You are the audit senior of Rhino & Co and you are planning the audit of Kangaroo Construction Co (Kangaroo) for the year ended 31 March 2013.

Kangaroo specialises in building houses and provides a five-year building warranty to its customers. Your audit manager has held a planning meeting with the finance director. He has provided you with the following notes of his meeting and financial statement extracts:

Kangaroo has had a difficult year; house prices have fallen and, as a result, revenue has dropped. In order to address this, management has offered significantly extended credit terms to their customers.

However, demand has fallen such that there are still some completed houses in inventory where the selling price may be below cost. During the year, whilst calculating depreciation, the directors extended the useful lives of plant and machinery from three years to five years. This reduced the annual depreciation charge.

The directors need to meet a target profit before interest and taxation of $0•5 million in order to be paid their annual bonus. In addition, to try and improve profits, Kangaroo changed their main material supplier to a cheaper alternative.

This has resulted in some customers claiming on their building warranties for extensive repairs. To help with operating cash flow, the directors borrowed $1 million from the bank during the year. This is due for repayment at the end of 2013.

Financial statement extracts for year ended 31 March

	draft	**actual**
	2013	**2012**
	$m	**$m**
revenue	12.5	15.0
cost of sales	(7.0)	(8.0)
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gross profit	5.5	7.0
operating expenses	(5.0)	(5.1)
	--------	--------
profit before interest and tax	0.5	1.9
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inventory	1.9	1.4
receivables	3.1	2.0
cash	0.8	1.9
trade payables	1.6	1.2
loan	1.0	---

Required:

Using the information above:

(i) Calculate FIVE ratios, for BOTH years, which would assist the audit senior in planning the audit; and (5 marks)

(ii) Using the information provided and the ratios calculated, identify and describe FIVE audit risks and explain the auditor's response to each risk in planning the audit of Kangaroo Construction Co. (10 marks)