**MARKING GUIDE FOR AUDIT AND ASSURANCE TEST 1 2024**

**Question 1**

ISA 200 requires an audit to be performed in accordance with the following general principles.

1. **Compliance with the code of ethics** relating to an audit of financial statements issued by ICPAU and IFAC that requires an auditor to comply with the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.
2. **Perform an audit in accordance with International Standards on Auditing (ISAs)** thatprovide the basic principles and essential procedures. An audit should comply with all the ISAs relevant to the audit engagement and an auditor is required to state whether the audit complies with all relevant ISAs.
3. **Professional scepticism** is an attitude of a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud and a critical assessment of audit evidence. For example, the auditor should be alert to conditions which may indicate possible fraud.
4. **Professional judgment** is the application of relevant training, knowledge and experience in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement. For example professional judgment is required in determining the level of audit risk.
5. **Sufficient appropriate audit evidence** should be obtained during the audit in order to obtain reasonable assurance and reduce audit risk to an acceptably low level to enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion.

**(A mark for each properly explained principles, a mark for good presentation)**

**Question 2**

Ethical threats and safeguards.

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| **Ethical threats** | **Safeguards** |
| The finance director is the sister-in-law of the audit engagement partner that creates a familiarity and self-interest threat as both hold senior positions and therefore are in a position to influence the outcome of the audit. They may place their family relationship above the needs of the users of the financial statements. | The audit engagement partner should be removed and an alternative partner appointed. |
| Tina’s finance director has requested that a member of the audit team be seconded to fill the role of finance manager. A self-review risk arises if the team member prepares records and schedules which support the financial statements and is then part of the audit team responsible for auditing these. | Tanga & Co should clarify exactly which areas the seconded team member would assist Tina on. Though it is likely that as the finance manager, the team member will be directly involved in dealing with items related to the financial statements. As such, the request from the finance director should be declined, or the team member should be removed from the audit of Tina. |
| Two members of the audit team have significant loans owing to Team. Team is a financial institution and hence the provision of a loan is within the normal course of business. However, if either of the loans has any preferential terms, such as rates or repayment periods, then this would represent a self-interest threat. | The terms of the loans should be reviewed to ascertain whether they are in any way preferential. If not, no further action is required. However, if the terms are preferential then either the terms should be amended or these two members should be removed from the audit team. |
| Tina has requested that Tanga’s taxation department represents them in negotiations to resolve some outstanding issues with the tax authority. There is a potential advocacy threat where the firm may promote an opinion on behalf of Tina, such that the independence of the firm is compromised. In addition, the outcome of these issues may have a material impact on the financial statements, resulting in a self-review threat. | Assistance services must not be provided by a member of the audit team.  Independence review of audit work should be conducted by a reviewer who was not involved in providing the assistance.  Such services may not be provided if they involve the firm acting as an advocate for the audit client before the Tax Appeal Tribunal or court and the amounts involved are material to the financial statements being audited. |
| The taxation fees being quoted to Tanga are substantial. There is a potential self-interest threat as the total fees could represent a significant proportion of Tanga’s income and the firm could become overly reliant on Tina. | Tanga should assess whether audit, non-audit and total taxation fees would represent a significant proportion of recurring fee income. If the recurring fees are likely to be significant, additional consideration should be given as to whether the taxation and/or non-audit assignments should be undertaken by the firm. |
| The finance director has promised air tickets for the Dubai tour. This represents a self-interest as the acceptance of goods and services, unless insignificant in value, is not permitted. | As the air tickets to the audit team are of significant value, the offer should be politely declined. |

**(2 marks for each properly explained ethical threat and for each safeguard, total, 12 marks)**

**Question 3**

Audit risks and responses

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| Audit risk | Auditors response |
| Moon has decreased the selling price of products significantly since September 2024 and there are  increased levels of inventory expected at the year end. It is possible that the selling price may have fallen so that the net realisable value (NRV) of inventory is below cost.  IAS 2 *Inventory* requires inventory to be stated at the lower of cost and NRV. Hence it is possible that inventory is overvalued. | The auditor should undertake detailed cost and NRV testing to assess whether inventory is overvalued and requires write down. |
| A key customer of Moon has been experiencing financial difficulties and Moon has agreed a six-month payment break; however, the finance director does not believe an allowance is required. | If the six-months payment break has now ended, review after date cash receipts for this customer to assess whether any payments have been made. |
| If the customer is experiencing difficulties, there is an increased risk that the receivable is not recoverable and hence is overvalued. | Discuss with the finance director why he feels an allowance is not required. Review whether any general allowance for uncollectable accounts is sufficient to cover the amount of this receivable. |
| In light of the increased competition, reduction in selling price and financial difficulties of a key customer, there is an increased risk that Moon is facing going concern difficulties. | The auditor should undertake detailed going concern testing.  They should review the cash flow forecast for the foreseeable future to assess whether the going concern basis is appropriate or whether additional going concern disclosures are required in the financial statements. |
| The financial controller of Momo was dismissed in October and is threatening to sue the company for unfair dismissal.  If it is probable that Momo will make payment to the financial controller, a provision for unfair dismissal is required. If the payment is possible rather than probable, a contingent liability disclosure would be necessary. If Moon has not done this, there is a risk over the completeness of any provisions or contingent liabilities. | The audit team should write to the company’s lawyers to enquire of the existence and likelihood of success of any claim from the former financial controller. |
| The financial controller has been dismissed and his tasks have been allocated between the finance department team, this has increased their workload. | The team should remain alert throughout the audit for additional errors within the finance department. |
| This increases the inherent and control risk within Moon as errors may have been made within the accounting records by the overworked finance team members and there is no one working in a supervisory capacity. | In addition, discuss with the finance director whether he will be able to provide the team with assistance for any audit issues as there is no financial controller available. |
| The purchase ledger supervisor left in August and no reconciliations of supplier statements and purchase ledger control account have been performed. There is an increased risk of errors within trade payables and the year-end payable  may be under or overstated. | The audit team should increase their testing on trade payables at the year end, with a particular focus on completeness of payables. A detailed review of the year-end purchase ledger control account reconciliation should be performed with a focus  on any unusual reconciling items. |

**(2 marks for each properly explained risk and for each response, total, 12 marks)**