Module Title: Audit and Investigations  
Level: Six  
Time Allowed: Three hours plus 15 minutes of reading time. Students must not commence answering the questions until the reading time has ended.

Instructions to students:

- Enter your student number **not** your name on all answer books.
- Answer any **four** questions.
- All questions are equally weighted.
- Begin each question in a separate answer book; label each answer book clearly with the number of the question you are answering.
- The use of a non-programmable calculator is permitted.
- Please note: the 15 minutes reading time has been allotted for students to read the exam paper thoroughly and to make notes. However, students may not commence answering the questions until the reading time has finished.

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Answer any four questions.

**Question 1**

ISA 200 ‘Objectives and general principles governing an audit of financial statements’ deals with amongst other matters with the responsibility for the preparation of financial statements and the concept of reasonable assurance.

There are various limitations in assessing reasonable assurance. For example the auditor does not examine all the transactions, but only a sample. There are also many areas within financial statements which involve judgements.

**Required:**

a. In financial reporting clearly describe the responsibilities of the management of the entity and that of its external auditors.

   (8 marks)

b. Describe 3 limitations facing auditors in undertaking their work

   (7 marks)

c. Describe significant types of judgement made by auditors in gathering evidence to arrive at an opinion on the financial statements.

   (10 marks)

   (Total: 25 marks)

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**Question 2 overleaf**
Question 2

CM Ltd has grown rapidly over the years it has been trading and the directors are considering a public listing. They have read a number of articles about corporate governance but they are still a bit confused about audit committees.

Required:

Draft for inclusion in a letter to the board of CM matters which relate to an audit committee:

a. An explanation of the purpose and general responsibilities of an audit committee. (8 marks)

b. A description of the specific responsibilities with regard to internal and external auditors. (12 marks)

c. A suggestion for the composition of the audit committee of CM Ltd. (5 marks)

(Total: 25 marks)

Question 3

The directors of ALM Ltd have approached you and asked you to become their auditors. The year end of ALM is 31 March 2016 and their previous auditors have been dismissed after auditing the accounts for the year ended 31 March 2015.

Required:

a. Describe the practical and ethical matters you would consider before you can accept the appointment and start work on the audit of ALM for the year ended 31 March 2016. (15 marks)

b. List the main content of a letter of engagement you would send to ALM Ltd and explain why the auditor needs to have this letter before the audit can commence. (10 marks)

(Total: 25 marks)
**Question 4**

A proper understanding of internal controls is essential to auditors in order that they understand the business and then they can plan and undertake the audit using both system testing and substantive testing.

FB Ltd is a small hospitality company with 5 hotels and 4 restaurants. The majority of its employees are paid in cash weekly at 3.00pm on Fridays. The wages paid relate to the previous week, which starts on a Monday and ends on a Sunday. This type of business operates a full 7 day week.

**Required:**

a. For the payroll of FB Ltd, describe:
   
   i. The internal control objectives that should apply for this payroll system.
   
   ii. The internal control procedures that management should have put in place to achieve its control objectives.

   (10 marks)

b. Assuming that the year end is on a Sunday, for the payroll cost and disclosures in the financial statements of FB Ltd, list the control tests you would undertake and the substantive tests you would be expected to perform.

   Your substantive tests should also be done on any payroll accruals or prepayments.

   (15 marks)

(Total: 25 marks)
Question 5

Your firm, C & M Statutory Auditors have just completed the audit of Tony Ltd.

Last year’s accounts for the year ended 31 March 2015 were also audited by C & M and an unmodified opinion was given. Tony is not a large company having reported a turnover of £11m and a pre-tax profit of £1.6m.

For the year ended 31 March 2016, there were some very major problems. The unexpected bad weather in December 2015 caused some very serious flood damage, and important records were destroyed, including computer systems and back up information. Very few records remain for the period 1 April 2015 to December 2015.

The directors instructed the financial accountant to still prepare financial statements for the year to 31 March 2016. He used copies of management accounts which he kept at home to estimate accounts values to December, and from then the actual data was entered.

You the auditor have obtained all the information available and you have also examined the limited records available. There is no more audit work that can be undertaken.

You are required to:

a. Consider how you would draft the audit report in this case. This should include the opinion you would be giving. (5 marks)

b. Explain how you have arrived at this opinion. (5 marks)

c. Tony Ltd are arranging a loan with their local bank. Tony has prepared a 3 year cash flow forecast from 1 April 2016 as required by the bank but as a condition for the loan, the bank requires a report from you the auditors on the cash flow.

Assuming that in this case you consider that the statement of financial position at 31 March 2016 to be reasonable, what test would you undertake on the forecast to assess its reasonableness and what type of opinion would you give in this case. (15 marks)

(Total: 25 marks)
Question 6

MIKE Ltd has just prepared the financial statements for the year ended 31 December 2015. This is the fourth consecutive year of reporting losses, and the retained profit is now in debit.

You the audit manager have just finished the audit and other than the matter above the financial statements are reasonable.

You are now at a meeting with the partner of the audit firm and are considering the appropriate opinion to be given.

Required:

a. Explain what you understand by the term ‘going concern basis’ in relation to the preparation of financial statements.  
   (6 marks)

b. Describe the audit procedures required to gain sufficient and appropriate evidence in order to form an opinion on the going concern status of MIKE Ltd.  
   (9 marks)

c. List 5 factors which would generally cast doubt on a company’s going concern status.  
   (10 marks)

(Total: 25 marks)