

THE ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

FINAL EXAMINATION – JANUARY 2015

(61) AUDITING

18-01-2015
Afternoon
[2.00 - 5.00]

Time: 03 hours

• **Instructions to candidates:**

No. of Pages : 03
No. of Questions : 06

- (1) **All questions should be answered.**
- (2) **Answers should be in one language, in the medium applied for, in the booklets provided.**
- (3) **Use of calculators is permitted.**
- (4) **Submit all workings and calculations. State clearly assumptions made by you, if any.**
- (5) **100 Marks.**

- 01.** (a) Briefly explain the difference between "Statutory Audit" and "Internal Audit".
(02 marks)
- (b) List two(02) factors that determine the scope of an audit.
(04 marks)
- (c) Confidentiality is a fundamental principle in the Code of Professional Conduct and Ethics applicable for the members of AAT Sri Lanka. Explain this principle.
(03 marks)
- (d) State four(04) important matters to be included in a letter of engagement of an audit of a limited liability company.
(04 marks)
- (e) Briefly explain the responsibilities of the auditor for detecting material misstatements due to fraud.
(03 marks)
(Total 16 marks)
- 02.** (a) (i) List three(03) reasons justifying the importance of implementing quality control procedures over audit work.
(03 marks)
- (ii) State four(04) objectives of the quality control policies to be adopted by an audit firm.
(04 marks)
- (b) List three(03) limitations of internal control.
(03 marks)
- (c) **Crunch (Pvt) Ltd.** manufactures biscuits for the local market. Their customers are primarily retail shops located island wide. The sales staff who visit retail shops can raise manual invoices based on the approved price list. The sales staff can grant discounts up to 30% when raising such manual invoices. The sales staff collect cash from the retail outlets for the sales made, and a manual receipt is handed over to the customers. The manual invoices, the copies of manual receipts, and the cash collected are handed over to the accounts department of head office on a monthly basis to be entered into the general ledger.
- List three(03) weaknesses in the internal control system explained above and describe how you would overcome each of those weaknesses.
(06 marks)
(Total 16 marks)

- 03.** (a) (i) Explain the difference between a permanent audit file and a current audit file. (03 marks)
- (ii) List four(04) documents that would generally be kept in a permanent audit file. (04 marks)
- (b) **White Sand Hotel Ltd.** has revalued its hotel land and building using a professional valuer. The revaluation value was significantly higher than the previous carrying value (book value).
- List two(02) matters that the auditor should consider in assessing the appropriateness of the professional valuer's valuation as audit evidence. (04 marks)
- (c) Assume that you are the senior auditor in charge of the audit of **Furniture (Pvt) Ltd.** for the year ended 31st March 2014. The company is engaged in the business of import and sale of furniture. The company has 3 sales outlets and a central warehouse.
- State three(03) main areas that need to be given special attention in the preparation of the audit plan of **Furniture (Pvt) Ltd.** (06 marks)
- (Total 17 marks)

- 04.** (a) List three(03) examples of input controls that can be established as application controls in a Computerized Information System (CIS) environment. (03 marks)
- (b) Assume that you are working as an audit senior of **Suhada (Pvt) Ltd.** The company has purchased a used machinery for its operations during the year. There are no supporting invoices from the supplier (seller) of this machinery to check the cost of this machinery recorded in the financial statements of **Suhada (Pvt) Ltd.** The management written representation has given as a substitute for the unavailable supporting invoices for the cost of the machine.
- Can you agree with this? Justify your answer. (03 marks)
- (c) In auditing the inventory valuation of **ABC Ltd.,** you have found that the unit cost of 6 inventory items from your sample of 25 was incorrect. You then selected 5 more items to the sample and found that the unit cost of 2 of the 5 items was incorrect. There are 900 items in the inventory valuation and management has accepted the error. How should you respond to this error? (03 marks)
- (d) **Lucky (Pvt) Ltd.** is a company that imports and sells fertilizer. **R.T. Samarasinghe** owns 80% of **Lucky (Pvt) Ltd.** You have been assigned to audit the debtors of **Lucky (Pvt) Ltd.** as part of the audit of its financial statements for the year ended 31st March 2014. The debtors' age analysis of **Lucky (Pvt) Ltd.** as at 31st March 2014 is given below:

Debtor	0 - 30 Days (Rs.)	31 - 60 Days (Rs.)	61 - 90 Days (Rs.)	91 - 365 Days (Rs.)	More than 365 Days (Rs.)	Total (Rs.)
Sagara Distributors	50,000	30,000	10,000	-	-	90,000
RVS (Pvt) Ltd.	-	75,000	-	-	-	75,000
Suspense account	-	-	45,000	-	-	45,000
Ruhunu Traders	-	-	-	-	90,000	90,000
R.T. Samarasinghe	100,000	50,000	-	-	-	150,000
Sahana Traders	-	(20,000)	-	-	-	(20,000)

You are required to, identify three(03) audit issues apparent from the above data giving reasons why special attention should be given for those areas in the audit.

(06 marks)

(Total 15 marks)

- 05.** (a) List three(03) substantive audit procedures that could be performed for each of the following when auditing inventories:
- (i) Before the stock taking.
 - (ii) After the stock taking. (06 marks)
- (b) (i) State two(02) purposes of analytical procedures. (04 marks)
- (ii) State an analytical procedure that could be used when auditing the interest expense on a loan. (02 marks)
- (c) State a substantive audit procedure that should be performed in obtaining audit evidence for each of the following items:
- (i) Existence of computers.
 - (ii) Accuracy of credit sales.
 - (iii) Valuation of Investment in shares. (06 marks)
- (Total 18 marks)
- 06.** (a) In terms of the basic elements of an auditor's report:
- (i) To whom should the auditor's report be addressed? (02 marks)
 - (ii) State two(02) important matters that should be stated in the scope paragraph. (04 marks)
- (b) You are a member of the team auditing the financial statements of **Matara Traders (Pvt) Ltd.** for the year ended 31st March 2014. You have noted that the company had not been able to pay 6 installments during the year of a significant bank loan taken to finance its working capital requirements.
- You have doubts about the ability of **Matara Traders (Pvt) Ltd.** to continue as a going concern. State two(02) audit procedures that you could perform in this connection. (04 marks)
- (c) State two(02) audit procedures you could perform to obtain sufficient audit evidence that subsequent events up to date of the auditor's report that may require adjustment to the financial statements are identified. (04 marks)
- (d) List two(02) rights of the auditor as per the Companies Act No. 07 of 2007. (04 marks)
- (Total 18 marks)