

# Examiners' report

F8 Audit and Assurance  
December 2008

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 five compulsory questions (Question 1 for 30 marks. Question 2 for 10 marks and three further questions of 20 marks each). 15 minutes reading time was provided at the commencement of the examination.

The vast majority of candidates attempted all five questions. Many candidates presented their answer to question 1 first, indicating appropriate use of reading time to prepare for the main scenario. A significant number of candidates answered questions in reverse order in this sitting (i.e. 5,4,3,2 and finally 1) or attempted question 2 first, leaving question 1 to the end of the examination. These candidates appeared to encounter significant time pressure at the end of the examination, with question 1 rarely being completed. The pass rate for these candidates was also lower than those where question 1 was attempted first.

Many candidates presented a high standard of answer for all five questions. Question 4 appeared to be the most challenging as this was based on a charity. However, not for profit entities are within the syllabus and candidates who applied their auditing knowledge to this question did obtain a pass standard.

The inadequate performance of many candidates was once again exacerbated by a clear failure to carefully read the content and requirements of questions. Of significant concern this diet was the lack of understanding of the meaning of requirement verbs such as "list" particularly in relation to question 2. Rather than "list", many candidates provided a detailed discussion in their answers; at the extreme some candidates provided 3 or 4 pages of writing in answering this question, when a pass standard could easily be obtained from one page of writing.

As in previous diets, many candidates continue to display their answers inadequately, with a lack of clear labelling to indicate which questions are being attempted. Each question should be started on a new page and candidates must give more thought to the layout and organisation of their answers. Many scripts were also presented quite inadequately, with lengthy paragraphs of writing "hiding" many individual relevant points. Use of headings with short paragraphs is strongly recommended.

## Specific Comments

### Question 1

This question was based on a wages system, being based on an amalgamation of real world information obtained by the examiner. Candidates were expected to use information in the scenario for all sections of the answer apart from section (a).

#### 1a

Candidates were required to list four control objectives of a wages system.

The question was worth 2 marks. Most candidates provided 4 points in their answers, although a minority provided more than 4 (sometimes up to 8 points). However, only a maximum of 2 marks was available. The requirement verb "list" also indicated that no explanation of the control objective was needed; however a minority of candidates did provide a detailed explanation which was not required.

Most candidates provided a list of controls, although a minority did provide significant explanation of the controls; detail that was not needed for this answer.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

**Answer comment**

“The auditor will confirm the accuracy of the wages calculation”

**Examiners assessment of comment**

This is not a control objective of a wages system but appears to relate to audit procedures. The comment is therefore not relevant.

Other common errors included:

- Listing controls over computer systems, not the wages system (e.g. access controls or backup of computer data).
- Provided detailed explanation of each control, which as noted above was not required.
- Stating possible controls from the scenario when generic control objectives of a wages system were required. For example, stating that foremen should observe the clocking in process but the control objective was to ensure accuracy of hours worked.

The majority of candidates answered this question well, with a significant number obtaining full marks.

**1b**

Candidates were required to use the scenario to write a management letter to identify and explain weaknesses, explain the effect of each weakness and finally recommend a method of alleviating the weakness.

The question was worth 14 marks. The requirement stated that 4 weaknesses were required and that 2 marks were available for presentation. The marking scheme was therefore 3 marks for 4 groups of weakness. effect and recommendation plus the 2 presentation marks. A minority of candidates provided more than 4 weaknesses in which case only the best 4 were marked.

Most candidates provided a brief introductory comment in a letter or report format, followed by a table with three columns normally headed Weakness, Effect and Recommendation. This clear presentation made the answers easy to follow. Two other answer formats were also adopted:

- Firstly, using a heading for the weakness (eg lack of authorisation of overtime) and then providing the weakness, effect and recommendation as three paragraphs under this heading. This format was again clear and easy to follow.
- Secondly, a minority of answers listed all the weaknesses in one section, then all the effects in another and finally the recommendations in a third section. Apart from being somewhat repetitive in the comments made, it was very difficult to follow the structure of weakness > effect > recommendation, especially where the order of the points was not followed. For example, weakness 1 could relate to effect 3 and recommendation 2. Answers taking this latter approach were of a lower standard simply because the logic of points could not be followed.

There was also some confusion regarding the requirement to “write a letter”. A significant number of candidates used a report or memo format which was clearly inappropriate. Provision of basic information such as addresses, heading and an introductory paragraph, as outlined in the suggested answers, was expected.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

**Answer comment**

One weakness is that normal working is not monitored.

### Examiner's assessment of comment

Normal working time was monitored. This is an example of a point starting which was not relevant to the question, ie it was not a weakness.

### Answer comment

The code is generally known being based on the name of a domestic pet; this means that any member of staff can amend wages information. I recommend that only the chief accountant knows the code word.

### Examiner's assessment of comment

Although this example is relatively brief, the main issue is that the recommendation does not completely overcome the weakness; the point is the code word also needs to be not so easily "guessable", not simply allowing one official to have the codeword as this is probably not realistic in practice.

Other common errors included:

- Explaining weaknesses that were not part of the scenario. These points normally started "there is no mention of.." indicating that the candidate was attempting to write weaknesses into the scenario which were not evident from the information given. For example, "there is no mention of backup procedures for wages information". While this may be correct, the question requirement was clearly focused on the recording and payment systems as given in the scenario; there was no need to "make up" additional weaknesses.
- Not always fully explaining the points being made. For example, the code word being generally known so any employee could authorise wages does not, in itself, constitute a problem. It is the unauthorised amendment of wages information increasing hours worked, adding "dummy employees," etc that is the problem. In situations such as these candidates were not always awarded a full mark as points had not been fully explained.

Overall, the standard of answers for this section was very high. A minority of candidates did not obtain a pass standard either due to lack of knowledge of wages systems or because this question was answered last and insufficient time was allocated to produce a full answer. The high standard indicates that *letters* of weakness remain popular with candidates.

### 1c

Candidates were required to list three substantive analytical procedures and to state their expectation of the result of each procedure. In other words, candidates were expected to provide valid substantive analytical procedures such as a month by month analysis of salaries and then state expectation in terms of some months salaries being higher because of bonus payments or salary increases.

The question was worth 6 marks. The question requirement was for three procedures giving a clear guide that each substantive analytical procedure was worth 1 mark and the expectation from that procedure was also worth 1 mark.

Most candidates provided three (or sometimes fewer procedures); a minority provided more than three when the best three procedures were marked.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

### Answer comment

"Test the calculation of gross salaries deductions and net salary and ensure that net salary was paid to the correct individual."

### Examiners assessment of comment

The answer appears to be a substantive procedure rather than a substantive *analytical* procedure. The point is therefore not relevant because the question requirement has not been met.

### Answer comment

“Compare manager’s salary to the industry average to determine accuracy of amount paid”.

### Examiners assessment of comment

The point appears to be an analytical procedure; however, comparison to industry average does not necessarily help ensure that the amount paid is accurate as different companies pay different rates. Comparison of salaries to prior years in the same company may be valid if the method of comparison and the expectation of seeing an increase dependent on salary increase and change in number of managers was mentioned.

Other common errors included:

- Stating procedures in very general terms such as reviewing salaries to show that a bonus was paid.
- Inclusion of comments relating to checking overtime amounts; managers were not paid overtime.
- Inclusion of comments relating to the accuracy of the time recording system; not relevant as managers receive a standard amount each month so again they do not receive overtime payments.

The standard of answers for this question was inadequate. Many candidates did not distinguish between substantive procedures and substantive *analytical* procedures, or simply provided vague points, as noted above.

### 1d

Candidates were required to explain various procedures for collecting audit evidence and then to discuss whether the auditor will benefit from that evidence. The specific example of audit procedure of *inspection* was given in the question requirement to indicate that other procedures apart from this were to be included in the answer. Answers also had to refer to the time recording system mentioned in the scenario.

The question was worth 8 marks. The question requirement was to include 4 procedures in the answer. Most candidates mentioned 4 (or sometimes fewer) procedures although a minority mentioned more than 4; in this situation the best 4 procedures were marked. Two marks were therefore available for each procedure. The marking guide was therefore 0.5 for stating the procedure, 0.5 for explaining the procedure and 1 mark for discussing the benefit of the procedure to the auditor.

Most candidates appeared to understand the question and provided an appropriate range of procedures. A minority of candidates mentioned and explained audit procedures such as observation to obtain the first mark for that procedure, but then discussed the benefit by including an actual procedure e.g. observing the clocking in process to ensure this was being followed. This interpretation of the question requirement was acceptable and marked accordingly.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

### Answer comment

“Re-calculation; the benefit of this procedure is that the auditor obtains evidence that clients systems are working correctly, e.g hours worked are correctly calculated.”

### Examiners assessment of comment

The audit procedure and the explanation of the benefit are fine; however, there is no explanation of what recalculation is limiting the marks awarded by 0.5.

### **Answer comment**

For the procedure recalculation -“Ensure that net wages are correctly calculated by the wages programme to show the auditor that the wages programme is working correctly”.

### **Examiners assessment of comment**

While there is some benefit in the procedure, it did not relate to the time recording system. To obtain the mark for explaining the benefit, ensuring that the time recording system had correctly calculated hours worked would have to be mentioned.

Other common errors included:

- Explaining the audit procedure *inspection* although this was specifically excluded by the question requirement.
- Using a list of assertions instead of audit procedures
- Including comments about wages systems in general when the question requirement was to focus on the time recording system.

The standard of answers was variable. Inadequate answers tended only to list procedures and then provide little or no detail on the procedure itself. Many candidates obtained between 6 and 8 marks for clearly stating procedures and explaining them per the question requirement. There tended to be relatively few answers between these extremes.

### **2a**

This was worth 3 marks and required candidates to explain 3 factors that the external auditor should consider when assessing the competence and objectivity of an expert.

Most candidates provided three, or occasionally two, valid points; appropriate qualification, experience and independence from the client being the most popular points. There were very few non-relevant points, the most common being checking the scope of work of the expert, ensuring that the expert had a confidentiality agreement and ensuring that the expert had project management experience.

In summary, the question was well-answered.

### **2b**

This was worth 3 marks and required candidates explain 3 rights that enable auditors to carry out their duties.

Most candidates provided three, or occasionally two, valid points; although there was some confusion regarding rights and professional ethics and experience. The basic points of access to documents, access to directors/explanation and attend and speak at meetings were mentioned by a majority of candidates.

Non-relevant points mentioned included:

- Right to obtain a management letter
- Right to obtain third party confirmations
- Right to resign (unless linked to calling of a GM)
- Right to use an expert.

While the auditor will normally obtain a management letter, for example, the auditor cannot force management to provide this. Marks were generally awarded for the generic points of right of obtain information from management, as noted above.

A minority of candidates approached the question by stating the professional and/or ethical requirements of an auditor; for example the auditor must be qualified and regulated. While factually correct, these points did not relate to the rights of auditors to carry out their duties and so no credit could be given.

In summary, the question was relatively well-answered.

### **2c**

This was worth 4 marks and required candidates list four assertions relevant to the audit of tangible non-current assets and state one audit procedure which provides appropriate evidence for each assertion. With 4 assertions to mention and 4 marks, the marking scheme was clearly 0.5 for each valid assertion and 0.5 for each procedure. The question may initially appear to have been time-pressured, but given 2 marks could be obtained from writing 4 words (that is 4 assertions), this should not have been the case.

A majority of candidates provided 4 valid assertions, with an appropriate audit procedure. However, a significant number of incorrect points were made:

- Providing examples of audit procedures for current, rather than non-current assets. For example stating existence meant seeing inventory in the warehouse or valuation related to the lower of cost and net realisable value. These points were made in all paper variants indicating there may be some lack of paper F3 knowledge going into the F8 examination.
- Mentioning out-of-date assertions such as measurement
- Not linking the audit procedure with the assertion. The most common error here reversing audit procedures for completeness and existence.
- Defining the assertion rather than providing an audit procedure for that assertion.

In summary, the standard of answer was unsatisfactory.

### **3a**

Candidates were expected to explain ethical threats from the scenario provided and then for each threat explain how that threat could be mitigated.

The question was worth 12 marks. There was no requirement for specific number of threats to be mentioned, although the question requirement suggested 6 threats. The mark allocation would be 0.5 for identifying the threat, 0.5 for explaining the threat and then 1 mark for showing how the threat could be mitigated.

Most candidates identified up to 6 points although a minority mentioned 7 or more; the lack of a specific number of threats to mention in the requirement meant that candidates could accumulate marks over more than 6 threats.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

#### **Answer comment**

“The auditor should not accept the balloon ride from the client.”

#### **Examiners assessment of comment**

The answer identifies the ethical threat but does not state why it is a threat. Additional commentary such as showing that the ride would impair the teams' judgement – they would not want to annoy the client for fear of losing the balloon ride, was required to obtain full credit.

### Answer comment

“The threat of the balloon ride needs to be referred to the audit committee and checked against the audit firm’s ethical guidelines. There is a possibility of a threat but more work is needed to determine this; in the meantime the ride could be accepted”.

### Examiners assessment of comment

There is no clear method of mitigating the threat; the answer is attempting to “sit on the” fence rather than provide clear guidance. The only justification for reference to ethical guidelines is in jurisdictions where limited entertainment of auditors is allowed (e.g. Singapore). Correct mention of this point in the answer did enable the candidate to obtain credit.

Other common errors included:

- Not explaining the ethical threat (as noted above). Simply stating a threat was “intimidation” for example, tended to be insufficient as an explanation.
- Mentioning non-relevant points. Firstly, in this situation Zoe being part-qualified would not bar her from being on the audit team as this is how auditors obtain “on the job” training. A significant minority of candidates suggested that the entire audit team had to be qualified indicating a lack of practical audit experience. Secondly, the first time audit for the manager was not a threat; staff have to be changed at some stage. Lastly there was insufficient information to correctly determine a fee dependency threat; the contingent fee and fixed fee were sufficient to discuss in this area.
- Not mentioning sufficient points. A small minority of candidates only mentioned say 3 points and spent up to a page explaining each threat. Candidates are reminded again about the need to check the requirement verbs used in a question and how these relate to the number of points expected in an answer.

The standard of answers for this question was satisfactory; as with question 1(b), ethics appears to be a question most candidates like. As noted above, not providing sufficient points was the main reason for a candidate not achieving a pass standard.

### 3b

Candidates were required discuss the benefits to the company in the scenario of establishing an internal audit department.

The question was worth 8 marks. The marking scheme allowed for 1 point for explaining one benefit of internal audit and a further mark for relating this to the scenario information. In practice, almost all candidates provided a list of benefits of internal audit with little or no reference to the scenario, effectively limited marks to 1 out of 2. However, there was no limit to the number of points that could be made in this section so many candidates still obtained a good pass standard by explaining say 6 or 7 benefits of internal audit in generic terms only.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

### Answer comment

“Internal audit can help establish the internal control system for management.”

### Examiners assessment of comment

This point is technically incorrect; internal audit help to monitor and recommend improvements to the system; establishing the system immediately provides a self-review threat. This point along with duplication of internal control points mentioned below was extremely common.

### Answer comment

“Internal audit will help decrease the cost of external audit”.

### Examiners assessment of comment

The point is correct; however, there is no mention of how the cost reduction will actually happen. Addition detail is therefore needed to *discuss* this benefit.

Other common errors included:

- Repeating points already made. For example, a significant minority of candidates mentioned internal audit and internal control monitoring more than once; obviously only one mark was allowed for this duplication.
- Explaining the work of an audit committee such as recommending auditor appointment. These points did not meet the question requirement and so were not relevant.
- Explaining the problems of establishing an internal audit department. Again, these points did not meet the question requirement and so were not relevant.
- Explaining the benefits of internal audit rather than outsourcing. These comments did not focus precisely on the question requirement regarding the benefits of internal audit to the company in the scenario.

The overall standard of answers was satisfactory. As noted above, most candidates obtained a pass standard by stating generic points about the benefits of internal audit. It was pleasing to find the odd candidate making use of the scenario and providing valid reasons for an internal audit department from the scenario.

### 4a

Candidates were required to explain the term audit risk and then the three elements of risk that contribute to total audit risk.

The question was worth 4 marks. The question requirement was for 4 explanations, so 4 marks was 1 mark per explanation. Many candidates were uncertain of these concepts and did not manage to obtain the marks on offer.

Common errors included:

- Explaining audit risk in terms of errors in the financial statements rather than inappropriate audit reports.
- Omitting to explain that inherent risk is linked to the nature of the entity.
- Stating that control risk was the problem of not identifying the risk, rather than the error or fraud because the control system was inadequate.
- Explaining detection risk as the only risk that the auditor can amend rather than the auditor not detecting errors in the books, records, financial statements, etc.

The overall standard was therefore inadequate. Certainly an area to visit again at some stage.

### 4b

Candidates were expected to identify areas of inherent risk in the charity scenario provided and then to explain the effect of each risk on the audit approach.

The question was worth 12 marks. Given that the question requirement contained two requirement verbs, namely list and explain, and was linked to a scenario, then the mark allocation is 2 marks per point made. 1 mark was available for finding the inherent risk and 1 for explaining the effect on the audit approach. The question contained no upper limit on the number of points to make so marks could be accumulated from more than 6 points. A minority of candidates did mention more than 6 points, although most struggled to mention more than 4.

The standard of answer varied considerably. It appeared that the use of a charity was marginally concerning, although this was within the bounds of the study and followed the style of the examiner from previous diets (for the example the tennis club question from paper 2.6).



Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

**Answer comment**

“Cash is collected by volunteers in a public place. The auditor will need to review the effectiveness of internal controls over this procedure.”

**Examiners assessment of comment**

This point was typical of many. “Cash being collected by volunteers” starts to identify the risk but does not show sufficient detail; mentioning the potential for fraud shows what the risk is. The effect on the audit approach is weak, at best. The internal control system is limited to non-existent, so reviewing the effectiveness of this has little benefit. Other effects on the audit approach that could be mentioned would be the use of substantive analytical review to compare the trend of donations, or possibly observing the collectors to make sure they were not stealing donations for themselves.

**Answer comment**

“There are very few staff meaning that the control system will be weak”.

**Examiners assessment of comment**

The point is potentially correct, as few staff generally means lack of segregation of duties. However, the question requirement was to identify inherent risks, not control risks, hence the point is not relevant.

Other common errors included:

- Not being able to state a clear and logical effect on the audit approach for inherent risks identified, as noted above.
- Explaining control risks such as lack of segregation of duties, as mentioned above.
- Stating the effect on the audit approach in very general terms e.g. for each point stating that “additional substantive procedures will be required.” More focused comments were expected.
- In many situations, simply not stating the obvious. For example, the scenario stated that the taxation of charities was complicated in this specific jurisdiction. Many candidates explained the effect on the audit approach in terms of verifying income and expenditure to source documents, ensuring that the tax liability was paid, or even recommending the appointment of a qualified accountant at the charity to prepare the taxation computation. The obvious thing to do though was simply have a charity taxation specialist on the audit team.

Overall, this was a question that required some thinking but also use of common sense. As the last bullet point above suggested, stating the obvious for the weaknesses mentioned in the scenario would have provided some benefit to many candidates. The standard was therefore inadequate.

**4c**

Candidates were required to explain why the control environment may be weak in the charity in the question scenario.

The question was worth 4 marks. 4 points would therefore obtain the 4 marks on offer. The aim of the question was to try and get candidates to think about the bigger “control environment” issues within the entity. The relatively low mark allocation was to recognise that the question was actually quite difficult as candidates are more used to looking for detailed control weaknesses (see question 1b in this paper).

Common errors included:

- Re-stating points from part (b) as also relevant to part (c). For example, suggesting that cash collection tins should be sealed donations could be recorded incorrectly.
- Omitting the question completely from the candidate's answer.

The standard of answers for this question was inadequate. In any similar question in the future, candidates are recommended to “think big”, that is to see the larger picture of the control system rather than the detailed points such as lack of cash receipts which relate more to control components.

### 5a

Candidates were required explain whether two events were adjusting or non-adjusting (for part (i)) and then explain the auditor's responsibility and actions that should be carried out on the two events (for part (ii)).

The question was worth 16 marks in total. For part (i) with 4 marks, there was clearly 2 marks for explaining whether each event was adjusting or non-adjusting. For part (ii) with 12 marks, again there was clearly 6 marks to explain actions and responsibilities. 2 marks were also available for stating general responsibilities of the auditor regarding subsequent events.

In part (i) candidates normally recognised which event was adjusting and which was not, although a small minority did swap the events around. Candidates were not always clear regarding the reason for the events being adjusting or not, and frequently mentioned non-adjusting events as simply taking place after the end of the reporting period, without reference to the event affecting conditions at that date.

In part (ii), well prepared candidates gave comprehensive answers including many actions that the auditor could take. Less well-prepared candidates tended to focus on making general comments on subsequent events and in many cases providing significant details on the going concern review.

Example comments provided and reasons why those comments did not obtain a pass standard are noted below:

#### **Answer comment (part (i))**

“Event 2 is non-adjusting because it takes place after the year end and the amount of the claim has yet to be determined.”

#### **Examiners assessment of comment**

The answer is almost correct; however, reference must be made to the conditions at the year end to determine whether or not the event is non-adjusting, not the amount of the claim. Stating that the event did not affect conditions at the year-end would therefore be an appropriate comment.

#### **Answer comment (part (ii))**

“Regarding event 1, the auditor needs to amend the financial statements to show the fall in the value of inventory.”

#### **Examiners assessment of comment**

This was a very common error in answers. The auditor is not responsible for amending the financial statements – that is up to the directors of the company. The auditor simply audits the financial statements as amended to form an opinion on whether the amended statements show a true and fair view.

Other common errors included:

- Listing lots of general procedures for subsequent events rather than linking those procedures to the scenario. For example, stating that a lawyer's letter would be obtained but not stating that the lawyer's opinion was needed on the likelihood of being sued for environmental damage.

- Explaining the going concern review in detail. While event 2 could potentially impact on going concern and mention of this was worth a mark, stating 5 or 6 going concern procedures was clearly inappropriate.
- Provision of every possible type of audit report modification/qualification without clearly explaining first that the directors' amendments needed to be reviewed and then the appropriate report produced dependent on those amendments.

In summary there were two distinct types of answer to this section. Firstly, the well-prepared candidate who provided relevant actions that the auditor could take. The less well-prepared candidate who either spent far too much time explaining general points about subsequent events or in a few cases simply ran out of time to make any useful comments. As with similar questions in the past, this question scenario remains a good differentiator of candidate's knowledge and abilities.

### **5b**

Candidates were expected to explain the additional work an auditor should carry out in respect of a fine being levied on their client in respect of a non-adjusting event.

The question was worth 4 marks. Stating 4 relevant procedures would provide a candidate with full marks.

Most candidates provided some relevant and useful procedures such as obtaining revised letters of representation and contacting lawyers for additional advice. The main area that was not fully considered was that the audit report had already been signed; many candidates simply assumed that the auditor would issue a new report and management would accept this. Some candidates recognised the problem of attempting to recall the report and went on to suggest that the auditor speak at the upcoming AGM. Only a minority suggested resignation, which would not have been appropriate anyway given the proximity of the AGM.

Common errors included:

- Suggesting that the auditor would amend the financial statements
- Suggesting that the financial statements needed to include a monetary provision for this non-adjusting event
- Considering every possible type of audit report without any reference to managements' actions.

The standard of answers for this section was therefore adequate.