CERTIFIED ACCOUNTING TECHNICIAN

STAGE 3 EXAMINATIONS

S3.4 AUDIT AND ASSURANCE

DATE: TUESDAY, 27 AUGUST 2024

MARKING GUIDES AND MODEL ANSWERS

SECTION A

1	B
2	D
3	C
4	D
5	D
6	D
7	A
8	D
9	D
10	D

2 Marks for each correct answer
Total marks **20**

DETAILED MODEL ANSWERS

1. The correct answer is B.

Firms should have appropriate internal procedures to deal with potential independence problems, including:

- ✓ Internal rules, that for example no partners or staff should have shares in audit clients;
- ✓ Client acceptance procedures;
- ✓ An annual review of independence, both for the whole firm (circulation of a list of prohibited shareholdings) and for individual clients;
- ✓ Consultation procedures in cases of doubt.

Any additional safeguards required should be assessed by an independent partner, and might include second partner review of certain clients, rotation of the engagement partner or rotation of senior audit staff. In such circumstances, sole practitioners should consult another member externally.

A; C and D are among the safeguards mentioned above. Audit staff move to work at the audit client is an example of self-interest threats and Therefore, B is the correct

2. The correct answer is D.

ISA 210 states that in order to establish whether the preconditions of an audit are present the auditor is required to:

- ✓ Determine whether the financial reporting framework used is acceptable
- ✓ Obtain agreement from management that it acknowledges and understands its responsibility in respect of the following:
  - (i) For the preparation of the financial statements
  - (ii) For internal control relevant to the preparation of the financial statements
  - (iii) To provide the auditor with access to all information that is relevant to the preparation of the financial statements.

  This includes records and documents, additional information requested by the auditor for the purposes of the audit and unrestricted access to persons within the entity from whom the auditor wishes to obtain audit evidence.

If these preconditions are not present, the auditor must discuss the matter with management. If the situation cannot be resolved the engagement must not be accepted.

A statement that there may be circumstances where the actual form and content may differ from what was expected, is among the key content of the engagement letter that may be missed out. Therefore, the correct answer is D.

3. The correct answer is C.

Error is an unintentional misstatement in the financial statements, including the omission of an amount or a disclosure. On the other side, **Fraud** is an intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

The correct answer is C because the act of Director of Finance submits false invoice that he pretends are from a supplier, and then he approves them for payment, knowing the payment will actually go into a bank account belonging to him was done with intention. Therefore, this is a fraud.

But not posting the recorded transactions in various books of accounts to the respective accounts in ledger; mistakes in totaling or in carrying forward the totals to the next page and wrongly, writing it in a wrong account or on the wrong side of the account are unintentional misstatements.

4. The correct answer is D.

The auditor should develop an audit plan for the audit in order to reduce audit risk to an acceptably low level. As per ISA 300 ""*Planning an Audit of a Financial Report*", the audit plan includes:

- ✓ A description of the nature, timing and extent of planned risk assessment procedures sufficient to assess the risks of material misstatement.
- ✓ A description of the nature, timing and extent of planned further audit procedures at the assertion level for each material class of transactions, account balance and disclosure. This will include tests of controls and substantive procedures.
- ✓ Any other audit procedures required for the engagement to comply with ISAs.

Consider available time, staff and technical expertise is among the acceptance procedures to be carried out before the auditor accept an appointment. Therefore, the correct answer is D.

5. The correct answer is D.

It is important to understand that fair presentation/true and fair does not mean absolutely correct. Auditors cannot say that financial statements are absolutely correct because:

- ✓ Financial statements are a combination of fact and judgement.
- ✓ An audit also includes judgements made by the auditors.
- ✓ Auditors do not test every transaction (or audits would be too expensive).
- ✓ Company management might tell lies/carry out hidden fraud which the auditors do not detect.

Auditors use selective testing, rather than testing every transaction; The inherent limitations of internal control. (Internal controls rely on human diligence and compliance, but there is always a risk of people failing to follow the correct procedures, or doing the wrong thing.) and The fact that much of the evidence available to the auditor is persuasive rather than conclusive are among the factors that to provide absolute assurance would be very difficult to the auditors' side. Therefore, the correct answer is D.

6. The correct answer is D.

There are many sources of information available to the auditor at this stage including interim financial information, budgets, management accounts, information for prior periods and industry information.

All of this information can be used by auditors to help them understand areas of risk. For example, ratios (such as the receivables days, inventory turnover and the current ratio) can be calculated using information from the financial statements. The financial statements can also be compared to prior years, or similar firms in the same industry.

Budgets are helpful in indicating the expectations of the organization, and management accounting information is useful for variance analysis. Variance analysis involves looking at actual income and expenditure against the expected figures and determining the reasons for any variances between the two.

Analytical procedures such as these can be extremely helpful at the risk assessment and planning stages of an audit and help the auditor to identify the areas of greatest risk, and therefore the areas where the risk of misstatement in the accounts is highest. These are the areas where the most work will be required during the audit. Therefore, the correct answer is B.

7. The correct answer is A.

Most accounting frameworks, for example, that provided by IAS 1 Presentation of financial statements, require management to make an explicit assessment of the entity's ability to continue as a going concern. However, some do not. Accordingly, the revised ISA 570 includes a reminder that 'the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for future events or conditions that may cause an entity to cease to continue as a going concern.

The auditor cannot predict such future events or conditions. Accordingly, the absence of any reference to a material uncertainty about the entity's ability to continue as a going concern in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a going concern.

when management are making an assessment on going concern, ***the following factors should be considered:***

- ✓ The degree of uncertainty about the events or conditions being assessed increases significantly the further into the future the assessment is made.
- ✓ Judgements are made on the basis of the information available at the time.
- ✓ Judgements are affected by the size and complexity of the entity, the nature and condition of the business and the degree to which it is affected by external factors.

Status of items involving subjective judgement/accounted for using preliminary data is among the audit procedures in testing subsequent events. Therefore, the correct answer is A.

8. The correct answer is D.

Analytical procedures are formulas and processes that compare financial data to non-financial data in order to determine relationships between the two.
Analytical procedures also help auditors investigate variations in figures that have shown consistency in the past or do not correlate with other values
There are many sources of information available to the auditor at this stage including interim financial information, budgets, management accounts, information for prior periods and industry information. Therefore, D is the correct answer as long all the scenarios provided are considered as analytical procedure.

9. The correct answer is D.

All members and students of the ICPAR are subject to the provisions of the ICPAR Code of Ethics, which conforms with the requirements of the IESBA Code of Ethics. Guidance is in the form of:

- ✓ Fundamental principles.
- ✓ Specific guidance and notes.

The fundamental principles Members and students must comply with the five fundamental principles set out in IESBA Code of Ethics. ***Those are:***

- ✓ **Integrity:** To be straightforward and honest in all professional and business relationships.
- ✓ **Objectivity:** Not to compromise professional or business judgements because of bias, conflict of interest or undue influence of others.
- ✓ **Professional competence and due care:** To attain and maintain professional knowledge or skill at the level required to ensure that a client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation. And to act diligently and in accordance with applicable technical and professional standards.
- ✓ **Confidentiality:** To respect the confidentiality of information acquired as a result of professional and business relationships.
- ✓ **Professional behavior:** To comply with relevant laws and regulations and avoid any action that the professional accountant knows or should know might discredit the profession.

Self-review is among the circumstances that threat compliance with the above fundamental principles reason why it’s not among the correct option. Therefore, D is the correct answer.

10. The correct answer is D.

A, B and C are not the correct answer to define the preliminary judgment about materiality.
The preliminary judgment about materiality is the **maximum** amount by which the auditor believes the statements could be misstated and still not affect the decisions of reasonable users

SECTION B

QUESTION 11

Marking guide **Marks**

a) Explaining the going concern concept **1**
b) Providing three factors that should be taken into consideration by management when making an assessment of going concern in the company (1 mark – each). **3**
c) Procedures that should be carried out by an auditor to ascertain the completeness of costs attributed to production (*1 marks-each*). **6**
Total marks **10 marks**

Model answers

a) Explaining the term "Going concern concept"

Going concern is an accounting term for a company that is financially stable enough to meet its obligations and continue its business for the foreseeable future.

Under the going concern basis of accounting the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. Assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.

b) Factors that should be taken into consideration by management when making an assessment of going concern in the company.

The auditor's responsibilities are to obtain sufficient appropriate audit evidence regarding, and conclude on, the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements, and to conclude, based on the audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern.

When management are making an assessment, the following factors should be considered:

- ✓ The degree of uncertainty about the events or conditions being assessed increases significantly the further into the future the assessment is made.
- ✓ Judgements are made on the basis of the information available at the time.
- ✓ Judgements are affected by the size and complexity of the entity, the nature and condition of the business and the degree to which it is affected by external factors.

c) Audit procedures that should be carried out by an auditor to ascertain the completeness of costs attributed to production

The audit procedures will depend on the methods used by the client to value work in progress and finished goods, and on the adequacy of the system of internal control. The auditors should consider what tests they can carry out to test the reasonableness of the valuation of finished goods and work in progress. Analytical procedures may assist comparisons being made with items and categories from the previous year's summaries. If the client has a computerized accounting system, the auditors may be able to request an exception report listing, for example, all items whose value has changed by more than a specified amount. A reasonableness test will also provide the auditors with assurance regarding completeness.

To determine the costs attributable to production, the auditor should carry out *the following procedures:*

For materials:

- ✓ Agree the valuation of raw materials to invoices and price lists to confirm accuracy.
- ✓ Confirm appropriate basis of valuation (eg FIFO) is being used to ensure that this is in accordance with IAS 2 and company policy.
- ✓ Confirm correct quantities are being used when calculating raw material value in work in progress and finished goods to confirm valuation.

For labour costs:

- ✓ Agree labour costs to wage records to determine whether the labour cost included is reasonable.
- ✓ Review standard labour costs in the light of actual costs and production.
- ✓ Agree labour hours to time summaries to confirm that the number of hours allocated to production is reasonable.

QUESTION 12

Marking guide	**Marks**
(a) Four considerations that should be taken into account by the auditor during examination of the accounting policies used by the company. (*1 mark for a valid consideration*).	4 marks
(b) To describe the two types of events after reporting period. (*0.5 mark for listing each type and 1 mark for correction explanation provided – maximum of 3 marks*).	3 marks
(c) Key areas of concern when auditor is testing tangible non-current assets (*1 mark each – maximum of 3 marks*).	(3 marks)
Total marks	**10 marks**

Model answers

(a) Four considerations that should be taken into account by the auditor during examination of the accounting policies used by the company.

Auditors must perform and document an overall review of the financial statements before reaching an opinion. This review should include a review of accounting policies and a review for consistency and reasonableness

This review of the financial statements, in conjunction with the conclusions drawn from the other audit evidence obtained, gives the auditors a reasonable basis for their opinion on the financial statements. It should be carried out by a senior member of the audit team, with appropriate skills and experience.

When examining the accounting policies, auditors should consider:
- ✓ Policies commonly adopted in particular industries.
- ✓ Policies for which there is substantial authoritative support.
- ✓ Whether any departures from applicable accounting standards are necessary for the financial statements to give a true and fair view.
- ✓ Whether the financial statements reflect the substance of the underlying transactions and not merely their form.

(b) To describe the two types of events after reporting period.

Event after the reporting period: An event, which could be favourable or unfavourable, that occurs between the end of the reporting period and the date that the financial statements are authorized for issue.

- ✓ **Adjusting event:** An event after the reporting period that provides further evidence of conditions that existed at the end of the reporting period, including an event that indicates that the going concern assumption in relation to the whole or part of the enterprise is not appropriate.
- ✓ **Non-adjusting event:** An event after the reporting period that is indicative of a condition that arose after the end of the reporting period.

(c) Key areas of concern when auditor is testing tangible non-current assets.

Non-current assets can be both “tangible” and “intangible.” Tangible non-current assets are the physical property, plant, and equipment that the business owns. They are the main form of assets in most industries and *include:*
- ✓ Buildings
- ✓ Land
- ✓ Machinery
- ✓ Vehicles (company cars, trucks, forklifts)
- ✓ Tools
- ✓ Computer equipment

The key areas when testing tangible non-current assets are:
- ✓ Confirmation of ownership.
- ✓ Inspection of non-current assets.
- ✓ Valuation by third parties.
- ✓ Adequacy of depreciation rates.

SECTION C

QUESTION 13

Marking guide **Marks**

a) Two types of confirmation (*1 mark each for listing each type and 1 mark for valid explanation – maximum of 4 marks*). **4**

b) Basic audit procedures that should be designed and performed by the auditor in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement (*1 mark each* – maximum of 5 marks). **5**

c) Principal procedures which may be carried out by auditors when attending a physical inventory count. (*1 mark each* – maximum of 5 marks). **5**

d) Elaborate the tests of controls performed by the auditor to obtain evidence that the client is carrying out adequate checks on the calculations of payroll. (*1 mark each procedure- 6 marks maximum*). **6**

Total marks **20 marks**

Model answers

a) Briefly describe Two types of confirmation that should be sent to the company's customers.

Testing accounts receivable by obtaining confirmation from customers (accounts receivable confirmation) is an example of obtaining written confirmations from third parties as audit evidence.

ISA 505 External confirmations cover confirmation of accounts receivable. It is intended to assist the auditor in designing and performing external confirmation procedures to obtain relevant and reliable audit evidence.

The ISA indicates that audit evidence in the form of external confirmations received directly by the auditor from confirming parties may be more reliable than evidence generated internally by the entity. This is because it is obtained from an independent source outside the entity, it is obtained directly by the auditor, and is in documentary form.

The verification of trade accounts receivable by direct communication is therefore the normal means of providing audit evidence to satisfy the objective of confirming whether customers exist and owe bona fide amounts to the company (existence and rights and obligations).

Types of confirmation

- ✓ **A positive confirmation request** is a request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

- ✓ **A negative confirmation request** is a request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.

b) Briefly explain the basic audit procedures that should be designed and performed by the auditor in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement.

Part of ISA 501 Audit evidence – specific considerations for selected items covers contingencies relating to litigation and legal claims, which will represent the major part of audit work on contingencies. Litigation and claims involving the entity may have a material effect on the financial statements, and so will require adjustment to/disclosure in those financial statements.

The following procedures should be performed to identify litigation and claims involving the entity which may give rise to a risk of material misstatement:

- ✓ Make appropriate inquiries of management including obtaining written representations.
- ✓ Review minutes of those charged with governance and correspondence with the entity's legal counsel.
- ✓ Examine legal expense account.
- ✓ Use any information obtained regarding the entity's business including information obtained from discussions with any in-house legal department.
- ✓ Obtain details of all provisions which have been included in the financial statements and all contingencies that have been disclosed.
- ✓ Obtain a detailed analysis of all provisions showing opening balances, movements and closing balances.
- ✓ Determine for each material provision whether the company has a present obligation as a result of past events by:
  – Review of correspondence relating to the item
  – Discussion with the directors. Have they created a valid expectation in other parties that they will discharge the obligation?
- ✓ Determine for each material provision whether it is probable that a transfer of economic benefits will be required to settle the obligation by:
  – Confirming whether any payments have been made after the end of the reporting period in respect of the item, or whether any events occurring up to the date of the auditor's report provide evidence regarding the provision
  – Review of correspondence with lawyers, banks, customers, insurance company and suppliers both pre and post period end:
  – Sending a letter to the lawyer to obtain their views (where relevant)

– Discussing the position of similar past provisions with the directors. Were these provisions eventually settled?
– Considering the likelihood of reimbursement x Recalculate all provisions made to confirm accuracy.

- ✓ Compare the amount provided with any payments after the period end and with any amount paid in the past for similar items to obtain evidence of valuation.
- ✓ In the event that it is not possible to estimate the amount of the provision, confirm that this contingent liability is disclosed in the financial statements.
- ✓ Consider the nature of the client's business to determine whether other provisions may be required.
- ✓ Consider adequacy of disclosure of provisions, contingent assets and contingent liabilities.

c) Elaborate the principal procedures which may be carried out by auditors when attending a physical inventory count.

The following are the principal procedures which may be carried out by auditors when attending a physical inventory count:

Gain understanding	-Review previous year's arrangements -Perform analytical procedures -Discuss with management inventory count arrangements and significant changes
Assess key factors	-The nature and volume of the inventory. -Risks relating to inventory. -The identification of high value items. -Method of accounting for inventory. -Location of inventory and how it affects inventory control and recording. -Internal control and accounting systems to identify potential areas of difficulty. -Possible internal audit involvement.
Plan procedures	-Ensure a representative selection of locations, inventory and procedures are covered. -Ensure sufficient attention is given to high value items. -Arrange to obtain from third parties' confirmation of inventory they hold. -Consider the need for expert help.

d) Elaborate the tests of controls performed by the auditor to obtain evidence that the client is carrying out adequate checks on the calculations of payroll.

- ✓ Review payroll and HR job descriptions and company policies on the payroll process, to evaluate whether proper segregation of duties is in place.
- ✓ Review a sample of starters and leavers in the year and verify that the correct documentation is in place.
- ✓ Review the entity's procedures for reporting changes to the payroll department.
- ✓ Obtain evidence of authorization of standing data in payroll system.
- ✓ Review and test authorization procedures for hiring staff, wage rates, overtime etc.

- ✓ Observe employees' use of clocking-in procedures.
- ✓ Inspect a sample of clock-cards/timesheets for evidence of approval by the appropriate level of management.
- ✓ Review documentary evidence that a sample of payroll calculations have been independently reperformed by entity staff.
- ✓ Test operation of computerized controls eg range checks.
- ✓ Inspect documentary evidence of management's review of agreement of gross earnings and total tax deducted to taxation returns.
- ✓ Examine paid cheques or a certified copy of the bank list for evidence of proper authorization.
- ✓ Where wages are paid in cash attend the pay-out and observe procedures.
- ✓ Review payroll budgeting procedures adopted by the client.
- ✓ Review reconciliation of the payroll master file to the wages and salaries account in the general ledger.
- ✓ Review procedures for classifying payroll costs to ensure that costs are not incorrectly capitalised.

QUESTION 14

Marking guide	**Marks**
a) Acceptance procedures that a nominee auditor should carry out before they accept an appointment. (*1.5 marks on each valid procedure – maximum of 4 marks*).	**4**
b) Briefly describes Two types of possible disclosure (1 mark for listing and 1 mark for valid explanation per each type – maximum of 4 marks).	4
c) Elaborate key consideration that the audit partner should take into account to ensure communication between the client and audit staff. (*1 mark each*).	4
d) Elaborate content of permanent audit file to your audit manager. (*1 mark each*).	8
Total marks	**20 mark**s

Model answers

(a) Acceptance procedures that a nominee auditor should carry out before accepting an appointment.

Before a new audit client is accepted, the auditors must ensure that there are no independence or other ethical problems likely to cause conflict with the ethical code.

Furthermore, new auditors should ensure that they have been appointed in a proper and legal manner. Before they accept an appointment, nominee auditors must carry out the *following procedures:*

Ensure professionally qualified to act	Consider whether they could be disqualified on legal or ethical grounds
Ensure existing resources adequate	Consider available time, staff and technical expertise.
Obtain references	Make independent enquiries if directors are not personally known.
Communicate with present auditors	Enquire whether there are any professional or other reasons for not accepting nomination; also, courtesy to the outgoing auditor.

(b) Briefly describes Two types of possible disclosure

Auditors have a professional duty of confidentiality. However, they may be compelled by law, or consider it desirable in the public interest, to disclose details of clients' affairs to third parties. *See below table for more details on types of disclosure*

Obligatory disclosure	**Voluntary disclosure**
✓ If a member knows or suspects his client to have committed the offence of treason, he is obliged to disclose all the information at his disposal to a competent authority. Suspicions of terrorism or money laundering also give rise to a duty to report.	✓ In certain cases, voluntary disclosure may be made by the member where: – Disclosure is reasonably necessary to protect the member's interests, for example to enable him to sue for fees or defend an action for, say, negligence. – Disclosure is authorized by statute, for example where in an action a member is required to give evidence or discovery of documents. – There is a public duty to disclose, say where an offence has been committed which is contrary to the public interest. – Disclosure to non-governmental bodies (where statutory powers exist).

(c) Elaborate key consideration that the audit partner should take into account to ensure communication between the client and audit staff.

Ensuring communication between client staff and audit staff will be more difficult as the audit engagement partner is unlikely to visit the client site during the audit. However, given that the audit partner has a responsibility here, he/she must take appropriate steps. What these should be will depend on the individual circumstances of the audit. *The audit engagement partner should consider the following:*

- ✓ Keeping in regular contact with both audit and client staff during the audit to assess the level of communication between them.
- ✓ Attending the site during the audit to facilitate better communication if he feels that it is necessary.
- ✓ Fostering lines of communication between client staff and audit staff during the period between audits, to ensure a good working relationship is built up between them.
- ✓ The availability of audit staff throughout the engagement (taking into account conflicting audit deadlines, holidays and study leave).

(d) Elaborate the contents of a permanent audit file to your audit manager.

Permanent audit files contain information of continuing importance to the audit. ***They contain:***

- ✓ Engagement letters.
- ✓ New client questionnaire.
- ✓ The memorandum and articles.
- ✓ Other legal documents such as prospectuses, leases, sales agreement.
- ✓ Details of the history of the client's business.
- ✓ Board minutes of continuing relevance.
- ✓ Previous years' signed accounts, analytical procedures and management letters.
- ✓ Accounting systems notes, previous years' control questionnaires.

QUESTION 15

Marking guide	**Marks**
a) Types of audit opinions that can be issued by auditor. (*1 mark for each type of opinion and 1.5 marks for valid explanation)*.	10
b) Define the term "Internal controls system" and elaborate objective of management in setting up an internal control in the accounting system (*1mark for definition and 1 mark for a correct objective well stated – maximum of 5 marks*).	5
c) Elaborate control activities related to o the ordering and credit control process (*1 mark for a correct control activity – maximum of 5 marks*).	5
Total marks	**20 mark**s

Model answers

(a) Types of audit opinions that can be issued by auditor.

- ✓ **An unmodified opinion** is the opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

  ISA 700 states that the auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

- ✓ **Qualified opinions**: A qualified opinion must be expressed in the auditor's report in the following two situations:
  - ✓ The auditor concludes that misstatements are material, but not pervasive, to the financial statements.

    Material misstatements could arise in respect of:

    -The appropriateness of selected accounting policies

-The application of selected accounting policies
-The appropriateness or adequacy of disclosures in the financial statements

- ✓ The auditor cannot obtain sufficient appropriate audit evidence on which to base the opinion but concludes that the possible effects of undetected misstatements, if any, could be material but not pervasive.

- ✓ The auditor's inability to obtain sufficient appropriate audit evidence is also referred to as a limitation on the scope of the audit and could arise from:
  -Circumstances beyond the entity's control (eg accounting records destroyed).
  -Circumstances relating to the nature or timing of the auditor's work (eg the timing of the auditor's appointment prevents the observation of the physical inventory count).
  -Limitations imposed by management (eg management prevents the auditor from requesting external confirmation of specific account balances).

- ✓ **Adverse opinions**: An adverse opinion is expressed when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements are both material and pervasive to the financial statements. The table below gives one example of why an adverse opinion might be expressed for each of the three possible reasons for misstatements being determined as pervasive.

- ✓ **Disclaimers of opinion**: An opinion must be disclaimed when the auditor cannot obtain sufficient appropriate audit evidence on which to base the opinion and concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive. The opinion must also be disclaimed in situations involving multiple uncertainties when the auditor concludes that, despite having obtained sufficient appropriate audit evidence for the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

(b) Define the term "Internal controls system" and elaborate objective of management in setting up an internal control in the accounting system

An internal control system is the safety net of a well-run organization. By considering financial aspects as well as operational and strategic dimensions, an ICS ensures the smooth, efficient, and legally compliant execution of business processes.

With the help of an internal control system, companies can record, evaluate, and manage risks related to their documented processes. What is more, clearly regulated control processes ensure that employees understand and comply with the established rules.

Objective of management in setting up an internal control in the accounting system

Management of an entity may set up internal controls in the accounting system to assess the following:

- ✓ Transactions are executed in accordance with proper authorization.
- ✓ All transactions and other events are promptly recorded at the correct amount, in the appropriate accounts and in the proper accounting period.
- ✓ Access to assets is permitted only in accordance with proper authorization.
- ✓ Recorded assets are compared with the existing assets at reasonable intervals and appropriate action is taken with regard to any differences.

(c) Elaborate control activities related to o the ordering and credit control process.

The following control activities relate to the ordering and credit control process; note the importance of controls over credit terms, ensuring that goods are only sent to customers who are likely to pay promptly:

- ✓ Segregation of duties; credit control, invoicing and inventory dispatch.
- ✓ Authorization of credit terms to customers:
  – References/credit checks obtained
  – Authorization by senior staff – Regular review
- ✓ Authorization for changes in other customer data"
  – Change of address supported by letterhead
  – Requests for deletion supported by evidence balances cleared/customer in liquidation
- ✓ Credit limits confirmed before new orders are accepted.
- ✓ Sequential numbering of blank order documents.
- ✓ Matching of customer orders with production orders and dispatch notes.

End of Marking Guide and Model Answers