided above:

(i) Outline factors that influence your evaluation of general controls for Knocked Down.

(ii) Identify application controls that exist in the inventory/accounts payable system.

(iii) Assess the level of control risk for the inventory/accounts payable system. Assess this level of risk as Low/Medium/High.

(c) Determine the most appropriate audit strategy for the inventory/accounts payable system. Categorize the extent of work to be undertaken under each type of testing (i.e., test of controls/substantive tests of details/substantive analytical procedures) as either none, small, medium or extensive. Justify your answer.

(d) Describe three (3) specific tests of control that would be undertaken for application controls identified in (b) (ii) above.

(e) Identify three (3) exception reports that could be generated by audit software that would assist you in the verification of the valuation assertion for inventory.

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Auditing in a CIS Environment – Substantive Testing

WORKSHOP 7: Week beginning 22 September 2003

READING GUIDE

Textbook Reference:
Gay and Simnett, Chapter 10 (page 477-481)

Standards:

AUS 214: Auditing in a CIS Environment.

AGS 1018 CIS Environments - Stand-alone Microcomputers.

AGS 1020: CIS Environments - On-line Computer Systems.

AGS 1022: CIS Environments - Database Systems.

A REVISION QUESTIONS

MaxMark Topic 8.

B PREPARATION QUESTIONS

1. Roebuck & Martinov Exam No. 1 Question 2 Page 164-5 and Solution Page 170.

2. Roebuck & Martinov Case 4.5 Page 63 – 4 and Solution page 220-2.

C HOMEWORK QUESTIONS

1. Toan & Associates are a firm of solicitors specialising in commercial law. An audit is required under the solicitors' trust regulations. Recent changes in government regulation have deregulated the fees of commercial lawyers, with the result that legal fees have decreased by 20% over the past year. The firm has 4 partners, 90 associates and 6 support staff. All financial records are contained on a personal computer. A general ledger software package that is widely used by legal firms is used by the organisation. The general ledger package also contains an accounts receivable subsidiary ledger, a work-in-progress file (which shows current status of legal cases) and a payroll subsidiary ledger.

   All financial records, including all payroll documentation, are maintained by the ledger clerk. The payroll details entered consist of changes to standing data, and transactions. The changes to standing data are additions and deletions of staff to the payroll master file, change of address, variation of approved fortnightly pay, and change to approved overtime rate. Any such changes are contained on a variation of payroll information form which is approved by the personnel partner and one other partner. After being entered into the system, the variation of payroll information form is filed in numerical sequence.

The transaction data is entered each fortnight when the partners and staff complete a pay sheet which assigns their times to jobs. This is entered into the computer package by the ledger clerk and is used to update the work-in-progress file and the payroll file. If any staff work overtime, which must be approved by the partner in charge of the case (evidenced by the partner initialing the pay sheet), this is entered and the overtime is paid at the approved set rate.

The following reports are produced each fortnight and are reviewed and authorised by all partners, at fortnightly partners' meetings:

- Printout of year-to-date payroll master file.
- Payroll transactions file for the last fortnight.
- List of staff who have undertaken overtime in the last fortnight.
- Current status of all cases in progress.
- Cases in progress where additional work has been undertaken over the last fortnight.
- Cases completed and billed over the last fortnight.
- List of accounts receivable master file.

Required:

(a) Evaluate the control risk as low, medium or high in the above payroll system. Justify your evaluation.

(b) Assume that inherent risk and control risk in relation to the payroll expense account have been both evaluated as high for occurrence and measurement assertions. Determine the most appropriate audit strategy for the payroll expense account. Categorise the extent of work to be undertaken under each type of testing (ie tests of control/substantive tests of detail/substantive analytical procedures) as either none, small, medium or extensive. Justify your answer.

(c) The client's software package contains a programmed range check on the payroll file. No associate's fortnightly pay (before overtime) should be outside the range of $2,200-$4,000. Identify and illustrate by example with respect to this control the technique(s) by which the auditor could obtain <u>direct</u> evidence that this programmed control is working.

(d) Some of the reports generated by the client each fortnight are exception reports. Identify which of the reports generated are exception reports. Explain and distinguish between the relevance of the reports to:

 (i) the partners of the law firm
 (ii) the auditors.

(e) The auditors also use the same exception reports for their audit. Instead of relying on the client-generated exception reports the auditors decide to generate their own. Which computer-assisted audit techniques will aid the auditors in generating these reports. Why would the auditors decide to generate their own reports rather than rely on the client-generated reports?

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 2, 2002 Exam Question 3 (10 Marks)**

Your client Global Limited holds a large portfolio of investments in shares of other entities, approximately 80% of them being listed on the stock exchange. Approximately 800 parcels of shares are held.

The following data on each share parcel is maintained on the computer system:

Date purchased
Date sold
Investee name
Total number of shares held (by class)
Number of shares sold (by class)
Class of shares held
Investment cost
Year-end market value
Profit/loss on sale
Dividend income

The above data is maintained on the computer for a period of two years.

Required:

2 a) Apart from report writing, detail two (2) examples of how generalised audit software (GAS) could assist in the audit of these investments.

2 b) Identify the key assertions the auditor will wish to gather evidence on for these investments.

6 c) Describe three (3) reports at least one (1) of which is an exception report, you would have the GAS produce. Your answer should indicate the report name, the details included in the report and how the report will be used by the auditor, including which management assertions (e.g. existence) are targeted by the report.

NOTE: Provide your answer in the following format:

Report Name and Content	Audit use of Report

2. **Session 1, 2003 Exam Question 3 (16 Marks)**

Question 3 (16 marks)

In reviewing the processes, procedures and internal controls of one of your audit clients, Superbikes Ltd, you notice the following practices in place. They have recently installed a new computer system that affects the accounts receivable, billing, and shipping records. Three computer operators have been employed, and each has been assigned to oversee one of the functions of accounts receivable, billing and shipping.

Each of these computer operators is assigned the responsibility of running the program for transaction processing, making program changes, and reconciling the computer log. In order to prevent any one operator from having exclusive access to the computer disks and documentation, these three computer operators randomly rotate the custody over the computer disks and the system documentation and the control tasks every two weeks. Access controls to the computer room consists of magnetic cards and a digital code for each operator. Access to the computer room is not allowed to either the systems analyst nor the computer operations supervisor.

The documentation for the computer system consists of the following: record layouts, program listings, logs and error listings.

Once goods are shipped from one of its three warehouses, warehouse personnel forward shipping notices to the accounting department. The billing clerk receives the shipping notice and accounts for the manual sequence of the shipping notices. Any missing notices are investigated. The billing clerk also manually enters the price of the item, prepares daily totals (supported by adding machine tapes) of the units shipped and the amount of sales. The shipping notices and adding machine tapes are sent to the computer department for data entry.

The computer output generated consists of a two copy invoice and remittance advice and a daily sales register. The invoices and remittance advices are forwarded to the billing clerk who mails one copy of the invoice and remittance advice to the customer and files the other copy in an open invoice file which serves as an accounts receivable document. The daily sales register contains the total of units shipped and sales amounts. The computer operator compares the computer generated totals to the adding machine tapes.

Required:

10 **a) Identify five (5) internal control weaknesses present in the system described above and make a specific recommendation for correcting each of the control weaknesses.**

Present your answer in the following format:

Control Weakness	Recommendation

2 **b) Explain how the presence of a CIS environment impacts the auditors' assessment of control risk.**

3 **c) Provide three (3) examples (other than use of exception reporting) of how Generalised Audit Software could be employed to assist in the audit of accounts receivable, and identify a major assertion addressed by the procedure.**

1 **d) Provide one (1) example of how exception reporting could be utilised in the audit of accounts receivable, and identify a major assertion addressed by the procedure.**

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Using the Work of Others/Internal Audit/Public Sector Auditing

WORKSHOP 8: Week beginning 6 October 2003

Note : Monday, 6th October is a public holiday. You will be advised to attend an alternate class if your workshop falls on this day.

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 8 (pages 361-364)
Gay and Simnett, Chapter 15
Gay and Simnett, Chapter 16

Standards:

AUS 102:	Introductory Statement of Applicability of Auditing Standards and Statements of Auditing Practice to Auditing in the Public Sector. Paragraph 43-44.
AUS 602:	Using the Work of Another Auditor.
AUS 604:	Considering the Work of Internal Auditing.
AUS 606:	Using the Work of an Expert.
ED 30:	Audit Exposure Draft, Compliance Auditing.
AUS 806:	Performance Auditing.
AUS 808:	Planning Performance Audits.
AUS 904:	Engagements to Perform Agreed-upon Procedures

A REVISION QUESTIONS

MaxMark Topic 10.

B PREPARATION QUESTIONS

1. Roebuck & Martinov Case 4.1 Part 3 Pages 58-59. Solution page 218.

2. Roebuck & Martinov Case 4.9 pages 68-9. Solution pages 223-4.

3. Roebuck & Martinov Mock Exam No. 1 Question 4 Part A page 166. Solution page 171.

C HOMEWORK QUESTIONS

1. Roebuck & Martinov, Case 9.2 Part A, Page 184

2. Your accounting firm has recently acquired a new audit client, which operates a major industrial plant. Coal is the main raw material used to generate power for the plant.

   (a) Consider whether the use of an independent expert will be necessary to determine the quantity of coal held in stockpiles at the plant.

   (b) Assuming such is required, outline the broad procedures that are necessary for you to be able to rely on the expert's work.

3. Roebuck & Martinov Case 4.12 Pages 71-2.

4. Explain how the objectives of public sector accounting differ from that of the private sector. What implications do these differences have for auditing the public sector in terms of the application of the risk methodology and the AUSs.

5. You are asked to conduct an operational/performance audit of the purchasing department for a government department.

   (a) List five (5) indicators of performance that you would include in planning the audit.

   What particular problems are associated with measuring performance?

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 1, 2003 Exam Question 4 Part A (3 Marks)**

   Distinguish between economy, efficiency and effectiveness, and explain whether they are related to the various audits under the comprehensive audit approach employed in the public sector.

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Workshop 9: Week beginning 13 October 2003

Assignment Presentations

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Legal Liability / Ethics

WORKSHOP 10: Week beginning 20 October 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 3 and Chapter 4

Other References

Standards:

AUS 204 Terms of Audit Engagements.

Joint code of Professional Conduct, Sections A,B,D,F1,F3,F5,F6 and F7.

AUS 206: Quality Control for Audit Work.

APS 4: Statement of Quality Control Standard.

APS 5: Quality Control Policies and Procedures General Guidelines.

A REVISION QUESTIONS

MaxMark Topics 8, 15 and 16.

B PREPARATION QUESTIONS

1. Roebuck & Martinov Mock Exam No. 1 Question 4 part B page 166 and solution page 171.
2. Roebuck & Martinov Case 6.1 page 88 and Solution page 227-8.
3. Roebuck & Martinov Case 6.3 Part 2 & 3 page 90 and Solution pages 229-31.

C HOMEWORK QUESTIONS

1. Roebuck & Martinov Case 6.3 Page 90.
2. Roebuck & Martinov Case 6.6 Page 93.
3. Roebuck & Martinov Mock Exam No. 3 Question 3 Page 181.
4. Roebuck & Martinov Case 6.9 Page 96-7.

5. Many of the 'Big 4' audit firms are undertaking internal audit engagements. For some clients they may also conduct the financial statement audit. Discuss whether or not engaging in such activities impinges on the audit firms' independence both 'in-fact and appearance'. (Your discussion should focus on the latest auditing standards, legislation, and community attitudes).

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 2, 2002 Exam Question 4 Part B (7 marks)**

b) Audit independence has been described as the cornerstone of the auditing profession.

2 i) Define actual and perceived independence
5 ii) Explain the importance of each of these components. Support your answer using references to recent events in the business world.

2. **Session 1, 2003 Exam Question 4 Part B (5 marks)**

Discuss the implications of CLERP 9 for the perceived and actual independence of auditors.

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Completing the Audit Process and Audit Reporting

WORKSHOP 11: Week beginning 27 October 2003

READING GUIDE

Textbook Reference:

Gay and Simnett, Chapter 12
Gay and Simnett, Chapter 13
Gay and Simnett, Chapter 14

Standards:

AUS 212: Other Information in Documents Containing Audited Financial Reports.

AUS 702: Audit Report on a General Purpose Financial Report.

AUS 706: Subsequent Events.

AUS 708: Going Concern.

AUS 802: The Audit Report on Financial Information Other than a General Purpose Financial Report.

AGS 1006: Expressions of Opinion on Internal Control.

AGS 1016: Audit and Review Reports - Half Year Accounts and Consolidated Accounts.

ED 66: Reporting on the Credibility of Information.

A REVISION QUESTIONS

MaxMark Topics 3 and 4

B PREPARATION QUESTIONS

1. Roebuck & Martinov Case 5.8 Pages 85-86 and solution page 226-7.

2. Roebuck & martinov Case 9.6 Page 189 and Solution page 243.

C HOMEWORK QUESTIONS

1. Turbo audited Charge Ltd. For the year ended 30 June 19X8. Turbo is aware that certain events and transactions that took place after 30 June 19X8, but before he issues his report dated 31 August 19X8, may affect the company's financial statements.

The following material events or transactions have come to his attention:

(a) On 15 July 19X8, the company settled and paid a personal injury claim to a former employee as the result of an accident that occurred in September 19X7. The company had not previously recorded a liability for the claim.

(b) On 25 July 19X8, the company agreed to purchase for cash the outstanding shares of Electronic Fuel Injection Ltd. The acquisition is likely to double the sales volume of Charge Ltd.

(c) On 1 August 19X8, a plant owned by Charge Ltd was damaged by a flood resulting in an uninsured loss of inventory.

(d) On 5 August 19X8, Charge Ltd. issued and sold to the general public $2 million in convertible notes.

Required:

(i) For each of the events or transactions described above, indicate the audit procedures that should have brought the item to the attention of the auditor.

(ii) Determine the action(s), if any, that the auditor needs to take in relation to each of the above events.

2. Explain how this situation should be dealt with in the financial statements. Justify your decision:

   You are the auditor of Codd Ltd. You are about to sign the audit report on the financial statements for the year ended 30 June, 1997 when you become aware that the client has received an amended assessment from the Tax Office. the amendment for $285,000 is a result of tax audit conducted in March 1997. The amount is material and the company has indicated that it will not appeal against the amendment.

3. Outline and justify the audit opinion that the auditor should issue in each of the following independent situations.

   With the exception of the issues outlined, assume that the auditor is satisfied in all other material respects.

   (i) Your client has intangible assets, being trademarks, which are recorded in the accounts at $4,500,000. the value is the same as in the prior year. During the year, your client commissioned in independent valuation of the trademarks. This valued them at $2,850,000. Management refuses to adjust the financial statements to reflect the revised valuation.

   The materiality for the client has been set at $1,200,000.

   (ii) The client's solicitor's representation letter reveals that there is a possibility of a large legal settlement being made against the client. The client refuses to disclose this fact in the accounts or the notes to the accounts as the cause of the legal action occurred after year end.

   (iii) A company loses most if its accounting records due to a fire in its accounts department. Although it is able to reconstruct its financial statements due to an asset stocktake, third party confirmation procedures and inquiries from creditors, there is no documentation to support transactions for the year.

(iv) A cut-off error is identified by the auditor which results in an understatement of sales, debtors and profit. The client decides not to adjust the accounts on the basis of this error and the auditor determines that the error is not material to the financial statements.

(v) A consignment of inventory is incorrectly excluded from inventory and creditors. The client decides not to adjust the accounts on the basis of this error and the auditor determines that the error is material to the financial statements.

D CLASS GROUP DISCUSSION QUESTIONS

1. **Session 2, 2001 Exam Question 4 Part C (8 Marks)**

2 (i) Explain briefly what is meant by the 'going concern' concept and its significance to the audit.

3 (ii) Based on the information provided what would be the value of buildings (a) under the going concern basis, and (b) if the company was not a going concern.

	$000
Buildings at cost	6,000
Accumulated depreciation	500
Current sales value (excl. land)	3,000
Cost of disposal	25

3 (iii) Detail three (3) factors that would assist you in determining the 'going concern' basis for a home unit property developer. (Justify the relevance of each of the factors chosen)

NOTE: You may wish to present your answer in the following format:

Factor	Relevance to going concern

2. Roebuck & Martinov Case 5.4 Parts (I), (ii), (iii), (vi), Pages 79-81.

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

Course Review and Current Issues

WORKSHOP 12: Week beginning 3 November 2003

READING GUIDE

No prescribed readings.

A REVISION QUESTIONS

None set. Note all topics are covered in the final exam.

B PREPARATION QUESTIONS

None set. Note all topics are covered in the final exam.

C HOMEWORK QUESTIONS

None set.

D CLASS GROUP DISCUSSION QUESTIONS

None set.

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ACCT 3708 AUDITING AND ASSURANCE SERVICES

ASSIGNMENT

SESSION 2, 2003
ASSIGNMENT: (20%)
Due: Workshop 9, Week Beginning 13 October 2003

Source: **This case has been adapted from the Professional Year Program of the Institute of Chartered Accountants in Australia**

After successfully completing the assignment you will be able to:

- perform analytical procedures and utilise their results;
- identify risks in relation to specific account(s) and the relevant assertion(s);
- outline the impact of the risks identified on audit procedure;
- determine and justify planning materiality $amount; and
- design substantive test procedures in relation to the relevant financial report assertions for a given account balance.

Your firm has just been appointed auditor of GC Limited (GC) and as the audit senior you have been asked to commence the detailed planning of the audit for the year ended 30 June 2003. Following preliminary discussions with the client's financial controller, you have collected the following information:

GC Limited
Draft Profit and Loss Account for 30 June 2003

	Unaudited year ended 30.6.2003 $'000	Audited year ended 30.6.2002 $'000
Operating revenue	20,452	22,402
Operating profit/(loss) before abnormal items and income tax	1,426	899
Abnormal items before income tax	-	(2,436)
Operating profit/(loss) before income tax	1,426	(1,537)
Income tax expense/(benefit) attributable to operating profit/(loss)	517	(303)
Operating profit/(loss) after income tax	909	(1,234)
Retained profits at the beginning of the financial year	459	1,903
Adjustment resulting from adoption of new accounting standard	-	(27)
Total available for appropriation	1,368	642
Dividends provided for or paid	569	183
Retained profits at the end of the financial year	799	459

GC Limited
Draft Balance Sheet as at 30 June 2003

	Note	Unaudited year ended 30.6.2003 $'000	Audited year ended 30.6.2002 $'000
Current assets			
Cash		442	296
Receivables	1	1,427	1,506
Inventories	2	6,667	5,465
Other	3	288	69
Total current assets		8,824	7,336
Non-current assets			
Investments	4	551	553
Inventories	5	3,292	5,336
Property, pant and equipment	6	1,193	1,163
Intangibles	7	890	890
Other	8	540	558
Total non-current assets		6,466	8,500
Total assets		15,290	15,836
Current liabilities			
Creditors and borrowings	9	4,899	5,838
Provisions	10	705	266
Total current liabilities		5,604	6,104
Non current liabilities			
Creditors and borrowings	11	1,830	2,359
Provisions	12	512	435
Total non-current liabilities		2,342	2,794
Total liabilities		7,946	8,898
Net assets		7,344	6,938
Shareholders' equity			
Share capital		191	189
Share premium reserve		6,354	6,290
Retained profits		799	459
Total shareholders' equity		7,344	6,938

Notes to the Financial Report

1. Current receivables

Trade debtors		1,196	704
Provision for doubtful debts		(3)	(3)
		1,193	701
Loans to director related entities		-	16
Other debtors		195	768
Deposits		39	21
Total current receivables		1,427	1,506

	Unaudited year ended 30.6.2003 $'000	Audited year ended 30.6.2002 $'000
2. Inventories		
Land held for resale at cost		
Cost of acquisition	2,495	3,839
Development expenses capitalised	3,390	2,851
Interest capitalised	58	125
	5,943	6,815
Provision for diminution	-	(1,468)
	5,943	5,347
Work in progress, at cost	724	118
Total inventories	6,667	5,465

The interest capitalised in the current inventory relates to land developments previously classified as non-current. Interest is no longer being capitalised on these amounts.

3. Other current assets		
Prepayments	288	69
4. Investments		
Investment properties – at cost	543	545
Other investments	8	8
Total investments	551	553
5. Inventories		
Land on hand		
Cost of acquisition	2,243	4,421
Development expenses capitalised	993	915
Interest capitalised	56	-
Total inventories	3,292	5,336
6. Property, plant and equipment		
Land and buildings – at cost	779	805
Provision for depreciation	(48)	(37)
	751	768
Plant and equipment – at cost	555	472
Provision for depreciation	(304)	(199)
	251	273
Leased plant and equipment – at cost	230	230
Provision for amortisation	(39)	(108)
	191	122
Total plant and equipment	442	395
Total property, plant & equipment at cost	1,584	1,507
Provision for depreciation and amortisation	(391)	(344)
Total property, plant and equipment	1,193	1,163
7. Intangibles		
Brand name, at directors' valuation	890	890

	Unaudited year ended 30.6.2003 $'000	Audited year ended 30.6.2002 $'000
8. Other non-current assets		
Future income tax benefit	529	545
Expenditure carried forward	11	13
Total other non-current assets	540	558
9. Current creditors and borrowings		
Bank overdraft – secured	10	387
Bank loans – secured	2,384	1,373
Other loans – secured	-	3,131
Lease liability – secured	43	39
Trade creditors	2,039	569
Other creditor	423	335
Director related entities	-	4
Total current creditors and borrowings	4,899	5,838
10. Current provisions		
Taxation	142	2
Dividends	382	-
Employee entitlements	78	63
Provision for rental guarantee	103	201
	705	266
11. Non-current creditors and borrowings		
Bank loan – secured	1,682	1,259
Lease liability – secured	148	51
Loan from holding company	-	1,049
Total non-current creditors and borrowings	1,830	2,359
12. Non-current provisions		
Deferred income tax liability	397	246
Employee entitlements	13	16
Provision for rental guarantee	102	173
	512	435
GC Limited Management Accounts		
Sales	20,342	20,767
Less: Cost of sales		
Opening stock	10,801	10,518
Purchases	14,062	16,760
Closing stock	(9,959)	(10,801)
	14,904	16,477
Gross profit	5,438	4,290
Less: Expenses		
Operating expenses	2,636	3,375
Selling and administration expenses	813	936
Other income	110	1,635
Operating profit before interest, abnormal items and income tax	2,099	1,614
Interest expense	(673)	(715)
Operating profit before abnormal items and income tax	1,426	899

Other Information:

- GC is a listed company involved in property development and residential construction in the Sydney region. It has experienced operating losses for the last four years. However, due to a strategy of high profile marketing, and the introduction of new marketing initiatives the company has improved its performance and is expected to make a profit in the current year.

- The shares issued during the year were pursuant to the Dividend Reinvestment Plan.

- Although GC is a listed company, the directors hold a significant percentage of the issued capital (45% at 30 June 2003).

- GC's share price has been subject to broad fluctuations during the past year, trading at a high of $2.95 and a low of $0.85 (the shares have a 50c par value). At 30 June 2003 they were trading at $2.95.

- GC's bank loan is subject to a debt covenant that total inventory must not exceed 70% of total assets excluding intangibles.

- The 2002 abnormal losses relate to the write down of current and non-current assets to recoverable amount and costs incurred in a business rationalisation program.

- The 2002 audit report contained an emphasis of matter related to significant uncertainly to GC continuing as a going concern.

REQUIRED:

(a) Outline any professional standards that need to be considered by your firm given that this is your first audit of GC.

(b) Perform preliminary analytical procedures for GC. These should include simple comparisons and ratio analysis where considered appropriate.

(c) Based on the analytical procedures performed and within the context of the additional information available:

  i) identify and discuss key risks in relation to the audit of GC.

  ii) for each of the risks discussed in i) identify the specific account balance and the key assertion(s) (as per AUS 502) affected.

  iii) Outline the impact of the risk identified on the nature and timing of audit procedures at the account and relevant assertion level.

(d) Provide a brief summary of the additional information you need in relation to this client for planning purposes.

(e) Determine planning materiality for the audit of the financial report for the period ended 30 June 2003. Justify the use of the base and % chosen.

(f) You have determined that the audit strategy for the trade creditors account will be substantive in nature. Prepare substantive audit program for this account. Procedures should be developed to address each of the relevant key financial report assertions.

The University of New South Wales

School of Accounting

ACCT 3708 – Auditing and Assurance Services
Session 2, 2003

GROUP ASSIGNMENT PEER EVALUATION FORM

The purpose of this form **is to allow you to assess the amount of effort each member of your group has put into the completion of the assignment**

You should take care to complete this form honestly.

Individual responses will be kept confidential.

In the spaces provided, list all members of your group (including yourself) and allocate a mark out of 10 to each group member to indicate their effort in completing the assignment

Each group member's mark will be determined using the following formula:

> Assume the assignment was awarded a mark of 6/10 and you were awarded a peer evaluation average of 8/10. This would result in you receiving a final mark of 4.8 out of 10, calculated as 80 percent of 6. If you were awarded a peer evaluation average of 10/10 you would receive the full 6 marks out of 10.

Please note that the marks are NOT allocated proportionally across the group members. In other words if all the group members receive a peer evaluation average of 10/10 then using the above example everyone will receive 6 out of 10.

Workshop Details:

Workshop Day and Time:……………………………………………………………

Tutor:…………………………………………

Group Details: Group Name (Optional): …………..……………..

Your Name and Student Number:………………………………………

Group Members:

Student Names:	Student Numbers:	Mark out of 10:
1.………………………………………………………	….…………	……………
2. ………………………………………………………	……………..	…………..
3. ………………………………………………………	……………..	……………
4. ………………………………………………………	…………….	…………..

PLEASE HAND THIS FORM TO YOUR TUTOR DURING YOUR WORKSHOP IN WEEK 11

THE UNIVERSITY OF NEW SOUTH WALES

SCHOOL OF ACCOUNTING

ACCT 3708 AUDITING AND ASSURANCE SERVICES

PAST FINAL EXAM – MULTIPLE CHOICE ANSWERS

PAST FINAL EXAM - MULTIPLE CHOICE ANSWERS							
YEAR	**2000**	**2000**	**2001**	**2001**	**2002**	**2002**	**2003**
SESSION	**1**	**2**	**1**	**2**	**1**	**2**	**1**
Question							
1	c	c	b	b	a	b	c
2	a	c	b	a	b	b	d
3	d	d	c	c	a	a	b
4	c	d	c	d	b	c	c
5	a or b	b	b	a	d	b	d
6	b	a	b	b	d	a	c
7	c	b	d	b	b	d	b
8	c	b	a	b	c	a	d
9	c	d	a	c	a	b	c
10	d	a	b	d	b	d	b
11				c	b	b	a
12				b	b	a	a
13				c	b	a	c
14				a	a	a	b
15				d	c	d	a
16							d