Part (e)	**Describe the fraud or errors that could occur during the consolidation process that would increase the risk of material misstatement in the *2020 consolidated financial statements* of the TWE Group.** **Ignore any matters related to presentation and disclosure.**	**Marks**
1.	Management may have an *incentive* to override the consolidation process **due to being listed** to misstate the financial results to increase the **share price** to appear more favourable to investors/meet the **listing requirements** due to being listed.	1
2.	Risk that the **management** may *intentionally* override the consolidation process to misstate the financial statements if they are **aware** (opportunity) that **JPA Auditors may not be competent** to perform the audit of DSS.	1
3.	Management may have an *opportunity* to **override group wide controls** in the consolidation process to misstate the group results.	1
4.	**Accounting policies** (significant judgements and estimates) may be **applied inconsistently** by companies within the group and adjustments are not made to reflect group policies, leading to errors on consolidation.	1
5.	There are various intercompany transactions (such as the management fee) which **may not be identified and/or eliminated** upon consolidation.	1
6.	There is a risk that related party transactions are **not at arm's length**. If not at arm's length, possible non-compliance with IAS24/Income tax act/Companies Act.	1
7.	**Group wide controls** may **not be effective** with regard to the *new subsidiary* as this is a new process and errors could be made.	1
8.	**IFRS 3/Consolidations is complex** and may not have been correctly applied. This risk is increased by virtue of complexity related to the following:	1
8.1	Risk that DSS is **equity accounted instead** of being **consolidated** due TWE's inability to apply establish ***control*** in terms of IFRS 10. This is because of the **manner in which control in DSS is obtained** (appointment of majority of directors rather than >50% voting rights).	1
8.2	The nature of the acquisition of DSS (**step acquisition** from 10% to 45%) may increase the complexity of the accounting and subsequently **errors** could be included in **these calculations**.	1
9.	Risk that fair value amounts are inappropriate due to: • **uncertainty/difficulty** involved, **no active market** available for valuations, • the use of incorrect **methodologies and assumptions** used; **incompetent** valuators; valuators not being **independent** etc.	 1 1
10.	Risk that **goodwill will not be determined appropriately** by failing to take into account all identifiable assets or determining the appropriate consideration. This risk is increased due to the following factors:	1
Consideration		
11.	There are **various components** (cash, contingent considerations and previously held interest) **related to the consideration** payable in respect of the DSS acquisition (including contingent consideration) which increases the complexity of the consolidation.	1
12.	The **fair value allocated** to the consideration of the 35% interest in DSS, particularly the shares issued, may not be appropriate.	1
13.	**Not all components related to the consideration may be accounted for** given the difficulty in allocating the R65 000 (transaction cost) payment to Moche Consultants.	1
14.	Risk that the **payment to acting COO** is inappropriately included as part of the consideration even though it relates to future services**.**	1
At acquisition assets		
15.	There is a risk that **Internally generated software** which will **not be**	1

	recognised by DSS.	
16.	Risk that computer equipment and the software intangible asset is **incorrectly eliminated** during the consolidation in error, when it should be depreciated/amortised/written down even though these items are currently sitting at nil values in DSS.	1
17.	Risk of **incorrectly including** the fair value of **accrued leave liability** as part of net assets even though it is a IFRS 3 measurement exception.	1
	Available	**20**
	Maximum	**11**
	Communication skills – clarity of expression	*1*
	Total for part (e)	**12**

Part (f)	**Describe the risks of material misstatement regarding the presentation and disclosure of the related party transactions and balances in the *separate* financial statements of TWE Holdings for FY2020.**	**Marks**
1.	**Inherently** the management of TWE Holdings will have an ***incentive*** to disclose as little information as possible about these transactions, and may also omit any such transactions that may not be perceived in a positive light by the shareholders.	1
2.	TWE Holdings **may fail to correctly (accurately) disclose** the related party transactions and balances in line with the requirements of **IAS 24.**	1
2.1	This specifically appears to be the case in relation to '**remuneration of key management personnel**' **–** as no information is provided on their 'normal' remuneration packages.	1
3.	There may be **difficulty in identifying all related party transactions (completeness) and balances.** This risk is increased given the following:	1
3.1.	The **number of entities/number of transactions among the entities** within the TWE Group.	1
3.2.	The **non-routine nature** of some of the transactions, e.g. intercompany loans may result in **not all of the disclosure requirements** regarding these transactions to be **met.**	1
3.3	**DSS is a new related party** and this creates an inherent risk of errors as management may not have the necessary familiarity with the entity and its operations.	1
4.	It may be **difficult for management to determine the value of the intercompany transactions.**	1
4.1.	This risk is increased given that **certain transactions** such as the management fee/loans may not be carried out **at arm's length**.	1
4.2	**TWE Production is not listed** and the **fair value** of its shares disclosed may be **complex** to calculate.	1
	Available	**10**
	Maximum	**6**
	Total for part (f)	**6**

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Part (g)	**Describe the substantive procedures Awdit should perform to gather sufficient and appropriate audit evidence with regard to the management fee earned from DSS.**	**Marks**
General procedures		
1.	Obtain a **signed management representation letter** relating to ***all assertions*** regarding the management fee earned from DSS.	1
2.	**Obtain client schedules** supporting the **management fee** earned from DSS.	0.5
3.	**Cast and cross cast** these client schedules.	0.5
4.	**Agree the total** of the client schedules to the **general ledger**, **trial balance** and **annual financial statements.**	1
5.	**Inspect the financial statements for adequate disclosures** in relation to the International Financial Reporting Standards, specifically IAS 24.	1
6.	Inspect the schedules and general ledger accounts for any **unusual entries** (negative, zero, large, round numbers and back dated journals).	1
7.	Perform **overall analytical review** (comparing to other subsidiaries within the group, similar industries/auditor's knowledge, month to month, etc.) and • Inspect that a fee has been recorded **for every month** since 1 September 2019 (the date confirmed) till the end of the financial year (i.e. 10 entries) / Perform a predictive analytical procedure on the total amount expected to be recorded in the general ledger (i.e. R140 000 **(14 000* 10 months)).**	1 1
8.	**Follow up on any discrepancies or abnormal relationships / unusual entries** with management via discussion and inspection of relevant *supporting documentation*.	1
Detailed substantive procedures		
9.	Inspect the **minutes of management and board meetings** for the discussion on the management fee to be paid and **approval** thereof.	1
10.	<u>*The contract:*</u> Obtain the agreement between the **TWE Holdings** and its subsidiaries and through inspection of the **underlying agreement / contract confirm:**	1
	a. **The names of the parties involved (TWE and DSS);**	0.5
	b. **The signatures of authorised individuals** from both parties;	0.5
	c. The **date** the agreement was entered into to assess the validity of the transactions; and	0.5
	d. The **terms and conditions** of the agreement entered into (including the *fee charged*).	0.5
11.	If deemed appropriate based on risk responses, obtain a legal opinion regarding the **legality of the contract/arrangement**.	1
12.	<u>*The invoice:*</u> Obtain and **inspect** the **tax invoices** to DSS and perform the following: **Recalculate** the invoice; confirm that it was **made out to DSS**; confirm the **date** of the invoice to ensure that it was recorded in the correct period; confirm the **description of the service**. i.e. That it related to management services.	1
13.	<u>*Related party transactions / market related:*</u> Determine whether the **fees** agreed to in the signed agreement are **market related** by performing the following:	
	a. Inquire with management / inspect supporting documentation for the **method, basis and assumptions** of the management fee charged and assess any **input data** and assumptions for **reasonability**.	1
	b. **Recalculate** the **R14 000** fee based on the input data and **methodology** above.	1
	c. The assessment above can be performed by **comparing the fee charged** and **terms** of the agreement with that charged by **third parties** performing a similar service to assess if the fee is market related.	1

14.	Inspect the general ledger / the schedule supplied of TWE Holdings for the management fee income recorded during FY2020 and agree the amounts per month recorded to the amounts received in the **bank statement** of TWE Holdings.	1
15.	Perform an **external confirmation** for the management fee **expense** recognised in the accounting records / Related party disclosure in the annual financial statements of **DSS** (Confirmation letter), or **JPA Auditors** / component auditors and compare this to the income recognised by TWE Holdings.	1
	Available	**19**
	Maximum	**10**
	Communication skills – appropriate style	*1*
	Total for part (g)	**11**

Part (h)	**Discuss <u>any concerns</u> you may have regarding the summary of *key points listed* in the email sent by Michelle to Arjun**	**Marks**
Specific concerns:		
1.	Michelle identifies DSS as a significant component. If this classification was because DSS includes **significant risks** to the group financial statements, then the communication should include these risks in order for JPA to put more focus on these areas. There was **no communication of the identified significant risks of material misstatement** of the group financial statements that may be relevant to the work of the component auditor.	1
2.	Awdit must not only consider **ethical requirements** (including independence) of JPA <u>in relation to DSS</u> (the subsidiary it is currently auditing) but also the independence of the Component auditor for the TWE **Group** of companies as a whole.	1
3.	It is inappropriate for the component auditor/JPA to set materiality at whatever level they deem appropriate, because • The **group engagement team / Awdit** is responsible to ***set and communicated*** **the component materiality** • **Component materiality** must be **<u>lower</u>** <u>than materiality for the group</u> as a whole) and therefore it is inappropriate for the component auditor/JPA to set materiality at whatever level they deem appropriate.	1 1
4.	The TWE Group Auditors must not only communicate related party transactions among entities within the TWE Group but **all related party transactions** identified (e.g. transactions with *key management personnel* should also be communicated).	1
5.	It is inappropriate for JPA to only communicate the draft audit report as **a final audit report** should be asked for***.*** • A Final audit report must be requested in order to identify the **subsequent event dates** for performance of further audit procedures.	1 1
6.	It is inappropriate for JPA to only communicate the **draft audit report** as ***further information*** should be provided to Awdit for them to determine that the audit of DSS was carried out in terms of all ethical and professional requirements. Also they stated that they will only focus on the consolidation process: • This implies that there is **no involvement** in the work to be performed by the component auditors, no reviews done on any work performed / risks identified and responses implemented / audit work papers drafted.	1 1
7.	It is concerning that no date has been specified by when the audit should be completed. (**completion date**) If the information for DSS is not received on a timely basis, this could delay the consolidation process.	1
8.	ISA 600 specifies the items that the component auditor is **expected to communicated** to the group auditor. These items should be specified in the	

	detail instructions to JPA and **has not been include**d, for example no request for cooperation has been specifically included as required; and the threshold amount (clearly trivial) have not been provided	1
Overall concerns		
9.	The **professional competence and due care** of Michelle (engagement partner) and Arjun (component auditor) is in question because based on the deficiencies in the communication and application of the ISA600 requirements, they may not have the required competence to perform this engagement in terms of required professional standards.	1
10.	Michelle and Arjun are not performing the engagement with **professional behaviour** as this is not in line with the Audit Professions Act, 2005 (non-compliance with laws and regulations).	1
11.	Given the possible **negligence** in the approach followed / not followed in terms of ISAs, the audit firm/engagement partner **can be held liable in terms** of section 46 of the **APA.**	1
12.	As basic requirements of ISA600 have not been adhered to within a group context and we have been performing the audit from 2019 at least, this also brings into question the **ISQC1, Quality control policies and procedures** at the overall firm level (which includes reviews that should have been performed by the Engagement Quality control engagement reviewer (EQCR) before issue of the audit report as TWE is a Public interest entity).	1
13.	Quality control at the engagement level is also a concern because it does not seem that Michelle (the engagement partner) has implemented quality control policies and procedures within the engagement in terms of **ISA220** as there is **no direction, supervision or review** on the audit.	1
14.	This may result in the **work of JPA not being appropriate** for the purposes of the consolidation of the TWE Group and thus causing the TWE Group financial statements to potentially be materiality misstated. There is concerns with regard to the **detection risk** and the consequential **risk responses** in place and ultimately issuing the **wrong audit opinion**.	1
	Available	**17**
	Maximum	**6**
	Communication skills – logical argument	*1*
	Total for part (h)	**7**

Part (i)	**Discuss the impact that the control deficiencies reported by JPA in Arjun's email would have on the *nature of the further* audit procedures Awdit should undertake in relation to the 2020 *consolidated* annual financial statements of TWE Holdings**	**Marks**
Factors to consider in order to respond appropriately:		
1.	As there is currently a control deficiency in the control activities at the subsidiary with regard to occurrence / authorisation of purchases, this will **increase the control risk** at the assertion level for purchases. / **No expectation** of controls operating effectively.	1
2.	As the group auditor we will still need to inquire of JPA / inspect relevant documentation to obtain an understanding of the **nature and significance** of the control deficiencies identified.	1
3.	Consider if the control deficiency is due to a **management override of controls** and could indicate possible fraud by the management (reportable irregularity), which will translate into a **significant risk** (increased inherent risk) at the **assertion level.**	1
4.	Management override of controls could indicate **possible fraud** by the management (reportable irregularity), which will also translate into a significant risk at the **overall level.**	1
5.	The significance of the deficiencies should be taken into account, taking into consideration whether the issue was **isolated** to purchases relating to	

	maintenance of IT infrastructure **and pervasive**.	1
Impact on the *separate* financial statements of DSS / responding to the risk:		
6.	**Purpose** of audit procedures: Awdit should request JPA (the component auditor) to adjust the audit plan at the assertion level and respond to the risk by placing no reliance on the controls and following a **substantive approach** at the assertion level by only performing **substantive procedures**: • **No test of controls** can be performed as there is no expectation that the controls are operating effectively.	1 1
7.	The Substantive procedures will focus on **test of details** and possibly a small focus on analytical procedures because controls are not functioning.	1
8.	The **type** of substantive procedures (ISA330.A5) to be performed by JPA will need to be responsive to the risk and places more reliance on: • **Inspection** of original documentation type of audit procedures and less on **enquiries**; • Evidence performed **directly by the auditor** and less from information provided by the management / staff; • Increased *professional scepticism* when **evaluating any evidence** presented to the auditors from management; • Incorporate additional elements of **unpredictability** in the selection of further audit procedures.	1 1 1 1
Impact at *group level* for TWE Holdings and other subsidiaries / responding to the risk:		
9.	Based on the email provided there seem to be a possibility that **controls exist** that operates at the overall group level that is relevant to the subsidiary. As this indicates a **possible expectation of controls** functioning at group level, the group auditor will respond by performing **test of controls** over the approval of costs incurred at all the group companies.	1
	Available	**13**
	Maximum	**7**
	Total for part (i)	**7**
	Total for part II	**43**

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