

[N.B. - The figures in the margin indicate full marks. Questions must be answered in English. Examiner will take account of the quality of language and of the manner in which the answers are presented. Different parts, if any, of the same question must be answered in one place in order of sequence.]

Marks

1. Smart Chemical Ltd. is a manufacturing company in the chemical industry. MM Ahmed & Co. Chartered Accountants have been its auditors and were appointed auditors for a period of three years. This is the last year of the engagement and the audit for the current year is about to commence. The opinion for the previous year was an adverse opinion which arose following a disagreement with management on the basis of the preparation of the financial statements and a material uncertainty with regards to going concern that existed at the time.

Before commencement of the audit for the financial statements of the year ended 31 March 2023, Smart Chemical Ltd. advertised for bids from reputable firms of auditors for offering of audit services. The advertisement indicated that the company wished to engage auditors who will be required to conduct the audit of the current year financial statements. MM Ahmed & Co. Chartered Accountants inquired of management of Smart Chemical Ltd. on why the company wants to replace them before the expiry of their term of office. A Board resolution was made by Smart Chemical Ltd. to terminate the contract with MM Ahmed & Co. Chartered Accountants and the Company Secretary formally wrote to the firm informing it of the decision and that the firm should return property belonging to Smart Chemical Ltd. immediately. The letter states that since the audit fee for the previous year audit was paid, the company does not owe MM Ahmed & Co.

You are the partner in charge of client acceptance in your firm of auditors, Rex & Partners. Your firm has been in existence for three years and it has grown from being a two (2) man partnership into a firm with six partners and ten other members of staff. Your client base comprises largely of trading companies and telecommunication companies.

Your firm decided to submit a bid in response to the invitation for bids by Smart Chemical Ltd. The senior members of your firm resolved that although this will be the first time that the firm will be auditing a client in this industry, it should be able to conduct a quality audit and if necessary, staff will undergo training before the commencement of the audit if appointed as auditors by Smart Chemical Ltd. Your firm has three other audit clients with the same year end as that of Smart Chemical Ltd. and the audits for their financial statements are due to begin soon.

Smart Chemical Ltd. received five bids from interested audit firms including one from Rex & Partners. In view of the tight deadlines requiring that the financial statements of Smart Chemical Ltd. should be finalized and the audit report signed by 27 April 2023 in readiness for the Annual General Meeting on 12 May 2023, the Board of Directors (BOD) of Smart Chemical Ltd. resolved to nominate Rex & Partners as the new auditors. The Company Secretary of Smart Chemical Ltd. formally wrote to Rex & Partners informing them of the appointment and requesting them to confirm acceptance by signing the agreement enclosed in the communication by a specified date.

As Partner in Charge of client acceptance, you received the letter from Smart Chemical Ltd. and you are expected to respond as quickly as possible within the timeframe indicated in the letter.

Requirements:

- a) Discuss the termination of the contract for audit services between Smart Chemical Ltd. and MM Ahmed & Co. Chartered Accountants clearly explaining the professional requirements that should be followed. 4
- b) Explain the matters that should have been considered before responding to the invitation for bids for offering of audit services by Smart Chemical Ltd. 3
- c) Explain the matters and actions that should be taken from receipt of the notice of appointment as auditors from Smart Chemical Ltd. to the time of making a decision whether to accept the appointment or not. 3

2. a) As a qualified senior along with one audit staff you are about to start work on an assignment. Before the file is passed on to the manager, you are responsible to review the work of audit staff.
Requirement:
What aspects you will have to be consider when reviewing the work? 3
- b) Honest Gentleman & Co., Chartered Accountants (HGC) has been regarded as one of the most respected auditors in the market. In a recent audit HGC had a serious disagreement with the directors of one of their major audit clients on several critical accounting treatments. As a result, the directors, being displeased, have threatened to recommend another firm of auditors for appointment in the upcoming AGM.
Requirement:
What are the statutory rights available for HGC to bank on if the directors carry out their threat? 3
- c) Recently you have come across the following professional issue.
During the audit of a listed company, you overheard the finance director on the telephone to a family friend requesting him to buy shares on his behalf, prior to an announcement about a new product which you know is likely to increase the share price significantly. The finance director is a chartered accountant.
Requirement:
Set out the problems inherent in the above situation and the action that you should take. 4
3. a) An assurance firm must accept an engagement judiciously and professionally ensuring compliance with critical conditions and requirements laid down in the respective ISAs, ethical codes, applicable laws, and regulations.
Requirement:
As an audit professional, you are asked to summarize the actions you need to know underlying acceptance of an audit engagement. 6
- b) You are an Audit Senior in Ahmed & Partners, a firm of chartered accountants. The Directors of Coppertech Industries Ltd have nominated Ahmed & Partners to accept appointment as auditors. Coppertech Industries Ltd is a family company which is involved in the manufacture of copper components required for electric cars. These are mainly sold abroad and 60 days credit is allowed. This will be the first time for Ahmed & Partners to audit a company in this industry. The Finance Director left last year and is yet to be replaced. Profits have declined in the last three years and this has eventually led to serious liquidity problems. The previous auditors resigned last month. The Partner who is in charge of client acceptance asked you to perform client screening procedures. Depending on the findings, the company will be put forward for approval. The Engagement Partner will be required to complete a client acceptance form which will be submitted to the Partner who is in charge of client acceptance. The acceptance form will be accompanied by the findings and relevant documentation.

If the appointment is accepted, you will be required to draft an engagement letter before the audit commences. Both Coppertech Industries Ltd and Ahmed & Partners will be required to sign the engagement letter.
Requirements:
- i) Describe the basic factors to consider when screening Coppertech Industries Ltd. 3
- ii) Explain why an engagement letter is important to both the client and the auditor. 3
- iii) Suggest the action(s) to take if Coppertech Industries Ltd does not sign the engagement letter. 3
4. a) During the course of your audit of Midget Ltd the credit controller asks for a private interview with you. During this interview he makes it known that he suspects the chief accountant through altering the books is misappropriating company funds received from debtors.
Requirement:
What steps would you like to take to assess whether the credit controller's suspicions are reasonable? 5
- b) ISA 701: Communicating Key Audit Matters (KAM) in the Independent Auditor's Report is a new ISA introduced as part of the International Audit and Assurance Standards Board's (IAASB) extensive revisions to International Standards on Auditing (ISAs) relating to audit reporting. The

objective of the IAASB's revisions was to make the auditor's report more detailed and useful for the intended users. ISA 701 applies to audits of complete sets of general purpose financial statements of listed entities.

Subsequently, the Institute of Chartered Accountants of Bangladesh (ICAB) issued a notice to practitioners which directed that auditor's report issued on financial statements for periods ending on or after 31 December 2018 for Public Interest Entities (PIEs) to include a communication on Key Audit Matters as required by ISA 701.

You are the Partner in charge of training with Azad and Associates. An audit team member informed you that one of the clients being audited has an issue which is being contemplated as to whether to report the issue as key audit matter, emphasis of matter paragraph, other matter paragraph, or to modify the audit opinion.

Requirements:

Prepare briefing notes for the staff of your firm regarding the following:

- i) KAMs and state **TWO (2)** categories of entities in Bangladesh which ISA 701 is applicable as adopted by ICAB 3
- ii) Factors to be considered in determining KAMs. 3
- c) Auditors should consider materiality when determining the nature, timing and extent of audit procedures. Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Ideally an item measuring in large figure having influence in the credibility of the financial statements is considered material. However, there is something called performance materiality which is set to a relatively smaller number.

Requirement:

Briefly discuss about the performance materiality. 4

- 5. a) The Brexit Group of Companies comprises a parent company and two subsidiaries based in foreign countries. The year end of the parent company and one subsidiary is 31 December. Brexit Group of companies acquired eighty percent of the shares in another company during the year.

The country in which the existing subsidiary is based has not yet adopted the International Financial Reporting Standards (IFRSs) in the preparation of financial statements. The country in which it is based has its own accounting standards which the subsidiary follows but are not similar with the international standards. As a result of this, there are disparities in some accounting policies adopted by this subsidiary with those of the parent company. The financial statements of subsidiaries are audited by local audit firms in their respective countries.

The subsidiary acquired during the current year is based in a country which follows the International Financial Reporting Standards (IFRSs). The subsidiary is audited by a local firm of Chartered Accountants. The auditors in this country are not regulated and do not perform audits in accordance with International Standards on Auditing (ISAs).

You work for Ahmed & Associates Chartered Accountants who are the auditors of the parent company. Your firm has been appointed auditor of the group financial statements. At a pre audit meeting with the group management, there was concern from one of the managers on why group financial statements should be audited in addition to the parent and subsidiary financial statements having already been audited by their respective auditors. Each of the subsidiaries maintains financial statements in the currency of the home country. The consolidated financial statements will be in the currency of the parent company.

You are planning the audit of the consolidated financial statements of the Brexit Group of Companies. The subsidiary acquired in the year under review is a significant component from the point of view of the group.

Requirements:

- i) Describe four matters that Ahmed & Associates Chartered Accountants should consider in the audit of the consolidated financial statements. 4
- ii) Explain the responsibility for the opinion of the separate financial statements of the parent and the subsidiaries with that of the consolidated financial statements. 3
- iii) Describe the work that should be performed by Ahmed & Associates Chartered Accountant on the subsidiary considered as a significant component of the Brexit Group of Companies. 4

- b) Omega Ltd was incorporated to engage in the production, supply and retail of sachet water. The final audit for the Financial Statements ending 31 December 2023 is nearly complete and it is proposed that the Financial Statements and Audit Report will be signed on March 31, 2024. Revenue for the year is TK.78 million and profit before tax is TK.7.5 million.

The following events have occurred subsequent to the end of the reporting year of the company.

Lawsuit

A key supplier of Omega Ltd is suing them for breach of contract. The lawsuit was filed prior to the year end, and the sum claimed by the supplier is TK.1 million. This has been disclosed as a contingent liability in the Notes to the Financial Statements. However, correspondence has just arrived from the supplier indicating that they are willing to settle the case for a payment by Omega Ltd of TK.0.6 million. It is likely that the company will agree to this.

Warehouse

Omega Ltd has three warehouses sited in different locations. Following extensive rain on 20 February, 2024, one of the warehouses was completely flooded and as a result, all inventory in the warehouse valued at TK.1 million was damaged and has been disposed off. The insurance company has already been contacted. No amendments or disclosures have been made in the financial statements.

Account Receivables

A customer of Omega Ltd has been experiencing cash flow problems and its year-end balance is TK.0.3 million. The company has just become aware that its customer is experiencing significant going concern difficulties. Omega Ltd believes that as the company has been trading for many years, they will receive some, if not full payment from the customer, hence the receivables balance has not been adjusted.

Requirements:

- i) Discuss whether the financial statements require amendment. 3
 - ii) Describe audit procedures that should be performed in order to form a conclusion on the amendment. 2
 - iii) Explain the impact on the audit report should the issues remain unresolved. 2
- c) You have commenced the audit of Atika Ltd, a company involved in the importation and sale of plumbing materials. As part of the audit, you have noticed the following:
- i) Atika Ltd does not pay its suppliers in Germany through the bank. It relies mostly on the black market for the transfer of funds to its suppliers.
 - ii) Atika only sells its goods in Bangladesh.
 - iii) On 25 March within the audit year, there was a cash deposit of US\$2,500,000.00 into the forex account of Atika Ltd.
 - iv) On 30 March the company transferred the following:
 - US\$499,999.99 to an unknown account in Canada
 - US\$399,999.99 to an unknown account in Kenya
 - US\$499,999.99 to an unknown account in Romania
 - US\$250,000 to the personal account of the Managing Director
 - US\$150,000 to an unknown company.
 - v) The company's general ledger shows a revenue of TK.1,560,000
 - vi) The import documentations show purchases of TK.36,000,000 There is no evidence of payment for the goods from Atika Ltd's bank accounts.
 - vii) The closing inventory amounted to TK.2,145,200

The Audit Manager has raised the issue of money laundering considering the nature of the transactions above.

Requirements:

As the Partner on the engagement,

- i) Explain to the team members the various stages of money laundering and show how the above transactions confirms the client's engagement in money laundering. 4
- ii) What are the obligations on the firm for money laundering? 3

6. a) On 1 July 2022, Dilli Aluminium Ltd introduced a ten-year warranty on all sales of its cooking equipment. Total sales of the cooking equipment for the year ended 31 March 2023 amounted to TK.2.5 million. The draft Auditor's Report for the year ended 31 March 2023 showed revenue of TK.5.6 million.

The notes to the financial statements disclosed that since the introduction of the warranty, Dilli Aluminium Ltd's cooking equipment has been guaranteed to be free from defects under normal household use. As a result, no provision was recognised, as the amount of the obligation cannot be measured with sufficient reliability."

The draft report on the Financial Statements of Dilli Aluminium Ltd for the year ended 31 March 2023 was unmodified.

Requirement:

As the Managing Partner, comment on the draft report before you.

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- b) Prominent Manufacturer Ltd (Prominent) is an established business in the manufacturing sector. The company has received different awards over the past decade. Prominent's year-end is 30 September 2022. The audit of the financial statements of Prominent is nearly complete and the financial statements and the audit report are due to be signed in a few days.

The following additional information on two material events has been given to the auditor on 3 December 2022:

Event 1:

This event occurred on 10 November, 2022. Production at the Hwange factory was halted for one day when a truck carrying dye used in coloring the fabric on mattresses reversed into a metal pylon, crashing the vehicle and causing a dye to spread across the factory premises and into a local river. The Environmental Authority of Bangladesh is currently considering whether the release of the dye was in breach of environmental legislation. The company's insurers have not yet commented on the event.

Event 2:

This event occurred on 19 October, 2022. The springs in a new type of mattress have been found to be defective making the mattress unsafe for use. There have been no sales of this mattress as it was due to be marketed in the next few weeks. The company's insurers estimated that inventory worth TK600,000 had been affected. The insurers also estimated that the mattresses were only worth TK100,000. No claim could be made against the supplier of springs as this company was in liquidation with no prospect of any amounts being paid to third parties. The insurers would not pay Prominent for the fall in value of the inventory as the company was underinsured. This entire inventory was in the finished goods store at the end of the year and no movements of inventory had been recorded post year-end.

Assume that on 10 December 2022, the financial statements and the audit report were signed, and the Annual General Meeting was to take place on 10 January 2023. The Environmental Authority issued a report on 28 December 2022 stating that Prominent was in breach of environmental legislation and a fine of TK800,000 would be levied on the company. The amount is material to the financial statements.

Requirements:

- i) Explain the reporting implication in accordance with IAS 10: Events after the Reporting Period. 3
 - ii) Explain the auditors' responsibility and the audit procedures that should be carried out in accordance with ISA 560: Subsequent Events. 3
 - iii) Explain the additional audit procedures the auditor should carry out in respect of the fine by the Environmental Authority. 2
- c) UVW Ltd (UVW) is a client of your firm that operates a chain of shops in Cardiff selling ethically produced herbal cosmetics and toiletries. Since opening its first store five years ago the company has expanded and now has ten outlets in Bangladesh. The directors wish to continue the company's expansion by opening additional stores in Chattogram city and by introducing a mail order service. In order to finance these expansion plans the directors of UVW have been discussing an increase in their borrowing with the company's bank. In support of the funding request the directors have

prepared profit and cash flow forecasts for the three years ending 31 December 2023, based on assumptions they have made about the future success of the business. UVW's bankers require this information to be examined and reported on by independent accountants, and the directors have asked your firm to undertake this assignment.

Two potential properties have been found for the new outlets, both of which are leasehold premises that will require considerable refurbishment to bring them up to the standard of existing stores.

The mail order service, for which postage will be charged, will be run from the main Cardiff branch which incorporates the central delivery warehouse of the company. The packaging for delivered items will be specially designed to protect the products in transit and to reflect the company's logo and ethical trading credentials. The ingredients for preparing the herbal products are purchased centrally on credit terms. All ingredients are sourced from Chattogram producers and all packaging is made from recycled materials. Employees at UVW are paid at rates above the industry average and are also paid bonuses linked to profits made by the company as a whole.

Requirement:

Describe the differences between the conclusion expressed in an assurance report on forecast information and the opinion expressed in an auditor's report on financial statements. Give reasons for these differences.

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- d) Various auditing standards require auditors to report certain matters arising to those charged with governance. This is typically 'private' by nature and just for the attention of those charged with governance, as opposed to the auditor's report, which is a published document. In our place the requirements in relation to this private reporting in ISA 260 (revised) **Communication with those charged with Governance** which deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements.

Requirement:

What are the matters to be communicated under the scope of ISA 260?

4

- e) It is often that a review work under ISRE 2400 is fallaciously interpreted as an audit by the clients. But it is always imperative that a practitioner undertakes appropriate measures to make the client understand the difference between an audit and a review. Ideally, like an audit engagement, the practitioner would issue an engagement letter delineating all critical requirements underlying a review under International Standards on Review Engagements (ISRE) 2400 (Revised)-Engagement to Review Historical Financial Statements.

Requirement:

As an engagement manager, you are advised to delineate all critical requirements underlying a review under ISRE 2400.

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