

**NOVEMBER 2024 PROFESSIONAL EXAMINATIONS
AUDIT & ASSURANCE (PAPER 2.3)
CHIEF EXAMINER'S REPORT, QUESTIONS AND MARKING SCHEME**

EXAMINER'S GENERAL COMMENTS

The standard of the paper was generally good covering all sections of the syllabus. The questions were practical and within the scope of the new syllabus in terms of structure and weightings.

PERFORMANCE OF THE CANDIDATES

The overall performance was good. A total of one hundred and thirty (130) candidates sat for the examination, out of this total, one hundred and eleven (111) passed nineteen (19) failed. In terms of percentages, the pass rate was 85.38 percent compared to 89.92 percent achieved in July 2024. The highest score was 84 marks as against the lowest of 23 marks.

STRENGTHS & WEAKNESS OF CANDIDATES

Strengths

Most Candidates demonstrated strengths in questions 1, 3 and 5 and scored higher marks.

Weaknesses

Some candidates struggled to answer the following questions:

- Question 2(a) cyber security threats and audit response.
- Question 4 (a) factors that can raise questions about going concern and how audit team should report their findings.
- Question 4(b) audit report and opinion section of the auditor's report.
- Question 5(a) test of control and method for testing controls.
- Question 5(b) Substantive testing.

However, these weaknesses did not affect majority of candidates who have prepared well to obtain a pass mark of fifty (50).

QUESTION ONE

- a) According to IAASB Handbook 2023-2024 edition, the degree of assurance that can be provided about the reliability of the financial statements of a company will depend on the amount of work performed in carrying out the assurance process and the result of that work. The resulting assurance falls into one of two levels – reasonable assurance and limited assurance.

Required:

In reference to the statement above, discuss the difference between *reasonable assurance* and *limited assurance* **(10 marks)**

- b) A firm or individual having accepted an appointment as an auditor of a client company, shall submit an engagement letter to the board of directors of the client company. The engagement letter can be seen as the basis for the contract between the company and the auditor.

Required:

In relation to the above statement, state and explain **FIVE** contents of the engagement letter. **(10 marks)**

(Total: 20 marks)

QUESTION TWO

- a) You are part of a team undertaking the audit of Glaglo LTD, a local retail company. The company recently introduced an online marketing and sales system. As part of understanding the company's revenue process by way of a walkthrough test, you noted that the company has recently engaged a fintech company to handle payment processing from these online sales.

Required:

- i) Discuss **FOUR** cyber security threats associated with the IT System employed by Glaglo LTD. **(8 marks)**
- ii) State the audit response to the cyber security threats associated with the IT System employed by Glaglo LTD. **(7 marks)**
- b) As organisations look for ways to cut costs, the idea of outsourcing internal audit work goes on the agenda. While outsourcing may be appealing in theory, there are good reasons to keep internal audit in-house.

Required:

In reference to the statement above:

- i) State **TWO** advantages of outsourcing the internal audit function. **(2 marks)**
- ii) State **THREE** disadvantages of outsourcing the internal audit function. **(3 marks)**

(Total: 20 marks)

QUESTION THREE

- a) **ISA 500: Audit Evidence** provides guidance for auditors intending to rely on the work of a management's expert. If the information to be used as audit evidence has been prepared using the work of a management's expert, the auditor must evaluate the management's expert.

Required:

- i) Explain the term management's expert. **(3 marks)**
ii) Explain **FOUR** factors to consider before relying on the work of a management's expert as audit evidence. **(12 marks)**

- b) Audit assertions are claims made by management regarding the accuracy and completeness of various elements of financial statements. These assertions are used by auditors to develop audit procedures and gather evidence to support their audit opinion. Assertions are categorised into those related to the income statement and those related to the statement of financial position.

Required:

Explain **TWO** key Audit Assertions for the Income Statement. **(5 marks)**

(Total: 20 marks)

QUESTION FOUR

- a) During the audit of Darko Retail LTD, the audit team from Zalia Audit Firm observed that management has not performed a formal assessment of the entity's ability to continue as a going concern. It was noted that though the financial statements show a favourable financial position, the company has been facing liquidity issues and has not been able to secure funds for a significant loan due shortly after the balance sheet date.

Required:

- i) Outline **FOUR** factors that can raise questions about the going concern of Darko Retail LTD in the absence of a formal assessment by management. **(4 marks)**
ii) Describe how the audit team should report their findings related to the going concern assumption in their auditor's report if they conclude that a material uncertainty exists but is not adequately disclosed in the financial statements. **(6 marks)**

- b) You are part of the audit team auditing a client in the retail business. During your risk assessment procedures, you were informed by management that accounts receivable records in one of the company's branches was destroyed in a fire. The company is in the process of obtaining these accounts receivable records but was not able to do so prior to the approval of the financial statements. The fire incident happened on 31 December 2023 and the estimated amount involved is GH¢20 million. The audit team assessed that they are unable to obtain sufficient appropriate audit evidence due to inadequate accounting records. Possible effects are deemed material but not pervasive.

Required:

- i) Justify the type of audit report to be issued in the above scenario. (2 marks)
- ii) Draft the basis for the above opinion section of the auditor's report. (8 marks)

(Total: 20 marks)

QUESTION FIVE

- a) Oboshie Audit Firm has been engaged to audit the financial statements of Abakah Manufacturing LTD for the year ended December 31, 2023. During the planning phase of the audit, the audit team identified that Abakah Manufacturing LTD relies heavily on its internal control system to ensure the accuracy and completeness of its financial reporting.

Required:

- i) Explain **TWO** tests of control to be performed by Oboshie Audit Firm to evaluate the effectiveness of Abakah Manufacturing LTD's internal controls over its financial reporting. (2 marks)
- ii) Identify a method that should be used under each test of control in (i) above. (2 marks)

- b) Baaba & Associates, an audit firm is conducting a year-end audit of Rashida LTD. The audit team is particularly concerned about the accuracy of the accounts receivable balance reported on the statement of financial position as of December 31, 2023. Therefore, as part of their audit procedures, they need to perform substantive tests to identify any material misstatements, errors or fraud that could impact the accuracy of the financial statements.

Required:

Explain **THREE** substantive tests that the audit team at Baaba & Associates should perform to obtain sufficient appropriate audit evidence regarding the accuracy of Rashida LTD's accounts receivable balance. (6 marks)

- c) There are general principles that guide the practice of auditing in the public sector in accordance with International Standards of Supreme Audit Institutions (ISSAI). The principles of auditing are not very different from auditing and assurance in the private sector.

Required:

In relation to the statement above, explain **FIVE** general principles of public sector audit. (10 marks)

(Total: 20 marks)

SOLUTION

QUESTION ONE

a)

Levels of assurance engagements

Reasonable assurance: This is the highest level of assurance that can be provided by a practitioner. It involves a comprehensive examination of the subject matter and aims to provide a high level of confidence that the information is free from material misstatement. The practitioner conducts extensive procedures, including detailed testing and analysis. This typically involves substantive procedures and evidence gathering to a significant extent. Nature of work includes a thorough review of internal controls, transactions, and other relevant information. The work performed is more extensive and involves a higher degree of judgment. Example of instances where a reasonable assurance is given is audit.

Limited assurance: This provides a moderate level of confidence that the information is free from material misstatement, but it is less comprehensive than reasonable assurance. The procedures performed are less extensive and are designed to provide a lower level of assurance. Example of instances where a limited assurance is given is review engagement.

(5 marks each for any 2 well explained points = 10 marks)

b)

Contents of Engagement Letter

An audit engagement letter is a formal document that outlines the terms and responsibilities of an audit engagement between the auditor and the client. In summary, an audit engagement letter serves as a contractual agreement between the auditor and the client, ensuring both parties understand their roles, responsibilities, and the scope of the audit engagement. It provides clarity and establishes expectations to facilitate a smooth and effective audit process.

Here are five key contents typically included in an audit engagement letter:

Objective and Scope of the Audit:

The engagement letter clearly defines the objective of the audit, which is usually to express an opinion on the fairness of the client's financial statements. It outlines the specific financial periods to be audited and details the scope of the audit work, including the nature and extent of audit procedures to be performed.

Responsibilities of the Auditor:

The letter specifies the responsibilities of the audit firm, including conducting the audit in accordance with relevant auditing standards (e.g., Generally Accepted Auditing Standards or International Standards on Auditing). It outlines the auditor's obligation to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement, whether due to fraud or error.

Responsibilities of Management:

The engagement letter delineates the responsibilities of management, such as providing access to all relevant financial records, supporting documents, and other information

necessary for the audit. Management is also responsible for preparing the financial statements in accordance with applicable financial reporting frameworks.

Communication of Audit Findings:

The letter specifies how audit findings will be communicated to management and those charged with governance (e.g., the board of directors or audit committee). It outlines the format and timing of the audit report, including any required communications of significant deficiencies or material weaknesses identified during the audit.

Limitations of Audit:

The engagement letter typically includes a section on limitations of the audit, clarifying that while the audit provides reasonable assurance, it does not guarantee that all material misstatements, whether due to fraud or error, will be detected. It also may outline any circumstances under which the auditor's liability is limited, such as to the extent permitted by law.

(2 marks each for any 5 well explained points = 10 marks)

(Total: 20 marks)

QUESTION TWO

a)

i) Cyber security threats associated with the IT System of Glaglo LTD.

- Loss/theft of data
- Loss of intellectual property
- Theft of funds
- Leakage of sensitive information
- Disruption of day-to-day business
- Prevention of timely access to information

(4 well explained points @ 2 marks each = 8 marks)

ii) Audit responses to Cyber security threats associated with the IT System

In addition to substantive procedures, appropriate automated controls within the revenue process will need to be identified and tested. This may include testing automated interface controls, access controls and configuration controls across systems involved in the origination and processing of transactions from the online sales. General IT controls will also need to be tested to ensure data/information within such systems have integrity.

(7 marks)

b)

Outsourcing of internal audit: Outsourcing internal audit functions involves hiring an external firm or specialist to perform some or all of the internal audit activities that would traditionally be handled by an internal audit unit.

i) **Advantages of outsourcing internal audit**

- Staff recruitment. There is no need for the company to recruit and train its own internal audit staff. An internal audit function can be instantly available by hiring the services of an accountancy firm.
- Auditor skills. The outside supplier is likely to have specialist staff available, such as computer audit experts. Internal auditors with an IT specialisation may be difficult to recruit as full-time employees.
- Costs and flexibility. The cost of the internal audit function is a variable cost rather than a fixed cost. A company therefore only pays for the internal audit time that it uses.
- Outsourcing is likely to be more economical for a small entity that does not have enough audit work to justify a full-time internal audit team.

(1 mark each for any 2 well explained points = 2 marks)

ii) **Disadvantages of outsourcing internal audit**

- Professional firms are not under the control of the entity in the same way as their 'in house' internal audit employees.
- Fees for internal audit work can be high.
- Professional firms may not have the same level of detailed knowledge of the entity and its operations that 'in house' internal auditors.
- There may be threats to the independence of the external audit where the firm acts as both internal auditors and external auditors.

(1 mark each for any 3 well explained points = 3 marks)

(Total: 20 marks)

QUESTION THREE

a)

- i) A management expert refers to an individual or entity with specialized knowledge, skills, and experience in a particular field relevant to the audit engagement. Management experts possess deep knowledge and expertise in their respective fields, which could include areas such as financial reporting, valuation, taxation, legal matters, engineering, environmental science, information technology, and more.

(3 marks for good definition and explanation)

- ii) When considering using the work of a management expert as audit evidence, auditors should evaluate several factors to ensure the reliability and relevance of the information. Here are key factors to consider:

1. **Expertise and Qualifications:** Assess the qualifications, expertise, and reputation of the management expert. Verify their credentials, relevant experience, and any certifications they hold in the field pertinent to the audit subject matter.
 2. **Independence and Objectivity:** Evaluate the independence and objectivity of the management expert. Consider any potential conflicts of interest that could affect the objectivity of their work or their relationship with the auditee.
 3. **Scope and Purpose of Work:** Understand the scope and purpose of the management expert's work. Clarify whether their work was specifically performed for the audit engagement or for another purpose, as this can impact its relevance to the audit objectives.
 4. **Methodology and Approach:** Review the methodology, techniques, and assumptions used by the management expert in their analysis or assessment. Assess whether these are appropriate and reliable for the audit context and whether they comply with relevant professional standards.
 5. **Documentation and Evidence Trail:** Ensure that there is sufficient documentation and an adequate evidence trail supporting the management expert's findings and conclusions. This includes detailed records of data sources, calculations, analyses, and any assumptions made.
 6. **Consistency and Reliability:** Evaluate the consistency and reliability of the management expert's findings with other audit evidence obtained. Consider whether their conclusions align with other information gathered during the audit process.
 7. **Communication and Collaboration:** Communicate effectively with the management expert to understand their work fully. Collaborate to address any questions or concerns regarding their findings, methodologies, or the interpretation of results.
 8. **Limitations and Assumptions:** Recognize any limitations or assumptions inherent in the management expert's work. Assess whether these limitations could impact the reliability or relevance of their findings to the audit objectives.
 9. **Audit Reporting Requirements:** Ensure that the use of the management expert's work meets the reporting requirements of the audit engagement. Clearly document the nature and extent of reliance placed on the management expert's findings in the audit report.
 10. **Reviewer Competence:** Consider the competence of the auditor or audit team members responsible for evaluating and using the management expert's work as audit evidence. Ensure they have the necessary knowledge and skills to assess its relevance and reliability.
- (3 marks each for any 4 well explained points = 12 marks)*

b)

The following are key Audit Assertions for the Income Statement

1. **Occurrence:**
Transactions and events that have been recorded have actually occurred and pertain to the entity. Example: Sales recorded in the income statement actually took place and are not fictitious.
2. **Completeness:**
All transactions and events that should have been recorded have been included in the financial statements. Example: All sales transactions that occurred during the period have been recorded in the income statement.
3. **Accuracy:**

Amounts and other data relating to recorded transactions and events have been recorded appropriately. Example: Sales and expense amounts are recorded accurately, reflecting the correct amounts and applicable discounts or returns.

4. **Cut-off:**

Transactions and events have been recorded in the correct accounting period. Example: Sales and expenses are recorded in the period they actually occur, ensuring that year-end transactions are not misstated.

5. **Classification:**

Transactions and events have been recorded in the proper accounts. Example: Expenses are classified correctly as cost of goods sold, operating expenses, or other categories in the income statement.

(Any 2 well explained points @ 2.5 marks each = 5 marks)

(Total: 20 marks)

QUESTION FOUR

a)

i) Factors that raise questions about the going concern of Darko Retail LTD

- Net liability or net current liability position
- Indication of withdrawal of financial support by creditors
- Adverse key financial ratios
- Arrears or discontinuation of dividends
- Change from credit to cash-on-delivery transactions with suppliers
- Loss of key management without replacement
- Labour difficulties
- Shortages of important supplies
- Emergence of highly successful competitor

(Any 4 points for 4 marks)

ii) **Reporting Findings:**

- **Modified Opinion:** If the audit team concludes that a material uncertainty exists and management has not adequately disclosed this in the financial statements, the team should consider issuing a qualified or adverse opinion.
- **Basis for Modification:** Clearly state the basis for the modified opinion in the auditor's report, explaining the nature of the material uncertainty and the inadequate disclosure.
- **Emphasis of Matter:** Alternatively, if the uncertainty is disclosed but needs more emphasis, include an emphasis of matter paragraph to draw attention to the note in the financial statements that describes the material uncertainty.

(3 points @ 2 marks each = 6 marks)

b)

- i) The fire destroyed the company's accounts receivable records, which was assessed as material but not pervasive to the financial statements hence a *qualified opinion* will need to be issued.

(2 marks)

ii) **Draft Basis for Qualified Opinion**

Because of a fire in a branch office on 31 December 2023 that destroyed its accounts receivable records, we were unable to confirm or verify by alternative means the carrying amount of accounts receivable included in the financial statements as at 31 December 2023, stated at GH¢20 million.

The Company is in the process of reconstructing these accounts receivable records but was not able to do so prior to the approval of the financial statements. Accordingly, we were not able to determine whether any adjustments might be necessary to the amounts shown in the financial statements for accounts receivable, sales, income taxes, net profit and retained earnings as at and for the year ended 31 December 2023.

(8 marks)

(Total: 20 marks)

QUESTION FIVE

a)

i) **Tests of control to be performed by Oboshie Audit Firm**

1) **Approval of Transactions:**

To verify that all significant transactions are authorized by appropriate personnel to ensure their validity and accuracy.

2) **Segregation of Duties:**

To ensure that no single individual has control over all aspects of a financial transaction, thereby reducing the risk of fraud and errors.

(2 marks)

ii) **Methods to be used under the tests of control**

Test: *Approval of transactions*

Method: **Inspection**

Select a sample of purchase orders and inspect them to ensure that each has been signed by the authorized manager as evidence of approval. Review a sample of high-value transactions to check for the presence of required approval signatures and any accompanying documentation that supports the transaction.

Test: *Segregation of Duties*

Method: **Observation**

Observe the process of cash handling, including receiving, recording, and reconciling cash transactions, to verify that these duties are performed by different employees. Watch the cash receipt process to ensure that the person receiving cash is not the same person recording the transaction in the accounting system, and another individual is responsible for reconciling the bank statements.

(2 marks)

b) Substantive tests that the audit team at Baaba & Associates should perform to obtain sufficient appropriate audit evidence regarding the accuracy of Rashida LTD's accounts receivable balance.

- **Confirmation of Accounts Receivable:** The audit team should send confirmation requests directly to customers to confirm the amounts owed to DEF Retail Ltd. This provides evidence directly from third parties, which is generally considered reliable. Select a sample of customer accounts from the accounts receivable ledger and send positive confirmation requests (where customers are asked to respond whether they agree or disagree with the stated amount). Follow up on any non-responses or discrepancies to resolve differences.
- **Subsequent Cash Receipts Testing:** The audit team should review cash receipts received after the year-end to determine whether outstanding receivables at the balance sheet date have been collected. This helps verify the existence and accuracy of the accounts receivable balance. Examine bank statements and cash receipt records for January and February 2024 to identify payments received from customers. Match these receipts to outstanding accounts receivable as of December 31, 2023, to confirm their accuracy.
- **Aging Analysis:** The audit team should obtain the accounts receivable aging report as of December 31, 2023, and analyze the age of the receivables. Review the aging report to identify any receivables that are significantly overdue (e.g., more than 90 days past due). For these overdue accounts, inquire with management about the collectability and consider whether an allowance for doubtful accounts is necessary.
- **Cut-Off Testing:** The audit team should test transactions around the year-end to ensure that sales and corresponding receivables are recorded in the correct period. Select a sample of sales transactions from just before and after December 31, 2023. Verify that sales made before the year-end are included in the accounts receivable balance and that sales after year-end are not included. Check shipping documents, invoices, and sales records to confirm the proper recording period.

(3 points for 6 marks)

c) **General principles of public sector Audit**

- **Ethics and independence:** Auditors should comply with ethical requirements and be independent. Auditors need to be independent so that their reports are impartial.
- **Professional judgement, due care and skepticism:** Auditors should apply professional skepticism, professional judgment and due care throughout an audit.
- **Quality control:** Auditors should perform the audit in accordance with professional standards on quality control.
- **Audit team and management skills:** Auditors should possess or have access to the necessary skills
- **Audit risk:** Audit risk is the risk that the audit report may be inappropriate and may reach inappropriate conclusions. Auditors should manage the risks to keep them within acceptable limits.
- **Materiality:** Materiality is relevant in all audits. Auditors should consider materiality throughout the audit process.

(2 marks each for any 5 well explained points = 10 marks)

(Total: 20 marks)