Part a) Work paper B100 (Risk of material misstatement and audit strategy)

The following are risks of material misstatement at the overall financial statement level:

The company is listed and the risk exists:
- management might overstate profits & assets to inflate the share price ½
- the company does not comply with the listing requirements resulting in incomplete disclosures, (also PIC own 26% - very active SH) etc. 1

Group of companies and the risk exist that on consolidation:
- inter-company balances and transactions not eliminated (complex consolidation/error on consolidation) ½
- related party transactions not treated at fair value and arm's length/correctly disclosed; 1
- correct disclosure not made for transactions of subsidiaries (e.g. remuneration of directors and prescribed officers); 1
- incorrect conversion of subsidiaries on IFRS for SMEs to IFRS; 1
- incorrect translation of foreign operations (i.e. quarry in Botswana)/Accounting policies in Botswana; 1
- non-compliance with foreign regulation as result of foreign operations; 1

Complex accounting transactions and the risk exist that on misstatement:
- due to complexity of application (business combinations, IFRS 10; 12, etc.) ½

Directors & key management remuneration largely based on performance & share price growth and the risk exists:
- That they have incentives to overstate profits & assets ½

Non-compliance with laws and regulations could point to a lack of management integrity and/or competence increasing risks of:
- Non companies act compliance (Audit Committee composition, non-executive fee approval, share buy-back); 1
- anti-competitive behaviour and price fixing (reason); and 1
- JSE listing requirements (reason). 1

Governance concerns/ weak control environment increasing the risks of manipulation because:
- Chairman not independent as he works 50% of his time for the company ½
- Practices of remuneration committee and how they set remuneration 1

Going concern risk due to: (marks below only awarded if linked to going concern)
- the company making significant losses at year end (liquidity & solvency, cash flow problem); ½
- extended slowdown in infrastructure expenditure in South Africa/African operations; 1
- pending fine from the Competition Commission (reason); 1
- labour problems and strikes which disruption operations 1

Operations are widespread/decentralized, which makes management oversight and control difficult and which could result in possible fraud, etc. 1

Risk resulting from IT operations
- unauthorised access via WAN/ corruption of data (reason) ½
- unauthorised amendment of data stored in the clouds – integrity of data 1
- loss of data stored in the clouds, resulting in incomplete financial records 1

Centralized accounting & IT create opportunity for group management to manipulate records of subsidiaries/(management override of controls) 1

Fraud risk (CFO involved in price fixing, trading in African countries (bribes, etc.)) 1
Briefly discuss a possible audit strategy (i.e. an overview of the nature, timing and extent of the audit procedures and resources required) which would respond appropriately to the risks identified in section (i) above.

(work paper B100)

The risk of material misstatement at the overall financial statement level can be assessed as high based on (i). I would therefore suggest the following audit strategy:

**AUDIT APPROACH**

- Generally a more substantive-based audit approach with less reliance on controls.
- More detailed substantive testing and less reliance on analytics.
- Specific focus on management overrides (year-end journal/control accounts, etc.).
- Decrease/less reliance on management representations (letter).
- More professional scepticism in testing (corroborate explanations with supporting documentation).
- More unpredictability in selecting items for testing.
- Focus on year-end balances and less on early verification (going concern risk).
- More work will need to be done to reduce the risk, **bigger samples, more testing/ Set overall materiality lower**
- given risk (listed company, going concern) –more accounts becomes significant that will require detail testing
- Increase the number and locations of components to be included (all subsidiaries and foreign operations) (increased audit coverage)

**RESPONSE TO SPECIFIC RISK AREAS**

- More work/focus on the going concern problems and assumptions.
- More work/focus on legal compliance (given price fixing, companies act issues, etc.)
- More work on specific consolidation adjustments & IFRS disclosure (related party disclosures, transactions with directors)
- Tests of detail focused on overstatement of revenue/assets and understatement of expenses / liabilities/ **Set lower performance materiality** for risky classes of transactions, account balances or disclosures (provisions, PPE).
- More focus on subsequent events procedures.
- Test general IT controls for shared services/cloud service provider (ISAE 3402 reports)

**RESPONSE IN RESPECT OF AUDIT STAFF**

- More senior and experienced staff on audit.
- Increased extent of supervision of staff and the review work to be undertaken.
- Involvement of quality review partner (listed entity/ISQC 1).
- Given nature of the systems, we would also need IT experts and CAATS.
- Consider **involvement of fraud specialist** (given unethical behaviour of management)/ Consider auditor expert and/or specialists (valuations, IFRS2, etc.)
- Other valid risks and responses (list ..........................................................)  

  Max 1

  Communication skills for part (a): language and clarity of expression  

  : structure and layout  

  Total for part (a): Max 27
**Part (b) Letter to the managing director of CFC noting possible non-compliance by CFC with the Companies Act, and any concerns you have regarding the ethical conduct of CFC’s financial director (WP B100)**

(Note: communication marks for letter only awarded if properly presented)

Dear Sir

The following are areas of concern where CFC and its subsidiaries possibly did not comply with, or is not complying with:

<table>
<thead>
<tr>
<th>THE COMPANIES ACT 71 OF 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Composition of the Audit Committee (S 94)</strong></td>
</tr>
<tr>
<td>The Audit Committee must consist of three directors who are not involved in day-to-day operations (section 94(4)(b)(i))</td>
</tr>
<tr>
<td>The board has three non-executive directors, one of them, the Chairman, spends 50% of his time on company business, and thus is involved in the day-to-day operations and would be disqualified as a member and is not valid</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Directors fees (S 66)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Directors’ fees (non-executive) must be approved by the shareholders via special resolution every two years.</td>
</tr>
<tr>
<td>RemCo approved the fees and not the shareholders, thus the fees are not valid.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Share re-purchase (S 48)</th>
</tr>
</thead>
<tbody>
<tr>
<td>For share repurchases from directors or more than 5% of the issued shares, a special resolution is required.</td>
</tr>
<tr>
<td>Only the board approved the repurchase and thus the transaction is not valid.</td>
</tr>
<tr>
<td>Share repurchase only possible if the requirements of section 46 of the Co-Act are met:</td>
</tr>
<tr>
<td>- the company will satisfy the solvency and liquidity test after the distribution.</td>
</tr>
<tr>
<td>- Given the financial difficulties listed in WP B100, it is unlikely that the solvency and liquidity requirements will be satisfied. (going concern, competition fine, etc.)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Price fixing (SS22, 76 &amp; 77): The directors’ actions regarding price fixing could be:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Directors could be seen to have acted recklessly/ with intention of defrauding certain parties, etc. (S22)</td>
</tr>
<tr>
<td>It could be interpreted that they did not act with the degree of care, skill and diligence required (S76)</td>
</tr>
<tr>
<td>The directors could be held liable (S77)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Number of directors: The company does not have the minimum number of directors (6) S66(2)(b)</th>
</tr>
</thead>
</table>

**ETHICAL CONDUCT**

<table>
<thead>
<tr>
<th>Code of Conduct (par. 100.05 and section 300, par. 300.06 and 300.04)</th>
</tr>
</thead>
<tbody>
<tr>
<td>The financial director (Mr Batting) is a CA(SA) and is accordingly bound by and should comply with the SAICA Code of Professional Conduct.</td>
</tr>
<tr>
<td>Thus he is bound by the fundamental principles (of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour).</td>
</tr>
<tr>
<td>As he was aware of the price fixing (illegal act) and did nothing to prevent this:</td>
</tr>
<tr>
<td>- he did not act with integrity, professional competence and due care, and</td>
</tr>
<tr>
<td>- acted in the public interest, professionally and exhibit professional behaviour</td>
</tr>
<tr>
<td>Mr Batting’s action is contrary to the Code and he should be reported to SAICA Disciplinary Committee</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Business Ethics</th>
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</thead>
<tbody>
<tr>
<td>Price fixing illegal and penalties could arise which would cost the company money.</td>
</tr>
<tr>
<td>Price fixing is also immoral and not in the public interest</td>
</tr>
<tr>
<td>Being party thereto also is contrarily to good corporate citizenship</td>
</tr>
<tr>
<td>The instances of non-compliance with the Companies Act could result in a Reportable Irregularity</td>
</tr>
<tr>
<td>Other valid business ethics considerations (list ....................................................) Max1</td>
</tr>
</tbody>
</table>

Please contact us if we can be of further assistance.

Kind regards

A Auditor (no identification of candidate)

Communication skills for part (b): Letter format and communication skills 1

Total for part (b) Max 12
Part (c)(i) With reference to Work Paper B200 (Risk at assertion level and procedures)

c)(i) Identify the risks of material misstatement related to property, plant and equipment and intangibles

Note: Risk are stated by assertion for presentation purposes only (not asked by assertion & marks should be awarded irrespective)

<table>
<thead>
<tr>
<th>Existence</th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>The risk that repairs and maintenance may be recorded as PPE and not expensed (going concern problems, etc.).</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>The risk that certain property, plant and equipment do not exist given the possible numbers and widespread use (vehicles, furniture equipment).</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Rights</th>
<th></th>
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</thead>
<tbody>
<tr>
<td>The risk that assets are recognised for which the client has no rights, such as freehold land, buildings and mineral rights (subject to legislation, uncertainty, etc.).</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>The risk that capitalised leased plant ASSETS do not qualify for capitalisation (rights have not/will not transfer)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Completeness</th>
<th></th>
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</thead>
<tbody>
<tr>
<td>The risk exists that not all qualifying cost and assets were capitalised for leased assets and decommissioning assets.</td>
<td></td>
<td>1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Valuation</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Land &amp; Mineral rights: risk of incorrect valuation if renewal not granted by government</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>- risk of incorrect calculation of amortization.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Factory decommissioning assets: The risk that –</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- the costs and calculations are not correctly calculated</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- the life of assets and amortisation periods are not correctly estimated</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- certain costs do not meet/qualify for capitalisation criteria</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Plant, vehicles, etc.: The risk that the accounting treatment is not correct/simple calculation for –</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- estimating the residual values and useful lives</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- component depreciation / identification of components</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- the depreciation method</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>The risk that translation of the PPE of foreign operations into rand may not be done in accordance with the requirements of IAS 21.</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Impairment: as a result of:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Difficult trading environment, and the likely increased competition in future, gives rise to an increased risk that the carrying amount of PPE should be impaired (Going concern)</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Difficulty of calculating the value with regard to the value in use of these assets</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Capitalised leased plant – the risk of</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- incorrect accounting treatment in terms of IAS 17:</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- COSTS capitalised that not qualify for capitalisation</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- the plant is capitalised at incorrect amounts, etc.</td>
<td>1</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Disclosure</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk of incorrect disclosure, (IAS 16 and IAS 17 - detailed and complex disclosure)</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Other valid marks (..........................................................)</td>
<td>Max1</td>
<td>1</td>
</tr>
</tbody>
</table>

Total for part (c)(i) Max 9

Part (c)(ii) Substantive procedures to verify the valuation of inventory in CFC’s consolidated financial statement at 30 September 2013 (with focus of inventory of subsidiaries).

<table>
<thead>
<tr>
<th>GENERAL PROCEDURES</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Obtain a management representation letter dealing specifically with the valuation of the different types of inventory</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Obtain a detailed inventory valuation schedule (raw materials, WIP and finished goods) at year end at cost from management, and</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>- cast and cross cast the schedules using CAATS; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- agree the schedule to the general ledger, trial balance and FS.</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Consider the adequacy of the inventory system for providing an accurate basis for the valuation of inventory</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Perform overall analytical procedures on an inventory valuation by comparing actual values at year-end to budgets, production reports, prior years (describe) and follow up on variances</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Using CAATS, identify abnormalities in inventory values at year end, such as negative values</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Review the accounting policy applied and ensures it is in line with IAS 2 requirements</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Review inventory accounts/reconciliation for unusual/abnormal items</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Consider the use of an expert for the valuation of work-in-progress</td>
<td>1</td>
<td></td>
</tr>
</tbody>
</table>
RAW MATERIAL

Agree, by inspection, the cost of selected items to invoices and price lists. 1
Agree the import duties & other direct cost (e.g. transport, handling, insurance, other directly attributable to acquisition) to supporting documentation (invoices or standard costing information) (IAS 2.11). 1
Verify that costs only comprise costs of purchase, conversion and other in bringing the raw materials to their present location and condition (IAS 2.10) (qualifying cost) 1

WORK IN PROGRESS (WIP) / FINISHED GOODS (FG)

Obtain and document an understanding of the methods and procedures for costing work in progress through discussion with management, review system, documentation, etc. (how) 1
Obtain from management their workings and calculations on how WIP / FG were calculated and
- test calculations, and 1
- agree to relevant records, management experts estimates, etc. 1
Material: Trace unit prices of WIP / FG to the detailed priced raw materials inventory listings or to suppliers’ invoices 1
Perform audit procedures regarding direct labour cost, including the following:
- Agree the labour hour content to job sheets, payroll records/or other supporting documentation. (Time) 1
- Ascertain the reasonableness and consistency of estimates of labour content in work in progress; and 1
- Compare pay Rates used to value labour hours to authorised pay rates/other supporting documentation (e.g., standard costing information). 1
Test the costing of the overhead component in WIP/FG to:
- Related supporting documentation (e.g., standard costing information/rates, etc.) 1
- Inspect the nature of the overheads and that it qualify for inclusion (production overheads and not admin) 1
Analytically compare the overhead component for the year to that of previous years, budgets, and different categories of costs (e.g. material, labour) and inspect variances (explain) 1
Ensure through inspection of production record and ledger accounts that unallocated overheads, such as idle capacity variances, are charged to the cost of sales in the current period. 1

IMPAIRMENT TESTING

Obsolescence, slow moving, scrapped, damaged
Ensure slow-moving, obsolete, scrapped or damaged items have been adequately identified, and correctly adjusted for by –
obtaining an understanding of the method used to identify slow-moving products and the process followed for the approval of obsolescence adjustments by enquiry from management/review of documents (how); 1
re-performing all calculations used in the workings supporting the adjustments recorded; 1
comparing the adjustment made at the end of the 2012 financial year to the actual write-offs in the subsequent period (to evaluate the reasonableness of management’s estimates); 1
inspecting production reports, etc., to determine if materials are current and usable / there are markets for them; 1
tracing information obtained during the observation of the physical inventory to management reports of slow-moving, obsolete, scrapped or damaged items; 1
discuss ageing of inventory with management and substantiate against supporting evidence (sales orders received/marketing forecasts; aged listings of inventory balances, etc.) 1
using CAATS, obtaining a report of all inventories that did not move in last 3 to 6 months. 1

Net realisable value
Test on a sample basis, the selling prices on the file against recent sales invoices, and approved price lists. 1
Using the inventory master files received, plot selling prices over the period per line item to determine trends and unusual fluctuations. 1
Test selling costs by enquiry of management as to the method used to compute this line item, and re-perform any calculations (test nature of selling cost) 1
evaluate financial statements/management accounts, etc., to determine the selling costs associated with the products by agreeing to supporting documentation (delivery records, invoices, etc.) 1
Using CAATS, calculate the NRV by taking selling price less selling expenses (how) 1
Compare the adjusted NRV with cost on an item-for-item basis and discuss with management. 1
Re-compute the final allowance and compare to client’s allowance. 1
Where WIP or FG impaired consider the impact on the NRV test of the relevant raw materials that are used in the manufacturing of the finished goods. 1

Other valid marks (.................................................................) Max1

Total for part (c)(ii) Max 16

Communication skills for part (c) – clarity of expression 1

Total for part (c): 26
Part (d) Discuss the control risk for each of the assertions of occurrence, accuracy and completeness regarding sales of cement (WP_N110)

**Note:** A candidate may have stated their answer in the positive or the negative format. During the marking consideration was given to the principle and the manner in which the candidate presented their answers.

### ALL ASSERTIONS

Control risk is **reduced (lower)** by the fact that management supervision and review are present, which result in an effective control environment.  

Control risk is **increased (higher)** given lack of controls regarding access or changes to master file information.

### OCCURRENCE

Control risk is **reduced (lower)** as a result of the following key controls which are present in the system:
- Orders are (not) vetted and approved
- Recorded sales (not) supported by a signed client delivery note
- Delivery note (not) signed by driver & gate control (to lesser extent)

Control risk is **increased (high)** given the following weaknesses in internal control:
- Pre-invoicing could occur as the delivery note goes to the accounting department and could be processed before goods are delivered (not processed from client signed copy).

### ACCURACY

Control risk is **reduced (lower)** as a result of the following key controls which are present in the system:
- Bags of segment: security guard (does not) check all goods leaving the premises against the delivery note and stamps a document as proof of checking.
- Trucks leaving the premises they are (not) weighed at the weighbridge to confirm the 35 tonnage and delivery note is stamped by security guards to indicate compliance.

Control risk is **increased (higher)** given the following weaknesses in internal control:
- There is no mention of edit and validation checks (processing controls) to ensure the accuracy of input. (no testing of accuracy of input)

### COMPLETENESS

Control risk is **reduced (lower)** as a result of the following key controls which are present in the system:
- The delivery note is also (not) signed by the driver to acknowledge receipt of goods.
- A security guard (does not) check all goods leaving the premises against the delivery note and it is stamped as proof of checking (bags and tucks).

Control risk is **increased (lower)** given the following weaknesses in internal control:
- The computer system carries out a comparison of all orders with the delivery notes generated on a weekly basis and produces a printout of outstanding orders, which is then followed up by the sales manager.
- There is no mention of other controls which could ensure completeness of processing, such as batch processing, control totals, etc.
- Documents are not sequentially numbered and followed up (sequence check)

Other valid marks (.................................................................) Max 1

**Communication skills for part (d) – Clarity of expression** 1

**Total for part (d): 10**
### Substantive procedures to assess the appropriateness of the going concern assumption underlying the 2013 consolidated financial statements of CFC

#### PROCEDURES REGARDING GOING CONCERN IN TOTALITY

Obtain a **management representation letter** dealing specifically with the actions taken and view of the directors regarding the going concern status.  

**Discuss with management the going concern status** of the entities in the group and, in particular, those elements that are significant to overcoming the adverse effects of the conditions and events and plans.

Obtain a **cash flow forecast** from management indicating expected cash inflows and outflows for the foreseeable future and:

- Test the **accuracy** of the forecast (castings, calculations);
- Consider the **reasonableness of assumptions** underlying the forecast;
- Perform **analytical procedures** to compare the figures used in the forecast to the comparable figures in the 2013 financial year (explain);
- Consider, based on past experience, the **competence of management** in terms of preparing forecasts (actual v projections); and
- **Confirm** the existence, terms and adequacy of **borrowing facilities**

Obtain a **letter from the entity’s attorney** detailing any possible liabilities which could affect the going concern status of the entity.

Analyse and discuss the CFC group’s **latest available management accounts/financial statements** (compare actual results to budgets to assess the accuracy of management’s estimates).

**Confirm** the existence, legality and enforceability of **arrangements to provide** or maintain **financial support** with related and third parties and assess the financial ability of such parties to provide additional funds.

Inspect and consider the **disclosure of the going concern assumption** in the financial statements.

#### SUGGESTED MANAGEMENT ACTIONS

**General**

Review **minutes of board meetings** for decisions taken and actions in this regard.

Inspect the **cash flow forecast, incorporating management’s actions**, to determine whether the company has sufficient cash to continue operating and paying its debts.

Consider **developments after year end** and whether the management actions materialised/other supportive information (performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity’s ability to continue as a going concern).

**Credit vetting**

Enquire from the **credit controller** if the person has been appointed and discuss with him/her the progress made.

Inspect the **credit vetting policy** and consider its effectiveness.

Inspect the **debtors’ age analysis** at the end of December 2013 / January 2014 and compare to that at the end of September 2013 for a marked decrease in balance.

Compare the **increased debtor collections projected** from this additional appointment (in the forecast) to those that actually materialised (per the cash book).

**Sale of debtors book/securitisation**

Consider any **restrictions on disposal of assets** (e.g. covenants limiting such transactions in loan agreements/encumbrances against assets).

Inspect the **agreement with ABC Finance** for the conditions, date and amounts.

Inspect the **bank account for receipt of the money**.

**Rights issue**

Inspect **minutes of shareholders’ meeting** for **authorisation of the rights issue** and the condition, amounts, etc.

Verify, by inspection of the company’s **MOI**, whether there are **sufficient unissued authorised shares available** for the rights issue to take place.

**Confirm the underwriting** of the **offer** with the **PIC**

Other valid marks (............................................................)  

Max: 1

| Total for part (e): | 16 |
Part (f)  Discuss the treatment of the settlement with the Competition Commission in the 2013 and 2014 consolidated financial statements

**Event after the reporting period**

The settlement is an event after the reporting period as –

- it entails a settlement which is unfavourable to the group because it will result in an outflow of future economic benefits in the form of the penalty paid; and

 - CFC agreed to a settlement on 14 October 2013, which was after the year end of 30 September 2013, and before financial statements were authorised for issue (the 2013 audit was still under way).

- Two types of events exist, namely those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and those that are indicative of conditions that arose after the reporting period (non-adjusting events) (IAS10.3)

  - The agreement to settle with the Competition Commission indicates that an obligation to pay penalties existed at the year-end, as there was already an on-going investigation.

  - Thus the event is an adjusting event after the reporting period and the amount should be recognised in the FS for 2013 (IAS 10.8).

**Recognition and measurement**

A provision should be recognised as –

(a) the entity has a present obligation (legal/constrictive) as a result of a past event being CFC entering into a cartel agreement with other cement producers

(b) it is probable that an outflow of economic benefits will be required to settle the obligation as CFC has agreed to pay a penalty to the Commission, thus creating a constructive obligation.

(c) a reliable estimate can be made of the amount of the obligation:

- amount of the obligation has been reliably estimated at R150 million, (being 6% of turnover.)

- the Commission also filed an application for confirmation of the settlement agreement with the Competition Tribunal (not likely to change).

CFC should recognise a provision of R150 million at 30 September 2013, with a corresponding expense for the penalty in the statement of comprehensive income.

Disclose in financial statements the development of compliance program as part of settlement

**2014 Financial year**

CFC should make an adjustment in its 2014 financial statements to the provision raised in 2013 if the Tribunal changes the amount of the penalty (change in estimate)

Alternative: if a candidate argued that the settlement is a non-adjusting event, they should be awarded a mark for stating that CFC should raise a provision in 2014.

**ALTERNATIVE APPROACH**

Candidates could have argued that the penalty was already accounted for in the 2013 financials and that the SETTLEMENT just provide additional information

Accordingly marks should be awarded for discussion the effect of the SETTLEMENT:

- confirming the provision of R150 million, and the settlement would only lead to a change in disclosure;

- confirming the provision but a different amount than the R150 million was provided, and accordingly accounting for any adjustments in the 2013 financials if a different amount was provided for, or

- if no provision was raised, and only a contingent liability disclosed, the settlement is now confirmed and thus should be provided for in the 2013 financials

**Communication skills for part (f) – Logical argument**

Total for part (f): 9