SOLUTION ASSURANCE & AUDIT PRACTICE NOV 2009

QUESTION 1

Auditor's responsibilities

Definition of fraud – Theft or use of deception to ……… unjust or illegal financial advantage

- The detection of fraud is the primary responsibility of management. Management is expected to put in place controls and strong emphasis within the company on fraud prevention.
- The auditor is not bound to detect fraud. However, the auditor has a duty to bring to bear on the work he has to perform that skill, care and caution that a reasonably competent, careful, cautious auditor would use.
- The auditor may discover fraud during an audit however, it is not a requirement auditing standard that auditor should detect fraud where an auditor detect fraud or have a reason to believe that fraud exists as a result of his audit the auditor;

  Refer auditors responsibility to properly …. Perform and evaluate by audit work to have reasons ………………….

  (i) The auditor should communicate the detected or suspected fraud to management as early as possible.

  (ii) Where fraud discovered involves management or an employee with significant role in internal control or the fraud has material impact on the Financial Statements the auditor must communicate the matter to those in charge of governance issues.

  (iii) Where the auditor has a statutory duty to report a fraud or suspected fraud to external regulators' he should do so.

  But he should report all instances of fraud to the appropriate level of management e.g. senior management.

(iv) Where fraud has material impact on the financial statement the auditor may have to qualify his opinion

(b)
- The auditor should obtain copies of the Bank Reconciliation Statement, account analysis along side bank statement on all current accounts, savings accounts
- Certificates of deposit and other bearing and non-bearing account should be obtained.

Statement of audit objectives

- To ensure that all deposit/lodgement have been appropriately credited, and
- All debits/withdrawals from the bank were properly ….. valid

The audit should perform the following test:

- Confirm the mathematical accuracy of the reconciliation

- Examine the bank statement for possible alterations
- Trace the balance on the bank statement back to bank confirmation statements.
- Agree the balance with the company's ledge
- Trace the deposits in transit to the bank statement at the end of the company's financial period to censure that the ………. is in the proper period.
- Examine cancelled cheques and compare to the list of outstanding checks
- Sample supporting documentation of cheques written for material amount
- Verify supporting documentation on outstanding cheques written for material amount
- Verify accuracy or non-operational cash or cash equivalent accounts (CDs and other investment accounts)

Analysis should include the verification of the banks and institution holding the funds, interest rate, maturity date, beginning and ending balances and current period activity.

Books and bank balances should be compared and any accruals of interest analysed.

(c) Potential areas of difficulty for audit committees are:

(i) The fear that the purpose of an audit committee is to expose/'catch' management out.

- Non-executive directors being over-burdened with detail of work
- A two-tier board of directors and the demand on management to produce report for all of them.
- Additional cost in terms of, at least, the time involved.

(ii) Advantages of Audit Committees are:

- They may improve the quality of management accounting being better placed to criticize internal functions
- They lead to better communication between the directors, external auditors and management
- They help to avoid conflicts arising between management and auditors

NB Go further and add role of audit Committees

QUESTION 2

a) (i) Contingency can be described as a condition which exists at the balance sheet date where the outcome will be confirmed only on the occurrence or non-occurrence of one or more uncertain future events.

A highly probable or virtually certain contingent liability should be provided for in the accounts.

A possible contingent liability should be disclosed by note whilst there should be no disclosure or note for remote ……….. of contingent liability

(ii) The following audit procedures are suggested for the verification of the existence of such contingent as pending:

a. Review the client's system of recording claims and the procedure for bringing these to the attention of management and board.

b. Discuss the arrangements for instructing solicitors with the official responsibility for legal matters

c. Examine the minutes of the Board of Directors and or executive or other relevant committee for references to, or indications of, possible claims.

d. Examine bills rendered by solicitors and correspondence with them, in which connection the solicitors should be requested to furnish bills or estimates of changes to date to confirm they have no unbilled changes.

e. Obtain a list of matters referred to solicitors from the appropriate director or officials with estimates of the possible ultimate liabilities.

f. Obtain a written assurance from the appropriate director or official that he is not aware of any matters solicitors other than those disclosed.

b) Other areas that might be investigated as part of the analytical procedures should include:

(i) Examine changes in products customers and level to returns

(ii) Assess the effect of price and mix changes and cost of sales

(iii) Consider the effects of inflation, industrial disputes, changes in production methods and changes in activity on the charge for wages

(iv) Obtain explanation for all major variances analysed using a standard costing system with particular attention to over/under absoption of overheads

(v) Compare Trends in production and sales and assess the effect on any provisions for slow moving stocks.

(vi) Review profit and loss for items which may have been omitted training levy, provision for dilapidation, contribution for pension funds.

(vii) Ensure expected variations arising from the underlisted which might have occurred.

- Industry or local trends

- Known disturbances of the trading pattern for example closed branches, strikes, failure by suppliers etc)

QUESTION 3

(a) Several reasons are available for Information …. Audit

- (i) It assures accuracy of financial reporting
- (ii) Support/effective risk management practices
- (iii) Assess/ensure compliance to standards regulations and rules (external and internal)
- (iv) It helps Safeguard Information assets through recommendation o controls or measure to address control deficiencies
- (v) Determine if Information Systems and processes are operating sounding within normal parameters. And in line with business needs.

Information systems Audit befits are:

- Improves Risk Management including potential enhancement of Risk Management Culture.
- Safe guarding of Information assets
- Achievement of legal and regulatory compliance (i.e avoid penalties, fines, jail by ensuring the right policies are in place.
- Ensures proper and effective and optimum utilization of Information Technology systems.
- Alignment with business process, needs and business risks

General controls to be considered when planning Information Technology Audit are:

- Physical and environmental security
- Logical security (Infrastructure)
- Change and release management
- Business Continuity, Resilience and (Disaster) Recovery Management
- Procurement/Supplier Management
- Database management controls
- Asset (Hardware/software) management
- Capacity and availability management
- Incident and problem management

Application controls to be considered includes

- Application Access controls
- Input Controls
- Output controls
- Processing Controls

- Interface (Data Transfer) Migration Controls

(b) The purpose and principles of quality controls.

i. Quality control is a means by which a firm obtains reasonable assurance that its expression of audit opinions always in line with approved auditing standards, statutory and contractual requirement and any professional standards set by the firm itself.

ii. Quality control promotes observance of the personal standards relevant to the work of an auditor, which are described in ethical statement instituted by Accountancy Bodies.

iii. Quality controls are also policies and procedures adopted by a firm to provide reasonable assurance that all audits done by the firm are being carried out in accordance with the objectives and goals and basic principles governing audit.

iv. Quality control policies are objectives and goals that steps should be taken to accomplish. An audit firm should adopt and implement quality control policies that incorporate the following which should be part of the training program.

(a) <u>Personal Qualities</u>
Personnel in the firm should adhere to the principles of integrity objectivity confidentiality and independence

(b) <u>Skill and Competence</u>
The firm should be staffed by personnel who have attained and maintained the skills and competence required to enable them to fulfil their responsibilities. This requires procedures relating to recruitment, technical training and updating and on the job training.

(c) <u>Assignment</u>
Audit work should be assigned to personnel who have the degree of technical training and proficiency required in the circumstances.

(d) <u>Direction and Supervision</u>
There should be sufficient direction and supervision of work at all levels to provide the firm with reasonable assurance that the work performed by the firm meets appropriate standards of quality. Whenever necessary, consultation should be made with those who have the appropriate expertise.

(e) <u>Acceptance and Continuance of Clients</u>
The firm should carry out evaluation of prospective client and should review on an on-going bases relationship with existing clients.

When making a decision to accept appointment or re-appointment the firm should consider its won independence, ability to provide adequate services to the client and the integrity of the client’s management.

(f) <u>Monitoring the Firm’s Procedures (Inspection)</u>
The firm should monitor the effectiveness of its quality control policies and procedures. The monitoring process should provide reasonable assurances that

measures are being maintained to ensure the professional standards of the firm are being properly carried out.

QUESTION 4

(a) Matters or situations that will affect the auditor's independence include:

(i) Fees
Advisably a firm should not derive more than 15% of its gross recurring fee income from any one client or group of connected clients.

(ii) Personal relationships
Professional relationship should be avoided if there exist personal relationship.

(iii) Beneficial ownership of shares
Ownership of shares in client companies by partners or family relations can affect the auditor's independence.

(iv) Loans to and from clients
It is not advisable to make loans to client or receive loans from clients or guarantee loans to clients.

(v) Acceptance of goods and services from client may also be a threat to independence.

(vi) Commission
Receiving commissions from financial institutions like insurance, on advice given can compromise the auditor's independence.

(vii) Conflict of interest situations can influence the auditors independence.

(b) Procedures that can be used to conduct the tax investigation include:

(i) Obtain terms of reference and examine it

(ii) Obtain copies of tax regulations pertaining to those years concerned – the five years.

(iii) Obtain the financial statements for the past five years.

(iv) Compute the corporate tax assessment for the years involved.

(v) Identify the tax credits, reliefs and tax holidays for the period concerned.

(vi) Ascertain the tax liabilities for the years.

(vii) Obtain information on taxes paid on account during the five years.

(viii) Ascertain the tax liability payable for the five years.

(ix) Seek confirmation on tax liability from the Internal Revenue Service.

(x) Hold discussions with management

(xi) Issue the final report on the investigation.

(c) a. A review of the post balance sheet events will cover the following:

(i) Reviewing matters fundamental to the continuing existence of Zebilla Ltd.

(ii) Examination of profit forecasts and cash flow forecasts for the new period; comparing with actual history.

(iii) Review of directors and shareholders minutes.

(iv) Examination of the accounting records of the subsequent period noting

- post balance sheet settlement of debtors
- stock movement
- liquidation of trade creditors
- work in progress

(v) Specific enquiries be made of management on

- whether new commitments, borrowings or guarantees have been entered into
- whether sale of assets have occurred or are planned
- whether any unusual accounting adjustments have been made or are contemplated on.

b. An examination of Zebilla Ltd's directors' minutes should focus on

i. Boafo's approval of the accounts and their report for the current financial year.

ii. Resolution to pay interim dividend if allowed by the company's Articles

iii. Changing in and rotation of directors

iv. Authority for the purchase of large …… of equipment and other unusual expenditure

v. Management future in the Zebilla Ltd

vi. Resolutions to make calls on partly paid shares

c. (i) Staff productions – Staff may spend time browsing the internet instead of working. This will reduce the entity's overall output.

(ii) Legal inability – Unlicensed software may be downloaded by staff on to the entity's system thus exposing it to legal risk.

(iii) Security – The operations of the entity is exposed to hackers and

QUESTION 5

(a) Analytical procedures mean the analysis of relationships.

(i) between items of financial data or between items of financial and non financial data deriving from the same period or

(ii) between comparable financial information deriving from different periods or different entities to identify consistencies and predicted patterns or significant fluctuations and unexpected relationships and the results of investigations thereof.

Analytical procedures include the consideration of comparisons of the entity's financial information with for example:

(i) comparable information for prior periods

(ii) anticipated results of the entity from budgets or forecasts

(iii) predictive estimates prepared by the auditors such as an estimation of the depreciation charge for the year and

(iv) similar industry information such as a comparison of the entity's ratios of sales to trade debtors with industry averages or with the ratios relating to the entities of comparable size in the same industry. Analytical procedures also include consideration of relationships

- between elements of financial information that are expected to conform to a predicted pattern based on the entity's experience such as the relations of gross profit to sales and

- between financial information and relevant non-financial information such as the relationship of payroll costs to number of employees.

Analytical procedures may be applied to consolidated financial statements, financial statements of components and individual elements of financial information.

The purposes for use of analytical procedures by auditors are

(a) to assist in planning the nature, timing and extent of other audit procedures

(b) as substantive procedures when their use can be more effective or efficient then other procedures in reducing detection risk for specific financial statement assertions and

(c) as part of the overall review of the financial statements when completing the audit.

(b) When intending to apply analytical procedures as substantive procedures, auditors consider a number of factors such as

(i) the plausibility and predictability of the relationships identified for comparison and evaluation. For example, there is a strong correlation between certain selling expenses and turnover in businesses where the sales force is paid by commission.

(ii) The objectives of the analytical procedures and the extent to which their results are reliable

(iii) The availability of information, both financial (such as budgets or forecasts) and non0financial (such as the number of units produced or sold).

(iv) The relevance of information available, for example whether budgets are established as results to be expected rather than as goals to be achieved.

(v) The comparability of the information available, for example broad industry data may need to be supplemented to be comparable with that of an entity that produces and sells specialised products.

(c) The principal auditor of Anansie Resources Ltd. Plc should consider

(i) the materiality of the portion of the financial statements which were audited by John & Co

(ii) the degree of their knowledge regarding the business of the components

(iii) the nature of their relationship with John & Co

(iv) their ability where necessary to perform additional procedures to enable them to act as principal auditors

(v) the risk of motional misstatements in the financial statements of the components audited by John & Co.