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CERTIFIED PUBLIC ACCOUNTANT

INTERMEDIATE LEVEL EXAMINATIONS

I1.4: AUDITING

DATE: FRIDAY, 01 APRIL 2022

MARKING GUIDE AND MODEL ANSWERS

SECTION A

QUESTION ONE

Marking guide

(A) Weaknesses discovered, risk associated and recommendations	**Marks**
1. Credit limits	
Weaknesses	
• Credit limits substantially exceeded	1
• New customers in the last twelve months had not been allocated credit limits	1
• Any other valid point	1
Risks	
• when credit limits are exceeded or not established the company's liquidity position is adversely affected	1
• Any other valid point	1
Recommendations	
• Credit limits should be carefully established and enforced	1
• Proper formalities should be followed, and the extension be approved by senior management	1
• Enforcement credit limits reduces the incidence of bad debts	1
• Any other valid point	1
Maximum marks	**3**
2. Purchases invoices	
Weaknesses	
• Invoice from a supplier posted twice to the suppliers' ledger card	1
• Unable trace two other purchase invoices credited to suppliers' accounts	1
• Any other valid point	1
Risks	
• possibility that there a fictitious charge	1
• Risk of paying for services or goods not received not ordered for	1
• Any other valid point	1
Recommendations	
• Raise purchase orders for any purchases	1
• Check the invoices against purchase orders and good received notes	1
• Invoices should be validated before payment and the cheque should be supported by invoices	1

- Claims that cannot be supported by invoices should be rejected for payment 1
- Any other valid point 1

Maximum marks **3**

3. Missing stock items

Weaknesses
- Some computers that were supposed to be in stock were missing 1
- Some computers returned by customers and in stock had not been recorded as retuned 1
- Some of the missing computers had been borrowed by the directors and some other staff for personal use at home 1
- Any other valid point 1

Risks
- Overstatement of sales if the computers were returned and the related invoices had not been reversed 1
- The stocks would be materially misstated because items that should be in stock are actually being used by staff 1
- The stocks of which no record exists could then be misappropriated and sold, thereby the company suffering more loss 1
- Any other valid point 1

Recommendations
- The company have puts in place proper measures to protect the stocks from misuse and other deterioration 1
- The company should maintain full stock records so that the movements of all stock items are closely monitored to guarantee proper use of the company's resources 1
- Any other valid point 1

Maximum marks **3**

4. Leasing agreements

Weaknesses
- Questionable terms of the lease agreements by RRA 1
- Treatment of Hire purchase agreements as lease agreement 1
- Any other valid point 1

Risks
- The risk is that additional assessments may be raised by the Rwanda Revenue Authority and company found non-compliant which can trigger for penalties 1

- Any other valid point 1

Recommendations

- We recommend immediate analysis of the position depending on the two different scenarios, this will be able to assess the exposure 1
- Any other valid point 1

Maximum marks 3

(B) The possible impact of the matters Marks

- More audit efforts to be placed on adequacy of the increase of provision for bad debts or bad debts 1
- Focus on company's overall financial position, particularly insolvency 1
- More audit efforts on creditors to check its misstatement 1
- More efforts on the valuation and existence of stocks 1
- The potential exposure to additional assessments will be of concern to the auditors 1
- Any other valid point 1

Maximum marks 4

(C) limitations facing auditors Marks

- The use of testing 1
- The limitations of internal control (for example, the possibility of management override or collusion) 1
- The fact that most audit evidence is persuasive rather than conclusive 1
- The work is also permeated by judgment 1
- Assessing the reliability of estimates made by management 1
- Any other valid limitation 1

Maximum Marks 4

Total Marks 20

Model answers

a. **Draft letter**

The Directors
Masoro Computer Ltd.
P.O. Box ……….
Kigali, Rwanda

Dear Sirs

Re: Management Letter for the Interim Audit of Masoro Computer Ltd

1. INTRODUCTION

In accordance with our normal practice, we wish to bring to your attention certain matters that have come to our attention during our interim audit assignment. These do not represent an exhaustive list of all weaknesses that may exist in the systems of accounting and internal controls.

Our report is a draft report and we hope that you will review it and append your management comments to enable us to finalise our report.

2. The Issue Identified, Implications and our Recommendations for Improvement

2.1. Failure to set credit limits for new customers and noncompliance with credit limits set on existing customers

- **Weakness**

We noted that the credit limits for four customers had been substantially exceeded and that new customers in the last twelve months had not been allocated credit limits. Enforcing credit limits reduces the incidence of bad debts.

- **Risk**

Conversely when credit limits are exceeded or not established the company's liquidity position is adversely affected.

- **Recommendations**

We recommend that credit limits be carefully established and then once established they should be enforced. When necessary that the limits be revised then proper formalities should be followed and the extension be approved by senior management.

- **Management comment:**

2.2. Purchases made without basis and authorizations

- **Weakness**

We noted a situation where an invoice from a supplier had been posted twice to the suppliers' ledger card. We also were unable trace two other purchase invoices that had been credited to suppliers' accounts.

- **Risks**

These discoveries raise the possibility that there a fictitious charges and invoices being introduced into the system. The company runs the risk of paying for services or goods not received not ordered for.

- **Recommendations**

We recommend that for the acquisition of goods, there must raise a purchase order, when the invoice is received it must be checked against the purchase order and the goods received note before it is entered into the records.

All invoices should be validated before payment and the cheque should be supported by invoices. All claims that cannot be supported by invoices should be rejected for payment.

- **Management comment:**

2.3. Missing stock items

- **Weaknesses**

We attended the half year stock take and the following discrepancies came to our attention

❖ Some microcomputers that were supposed to be in stock were missing and

❖ Some microcomputers returned by customers and in stock had not been recorded as retuned

❖ Some of the missing computers had been borrowed by the directors and some other staff for personal use at home.

- **Risks**

The clear risks that arise include the overstatement of sales if the computers were returned and the related invoices had not been reversed.

Also, the stocks would be materially misstated because items that should be in stock are actually being used by staff.

Furthermore, the stocks or which no record exists could then be misappropriated and sold, thereby the company suffering more loss.

- **Recommendations**

We recommend that the company puts in place proper measures to protect the stocks from misuse and other deterioration.

The company should maintain full stock records so that the movements of all stock items are closely monitored to guarantee proper use of the company's resources.

- **Management comment:**

2.4. Confusing lease and hire purchase agreements

- **Weakness**

The Rwanda Revenue Authority have queried the terms of the lease agreements. In their view these are hire purchase agreements since the customers have the right to purchase the equipment at a future date. We have vetted these agreements in the past and agreed with your treatment. Our position has not changed, and we shall take it up with the Rwanda Revenue Authority.

- **Risk**

The risk is that additional assessments may be raised by the Rwanda Revenue Authority.

- **Recommendation**

We recommend that the chief accountant immediately commence an analysis exercise of the position depending on the two different scenarios. In this way we will be able to assess the exposure.

- **Management Comment:**

- **Conclusion**

These are the weaknesses that came to our attention. There may be other weaknesses that we did not detect. We request that you critically consider these points and append your comment where indicated on the draft.

Having incorporated your comments, we will then release the letter formally.

Should you require any clarification please do not hesitate to contact us.

Yours truly

………………………………

Certified Public Accountants

b. The possible impact these matters may have on the year-end work

i. The concern over credit limits being exceeded or not fully enforced means that audit effort must focus on the adequacy of the provision for bad and doubtful debt at the year-end audit visit as well considering the company's overall financial position, particularly insolvency.

ii. Creditors could be materially overstated having non-genuine liabilities recognized. The existence of creditors will be an area of audit focus at the year-end visit

iii. The valuation and existence of stocks at the year-end will be key areas of audit.

iv. The potential exposure to additional assessments will be of concern to the auditors. If possible, all efforts should be made to resolve the matter before the year end so that any outstanding matters can be considered.

c. The limitations facing auditors

The limitations in an audit of financial statements that affect the auditor ability to detect material misstatements include:

- The use of testing
- The inherent limitations of internal control (for example, the possibility of management override or collusion)
- The fact that most audit evidence is persuasive rather than conclusive
- The work is also permeated by judgment
- Assessing the reliability of estimates made by management

QUESTION TWO

Marking guide

(A) Five main aspects of the client's business and environment **Marks**

- **Industry, regulatory and other external factors, including the applicable financial reporting framework** 1

The candidate should be able to mention some of the following details and why there are critical: the level of competition, the nature of the relationships with suppliers and customers, and the level of technology used in the industry. The specific laws and regulations which impact on the business. Consider wider economic factors such as the level and volatility of interest rates and exchange rates and their potential impact on the client 1

- **Nature of the entity and its accounting policies** 1

The candidate should be able to mention some of the following details and why there are critical: legal structure of the company, the ownership and governance structure, and the main sources of finance used by the company; the accounting policies selected and applied to the financial statements. The auditor must consider whether the accounting policies applied are consistent with the applicable financial reporting framework 1

- **Objectives and strategies and related business risks**

The candidate should be able to mention some of the following details and why there are critical: define the objectives of the business, Strategies are the operational approaches by which management intend to meet the defined objectives 1

- **Measurement and review of the entity's financial performance**

The candidate should be able to mention some of the following details and why there are critical: the performance measures, the company's financial and non-financial key performance indicators, targets, budgets and segmental information 1

- **Internal control**

The candidate should be able to mention some of the following details and why there are critical: control environment, the entity's risk assessment procedures, information systems, control activities, and the monitoring of controls. The design and implementation of controls should be considered as part of gaining an understanding. The auditor should also understand whether controls are manual or automated 1

- Any other valid point and its explanations 2

Maximum marks **10**

(B) Procedures used to gain understanding **Marks**

- **Inquiries of management and others within the company** 0.5

Candidate explanations should focus on the following points: discussion with management, meeting, other forms of inquiries 0.5

- **Analytical procedures** 0.5

Candidate explanations should focus on the following points: analytical procedures at the planning stage, in order to identify unusual transactions or events, and to understand the main trends reflected in the financial statements for the year, *Analytical procedures* as per ISA 520 0.5

- **Observation**

Candidate explanations should focus on the following points: physical observation of the internal control operations, and visits to premises such as factories, warehouses and head office, etc 0.5

- **Inspection**

Candidate explanations should focus on the following points: an inspection of business plans, internal control manuals, reports made by management such as interim financial statements, the minutes of board meetings, and reviewing the company's website and brochures 0.5

- **Any other valid point with its explanation** 1

Maximum marks **4**

(C) **Difference among inherent, control and detection risks** **Marks**

- **Inherent risk** is 'the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls 1
- Candidate should provide a valid example of inherent risk 1
- **Control risk is** 'the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control 1
- Candidate should provide a valid example of control risk 1
- **Detection risk** is defined as 'the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements 1
- Candidate should provide a valid example of control risk 1

- Any other valid differentiating point 1

Maximum Marks 6

Total Marks 20

Model Answers

a. ISA 315 states that there are five main aspects of the client's business and environment which the auditor should understand.

1. Industry, regulatory and other external factors, including the applicable financial reporting framework

This means having an understanding of the industry in which the company operates, including the level of competition, the nature of the relationships with suppliers and customers, and the level of technology used in the industry. The industry may have specific laws and regulations which impact on the business. The auditor should also consider wider economic factors such as the level and volatility of interest rates and exchange rates and their potential impact on the client.

The importance of these issues is their potential impact on the financial statements and on the planning of the audit. For example, if a client operates in a highly regulated industry, it may be worth considering the inclusion in the audit team of a person with specific experience or knowledge of those regulations. Regulations include the financial reporting framework, for example, whether the company uses local or international financial reporting standards.

2. Nature of the entity and its accounting policies

This includes having an understanding of the legal structure of the company (and group where relevant), the ownership and governance structure, and the main sources of finance used by the company. Complex ownership structures with multiple subsidiaries and/or locations may increase the risk of material misstatement. Understanding the nature of the company also includes an understanding of the accounting policies selected and applied to the financial statements. The auditor must consider whether the accounting policies applied are consistent with the applicable financial reporting framework.

3. Objectives and strategies and related business risks

The management of the company should define the objectives of the business, which are the overall plans for the company. Strategies are the operational approaches by which management intend to meet the defined objectives.

For example, an objective could be to maximise market share, and the strategy to achieve this could be to launch a new brand or product every year. Business risks are factors which could stop the company achieving its stated objectives, for example, launching a product for which there is limited demand. Most business risks will eventually have financial consequences, and thus an effect on the financial statements. This is why auditors perform a business risk assessment as part of their planning procedures.

4. Measurement and review of the entity's financial performance

Here the auditor is looking to gain an understanding of the performance measures which management and others consider to be of importance. Performance measures can create pressure on management to take action to improve the financial statements through deliberate misstatement. For example, a bonus payable to the management based on revenue growth could create pressure for revenue to be overstated. Thus, the auditor must gain an understanding of the company's financial and non-financial key performance indicators, targets, budgets and segmental information.

5. Internal control

The auditor must gain knowledge of internal control in order to consider how different aspects of internal control could impact on the audit. Internal control includes the control environment, the entity's risk assessment procedures, information systems, control activities, and the monitoring of controls. Put simply, the evaluation of the strength or weakness of internal control is a crucial consideration in the assessment of audit risk, and so will have a significant impact on the audit strategy. The design and implementation of controls should be considered as part of gaining an understanding. The auditor should also understand whether controls are manual or automated. ISA 315 contains a great deal of detailed guidance on the understanding of controls, which these briefing notes do not cover.

b. Procedures used to gain understanding

1. Inquiries of management and others within the company

A discussion with management is often the starting point in gaining understanding. A meeting is usually held with management to talk about all of the aspects of the company and its environment referred to in the first part of the briefing notes. However, inquiries can also be made of others, who may be able to provide a different perspective or provide specific insights into certain matters. For example, internal auditors would be able to comment specifically, on internal controls.

2. Analytical procedures

Auditors perform analytical procedures at the planning stage in order to identify unusual transactions or events, and to understand the main trends reflected in the financial statements for the year. This will enable the auditor, for example, to see if the company has experienced a growth or decline in turnover or profits in the year, which when reviewed in the context of industry or economic trends, may indicate a risk of material misstatement.

Analytical procedures should be performed in accordance with ISA 520 *Analytical procedures*.

3. Observation

Observation may help to support inquiries of management and others, and could involve, for example, physical observation of the internal control operations, and visits to premises such as factories, warehouses and head office.

4. Inspection

Inspection may support inquiries made of management and others. It could include, for example, an inspection of business plans, internal control manuals, reports made by management such as interim financial statements, the minutes of board meetings, and reviewing the company's website and brochures.

Conclusion

Auditors must make sure that they have gained and documented an understanding of five main aspects of the client's business and the environment in which it operates, and a variety of procedures can be used. Without a thorough knowledge of the business and its environment, an auditor would be unable to effectively assess the risk of material misstatement in the financial statements, and therefore could not plan the audit to minimise audit risk.

c. Difference among inherent, control and detection risks

Inherent risk is 'the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls

Inherent risk is generally considered to be higher where a high degree of judgment and estimation is involved or where transactions of the entity are highly complex.

For example, the inherent risk in the audit of a newly formed financial institution which has a significant trade and exposure in complex derivative instruments may be considered to be significantly higher as compared to the audit of a well-established manufacturing concern operating in a relatively stable competitive environment.

Control risk is 'the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.'

Organizations must have adequate internal controls in place to prevent and detect instances of fraud and error. Control risk is considered to be high where the audit entity does not have adequate internal controls to prevent and detect instances of fraud and error in the financial statements. Assessment of control risk may be higher for example in case of a small sized entity in which segregation of duties is not well defined and the financial statements are prepared by individuals who do not have the necessary technical knowledge of accounting and finance.

Detection risk is defined as 'the risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.'

QUESTION THREE

Marking guide

(A) Responsibilities with respect to financial statements	**Marks**
• ISA 200 explains the respective responsibilities.	
• The responsibility for the preparation and presentation of the financial statements in accordance with the applicable financial reporting framework is that of the management of the entity with oversight from those charged with governance	1
• The auditor is responsible for forming and expressing an opinion on the financial statements	1
• The audit of financial statements does not relieve management or those charged with governance their responsibility	1
• Any other valid point	1
Maximum marks	**2**

(B) Limitation of audit evidence	**Marks**
• Absolute proof is not possible	1
• Some assertions are not material	1
• Time and cost	1
• Sensitivity	1
• Inconsistent different source	1
• Any other valid limitation	1
Maximum marks	**3**

(C) Factors that may lessen sampling risk	**Marks**
• Taking larger size samples	1
• Using random sample selection methods	1
• Stratifying the sample	1
• Properly defining the test objective	1
• Properly defining a deviation	1
• Exclusion of non-recurring, non-systematic errors	1
• Properly evaluating errors	1
• **Any other valid point**	1
Maximum marks	**4**

(D) Forms of audit evidence	**Marks**
• Inspection of tangible assets	1
• Inspection of documents and records	1
• Observation	1
• Inquiry and confirmation	1
• Recalculation and Re-Performance	1

- Audit automation tools 1
- Analytical procedures 1
- Testimony from independent third parties 1
- Review of authoritative documents 1
- Testimony from management and employees 1
- Satisfactory internal control 1
- Calculations performed by the auditor 1
- Review of post balance sheet events 1
- Relationship evidence 1
- Agreement with expectation 1
- External events 1
- Any other valid point 1

Maximum Marks 8

(E) Advise on RMM Marks

- Assess the accounting information system as to its adequacy in producing a set of accounts for the entity 1
- Seek to identify any potential misstatements that could occur 1
- Consider all factors that might affect the risk of misstatements 1
- Design appropriate audit procedures whose nature, timing and extent are responsive to the risks 1
- Any other valid point 1

Maximum Marks 3

Total Marks 20

Model Answers

a. Respective responsibilities of directors and management of a company and its external auditors with respect to financial statements.

ISA 200, explains the respective responsibilities.

The responsibility for the preparation and presentation of the financial statements in accordance with the applicable financial reporting framework is that of the management of the entity with oversight from those charged with governance.

The auditor is responsible for forming and expressing an opinion on the financial statements.

The audit of financial statements does not relieve management or those charged with governance their responsibility.

b. Limitation of audit evidences

The quality and quantity of evidence is constrained by the following factors:

- Absolute proof is not possible;
- Some assertions are not material;
- Time and cost must be considered as accounts must be produced within certain time scales and the auditor may have to do with less than perfection, and ideal evidence may be too expensive to obtain.
- Sensitivity: some items are of greater importance than others or are capable of greater variations.
- To summarise: the auditor's degree of assurance is greater when evidence obtained from different sources is consistent with each other. However, when evidence from one source is inconsistent with that obtained from another then further procedures may have to be performed to resolve the inconsistency.

c. Factors that may lessen sampling risk include:

- Taking larger size samples
- Using random sample selection methods
- Stratifying the sample
- Properly defining the test objective
- Properly defining a deviation
- Exclusion of non-recurring, non-systematic errors.
- Properly evaluating errors.

d. Forms of audit evidences

- Inspection of tangible assets: Inspection confirms existence and valuation and gives evidence of completion. It does not however confirm rights and obligations.
- Inspection of documents and records: Confirmation of documentation confirms existence of an asset or that a transaction has occurred. Confirmation that items are in the books shows completeness. Also helps testing cut-off. It provides evidence of valuation, measurement, rights and obligations and presentation and disclosure.
- Observation: This procedure is of limited use in that it only confirms that a procedure took place when it was observed.
- Inquiry and confirmation: Information sought from client or external sources. The strength of the evidence depends on knowledge and integrity of the source of the information.
- Recalculation and Re-Performance: Checking calculations of client records.
- Audit automation tools: Such as computer assisted auditing techniques.
- Analytical procedures
- Testimony from independent third parties.
- Review of authoritative documents:

- Testimony from management and employees:
- Satisfactory internal control:
- Calculations performed by the auditor:
- Review of post balance sheet events
- Relationship evidence:
- Agreement with expectation:
- External events

e. Advise on RMM

The auditor is required to assess the risk of material misstatements. Misstatements can arise through inherent risks and control risks. So the auditor is concerned with assessing policies and procedures of the entity which are relevant to the financial statements. The auditor should:

- Assess the accounting information system as to its adequacy in producing a set of accounts for the entity,
- Seek to identify any potential misstatements that could occur,
- Consider all factors that might affect the risk of misstatements,
- Design appropriate audit procedures whose nature, timing and extent are responsive to the risks.

SECTION B

QUESTION FOUR
Marking guide

(A) Internal controls over sales	**Marks**
Ordering and credit approval	
• Segregation of duties	0.5
• Authorization of credit terms and other data	0.5
• Review of credit terms Document	0.5
• numbering and examination of correct pricing	0.5
• Matching of orders with dispatches	0.5
• Dealing with customer queries	0.5
Dispatch and invoicing	
• Authorization of sales	0.5
• Examination of dispatches - quantity & condition	0.5
• Matching of dispatches to orders and invoices and review of unmatched items	0.5
• Checking number sequence on documents	0.5
• Checking conditions of returns	0.5
• Signatures on delivery notes	0.5
• Checking pricing, quantity and details on invoices	0.5
• Checking update of stock records	0.5
Transaction's processing and credit control	
• Segregation of duties	0.5
• Review sequence of invoices	0.5
• Match receipts to invoices	0.5
• Review customer remittance advices	0.5
• Cut-off procedures	0.5
• Regular customer statements sent out	0.5
• Review of customer statements	0.5
• Authorization of any adjustments to accounts	0.5
• Reconcile sales	0.5
• ledger to debtors control account	0.5
• Review of margins	0.5
Maximum marks	**4**

(B) Stock	**Marks**
Ordering	
• Segregation of duties	0.5
• Custody and recording of stocks received	0.5
• Checking and recording of goods inwards	0.5
• Precautions against theft	0.5
Misuse and deterioration	
• Restriction of access to stores	0.5
• Controls on stores environment (temperature, precautions against damp)	0.5
• Control of stock levels	0.5
• Maximum stock limits	0.5
• Minimum stock limits	0.5
• Maintenance of stock records	0.5
• Stock ledgers	0.5
• Bin cards	0.5
• Transfer records	0.5
• Arrangements for dealing with returnable containers	0.5
• Security over stock held by third parties, and third party stock held by entity	0.5
Stocktaking	
• Regular stocktaking	0.5
• Fair coverage	0.5
• Counts by independent persons	0.5
Recording	
• Cut-off for goods in transit and time differences	0.5
• Reconciliation of stock counts to book records and control accounts	0.5
• Computation of stock valuation according with IAS 2	0.5
• Checking of calculations	0.5
Review of condition of stock	
• Treatment of slow-moving, damaged and obsolete stock	0.5
• Authorization of write-offs	0.5
• Accounting for scrap and wastes	0.5
Maximum marks	**4**

(C) Controls over purchases	Marks
Ordering	
• Segregation of duties	0.5
• Evidence of re-order quantities and levels	0.5
• Orders prepared from pre-numbered requisitions	0.5
• Orders authorized	0.5
• Pre-numbered order books and safe custody of such books	0.5
• Review orders not received	0.5
• Regular monitoring of supplier terms and conditions	0.5
Receipts and invoices	
• Examine goods received	0.5
• Checking quality and quantity	0.5
• Record receipt in goods inwards records	0.5
• Match receipts with order details	0.5
• Appropriate referencing of invoices	0.5
• Examine invoice and check price, quantity and calculations	0.5
• Match to receipts and order documents	0.5
• Record all goods returned and ensure credit is claimed	0.5
Accounting	
• Segregation of duties	0.5
• Record all purchases and returns in daybooks and appropriate ledgers	0.5
• Review purchase ledger and reconcile accounts to supplier statements	0.5
• Payments should be authorised only after all checking procedures	0.5
• Reconcile creditors control account to a list of purchase ledger accounts	0.5
• Cut-off is appropriate	0.5
Maximum marks	**4**

(D) Controls over payrolls	Marks
Setting of wages and salaries	
• Pay per unit produced (if applicable)	0.5
• Segregation of duties in payrolls	0.5
• Personnel records should be maintained with proper employment letters etc	0.5
• Authorization of rates of pay, deductions	0.5
• Maintain details of holiday entitlement, advance of pay etc	0.5

Recording

• Records maintained of timesheets, clock cards, units produced etc.	0.5
• Review of hours worked	0.5
• Review of wages cost against budgets	0.5
• Review by senior staff of data input and calculation work by other staff including checking procedures	0.5
• Appropriate analysis codes	0.5
• Maintenance and reconciliation of wages bank account	0.5

Payment

• Match units produced vs pay rate	0.5
• Custody of cash procedures	0.5
• Segregation of duties	0.5
• Verification of identity	0.5
• Preparation of pay packets, cash, cheque, payslip etc	0.5
• Records of amounts distributed	0.5
• Authorization of cheques and bank transfers	0.5

Deductions

• Maintenance of separate records for each employee	0.5
• Review deductions as between differing periods	0.5
• Review control accounts for deductions	0.5
Maximum marks	**4**

(E) Controls over cash	**Marks**
• Restrictions on opening new bank accounts	0.5
• Limitations on cash floats held	0.5
• Restrictions on payments out of cash received	0.5
• Restrictions on access to cash registers and offices'	0.5
• Independent checks on cash floats	0.5
• Surprise cash counts	0.5
• Custody of cash outside office hours	0.5
• Safeguarding of IOUs, cash in transit	0.5
• Insurance arrangements	0.5
• Control of funds held in trust for employees	0.5
• Bank reconciliation's	0.5
• Comparison with cashbooks	0.5
Maximum marks	**4**

Total Marks **20**

Model answers

a. Internal controls over sales

Ordering and credit approval

- Segregation of duties
- Authorization of credit terms and other data
- Review of credit terms
- Document numbering Examination of correct pricing
- Matching of orders with dispatches
- Dealing with customer queries

Dispatch and invoicing

- Authorization of dispatches
- Examination of dispatches - quantity & condition
- Matching of dispatches to orders and invoices and review of unmatched items
- Checking number sequence on documents
- Checking conditions of returns
- Signatures on delivery notes
- Checking pricing, quantity and details on invoices
- Checking update of stock records

Transaction's processing and credit control

- Segregation of duties
- Review sequence of invoices
- Match receipts to invoices
- Review customer remittance advices
- Cut-off procedures
- Regular customer statements sent out
- Review of customer statements
- Authorization of any adjustments to accounts
- Reconcile sales
- ledger to debtors control account
- Review of margins
-

b. Stock

- Segregation of duties;
- Custody and recording of stocks received

- Checking and recording of goods inwards

Precautions against theft

- Misuse and deterioration
- Restriction of access to stores
- Controls on stores environment (temperature, precautions against damp)
- Control of stock levels
- Maximum stock limits
- Minimum stock limits

Maintenance of stock records

- Stock ledgers
- Bin cards
- Transfer records
- Arrangements for dealing with returnable containers
- Security over stock held by third parties, and third party stock held by entity.

Stocktaking

- Regular stocktaking
- Fair coverage
- Counts by independent persons

Recording

- Cut-off for goods in transit and time differences
- Reconciliation of stock counts to book records and control accounts
- Computation of stock valuation according with IAS 2
- Checking of calculations
- Review of condition of stock
- Treatment of slow-moving, damaged and obsolete stock
- Authorization of write-offs
- Accounting for scrap and waste
- Control considerations: cash at bank and in hand-receipt

c. Controls over purchases

Ordering

- Segregation of duties
- Evidence of re-order quantities and levels
- Orders prepared from pre-numbered requisitions
- Orders authorized
- Pre-numbered order books and safe custody of such books
- Review orders not received
- Regular monitoring of supplier terms and conditions

Receipts and invoices

- Examine goods received.
- Checking quality and quantity
- Record receipt in goods inwards records
- Match receipts with order details
- Appropriate referencing of invoices
- Examine invoice and check price, quantity and calculations.
- Match to receipts and order documents
- Record all goods returned and ensure credit is claimed

Accounting

- Segregation of duties
- Record all purchases and returns in daybooks and appropriate ledgers
- Review purchase ledger and reconcile accounts to supplier statements
- Payments should be authorized only after all checking procedures complete
- Reconcile creditors control account to a list of purchase ledger accounts
- Cut-off is appropriate

d. Controls over payrolls

Setting of wages and salaries

- Pay per unit produced (if applicable)
- Segregation of duties
- Personnel records should be maintained with proper employment letters etc.
- Authorization of rates of pay, deductions
- Maintain details of holiday entitlement, advance of pay etc.
- Procedures for dealing with queries

Recording

- Records maintained of timesheets, clock cards, units produced etc.
- Review of hours worked
- Review of wages cost against budgets
- Review by senior staff of data input and calculation work by other staff
- including checking procedures
- Appropriate analysis codes
- Maintenance and reconciliation of wages bank account

Payment

- Match units produced vs pay rate
- Custody of cash procedures
- Segregation of duties
- Verification of identity
- Preparation of pay packets, cash, cheque, payslip etc.
- Records of amounts distributed
- Authorization of cheques and bank transfers
- Dealing with queries

Deductions

- Maintenance of separate records for each employee
- Review deductions as between differing periods
- Review control accounts for deductions
-

e. Controls over cash

- Restrictions on opening new bank accounts
- Limitations on cash floats held
- Restrictions on payments out of cash received
- Restrictions on access to cash registers and offices’
- Independent checks on cash floats
- Surprise cash counts
- Custody of cash outside office hours
- Safeguarding of IOUs, cash in transit
- Insurance arrangements
- Control of funds held in trust for employees
- Bank reconciliations.
- Comparison with cashbooks.

QUESTION FIVE

Marking guide

a. Tangible fixed assets

Completeness

- Obtain a summary of the assets showing the gross book value, the accumulated depreciation and the net book value and reconcile this with the opening position 0.5
- Reconcile the summary with the nominal ledger and the asset register and follow up on any discrepancies 0.5
- Physically inspect whether items on the summary actually exist 0.5

Existence

- Confirm that entity physically inspects all assets each year 0.5
- Inspect a sample of items on asset register paying attention to high value, portable and any material additions during the year and check that they are in use and in good order 0.5

Valuation

- Verify valuation of buildings to a valuation certificate, having regard to the experience of the valuer, his scope of work, the methods and assumptions he uses and whether the valuation bases are in line with accounting standards 0.5
- Check whether any surplus/deficit has been calculated correctly and is recognised in the profit and loss account or statement of total recognised gains and losses whichever is appropriate **0.5**
- Check whether regular valuations are being carried out 0.5
- For other asset types examine the purchase invoice or other supporting documentation 0.5
- Review depreciation rates and policies and assess their appropriateness having regard to the entity itself, asset lives, residual value, replacement policy, past history profits/losses on disposal and possible obsolescence 0.5
- Check that depreciation is charged on all assets in use and that none is charged on fully depreciated or disposed assets 0.5
- Check the calculation of a sample of depreciation charges 0.5
- Analytical review procedures such as comparing depreciation to previous years 0.5
- Review accounts for policy and rates disclosures 0.5
- Review the current insurance policies in place and consider the adequacy of the insured amounts 0.5

Rights

- Inspect title deeds, leases and land registry certificates 0.5
- Confirm through lawyers that deeds are free from charge 0.5

- Examine documents of title for other assets including invoices, lease agreements, contracts or architect certificates 0.5
- Review statutory books and leases and agreements to ensure all charges and commitments are noted 0.5
- Examine post year end transactions and minutes of management meetings for any evidence of capital commitments 0.5

Additional testing is carried out on additions, disposals and where an entity constructs its own assets

Additions- rights and obligations, valuation, completeness

- Inspect architects' certificates and suppliers' invoices 0.5
- Check whether the capitalising of the asset is correct and whether there is consistency with previous years 0.5
- Check whether amounts are posted to correct accounts in nominal ledger 0.5
- Check whether the additions have been authorized 0.5
- Where assistance or grants are available, check that such are claimed and have been received and correctly accounted for 0.5
- Check additions are recorded on the asset register 0.5

Disposals- rights and obligations, completeness, occurrence and measurement

- Verify disposals with supporting documentation, checking transfer of title, sales price and dates of completion and payment 0.5
- Check calculation of profit and loss and has it been recorded properly 0.5
- Check that disposals are authorized 0.5
- If the asset is used as security, ensure that a release has been correctly made **0.5**

In-house construction of assets-valuation and completeness

- Verify material and labour costs to suppliers' invoices and payroll records **0.5**
- Ensure expenditure is capital. It should enhance the economic benefits, replace or restore a component or relate to a major inspection or overhaul **0.5**
- Check whether finance costs are capitalized **0.5**

Maximum marks 4

b. Procedures for Receivables and prepayments Marks

- Check the balances from the list and match to the sales ledger **0.5**
- Check balances within the sales ledger and match to the list **0.5**
- Reconcile the total of the list to the total of the sales ledger balances and the debtors control account in the nominal ledger **0.5**

- ISA 501 additional considerations and ISA 505 external confirmations refer to the confirmation of accounts receivable **0.5**
- Review post year-end receipts **0.5**
- Verify that valid sales orders exist and goods were dispatched **0.5**
- Examine invoices specifically making up the account balance **0.5**
- Enquire from management as to why debt remains unpaid **0.5**
- Compare prepaid with previous years using analytical procedures **0.5**
- Verify prepaid to payments book and supporting documentation **0.5**
- Check calculation for reasonableness **0.5**
- Review nominal ledger accounts for journal adjustments for prepaid **0.5**

Maximum marks **4**

c. Cash balances **Marks**

- Obtain standard bank confirmations from all relevant banks **0.5**
- Agree each balance to the accounting records and note all other relevant comments for disclosure in accounting notes **0.5**
- Obtain bank reconciliations for each bank account operated **0.5**
- Check the arithmetic calculations of these reconciliations **0.5**
- Trace outstanding cheques to the payments book prior to the year-end and to the post year-end bank statements **0.5**
- Enquire as to any large or unusual items not cleared at the time of the audit **0.5**
- Compare cash books and bank statements in detail for the final month and check that un-reconciled items are appearing on the bank reconciliation **0.5**
- Review the reconciliations for older items and enquire as to their validity **0.5**
- Trace outstanding lodgements back to cash book before year-end and bank statement post year-end **0.5**
- Review bank paying-in slips **0.5**
- Match balances per the cashbooks to the ledger and the reconciliations **0.5**
- Scrutinise the cashbooks and the bank statements for any large or unusual items and follow up on same **0.5**
- Count all cash balances and agree to petty cash book or other record kept **0.5**
- Count all cash at same time and ensure all work is done in presence of staff **0.5**
- Obtain a certificate of cash in hand from staff member **0.5**
- Enquire about IOUs or cheques cashed **0.5**
- Confirm balances are in agreement with the accounts **0.5**
- Verify that IOUs and un-cashed cheques have subsequently been dealt within a reasonable period of time **0.5**

Maximum marks **4**

d. Accounts payables and provisions for liabilities **Marks**

- Check the balances from the list and match to the purchases ledger **0.5**
- Check balances within the purchases ledger and match to the list **0.5**
- Reconcile the total of the list to the total of the purchases ledger balances and the creditors control account in the nominal ledger **0.5**
- Check all arithmetical calculations **0.5**
- Obtain a sample of suppliers' statements, reconcile and trace back each of the reconciling items to source documentation **0.5**
- Agree the ledger balance and the statement balance to the reconciliation **0.5**
- Ensure that all trade accruals are correctly accounted for **0.5**
- Follow up on un-cleared year-end items at the time of the audit **0.5**

Cut-off testing-evidence for completeness

- Obtain details of last good received note in and last goods returns note out **0.5**
- Select a sequence of movement notes before and after the cut-off point and match to invoices and credit notes in the correct accounting period or a list of trade accruals where necessary **0.5**
- Select a number of invoices, credit notes and items per the list of trade accruals and match back to the appropriate goods received notes and goods returns notes **0.5**
- Follow up and assess any exceptions **0.5**
- Review outstanding purchase orders for any evidence of any purchases completed but not invoiced **0.5**
- Review the creditors control account for any unusual transactions around the year- end **0.5**
- Obtain details of all provisions that have been included in the accounts and all contingencies that have been disclosed **0.5**
- Obtain a detailed analysis of all provisions showing the yearly movements **0.5**
- Determine for each material provision whether the company has a present obligation as a result of past events by review of correspondence and discussion with directors **0.5**
- Determine for each material provision whether it is probable that a transfer of benefits will be required to settle the obligation by checking whether any payments have been made in the post balance sheet period in respect of the item and review of correspondence with lawyers, banks, customers insurance company and suppliers **0.5**
- Recalculate all provisions made and assess their reasonableness **0.5**
- Compare the amount provided with post year-end payments and with any amount paid in the past for similar items **0.5**
- In the event that it is not possible to estimate the amount of the provision, check that there is disclosure in the accounts **0.5**

- Consider the nature of the client's business for example would you expect to see any other provisions such as warranties **0.5**
- Consider the adequacy of disclosure of provisions and contingencies **0.5**

Maximum marks **4**

e. Share capital and issues of shares **Marks**

- Agree the authorized share capital with the statutory documents **0.5**
- Agree any changes to properly authorized resolutions **0.5**
- Verify with board minutes and resolutions and general meeting **0.5**
- Ensure issue or change of shares is in line with company's constitution and that the directors have the authority to issue such shares **0.5**
- Confirm that cash or other consideration has been received in respect of the shares **0.5**
- Verify by reference to complete stamped transfer forms, cancelled share certificates, correspondence and minutes of directors' meetings **0.5**
- Agree balances on shareholders' accounts in the register of members to the issued share capital figure in the nominal ledger **0.5**

Maximum marks **4**

Total Marks **20**

Model Answers

a. Tangible fixed assets

Completeness

- Obtain a summary of the assets showing the gross book value, the accumulated depreciation and the net book value and reconcile this with the opening position.
- Reconcile the summary with the nominal ledger and the asset register and follow up on any discrepancies.
- Physically inspect whether items on the summary actually exist.

Existence

- Confirm that entity physically inspects all assets each year.
- Inspect a sample of items on asset register paying attention to high value, portable and any material additions during the year and check that they are in use and in good order.

Valuation

- Verify valuation of buildings to a valuation certificate, having regard to the experience of the valuer, his scope of work, the methods and assumptions he uses and whether the valuation bases are in line with accounting standards.
- Check whether any surplus/deficit has been calculated correctly and is recognized in the profit and loss account or statement of total recognized gains and losses whichever is appropriate.
- Check whether regular valuations are being carried out.
- For other asset types examine the purchase invoice or other supporting
- documentation.
- Review depreciation rates and policies and assess their appropriateness having regard to the entity itself, asset lives, residual value, replacement policy, past history profits/losses on disposal and possible obsolescence.
- Check that depreciation is charged on all assets in use and that none is charged on fully depreciated or disposed assets.
- Check the calculation of a sample of depreciation charges.
- Carry out analytical review procedures such as comparing depreciation to previous years.
- Review accounts for policy and rates disclosures.
- Review the current insurance policies in place and consider the adequacy of the insured amounts.

Rights

- Inspect title deeds, leases and land registry certificates.
- Confirm through lawyers that deeds are free from charge
- Examine documents of title for other assets including invoices, lease agreements, contracts or architect certificates.
- Review statutory books and leases and agreements to ensure all charges and commitments are noted.
- Examine post year end transactions and minutes of management meetings for any evidence of capital commitments.

Additional testing is carried out on additions, disposals and where an entity constructs its own assets.

Additions- rights and obligations, valuation, completeness

- Inspect architects' certificates and suppliers' invoices.
- Check whether the capitalizing of the asset is correct and whether there is consistency with previous years.
- Check whether amounts are posted to correct accounts in nominal ledger.
- Check whether the additions have been authorized.
- Where assistance or grants are available, check that such are claimed and have been received and correctly accounted for.

- Check additions are recorded on the asset register.

Disposals- rights and obligations, completeness, occurrence and measurement

- Verify disposals with supporting documentation, checking transfer of title, sales price and dates of completion and payment.
- Check calculation of profit and loss and has it been recorded properly.
- Check that disposals are authorized.
- If the asset is used as security, ensure that a release has been correctly made.

In-house construction of assets-valuation and completeness

- Verify material and labor costs to suppliers' invoices and payroll records.
- Ensure expenditure is capital. It should enhance the economic benefits, replace or restore a component or relate to a major inspection or overhaul.
- Check whether finance costs are capitalized.

b. Procedures for Receivables and prepayments

- Check the balances from the list and match to the sales ledger.
- Check balances within the sales ledger and match to the list.
- Reconcile the total of the list to the total of the sales ledger balances and the debtors control account in the nominal ledger.
- ISA 501 additional considerations and ISA 505 external confirmations refer to the confirmation of accounts receivable. Verification from external sources is strong evidence for existence of rights and obligations
- Review post year-end receipts.
- Verify that valid sales orders exist and goods were dispatched.
- Examine invoices specifically making up the account balance.
- Enquire from management as to why debt remains unpaid.
- Compare prepaids with previous years using analytical procedures.
- Verify prepaids to payments book and supporting documentation.
- Check calculation for reasonableness.
- Review nominal ledger accounts for journal adjustments for prepaids.

c. Cash balances

- Obtain standard bank confirmations from all relevant banks.
- Agree each balance to the accounting records and note all other relevant comments for disclosure in accounting notes.
- Obtain bank reconciliations for each bank account operated.
- Check the arithmetic calculations of these reconciliations.

- Trace outstanding cheques to the payments book prior to the year-end and to the post year-end bank statements.
- Enquire as to any large or unusual items not cleared at the time of the audit.
- Compare cash books and bank statements in detail for the final month and check that un-reconciled items are appearing on the bank reconciliation.
- Review the reconciliations for older items and enquire as to their validity.
- Trace outstanding lodgments back to cash book before year-end and bank statement post year-end.
- Review bank paying-in slips.
- Match balances per the cashbooks to the ledger and the reconciliations.
- Scrutinize the cashbooks and the bank statements for any large or unusual items and follow up on same.
- Count all cash balances and agree to petty cash book or other record kept.
- Count all cash at same time and ensure all work is done in presence of staff.
- Obtain a certificate of cash in hand from staff member.
- Enquire about IOUs or cheques cashed.
- Confirm balances are in agreement with the accounts.
- Verify that IOUs and un-cashed cheques have subsequently been dealt within a reasonable period of time.

d. Accounts payables and provisions for liabilities

- Check the balances from the list and match to the purchase's ledger.
- Check balances within the purchase's ledger and match to the list.
- Reconcile the total of the list to the total of the purchase's ledger balances and the creditors control account in the nominal ledger.
- Check all arithmetical calculations.
- Obtain a sample of suppliers' statements, reconcile and trace back each of the reconciling items to source documentation.
- Agree the ledger balance and the statement balance to the reconciliation.
- Ensure that all trade accruals are correctly accounted for.
- Follow up on un-cleared year-end items at the time of the audit.

Cut-off testing-evidence for completeness

- Obtain details of last good received note in and last goods returns note out.
- Select a sequence of movement notes before and after the cut-off point and match to invoices and credit notes in the correct accounting period or a list of trade accruals where necessary.
- Select a number of invoices, credit notes and items per the list of trade accruals and match back to the appropriate goods received notes and goods returns notes.

- Follow up and assess any exceptions.
- Review outstanding purchase orders for any evidence of any purchases completed but not invoiced.
- Review the creditors control account for any unusual transactions around the year- end.
- Obtain details of all provisions that have been included in the accounts and all contingencies that have been disclosed.
- Obtain a detailed analysis of all provisions showing the yearly movements.
- Determine for each material provision whether the company has a present obligation as a result of past events by review of correspondence and discussion with directors
- Determine for each material provision whether it is probable that a transfer of benefits will be required to settle the obligation by checking whether any payments have been made in the post balance sheet period in respect of the item and review of correspondence with lawyers, banks, customers insurance company and suppliers.
- Recalculate all provisions made and assess their reasonableness.
- Compare the amount provided with post year-end payments and with any amount paid in the past for similar items.
- In the event that it is not possible to estimate the amount of the provision, check that there is disclosure in the accounts.
- Consider the nature of the client's business for example would you expect to see any other provisions such as warranties.
- Consider the adequacy of disclosure of provisions and contingencies.
-

e. Share capital and issues of shares

- Agree the authorized share capital with the statutory documents.
- Agree any changes to properly authorized resolutions
- Verify with board minutes and resolutions and general meeting.
- Ensure issue or change of shares is in line with company's constitution and that the directors have the authority to issue such shares.
- Confirm that cash or other consideration has been received in respect of the issue of shares.
- Verify by reference to complete stamped transfer forms, cancelled share certificates, correspondence and minutes of directors' meetings.
- Agree balances on shareholders' accounts in the register of members to the issued share capital figure in the nominal ledger.

QUESTION SIX

Marking guide

a. Objective of independent external auditor **Marks**

The objective of an external audit of financial statements is to determine whether, in the auditor's opinion, the statements present fairly in all material respects - that is, they show a true and fair view in all material respects of the company's financial position, results of operations, and cash flows, in conformity with national or international generally accepted accounting principles (GAAP) **2**

Maximum marks for the question (c) **2**

b. Responsibility in relation to the information published on company website **Marks**

The auditors are not required to read information contained in electronic sites, such as the company's Web site, that also contain the company's audited financial statements and the auditor's report. Auditing standards do not consider electronic sites to be documents that can be based on forming an opinion **2**

Maximum marks for the question (c) **2**

c. Responsibility for the information published in FSs and Audit report **Marks**

This is different from the auditor's responsibility for published (hard copy) documents that contain information in addition to audited financial statements and the auditor's report. In this example, the auditor is responsible for reading other information that is published with audited financial statements and the auditor's report to determine whether it is materially inconsistent with information in the audited financial statements

Maximum marks for the question (c) **4**

d. Basic elements of the auditor's report **Marks**

1. Title **0.5**

It should clearly indicate that the report is prepared by an independent auditor. This independence confirms that all the relevant ethical standards have been met **0.5**

2. Addressee **0.5**

The auditor needs to consider the circumstances of the engagement and local regulations. Under company law the audit report should be addressed to the shareholders **0.5**

3. Opinion paragraph **0.5**

This paragraph will:

- Identify the entity been audited
- State that the financial statements have been audited
- Identify each of the financial statements being audited
- d. Refer to the significant accounting policies and other notes contained within the

- financial statements
- Specify the date and period covered by the financial statements.

If the auditor expresses an unmodified opinion on financial statements prepared in accordance with a fair presentation framework, the opinion shall use one of the following equivalent phrases:

- The financial statements present fairly, in all material respects, …in accordance with [the applicable financial reporting framework]; or
- The financial statements give a true and fair view of … in accordance with [the applicable financial reporting framework].

Maximum marks on the above explanations **0.5**

4. Basis for audit opinion **0.5**

- The basis for opinion paragraph must state that the audit was conducted in accordance with the ISAs and refer to the 'Auditor's responsibilities for the audit of the financial statements' section which describes the auditor's responsibilities under the ISAs.
- The auditor must also state that they are independent of the audited entity, in accordance with the relevant ethical requirements relating to the audit.
- Finally, the auditor must state that they believe the audit evidence obtained is sufficient and appropriate to provide a basis for the audit opinion.

Maximum marks on the above explanations **0.5**

5. Going concern **0.5**

Where the auditor considers a material uncertainty related to going concern exists, this should be described in a separate paragraph headed 'Material uncertainty related to going concern'.

Maximum marks on the above explanations **0.5**

6. Key audit matters **0.5**

For the audit of listed entities, or where required by law or regulation, the auditor should include a 'Key audit matters' section. This section describes the matters that, in the auditor's professional judgement, are most significant to the audit.

Maximum marks on the above explanations **0.5**

7. Other information **0.5**

For the audit of listed entities or any other entity where the auditor has obtained other information, an 'Other information' section should be included in the auditor's report. This section should include:

- a statement that management is responsible for the other Information
- an identification of the other information obtained before the date of the auditor's report (for listed entities, also the other information expected to be obtained after the date of the auditor's report)
- a statement that the auditor's opinion does not cover the other Information

- a description of the auditor's responsibilities for reading, considering and reporting on other information, and
- where other information has been obtained, either a statement that the auditor has nothing to report, or a description of any uncorrected material misstatement

Maximum marks on the above explanations **0.5**

8. Responsibilities for the financial statements **0.5**

This part of the report describes the responsibilities of those who are responsible for the preparation of the financial statements. This section should describe management's responsibility including the following:

- The preparation of the financial statements in accordance with the applicable financial reporting framework.
- The implementation of such internal control as are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to error or fraud.
- The assessment of the entity's ability to continue as a going concern, the appropriateness of the going concern basis of accounting and adequacy of related disclosures.
- Reference shall be made to 'the preparation and fair presentation of these financial statements'

Maximum marks on the above explanations **0.5**

9. Auditor's responsibilities for the audit of the financial statements **0.5**

The report must state that:

- The auditor's objectives are to obtain reasonable assurance whether the financial statements as a whole are free from material misstatement, and to issue an auditor's report that includes the auditor's opinion.
- Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists.

The report must also:

- Explain that misstatements can arise from fraud or error
- Describe the meaning of materiality
- Explain that the auditor exercises professional judgement and maintains professional scepticism throughout the audit
- Describe the auditor's responsibilities in an audit.
- Describe the auditor's responsibilities in an audit.

Maximum marks on the above explanations **0.5**

10. Other reporting Responsibilities **0.5**

If the auditor is required by law to report on any other matters, this must be done in an additional paragraph titled 'Report on other legal and regulatory requirements' or otherwise as appropriate.

Maximum marks on the above explanations **0.5**

11. Name of the engagement Partner **0.5**

The name of the engagement partner should be identified, unless such a disclosure is reasonably expected to lead to a significant personal security threat.

Maximum marks on the above explanations **0.5**

12. Auditor's signature **0.5**

The report must contain the auditor's signature, whether this is the auditor's own name or the audit firm's name or both.

Maximum marks on the above explanations **0.5**

13. Auditor's address **0.5**

The location where the auditor practices must be included **0.5**

14. Date of the report **0.5**

The report must be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements.

Maximum marks on the above explanations **0.5**

Maximum marks for the question (d) **12**

Total Marks **20**

Model Answers

a. Objective of independent external auditor

The objective of an external audit of financial statements is to determine whether, in the auditor's opinion, the statements present fairly in all material respects - that is, they show a true and fair view in all material respects of the company's financial position, results of operations, and cash flows, in conformity with national or international generally accepted accounting principles (GAAP).

b. Responsibility in relation to the information published on company website

The auditors are not required to read information contained in electronic sites, such as the company's Web site, that also contain the company's audited financial statements and the auditor's report. Auditing standards do not consider electronic sites to be "documents."

c. Responsibility in relation to the information published in Financial Statements and Audit report

This is different from the auditor's responsibility for published (hard copy) documents that contain information in addition to audited financial statements and the auditor's report. In this latter example, the auditor is responsible for reading other information that is published with audited financial statements and the auditor's report to determine whether it is materially inconsistent with information in the audited financial statements.

d. Basic elements of the auditor's report

6. Title

It should clearly indicate that the report is prepared by an independent auditor. This independence confirms that all the relevant ethical standards have been met

7. Addressee

The auditor needs to consider the circumstances of the engagement and local regulations. Under company law the audit report should be addressed to the shareholders

8. Opinion paragraph

This paragraph will:

- Identify the entity been audited
- State that the financial statements have been audited
- Identify each of the financial statements being audited
- d. Refer to the significant accounting policies and other notes contained within the
- financial statements
- Specify the date and period covered by the financial statements.

If the auditor expresses an unmodified opinion on financial statements prepared in accordance with a fair presentation framework, the opinion shall use one of the following equivalent phrases:

- The financial statements present fairly, in all material respects, …in accordance with [the applicable financial reporting framework]; or
- The financial statements give a true and fair view of … in accordance with [the applicable financial reporting framework].

9. Basis for audit opinion

- The basis for opinion paragraph must state that the audit was conducted in accordance with the ISAs, and refer to the 'Auditor's responsibilities for the audit of the financial statements' section which describes the auditor's responsibilities under the ISAs.
- The auditor must also state that they are independent of the audited entity, in accordance with the relevant ethical requirements relating to the audit.
- Finally, the auditor must state that they believe the audit evidence obtained is sufficient and appropriate to provide a basis for the audit opinion.

10. Going concern

Where the auditor considers a material uncertainty related to going concern exists, this should be described in a separate paragraph headed 'Material uncertainty related to going concern'.

6. Key audit matters

For the audit of listed entities, or where required by law or regulation, the auditor should include a 'Key audit matters' section. This section describes the matters that, in the auditor's professional judgement, are most significant to the audit.

7. Other information

For the audit of listed entities or any other entity where the auditor has obtained other information, an 'Other information' section should be included in the auditor's report. This section should include:

- a statement that management is responsible for the other Information
- an identification of the other information obtained before the date of the auditor's report (for listed entities, also the other information expected to be obtained after the date of the auditor's report)
- a statement that the auditor's opinion does not cover the other Information
- a description of the auditor's responsibilities for reading, considering and reporting on other information, and
- where other information has been obtained, either a statement that the auditor has nothing to report, or a description of any uncorrected material misstatement

8. Responsibilities for the financial statements

This part of the report describes the responsibilities of those who are responsible for the preparation of the financial statements. This section should describe management's responsibility including the following:

- The preparation of the financial statements in accordance with the applicable financial reporting framework;
- The implementation of such internal control as are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to error or fraud.
- The assessment of the entity's ability to continue as a going concern, the appropriateness of the going concern basis of accounting and adequacy of related disclosures;
- Reference shall be made to 'the preparation and fair presentation of these financial statements'

Maximum marks on the above explanations

9. Auditor's responsibilities for the audit of the financial statements

The report must state that:

- The auditor's objectives are to obtain reasonable assurance whether the financial statements as a whole are free from material misstatement, and to issue an auditor's report that includes the auditor's opinion;
- Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists.

The report must also:

- Explain that misstatements can arise from fraud or error
- Describe the meaning of materiality
- Explain that the auditor exercises professional judgement and maintains professional scepticism throughout the audit
- Describe the auditor's responsibilities in an audit.

- Describe the auditor’s responsibilities in an audit.

10. Other reporting Responsibilities

If the auditor is required by law to report on any other matters, this must be done in an additional paragraph titled ‘Report on other legal and regulatory requirements’ or otherwise as appropriate.

Maximum marks on the above explanations

11. Name of the engagement Partner

The name of the engagement partner should be identified, unless such a disclosure is reasonably expected to lead to a significant personal security threat.

12. Auditor’s signature

The report must contain the auditor’s signature, whether this is the auditor’s own name or the audit firm’s name or both.

13. Auditor’s address

The location where the auditor practices must be included

14. Date of the report

The report must be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor’s opinion on the financial statements.

END MARKING GUIDE AND MODEL ANSWERS