

## Sample Paper

# PRINCIPLES OF AUDITING

## Level 3

Subject Code: 20060

Time allowed: **75 minutes**

### You need

- This test paper
- An answer sheet
- An HB pencil
- An eraser

**You may NOT use a dictionary**

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**Do NOT open this paper until you are told to do so by the supervisor.**

**There are 20 questions in this paper**

**Total marks available: 30**

**Try to answer ALL the questions**

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### INSTRUCTIONS

- Make sure your personal details are entered correctly on the candidate answer sheet
- This paper is in **two** sections, Part A and Part B. Questions in Part A carry one mark for each correct answer; whilst questions for Part B, carry two marks, for each correct answer.
- Read each question carefully and choose the correct answer – A, B, C or D
- Enter your answers on the candidate answer sheet using an HB pencil
- Make sure you only mark **one** answer for each question and that you completely fill the circle
- If you make a mistake, make sure you erase it completely
- Only complete as many answers as there are questions
- At the end of the test hand the question paper, your answer sheet and all notes to the supervisor

**NB. This sample paper contains only 10 questions.**

**PART A**

(1 mark for each correct answer)

- 1 There are **five** fundamental principles that auditors must follow, as laid down by the International Federation of Accountants' Code of Ethics. Which of the following is **not** one of these five?

**Please select**

- (a) Integrity
- (b) Prudence
- (c) Objectivity
- (d) Confidentiality.

- 2 The auditor discovers that the closing inventory has been incorrectly totalled and the correct figure is higher than the figure originally calculated. An adjustment to correct this error will result in which of the following?

**Please select**

- (a) Gross profit being increased.
- (b) Gross profit being decreased.
- (c) The Trial Balance will now not balance.
- (d) Gross profit will not change.

- 3 An audit is being undertaken. The auditor discovers that the client created a suspense account due to their trial balance not balancing. The suspense account has a debit balance of £80.

The client had then produced final accounts. Which of the following errors, found by the auditor, would account for the original suspense account?

**Please select**

- (a) A prepayment of £80 had been ignored in the statement of financial position.
- (b) Closing inventory had been over added by £80.
- (c) A sale of £80 had been posted to sales account but not to the buyer's account.
- (d) An accrual of £80 had been ignored in the statement of financial position.

4 The auditor could be legally liable under breach of contract to

**Please select**

- (a) the shareholders.
- (b) the Directors.
- (c) the employees.
- (d) the creditors.

5 An item, to be considered material by the auditor, must

- (i) have physical existence
- (ii) reduce the net profit by any amount
- (iii) be part of the closing stock
- (iv) be a debit balance in the ledger

**Please select**

- (a) All of the above
- (b) None of the above
- (c) (i) and (ii)
- (d) (ii), (iii), (iv)

6 To check the accounting system for controlling purchases, among other actions the auditor should

**Please select**

- (a) check that all goods bought have been sold.
- (b) ask customers to confirm the balances owed by them.
- (c) check that all goods bought are still in store.
- (d) ask suppliers to confirm the balances owed to them.

7 Physical examination is most suited for checking

**Please select**

- (a) debtors.
- (b) goodwill.
- (c) plant and machinery.
- (d) capital.

8 If the auditor is using random sampling, then

**Please select**

- (a) every item in the population has an equal chance of being chosen.
- (b) large balances in the population are more likely to be chosen.
- (c) small balances in the population are more likely to be chosen.
- (d) items chosen will be regularly spaced throughout the population.

**PART B**

(2 marks for each correct answer)

9 Two firms have the following capital structures:

	Firm A		Firm B	
	£	£	£	£
Share Capital		400,000		150,000
Debentures		100,000		100,000
Profit and Loss balance b/f	150,000		(35,000)	
Profit this year	50,000		75,000	
	200,000		40,000	
less proposed dividend	40,000	<u>160,000</u>	15,000	<u>25,000</u>
Total		<u>660,000</u>		<u>275,000</u>

Considering the organisation risk factor, which option would be most suitable?

- (i) firm A should pay a dividend but Firm B should not
- (ii) firm B is in an improving profit situation
- (iii) firm A is proposing too high a dividend compared to this year's profit
- (iv) both firms should pay the proposed dividend.

**Please select**

- (a) (ii) is incorrect but the rest are accurate.
- (b) All four points are correct.
- (c) (ii) is accurate but the remainder need further information.
- (d) To assess the risk of any of the points requires further information.

- 10 A firm has an entry in its books for machinery of £550,000. On checking the ledger the auditor finds the following entries for the last year.

Machinery Account	Debit £	Credit £	Balance £
Balance at 1 <sup>st</sup> April (start of year)			380,000
20 <sup>th</sup> May Machine sold		75,000	305,000
20 <sup>th</sup> March Machine bought	245,000		550,000

There were no other entries. In order to be satisfied that the balance is correct the auditor should, among other things, check which of the following?

- (i) That the sale and purchase were correctly authorised
- (ii) That the sale made a profit
- (iii) That the machinery has been paid for
- (iv) That the machine actually exists.

**Please select**

- (a) (i), (iii) and (iv)
- (b) All of them
- (c) (i), (ii) and (iv)
- (d) (i) and (iv)