2023 FULL AUDIT COMPETENCE PRACTICE EXAMINATION (CPE)

QUESTION ONE

BACKGROUND

Nyeleti Chartered Accountants is an accountancy firm which is duly registered with the Zambia Institute of Chartered Accountants (ZiCA). It is licensed to offer both assurance and non-assurance services. The firm is a result of a merger of two (2) small accountancy firms which happened in 2004. As a result of the merger, Nyeleti Chartered Accountants is now able to attract even listed companies. Most of the operations and systems for listed companies are computerized.

The firm currently has seven (7) partners, twelve (12) managers and thirty (30) employees at various levels. The firm is profitable and employees are reasonably remunerated. Labour turnover is very low compared to other accountancy firms within the industry. The firm is currently developing detailed policies on human resource management (HRM) which will incorporate compliance with legal provisions and a specific policy of social media.

The firm has integrated Computer Assisted Audit Techniques (CAATs) in its audit methodology. This is clearly reflected in the audit approach to planning, testing and reporting. Nyeleti Chartered Accountants ensures all audit staff have appropriate data analytics skills and experience. CAATs continues to be very instrumental, especially when auditing listed companies. However, a number of disadvantages of CAATs do exist.

A month ago, officers from the Practice Review Department of the Zambia Institute of Chartered Accountants (ZiCA) visited Nyeleti Chartered Accountants. The outcome of the visit has been classified as partly **"Un*satisfactory*"**. The Managing Partner wants a detailed analysis of the entire Audit Monitoring Report.

You are a Senior Audit Manager in Nyeleti Chartered Accountants and you are currently responsible for the following assignments:

(1) Analysis of the Audit Monitoring Report.

(2) Mpandila Ltd – Ethical and professional issues.

(3) Hamasamu Plc – Business advisory services.

(4) Daka Plc – Audit of the financial statements for the year ended 31 March 2023.

(5) Kapapa Ltd – Audit of the financial statements for the year ended 30 June 2023.

ANALYSIS OF THE AUDIT MONITORING REPORT

The report contained findings from the review of the firm and three (3) audit files:

- **Review of the firm** – The firm's mission statement includes a phrase that "quality must follow profitability".
- **File no. 1** – No risk assessment was conducted in respect of the financial statement audit for the client. A note from the Audit Senior stated that since the internal audit function also integrates Computer Assisted Audit Techniques (CAATs) in its methodology and recently conducted a risk assessment, the audit team decided to rely on the internal audit function's work.
- **File no**. **2** – The written representation letter was not dated and signed.
- **File no**. **3 –** No confirmation was obtained from the Managing Director (MD) regarding unretired imprest of K2 million. The Audit Senior stated that this is handled by a special committee appointed by Cabinet Office. However, there was no written evidence on the matter from Cabinet office. The audit opinion was unmodified.

MPANDILA LTD

Mpandila Ltd is an exclusive women's shop that sells only coats of famous international brands. It was incorporated in the year 2019 and started operations immediately. On 1 August 2022, Nyeleti Chartered Accountants was appointed as external auditors of Mpandila Ltd. The audit of the financial statements for Mpandila Ltd for the year ended 31 December 2022 is about to start. You are have been asked to evaluate the following ethical and professional issues which were identified during the planning meetings with management and those charged with governance:

(1) One (1) of the audit seniors has been seconded to Mpandila Ltd for the past eight (8) months and is expected to return to Nyeleti Chartered Accountants before the audit work commences. The Managing Partner is excited that the audit of Mpandila Ltd will be easy.

(2) The majority shareholder of Mpandila Ltd has been appointed as a District Commissioner (DC) for a newly created district with immediate effect.

(3) The Director of Finance of Mpandila Ltd has requested that a certain audit senior be assigned to the audit team.

(4) Management has promised to provide the audit team with snacks and refreshments throughout the period of audit.

(5) The audit fee represents eight percent (8%) of the firm's income. Mpandila Ltd is considering a major new project and has asked Nyeleti Chartered Accountants if it would be happy to undertake some one-off consultancy work. It is possible that the fee income for this contract would represent 10% of that year's income for Nyeleti Chartered Accountants. The Consultancy Department of Nyeleti Chartered Accountants is keen to take on the work.

(6) A Junior Auditor has shared a post on social media which accuses the Chief Accountant of having an intimate relationship with the Accountant-in-Charge (AIC).

HAMASAMU PLC

The Finance Director (FD) of Hamasamu Plc, an audit client, contacted the Managing Partner on 16 November 2023 regarding engagement of a tax expert to assist in resolving a tax dispute with the Zambia Revenue Authority (ZRA) involving transfer pricing. One (1) of the Senior Auditors in Nyeleti Chartered Accountants has drafted the following advertisement, which the Managing Partner wants you to evaluate given the sensitivity of the matter:

Hamasamu Plc

Required: Tax Expert

Hamasamu Plc is one (1) of the largest reputable Zambian mining company.

The company is looking for the services of Chartered Accountants as tax experts. Interested firms should submit their detailed proposal.

This should be delivered to:

The Managing Director,

Hamasamu Plc,

Lusaka.

Sealed Envelopes should be deposited at company's head office or emailed to info@hamasamuplc.com by 8th December 2023 at 14:30hrs. Proposals received after the deadline will not be accepted.

For more information you can email us at info@hamasamuplc.com or visit our website at www.hamasamuplc.com

On 20 November 2023, an initial meeting between the Managing Partner and the Finance Director (FD) of Hamasamu Plc was held. The notes from the meeting are given below:

Notes from the meeting with the Finance Director

Hamasamu Plc is a Zambian resident subsidiary of a foreign based Multinational Mining Company. The company is engaged in mining operations of base metals and precious metals.

On 1 October 2023, the Zambia Revenue Authority (ZRA) commenced a field tax audit at the head office for Hamasamu Plc. However, during the course of the tax audit, the tax auditors suspected that serious tax offences had occurred on transfer pricing and reconstituted the audit as an investigation.

The company does not want to use Nyeleti Chartered Accountants for ethical reasons.

DAKA PLC

Daka Plc is listed on the Lusaka Securities Exchange (LuSE) and its principal activity is the manufacture and sale of affordable memory chips. The audit plan for the audit of the financial statements for the year ended 30 September 2023 is almost complete. The following are some of the audit responses suggested by the Audit Senior in respect of the audit risks identified:

Audit risks	Audit responses
(1) Delivery vans – six (6) out of eighteen (18) delivery vans were sold during the year, resulting in significant losses. There is a risk that an impairment review has not been conducted, resulting in the overstatement of both non-current assets and profit.	Carry out an impairment review as guided by IAS 36 *Impairment of assets.* The remaining delivery vans should be tested for impairment by comparing their recoverable amount with their carrying amount.
(2) Government – more than fifty percent (50%) of the company's sales are made to Government institutions. This business relationship is inherently risky as it is significantly affected by politics. Various items in the financial statements could be affected by this inherent risk. This could ultimately lead to Daka Plc having going concern issues.	Obtain contracts with Government institutions and review the specific details. Review correspondence with Government institutions and take note of any indicators of political interference. Seek legal advice especially on important clauses regarding termination of contract.
(3) Convertible bonds – there is a risk that the valuation of these may not be in line with IFRS 9 *Financial Instruments.*	Carry out substantive procedures designed to detect material misstatements regarding the valuation.

(4) First audit - Nyeleti Chartered Accountants were appointed recently. There is a high detection risk mainly due to not have sufficient knowledge of the business.	Use only qualified and experienced audit staff.
(5) Research and development – Daka Plc has capitalized K15 million of the research and development cost. There is a risk that the capitalized amount does not meet the criteria laid down in IAS 38 *Intangible assets.*	Obtain a breakdown of the capitalized cost and check against relevant supporting documents e.g. invoices

KAPAPA LTD

Kapapa Ltd, a major player in the energy sector, is owned by the Government of the Republic of Zambia. The demand for energy has significantly increased over the last five (5) years as a result of increased business activities, especially in the informal sector. The informal sector continues to grow every year and it is expected that total energy requirement will double by the year 2027.

On 30 June 2023, the directors approved the acquisition of modern computerized machinery to improve company operations. This followed a detailed presentation by Finance Director (FD) regarding the acquisition decision. The evaluations presented by the Finance Director (FD) consistently showed positive net present values (NPVs) under different scenarios. However, the financing decision had to be delayed since the board was concerned about the rise in the interest rates which followed the increase in the policy rate by the Bank of Zambia (BOZ). On 1 September 2023, the board finally approved funding through $17 million, two per cent (2%) twelve (12) year Green Bonds.

Kapapa Ltd offer a thirty (30) day credit to all customers. The receivables are managed by a qualified ZiCA accountant, while the payables are managed by a ZiCA intern who was the best student in Financial Accounting two (2) years ago. There are no reported problems in the management of both receivables and payables. Most of the spare parts are imported and foreign suppliers demand advance payments. The labour turnover rate for technical staff at the end of the year 2023 showed an increase of thirty percent (30%) compared to the year 2022.

On 1 November 2023, Nyeleti Chartered Accountants was appointed as auditor of Kapapa Ltd for the financial statements for the year ending on 31 December 2023. The Audit Senior in charge of the financial statement audit for Kapapa Ltd has stated that he has no idea on Green Bonds and would require assistance.

SECTION A

Required:

(1) Critically analyze the findings contained in the Audit Monitoring Report. (18 marks)

(2) Making particular reference to Nyeleti Chartered Accountants, where necessary:

(a) State three (3) main contents of a social media policy and explain the importance of compliance with the laws when developing Human Resources Management (HRM) policies. (9 marks)

(b) Explain four (4) practical disadvantages which the audit teams usually encounter when using Computer Assisted Audit Techniques (CAATs). (8 marks)

(3) For the financial statement audit of Mpandila Ltd:

(a) Evaluate the six (6) ethical and professional issues. (9 marks)

(b) Provide a recommendation to address each ethical and professional issue. (6 marks)

[Total: 50 marks]

SECTION B

Required:

(4) Using the information given in respect of Hamasamu Plc, identify and explain six (6) key deficiencies of the advertisement. (12 marks)

(5) Using the information given in respect of Daka Plc, evaluate each audit response proposed by the Audit Senior in respect of the audit risks identified, and suggest any relevant amendments, where necessary. (15 marks)

(6) Making reference to the information given in respect of Kapapa Ltd, where appropriate:

(a) Explain the nature of Green Bonds and recommend five (5) appropriate audit procedures to be carried out regarding the Green Bonds. (13 marks)

(b) Explain any five (5) business risks. (10 marks)

[Total: 50 marks]

QUESTION TWO

BACKGROUND

Moyo Associates is a medium-sized accountancy firm. It is registered with the professional bodies in Zambia, Zimbabwe and South Africa. The head office is in Lusaka and it has branches in Harare and Pretoria. Most of its clients are in the agriculture, mining, local authorities and hospitality industries. The foreign offices are independently run by qualified local professionals in the respective countries.

You are an Audit Manager responsible for the following engagements:

(1) Evaluation of the deficiency letter received from the Zambia Institute of Chartered Accountants (ZiCA).

(2) Audit of Constituency Development Fund (CDF).

(3) Audit of the financial statements for Omusati Ltd for the year ended 31 December 2023.

(4) Audit of the financial statements for Ottawa Plc for the year ended 30 September 2023.

(5) Evaluation of suggested audit opinions for three (3) clients.

EVALUATION OF THE DEFICIENCY LETTER RECEIVED FROM THE ZAMBIA INSTITUTE OF CHARTERED ACCOUNTANTS (ZICA)

The Zambia Institute of Chartered Accountants (ZiCA) in conjunction with the Financial Intelligence Centre (FIC) recently conducted a motoring exercise at Moyo Associates. The findings are in the draft deficiency letter and among the key deficiencies are the following:

- Identification of customer that is not physically present – Moyo Associates did not carry out any identification procedures since the client had no physical presence in the Republic of Zambia.
- Tipping – off offence – Moyo Associates, acting as independent professionals, formed a suspicion of money laundering against a new client but went ahead and conducted a customer identification and verification requirement which resulted in tipping off the client, who has since left the country.
- Prevention of compliance with the obligations under the Financial Intelligence (FIC) Act – The Managing Partner stated that the laws in the foreign branches do not require observance of the Financial Intelligence Centre (FIC) Act obligations and no training has been offered for the foreign staff members.

- Misleading information – The Managing Partner gave misleading information to FIC inspectors regarding an enquiry by the inspectors concerning the wire transfers between the foreign branches and head office.

You have been requested to prepare briefing notes which will be used to prepare responses to the Zambia Institute of Chartered Accountants (ZiCA) and the Financial Intelligence Centre (FIC). The Managing Partner thinks the appointment of a Compliance Officer could significantly reduce the deficiencies.

AUDIT OF CONSTITUENCY DEVELOPMENT FUND (CDF)

The Government of the Republic of Zambia has prioritized Decentralisation as a major driver for attaining development, reducing poverty and supporting job creation through citizen engagement and participation at the local level. To actualize Decentralisation in line with the Constitution, Government has decided to take significant resources from the National to the Local Government level.

Last month, the Auditor-General (AG) appointed Moyo Associates to audit the utilization of the Constituency Development Fund (CDF) in two (2) constituencies. The audits are at various stages as follows:

Constituency one

Risk assessment has been completed and Constituency one has been assessed as high risk especially that segregation of duties is almost non-existent and most members of staff are unqualified. The audit team has requested for guidance on the audit procedures to be performed regarding the figure for fuel consumption for the earth moving equipment which was commissioned by the District Commissioner (DC) four (4) months ago.

All works are approved by the Works Committee and implementation is done by Council employees. Fuel is supplied by a local private filling station based on approved orders by the Town Clerk. The internal auditors undertake pre-audits for all fuel payments.

Constituency two

The audit is almost complete and you have been asked to evaluate the sufficient and appropriateness of the audit evidence obtained in respect of the following matters:

(1) Constituency two is involved in a court case with a local contractor which is demanding damages in respect of the illegal termination of a contract. The evidence obtained is a written management representation letter. The damages claimed are considered material.

(2) A comparison of the current figure for accounts payables with that for last year indicated possible understated. The audit team has obtained reconciliations with supplier year-end statements.

(3) At the year-end, Constituency two had a number of capital work-in-progress. These were all physically inspected by the audit team and no further procedures relevant to these items have been performed.

(4) Audit of payments involved confirming that the internal auditors had undertaken pre-audits for all payments by reviewing the payment vouchers and supporting documentation.

AUDIT OF THE FINANCIAL STATEMENTS FOR OMUSATI LTD FOR THE YEAR ENDED 31 DECEMBER 2023

Omusati Ltd is a company that carries out different agricultural activities in the Republic of Zambia. Omusati Ltd is very profitable and most of its produce is exported to Europe and countries in the COMESA region. Moyo Associates has been auditing Omusati Ltd for over six (6) and the Engagement has remained the same.

The detailed audit work has been completed and the Engagement Partner wants you to consider the use of Artificial Intelligence (AI) to review the audited financial statements. The Engagement Partner is not happy that the significant investment made by the firm in Information Technology (IT) platforms has not delivered the much anticipated audit efficiency. The Engagement Partner has, however, asked you to first consider the ethical implication of the use of Artificial Intelligence (AI).

The audit report is expected to be signed next week and the Engagement Partner does not want to miss the set deadline.

AUDIT OF THE FINANCIAL STATEMENTS FOR OTTAWA PLC FOR THE YEAR ENDED 30 SEPTEMBER 2023

The final audit for the year ended 30 September 2023 is nearing completion and you are reviewing the audit working papers. The draft financial statements recognize total assets of K50 million (2022 – K45 million), revenue of K60 million (2022 – K48 million) and profit before tax of K8 million (2022 – K7 million). The following three (3) issues, which are summarized below, have been brought to your attention:

- Inventory which was designed to specification for a customer is included in the total value of inventory at the year-end at a cost of K1 million. The customer was deported on 8 October 2023, in connection with serious money laundering offences. After much effort, the Marketing Director (MD) eventually managed to a find a customer who bought the inventory on 31 October for only K350,000. The Finance Director (FD) has promised to make the necessary adjustment.

- A deposit of K30,000 paid by a customer has been recognized in the statement of profit or loss as part of revenue. The Finance Director (FD) is not willing to make any adjustment.
- The company owns an investment property. During the year, part of the heating system of the property, which had a carrying value of K120,000 was replaced by a new system, which cost K450,000. The company uses the fair value model for measuring investment property. The Finance Director (FD) has debited Investment property with K450,000 and credited Bank with same amount.

EVALUATION OF SUGGESTED AUDIT OPINIONS FOR THREE (3) CLIENTS

As part of the quality management processes within Moyo Associates, you have been requested to evaluate the suitability of the suggested audit opinions regarding the following clients:

- **Client one** – At the year-end, the client leased a machine. The Finance Director (FD) correctly recognized the lease liability but the right of use asset was understated by a material amount, due to the omission of direct costs incurred.
  The Audit Senior has suggested a modified audit report containing a modified audit opinion in the form of a qualified audit opinion. (5 marks)

- **Client two** – The client is a very large mining company. The client uses hedge accounting even if the hedging relationship does not meet all of the IFRS 9 *Financial instruments* hedge effectiveness criteria.
  The Audit Senior has suggested an unmodified audit report containing a modified audit opinion in the form of an adverse audit opinion. (5 marks)

- **Client three** – The client's Board of Directors (BOD) has approved the financial statements. However, the audit team has not been provided with the workings for the Earnings per Share (EPS) of 14 ngwee.
  The Audit Senior has suggested an unmodified audit report containing unmodified audit opinion with an emphasis of matter paragraph. (7 marks)

Assume that in all cases the directors are not willing to make any necessary adjustments.

SECTION A

Required:

(1) Prepare briefing notes to be submitted to the Managing Partner of Moyo Associates, in which you:

(a) Explain how a Compliance Officer can assist in reducing deficiencies. (10 marks)

(b) For each of the deficiencies, comment on the FIC Act requirement and advise on the actions to take by Moyo Accountants, where relevant. (12 marks)

Professional marks available on this question (2 marks)

(2) Using the information on the audit of Constituency Development Fund (CDF):

(a) Suggest seven (7) audit procedures for the fuel consumption figure. (14 marks)

(b) Explain the sufficiency and appropriateness of the audit evidence obtained in respect of each of the four (4) matters. (12 marks)

[Total: 50 marks]

SECTION B

Required:

(3) Discuss the ethical implications of using Artificial Intelligence (AI) when reviewing the audited financial statements for Omusati Ltd. (15 marks)

(4) In undertaking your review of the audit working papers and financial statements of Ottawa Plc for the year ended 30 September 2023, for each of the issues:

(a) Comment on the matters to be considered; and (12 marks)

(b) State any two (2) audit evidence you should expect to find during your review. (6 marks)

(5) For each client, evaluate the suitability or otherwise of the suggested audit opinions, and make appropriate recommendations where necessary. (17 marks)

[Note: The split of the total marks are shown after the details for each client].

[Total: 50 marks]

END OF PAPER

FULL AUDIT COMPETENCE PRACTICE EXAMINATION (CPE)

SOLUTION ONE

SECTION A

(1) ANALYSIS OF THE FINDINGS CONTAINED IN THE AUDIT MONITORING REPORT

- **Review of the firm** – The firm's mission statement includes a phrase that "quality must follow profitability". Quality may be defined as the degree of excellence. It is crucial both to users and to the profession as a whole. ISQM1, ISQM2 provides detailed guidance in this area. The firm understandably is motivated by profit – it is what firm's expect – and there may appear to be a conflict of interest between profit and quality. However, in the long run, poor audit quality damages the reputation of the firm and loss of clients and thus fees, as well as an increased risk of litigation and concomitant professional insurance costs. Hence, neglect of quality may significantly harm profitability. Since, quality could result in improved profitability, the firm must instead consider the following opposite phrase, "profitability must follow quality".

[Award marks as follows:

1 mark for reference to ISQM1/ISQM2

Up to 2 marks for importance of quality

1 mark for importance of profitability

1 mark for suggested rephrasing]

- **File no. 1** – No risk assessment was conducted in respect of the financial statement audit for the client. A note from the Audit Senior stated that since the internal audit function also integrates computer assisted audit techniques (CAATs) in its methodology and recently conducted a risk assessment, the audit team decided to rely on the internal audit function's work. ISA 610 *Using the Work of Internal Auditors* gives detailed guidance in this area. It is important to note that although some of the work carried out by internal auditors are similar to that performed by external auditors, there are important distinctions between the two functions in terms of their responsibilities, scope and relationship with the company. Independence and objectivity may be questionable. ISA 315 requires external auditors to conduct risk assessment.

[Award marks as follows:

1 mark for reference to ISA 315

1 mark for reference to ISA 610

Up to 2 marks for importance of risk assessment

1 mark for independence and objectivity]

- **File no**. **2** – The written representation letter was not dated and signed. ISA 580 *Written Representations* states that written representations are written statements by management provided to the auditor to confirm certain matters or to support other audit evidence. The date of the representation letter must be as near as practicable to, but not after, the date of the auditor's report on the financial statements. Hence, if the written representation is not dated, there will be a misunderstanding whether this evidence was taken into account in arriving at the audit opinion. This could undermine the credibility of the audit opinion. Without a signature, it may be difficult to hold management or those charged with governance accountable regarding the written representation.

[Award marks as follows:

1 mark for reference to ISA 580

1 mark for valid point on date

1 mark for valid point on signature

1 for accountability]

- **File no**. **3 –** No confirmation was obtained from the Managing Director (MD) regarding unretired imprest of K2 million. The Audit Senior stated that this is handled by a special committee appointed by Cabinet Office. However, there was no written evidence on the matter from cabinet office. The audit opinion was unmodified. It is possible that issue could have been considered immaterial and as such the unmodified audit opinion is correct. However, if the issue was material, then an unmodified audit opinion was inappropriate. It possible that the issue could be material by nature as it involves a related party. IAS 24 gives accounting guidance while, ISA 550 gives auditing guidance.

[Award marks as follows:

1 mark for reference to IAS 24

1 mark for reference to ISA 550

1 mark for immaterial

1 mark for material]

(2) Nyeleti Chartered Accountants

(a) Main contents of a social media policy

The main contents of a social media policy include:

- Provide guidelines on using personal social media at work so that productivity is not adversely affected.
- Give clear instructions for employees representing the company on social media, emphasizing respect, accuracy and responsibility.
- State disciplinary consequences for policy violation, including potential termination.

[Award up to 2 marks for each valid content – Maximum 6 marks]

Importance of compliance with the laws when developing Human Resources Management (HRM) policies

The main reasons for the importance of compliance with the laws when developing Human Resources Management (HRM) policies include:

- Ensures employees are treated fairly and equitably
- Protects the organization from potential legal repercussions
- Staying abreast of legal development and adapting their policies accordingly, organizations can maintain a legally sound and compliant work environment.
- Adherence to the fundamental ethical principle of professional behaviour.

[Award 1 mark for each valid reason – Maximum 3 marks]

(b) Disadvantages which the audit teams may encounter when using Computer Assisted Audit Techniques (CAATs)

The disadvantages include:

- Client permission and co-operation may be difficult to obtain.
- Potential incompatibility with the client's computer system.
- The audit team may not have sufficient IT skills and knowledge to create the complex data extracts and programming required.
- The audit team may not have the knowledge or training needed to understand the results of the CAATs.
- Data may be corrupted or lost during the application of CAATs.

[Award up to 2 marks for each disadvantages – Maximum 8 marks]

(3) Mpandila Ltd

Ethical and professional issues	**Evaluation**	**Recommendation**
(1) Inclusion of seconded Audit Senior on the audit	This will create a self-review threat as there is the risk that the Audit Senior will be auditing his own work on return to the audit firm. In addition, there will be a familiarity threat and the seconded Audit Senior may fail to exercise the required professional skepticism. Hence, his objectivity and independence could be seriously impaired. Even if the seconded Audit Senior is not part of the audit team, there is a risk that the audit team over relies on work carried out by him.	The seconded Audit Senior must not be included as part of the audit team. Nyeleti Chartered Accountants must also incorporate serious quality reviews.
(2) Appointment of majority shareholder as District Commissioner (DC)	This increases the reputational risk of Nyeleti Chartered Accountants as the appointment makes the	Nyeleti Chartered Accountants should consider whether it should continue to act as auditors

	majority shareholder a politically exposed person (PEP). There will be more publicity if something goes wrong.	for Mpandila Ltd. Guidance in legislation, especially on money laundering and financial intelligence must followed strictly.
(3) The Director of Finance of Mpandila Ltd has requested that a certain audit senior be assigned to the audit team.	The client has a legitimate right to make such a request provided that it does not undermine objectivity and independence. However, it must be stressed that appointment of audit team members is a sole responsibility of the audit firm.	Discuss the matter with the Director of Finance and if it undermines objectivity and independence, the request must be politely declined.
(4) Management has promised to provide the audit team with snacks and refreshments throughout the period of audit.	This could give rise to a self-interest threat, which could impair objectivity. The audit team may feel obliged to impress Mpandila Ltd at all costs.	No safeguard is recommended if the value of the snacks and refreshments is considered to be trivial and inconsequential. If the value is significant, then this should be politely declined.
(5) Acceptance of one-off consultancy work.	The expected fee of 10% will push the total to 18%, which is above the recommended threshold of 15%. Nyeleti Chartered Accountants may be considered to overly dependent on Mpandila Ltd. Its independence and objectivity could be questionable.	Since this is a one-off consultancy work, it could be accepted provided necessary safeguards are put in place e.g. use of separate teams, avoiding undue influence by the Consultancy Department on the audit team, quality reviews by independent senior personnel etc.
(6) A Junior Auditor has shared a post on social media which accuses the Chief Accountant of having an intimate relationship with the Accountant-in-Charge (AIC).	If true, this will create serious familiarity and self-interest threat. The intimate relationship could seriously impair independence and objectivity.	More information must be obtained before further action is taken. The Accountant-in-Charge (AIC) may also be questioned in this regard.

[Award marks as follows:

Up to 1 ½ marks for each evaluation – Maximum 9 marks

1 mark for each recommendation – Maximum 6 marks]

SOLUTION ONE

SECTION B

(4) Hamasamu Plc

Key deficiencies of the advertisement

- The advertisement mentions "Chartered Accountants" without including registered with the Zambia Institute of Chartered Accountants (ZiCA). In the Republic of Zambia, before any person engages an accountant to perform any work, they must verify their membership with the Zambia Institute of Chartered Accountants (ZiCA). It is therefore important that the advertisement includes this fact.
- The advertisement does not mention specific qualifications required. Specialised training in tax could be an added advantage. This could significantly ensure that Hamasamu Plc gets value for money.
- The advertisement mentions submission of detailed proposal but offers no guidance on what should be included in the detailed proposal. The submissions will not be standard and this will make evaluation of the bids very difficult. The advertisement should provide sufficient guidance on the details to be included in the proposal.
- The advertisement does not mention experience in tax work. Professional competence and due care requires that members engaged in providing tax services shall maintain professional competence and take due care in the performance of their work. To achieve this, members shall remain continuously aware of developments in the tax profession and tax legislation to ensure that they have the requisite knowledge related to such developments, including an awareness of relevant national pronouncements and other relevant statutory requirements and regulations.
- The advertisement makes no specific mention to transfer pricing. The country has very few experts in transfer pricing and only a few proposals could touch on transfer pricing. The advertisement should make specific mention to transfer pricing as this will also assist in estimating the fee to be charged.

- The advertisement does not mention the issue of references. Referees may provide invaluable information which will be of great help in the selection process.
- The address given in the advertisement is not specific and some bidders may be disadvantaged. More details must be given.

[Award up to 2 marks for each deficiency – Maximum 12 marks]

(5) Daka Plc

Evaluation of audit responses and suggested amendments

Audit responses	Evaluations	Suggested amendments
Carry out an impairment review as guided by IAS 36 *Impairment of assets.* The remaining delivery vans should be tested for impairment by comparing their recoverable amount with their carrying amount.	This is a management responsibility and hence is not an appropriate response to the audit risk. Nyeleti Chartered Accountants should not take up management responsibilities.	Discuss with management and those charged with governance the need for them to carry out an impairment review.
Obtain contracts with Government institutions and review the specific details. Review correspondence with Government institutions and take note of any indicators of political interference. Seek legal advice especially on important clauses regarding termination of contract.	This response is appropriate as the audit team may be able to obtain sufficient appropriate audit evidence to support any conclusions.	No amendments suggested.
Carry out substantive procedures designed to detect material misstatements regarding the valuation.	This audit response is too general and offers no specific guidance to the audit team members.	Obtain and review workings on the valuation of convertible bonds. Re-perform the calculations to ensure they are in accordance with guidelines given in IFRS 9 *Financial Instruments.*

Use only qualified and experienced audit staff.	The response could prove to be very expensive and Nyeleti Chartered Accountants will unnecessarily end up making losses on this engagement.	More time should be spent on understanding the entity and its environment as guided by ISA 315. Qualified and experienced audit staff should be used in risky areas.
Obtain a breakdown of the capitalized cost and check against relevant supporting documents e.g. invoices	The response is partly appropriate as it does not specifically provide guidance on adherence to the criteria given in IAS 38.	Include in the audit response, ensuring that the capitalized cost meet the criteria laid down in IAS 38 *Intangible assets.*

[Award marks as follows:

1 ½ marks for each correct evaluation – Maximum 7 ½ marks

1 ½ marks for each correct suggestion – Maximum 7 ½ marks]

(6) Kapapa Ltd

(a) Green Bonds

Nature of Green Bonds

Green Bonds are fixed-income instruments designed to support climate related or environmental projects. They are part of a larger trend in socially responsible and environmental, social, and governance (ESG) investing.

The phrase "Green Bond" is sometimes used interchangeably with "Climate Bond" or "Sustainable Bond".

Green Bonds often come with tax incentives to enhance their attractiveness to some investors.

[Award 1 mark for each valid point – Maximum 3 marks]

Appropriate audit procedures on Green Bonds

These include

- Obtain the relevant signed board minutes to confirm approval of the issuance of Green Bonds and their authenticity

- Obtain the contractual agreement and review the contents, especially the restrictive covenants
- Review correspondence with bondholders and investigate any indications of non-compliance with agreed terms and conditions
- Agree the value of the Green Bonds to the General Ledger and workings
- Confirm that the workings are in accordance with the guidance in IFRS 9 *Financial Instruments*
- Recalculate the figures to confirm their arithmetical accuracy
- Agree interest charges to the contractual agreement and supporting documentation
- Obtain direct confirmation from bondholders of the amounts outstanding, accrued interest and what security they hold
- Check repayments in the cashbook and bank statement to confirm repayments are in accordance with the contractual agreement
- Check the presentation and disclosures in financial statements to confirm that they are in accordance with IFRS 9 *Financial Instruments*

[Award up to 2 marks for each audit procedure – Maximum 10 marks]

(b) Business risks

These include:

- Government ownership – political decisions may take priority over business decisions. This may affect the profitability of Kapapa Ltd and eventually it's going concern status in the long-run.
- Informal sector – the projected growth in demand mainly driven by the informal sector may not be reliable. This will affect Kapapa Ltd's ability to meet its future obligations.
- Green Bonds – the gearing of Kapapa Ltd has increased and if not managed properly, the going concern status of Kapapa Ltd could become highly questionable.
- Imported spare parts – these could become too expensive due to the deterioration in the exchange rate. Kapapa Ltd may be forced to turn to cheaper sources which could negatively affect their operations resulting in loss of customers.
- Technical staff – the increase in labour turnover will definitely have a significant negative impact on the operations if not addressed quickly.

[Award up to 2 marks for each valid business risk – Maximum 10 marks]

SOLUTION TWO

<u>SECTION A</u>

(1) **Briefing notes**

To: Managing Partner

From: Audit Manager

Subject: key findings in the deficiency letter

Introduction

These briefing notes explains how a Compliance Officer can assist in reducing deficiencies and for each of the deficiencies identified, comments on the FIC Act requirement and advise on the actions to take by Moyo Accountants, where relevant.

[Award professional marks as follows:

1 mark for format and 1 mark for introduction]

How a Compliance Officer can assist in reducing deficiencies

The Financial Intelligence Centre (Amendment) Act 2020 states that a reporting entity shall designate a compliance officer at **senior management level** to be **responsible** for the implementation of, and ongoing compliance with this Act by that reporting entity.

It also states that a person shall not be designated as a compliance officer unless that person:

(a) **has two years' experience** in the field of regulatory compliance;

(b) **is not convicted** of an offence under this Act or any other written law and sentenced to a term of imprisonment of not less than six months without the option of a fine; and

(c) is **certified and approved by the Centre**.

It is therefore likely that the Compliance Officer can assist in reducing deficiencies mainly in the following ways:

(1) As a result of being a senior member of management, he or she will have the authority to ensure directives are executed on a timely basis. There will be a high probability that the recommendations of the Financial Intelligence Centre (FIC) and the Zambia Institute

of Chartered Accountants (ZiCA) will be implemented and this will significantly contribute to the reduction of deficiencies.

(2) The responsibilities of the Compliance Officer are specified in the Financial Intelligence Centre Act and as such will not be subject to any debate. This will greatly improve his or her effectiveness and greatly contribute to reduced deficiencies.

(3) Experience in the field of regulatory compliance will make identification and correction of deficiencies much easier. Management and employees within Moyo Accountants will learn a lot from the Compliance Officer and this will significantly contribute to the reduction in deficiencies.

(4) The point on conviction means the Compliance Officer is expected to be a person of integrity and high moral standing in society. This means deficiencies will have to corrected without necessary waiting for inspection by the Financial Intelligence Centre (FIC) and/or the Zambia Institute of Chartered Accountants (ZiCA).

(5) The approval and certification by the Centre is an added assurance that the Compliance Officer is expected to have sufficient knowledge in various legal provisions, especially the Financial Intelligence Centre (FIC) Act. This is an invaluable ingredient in the reduction of deficiencies.

[Award up to 2 marks for each valid point – Maximum 10 marks]

Comments on the FIC Act requirement and advice on the actions to take by Moyo Accountants, where relevant

- **Identification of customer that is not physically present** – Moyo Associates did not carry out any identification procedures since the client had no physical presence in the Republic of Zambia. **Section 18** of the Financial Intelligence Centre Act 2010 gives detailed guidance on what the reporting entity shall do where it conducts any business relationship or executes transactions with a customer that is not physically present for purposes of identification. Moyo Accountants was in breach of this section and must therefore seek detailed guidance from the Financial Intelligence Centre (FIC) on the way forward.
- **Tipping – off offence** – Moyo Associates, acting as independent professionals, formed a suspicion of money laundering against a new client but went ahead and conducted a customer identification and verification requirement which resulted in tipping off the client, who has since left the country. **Section 16 (10)** of the Financial Intelligence Centre Act 2020 (Amendment) provides detailed guidance in this area. Moyo Associates should have instead filled a suspicious transaction report as required by the Act. Moyo Associates was in breach of this section and must plead guilty and honestly cite reasons for this deficiency.

- **Prevention of compliance with the obligations under the Financial Intelligence (FIC) Act** – The Managing Partner stated that the laws in the foreign branches do not require observance of the Financial Intelligence Centre (FIC) Act obligations and no training has been offered for the foreign staff members. **Section 27 (2)** of the Financial Intelligence Centre Act 2020 (Amendment) provides detailed guidance in this area. Moyo Associates should urgently contact the Zambia Institute of Chartered Accountants (ZiCA) on the way forward as it is the supervisory authority.
- **Misleading information** – The Managing Partner gave misleading information to FIC inspectors regarding an enquiry by the inspectors concerning the wire transfers between the foreign branches and head office. **Section 11B (4) (c)** of the Financial Intelligence Centre Act 2016 (Amendment) gives detailed guidance in this area. Moyo Associates was in breach of this section and must plead guilty and seek leniency.

[Award up to 3 marks for each comment and advice on each deficiency – Maximum 12 marks]

(2) Audit of Constituency Development Fund (CDF)

(a) Constituency one – Suggested audit procedures for the fuel consumption figure

These include:

- Ascertain the system used for accounting for fuel consumption using enquiries, observation etc.
- Document the system and confirm its accuracy by carrying out a walkthrough test.
- Inspect the earth moving equipment and enquire on the fuel consumption.
- Visit the private filling station to physically confirm the re-fuelling process and the documentation issued.
- Obtain a list of all approved works during the period under review and use an expert to estimate the fuel consumption for the earth moving equipment.
- Compare actual fuel consumption based on approved orders and supporting invoices or other documentation from the private filling station with the estimated fuel consumption. Discuss any significant differences with management.
- Obtain copies of approved fuel orders for the period under review and agree total value to the value shown in the financial statements. Significant differences must be investigated.

- Agree payments on the bank statements to pre-audited payment documentation e.g. approved orders. Any unsupported payments must be investigated.
- Interview the operatives regarding any fuel wastage experienced during the period under review.
- Review internal audit reports for any evidence of theft of fuel.
- Review the working papers for any closing inventory and ensure appropriate adjustments have been made in accordance with the IAS 2 *Inventories* guidelines.

[Award up to 2 marks for each valid audit procedure – Maximum 14 marks]

(b) Constituency two – Sufficiency and appropriateness of the audit evidence obtained

(1) Court case – Written management representation letter

Sufficiency

Management are interested parties and may be faced with serious conflict of interest. Hence, the written management representation letter may not be sufficient as management may deliberately leave out certain facts.

Appropriateness

The written representation letter may not be appropriate mainly due to management bias and possible lack of the required legal expertise.

(2) Accounts payables – Reconciliations with supplier year-end statements

Sufficiency

Depending on the auditor's assessment of materiality and risk of misstatement, reconciliations with supplier year-end statements may be considered sufficient.

Appropriateness

Supplier statements may be appropriate since they are external documentary evidence.

(3) Capital work-in-progress – Physical inspection

Sufficiency

Physical inspection may be sufficient as to the financial assertion of existence but not for others.

Appropriateness

Depending on the competences of the auditor, this could be appropriate as it is auditor-generated.

(4) Payments – Confirming that the internal auditors had undertaken pre-audits for all payments

Sufficiency

This is clearly not sufficient as the functions of internal auditors and external auditors are not the same.

Appropriateness

This will depend on the auditor's overall assessment of the internal audit department.

[Award marks as follows:

Up to 1 ½ marks for sufficiency on each matter – Maximum 6 marks

Up to 1 ½ marks for appropriateness on each matter – Maximum 6 marks]

SOLUTION TWO

<u>SECTION B</u>

(3) Ethical implications of using Artificial Intelligence (AI) to review the audited financial statements for Omusati Ltd

These are as follows:

- Integrity – this means auditors must be straightforward and honest in all professional and business relationships. The developers of Artificial Intelligence (AI) may be dishonest individuals and this will also impact on the reviewer using it. The reviewer may also want to give a positive response just to impress the Engagement Partner that the investment in IT is delivering efficiency.
- Objectivity – this means auditors must not allow bias, conflict of interest or undue influence of others to override professional or business judgements. The details supplied to develop the Artificial Intelligence (AI) may be biased and this will also affect the reviewer of the audited financial statements. The Engagement Partner may exercise undue influence on the reviewer so that the use of Artificial Intelligence (AI) is justified.

- Professional competence and due care – this means auditors must maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional services based on current developments in practice, legislation and techniques and act diligently and in accordance with applicable technical and professional standards. The reviewer may not understand the Artificial Intelligence (AI) processes and this will affect the quality of the review. In addition, the Artificial Intelligence (AI) may not be regularly updated meaning the review may not be based on current developments.
- Confidentiality – this means auditors must respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, 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, nor use the information for the personal advantage of the professional accountant or third parties. Internet based-technologies like Artificial Intelligence (AI) are prone to cybercrime which could affect confidentiality of client information. This could have serious legal and reputational risks.
- Professional behaviour – this means auditors must comply with relevant laws and regulations and avoid any conduct that discredits the profession. The use of Artificial Intelligence (AI) may be illegal in some countries.

[Award up to 3 marks for each ethical implication – Maximum 15 marks]

(4) Ottawa Plc

Issue one – Inventory

(a) Matters to consider

- Materiality – The misstatement of K0.65m (K1m – K0.35m) is material to both the statement of financial position and statement of profit or loss at 1.3% of total assets (0.65/50 X 100%) and 8% of profit before tax (0.65/8 X 100%) respectively.
- Risk – There is a risk that both profits and assets may be overstated, if the Finance Director (FD) does not make the necessary adjustment.
- Relevant accounting standard – Under IAS 2 *Inventories,* inventory must be valued at the lower of cost and net realizable value. In this case, the inventory must be included at a value of K350,000.

- Impact on audit opinion – Since the misstatement is material, the audit opinion will modified if the Finance Director (FD) does not make the necessary adjustment. A qualified audit opinion will be appropriate.

(b) Evidence

- Copy of relevant management and/or board minutes
- Relevant correspondence regarding the issue

Issue two – Deposit

(a) Matters to consider

- Materiality – The deposit of K30,000 is clearly immaterial to the statement of profit or loss at 0.05% of revenue (0.03/60 X 100%).
- Risk – There is a risk that revenue is deliberately overstated to show a picture which favours management position.
- Relevant accounting standard – IFRS 15 *Revenue from contracts with customers* requires that revenue should be recognized when the performance obligation has been satisfied. This is not the case here and therefore accounting treatment is incorrect.
- Impact on audit opinion – This issue is immaterial and therefore the audit opinion will be unmodified.

(b) Evidence

- Copy of the receipt for the deposit
- Written response from the Finance Director (FD) regarding his unwillingness to make any adjustment.

Issue three – Investment property

(a) Matters to consider

- Materiality – there is no accounting entry for the old heating system, resulting in a misstatement of K120,000. This misstatement is immaterial to both the statement of financial position and statement of profit or loss at 0.24% of total assets (0.12/50 X 100%) and 1.5% of profit before tax (0.12/8 X 100%) respectively.
- Risk – both the profit and investment property are overstated, although it seems it could simply be error which the Finance Director (FD) should be willing to correct.

- Relevant accounting standard – IAS 40 *Investment property* requires that the old heating system must be written off by debiting the profit or loss and crediting investment property. The accounting treatment is therefore not complete.
- Impact on audit opinion – the audit opinion will be unmodified given that the issue is immaterial.

(b) Evidence

- Copy of relevant documentation e.g. invoices
- Notes of any discussion with the Finance Director (FD)

[Award marks as follows:

1 mark for materiality – Maximum 3 marks

1 mark for risk – Maximum 3 marks

1 mark for relevant accounting standard and treatment – Maximum 3 marks

1 mark for impact on audit opinion – Maximum 3 marks

1 mark for each audit evidence – Maximum 6]

(5) **Suggested audit opinions**

Client one – the question states that the matter is **material** which means it may lead to a modified audit opinion but the form of modified audit opinion will depend on the pervasiveness of the misstatement. **Audit reports** which contain modified audit opinions are automatically considers as modified audit reports as the standard audit report given in ISA 700 contains an unmodified audit opinion. The suggested modified audit report by the Audit Senior is therefore suitable. However, the suggested **modified opinion in the form of a qualified opinion** is debatable since the question is silent on the pervasiveness of the misstatement. If the misstatement is not pervasive, which is likely to be the case, the qualified audit opinion is suitable.

[Award marks as follows:

1 mark for materiality

Up to 2 marks for modified audit report

Up to 2 marks on suitability of qualified audit opinion]

Client two – the question is silent on whether the issue is material or not. However, given that client two is a large mining company, it may be appropriate to assume that the matter in question could be material since hedging is more generally big business in the mining sector. Hence, if the misstatement is material then this means a modified audit opinion will apply but the form of modified audit opinion will depend on the pervasiveness of the misstatement. **Audit reports** which contain modified audit opinions are automatically considers as modified audit reports as the standard audit report given in ISA 700 contains an unmodified audit opinion. The suggested unmodified audit report by the Audit Senior is therefore unsuitable. However, the suggested **modified opinion in the form of an adverse audit opinion** could be suitable if the misstatement is pervasive.

[Award marks as follows:

Up to 2 marks for materiality

1 mark for modified audit report

Up to 2 marks on suitability of qualified audit opinion]

Client three – the 14 ngwee Earnings per Share (EPS) is not material in terms of value. However, this is an important investor ratio used to assess performance. It is therefore material by nature. **Material** lack of sufficient appropriate audit evidence should result in a modified audit opinion but the form of modified audit opinion will depend on the pervasiveness of the misstatement. The Audit Senior has suggested an unmodified audit report containing unmodified audit opinion with an emphasis of matter paragraph but this seems premature. The audit team should have simply used the audited financial statements to recalculate the Earnings per Share (EPS). Auditors are expected to have sufficient knowledge of accounting standards, in this case, IAS 33 *Earnings per Share.*

The Audit Senior must use the audited financial statements to recalculate the Earnings per Share (EPS). The outcome of this audit work will give an indication of the way forward.

If the lack of sufficient appropriate audit evidence will be considered material and pervasive, then a modified audit report with a modified audit opinion in the form of a disclaimer of audit opinion will be suitable. A qualified audit opinion will only be appropriate if the lack of sufficient appropriate is material but not pervasive. The emphasis of matter paragraph is not used with modified audit opinions.

[Award marks as follows:

Up to 2 marks for materiality

Up to 2 marks for suggestion premature

1 mark for suggested audit work

Up to 2 marks on suitability of audit opinions]

END OF SOLUTIONS