

Examiner's report

P7 Advanced Audit and Assurance

September 2017

The ACCA logo consists of the letters 'ACCA' in a bold, white, sans-serif font, centered within a solid black square.

General Comments

The examination consisted of two sections. Section A contained one question for 35 marks and one of 25 marks both of which were compulsory. Section B contained three questions of 20 marks each, from which candidates had to answer two questions.

As in previous examination sessions, to score well in the examination candidates needed to demonstrate good technique combined with a strong appreciation of the syllabus, building upon knowledge from both F8 Audit and Assurance and P2 Corporate reporting. Candidates and tutors will also need to be aware of current developments in the field and should take note of the inclusion of new examinable documents and updates to the syllabus in conjunction with recent articles published by ACCA relevant to the syllabus. Two such areas where candidates appear to be referring to out-of-date standards are those on revenue recognition and auditor's reports.

In this exam, well-prepared candidates demonstrated an ability to use their knowledge and experience to relate their answers to the question requirements given. Generally, candidates were able to demonstrate good time management and address the required number of questions. However, many candidates appeared to have lost focus on the requirement or failed to appreciate it in detail and therefore gave answers which were irrelevant and could not gain credit. It is important candidates invest time upfront in analysing what the requirement is asking for rather than spending time detailing points which do not address the requirement.

For candidates preparing for this exam, it is especially important to focus on tailoring the number of points written to the marks available and to take note of areas that the requirement flags as not required. In the past several sessions candidates have been specifically told about areas which did not need to be addressed and many went on to cover those areas regardless, losing time which could be spent earning marks on another requirement.

It is also important to consider at which stage of the audit process a scenario is occurring. At the planning phase of an audit the auditor's report outcome is unlikely to be a discussion point, at completion there may be a requirement for additional procedures to occur but this is not generally something that occurs at the reporting stage when candidates are told the testing is complete and concluded on correctly.

Specific Comments

Question One

This question was set at the planning stage of the audit cycle and was set pre-year end. The question asked candidates to identify and explain business risks and risks of material misstatement from a scenario given on a luxury hotel company. In this respect the requirements resembled those from December 2014. Generally, candidates did well in these sections and were capable of producing explained answers that often scored close to maximum marks.

When preparing for future exams candidates are advised to try and remain focused on the risks which arise from the scenario given for while there are additional risks which may be relevant and obtain credit outside of those there are adequate marks available for explaining the risks arising

from the information given. In particular when addressing risks of material misstatements candidates are more likely to attract credit for the material issues described by the examiner than from those they hypothesize might be present and which may be considered immaterial. It should also be noted that when the examiner states that company brand is not capitalised because it was internally generated this means that it does not give rise to a risk of material misstatement that it should have been on the statement on financial position. Where brands are examined in planning questions the examiner will generally flag whether they are internally generated or purchased.

One important piece of information candidates need to take note of is the year-end date compared to the examination date. Planning questions are generally set prior to the year end and in this examination the year-end date was 31 December 2017. As the examination was sat on 5 September 2017 none of the events within the scenario were subsequent events as they had already taken place four months prior to the year end.

Finally candidates were asked to respond to an email from the finance director of the client. The first connected requirement asked for the implication of the director restricting access of the auditor to information regarding a legal claim and thus giving rise to a potential limitation of scope and some additional points on confidentiality and compliance with laws and regulations. Disappointingly the majority of candidates did not appear to identify that the requirement was specifically referenced to the finance director's email and discussed how to audit the risks identified in part b or made general points on auditing subsidiaries. Attention to the wording of requirements is vital to perform well in examinations in general.

Lastly candidates were asked for audit procedures in relation to a legal case and this was well answered.

Question Two

This question focused on matters and evidence and was set at the completion stage of the audit and was similar to Question four of the sample March/June 2017 exam. In such questions candidates are required to cover the matters arising from each of the issues flagged during the audit where marks are awarded for the calculation and conclusion on materiality, for knowledge of appropriate accounting treatment and for applying that to the question to be able to identify risks or misstatements and whether the treatment described is inappropriate. Candidates are then asked to explain the evidence that the manager would expect to see on the file in order to conclude.

In addressing this style of question, candidates need to demonstrate an understanding of underlying accounting principles and how they have been applied in the scenario. This particular examination covered decommissioning provisions, a change in depreciation estimates and impairments of trade receivables. Candidates generally did well regarding decommissioning provisions but appeared weaker with respect to a change in useful economic life of plant and machinery where many candidates chose to interpret the issue as a change in policy to a revaluation model.

The area of trade receivables tested candidate's ability to apply the skills used in an analytical review and identify that the increase in provision was inconsistent with the fall in collection days and as such candidates often missed the risk in the question of overprovision and spent time discussing the provision being understated.

When candidates are describing evidence expected in these questions, in order to attract marks the evidence must be explained rather than simply a list of documents as the requirement wording is “explain the audit evidence you should expect to find during your file review”. This means candidates should state a purpose as well as a source to attract strong marks here.

Question Three

This question focused on due diligence where a separate team from the firm were working on due diligence at an audit client. Here two issues had been identified and candidates had to explain why they warranted further investigation and what procedures they would perform. Stronger candidates here were able to see the future implication for the valuation of the target company from both the loss of a major customer and a new entrant into the market, and from the ownership of land with restricted use.

Candidates should try to remain focused on the future value of the company in such questions and not dwell on the financial reporting aspects. Here there was a piece of land recorded in the accounts at its historical cost of zero as it had been gifted. A significant portion of candidates spent time on this fact and stated that it was in breach of accounting rules not to revalue PPE. This is not the case, a revaluation model may be adopted by companies but is not required. The market value of the land was important in valuing the company but its carrying amount was not for the purposes of this question.

Part (b) of this question addressed ethical issues which would arise if the firm was to attend a meeting with the bank regarding financing for this acquisition and this requirement was well answered with well-prepared candidates being able to recognise advocacy and intimidation threats.

Candidates often missed the point that a separate team was already preparing the due diligence, as detailed in the scenario and incorrectly recognised the use of separate teams as a safeguard, which was not relevant.

It should be noted that to attract credit for ethical threats candidates should not simply state the name of the threat, they should explain what it means and relate it to the scenario. Simply listing the name of ethical threats does not attract credit. An example of wording required to attract the full credit for advocacy is below

The client’s request for the auditor to attend the meeting with the bank would create an advocacy threat to objectivity, as the auditor would be perceived to be representing the client to the bank, and therefore the bank may take assurance from the auditors’ response regarding the suitability of providing finance.

Question Four

This question presented three scenarios focused on ethical and professional issues and was similar to Question four of the sample September/December 2015 exam. Issues relating to the acceptance of a large multinational client moving away from a large global firm after qualification of their auditor’s report, assisting a listed group with the valuation of an acquisition target, the issue of familiarity and partner rotation in the audit of a non-listed client were covered. Answers often identified the general threats and rules but lacked detail of how they applied to the scenario or the appreciation of listed versus non-listed status and material versus immaterial items in financial

statements.

In this examination, part (a) raised a potential self-interest threat, due to the potentially large fee received for the audit of a large multinational company. As the audit firm is a medium size firm, the fee is likely to be large and therefore the audit firm may become dependent on the fee, particularly if it exceeds 15% of the firm's total income, the threshold for a listed entity.

Many candidates missed the issue in part (c), whereby the company was not listed and therefore it was not mandatory that they adhered to the code requirements for the rotation of the partner after seven years, and that in fact they were adhering to the firm's own internal control procedures.

Question Five

Question 5 was a reporting question focusing on going concern and the adequacy of evidence which had been gathered. Candidates were asked to discuss the sufficiency of several pieces of evidence and needed to be able to identify which elements of an item were covered by the evidence and which would require further investigation. For example, there was a sale and leaseback of assets agreed in principle to cover a cash shortfall for which the evidence obtained was management discussion of the arrangement and the historical cost of the asset included in the non-current asset register. Candidates needed to appreciate that the verbal evidence provided by the director regarding the arrangement needed to be backed up by the finance provider in writing and that the valuation of the property, its condition and its existence were not present in the asset register, merely its historical cost. It should be noted though that the current valuation at historical cost and the fact that the directors' hadn't arranged a valuation did not mean that the financial statements were incorrect or that they were lacking in integrity for not having paid for a valuation.

Candidates were then asked to describe the additional evidence they needed before commenting on a proposed auditor's report.

Candidates were asked to critically appraise an auditor's report in a similar style question to Question 5 of the sample March/June 17 exam. This part of the requirement specifically stated that the firm now had enough evidence to confirm the client was a going concern and the accounts were appropriately prepared on that basis. Often candidates failed to identify that this was the case resulting in incorrect discussion of disclosures regarding going concern in the auditor's report. The proposed report contained an erroneously worded opinion, and an incorrect and unnecessary disclosure on going concern. Candidates had to identify errors in the report such as inappropriate abbreviations and unprofessional language. It is clear from the answers of many candidates that they are still answering with the older format auditor's report in mind and not the current examinable documents. Candidates should check they are up to date with the formats and terminology in the current examinable documents for the session they are sitting the examination.

Conclusion

It is clear again that many candidates did not prepare properly for the exam and failed to learn the topics in sufficient depth. A large number have a narrow focus on the topic that they are studying and are not keeping up to date with changes to accounting standards, such as revenue recognition and auditing standards in relation to auditor reporting.

Once again, candidates are urged to re-learn the basics of auditing – independence, ethics, robust



third party evidence, audit risks and understanding the proper use of audit opinions – and are encouraged to use past questions to help them study and revise for the exam.