



Initial Assessment of Competence

Professional Paper 1

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Part (e) Discuss the business ethics and professional ethical considerations that NKT would need to consider about the alleged impact of defaults on loan covenants.		Marks
• Include relevant safeguards. • Assume that NKT also performed the interim review for the year.		
1	ISSUE 1: Pressure to conceal breach of loan covenants to avoid impact	
1.1.	Business ethics considerations (including King IV Principle 1 & 3) from management's perspective	
1.1.1.	Inpahla management might be under pressure to conceal the breach in loan covenants (to avoid its impact), which would compromise their ethical leadership due to failure to act transparently (King IV. P1.RP1f).	1
1.1.2.	Management might engage in dubious or fraudulent actions to conceal material misstatements and avoid a modified audit opinion.	1
1.1.3.	This would lead to a lack of fairness towards the public and government (key stakeholders of the company) (King IV.P1.RP1e), which would lead to loss of public trust .	1
1.1.4.	Due to the impact that default on loan covenants could have on the company and potentially the country, management is incentivised to manipulate the financial statements to hide high debt exposure . Engaging in such an action would lead to a lack of integrity (due to dishonesty), hence failing to lead ethically as required by King IV (P1.RP1a).	1
1.2.	Professional ethics considerations for NKT arising from management pressure to conceal breach of loan covenants to avoid impact	
1.2.1.	The auditors might fail to identify and report on reportable irregularities and material irregularities , hence failing to comply with the Auditing Professions Act.	1
1.2.2.	The auditors might not act appropriately in accordance with the requirements of the SAICA/IRBA Code of Professional Conduct and NOCLAR requirements if they come across suspected or actual non-compliance with key financial reporting legislation in the SOC .	1
2.	ISSUE 2: Management may attempt to unduly influence, through intimidation/emotional blackmail, the auditors' audit opinion	
2.1.	Business ethics considerations (including King IV Principle 1 & 3) from management's perspective	
2.1.1	Management might try to unduly influence /place pressure on the auditor's sound judgement using emotional blackmail of the alleged potential impact this could have on the country to avoid a modified audit opinion.	1
	<i>Inpahla is a SOC and has adopted the recommended practices of King IV, hence engaging in emotional blackmail would result in a contravention with the following recommended practices of the King IV Code:</i>	
2.1.2.	Emotional blackmail of the auditors would not exhibit integrity (P1.RP1a), acting in good faith , as the intention is to take advantage of the impact that a modified opinion could have on the company (and allegedly the country) to prevent the auditors from pointing out material misstatements that could be as a result of fraud .	1
2.1.3.	Management may intentionally make an effort to divert responsibility (King IV P1.RP1c) and accountability (King IV P1.RP1d) for material misstatements (which could potentially also be as a result of material irregularities) and non-compliance with key laws and regulations, as they want an unmodified opinion regardless of the auditors' findings .	1

2.1.4.	Those charged with governance would not be acting with fairness (King IV P1.RP1e) towards stakeholders (the government and the public) by wanting an audit opinion to be issued that may not reflect the true outcomes of the findings of the audit which would compromise their decision-making.	1
2.1.5.	The governing body of Inpahla must ensure that the company is in compliance with the Constitution (King IV P3.RP12), and the Public Audit Act instituted by the Constitution, requires public audits to be conducted in a manner that enforces financial accountability, and transparency , and pressuring the auditors to issue an improper audit opinion would go against these requirements.	1
2.2.	Ethical theories consideration	
2.2.1.	Giving in to pressure to conceal a breach of loan covenants would exhibit the agency problem per the agency theory , as management might want to protect their own reputation/own image (of failing to steer the company effectively) whilst not acting in the best interest of the SOC and its stakeholders (the government and the public).	1
2.2.2.	The fiduciary duty of the directors to fulfil their role of safeguarding and appropriately accounting for the use of taxpayer money (provided by the government as key shareholder) would be breached if the financial statements are fraudulent , as directors would not be acting in the best interest of all stakeholders involved, contrary to the requirements of the stakeholder theory .	1
2.3.	Companies Act of 2008 (as amended) fiduciary duty considerations:	
2.3.1.	If the directors engage in actions to manipulate the financial statements in order to avoid a breach of loan covenants (especially in the second half of the financial year), this would be a lack of good faith (as it is dishonest) and the directors would be in breach of their fiduciary duty in terms of the Companies Act (s76).	1
3	General business ethics considerations for NKT arising from ISSUE 2:	
3.1.	NKT may face a moral/ethical dilemma of balancing the client's/management interests versus ensuring that an appropriate audit opinion is provided.	1
3.2.	<i>On the one hand:</i> if an unfavourable audit opinion is issued, it would lead to debt covenants being breached, which could result in compromising the going concern of the entity and could lead to thousands of job losses and triggering government support (<i>bad for others</i>).	1
3.3.1.	Government support would mean that taxpayer money would need to be redirected from service delivery (e.g. healthcare, education, water and sanitation, etc.) to save the struggling company (<i>bad for others</i>).	1
3.3.2.	Further government bailouts could trigger a lowered credit rating for the country which could have a negative impact on the citizens (<i>bad for others</i>).	1
3.4.	<i>On the other hand:</i> if NKT expresses an inappropriate audit opinion over the Inpahla financial statements, they would be issuing a false statement , and the auditors would be in contravention with the Auditing Profession Act of 2005 (section 44 and 52) and would be found guilty of improper conduct (<i>bad for self</i>).	1
3.5.	In addition, expressing an unmodified audit opinion over financial misstatements that are materially misstated due to fraud will lead to no consequence management for those involved in the fraud (if any) which is not in the best interest of the government or the public (<i>bad for others</i>).	1
3.6.	NKT as a firm has a duty as a corporate citizen and should consider all stakeholder interests and not just Inpahla's in its decision and given the nature	1

	of the circumstances.	
3.7.	The effective functioning of the audit committee should be considered since, with their proper oversight over the audit process, management would be less likely to pressure the auditors into an inappropriate audit opinion.	1
4	Professional ethics considerations for NKT arising from ISSUE 2	
	<i>If, as a result of the pressure that management faces to prevent and conceal a breach of loan covenants, management requests the auditors to express an unmodified opinion over the financial statements, the auditor should consider the following professional ethics considerations:</i>	
4.1.	NKT is a registered audit firm providing professional services to the public and, thus, professional accountants in public practice; hence, the audit engagement team (including the engagement partner) must comply with parts 1, 2 (in capacity as employees of NKT), 3, and 4A (in their capacity as auditors) of the SAICA/IRBA Code of Professional Conduct .	1
4.2.	NKT would need to consider that if they issue an inappropriate audit opinion over a set of financial statements that contain material misstatements, they could be found guilty of misconduct per the IRBA Rules Regarding Improper Conduct for failing to adhere to the Auditing Professions Act of 2005 (section 44).	1
5.	Consideration of threats that could arise towards compliance with fundamental principles:	
5.1.	Due to the implications of the defaults, there might be a perceived intimidation threat if NKT is under pressure (perceived or real) to issue an unmodified audit opinion, and this threat will influence the auditors' adherence of the following fundamental principles:	½
5.1.1.	Integrity Intentionally issuing an inappropriate audit opinion would exhibit a lack of honesty, as NKT would knowingly be associated with false or misleading financial statements.	½ 1
5.1.2.	Objectivity NKT's professional judgement could be compromised by management's emotional blackmail regarding the potential impact of a modified opinion on Inpahla's loan covenants. This creates the risk that the auditor may be biased or pressured into issuing an unmodified audit opinion in response to management's concerns.	½ 1
5.1.3.	Professional behaviour - Intentionally issuing an inappropriate audit opinion over financial statements would result in a breach of the Auditing Professions Act - Issuing an <u>incorrect audit opinion</u> over a set of SOC financial statements that are materially misstated would not be acting in the best interest of the public and may discredit the profession. - Close <u>association</u> with a client (and its management) who are not transparent with key stakeholders in order to protect their self-interest whilst breaching laws such as the Companies Act and potentially the PFMA could reflect badly on NKT's reputation and bring the profession into disrepute.	½ 1 1 1
5.1.4.	Professional Competence and Due Care/Professional Behaviour Issuing an audit opinion contrary to audit findings would be contrary to the requirements of ISA (<i>ISA220R in terms of audit quality ethical requirements; ISA450 for inappropriate evaluation of misstatements identified; and ISA 700R for forming an inappropriate audit opinion</i>) with auditing pronouncements relating to the conduct of an audit.	½ 1

	(Note: the mark is awarded based on the angle of the candidate's discussion – not adhering to auditing pronouncements is a breach section 44 of the Auditing Professions Act).	
5.2.	Level of the threats: It appears that these threats are not at an acceptable level because of the political pressures to improve and report favourable results and the pressure management is under to show good results due to the impact of loan defaults .	1
5.3.	Any threats arising from the ethical issue would be significant/not at an acceptable level due to the significant public interest of Inpahla and the negative impact on stakeholder trust.	1
5.4.	Actions/safeguards to reduce the threats - Safeguards that NKT may consider if they are faced with the ethical dilemma include the following (Maximum 3 marks):	
5.4.1.	Reporting any undue pressure faced to appropriate authorities such as an audit committee, the AGSA, and/or the Regulatory Body (the IRBA).	1
5.4.2.	Seeking guidance from NKT's firm policy in dealing with such matters.	1
5.4.3.	Appoint a quality reviewer to review the audit file and determine if the audit opinion is appropriate.	1
5.4.4.	NKT should take care that all decisions, discussions, and pertinent information are properly documented .	1
5.4.5.	NKT should include more experienced team members on the audit.	1

	Available	41,5
	Maximum	13
<i>12 Business ethics - the PVAA mark is awarded if candidates demonstrate the ability to identify and evaluate the ethical issues arising from the scenario from the perspectives of more than one party or stakeholder (i.e., from the view of management, auditors, and possibly other stakeholders)</i>		1
Total for part (e)		14
Note: The principles for ethical leadership under P1 of the King IV Code are universal ethical principles and candidates are awarded the marks for discussing these, even if they did not link it to King IV.		

Part (f) Discuss the factors that NKT should have considered before the firm accepted the audit of Inpahla for FY2026.		Marks
Exclude the factors considered in part (e) from your answer.		
1	Client consideration	
1.1.	Aspects negatively affecting the integrity of Inpahla and those charged with governance:	
1.1.1.	Instances of crime, theft, irregular tender processes, and corruption have been reported and raise questions regarding management's integrity.	1
1.1.2.	Downgrading by the debt rating agencies given the problems at Inpahla reflect negatively on management and governance oversight and directional leadership.	1
1.1.3.	The political pressure on the company to show improved results could affect management's integrity and decisions made and lead to a possible manipulation of results.	1
1.1.4.	Management's request for exemption from compliance with PFMA and other relevant regulations casts doubt on their integrity, as this shows a disregard for compliance with key laws and regulations intended to protect the public.	1
1.1.5.	Management has disregarded the requirements of section 90(2)(iv) read with (v) of the Companies Act since a cooling-off period of 2 financial years has not yet passed since NKT provided accounting services and hence NKT is not eligible to be appointed as auditors. <i>Note: section 90(2) applies to a person or firm.</i>	1
1.1.6.	In addition, it is questionable whether the audit committee is performing their functions of nominating an auditor that is independent, as set out in section 94(7)(a) of the Companies Act OR Management did not consider the recommendations of the audit committee pertaining to the independence of auditors, as the previous auditing firm held the position for 35 years.	1
1.2.	The auditors should consider the outcomes of any recent performance audits conducted on Inpahla and whether the company's resources are being managed with economy, efficiency, and effectiveness .	1
1.3.	NKT should consider whether prior years' audit reports contained any material irregularities and whether proactive measures are in place to address/resolve them.	1
1.4.	NKT should consider the level of past unauthorised, irregular, fruitless, and wasteful expenditure incurred at Inpahla, and whether management is making a proactive, rigorous effort to reduce them.	1
	Aspects positively affecting management integrity:	
1.5.	A positive factor is that the company has been in operation since 1860 and management has plans to implement turnaround strategies to curtail the losses showing commitment to effective leadership.	1
1.6.	The company has adopted the recommended practices of the King IV Report , suggesting management's effort to strive for good governance and commitment to effective and ethical leadership.	1
1.7.	Management has also demonstrated commitment to preserving the natural environment as Inpahla invested in green initiatives to minimise its impact on the environment and to align with the United Nations Sustainable Development.	1

2	Ethical considerations, including those related to independence	
2.1.	NKT is an audit firm and provides assurance services to the public and, therefore, professional accountants in public practice; hence, the firm and the audit team members must apply sections 1, 3, and 4A of the SAICA and IRBA Codes of Professional Conduct .	1
2.2.	In terms of the Companies Act section 90(2), any person who has been involved in the maintenance of financial records or preparation of financial statements (in the past two years) or habitually performs the duties of accountant will not be perceived as independent and NKT should first evaluate what 'some accounting services' entailed and for how long it was provided to determine if it is allowed to take up this appointment while still being able to adhere to the Companies Act. (Theory)	1
2.3.	The size of the audit fee for the services rendered and the impact on the overall audit fee structure of NKT, as this engagement will bring significant revenue to NKT should be considered.	1
2.4.	NKT needs to consider whether the audit fee from Inpahla represents more than 15% of NKT's total audit fee income. If so, NKT must determine whether a quality reviewer is available , as a review of the engagement quality will be required (ET410.18).	1
3	The following circumstances create threats to the fundamental principles:	
3.1.	Issue 1: NKT has rendered some <u>accounting services</u> to Inpahla during the past five years (ET601.4):	½
3.1.1.	This creates a self-review threat to objectivity since: NKT team members might be biased when assessing financial information/financial statement areas that are derived from the accounting services NKT provided and not appropriately review the judgments that went into the work.	½½ 1
3.1.2.	This also creates a self-review threat to professional competence and due care since: The team may not act diligently when applying the ISAs (especially risk assessment and response) due to overreliance on the prior work executed by the firm.	½½ 1
3.1.3.	This also creates a self-interest threat to integrity since: Since the NKT might overlook material misstatements in financial information/records that were prepared by NKT accounting service providers to hide these in order to avert reputational damage.	½½ 1
3.2.	Issue 2: The Inpahla audit will bring in a <u>significant amount of revenue</u> for NKT and if the fees are significant in proportion to the total audit fees of NKT (ET410.11).	½
3.2.1.	It creates a self-interest threat to objectivity/integrity : - As the audit team members might overlook material misstatements or non-compliance with significant laws and regulations to maintain a positive relationship with management to keep the NKT audit engagement. - The auditors might fail to report reportable irregularities and material irregularities in order to preserve the relationship with the client.	½½ 1 1
3.3.	Issue 3: NOCLAR (ET360) considerations due to many <u>instances of crime and theft that included irregular tender processes</u> and corruption that could include management involvement.	½
3.3.1.	The presence of alleged corruption and fraud creates a self-interest/intimidation threat to professional behaviour : If the team becomes aware of corruption or fraud, they might be tempted	½ ½

	not to disclose this out of fear of association with a client that undermines public confidence or fear that it could create a perception to the public that the auditor was accepting of the behaviour.	1
3.4.	Level of threats/significance of threats – all threats are significant, as Inpahla is a SOC and of significant public interest.	1
3.5.	Safeguards to reduce the level of threats to an acceptable level or to eliminate the threats include (max 2):	
3.5.1.	NKT should not have accepted the audit since the firm is not eligible to be appointed as auditors of Inpahla since no 2-year cooling-off period (required by s90 of the Companies Act) has passed since they provided accounting services.	1
3.5.2.	NKT should consider whether it may be appropriate to appoint a quality reviewer if it aligns with the firm policy.	1
4	Auditor consideration	
4.1.	Whether NKT, as a medium-sized audit firm, has sufficient staff with available time to audit Inpahla, given that it has six divisions and widespread business operations throughout South Africa (increased scope of the audit).	1
4.2.	Whether NKT has the accounting expertise to audit the complex accounting issues resulting from the bonds, forex transactions, and areas of high estimation uncertainty such as the assessment of the appropriate use of the going concern assumption in the preparation of the financial statements.	1
4.3.	Whether NKT has the necessary knowledge/sufficient time to gain knowledge and understanding to audit state-owned entities / given the unique legislation, regulations and accounting and audit requirements relating to it (PFMA, Public Audit Act, etc.).	1
4.4.	NKT staff may not have sufficient knowledge/sufficient time to gain knowledge and understanding of government support, including guarantees , and the impact these have on the assessment of the going concern of SOCs.	1
4.5.	The outcome of communications with the previous auditors , BAC Inc., and whether any professional reasons exist for not accepting the audit engagement (Also consider whether communication with the AGSA would be relevant).	1
5.	Financial responsibility	
5.1.	Given concerns about Inpahla's going concern, consider its ability to pay the audit fee.	1
6.	Preconditions of the audit	
6.1.	NKT should consider whether IFRS is permitted and whether it conflicts with any requirements of the PFMA Act regarding its adoption.	1
6.2.	Given that Inpahla is a state-owned entity, its audit falls within the scope of the Public Audit Act (PAA) and its regulations.	1
6.2.1.	Therefore, the auditor appointment process in terms of the PAA, its regulations and the <i>IRBA Guide for RA's performing audits where the AGSA has opted not to perform the audit</i> must be complied with:	1
6.2.2.	Inpahla should have notified the AGSA of its intention to appoint NKT, and the AGSA must have given its consent for the appointment	1
6.2.3.	Considerations on whether there are any conditions of appointment / reporting deadlines, from the AGSA , that must be accepted by NKT and Inpahla before the appointment, as most SOCs must submit their final audit reports four months after year-end.	1

7	Terms of engagement	
7.1.	The board's comment that an existing engagement letter for accounting services can be used as the engagement letter for the audit will not be sufficient, and a new engagement letter must be agreed upon, because the scope, responsibilities, and the nature of the services required have changed.	1
	Additional issues (from part e) if candidates did not interpret question e appropriately:	
	It appears that management has the intention of hiding any breach of loan covenants , bringing their integrity into question.	1
	Professional ethical consideration related: The auditors may fail to report any reportable or material irregularities arising from management's efforts to conceal a breach of loan covenants.	1
	Management's integrity may be in question if they attempted to unduly influence the audit opinion through emotional blackmail of the impact an unmodified opinion could have on loan covenants.	1
	Professional ethical consideration related: Management is of the <u>view that a modified audit opinion</u> would result in default on loan covenants that could have a significant impact on the company and the economy,	½
	This creates an intimidation threat to objectivity/integrity : The audit team members might feel pressured to issue an unmodified audit opinion regardless of the actual outcome of the work executed on the audit due to concerns of the impact a negative audit outcome would have on the company, jobs in the public sector and potentially the South African economy.	½ ½ 1
Available		50
Maximum		10
<i>X1 Communication skill - the PVAA mark is awarded where candidates presented a balanced discussion of both client-specific and audit firm-specific factors when evaluating whether NKT Inc. should accept or continue the audit engagement.</i>		1
Total for part (f)		11

Part (g)(i) Assess the risk of material misstatement at the financial statement level of Inpahla for the FY2026 audit; and		Marks
The following are factors that will increase the risk of material misstatement at the financial statement level:		
1.	Inpahla bonds' are listed on the JSE, and there is a risk that Inpahla might manipulate the financial statements in order to comply with the requirements of the JSE to be eligible to list bonds and/or to meet shareholders' expectations.	1
2.	Management may have an incentive to fraudulently manipulate the financial statements to meet the financial ratios and other requirements specified in the debt covenants/improve the level of debt , as non-compliance could trigger the immediate repayment of the outstanding debt.	1
3.	Debt agencies have downgraded Inpahla's credit rating , thereby creating incentive for management to manipulate the financial statements to present more favourable financial performance and financial position in an effort to sway the credit agencies' rating in a positive direction.	1
4.	The reported fraud, irregular tender processes and other governance deficiencies may indicate a weakened control environment , which increases the susceptibility of the financial statements to material misstatement due to fraud.	1
5.	Non-compliance with the Companies Act (sections 76 and 90), together with the stringent regulatory requirements of the Public Finance Management Act (PFMA), may create an incentive for management to manipulate financial statements to conceal non-compliance or to present the entity as compliant with applicable laws and regulations.	1
6.	NKT was newly appointed as auditors for FY2026 , and since it will be the first time that NKT audits Inpahla's financial statements:	
6.1.	There is a risk that management will use it as an opportunity to misstate opening balances (as they know the auditor would not have audited the prior year amounts)	1
6.2.	There is a risk that the accounting policies may not be consistently applied compared with prior financial years.	1
7.	The company operates through multiple divisions , increasing the risk that errors may occur when the financial information of the various divisions is aggregated into the company's financial statements , including the incorrect accounting for or elimination of interdivisional transactions.	1
8.	There is a high risk that Inpahla may inappropriately prepare its financial statements on the going concern basis (use of the going concern assumption not appropriate) due to the following (max 3):	1
8.1.	The interim results for FY2026 reflected a significant deterioration in liquidity and an increase in obligations; and the reported operating loss represents a continued increase in losses from previous years.	1
8.2.	There is increased financial pressure resulting from external pressures such as increases in the oil price, loadshedding; the deterioration of the rand and losses stemming from adverse foreign exchange movements.	1
8.3.	There are several operating challenges for Inpahla, including (but not limited to) ageing infrastructure, damage due to train collisions; lack of support from equipment manufacturers; instances of train derailments, which could contribute to ongoing financial strain on the company .	1
8.4.	The inability to settle long-term debts should the loan covenants be breached, resulting in long-term debt becoming repayable immediately place further	1

	financial strain on Inphala.	
8.5.	The legal dispute with the supplier (Wuoche), may significantly disrupt Inphala's operations, resulting in an inability to provide services to customers, reduced tax revenues and increased unemployment. These factors may adversely affect Inphala's future cash flows.	1
9.	Due to the perceived political pressure to improve and report favourable results, management will have an incentive to misstate the financial results to present a better financial position and profits than is actually the case.	1
10.	Inphala is exploring a potential partnership with the private sector ; hence, there is an incentive to manipulate the financial statements by overstating assets and income and understating liabilities and expenses to make the SOC appear like a lucrative investment.	1
11.	There are transactions with related parties (other SOC's, government entities, including national, provincial and local):	
11.1	This provides management with an opportunity to conceal fraudulent financial reporting (transactions not at arm's length).	1
11.2	The related party transactions may not be correctly disclosed in terms of the requirements of IAS 24.	1
12.	The financial statements are subject to an increased risk of material misstatement due to the significant judgments, estimation uncertainty and technical complexity involved in applying multiple IFRS requirements. Examples include (max 2):	1
12.1	IFRS 9: Classification and measurement of bonds, foreign exchange contracts, covenant-related considerations, and financial liabilities.	1
12.2	IAS 21: Accounting for foreign currency transactions and translation.	1
12.3	IAS 36: Impairment assessments require significant estimates of future cash flows and recoverable amounts.	1
The following factors will reduce the risk of material misstatement at the financial statement level:		
13.	Management is committed to finding solutions to funding problems as they have implemented turnaround strategies (government funding and privatisation) which mitigate the risk that the going concern basis of accounting is not appropriate.	1
14.	As the government is the sole shareholder , it could provide financial support for Inphala's operations, given their strategic significance to the country, thereby mitigating the risk that the going-concern basis of accounting is not appropriate.	1
15.	The audit committee's involvement in the appointment of NKT as the auditors/management's reasons for changing auditors is intended to improve public trust in the entity's financial reporting and mitigate conflicts of interest and perceived biases. Therefore, there is a commitment to improve the reliability of financial reporting.	1
16.	The adoption of the King IV Report suggests efforts towards good governance that improve the control environment and reduce the risk of material misstatements.	1
17.	Conclusion: Given the significance of the risks discussed above, the risk of material misstatement at the financial statement level for the company will be assessed as high.	1
Available		27
Maximum		12
Total for part (g)(i)		12

Part (g)(ii) Describe a suitable overall audit response for the FY2026 audit based on your risk assessment.		Marks
Do not address the risks identified in part (g)(i) individually but describe the risk responses in general for all risks.		
1.	Due to the high risk of material misstatement, coupled with a weakened control environment, and increased risks of fraudulent financial reporting, a more substantive-based audit approach will be followed with less reliance on controls.	1
1.1.	The nature of the procedures will also be more detailed testing with less reliance on analytical procedures.	1
1.2.	There will be a focus on opening balances , as it is a first-time audit.	1
1.3.	Lower overall/performance materiality in planning and performing the audit.	1
1.4.	Increase sample sizes and/or locations (divisions) to be tested.	1
2.	The areas of high risk require specific audit attention , which will focus on:	
2.1.	The concerns identified on whether the going concern of accounting is appropriate;	1
2.2.	Compliance with laws and regulations (with reference to irregular tender processes);	1
2.3.	Areas where management has an incentive and opportunity to override controls and engage in fraudulent financial reporting ;	1
2.4.	Legal disputes and their impact on financial statements , including disclosure of notes to the financial statements.	1
2.5.	Identification of unauthorised, irregular, fruitless and wasteful expenditure .	1
2.6.	Presence of material irregularities to be dealt with under the material irregularity process set out in the Public Audit Act.	1
3.	Direction and control of the audit, which will include:	
3.1.	Application of more professional skepticism and judgement in testing and interpretation of findings and management's responses; and	1
3.2.	Incorporating an element of unpredictability in selecting items for testing and the audit procedures to be performed.	1
4.	Given the increased political pressure and debt exposure and the related incentive for manipulation of financial results to meet debt covenants, and allegations of fraud and corruption, NKT should:	
4.1.	Place less reliance on management representation letters and obtain more persuasive evidence ;	1
4.2.	Include more experienced staff on the engagement (involvement of fraud experts and senior staff in the audit); and	1
4.3.	Increased direction, supervision and review of work performed by team members.	1
4.4.	Make use of an engagement quality control reviewer to review the work performed (due to all judgement involved and the increased risk of inappropriateness of going concern basis of accounting).	1
4.5.	Engage experts/specialists within NKT who have public sector audit expertise to support the planning and execution of the audit.	
Available		18
Maximum		6
X1 Communication skill – clarity of expression <i>The PVAA mark is awarded where candidates clearly distinguish between a risk of material misstatement and the auditor's response to that risk. The candidate's expression should make it clear whether the point describes a risk or the auditor's response to that risk.</i>		1
Total for part (g)(ii)		7

Total for part (g)	19
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Part (h) Formulate the audit procedures to perform at the FY2026 year end to audit the going concern of Inpahla.		Marks
1	Standard procedures to assess the going concern status of Inpahla	
1.1	Obtain a management representation letter dealing specifically with the going concern of Inpahla and the status of the turnaround strategies proposed by management.	1
1.2	Inspect the board meetings and have discussions with management on the going concern status of the company and assess whether management's plans (including the turnaround strategies) are significant to overcome the adverse effects of the operational challenges and high debt levels.	1
1.3	Obtain the cash flow budgets and forecast from Impala and perform the following procedures:	
1.3.1	Recalculate/cast and cross-cast the forecasts to verify the accuracy of the forecast.	1
1.3.2	Determine whether the period used by management is appropriate and for at least 12 months .	1
1.3.3	Inspect the cash flow forecasts for obvious errors and omissions (for example, inclusion of non-cash flow terms, duplicate amounts, direction of the in and outflows)	1
1.3.4	Compare the cash flow forecast for the current financial year with events after the financial reporting date (subsequent to year-end) to identify whether adjustments are required to the cash flow forecast/whether additional information is available about amounts included in the forecast.	1
1.3.5	Obtain the budgets and forecast for 2025 and compare with the actual results as per the trial balance/management accounts for 2025 and consider the reliability and accuracy of management's budgeting and forecasts (based on experience, the competence of management in terms of preparing forecasts, etc.);	1
1.3.6	Through discussion with management (or inspection of supporting documentation), assess the knowledge, experience, and competence of the individual(s) who prepared the cash flow forecasts.	1
1.3.7	Through inspection of cash flow forecast/management discussions, assess whether there are indicators of management bias in selecting the method, significant assumptions and data used in performing the cash flow forecast (ISA 540).	1
1.3.8	Through discussion with management, assess whether management has taken the appropriate steps to understand and address estimation uncertainty (ISA 540).	1
1.3.9	Where management has not taken the appropriate steps to understand and address estimation uncertainty, request that they perform additional procedures to do so (ISA 540).	1
1.3.10	Through discussions with management (and if supporting documentation is available), consider the reasonableness of assumptions underlying the forecast.	1
1.4	Inspect loan agreements, guarantee agreements, and other supporting documentation to confirm the existence, legality, and enforceability of arrangements with lenders and credit providers to provide or maintain financial support and evaluate the financial ability of these parties to provide additional funding.	1

1.5	Inspect minutes of the board to review their assessment of the liquidity and solvency of the company/discussions around the appropriateness of going concern and the approval of the cash flow forecast.	1
1.6	Obtain legal confirmation from Inpahla's lawyers to confirm the status of any pending lawsuits and the possibility of outflows in the next 12 months.	1
2	Consider and audit the impact of the turnaround strategies on the going concern of the company	
2.1	Inspect minutes of shareholders' and directors' meetings supporting the turnaround strategies (government as shareholder, board).	1
2.2	Confirm , with management's permission, directly from the government:	
2.2.1	The R47 billion guarantee at the date of finalising the audit and the conditions thereof;	1
2.2.2	The injection of additional equity : amount, condition, date of injection, and	1
2.2.3	The outcome of the request for the reduction/exemption of certain PFMA procurement requirements.	1
3	Privatisation considerations	
3.1	Enquire from the government, as a shareholder (minister), the status of the request/plans for privatisation and the conditions and timeliness, etc.	1
3.2	Enquire from management whether legislative approval has been granted under the Public Finance Management Act (PFMA) for Inpahla to proceed with issuing notice to private sector to consider the proposed partnership.	1
3.3	Inspect the MOI of Inpahla to determine whether there are any restrictions in terms of entering into partnerships/selling of a stake to the private sector.	1
3.4	Discuss with management (lawyers/head of unions) the potential impact of the proposed privatisation on unions and other key stakeholders , including the likelihood of industrial action or legal proceedings.	1
3.5	Inspect supporting documentation/evidence regarding the privatisation arrangements (contracts, agreements, government pronouncements, etc.) and the procedures to be followed when such transactions are on the table.	1
3.6	Enquire from management whether the transaction would be overseen by the National Treasury and the Competition Commission should approval be granted for the transaction to proceed.	1
3.7	Recalculate the entity's key liquidity and solvency ratios using draft financial information/results and evaluate whether they are consistent with management's assessment of the entity's ability to continue as a going concern.	
Available		25
Maximum		10
Total for part (h)		10
Total for part II		54