

# Examiner's report

## FAU Foundations in Audit December 2013

The ACCA logo is a black square with the letters 'ACCA' in white, bold, sans-serif font.

### General Comments

The examination consisted of ten objective test questions in Section A, worth 20 marks overall, and nine questions in Section B, with one question worth 15 marks, two questions each worth 10 marks and finally six questions each worth 6 marks. All questions were compulsory.

Only a tiny minority of candidates did not answer all of the questions in Section A, and most obtained more than half of the 20 marks available. Most candidates attempted all questions in Section B. Whilst there was a good number of good quality answers submitted and a significant number of good to excellent performances by individual candidates, it was evident that a significant minority of candidates were totally unprepared for the questions in this Section. There were no indications that time pressure was a problem to candidates generally.

Common issues arising in candidates' answers at section B, included:

- An apparent failure to read the question requirement carefully - resulting in answers that contained irrelevant points and few of the available marks being obtained.
- Poor exam technique, often resulting in illegible handwriting, poor layout of questions, overly brief answers (on many occasions comprising two words or less) or, alternatively, longwinded rambling answers - containing few, if any, relevant points.
- Out of context use of technical audit terms in an apparent attempt to obtain marks by including auditing jargon inappropriately.
- Answering with more than the required number of points, and on occasion (seemingly) including a list of wide ranging points in the apparent hope that at least one or some of them may be relevant and so be awarded marks.
- Failure to recognise the auditor's primary objective when reporting to the shareholders of a company.

### Section A

It was encouraging that a significant majority of candidates answered this Section to a pass standard. It was perhaps to be expected that there was a strong correlation between individual candidates scoring well in this section and in section B. Of the ten questions included, three were answered correctly by the majority of candidates. The topics covered by these questions were auditor's independence, the objective of an external audit and the purpose of a trade payables circularisation. Conversely, questions about the auditor's opinion, on inventory and on substantive procedures were answered incorrectly by the majority of candidates. It seems that the primary reason for poor performance in this Section is poor preparation - it is imperative that candidates spend time practising MCQ style questions in preparation for the exam. It is pointless to try to identify discernable pattern of the letters, for example by assuming that if by question seven a letter 'D' answer has not been selected - then the correct answer to the at least one of the remaining questions will be at 'D'. This is because the correct answers in Section A are always set to a random order.

In this section, a many candidates had difficulty with the following question:

Which of the following populations should an auditor start from when testing for the completeness of reported sales of a manufacturing company?

- A Sales receipts
- B Sales invoices
- C Goods despatch notes
- D Sales orders

The correct answer is C. The point at which sales revenue should be recognised by a manufacturing company is the point at which the ownership of goods is transferred to a customer. This is normally the date of despatch/ customer receipt of goods, and the transaction is usually evidenced by a goods despatch note signed (for goods received) and returned by the customer. Contrary to much popular understanding, the resultant sales invoice is merely a formal request for payment in respect of the transaction, and it is used as the source for posting the revenue and right of a claim against a customer, in the company's general ledger. At the end of an accounting period, where a sales invoice has not been raised for goods despatched then an entry should be posted to the general ledger, to recognise the revenue that has been earned and the right to receive payment as a consequence of the goods being despatched and received by the customer.

Given the foregoing, it follows that an auditor should start from goods despatch notes when testing for the completeness of sales of a manufacturing company.

## Section B

It was pleasing that a substantial number of answers submitted to questions on the internal control of a wages system, audit documentation and auditors' professional judgement were answered to a very good pass standard; with a good number of answers to questions on audit risk assessment and planning, going concern and audit evidence also being of a good pass standard.

Of concern was the fact that a significant tranche of candidates did not obtain any of the six marks available for meeting a requirement to state three procedures that should be included in the year – end inventory count of a manufacturing company. Inexplicably a large proportion of these ignored the requirement and proceeded to state three procedures that the auditors should carry out at the inventory count. Of similar concern, was that on the same question (on inventory), a relatively high number of candidates could not provide two procedures that should apply to the company's continuous perpetual inventory counting system or comment correctly on the (lower of cost or net realisable value) principle which the company should adopt in the value of its inventory. With regard to this latter point the range of incorrect answers submitted was surprising with some suggestions having no relevance to inventory valuation.

The Section included a ten mark question testing candidates' knowledge of internal control in a computer - based accounting environment. A large number of candidates encountered problems with this very straight forward question, on application controls and general IT controls. It was apparent that whilst those candidates working in almost any office environment may well have experience of application controls and general IT controls 'in operation', few were able to translate this experience into their answers. Whilst some were obviously familiar with the term "application controls" only a small minority were able to provide two examples of application controls relevant to ensuring the completeness of input of data. Conversely, a disappointingly low number of candidates were able to accurately define the term "general controls" although more provided the requisite two examples of such controls in operation.

Candidates should be aware that this Exam Paper often tests knowledge of audit testing by including a six mark question, in which there is a requirement to state two substantive procedures used to test

assertions relevant to a specified area of a set of financial statements. This particular paper included such a question, with a requirement to state two substantive procedures used to audit prepayments. Many candidates lost marks here with an unduly high proportion confusing tests of control with substantive procedures or being seemingly unfamiliar with the term “prepayments”, with others mustering only one relevant procedure.

## Conclusion

Most of the marks in this paper were again (and will continue to be), allocated to ‘knowledge’ aspects of the Foundations in Audit syllabus, and it is apparent that most candidates fared better with knowledge-based questions, than scenario-based questions - which test the more difficult ‘application’ skills. This is because the majority of candidates have little (if any) practical auditing experience and also because, by their very nature, scenario-based questions often require candidates to consider and display understanding over a range of auditing issues.

Given the above it is vitally important that in working towards the exam, candidates continue to ensure they have a good understanding of elementary auditing concepts including audit risk, internal control, audit evidence and the auditor’s report including the differing types of modified opinion. It is imperative that candidates should be totally familiar with the role of the external auditor, and be able to precisely define the auditor’s primary objective (of expressing an opinion on the truth and fairness of the financial statements - when reporting to the shareholders of a company). Candidates should also ensure that they are able to accurately define or explain the meaning of key terms – for example ‘material misstatement’, ‘control activity’, ‘audit objective’, ‘audit procedure’, ‘test of control’ substantive procedure’ ‘inspection’ ‘observation’ ‘qualified opinion’ and ‘disclaimer of opinion’. Such a level of understanding represents the foundation from which relatively straight forward knowledge-based marks can be obtained and from which practical application skills can be developed by practising exam standard scenario-based questions.

Of note at this session, was that there was a relatively large core of candidates that performed poorly in both Sections A and B. There is no apparent reason for this other than, perhaps, lack of adequate preparation. It is for individual candidates to analyse their performance and determine the reason(s) for their not achieving a “pass” at this sitting. If, on reflection, it is determined that a lack of preparation was the major contributing factor, then candidates should be encouraged and plan to both study and revise hard and constructively, with a view to sitting for the exam again and with confidence, at the earliest opportunity.