

RELEVANT TO ACCA QUALIFICATION PAPER P7

Studying Paper P7?

Performance objectives 19 and 20 are relevant to this exam

Change in question style

An examiner's article published in March 2010 explained the rationale for changing the style of question requirements to be seen in UK and IRL papers from June 2010. This article provides further guidance on the new question style, which will be seen in all adaptations of the paper from June 2011, and also gives insight to the examiner's approach to questions in general.

Question requirements

Section A questions will include requirements which are contained within the question scenario itself, usually in an email from an audit engagement partner, or other person, who is requesting that you perform certain tasks relevant to the question scenario. This change in how some question requirements will be presented is not intended to make the questions more difficult. Examples of two past questions, which have been redrafted in this new style, are included in this article.

Section B questions may contain similar requirements, though based on shorter scenarios, where candidates are required to respond to communications presented in the question scenario.

For the UK and IRL adapted papers, the requirements may be differently worded. This is to make the requirements more open-ended and practical in nature, in response to recommendations from the Professional Oversight Board (part of the Financial Reporting Council which oversees the Paper P7 UK and IRL syllabus and exams). In addition, for UK and IRL candidates, requirements may be combined together to form a single requirement covering different aspects of the scenario. These developments of the paper are not intended to make the requirements more difficult, but to allow for a wider range of responses to be made by candidates, especially those who work in audit practice. Again, examples of the open-ended and combined type of requirement are included in this article for UK and IRL candidates.

Practical nature of scenarios

Candidates are reminded of the practical nature of scenarios that they are likely to face in Paper P7. The exams from June 2011 onwards will contain practical requirements asking candidates to demonstrate their ability to apply knowledge in a practical way. For example, candidates may be required to perform analytical procedures, to calculate materiality and to demonstrate its use, or to calculate and explain adjustments necessary to financial statements. It is, therefore, likely that there will be an added emphasis on calculations in some exams,

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though it is the use of such calculations which demonstrates the higher skill, and so it will not be possible to gain more than minimal marks for calculations which are not then utilised to properly answer the specific question requirement.

Application of knowledge

Almost all marks in Paper P7 will be awarded for the application of knowledge. It will not be possible to pass any question requirement by stating rote-learned facts with no application to the given scenario, nor will marks be awarded for facts simply restated from the question scenario.

Opinions, judgment and advice

Candidates are reminded that they should be able to offer an opinion or reach a judgment. There is likely to be increased use of verbs such as 'evaluate', 'justify' and 'assess', all of which require candidates to demonstrate the use of higher reasoning and judgment skills. In addition, requirements may instruct candidates to 'advise' a client on a particular issue. This verb requires candidates to evaluate a situation by examining the information provided, to apply knowledge to the situation, and then give to advice based on the evaluation.

Conclusion

This article has illustrated the different types of requirements that will be seen in Paper P7 from June 2011. The new style of question and emphasis on higher level, practical requirements should indicate to candidates that Paper P7 will remain a challenging exam, but candidates with audit experience and the ability to apply their knowledge to a variety of audit and assurance scenarios should perform well given the practical nature of the paper.

Please note: Candidates are reminded that they must complete either the UK or IRL adapted Paper P2 and P7 to obtain the UK or Irish audit qualification (to practise as an auditor within the UK or Ireland) from June 2011.

Lisa Weaver is examiner for Paper P7

Question examples

Question 1 June 2010 Revised – INT and adapted papers other than UK and IRL

You are a senior audit manager in Vegas & Co, responsible for the audit of the Grissom Group, which has been an audit client for several years. The group companies all have a financial year ending 30 June 2010, and the group's operations focus on the manufacture and marketing of

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confectionery and savoury snacks. None of the companies in the group are listed.

You have just received the following email from Jackson Yip, the audit engagement partner:

To: Audit manager
From: Jackson Yip
Regarding: Vegas & Co – audit planning

Hello

I have just returned from a meeting at Vegas & Co, where I discussed recent events with Li Shen Wu, the group finance director. It seems that this has been a busy year for the group, and notes from my meeting outlining some potentially significant issues are attached.

(a) I would like you to start to plan the audit by preparing some notes, which will be included in the planning section of the working papers, which identify and explain the principal audit risks to be considered in planning the final audit. (18 marks)

(b) As there has been a change in group structure during the year, your notes should also explain the factors that should be considered, and the procedures that should be performed, in deciding the extent of reliance to be placed on the work of Sidle & Co.

(8 marks)

(c) Please also recommend the principal audit procedures to be performed in respect of:

(i) The classification of non-controlling investments made by Grissom Co; (4 marks)

(ii) The condition attached to the grant received by Hodges Co. (4 marks)

Thank you.

Attachment: Notes from meeting with Vegas Group finance director

Grissom Co

This is a non-trading parent company, which wholly owns three subsidiaries – Willows Co, Hodges Co and Brass Co, all of which are involved with the core manufacturing and marketing operations of the group. This year, the directors decided to diversify the group's activities in order to reduce risk exposure. Non-controlling interests representing long-term investments have been made in two companies – an internet-based travel agent, and a chain of pet shops. In the consolidated statement of financial position, these investments are accounted for as associates, as Grissom Co is able to exert significant influence over the companies.

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As part of their remuneration, the directors of Grissom Co receive a bonus based on the profit before tax of the group. In April 2010, the group finance director resigned from office after a disagreement with the chief executive officer over changes to accounting estimates. A new group finance director is yet to be appointed.

Willows Co

This company manufactures and distributes chocolate bars and cakes. In July 2009, production was relocated to a new, very large factory. One of the conditions of the planning permission for the new factory is that Willows Co must, at the end of the useful life of the factory, dismantle the premises and repair any environmental damage caused to the land on which it is situated.

Hodges Co

This company's operations involve the manufacture and distribution of packaged nuts and dried fruit. The government paid a grant in November 2009 to Hodges Co to assist with costs associated with installing new, environmentally friendly, packing lines in its factories. The packing lines must reduce energy use by 25% as part of the conditions of the grant, and they began operating in February 2010.

Brass Co

This company is a new and significant acquisition, purchased in January 2010. It is located overseas, in Chocland, a developing country, and has been purchased to supply cocoa beans, a major ingredient for the goods produced by Willows Co. It is now supplying approximately half of the ingredients used in Willow Co's manufacturing. Chocland has not adopted International Financial Reporting Standards, meaning that Brass Co's financial statements are prepared using local accounting rules. The company uses local currency to measure and present its financial statements.

Further information

Your firm audits all components of the group with the exception of Brass Co, which is audited by a small local firm, Sidle & Co, based in Chocland. Audit regulations in Chocland are not based on International Standards on Auditing.

Required:**Respond to the partner's email.****(34 marks)****Note the mark allocation is shown within the partner's email.**

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Professional marks will be awarded for the presentation and clarity of your answer. (2 marks)

This is potentially how the embedded requirement would be presented for the UK and IRL papers:

**To: Audit manager
From: Jackson Yip
Regarding: Vegas & Co – audit planning**

Hello

I have just returned from a meeting at Vegas & Co, where I discussed recent events with Li Shen Wu, the group finance director. It seems that this has been a busy year for the group, and notes from my meeting outlining some potentially significant issues are attached.

(a) I would like you to start to plan the audit by preparing some notes which will be included in the planning section of the working papers, which identify and explain the matters to be considered in planning the final audit. As there has been a change in group structure during the year, your notes should also recommend the procedures that should be performed, in deciding the extent of reliance to be placed on the work of Sidle & Co. (26 marks)

(b) Please also recommend the principal audit procedures to be performed in respect of:

(i) The classification of non-controlling investments made by Grissom Co; (4 marks)

(ii) The condition attached to the grant received by Hodges Co. (4 marks)

Thank you.

Required:

Respond to the partner's email. (34 marks)

Professional marks will be awarded for the presentation and clarity of your answer. (2 marks)

Revised Question 2, December 2009 (requirements (a) and (b) only) – INT and adapted papers other than UK and IRL

You are a manager in Grape & Co, a firm of Chartered Certified Accountants. You have been temporarily assigned as audit manager to the audit of Banana Co, because the engagement manager has been taken ill. The final audit of Banana Co for the year ended 30 September

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2009 is nearing completion, and you have just received the following email:

To: Audit manager
From: Anaya Kalu, Audit engagement partner
Regarding: Banana Co

Hello

Thanks for taking on the audit manager's role for Banana Co at such short notice. The final audit is nearing completion, and I have attached two items which need your review.

(a) The audit senior has prepared notes for your review in relation to two items recognised in the financial statements. You need to prepare briefing notes for my attention in which you discuss the matters to be considered, and explain the audit evidence you should expect to find in respect of these two items. (12 marks)

(b) In your briefing notes you must also evaluate the audit junior's concerns regarding the management of the audit of Banana Co. These comments were made to me when I visited Banana Co last week and spoke to each member of the audit team. (10 marks)

Thank you.

Attachment 1: Notes for manager's review, prepared by audit senior

Banana Co designs and manufactures equipment such as cranes and scaffolding, which are used in the construction industry. The equipment usually follows a standard design, but sometimes Banana Co designs specific items for customers according to contractually agreed specifications.

The draft financial statements show revenue of \$12.5m, net profit of \$400,000, and total assets of \$78m.

During the year, a new range of manufacturing plant was introduced to the factories operated by Banana Co. All factory employees received training from an external training firm on how to safely operate the machinery, at a total cost of \$500,000. The training costs have been capitalised into the cost of the new machinery, as the finance director argues that the training is necessary in order for the machinery to generate an economic benefit.

After the year end, Cherry Co, a major customer with whom Banana Co has several significant contracts, announced its insolvency, and that procedures to shut down the company had commenced. The administrators of Cherry Co have suggested that the company may be

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able to pay approximately 25% of the amounts owed to its trade payables. A trade receivable of \$300,000 is recognised on Banana Co's statement of financial position in respect of this customer.

Attachment 2 – comments made by audit junior

'I have only worked on two audits prior to being assigned to the audit team of Banana Co. I was expecting to attend a meeting at the start of the audit, where the partner and other senior members of the audit team discussed the audit, but no meeting was held. In addition, the audit manager has been away on holiday for three weeks, and left a senior in charge. However, the senior was busy with other assignments, so was not always available. I was given the task of auditing the goodwill which arose on an acquisition made during the year. I also worked on the audit of inventory, and attended the inventory count, which was quite complicated, as Banana Co has a lot of work-in-progress. I tried to be as useful as possible during the count, and helped the client's staff count some of the raw materials. As I had been to the inventory count, I was asked by the audit senior to challenge the finance director regarding the adequacy of the provision against inventory, which the senior felt was significantly understated.

Lastly, we found that we were running out of time to complete our audit procedures. The audit senior advised that we should reduce the sample sizes used in our tests as a way of saving time. He also suggested that if we picked an item as part of our sample for which it would be time consuming to find the relevant evidence, then we should pick a different item which would be quicker to audit.'

Required:

Respond to the partner's email. (22 marks)

Note the mark allocation is shown within the partner's email.

Professional marks will be awarded for the presentation and clarity of your answer. (2 marks)

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This is potentially how the embedded requirement would be presented for the UK and IRL papers:

To: Audit manager**From: Anaya Kalu, Audit engagement partner****Regarding: Banana Ltd**

Hello

Thanks for taking on the audit manager's role for Banana Ltd at such short notice. The final audit is nearing completion, and I have attached two items that need your review.

(a) The audit senior has prepared notes for your review in relation to two items recognised in the financial statements. You need to prepare briefing notes for my attention in which assess the audit implications of the issues raised by the audit senior. You should also discuss the implications of the audit junior's comments, which were made when I visited Banana Ltd last week. (22 marks)

Thank you.