APRIL 2022 PROFESSIONAL EXAMINATIONS
ADVANCED AUDIT & ASSURANCE (PAPER 3.2)
CHIEF EXAMINER'S REPORT, QUESTIONS AND MARKING SCHEME

QUESTION ONE

a) When a firm concludes that a breach has occurred, the firm shall terminate, suspend or eliminate the interest of relationship that caused the breach and address the consequences of the breach.

Required:
Evaluate **FOUR (4)** factors that determine the significance of a breach of IESBA code of ethics. **(4 marks)**

b) Where an audit firm own shares or is a trustee of a trust that hold shares in a client, there is said to be a financial interest in the client's affairs. According to the IESBA, some selected parties are not allowed to own direct or indirect material financial interest in a client.

Required:
i) Explain **THREE (3)** parties that are not allowed to own direct or indirect financial interest in a client. **(3 marks)**
ii) Identify **THREE (3)** safeguards that may be relevant in relation to direct or indirect financial interest in a client. **(3 marks)**

c) K. O. and Associates, a firm of Chartered Accountants has accepted a statutory Audit engagement from Special Cream Ltd, a bookshop with many sales point across the country. In 2021, the company implemented a computerised system that has been networked to all sales point to the Head Office in Accra. In the middle of 2021, the company started accepting mobile money as a means of payment in addition to cash and cheque payment. Mobile money payments are confirmed with an accounts staff before books are supplied.

In planning the audit of Special Cream Ltd, the Audit Manager, Samuel Alhassan, identified risks associated with electronic processing systems which provides additional challenges for auditors.

Required:
i) Discuss **FOUR (4)** challenges K. O. and Associates would encounter in performing an assurance engagement on the electronic processing system. **(4 marks)**
ii) Discuss **FOUR (4)** audit approaches K. O. and Associates should adopt in performing an assurance engagement on electronic processing system. **(6 marks)**

(Total: 20 marks)

QUESTION TWO

Lartey Company Ltd (LCL) is a Private Limited Liability Company that was incorporated several years ago under the Companies Act, 1963 (Act 179) now Companies Act, 2019 (Act 992). The company is currently listed on the Ghana Stock Exchange. LCL is one of the world's leading leisure travel providers, operating under several brand names to sell packaged holidays. The company catered for more than 10 million customers in the last 12 months. Draft figures for the year ended 30 September 2020 show revenue of GH¢320 million, profit before tax of GH¢15 million, and total assets of GH¢410 million. LCL's executives earn a bonus based on the profit before tax.

You are the senior manager responsible for the audit of LCL. The final audit is nearing completion, and the following points have been noted by the audit senior for your attention:

Acquisition of Esinam Co. Ltd.
On 15 November 2020, LCL acquired Esinam Co. Ltd, a company offering adventure holidays for independent travelers. Esinam Co. Ltd represents a significant acquisition, but this has not been recognised in the financial statements. **(5 marks)**

Aseye Cruises
One part of the company's activities, operating under the Aseye Cruises brand, provides cruise holidays. Due to economic recession owing to Covid-19 pandemic, the revenue of the Aseye Cruises business segment has fallen by 25% this year, and profit before tax has fallen by 35%. Aseye Cruises contributed GH¢64 million to total revenue for the year ended 30 September 2020, and has identifiable assets of GH¢23.5 million, including several large cruise liners. The Aseye Cruises brand is not recognised as an intangible asset, as it was internally generated. **(7 marks)**

Compensation Claim
In July 2020, thousands of holiday-makers were left stranded abroad after the company operating the main airline chartered by LCL suffered Covid-19 restrictions. The holiday-makers were forced to wait an average of two weeks before they could be returned home using an alternative airline. They have formed a group which is claiming compensation for the time they were forced to spend abroad, with the total claim amounting to GH¢2 million. The reasons for the group claiming compensation include accommodation and subsistence costs, lost income and distress caused by the situation. The claim has not been recognised or disclosed in the draft financial statements, as management argues that the full amount payable will be covered by LCL's insurance cover. **(8 marks)**

Required:
Comment on the matters raised and in your review of the working papers, state the audit evidence required to draw reasonable conclusions for the year end 30 September 2020.

(Total: 20 marks)

QUESTION THREE

Aseda Manufacturer Ltd (Aseda) is one of the established business in the manufacturing sector. The company has received different awards over the past decade. Aseda's year-end was 30 September 2020.The audit of Aseda is nearly complete and the financial statements and the audit report are due to be signed in a few days. However, the following additional information on two material events has just been presented to the auditor on 3 December 2020.

Event 1
This event occurred on 10 November, 2020. Production at the Aluta factory was halted for one day when a truck carrying dye used in colouring the fabric on mattresses reversed into a metal pylon, crashing the vehicle and causing a dye to spread across the factory premises and into a local river. The Environmental Protection Agency (EPA) of Ghana is currently considering whether the release of the dye was in breach of environmental legislation. The company's insurers have not yet commented on the event.

Event 2
This event occurred on 19 October, 2020.The springs in a new type of mattress have been found to be defective making the mattress unsafe for use. There have been no sales of this mattress as it was due to be marketed in the next few weeks. The company's insurers estimate that inventory worth GH¢600,000 has been affected. The insurers also estimate that the mattresses are now only worth GH¢100,000. No claim can be made against the supplier of springs as this company is in liquidation with no prospect of any amounts being paid to third parties. The insurers will not pay Aseda for the fall in value of the inventory as the company was underinsured. All of this inventory was in the finished goods store at the end of the year and no movements of inventory have been recorded post year-end.

Required:

a) For each of the two events above:

i) Explain the reporting implication of the issues in accordance with ***IAS 10: Events after the Reporting Period.*** **(4 marks)**

ii) Explain the auditors' responsibility and the audit procedures that should be carried out in accordance with ***ISA 560: Subsequent Events***. **(12 marks)**

b) Assume that the date is now 10 December 2020, the financial statements and the audit report have just been signed, and the Annual General Meeting is to take place on 10 January 2021. The Environmental Agency has issued a report on 28 December 2020 stating that Aseda is in breach of environmental legislation and a fine of GH¢800,000 will now be levied on the company. The amount is material to the financial statements.

Required:

Explain the additional audit work the auditor should carry out in respect of this fine. **(4 marks)**

(Total: 20 marks)

QUESTION FOUR

a) Going Concern assumption is important in Financial Audit, without which an entity being audited is viewed as not operating to a foreseeable future. In public sector, going concern is also assumed, though the assumption may be different from financial consideration.

Required:
Discuss the factors an auditor will consider in determining the going concern assumption of a public sector entity. **(10 marks)**

b) Supreme Audit Institutions (SAI) are external auditors for the state or a country. They are set up to audit the work of state institutions and usually report to parliament. They are independent in nature and their work is not subject to control of the executive.

Required:
Discuss the merits of Supreme Audit Institution (SAI) on a state economy. **(10 marks)**

(Total: 20 marks)

QUESTION FIVE

a) Companies Act, 2019 (Act 992) section 143 (2) states among others that a company, person or firm that carries out duties of an auditor should ensure that the personal judgement of the auditor is not impaired by reason of any relationship with a client that will result in a conflict of interest.

Some governance experts consider the provision of non-audit services to audit clients as an example of conflict of interest and could impair the firm's independence.

Required:
In reference to the above concern, discuss **FOUR (4)** non-audit services that could lead to conflict of interest or impair the independence of an Auditor. **(10 marks)**

b) Asogli has been in existence since 2005, operating a car repair and servicing business. The car service solutions offered to its clients are diagnosis, ECU programing, key programing, body works, electrical works and air conditioning. Its year end was 31 October 2020. You are the senior audit manager of KK and Associates, the Auditor of Asogli. The audit is due to commence and Asogli intend to sign the audit report on 20 November, 2020.

Your attention has been drawn to the following matters by the Partner-in-charge:

i) Asogli's Finance Director has notified you that an error occurred in closing the purchase ledger at the year end. Rather than closing on 31 October, it accidentally closed one week earlier on 24 October. All purchase invoices received between 25 October and the year-end have been posted to the 2021 year-end purchase ledger.

Required:
Describe substantive procedures you would perform to obtain sufficient and appropriate audit evidence in relation to the above. **(5 marks)**

ii) Asogli recently announced its plans to reorganise its business operations. This will involve closing some units, retraining some existing staff and disposing off some surplus assets. These plans were agreed at a board meeting in October and announced to their shareholders on 29 October, 2020. Asogli is proposing to make a reorganisation provision in the financial statements.

Required:
Assume that the reorganisation occurred on 15 November, 2020, what will be the responsibility of the auditor in line with auditing standards? **(5 marks)**

(Total: 20 marks)

SOLUTION TO QUESTIONS

QUESTION ONE

a) When a breach occurs, the firm should consider whether any legal or regulatory regulations apply, and if necessary report the breach to a member body or regulator. The breach should be communicated to the engagement partner (and other relevant parties).
Evaluate the significance of the breach, based on;

- The nature and duration of the breach
- Any previous breaches re. the current audit engagement
- Whether a member of the audit team had knowledge of the interest or relation caused the breach
- Whether the individual who caused the breach is a member of the audit team.
- If they were on the audit team, their role
- The impact of any relevant services on the accounting records or the amounts of the financial statements
- The extent of any threats created by the breach

(Any 4 points @ 1 mark each = 4 marks)

b)

i) A financial interest in a client constitutes a substantial self-interest threat. According to both the ICAG and the IESBA, the parties listed below are not allowed to own a direct financial interest or an indirect material financial in a client.

- The assurance firm
- A member of the assurance team
- An immediate family member of a member of the assurance team

(3 marks)

ii) The following safeguards may therefore be relevant.

- Disposing of the interest
- Removing the individual from the team if required
- Keeping the clients audit committee informed of the situation
- Using an independent partner to review work carried out if necessary

Such matters will involve judgement on the part of the partners making decisions about such matters. For example, what constitutes a material interest? A small percentage stake in a company might be material to its owner. How does the firm judge the closeness of a relationship between staff and their families, in other words, what does immediate mean in this contest?

Audit firms should have quality control procedures requiring staff to disclose relevant financial interest for themselves and close family members. They should also foster a culture of voluntary disclosure on an ongoing basis so that any potential problems are identified on a timely basis.

(3 marks)

c)

i) Challenges in performing an assurance engagement on an electronic processing system

- The need for specialist knowledge about e-commerce systems.
- Problems that may arise when some aspects of the e-commerce system (such as the electronic payments system) are outsourced by the client to another entity.
- The role of the client's internal auditors in monitoring the integrity of the e-commerce system.
- The need for specialist controls (general and application controls) for the system
- Possible problems of independence and conflicts of interest, if the audit firm was involved in designing or setting up the e-commerce system that is now subject to 'audit'.

(Any 4 points @ 1 mark each = 4 marks)

ii) The audit approach to an e-commerce system should include the following elements:

- First of all, the audit firm should decide whether the engagement should be accepted (as in any professional engagement)
- The firm should then plan the engagement: an important aspect of planning may be to make available audit staff with appropriate expertise in e-commerce systems.
- The firm should obtain a detailed knowledge of the client's business.
- It should consider liaison with the internal auditors of the client, if there have been internal audit investigations into the client's e-commerce transactions or system.
- The firm should identify and evaluate the risks in the system.
- It should ascertain and evaluate the control environment and the specific internal controls that are in operation.
- It may also be appropriate to perform a going concern review, particularly in the case of entities that rely mainly on e-commerce activities for their income.

(Any 4 points @ 1.5 marks each = 6 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

This question was made up of three (3) sections (i.e. A,,B,&C) with total of 20 marks.

The a) part of the question required candidates to evaluate four (4) factors that determine the significance of a breach of IESBA Code of ethics. Some candidates provided factors that constitute a breach rather than evaluation of factors that determine the significance of a branch of the IESBA code of ethics. Some candidates also explained the various threats. Others also wrote on factors that cause the breach, instead of factors that determine the significance of the breach. This section was badly answered by candidates.

Sub-question b) was made up of subsections i) and ii). Subsection (i) required candidates to "explain three (3) parties that are not allowed to own direct or indirect financial interest in a client. Section ii) on the other hand required candidates to identify three (3) safeguards that may be relevant in relation to direct or indirect financial interest in a client.

Question c) was made up of subsections i) and ii). Subsection i) required candidates to discuss four (4) challenges that would be encountered in performing an assurance engagement on an electronic processing system from a given scenario, subsection ii) on the other hand required candidates to discuss audit approaches that should be adopted in performing an audit in electronic processing system from a given scenario. These subsection of the question was fairly well attempted.

QUESTION TWO

Esinam Co. Ltd
Matters to consider
According to IAS 10 Events After the Reporting Period, the acquisition of a subsidiary after the year-end is a non-adjusting event, as it is unrelated to a condition existing at the year-end. If non-adjusting events after the reporting date are material, non-disclosure could influence the economic decisions of users taken on the basis of the financial statements.

A note to the financial statements should disclose for each material category of non-adjusting event the nature of the event and an estimate of its financial effect, or a statement that such an estimate cannot be made.

As a note has not been provided, and Esinam Co. Ltd represents a significant acquisition, there is currently a breach of the disclosure requirements of IAS 10. If a note is not provided, the audit opinion should be qualified 'except for' due to material misstatement caused by a lack of disclosure required by accounting standards.

Evidence:

- A copy of the press release announcing the acquisition, including the date of the announcement.
- A copy of any legal agreement pertaining to the acquisition, including the date that control passes to Leisure Company Limited.
- A review of any due diligence report received pertaining to the acquisition, detailing the value of assets purchased, and the consideration paid.
- A review of the financial statements of Esinam Co. Ltd, to determine that it represents a significant acquisition for the group, therefore warranting a disclosure note.
- A review of any note provided by management to be included in the financial statements.

(5 marks)

Aseye Cruises
Matters to consider
The Aseye Cruises operation is clearly a significant part of Leisure Company Limited's activities, contributing 20% to revenue (640/3,200 x 100%). This revenue stream is material to the financial statements. The identifiable assets of the business segment represent 5·7% of total assets (235/4,100 x 100%), so they are material to the statement of financial position.

The fact that the brand has performed badly is an indicator of impairment according to IAS 36 Impairment of Assets. Although the brand itself is not recognised, the assets identifiable with the brand should be assessed for impairment by management, to determine their recoverable amount.

The assets represent a cash generating unit, as the cash flows generated by the assets identifiable with Aseye Cruises are independent of cash flows generated by other assets of the company. Management should conduct an impairment test by calculating the value-in-use of the cash generating unit, and also calculate the fair value less cost to sell, to determine the recoverable amount of the assets collectively. Any impairment loss should be expensed. Management will want to avoid recognising an impairment loss in profit due to the detrimental impact on their bonus payment.
The calculations involved in the impairment test contain subjective elements, such as determining the appropriate discount rate for discounting cash flows to present value, and assumptions over the projected cash flows of the brand. Management's assumptions may need to be approached with scepticism due to the bonus based on profit.

Evidence:

- A review of management's impairment test (if conducted), including:
  - ✓ assessment that an appropriate discount rate has been used
  - ✓ agreement that the assumptions to determine future cash flows are reasonable and in
  - ✓ line with business understanding
  - ✓ agreement that the correct carrying value of assets has been used for comparison of recoverable amount
  - ✓ agreement that all identifiable assets have been included in the cash generating unit
  - ✓ recalculation of all figures.
- Discussion with management over the expected future performance of Aseye Cruises including any strategies to be put in place to combat the declining performance.
- A review of post year-end management accounts for the performance of Aseye Cruises after the reporting date.
- A review of the level of bookings made in advance for cruises to be taken in the future.

(7 marks)

Compensation claim
Matters to consider
The claim for compensation is material to profit as it represents 13·3% of profit before tax (20/150 x 100%). It is not material to the statement of financial position as it represents only 0·49% of total assets (20/4,100 x 100%).

Management may want to ignore the provision, as its recognition would reduce profit before tax by a material amount, therefore reducing their bonus payment. This issue is also inherently risky as it is based on reaching a judgement about the probability of the amount becoming payable.

However the claim cannot be ignored. A proper assessment should be made as to whether the amount claimed should be treated as a provision or a contingent liability. According to IAS 37 Provisions, Contingent Liabilities and Contingent Assets, a provision should be recognised where there is a present obligation as a result of a past event, a probable outflow of economic benefit, and a reliable estimate can be made of the amount. In the event that there is a possible outflow of economic benefit, a note to the financial statements describing the nature and estimated potential financial effect of contingent liability should be provided.

The fact that the compensation, if paid, would be covered by insurance does not mean that the matter should be ignored. Any amount potentially recoverable from the insurers should be assessed as to whether it is virtually certain to be received, in which case a receivable should be recognised, or if the recoverability is less than virtually certain, a note to the financial statements describing the contingent asset should be provided. An assessment should be carried out on the recoverability of the amount claimed.

Further liabilities may also need to be recognised in respect of legal costs. This would further reduce the year-end profit figure.
In the event that the claim results in the recognition of a provision, and the insurance reimbursement results in the recognition of a receivable, the two items should be separately presented in the statement of financial position, and not netted off.

Evidence:
- A copy of the claim made by the group of holiday-makers, detailing the GH¢20 million claimed and the basis of the claim.
- A review of correspondence between the 'claim group' and the company.
- Correspondence from Leisure Company Limited's legal representatives, showing their opinion on the most likely outcome of the claim.
- A copy of any press releases made by Leisure Company Limited concerning the stranded holiday-makers – this could help to establish whether a constructive obligation exists.
- A review of press coverage and internet stories about the situation, to assess any comments made in public by company representatives regarding the claim.

- A review of the standard terms and conditions that holiday-makers agree to on booking a holiday – this could help to establish any legal obligation, e.g. to cover the cost of accommodation before being returned home.
- Details of any helpline or other means by which the stranded holiday-makers were given advice at the time of the incident (e.g. if the company advised them to book alternative accommodation this may imply that the company is liable for the cost).
- A review of invoices received pre and post year-end in respect of legal costs, to ensure adequately included in expenses and accrued for if necessary.
- A copy of the business insurance contract detailing the level of cover, if any, provided for this situation, and any amount that will not be covered (an excess on the policy).
- Correspondence between the insurance company and Leisure Company Limited establishing whether a claim on the insurance has been made.
- A written management representation stating management's opinion on the outcome of the court case, and the likelihood of reimbursement from the insurance cover.

(8 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS
The question required candidates to comment on matters raised in three (3) different scenarios given and the audit evidence required to draw reasonable conclusions in respect of each scenario.

Scenario 1: Acquisition of Esinam Co Ltd. This required knowledge of IAS 10: Events after the Reporting Period.
Some candidates were able to state that the acquisition was a non- adjusting event and for that matter a note to the financial statement should be made.

Scenario 2: Aseye Cruises.
This required knowledge of ***IAS 36: Impairment of Assets***. Some candidates performed fairly well while others performed badly.

Scenario 3: Compensation claim
This required knowledge of IAS 37: Provisions, Contingent Liabilities and Contingent Assets. This was fairly well attempted by some candidates.

NOTE: As per the requirement, each of the three (3) events required comments and Audit Evidence. Some candidates did not structure their answers well hence failed to satisfy the requirements.

QUESTION THREE

a)

i) **Reporting Implication**

Event 1

The release of dye occurred after the end of the reporting period, so this is indicative of conditions existing after the end of the reporting period – the event could not be foreseen at the end of the reporting period.

In this case, no adjustment to the financial statements appears to be necessary.

However, the investigation by the Environmental Agency could result in a legal claim against the company for illegal pollution so as a material event it will need disclosure in the financial statements.

Event 2

The problem with the inventory of mattress provides additional evidence of conditions existing at the end of the reporting period as the inventory was in existence and the faulty springs were included in the inventory at this time.

The value of the inventory is overstated and should be reduced to the lower of cost and net realisable value in accordance with IAS 2 Inventories.

An adjustment for this decrease in value must be made in the financial statements. The mattresses should therefore be valued at GH¢ 100,000 being the net realisable value.

The decrease in value of inventory took place after the end of the reporting period but before the financial statements and the audit report were signed.

The auditor has an active duty to design and perform audit procedures to obtain sufficient and appropriate evidence of all events up to date of the auditor's report that require adjustment or disclosure in the financial statements are:

- Identified
- Are suitably reported in the financial statements

(4 marks)

ii) **Auditors Responsibility**

Event 1

As with event 1, the event takes place before the signing of the audit report, therefore the auditors have a duty to identify material events affecting the financial statements.

The event is after the reporting period but represent new conditions arising and therefore will qualify to be non-adjusting event. If the impact on the financial statements is material, the auditor should ensure adequate disclosure.

Where disclosure is not made and the auditor considers disclosure is necessary, modify the audit opinion on the grounds that the Financial Statements did not disclose all the information required. This will be for lack of disclosure (not provision) even though the amount cannot yet be determined.

Alternatively, if the auditor considers that the release of dye and subsequent fine will affect Aseda Manufacturer Limited's ability to continue as a going concern, draw the members' attention to this in the material uncertainty relating to going concern paragraph of the audit report.

Audit procedures will include:

- Obtain any documentation on the event, for example board minutes, copies of environmental legislation and possibly interim reports from the Environmental Agency to determine the extent of the damage.
- Inquire of the directors whether they will disclose the event in the financial statements.
- If the directors plan to make disclosure of the event, ensure that disclosure appears appropriate.
- If the directors do not plan to make any disclosure, consider whether disclosure is necessary and inform the directors accordingly.

Event 2
Auditor's Responsibility
These procedures should be performed as close as possible to the date of the auditor's report and in addition representation regarding subsequent events should be sought on the date the report was signed. The auditor should ensure that management have accounted for or disclosed subsequent events properly if not the implication on the audit report should be considered.
Audit procedures are therefore required to determine the net book value of the inventory and check that the GH¢ 100,000 is the sales value of the mattresses.

Audit procedures will include:

- Obtain documentation from the insurers confirming their estimate of the value of the mattresses and that no further insurance claim can be made for the loss in value.
- Contact solicitors/administrators of the spring supplier to confirm no refund can be expected for the defective springs.
- Obtain the amended financial statements and ensure that the directors have included GH¢ 100,000 as at the end of the reporting period and that the year-end value of inventory has been decreased to GH¢ 100,000 on the statement of financial position, statement of financial position note and the statement of comprehensive income.
- Review inventory lists to ensure that the defective springs were not used in any other mattresses and that further adjustments are not required to any other inventory.
- Obtain an additional management representation point confirming the accuracy of the amounts written-off and confirming that no other items of inventory are affected.
- Finally, assessing the effect on the audit opinion after the decision of the directors regarding the inventory value is known. A qualified opinion may be required where appropriate adjustments are not made to the financial statements.

(12 marks)

b) Additional Audit Work

The notification of a fine has taken place after the audit report has been signed. Audit procedures will include:

- Discuss the matter with the directors to determine their course of action.
- Where the directors decide to amend the disclosure in the financial statements, audit the amendment and then re-draft and re-date the audit report as appropriate.
- Where the directors decide not to amend the disclosure in the financial statements, the auditor can consider other methods of contacting the members. For example, the auditor can speak in the upcoming general meeting to inform the members of the event.
- Other options such as resignation seem inappropriate due to the proximity of the annual general meeting (AGM). Resignation would allow the auditor to ask the directors to convene an extraordinary general meeting, but this could not take place before the AGM so the auditor should speak at the AGM instead.

(4 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

The question provided two scenarios about two (2) different events. The question was in two sections (a&b) with a) sub- divided into i) and ii). i) required candidates to explain the reporting implication for each of the two (2) events, while ii) required candidates to explain for each of the two events the auditor's responsibility to be carried out in accordance with ISA 560: Subsequent Events.

Note: Event 2 required knowledge of IAS 2: Inventories. This was fairly attempted.

For the b) part, the question required candidates to explain the additional audit work the auditor should carry out in respect of a fine from a given scenario. This was fairly attempted by candidates.

QUESTION FOUR

a) Cessation of a public sector entity is most likely to result from a government policy decision. A policy decision may be taken to wind up and dissolve an entity in its entirety, to scale back its operations and transfer some of its functions to another public entity, merge with another public entity or privatize the entity. In each of these cases the operational existence of all or part of the entity ceases. Only in the case of dissolution without any continuation of the entity would the going concern basis cease to be appropriate. In the other cases public sector auditors consider the basis on which the activities are transferred, from the viewpoint of the entity that is relinquishing the assets and liabilities at the accounting date.

   In forming a view of the entity's ability to continue its operations, public sector auditors' consideration of going concern embraces two separate, but sometimes overlapping, factors:

- The greater risk associated with changes in policy direction (for example, where there is a change in government); and
- The less common operational, or business, risk (for example, where an entity has insufficient working capital to continue its operations at its existing level).

  To minimize the risk of changes in government policies not coming to the auditor's attention which could impact on the going concern assumption, the auditor ascertains whether:

- The government has declared its intention to review an area of policy affecting the audited entity;
- A review has been announced and is in progress;
- A review has indicated that the audited entity could be rationalized or that an entity's future may be re-examined;

  The fact that a public sector has liquidity problem or is not profitable does not in itself mean that it has going concern problems. It is when the government decides not continue with its operation since the government may choose to resource it when the need be to continue with its operation.

(Any 5 points @ 2 marks each = 10 marks)

b) Merits of Supreme Audit Institution (SAI) on a state economy:

- The institution is an independent body and works without fear or favour, this helps to instil discipline in the financial system of a country as the true state of the state institutions are reported on, inuring investor confidence and going a long way to improve investor relationship.
- As a result of the checks it brings to bear on executives in charge of public funds, it makes people accountable ensuring state funds are not misused.
- The citizens of a state develop confidence in ability of the state to protect their resources and rely on the institutions of the state for their economic activities.
- It provides management boards of entities with reliable information enabling them to assess their operations and plan ahead.
- It provides the legislature with timely information to facilitate transparency and accountability of how government resources are applied by state institutions.
- Because people are charged for misapplication and embezzlements of state resources, the government can use its resources judiciously for intended purpose.
- Audit reports are made available to public through parliament enabling the citizenry to know for what purposes state resource were used.
- Comments on relevance of programmes executed, prompting the executives to be conscious of their performance to advance the national interest.
- Proper monitoring of states resources enhances transparency, accountability and national growth
- It can minimize crime as public sectors becomes aware of the fact that they should perform their national assignment with a high level of integrity. etc

- The above goes a long way to increase the national wealth and improve the economy.

(Any 10 points @ 1 mark each = 10 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

This question was in two sections (a&b). The a) part, required candidates to discuss the factors the auditor will consider in determining the going concern assumption of a public entity. This had not been very well answered as most candidates produced answers relating to profit making entities.
The b) part of the question required candidates to discuss the merits of Supreme Audit Institution on a state economy. This was very well attempted by most candidates.

QUESTION FIVE

a) Non-audit services that might impair the firms independence
The Sarbanes-Oxley Act 2002 lists nine non-audit services that are considered to impair the firm's independence if they are provided to an audit client by the firm. These are set out below;

- **Book-keeping or other services related to the accounting records or financial statements of the audit client**
  The rules prohibit an accountant from auditing the book-keeping work performed by his or her accounting firm on behalf of a client.
- **Financial information systems design and implementation**
  The rules prohibit a firm from providing any service related to the information systems of the audit client, unless it is reasonable to conclude that the results of these services will not be audited.
  These rules do not prevent a firm from working on the hardware or software system of an audit client, if these are unrelated to the client's financial statements or accounting records and provided that the provision of these services by the firm is approved in advance by the audit committee.
- **Appraisal or valuation services, fairness opinions or contribution-in-kind reports**
  All these activities are essentially services involving a report from an accountancy firm on the valuation used in a transaction.
  The rules prohibit an accounting firm from providing such services, unless the results of these will not be audited as part of the audit of the financial statements.
- **Actuarial services**
  The rules prohibit an accounting firm from providing any actuarial advisory service to an audit client that involves a decision about amounts to be recorded in the financial statements (and related accounts) of the audit client.
  Such a service may apply for example, to the valuation of pension funds (which is connected to the valuation of pension fund liabilities)

An accounting firm may however assist a client in understanding the methods, models, assumption and inputs used in computing an amount.

- **Internal audit outsourcing services**
  the rules prohibit the accounting firm from providing any internal audit service that has been outsourced by the audit client, where the internal audit work relates to the audit client's internal accounting controls, financial systems or financial statements.
  This means that internal audit work relating to operational controls and compliance (operational audits, VFM audits and compliance audits) by the accounting firm are permissible.
- **Management functions or human resources**
  The rules prohibit an accounting firm from:
  - Acting (even in a temporary capacity) as a director, officer or employee of an audit client.
  - Performing any decision making, supervisory or ongoing monitoring function for the audit client
  - The independence of an accounting firm will also be impaired if the firm aids the audit client in connection with any senior level management appointment. An accountant's independence is impaired with respect to an audit client when the accountant:
    - ✓ Seeks out prospective candidates for managerial, executive or director positions within the client company.
    - ✓ Acts as negotiator, on the audit client's behalf , with any person who has applied for a senior management position
    - ✓ Undertakes reference checks of prospective candidates for a senior management position.
    - ✓ Under this rule, an accountant's independence will also be impaired when the accountant:
      - ❖ Engages in psychological testing or other formal testing or evaluation programmes.
      - ❖ Recommends or advises the audit client to hire a specific candidate for a specific job.
- **Broker or dealer, investment adviser or investment banking services**
  Acting as a broker-dealer, promoter or underwriter on behalf of an audit client will make the accountant an advocate for the audit client and will impair his independence.
- **Legal services**
  an accountant firm is prohibited from providing to an audit client any service that could be provided only by someone qualified to practice law in the jurisdiction in which the service is provided.
- **Expert services unrelated to the audit**
  The rules prohibited an accounting firm from providing expert opinions to an audit client, for the purpose of advocating that audit client's interests in litigation or in any regulatory or administrative proceeding or investigation.

(Any 4 points @ 2.5 marks each = 10 marks)

b)

i) Trade payables and accruals

- Calculate the trade payable days for Asogli and compare to prior years, investigate any significant difference, in particular any decrease for this year.
- Compare the total trade payables and list of accruals against prior year and investigate any significant differences.
- Discuss with management the process they have undertaken to quantify the understatement of trade payables due to the cut-off error and consider the materiality of the error.
- Discuss with management whether any correcting journal entry has been included for the understatement.
- Select a sample of purchase invoices received between the period of 25 October and the year end and follow them through to inclusion within accruals or as part of the trade payables journal adjustment.
- Review after date payments; if they relate to the current year, then follow through to the purchase ledger or accrual listing to ensure they are recorded in the correct period.
- Obtain supplier statements and reconcile these to the purchase ledger balances, and investigate any reconciling items.
- Select a sample of payable balances and perform a trade payables' circularisation, follow up any non-replies and any reconciling items between the balance confirmed and the trade payables' balance.
- Select a sample of goods received notes before the year end and after the year end and follow through to inclusion in the correct period's payables balance, to ensure correct cut-off.

(Any 5 points @ 1 mark each = 5marks)

ii) Events occurring up to date of the auditor's report

The auditor has an active duty to design and perform audit procedures to obtain sufficient and appropriate evidence of all events up to date of the auditor's report that require adjustment or disclosure in the financial statements are identified and are suitably reported in the financial statements

These procedures should be performed as close as possible to the date of the auditor's report and in addition representation regarding subsequent events should be sought on the date the report was signed. The auditor should ensure that management have accounted or disclosed subsequent events properly if not the implication on the audit report.

Audit procedures:

- The auditor should also actively look for 'subsequent events', up to the time that he prepares the audit report. Taking into account his risk assessment of this area, he should:
- obtain an understanding of management's procedures for identifying subsequent events
- read the entity's latest subsequent financial statements

- read minutes of shareholders' meetings, meetings of the board of directors and senior management meetings held after the date of the financial statements and for the discussion of the reorganisation.
- obtain written representations regarding the treatment of the reorganisation.
- obtain correspondence from solicitors of the outcome of any pending legal case due to the reorganization.

(5 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

This question was in two sections (a&b). The a) part required candidates to discuss four (4) non- audit services that could lead to conflict of interest or impair the independence of an auditor from a given scenario. This was very well attempted by candidates.

The bi) part required candidates to describe the substantive procedures that would be performed to obtain sufficient and appropriate audit evidence from a given scenario. This was fairly attempted by candidates. The bii) required candidates to state the responsibility of the auditor that would be in line with auditing standards applicable to a reorganisation activity that occurred at a given date after the year end but before the signing of the audit report. This was equally well attempted by candidates.