

Final Admitting Examination



PAPER 3 ADVANCED AUDITING & ASSURANCE

SUMMER 2016 (Friday 19th August 2016: 10.00 am – 2.30 pm)

INSTRUCTIONS TO CANDIDATES

1. The first 30 minutes of this examination is dedicated to reading time.

During this time, candidates may make notes on this examination paper or on their own paper and refer to their materials.

Candidates are **NOT** permitted to open their answer books until instructed to do so.

2. Two answer books are provided (marked Case Study 1 and Case Study 2). Please answer each Simulation / Case Study in the correct answer book.
3. Answer **BOTH** Simulations.
4. Candidates should indicate clearly whether they are answering the paper in accordance with the law and practice of Northern Ireland or the Republic of Ireland.
5. Candidates should deem each monetary amount shown with the €/£ symbol to be stated in their relevant currency.
6. All workings should be shown.
7. **Simulation 1** begins on Page 2 overleaf.

SIM 1: FINE FURNITURE LIMITED

(Recommended time: 120 minutes)

You are Tom Canning, an audit senior working for Jackson & Co. You have been asked to lead the year-end audit fieldwork of Fine Furniture Limited ("FINE"), an audit client of our firm for the last 3 years. The FINE year end is 31 August 2016 however an interim audit was performed in early July 2016.

The team manager, Philip White, calls a briefing meeting with you in August 2016. He explains: "FINE manufactures fitted and free standing bedroom furniture from its purpose built factory just outside Cork city. The company leases a number of showrooms across Ireland where customers can view the current range. Recent popular product developments include high gloss finish coloured units.

During the interim fieldwork, controls testing was carried out over the revenue and receivables and inventory cycles by Jane Smith, the previous audit senior. As she has recently left Jackson & Co, we need to review and follow up on any findings from the interim work. Before Jane left she gave me her working papers which I now want you to read over to familiarise yourself with the work already done (see **Appendix I & II**).

Following your review, please provide a memo to myself detailing the audit risks arising from any control issues identified. In addition, can you document the substantive audit tests we need to perform during the final fieldwork (including the inventory count) to address these risks.

I would also like you to outline the implications for the company of the control weaknesses identified together with recommendations on how the controls can be improved. I will use this information to draft the management letter on receipt of your memo."

As you are starting this work you receive an email from Philip. Philip writes:

"Whilst arranging the inventory count with me, the company accountant, Ian Watson, noted that he would like a meeting next week to discuss some suspicions over the fraudulent behaviour of a store manager. He wouldn't say anything further by phone, however to be prepared for this meeting please document what Jackson & Co.'s procedures should be, including our reporting obligations to third parties, with regard to instances where fraudulent activity is suspected or carried out by client staff. We look forward to receiving your memo."

END OF SIM 1

SIM 2: O'DONNELL INSURANCE BROKERS LIMITED

(Recommended time: 120 minutes)

You are Declan Ryan, an audit manager in Denver, Devine & Co. The audit of a group of multi agent insurance brokers, O'Donnell Insurance Brokers Limited ("ODI") is in progress. ODI is an all-Ireland firm operating from Dundalk with a number of subsidiaries who separately operate as insurance brokers in Dublin City (DC Limited), Cork City (CKC Limited), Galway City (GAL Limited) and Belfast City (BC Limited). Its main source of income is commission earned on insurance sold.

The audits of CKC Limited, GAL Limited and BC Limited have already been completed with three unmodified audit reports being issued. ODI is hoping to streamline all its group company year ends next year, but for this year's audit, the year ends for CKC Limited, GAL Limited and BC Limited are four months' earlier (January 2016) than that of ODI and DC Limited. ODI and DC Limited's year end is 31 May 2016.

It is August 2016 and the audit of DC Limited is coming to completion stage and you are reviewing the work carried out by the audit senior Lisa Brady (LB), and junior, Robert Feeney (RF), with a view to presenting the file to the audit partner Niamh Begley for completion and sign off. Niamh is eager for this audit to be completed as she wishes for the audit of the parent entity ODI, to commence as soon as possible as a report on the compliance status of ODI has to be completed for the Central Bank very shortly. Niamh wants you to work on the audit of ODI.

Materiality for DC Limited has been set at €/\$ 63,000 with performance materiality set at €/\$ 47,000, based on profit before tax of €/\$ 1,260,000. You have already agreed these materiality levels with Niamh and reviewed a large portion of the file. You are currently reviewing the remaining working papers (see **Appendix I & II**).

You are aware from your discussions with Niamh that DC Limited felt more confident following the recession and decided to build a new state of the art office building just outside Dublin City, having previously rented offices on short term leases. Construction commenced and finished within the financial year and DC Limited moved into the new offices a month before the end of the financial year. DC Limited borrowed during the year for this specific purpose. Legal fees incurred directly related to the new office buildings amounted to €/\$ 300,000.

Niamh comes to speak to you at your desk: "I am currently reviewing the quality of audit work in the practice and would like to receive specific feedback on the working papers in the file, including any additional work the seniors will need to perform following your review and any potential journal entries required.

Please provide this information in a memo to me, along with the potential impact on the audit report (including a draft of any modified audit report paragraphs), if the issues identified are not corrected by the client. I'm also keen that the audit of ODI commences as soon as possible, so please commence planning the audit of the parent company, including setting materiality and identifying any risks to be aware of for the audit. Details of this planning should also be included in your memo."

Financial information for ODI is included (see **Appendix III**). Niamh also tells you: "Most of ODI's receivables are from large, reputable, insurance companies. As such, bad debt provisioning is not considered necessary by ODI. I've noticed that one of ODI's customers, UKL Insurances, has been experiencing some difficulties recently and that despite the improvements in the economy, it may not survive in its current format. The balance due is €/\$ 630,000.

Furthermore, ODI is in the middle of an ongoing lawsuit in relation to mis-selling of income protection insurance to self-employed individuals. ODI's legal team believe it highly likely that the only consequence will be to incur a fine given the nature of the lawsuit, but the amount to be paid is uncertain at present. I look forward to receiving your memo as soon as possible."

As Niamh leaves you start work on the memo.

**END OF SIM 2
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