AUDIT & ASSURANCE

PROFESSIONAL LEVEL EXAMINATION

APRIL 2021

NOTES:

Section A - You are required to answer Questions 1, 2 and 3.
Section B - You are required to answer any **one** out of Questions 4 or 5. Should you provide answers to both Questions in this section, only Question 4 will be marked.

TIME ALLOWED:
3.5 hours, plus 10 minutes to read the paper. This is a closed book examination.

INSTRUCTIONS:
During the reading time, candidates are encouraged to use this time to read each Question carefully. Please note, however, candidates will not be prevented from using this time to start typing notes and solutions.

Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

You are reminded to pay particular attention to your communication skills, and care must be taken regarding the format and literacy of your solutions. The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples, where appropriate.

<u>N.B.</u> Please note that the right click function has been disabled during your examination. Should you wish to copy and paste, please use the following shortcuts: Copy (Ctrl + C) and Paste (Ctrl + V).

SECTION A - Questions 1, 2 and 3 are Compulsory.

Question 1

Skii Ltd, based in Dublin, is a high-end manufacturer of specialist raw material products selling to companies operating in the medical devices sector.

You are the audit senior on the engagement and you have been presented with the information below by the company's financial controller in respect of the non-current assets for the year ended 31 December 2020:

	Buildings	**Investment Properties**	**Vehicles**	**Office Equipment**
Cost	**€**	**€**	**€**	**€**
As at 1 January 2020	4,000,000	5,000,000	50,000	800,000
Additions in Year	1,000,000	2,000,000	10,000	50,000
Disposals			(5,000)	
As at 31 December 2020	5,000,000	7,000,000	55,000	850,000
Accumulated Depreciation				
As at 1 January 2020	400,000		20,000	160,000
Charge for Year	200,000		5,250	85,000
Disposals			(1,000)	
As at 31 December 2020	600,000	-	24,250	245,000
Depreciation Method	*Straight Line*		*Reducing Balance*	*Straight Line*
Depreciation Rate Per Annum	*4%*		*15%*	*10%*

Notes:

(i) The directors of the company revalue investment properties periodically based on increasing rent and property prices in Dublin.

(ii) The company acquired a new investment property in June 2020 for €1,500,000 but subsequently revalued this property to €2,000,000.

(iii) The company purchased all its investment properties in the hope that it would move into the properties to expand the manufacture of medical devices. However, due to the purchase of a new building which is adjacent to its original building, Skii Ltd now leases all investment properties to third parties.

REQUIREMENT:

(a) Describe TWO significant auditing assertions in relation to property, plant and equipment. **(4 marks)**

(b) Set out the programme of audit work for the substantive testing of non-current assets, including depreciation, in respect of Skii Ltd for the year ended 31 December 2020. You should take care to also highlight the relevant assertions being tested.

(14 marks)

(c) Explain and discuss what is meant by a Non-Current Asset Register and outline the steps that you, as auditor, should take to confirm that the register is up to date and can be relied upon during audit testing.

(4 marks)

(d) The UK Corporate Governance Code 2018 states there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.

Discuss how the board of directors can ensure that the process for new appointments to the board fulfils this corporate governance requirement.

(8 marks)

[Total: 30 Marks]

Question 2

You are an audit manager working with Smiths & Co. Certified Public Accountants and Registered Auditors (Smiths & Co.). You are currently working within the accounting department of the firm, as an internal expert for audit teams. It is 25 March 2021 and you have been on annual leave for a number of days and are expecting a long and busy day catching up on the work you missed. When you arrive in the office you have four voicemails requesting extremely urgent responses to items that have been emailed to you. A summary of the issues from the emails is given below:

(i) Alpha Ltd (Alpha) is currently involved in litigation. Alpha is being sued for breach of a contract. The audit team has reviewed correspondence and obtained confirmations from Alpha's solicitors. The correspondence and confirmations note that the clause in question is subjective and as such, they are unable to conclude whether it is likely that Alpha can win the case. If Alpha loses the case, the implications will have a severe negative impact on its financial standing. Alpha has not disclosed this matter in the financial statements.

(ii) WW Ltd (WW) has a year end of 31 March 2021. The audit has been progressing well with the exception of accounts receivable. WW sells predominantly to small newsagents who do not respond to confirmation requests and are typically slow to pay. As a result, the audit team has been unable to obtain comfort over the recoverability of accounts receivable and does not expect to be able to resolve this before the audit report is signed.

(iii) Quest Ltd (Quest) has historically been in a permanent overdraft situation. The budget for the coming 12 months shows a continued requirement for the overdraft. The overdraft facilities have expired, and Quest has not yet managed to renegotiate them due to stricter controls and requirements having been brought into their bank's processes since the last renewal date. If an overdraft cannot be arranged, Quest will not be a going concern. Management is confident that a renewal will be negotiated. The accounts have to be signed by the auditor as Quest is required to file them with a regulatory authority for its industry on 30 June 2021. The audit team cannot say whether it is likely or not that Quest will be able to renegotiate the facility.

(iv) Thomond Ltd (Thomond) has a year end of 31 December 2020. Thomond had a disagreement with its previous auditors which came to a crisis in March 2021. Thomond decided to change auditors at that point. Due to the late appointment of Smiths & Co., attendance at the year-end inventory count was not possible. After the appointment, consideration was made to performing an inventory in March 2021 and rolling the inventory balance back to year end, but it was concluded with Thomond that this would not be possible due to system limitations within the inventory management system.

REQUIREMENT:

(a) Describe briefly the main contents of an audit report. **(4 marks)**

(b) In respect of audit issues (i) to (iv), evaluate the potential impact on the audit report. **(16 marks)**

(c) Discuss the impact of emerging technologies on the auditing and the accounting profession. **(5 marks)**

(d) Explain the term 'Professional Scepticism' in relation to audit and discuss the importance of being professionally sceptical when undertaking an auditing engagement. **(5 marks)**

[Total: 30 Marks]

Question 3

The following multiple-choice question contains eight sections, each of which is followed by a choice of answers. Only one of the answers offered is correct. Please note that the marks for Sections 1 – 4 are worth 2 marks each and Sections 5 – 8 are worth 3 marks each.

REQUIREMENT:

1. Which TWO of the following substantive procedures provide evidence regarding the EXISTENCE of trade receivables?

(2 marks)

(1) Agreeing a sample of goods despatched notes to sales invoices and to the sales ledger.
(2) Undertaking a receivables circularisation.
(3) Review of post year-end cash receipts and, if these relate to year-end receivables, follow through to the sales ledger.
(4) Recalculating the allowance for uncollectible accounts.

(a) 1 and 3
(b) 2 and 4
(c) 2 and 3
(d) 1 and 4

2. With regard to which of the following financial statement assertions might an auditor encounter particular difficulties in obtaining sufficient audit evidence where internal controls are weak? **(2 marks)**

(a) Ownership
(b) Existence
(c) Valuation
(d) Completeness

3. Before accepting an appointment as auditor, the nominated auditor is expected to communicate with the existing auditor to ensure that there is no professional reason why he/she should not accept the appointment: **(2 marks)**

(a) Only in respect of audits to be performed under the Companies Act.
(b) Only in respect of audits of large companies.
(c) Only where he/she has reasonable cause to believe that there is some such reason.
(d) In all cases.

4. Which of the following statements correctly describes the auditor's responsibilities in accordance with *ISA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*? **(2 marks)**

(a) The auditor is responsible for the prevention and detection of fraud and error.
(b) The auditor is not responsible for the prevention of fraud and error, but is responsible for detection.
(c) The auditor is responsible for obtaining reasonable assurance that the financial statements are free from material misstatement whether caused by fraud or error.
(d) The auditor is responsible for detecting all errors and should attempt to detect fraud where information comes to light as a result of standard audit procedures.

5. Which of the following is not a key component of a preliminary assessment of control risk? **(3 marks)**

(a) Interview entity personnel to find evidence of management's commitment to the design, implementation, and maintenance of sound internal controls.
(b) Identify possible liabilities which may arise.
(c) Consider the results of previous audits that involved evaluating the operating effectiveness of internal control.
(d) Discuss the possibility of audit risk with audit firm personnel.

6. Which of the following statements describes most accurately the principal purpose of the engagement letter in respect of a Ltd company audit assignment? **(3 marks)**

(a) To define the extent of the auditor's responsibilities.
(b) To set out the proposed timetable for the audit.
(c) To establish the audit fee for the current year.
(d) To draw the attention of the directors to the range of services that the firm can offer.

7. Internal Auditors are appointed by: **(3 marks)**

(a) Management
(b) Shareholders
(c) Government
(d) Statutory Body

8. For which of the following procedures may audit software be used to perform? **(3 marks)**

1. Testing the programmed controls of a system.
2. Calculating ratios.
3. Extracting samples.
4. Checking arithmetical accuracy.

(a) 1, 2 and 3
(b) 2, 3 and 4
(c) 1, 2 and 4
(d) 1, 3 and 4

[Total: 20 Marks]

Question 4

FameTech Ltd (FameTech) is a computer hardware specialist company and has been trading for over five years. The company is funded partly through loans and overdrafts and also by several large equity shareholders.

FameTech has experienced significant growth in previous years. However, in the current year, a new competitor PCT, entered the market and, through competitive pricing, gained a considerable market share, largely to the detriment of FameTech.

One of FameTech's larger customers has moved its business to PCT. In addition, a number of FameTech's specialist developers have left the company and joined PCT. FameTech has found it difficult to replace these employees due to the specialist level of their skills and knowledge.

FameTech has just received notification that its main supplier, who provided the company with specialist electrical equipment, has ceased to trade.

FameTech is looking to develop new products to differentiate itself from its competitors. The directors recently approached the company's shareholders to seek additional funding in order to finance this development. However, the shareholders do not want to invest further at this time.

FameTech's loan is long-term, and the company has met all repayments on time.

The company overdraft has increased significantly over the year. The directors have informed you that the overdraft facility is due for renewal next month and they are confident it will be renewed.

The directors have produced a cash flow forecast which indicates a significantly worsening position over the coming 12 months.

Overall, however, the directors are confident in relation to new products being developed. In light of their trading history of significant growth, they believe it is unnecessary to make any disclosures in the financial statements regarding going concern.

REQUIREMENT:

(a) Outline what is meant by 'going concern' and outline management's responsibility in relation to going concern.

(5 marks)

(b) Assess SIX potential indicators that FameTech may not be a going concern.

(6 marks)

(c) Evaluate key audit procedures that should be performed to identify these indicators as to whether FameTech is a going concern.

(9 marks)

[Total: 20 Marks]

Question 5

(a) A member is required to comply with the five key fundamental principles laid out within the *CPA Ireland Code of Ethics*.

REQUIREMENT:

Evaluate any FOUR of these fundamental principles.

(8 marks)

(b) The auditors of Plato Ltd, a large engineering company with operations and subsidiaries in multiple countries, have commenced the audit of its financial statements for the year ended 31 March 2021.

At a recent board meeting, one of the directors highlighted a problem with the latest management report because one of the major reserve figures had recently been found to be incorrect in the company's year-end accounts. The difference in question is material.

At this board meeting, another director questioned the adequacy of internal audit and control systems. The company's IT Director explained that a breakdown in the interface between the company's international servers for a few days at the end of the quarter in question meant that several entries made locally in respect of movements in reserves had not been updated at the company's headquarters, where all financial reporting matters are processed.

REQUIREMENT:

Assess, in the context of Plato Ltd, how a company's IT environment and computer-based accounting system may:

(i) Positively impact its overall internal control environment. **(6 marks)**

(ii) Pose significant risks to its internal control environment. **(6 marks)**

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS IN IRELAND

AUDIT & ASSURANCE

PROFESSIONAL LEVEL - APRIL 2021

SOLUTION 1

(a) **Existence (E):** That tangible non-current assets as recorded in the accounting records do actually exist.

Rights and Obligations (R/O): That the reporting company has the right of control over the tangible non-current assets which have been accounted for.

Accuracy/Valuation (A/V): That the tangible non-current assets are carried at the correct amounts/valuations in the financial statements.

Completeness (C): That all tangible non-current assets which exist at the year-end are accounted for in the books and records.

Occurrence (O): That all additions and disposals of property, plant and equipment in the financial statements took place (i.e. are real)).

Classification and Presentation (C/P): That an item is adequately disclosed/classified and presented in the financial statements.

Cut-Off (C/O): That any additions or disposals of property, plant and equipment is recorded in the correct accounting period.

(4 Marks)

(b) A sample programme of audit work that should be undertaken for substantive testing of non-currents assets is as follows:

Test	**Assertions**
Ensure accounting polices appropriate	V, A, C/O, C/P
Obtain fixed asset register – tot check, agree to nominal ledger & agree opening balances	V, A, C, C/O, C/P
Vouch additions in year to supporting docs e.g. supplier invoice, bank statement	O, A, C/O, E, R/O
For any internally generated additions, vouch to supporting docs e.g. raw material invoices, employee time records	O, A, C/O, E, R/O
Vouch disposals in year to supporting docs e.g. sales invoice, bank statement	O, A, C/O, R/O
Vouch revalued assets to supporting docs e.g. independent third party valuation report	V, C/O
Review clients consideration of impairment and identify any indications of impairment	V, C/O
Inspect title deeds or obtain confirmation from third parties (if not held by client)	E, R/O
Inspect vehicle registration documents	E, R/O
Inspect office equipment documents	E, R/O
Physically inspect a sample of assets & perform floor-to-sheet and sheet-to-floor testing, if necessary	E, C, R/O
Review P&L items (e.g. repairs) for capital expenditure	A, V, C
For capitalised leases, review lease agreement and confirm finance lease	A, V, C
Conclude on appropriateness of depreciation rates and recalculate sample	A, V, C/O
Ensure all appropriate disclosures are made (capital commitments, security for loans etc)	C/P

Specific to depreciation we should:

- Review depreciation rates in relation to:
  - Asset useful life
  - Disposal value
  - Replacement policy
  - Prior year experience regarding profit/loss on disposal
  - Consistency with previous accounting policies
  - Possible obsolesce
- Verify with asset register, depreciation charges on all assets with limited useful life
- For revalued assets, ensure the correct deprecation is charged on the revalued amount
- Re-perform and re-calculate deprecation charges
- Compare depreciation rates with previous years ratio and depreciation method
- Verify that depreciation rate and method is disclosed correctly in the financial statements.

Issues noted specific to Skii Limited based on the information provided by the financial controller:

Item	Issue	Recommendation
Accounting Policies	Incorrect treatment of investment property valuation	Undertake third party independent valuation of investment property. See part (c) for more information.
Depreciation	Potential incorrect depreciation charges included	Re-calculate depreciation charges and undertake additional testing on depreciation including specifics listed above.
Classification & Presentation	Incorrect classification and presentation under IAS16 Plant, Property & Equipment. There is no Net Book Value for the non-current assets in Skii Limited.	Ensure correct classification and presentation of non-current asset table under IAS 16 Plant, Property & Equipment.

(14 Marks)

(c) Non-current asset registers are a record of the non-current assets held by a company. These form part of the internal control system of an organisation. The non-current asset register is a key link for the auditor between the physical assets and the balance in the property, plant & equipment nominal ledger accounts which underpin the Financial Statements. Details held on such a register may include:

- Cost
- date of purchase
- description of asset
- serial/reference number
- location of asset
- depreciation method
- expected useful life
- net book value
- insurance cover.

Steps that an auditor should take to confirm the register is up to date:

- Obtain/prepare summary of non-current assets showing:
  - gross book value
  - accumulated depreciation
  - net book value
- Reconcile summary with opening position
- Reconcile non-current asset general ledger with non-current asset register, obtain explanation about differences, if any
- Physically inspect assets mentioned in non-current asset register
- Confirm items:
  - exist
  - are in use
  - are in good condition
  - match to serial/reference number on non-current asset register
- Select all/sample of additions and disposals during the year which are included in the non-current asset register and vouch to supporting documentation.

(4 Marks)

(d) The Board of Directors should establish a nomination committee which would lead the process for appointments and would make recommendations to the board. The nomination committee should be chaired by the chairman and populated by independent non-executive directors, except on the occasion whereby it is the chairman who is being replaced.

The terms of reference of the nomination committee must be clearly determined to ensure that a formal and rigorous approach to appointment is undertaken. The search for and the appointment of board members should be made on the basis of merit with the consideration for the need for diversity on the board including gender.

The nomination committee should consider skills, experience, independence and knowledge currently on the board and identify the role and capabilities required for the new appointment. The object is to ensure that there is an appropriate balance of skills and experience on the board and to continually refresh the skills and talents on the board. The board should ensure that there are plans in place for orderly succession for appointment to the board and to senior management to ensure continuity and succession planning.

(8 Marks)

[Total: 30 Marks]

SOLUTION 2

(a) The contents of an unmodified audit report should include the following:

- Title
- Addressee
- Introductory Paragraph
- Respective responsibilities of those Charged with Governance and Auditors.
- Scope of the Audit of Financial Statements
- Auditors Opinion
- Opinions on Other Matters
- Date of Report
- Address of Office
- Auditors signature

(4 Marks)

(b) **Issue (i): Alpha Limited**

This issue represents a material uncertainty. If management have given appropriate adequate disclosures, the auditors should issue an unqualified opinion, modified by an emphasis of matter paragraph highlighting the matter.

If management have not provided adequate disclosures, the auditors should issue a qualified report or adverse opinion. As this matter is material, but not pervasive, the opinion would be qualified, “except for” the disclosures surrounding the legal case.

Issue (ii): WW Limited

The auditor should conduct other audit procedures to satisfy themselves as to validity of the debtor balances. Only if this and other work fails to provide appropriate comfort the audit report may need to be qualified.

Issue (iii): Quest Limited

This represents an uncertainty regarding going concern. The auditors at this point do not disagree with the preparation of accounts on the going concern basis.

If management have given appropriate adequate disclosures, the auditors should issue an unqualified opinion, modified by an emphasis of matter paragraph highlighting the matter. If management have not provided adequate disclosures, the auditors should issue a qualified report.

Issue (iv): Thomond Limited

This represents a limitation of scope as the auditors have been unable to obtain comfort over the existence of inventories due to the circumstances of appointment.

Depending on the materiality and pervasiveness of the issue a qualified report (except for in cases of material but not pervasive, adverse in the case of material and pervasive) should be issued describing the limitation and the potential impact on the figures had the limitation not existed.

(16 Marks)

(c) The role of emerging technologies (Artificial Intelligence, Blockchain Technology, Data Analytics and the use of Big Data, Machine Learning and Robotic Process Automation), has had a substantial impact on the accounting profession with more emphasis on automation and accountants adding value to their clients by making advisory decisions.

The audit profession, professional bodies and regulators are increasing their focus on the impact of technology. There are clear benefits that technology can bring from operational efficiency to financial inclusion and greater insights. However, alongside these benefits comes a range of risks, many of which are still not fully understood. The modern role of the auditor/accountant now means they need to be more technology savvy and understand the key controls in place to ensure no material misstatements or instances of fraud exist.

* Note: This can be a subjective answer and differ based off candidates experience in the workplace.

(5 Marks)

(d) Professional scepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

ISA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing, requires the use of professional scepticism as a means of enhancing the auditor’s ability to identify risks of material misstatement and to respond to the risks identified. Professional scepticism is closely related to fundamental ethical considerations of auditor objectivity and independence.

This concept is very important from an auditing perspective and by applying professional scepticism, this should reduce detection risk because it enhances the effectiveness of applied audit procedures and reduces the possibility that the auditor will reach an inappropriate conclusion when evaluating the results of audit procedures.

(5 Marks)

[Total: 30 Marks]

SOLUTION 3

1. **C** 2 and 3 (Undertaking a receivables circularisation AND Review of post year-end cash receipts, if these relate to year-end receivables follow through to the sales ledger).

2. **D** Completeness.

3. **D** In all cases.

4. **C** The auditor is responsible for obtaining reasonable assurance that the financial statements are free from material misstatement whether caused by fraud or error

5. **B** Identify possible liabilities which may arise.

6. **A** To define the extent of the auditor's responsibilities.

7. **A** Management.

8. **B** 2, 3 and 4 (Calculations of ratios, extracting samples and checking arithmetical accuracy).

SOLUTION 4

(a) The going concern principle is the assumption that a company will remain in business for the foreseeable future. ISA 570 Going Concern, deals with the auditor's responsibilities in auditing the management's use of the going concern basis in the preparation and presentation of the accounts. The standard sets the objectives of the auditor's work and the specific requirements to fulfil. In addition ISA 570 clarifies the respective responsibilities of the management of the company and of the auditor in assessing the entity's ability to continue in business as a going concern.

Management's responsibility in relation to going concern is to undertake the going concern assessment and making related disclosures in accordance with the applicable financial reporting framework. They should consider all the facts and circumstances about the foreseeable future of a company known at the date of approval of the accounts. It would be advisable for the assessment to include, as a minimum, the preparation of a budget, trading estimates and cash flow forecasts and an analysis of the company's borrowing requirements and facilities.

When conducting their going concern assessment, the management will have to evaluate which of three potential conclusions is appropriate to the circumstances of the company. In particular they may conclude that:

- There are no material uncertainties that may cast significant doubt about the company's ability to continue as a going concern
- There are material uncertainties related to events or conditions that may cast significant doubt about the company's ability to continue as a going concern but the use of the going concern basis remains appropriate; or
- The use of the going concern is not appropriate.

FameTech's management has undertaken some of the above work already but they believe it is unnecessary to make any disclosures in the financial statements regarding going concern. This will be need to be agreed with by the auditors and in the auditor's judgment, if management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the auditor shall express an adverse opinion.

(5 Marks)

(b) Below are some potential indicators which suggests that FameTech is not a going cocern:

- **New competitor:** FameTech has experienced significant growth in previous years, however, in the current year and new competitor PCT, has entered the market and through competitive pricing has gained a considerable market share from FameTech – This can suggest FameTech is not a going concern as PCT has already gained some of their market share and this does not bode well for the future unless FameTech can differentiate itself against their competitors.

- **Loss of large customer:** One of FameTech's larger customers has stopped trading with them and has moved its business to PCT. This further strengths PCT and is of concern for FameTech. We would need to consider what percentage of revenue this client represented and if it was recurring revenue. If it represented a large proportion of annual sales it could suggest FameTech is not a going concern.

- **Loss of key staff:** A number of FameTech's specialist developers have left the company and joined PCT. FameTech has found it difficult to replace these employees due to the level of their skills and knowledge. This is alarming for FameTech as key staff have left and joined their main competitor. Their skill and knowledge is a competitive advantage for their competitors but FameTechs inability to replace them could suggest FameTech is not a going concern.

- **Cessation of main supplier:** FameTech received notification that its main supplier who provided the company with specialist electrical equipment has ceased to trade. Another major concern for FameTech that they are not a going concern. Depending on the supplier arrangements and the suppliers that work with PCT they might find it very difficult to obtain new suppliers at an affordable price.

- **Future funding requirements:** FameTech approached its shareholders to finance future development and seek further funding, however, they did not want to invest further at this time. They have increased their overdraft significantly over the year and the directors have stated that the overdraft facility is for renewal next month. This is another cause of concern for FameTech as due to the entrance of a new major competitor, loss of key staff and issues with large customers and suppliers it is expected that they will need further funding to develop new products. If they are not in a good financial position this could stagnate their previous growth which could lead to them lagging behind their competitors which could further dent their market share.

- **Cash flow forecasts:** The directors have produced a cash flow forecast which shows a significantly worsening position over the coming 12 months. In order to consider whether a company is a going concern or not, cash flow forecasts and future projections are essential. If the directors have produced worsening cash flow forecasts this is a major concern for FameTech and would again suggest that they are not a going concern.

(6 Marks)

(c) ISA 570 clearly outlines the objectives of the auditor in respect of the use of the going concern basis in the accounts:

- To obtain sufficient appropriate evidence regarding the appropriateness of management's use of the going concern basis
- To conclude, on the basis of the audit evidence, whether a material uncertainty exists in respect of events or conditions that may cast significant doubt about the entity's ability to continue as a going concern; and
- To determine the implications for the auditor's report.

ISA 570 requires the auditor to consider going concern at the early stages of the audit, in particular when performing risk assessment procedures at the planning stage. At that point the auditor should consider whether there are events or conditions that may cast significant doubt about the going concern assumption.

Events and conditions that may cast doubt about the going concern assumption could be of financial, operating or other nature. ISA 570 highlights a number of such events and conditions that are commonly encountered in real life and that the auditor should be familiar with. They include Financial and Operational uncertainties, some of which are clearly evident in FameTech.

Below is a sample of procedures which might suggest whether a company is a going concern or not:

Financial:
- Net liability or net current liability position.
- Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets.
- Indications of withdrawal of financial support by creditors.
- Negative operating cash flows indicated by historical or prospective financial statements.
- Adverse key financial ratios.
- Inability to obtain financing for essential new product development or other essential investments.

Operational:
- Management intentions to liquidate the entity or to cease operations.
- Loss of key management/staff without replacement.
- Loss of a major market, key customer(s), franchise, license, or principal supplier(s).
- Labour difficulties.
- Shortages of important supplies.
- Emergence of a highly successful competitor.

Procedures which the auditor need to consider undertaking are as follows:

- A review of the management's plans for future actions in respect of going concern, including, for example, enquiries about their plans to liquidate assets, borrow money or restructure debts, reduce or delay expenditures, or increase capital, in order to establish whether they are feasible and likely to improve the situation.
- f the entity has prepared cash flow forecasts and their consideration is critical in the management's plans in respect of going concern, the auditor shall evaluate the reliability of the underlying data used in the forecasts and determine whether the assumptions underlying the forecast can be adequately supported by evidence. The analysis of the cash flow forecasts can also be extended by comparing forecasts for recent prior periods with historic results and the forecasts for the current period with actual results to date.
- Consideration of whether any additional facts or information have become available since the date of the management's assessment.
- Where management's assumptions include continued financial support by third parties and such support is important to the ability of the entity to continue as a going concern, the auditor may need to request written confirmations, including terms and conditions, from those third parties and to obtain evidence about their ability to provide support.
- Written representations from management regarding their future action plans and the feasibility of the plans.
- Performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity's ability to continue as a going concern.

On the basis of the evidence obtained, the auditor shall conclude whether a material uncertainty exists that may cast significant doubt about the ability of the entity to continue as a going concern.

(9 Marks)

[Total: 20 Marks]

SOLUTION 5

(a) Fundamental Principles

A member is required to comply with the following fundamental principles:

1. Integrity: A member shall be straightforward and honest in all professional and business relationships.
2. Objectivity: A member shall not allow bias, conflict of interest or undue influence of others to override professional or business judgments.
3. Professional Competence and Due Care: A member shall maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques. A member shall act diligently and in accordance with applicable technical and professional standards when providing professional services.
4. Confidentiality: A member shall respect the confidentiality of information acquired as a result of professional and business relationships and shall not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose. Confidential information acquired as a result of professional and business relationships shall not be used for the personal advantage of the member or third parties.
5. Professional Behaviour: A member shall comply with relevant laws and regulations and shall avoid any action that discredits the profession.

(8 Marks)

(b)

(i) An entity's mix of manual and automated elements in internal control varies with the nature and complexity of the company's use of IT.

Plato Ltd are a large company operating in multiple locations and have a number of subsidiaries. Having the correct IT and computer-based accounting systems in place can improve their internal controls. There should be less risk of errors and inter-operability between accounting software packages across locations and subsidiary companies.

Generally, IT and computer-based accounting benefits an company's internal control by enabling an entity to:

- Consistently apply predefined business rules and perform complex calculations in processing large volumes of transactions or data;
- Enhance the timeliness, availability, and accuracy of information;
- Facilitate the additional analysis of information;
- Enhance the ability to monitor the performance of the entity's activities and its policies and procedures;
- Reduce the risk that controls will be circumvented; and
- Enhance the ability to achieve effective segregation of duties by implementing security controls in applications, databases, and operating systems.

(6 Marks)

(ii) Plato Ltd are a large company operating in multiple locations and have a number of subsidiaries. However, even if the correct IT and computer-based accounting systems are in place, if errors occur the internal controls across all locations and subsidiary companies can be unreliable leading to further audit work and testing across all locations and subsidiary companies. Constant review between the IT and computer-based accounting systems and their inter-operability with the internal process are essential.

A company's IT environment and computer-based accounting system can also poses specific risks to an entity's internal control, including, for example:

- Reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both.
- Unauthorized access to data that may result in destruction of data or improper changes to data, including the recording of unauthorized or non-existent transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database.
- The possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties.
- Unauthorized changes to data in master files.
- Unauthorized changes to systems or programs.
- Failure to make necessary changes to systems or programs.
- Inappropriate manual intervention.
- Potential loss of data or inability to access data as required.

(6 Marks)

[Total: 20 Marks]