SOLUTION: ASSURANCE AND AUDIT PRACTICE NOV 2007

QUESTION 1

(a) (i) The audit of the sales transaction system will tend to be based on transactions testing. It would be appropriate to use statistical techniques – for example random tables to select items for testing, such as Debit Note Numbers or Sales Invoice Numbers. Statistical techniques will also be required to determine how large the sample size needs to be to give a particular confidence level, and how far a test need be extended if errors are found.

Judgemental sampling may be used in other areas, although here again random numbers may be used – for example, to select the monthly sales to be cast or the month's control account reconciliation to be checked.

(ii) In verifying year-end debtors, it will be necessary to use judgement in reviewing the doubtful debt provision to ensure that it is adequate but not overstated. This will require a review of individual old balances to ensure that all necessary provisions have been made, and that non-provision can be justified by the client. The auditor will need to draw on past experiences of the adequacy of provisions and also to assess whether any new factors may change the level of provision required. It may be helpful to use statistics in comparing the percentage provision made in the current and previous years. Statistics might possibly be used in selecting a random sample of individual balances to be checked to the list of debtors from the sales ledger but on the whole, year-end debtors are an area calling for judgemental review.

(b) The following procedures could be used to verify the fixed assets:

(i) Verify the opening balances by reference to the previous years balance sheet and audit files.

(ii) Vouch the cost with documentary evidence such as invoices to ascertain the new acquisitions.

(iii) Vouch the authority for the acquisition with minutes or with authorized delegated authority.

(iv) Vouch the authority for disposal to minutes or company procedures.

(v) Examine documentation for the disposal.

(vi) Verify reasonableness of the sales proceeds

(vii) Examine scrapings.

(viii) Note accounting treatment of items.

(ix) Vouch the authorization of depreciation policy with minutes.

(x) Examine adequacy and appropriateness of the depreciation policy.

(xi) Check the calculations on the schedule.

(xii) Examine the fixed assets register and reconcile physical quantities to the closing value.

QUESTION 2

(a) Advertising and Publicity

Advertising is the communication to the public of information as to the services or skills provided by an accountant or firm of professional accountants with a view to procuring professional business.

Publicity on the other hand is communication to the public of facts about an accountant or a firm of accountants not designed for the deliberate promotion of the accountant

Currently both advertising and publicity are allowed but must follow the Rules on Advertising and Publicity.

The rules require that material may not:

(i) bring the ICA(G) into disrepute or bring discredit to the advertiser, his firm or the accountancy profession.

(ii) Discredit the services offered by others

(iii) Be misleading

(iv) Fall short of any code on advertising standard

(b) Tendering for audit work

When tendering for audit work the auditor must consider the following factors

(1) Ability of the firm to do the work professionally at a low fee.

(2) Any independence, professional or conflict of interest problems that may arise should the firm tender.

(3) Technical competence and expertise to do the audit.

(4) Timing and geographical reasons against tendering.

(5) Special reasons for wanting the audit. The firm might wish to enter a particular market, for example charities or wish to consolidate hold on particular market.

(6) The reason why the firm has been asked to tender.

(7) The audit risks that might arise with the particular client.

(8) Perceived problems with the current audit or auditor.

(c) Tax Investigations

The form of the investigation will be determined by the nature of the taxpayer's affairs. However the following points should be considered.

(1) Obtain copies of all tax returns submitted by the taxpayer.

(2) Consider whether the taxpayer can be persuaded to make a voluntary disclosure of undisclosed income in order that some mitigation of penalties can be negotiated.

(3) Consider whether the undisclosed income might be readily ascertainable from the taxpayer's books and records.

(a) The tax returns may, simply, not be in agreement with the books and records or the taxpayer may have kept two sets of books and can be persuaded to make a voluntary disclosure.

(b) Audit procedures applicable to small business audit, may be sufficient to reveal undisclosed revenues or personal expenditures improperly charged against business revenues.

(4) The investigation should extend to the taxpayer's spouse and dependants, into investments and assets held in their names.

(5) Obtain copies of all available records such as bank statements, building society statements, brokers or investments adviser's statements and estate agent's statements with respect to property transactions, including sales and rents.

(6) Ascertain details of all investment transactions both capital and revenue such as sales and purchases, dividends, rights issue etc.

(7) Ascertain details of purchases and disposals of other assets such as life insurance, chatters and property.

(8) Ascertain details of non-taxable receipts and payments such as gifts, legacies, gambling winnings etc.

(9) Estimate normal expenditures consistent with the taxpayer's standard of living. Consideration must be given to such matters as type of housing, quality of furnishings, types of holidays taken, ownership of cars, jewellery, other capital assets, private school fees and private medical expenses. The assumption on which the estimate is based must be clearly stated.

(10) Consider what other clues might be available such as value of assets insured, receipts and payments through the bank and building society accounts etc.

(11) Determine the wealth of the taxpayer at the commencement of the period in the form of cash, investments and property and other property and capital assets, add to this the declared income and other sources of income not subject to taxation, and then deduct expenditure consistent with the taxpayers standard of living and other losses and decreases in wealth. The resulting balance should proximate the total wealth of the taxpayer at the conclusion of the period. If actual wealth is greater than the difference is due to sources of income not properly disclosed to the Internal Revenue Service and on which taxes will be assessed.

QUESTION 3

a) (i) Responsibilities for prior period financial information include:

- the opening figures form part of the current year's accounts, for example stock is part of cost of sales. Ensure that all such figures have been subjected to audit opinion obtained through audit evidence.

- ensure that the previous and current year accounts are consistent in accounting policies.

- the previous year's figures form the comparative figures. The auditor must see that they are indeed the figures (possibly restated) appearing in the previous year's accounts.

(ii) Procedures to be adopted to discharge the responsibilities include:

- determining if opening figures are correctly brought forward and are correct, by seeking evidence from:
    1. current year work
    2. consultation with management
    3. review of client's records in previous year
    4. if necessary enquiry of previous auditor to determine the adequacy of his audit procedures.
- Reviewing accounting policy consistency; any changes will need to be in conformity with standard practice.

b) The following are the principal accounting policies that a trading organization may disclose in its financial statements:

(i) Historical Cost Convention

The financial statements have been prepared under the historical cost convention.

(ii) Foreign Currency

Transactions denominated in foreign currencies are translated into cedis and recorded at rates of exchange ruling on the date of the transactions. Balance sheet items denominated in foreign currencies are stated in cedis at rates ruling at the balance sheet sate.

(iii) Depreciation and Fixed Assets

Fixed Assets are shown at cost or valuation less depreciation.

Depreciation is computed using the straight line method so as to write off the cost of the assets over their estimated useful lives.

The annual rates used are as follows:

Leasehold Properties	-	2%
Furniture & Equipment	-	20%
Motor Vehicles	-	20%
Computers – Hardware and		
Software	-	33.33%

Full year's depreciation provision is made irrespective of the date of purchase and no provision is made in the year of disposal.

(iv) Stocks

Stocks are valued at the lower of cost or net realizable value

(v) Debtors

Debtors for trade are stated net of provision for Bad and Doubtful debts.

(vi) Investments

Investments are held for the purposes of trading. They are stated at cost and provision is only made where, in the opinion of the directors, there is a permanent diminution in the value of an investment, it is recognized as an expense in the period in which the diminution is identified.

(vii) Taxation

Taxation is provided for at the current rates on taxable profit.

Disclosure of accounting policies is important to the auditor in that it is a standard practice. It shows how items which are material or critical in determining profit or loss for the year and in stating the financial position have been dealt with. These policies need to be followed consistently, but if there are any departures, they should be justified and fully explained.

c) Investigation is an enquiry commissioned by a client for some specific purpose of the client. This enquiry may be requested for, for a number of reasons and the scope of enquiry may be large. Investigations may be conducted for acquisition of companies, purchase of businesses, prospective investments, fraud, etc.

Specific reports are issued at the end of each investigation.

Verification on the other hand is an examination of items shown in the balance sheet to establish their value, ownership, existence and presentation in the financial statements. It is thus part of the general audit work and no specific report is issued after the verification of balance sheet items.

QUESTION 4

1) Circumstances under which an auditor can qualify his opinion

   (i) Limitation in scope of the auditor's examination

   (ii) Disagreement with the treatment or disclosure of a matter in the financial statement including inherent circumstances.

2) For both circumstances there can be two levels of qualified opinion.

   (i) Material but not fundamental where the circumstances prompting the uncertainty or disagreement is material but confined to one particular aspect of the financial statement so that it does not affect their overall value to any potential user.

   (ii) The more serious qualification where the extent of the uncertainty or disagreement is such that it will be fundamental to the overall view shown by the financial statements, that is the Financial Statement could be misleading.

Table II

3) General form of qualification appropriate to each Potential Situation.

Circumstance	Material but not Fundamental	Fundamental
Uncertainty	Except for …… …. might	Disclaimer of opinion
Disagreement	Except for ………..	Adverse opinion

   (ii) The following can be considered under inherent uncertainties.

      (i) Inherent Uncertainties about the outcome of future events frequently affect, to some degree a wide range of components of a financial statement at the date they are approved.

(ii) Adequacy of accounting treatment, estimates, and disclosures of these inherent uncertainties in the light of available evidence at the date the opinion is expressed.

(iii) Inherent uncertainties regarded as fundamental when they involve a significant level of concern about the validity of on-going basis or other matters whose potential effect on the fundamental is unusually large.

A common example of fundamental uncertainty is the outcome of major litigation.

Matters to be considered and procedures to be followed

(a) Matters to be considered

(i) The nature of business plan and compare with projection in previous business plan to ascertain their reasonableness.

(ii) The intended use of the information

(iii) Specific requirement of the bank

(iv) Probable accuracy and reliability of the information in the plan

(v) The period covered by the information in the plan

(vi) Form of opinion required and knowledge of business

(vii) Ensure that the entire report on the figures in the projections are not at variance

(viii) There should be sensitivity analysis on the projections to assess the margin for error or likelihood of bank conditions not being met

(ix) Additions and calculations should be recomputed to ensure accuracy.

(b) Profit Forecast

(i) Discuss with management the means by which the projected profit was made and determine whether the forecast figures are accurate and reliable.

(ii) Compare the result shown by the most recent management accounts with the forecast and obtain explanation for any material difference.

(iii) Where the forecast results differ materially from actual result achieved in the past inquire whether the reasons justify the differences.

(iv) Check that assumptions made are consistently applied.

(v) Ascertain whether assumptions made for the forecast purpose and other information in the company are in line e.g. sale and marketing plans are in line with expected growth.

(vi) Compare assumptions with general industry dates and trends particularly in respect of Sea Foods market.

(c) Cash Forecast

(i) The cash forecast should be checked to ensure that it correlates to projections with profit forecast.

(ii) The timing should be reviewed to ensure that they are reasonable.

(iii) Any capital expenditure should be verified to supplier's quotations or other reasonable sources such as supplier's sales catalogues.

(iv) Compare cash flow made in the past with current and state any weakness that may turnout in the forecasting procedure.

QUESTION 5

a) Controlling and Monitoring Audit Time & Cost

The strategies for controlling audit time and cost include:

(1) Planning and budgeting time and cost

During the planning the auditor obtains knowledge about the business, identifies critical areas of the audit and assesses levels of risk attached to such areas; determine the level of skill and competence of staff needed to carry out the audit effectively and efficiently. This involves determining the likely reliance on experts, as well as reliance on client's internal audit and client's staff to prepare schedules and summaries supporting the figures in the financial statements and the level of supervision required.

Consideration of the foregoing enables the auditors to prepare the time and cost budgets for the expected scope and conduct of the audit after drawing up the overall audit plan and the audit programmes.

(2) The Time Budget: The final phase of planning is the drawing up of the time budget identifying the timing of individual components of audit work, the grade and number of staff required, the specialist staff requirement and the planned length of time required for each individual phase of the audit.

The time budget provides a basis for:

(a) assigning audit staff

(b) indicating to staff members the work expected of them

(c) monitoring the performance of staff

(d) reviewing the efficiency and effectiveness of each component of the audit

(e) estimating audit costs and negotiating the current year's fees with the client.

(3) Assignment of personnel to engagements

Time budgets for each engagement provide the basis for the allocation of total demands on the firm's resources. The firm can then plan the allocation of staff to audits so as to ensure that staff with appropriate experience and expertise are available. In the absence of advance planning the firm might find itself unable to complete the audit on time.

(4) Evidence and Assistance

This relates to the application of technical standards to individual audits. It is achieved by the use of each audit standard documentation and the use of audit programmes. The audit programme is prepared in the final phase of an audit planning, and details the specific audit procedures and extent of testing. The programmes are reviewed by the partner and constitute procedures to be followed by audit staff.

The firm also identifies procedures for use of expert's advice, such as on tax and computer audit.

All staff assigned to the engagement are briefed as to any problems identified during the planning phase, particularly those related to inherent risk such as going concern problems.

Proper guidance and assistance help audit staff to complete their assignments without much difficulty and in time.

(5) Supervision: The assignment of staff ensures that the work of junior staff is adequately supervised by more senior staff on jobs involving two or more members of staff working together at the client's premises, an adequately experienced staff member is designated as an audit senior with responsibility for directing and supervising the work of less experienced staff. In addition the audit manager and the partner keep in touch with the audit senior, making regular enquiries as to any problems or unusual items encountered. Adequate supervision helps to resolve problems encountered by the audit staff and results in completing the audit in time.

(6) Time Recording: Audit firms require that staff fill time sheets detailing time spent on each sector of the audit programmes on hourly basis. The summary of the recorded times by each staff is compared with the time budget for such staff and each audit area.

The total time summary is then compared with the total time budget for the audit and reasons for any variations sought.

The actual time recorded on the audit then serves as a guide for budgeting time and cost for the next audit taking into account changes that have taken place in the operations of the client and/or the discovery of other critical areas during the planning of the next audit.

b) Review of financing statements

(1) Review of the accounting policies for suitability acceptability, consistent and correct application.

(2) Review of the classification, description and adequate disclosure of items in the financial statements.

(3) Review of the view given by the financial statements whether it is in accordance with the auditor’s knowledge of the economic circumstances of the business.

(4) Review of the financial statements to ensure that the view given thereof will accord with any conclusions to be drawn by reasonable users of the financial information.

(5) Review of post balance sheet events and contingencies to ensure proper reflection of adjusting events and crystallised contingencies and disclosure of material non adjusting events and possible contingent liabilities.

(6) Review of financial statements for going concern applicability.

(7) Review of the financial statements for compliance with accounting standards.

(8) Review of the financial statements for compliance with statutory requirements.

(9) Final analytical review to ensure that the financial statements make sense.

(10) Review of the director’s report to ensure that it is consistent with the financial information.