

Audit and Assurance (AA)

March/June 2025

Examiner's report

The examining team share their observations from the marking process to highlight strengths and weaknesses in candidates' performance, and to offer constructive advice for those sitting the exam in the future.

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General comments

The Audit and Assurance exam is offered in computer-based (CBE) format. The model of delivery for the CBE means that candidates do not always receive the same set of questions. In this report, the examining team share their observations from the marking process to highlight strengths and weaknesses in candidates' performance, and to offer constructive advice for future candidates.

- Section A objective test (OT) case questions – here we look at the key areas for this section in the exam.
- Section B constructed response questions – here we provide commentary around some of the main themes that have affected candidates' performance in this section of the exam, identifying common knowledge gaps and offering guidance on where exam technique could be improved, including in the use of the CBE functionality in answering these questions.

There are two sections to the examination and all questions are compulsory. Section A consists of three OT cases, each comprising five OT questions for a total of 30 marks, which cover a broad range of syllabus topics. In Section B, candidates are presented with one constructive response question worth 30 marks and two constructive response questions worth 20 marks each; testing the candidates' understanding and application of audit and assurance in more depth.

To pass this examination, candidates should ensure they devote adequate time to obtain the required level of knowledge and application. Candidates who do not spend sufficient time practising questions are unlikely to be successful, as the written questions in particular aim to test candidates' application skills.

Section A

Example of a case scenario

It is 1 July 20X5. You are an audit supervisor for Ganymede & Co working on the audit of Jovian Co. The audit for the year ended 31 March 20X5 is at the completion stage and the auditor's report is due to be signed next week. Draft profit before tax is \$1,600,000.

Misstatements

During the audit, the following misstatements were discovered and recorded in the schedule of uncorrected misstatements:

Misstatements	Statement of profit or loss		Statement of financial position	
	Debit \$	Credit \$	Debit \$	Credit \$
(1) Purchases	18,400			18,400
(2) Allowance for receivables	124,000			124,000
(3) Depreciation		114,000	114,000	

- (1) Errors were found when testing a statistical sample of purchase invoices. When extrapolated, this results in a total estimated misstatement of \$18,400.
- (2) Audit procedures over the recoverability of receivables indicate that an additional allowance for receivables of \$124,000 is required.
- (3) A calculation error has resulted in depreciation for the year being overstated by \$114,000.

The finance director has refused to adjust the misstatements in the 20X5 financial statements.

Analytical procedures

All of the ratios calculated when performing final analytical procedures are consistent with the results of the audit work performed, except for the current ratio which has increased from 1.3 at 31 March 20X4 to 1.8 at 31 March 20X5.

Legal claim

While undertaking the audit completion work, it was discovered that a customer has taken legal action against Jovian Co. The customer claims that during 20X5, Jovian Co supplied defective materials and is claiming \$100,000 from the company.

Jovian Co's directors have included a detailed note in the financial statements explaining the issue and the amounts involved. The claim is not due to be settled by the court until after the auditor's report has been signed.

Question one

Which of the following procedures must be undertaken as part of the overall review of the financial statements of Jovian Co?

- A. Perform tests of controls on Jovian Co's procedures for identifying subsequent events
- B. Perform a detailed review of the audit working papers to ensure the audit work has been properly performed
- C. Reassess materiality to confirm it remains appropriate in the context of Jovian Co's final financial statements
- D. Re-evaluate compliance with ACCA's Code of Ethics and Conduct in relation to auditor independence

The correct answer is **C**. The other options would be performed at the completion stage of the audit but not as part of the overall review of the financial statements.

Question two

Indicate, by clicking on the relevant boxes in the table below, whether each of the following statements relating to the misstatements identified by the auditor is **TRUE** or **FALSE**.

The auditor must communicate with those charged with governance of Jovian Co the uncorrected misstatements and the effect they will have on the audit opinion	TRUE	FALSE
The auditor must accumulate all misstatements identified during the audit except those which are clearly trivial	TRUE	FALSE
A summary of uncorrected misstatements must be included with the written representations from management	TRUE	FALSE

Statement 1 is **TRUE**. The auditor must communicate uncorrected misstatements and their potential effect on the audit opinion to those charged with governance (ISA 450, 12).

Statement 2 is **TRUE**. The auditor must keep a record of misstatements identified during the audit unless clearly trivial (ISA 450, 5).

Statement 3 is **TRUE**. The auditor must request written representation from management whether they believe the effects of uncorrected misstatements are immaterial (individually and in aggregate) to the financial statements as a whole. A summary of these items shall be included in or attached to the representation (ISA 450, 14).

Tutorial note: Candidates should not assume that answers will be a mix of true and false in all questions of this type. In this question, all statements were true. Candidates need to be confident with their knowledge and not second-guess themselves.

Question three

Which of the following statements is TRUE in relation to the uncorrected misstatements numbered (1), (2) and (3) for the auditor to issue an unmodified opinion?

- A. Misstatement (1) must be adjusted for as it is based on the results of a statistical sample and may be indicative of a larger misstatement
- B. Misstatements (2) and (3) do not need to be adjusted for as the net effect of these misstatements is not material
- C. Misstatements (2) and (3) must be adjusted as they are individually material
- D. Misstatements (1), (2) and (3) must be adjusted for as they were identified during the audit

The correct answer is **C**. In accordance with ISA 450 Evaluation of Misstatements Identified During the Audit, misstatements which are individually material cannot be offset by other misstatements. Therefore, to avoid a modified opinion being issued, misstatements (2) and (3) must be adjusted.

Question four

Indicate, by clicking on the relevant boxes in the table below, whether each of the following suggestions provide VALID or NOT VALID explanations for the INCREASE in the current ratio.

The allowance for inventory has been increased compared to the prior year	VALID	NOT VALID
The overdraft balance significantly decreased during the year as Jovian Co took out a long-term loan	VALID	NOT VALID

The current ratio will increase if current assets increase or current liabilities decrease.

Statement 1 is **NOT VALID**. Increasing the allowance for inventory will reduce inventory and therefore current assets, therefore would cause the current ratio to decrease rather than increase.

Statement 2 is **VALID**. If the overdraft is converted to a long-term loan, current liabilities will decrease with no effect on current assets, therefore the current ratio would increase.

Question five

All issues identified in the schedule of uncorrected misstatements have now been resolved. The audit evidence obtained confirms that it is possible but not probable that the legal claim will be successful. The legal claim is not fundamental to the users' understanding of the financial statements.

Identify the type of audit opinion which should be given and where, if at all, the matter should be disclosed in the auditor's report.

Type of audit opinion	Type of audit opinion	Disclosure
Unmodified	Type of opinion answer	Disclosure answer
Qualified		
Disclaimer		
Disclosure		
No related disclosure		
Basis for opinion paragraph		
Other matter paragraph		

Although the matter is material, it has been correctly disclosed in the financial statements. As it is not fundamental to the users' understanding, no additional disclosure should be made in the auditor's report. The opinion will be **unmodified** with **no related disclosure**.

Section B

Pimento Co

This 30-mark question is based on Pimento Co, which is a retailer of food and household items with a large network of stores across the country. This question tests candidates' knowledge of the auditors' responsibilities for fraud and error, audit risks and responses, substantive procedures for a trade discount receivable, and ethical threats and safeguards.

Requirement (a) – 4 marks

Explain the responsibilities of Coronado & Co under ISA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements.

Question requirements such as this demonstrate the importance of having a detailed understanding of the ISAs, and in this case ISA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements. This is a relatively straightforward knowledge requirement which has been tested in previous exam sessions and candidates should be aiming to score full marks.

One mark was available for each well explained point, therefore candidates should have provided four well-explained points. It is important to ensure that the points are fully explained as it was common to see candidates only gaining ½ mark rather than 1 mark. For example, simply stating 'the auditor has to obtain reasonable assurance that the financial statements are free from material misstatement' is awarded ½ mark. To gain the other ½ mark the answer needs to add 'whether caused by fraud or error.'

Care should be taken when reading the requirement to ensure that answers focus on the right issues. For example, some candidates incorrectly focused their answers on management's responsibilities despite the requirement only relating to the responsibilities of auditors. In addition, some candidates listed procedures the auditor should adopt when meeting their fraud responsibilities or provided lots of points the auditor should consider when reporting on potential frauds, such as whether this was in the public interest. These are not responsibilities under ISA 240 and so did not gain credit. Candidates must take the time to carefully read and identify key words in the requirement to ensure their answer is relevant.

Requirement (b) – 16 marks

Describe EIGHT audit risks and explain the auditor's response to each risk in planning the audit of Pimento Co.

Marks are awarded for identification of audit risks (½ mark each), explanation of audit risks (½ mark each) and an appropriate auditor's response to each risk (1 mark each). With a scenario-based requirement such as this, good exam technique is critical.

The scenario will typically contain more than the number of risks required, so it is important that candidates plan their time carefully and only attempt to list the required number of points.

The first step is to identify the factors which will give rise to an audit risk. This information can be found in the scenario. The information in the scenario should be read carefully, including the opening paragraph as this may include information relevant to the identification of audit risks. When undertaking this read through it is good exam technique to use the highlight function as this provides a visual aid for quickly spotting audit risks. Having looked at the whole scenario and highlighted relevant points candidates should pick their eight strongest points, re-read them from the scenario, drafting their answer as they go along.

Candidates often use the copy and paste function when drafting answers for the identification of the risk. However, care should be taken to ensure that the risk is actually identified. Simply stating a fact from the scenario is not always the same as identifying an audit risk.

Financial accounting knowledge is also important as audit risks will often focus on the accounting treatment used in the financial statements. In Pimento Co, accounting issues which give rise to audit risks include those relating to inventory valuation, property plant and equipment and bonus issue of shares. Hence a strong knowledge of relevant accounting standards is required to adequately explain the audit risk and provide a relevant auditor response.

Candidates should expect a range of topic areas within an audit risk scenario, some of which may be more challenging than others. In this session it was pleasing to see that candidates were able to confidently identify a good cross section of the risks. However, there was a significant minority of candidates who incorrectly identified as an audit risk that the internal audit department only visit stores every 24 months. This is not a risk that the auditor would be concerned with.

Having identified the risk factor the next step is to explain the risk. To do this, candidates need to state the specific area of the financial statements impacted with an assertion (for example cut off, valuation etc.), or, a reference to over/under/misstated, or, a reference to inherent/control/detection risk. Misstated will only be awarded if it is clear the balance could be either over or understated. If a balance is clearly at risk of understatement then no credit would be awarded if candidates referred to the risk that the balance could be misstated. Candidates cannot hedge their bets by providing both options.

The explanation of the risk must also clearly state the specific area of the financial statements impacted. For example, in respect of the issue relating to the loss on disposal, only noting that non-current assets or assets could be overstated would not be awarded credit. An appropriate explanation in this instance would be that property, plant and equipment could be overstated. In addition, stating that expenses could be understated would not earn credit as it is specifically the depreciation expense that would be understated.

In addition, some risk explanations were inappropriate. For example, for the risk relating to reliance on internal audit, few candidates correctly explained that there was a detection risk if

the work undertaken by internal audit was irrelevant or poorly performed. Also, for the risk relating to the upgrading of the distribution depot facilities, some candidates incorrectly believed this to be a revaluation of the depot, rather than asset expenditure which needed to be correctly classified.

For the risk relating to the inventory valuation methodology many candidates incorrectly focused on how inventory should be valued at the lower of cost and NRV, rather than on whether the methodology adopted was a close approximation to cost, as permitted under IAS 2 Inventories.

For the risk relating to the bonus issue of shares, some candidates incorrectly believed that as a dividend was not being paid, this must mean a going concern risk arises. This is not the case and so no credit was awarded. Candidates must take the time to carefully read the scenario, noting any relevant information, to ensure that they correctly understand and describe the audit risks arising.

Having identified and explained the risk, the next step is to provide the auditor's response. Responses must be practical within the context of the scenario and care should be taken to ensure the response is one an auditor would make and not a management response. Candidates are advised to take a moment to read their responses and ensure that what they are suggesting will help the auditor to form a conclusion on the identified audit risk.

In this session some candidates struggled to produce valid auditor responses for the risk relating to the loss on disposal. Candidates focused on whether the asset disposed of had been removed from the non-current assets register, rather than on whether the loss was a result of an inappropriate depreciation policy.

Additionally, a significant minority of candidates gave general statements of the required accounting treatment. For example, for the inventory valuation risk, it was common to see 'inventory should be valued at the lower of cost and NRV' rather than how the auditor would test whether the valuation method adopted was a close approximation to cost. This general statement approach indicates a lack of practice in tackling different risks and responses questions from previous exams.

Candidates often suggest increased professional scepticism for a whole range of audit risks, and whilst valid, it is not a suitable auditor's response for 1 mark. This is because increasing scepticism does not, on its own, help the auditor to gain suitable audit evidence over the identified audit risk. For the fraud discovered in the finance department, simply stating 'increase professional scepticism' will only gain ½ mark. To gain the full 1 mark, candidates need to focus on additional substantive testing of the affected areas or discussing with management the extent of the fraud and the procedures adopted to identify all potential adjustments. The delay in processing accounting records was the only other risk which gained credit for the need for increased professional scepticism.

Auditor responses do not have to be a detailed procedure, rather it is an approach the audit team will take. Care must be taken however, to ensure that the approach suggested actually addresses

the risk identified and contains sufficient detail. A response of 'discuss with management' will not gain any credit as candidates need to be very clear exactly 'what' they are 'asking management' about. Where further documentary evidence is required, candidates need to refer to this to gain the available 1 mark per response. Also, consideration should be given to the reliability of audit evidence gained; for example, evidence gained via confirmation from a third party, such as lawyers, will be more reliable than verbal representations from management.

Future candidates are advised that audit risk is, and will continue to be, an important element in the syllabus and must be understood. Candidates must ensure that they include adequate question practice as part of their revision on this key topic.

Good scenario-based audit risk questions to practice from published sample exams are: Musitastic Co September/December 2024, Green Co March/June 2024, Knight Electronics Co September/December 2023, Lapis Co March/June 2023, Magpie Co September/December 2022, Esk Co March/June 2022, Peach Co September/December 2021, Corley Appliances Co March/June 2021, Hart Co September/December 2020, Scarlet Co March/June 2020, Harlem Co September/December 2019 and Peony Co March/June 2019.

Requirement (c) – 4 marks

Describe substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in relation to the trade discounts receivable for Pimento Co at 31 August 20X5.

One mark is available for each well-described substantive procedure, therefore candidates should aim to produce four tests for this requirement. Candidates should plan their time accordingly.

Many candidates fail to score well in this type of requirement because their procedures are vague or too brief. Tests must be sufficiently detailed noting clearly which source document should be used and the evidence it will provide. Candidates must ensure that they can distinguish between a substantive procedure and a test of control as many candidates lose marks by giving tests of control when the requirement specifies substantive procedures.

When tackling a substantive procedures question on an unfamiliar balance it is important to consider first principles. Is the balance an asset or liability, is the accounting treatment governed by an accounting standard. A receivable will be due to be received post year end and therefore this can be tested. The discount is from a supplier and is determined by the volume of goods purchased in a year and presumably is based on a percentage or some formula. Therefore, the discount should be recalculated and the volume of purchases with this supplier agreed to the purchases listing. Having taken this first principles approach, an appropriate number of substantive procedures to pass the question can be generated.

Candidates who focused on recalculating the trade discount receivable and agreeing to the trial balance, analytical review of the receivable to prior year/budget, agreeing the payment of the discount to the post-year-end bank ledger account and agreeing the terms of the discount to supplier correspondence/contract were able to gain credit.

When generating substantive procedures, it is important to ensure the tests have sufficient detail and are clear. For example, 'agreeing the payment of the discount post year end' without specifying what the payment is being agreed to will not gain the available 1 mark. It is important to stress that the source document is the post-year-end bank statement or bank ledger account.

In this session a significant proportion of candidates incorrectly provided trade receivables procedures such as reviewing the receivables allowance. The requirement was for a trade discount receivable, but it seemed that candidates ignored the word 'discount'. Take the time to read the question requirement carefully and spend time thinking about what is needed prior to producing an answer.

Requirement (d) – 6 marks

- (i) Identify and explain THREE ethical threats which may affect Coronado & Co's audit of Pimento Co; and**
- (ii) For each threat, recommend an appropriate safeguard to reduce the threat to an acceptable level.**

For ethical threats and safeguard questions candidates are generally asked to identify and explain a set number of ethical threats from a given scenario and give a relevant safeguard to address the threats identified. Candidates are awarded ½ mark for identifying the ethical threat and ½ mark for explaining the implication of the threat. Candidates are awarded 1 mark for each well explained safeguard.

To be awarded the ½ mark for identification, candidates are required to identify the issue from the scenario and correctly state which type of ethical threat it relates to. Both elements must be provided to earn the ½ mark. For example, simply identifying that the audit manager is considering including an audit assistant who is the daughter of the finance director of Pimento Co in the audit team, is not sufficient. The candidate needs to also state that this is a self-interest, familiarity or intimidation threat. The threat arising from the request by the finance director about Habanero Co's going concern status was often incorrectly identified as an advocacy threat, rather than intimidation or confidentiality threat.

The next step is to clearly explain the implication of the threat. Candidates often fail to do this and miss out on the ½ mark available. The explanation needs to be clear as to why this is an ethical issue. For example, just stating 'this will impact the auditor's independence' would not be awarded credit. Candidates must explain HOW independence will be impacted, for example, the self-interest threat arising from the contingent fee could cause the audit team to ignore audit

adjustments which will reduce the profit. For the self-review threat relating to the provision of accounting and bookkeeping services, many candidates simply defined what self-review is, rather than explaining that the auditor may be less likely to challenge their own work or identify potential errors.

The final step is to then suggest a safeguard and it is important that this is phrased as an action; often candidates provide objectives rather than actions. For example, for the threat relating to audit fees being based on the level of Pimento Co's final profit, a safeguard of 'contingent fees are not allowed' will not be awarded credit. To gain the 1 mark available, the safeguard must give a clear action, for example that the audit firm should inform Pimento Co that they cannot agree to the proposed fee basis and that the audit fee will be based on the level of work undertaken.

Additionally, safeguards must be practical, constantly recommending that the audit firm should resign is unlikely to be a sensible safeguard. Whilst resignation would remove the ethical threat it would also result in the loss of work and if every potential ethical threat was resolved by resigning, the audit firm would have no clients left. Resignation should be viewed as the last resort when considering safeguards.

Harper Co

This 20-mark question is based on Harper Co, which is a home furnishings retailer which sells from 20 stores across the country. This question tests candidates' knowledge of outsourcing an internal audit function and control deficiencies and recommendations.

Requirement (a) – 4 marks

Describe TWO ADVANTAGES and TWO DISADVANTAGES to Harper Co of outsourcing its internal audit function.

Candidates were required to describe two advantages and two disadvantages to Harper Co of outsourcing its existing internal audit function. As the verb in the requirement was 'describe' candidates need to ensure that they write enough detail in their answers. Simply providing a few words such as 'cost savings' is not enough for a description. Candidates therefore need to consider when reviewing their answers whether they have written enough.

When tackling this requirement it is important that candidates only consider advantages and disadvantages from the company's perspective. Answers which consider the impact on the outsourced service provider, such as the audit firm, will not gain any credit. In addition, the requirement is for two advantages and two disadvantages, therefore where three points are made for say advantages, then all three will be reviewed, but marks will only be awarded for the best two points. Candidates are therefore reminded to spend time carefully reading the requirement, to ensure that any key words, such as those in capitals, are fully understood.

Commonly awarded points for advantages included gaining access to specialist skills and possible cost savings if the outsourcing fee is less than the employment and training costs of employees. For disadvantages, points were awarded for redundancies and the potential impact on morale and productivity and loss of in-house skills which may be difficult to bring back in future if required. However, it was very common to see incorrect disadvantages of loss of confidential information and the outsourced provider may lack business/industry knowledge. These two points did not earn any marks. Just because the service is outsourced does not mean that there will be a risk to confidential information. The service provider is likely to have the necessary business/industry knowledge, it is knowledge of the company's internal control systems that will be lacking initially.

Requirement (b) – 16 marks

Identify and explain EIGHT DEFICIENCIES in Harper Co's system of internal control and provide a control recommendation to address of these deficiencies.

Marks are awarded for identification of deficiencies (½ mark each), explanation of the implication of the deficiency to the company (½ mark each) and an appropriate control recommendation to address each deficiency (1 mark each).

The first step in tackling deficiencies is to read through the whole scenario in full, this gives an understanding of what the potential answer points are as some deficiencies are easier to explain than others. Having looked at the whole scenario, candidates should re-read it, drafting their answer as they go along. Do not be daunted by the length of the scenario, be methodical and stay focused.

In a multi-cycle question such as Harper Co there is likely to be a good cross section of points across each of the three cycles presented and only eight deficiencies are required.

In identifying deficiencies, candidates often copy and paste facts from the scenario but fail to spot deficiencies. In Harper Co, some candidates identified irrelevant deficiencies such as:

- Sales are generated by members of Harper Co's sales team visiting corporate customers' premises. There is nothing wrong with sales representatives visiting customers.
- Customers pay in cash. The company is a retailer and therefore some customers will always pay in cash.
- Purchase orders are raised without checking the inventory levels. The scenario stated that approved requisitions were received as part of the ordering process. There was no indication in the scenario that inventory levels had not been checked as part of approving these requisitions. Candidates should not assume there is a deficiency unless there is some indication in the scenario.

The least commonly provided deficiency related to goods received by the warehouse only being checked to the supplier's delivery note. In this case the deficiency had to be identified based on

what was not being described in the scenario. The deficiency is the fact that the goods are only checked against the supplier's delivery note and not to the purchase order therefore the company could take delivery for goods not ordered.

Having identified deficiencies, candidates are required to explain the implication to the business. The explanation needs to be specific to each deficiency, as it is not sufficient to state 'this will result in fraud/error' as all deficiencies can lead to increased fraud and error. A clear understanding of how the deficiency will result in fraud and error is needed.

This session it was apparent that some deficiencies were misunderstood by candidates. For the deficiency of credit checks not always being performed for all customers, a significant proportion of candidates referred to a loss of revenue or customer goodwill. To gain the explanation mark it was important to understand that if credit checks were not performed then sales may be made to uncreditworthy customers resulting in irrecoverable receivables.

Also, for the deficiency of the daily sales report being reconciled to cash/credit card receipts once a week, many candidates did not even provide an explanation as to why this was a deficiency. The deficiency relating to payroll calculations not being checked also proved problematic for some candidates. To gain the ½ mark available, candidates needed to state that system errors may arise which may not be spotted leading to under or overstated payroll. Simply stating that payroll may be misstated, without referring to system errors, would result in credit not being awarded as the explanation must be complete.

The next part of the requirement is for candidates to describe control recommendations. To gain the 1 mark available it is imperative that the descriptions of the recommendations are detailed enough. Additionally, recommendations must be actions rather than just objectives, recommendations which are phrased as 'ensure that....' are unlikely to gain much credit.

Candidates need to ensure that recommendations are well described, clearly address the specific control deficiency identified and are practical suggestions. Also, it is important that recommendations are as complete as possible. For the deficiency that the purchasing department does not have access to GRNs, the recommendation of 'give the purchasing department access to view GRNs' would only gain ½ mark. The recommendation needs to also state that the purchasing department should match GRNs to orders or follow up on unfulfilled orders as this is why the purchasing department needs to be able to view the GRNs.

For the deficiency that the payables clerk only uses document count controls when inputting invoices, a significant proportion of candidates focused their recommendations on the seniority of the clerk and recommended that a senior member of the team inputs the invoices or that each invoice is checked by another clerk. These recommendations are impractical and were not awarded credit. The issue here is that input checks need to address completeness and accuracy, and count controls will only address completeness.

Some candidates incorrectly provided tests of controls and even substantive procedures rather than control recommendations. Control recommendations should be focused on what management should do, rather than the auditor.

Good questions to practice from published sample exams include: Granstan Co September/December 2024, Francisco Co March/June 2024, Silver Co September/December 2023, Petra Co March/June 2023, Daley Co September/December 2022, Whittaker Co March/June 2022, Pomeranian Co September/December 2021, Castle Couriers Co March/June 2021, Snowdon Co March/June 2020, Amberjack Co September/December 2019, Freesia Co March/June 2019 and Camomile Co September/December 2018.

Everest & Co

This 20-mark question is based on Denali & Co, an audit firm due to commence the audit of an existing client, Everest Co which manufactures garden furniture. This question tests candidates' knowledge of substantive procedures for property, plant and equipment (PPE) and a current asset receivable, going concern procedures and auditor's reports.

Time allocation should be based on 1.8 minutes per mark. Therefore, the available time should be split at 11 minutes for requirement (a), 7 minutes for (b) and 9 minutes for each of (c) and (d). One mark is available for each well-explained procedure therefore candidates should aim to produce 6 tests for requirement (a), 4 tests for (b) and 5 tests for (c).

Candidates must strive to understand substantive procedures and apply good exam technique. This includes tailoring procedures to the specific requirements of the question. Too often candidates have rote learnt a set of standard tests and these are then produced for each requirement without consideration of their relevance to the scenario provided. This approach tends to generate few marks. Audit procedures must be sufficiently detailed, for example, 'review disclosures' would only score ½ mark. To score a full mark the procedure should go on to say, 'in accordance with accounting standards/relevant legislation'.

Requirement (a) – 6 marks

Describe substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in relation to the matters identified regarding Everest Co's property, plant and equipment (PPE).

The scenario for this requirement stated that an earthquake occurred near the site of one of the company's three factories. This factory was significantly damaged, but all other company properties and inventory were unaffected. \$0.8m had been spent on repairing the factory, of which some was recognised within PPE. The company also incurred asset expenditure on the purchase of new plant and equipment to replace assets which were damaged and were therefore scrapped.

It is important to consider the issue in the scenario and compare this to the question requirement. Question requirements can sometimes focus on a specific assertion such as valuation or completeness, or on a particular element of an account balance, such as just revaluations. Where this is the case, care must be taken to ensure that answers only relate to this assertion or account element. Spending time understanding the issue and carefully reading the question requirement ensures that the procedures given are tailored and more likely to score marks. This requirement was only in relation to 'matters identified regarding Everest Co's PPE' therefore general PPE procedures would not gain credit.

The scenario contained details of the cost of repairing the damaged factory, of which only some expenditure had been included in PPE, therefore the remainder must have been expensed as repairs and maintenance within the statement of profit or loss. For plant and equipment there were additions as well as disposals of scrapped assets. Candidates should have considered how to test each of the three elements of the scenario; treatment of the repair costs of the factory, additions of plant and equipment and disposals. Two substantive procedures should then have been generated to test each element.

Procedures such as casting the additions and agreeing them to the non-current assets register, agreeing additions to invoices to ensure in company name and correct value recognised, physically inspecting the additions for existence, recalculating the depreciation expense for the correct time period, reviewing a breakdown of the \$0.8m spent on repairing the factory and agreeing to invoices that the \$0.5m recognised as PPE was in fact PPE and reviewing the disclosures for compliance with relevant accounting standards would all gain credit.

Some candidates included procedures such as obtain written representation from management and review board minutes for authorisation of the additions, both of which did not gain credit. Requesting written representation should be restricted to areas where the auditor is relying on management's judgement or where there is little independent evidence available. Reviewing the board minutes for authorisation is a test of control rather than a substantive procedure.

Additionally, some candidates ignored the requirement to only provide procedures for the matters identified and listed generic PPE tests such as for revaluations. A significant minority also provided procedures for inventory, this is despite the scenario stating that inventory was not damaged, and the requirement only related to PPE. Candidates must carefully read the information in the question and tailor their answers accordingly so that tests fit with the requirement and scenario.

Requirement (b) – 4 marks

Describe substantive procedures the auditor should perform to obtain sufficient and appropriate audit evidence in relation to the matters identified regarding Everest Co's current asset receivable.

In common with part (a) it is important to carefully consider the requirement and review the scenario to understand the issue being described. In this case the scenario indicated that a claim

had been submitted to the insurance company for the damage to PPE caused by the earthquake as well as for loss of profits. The scenario clearly stated that a current asset receivable had been included within the financial statements for the total claim of \$1.8m.

As the requirement is for 4 marks, only 4 procedures were required. Straightforward procedures which gained credit in this session included reviewing correspondence with the insurance company for the status of the claim, reviewing the post-year-end bank ledger for payments received and agreeing this to the financial statements, reviewing the board minutes to assess whether the directors believe the insurance claim will be successful, obtaining written representation on managements view of the outcome of the claim, and reviewing the disclosure of the insurance claim is in accordance with accounting standards.

Common incorrect procedures included:

- Procedures relating to trade receivables. The insurance claim is not a trade receivable.
- Contact the company's lawyer. This was an insurance claim and so contacting lawyers is irrelevant.
- Contact the company's insurance company. The insurance company will not respond to a request from the audit firm as to whether the claim will be paid.

Candidates must ensure they practice generating substantive procedures for different account balances. Good examples to practice are: Tennessee & Co September/December 2024, Cookit Co March/June 2024, Latte Co September/December 2023, Heron Co March/June 2023, Pacific Co September/December 2022, Spinach Co March/June 2022, Danube Co September/December 2021, Purrfect Co March/June 2021, Sagitarrii & Co September/December 2020, Encore Co March/June 2020, Spadefish Co September/December 2019, Hyacinth Co March/June 2019, Jasmine Co September/December 2018, and Gooseberry Co March/June 2018.

Requirement (c) – 5 marks

Describe the audit procedures the auditor should perform in assessing whether or not Everest Co is a going concern.

One mark is awarded for each valid going concern procedure and therefore 5 procedures are required for full marks. There are many standard going concern procedures and these can be supplemented by procedures generated from the information in the scenario.

The scenario contained details of an overdraft facility on which the company relies heavily, and the renewal of the facility is annually reviewed by the bank. The overdraft facility has covenants relating to minimum levels of profit and total assets. Candidates can use this information to generate appropriate procedures. Credit would be awarded for procedures such as reviewing bank correspondence to assess the likelihood of the overdraft facility renewal, reviewing financial

statements for the impacted areas to assess whether the covenants are likely to be breached and discuss with management alternative financing options if the overdraft facility is not renewed.

Having considered procedures specific to the scenario, candidates could list standard going concern procedures such as review of cash flow forecasts and assumptions for reasonableness, review of board minutes for discussions on matters related to going concern, and review of disclosures and their appropriateness in relation to going concern.

Some candidates listed going concern indicators rather than procedures and these were not awarded any credit. In addition, a number of procedures were too brief or vague, often not giving the source for the test, or, stating 'ensure' without explaining how the test would achieve this. For example, 'contact the company's lawyers' would not have gained any credit, to obtain the available mark the procedure should be 'contact the company's lawyers to enquire of any litigation and the likely outcome'.

Requirement (d) – 5 marks

Discuss the issue and describe the impact on the auditor's report of Everest Co of ADEQUATE and INADEQUATE going concern disclosure.

Although auditor's reports feature regularly in the AA exam, there are several ways in which they can be tested, and candidates must be prepared for any type of question. For this requirement marks are awarded for a discussion of the issue (1 mark), the impact on the auditor's report of adequate disclosure (2 marks) and inadequate disclosure (2 marks).

The first step is to identify the issue. This should be relatively straightforward as the details will be provided. In this case the issue relates to whether going concern uncertainties relating to the renewal of the overdraft facility have been adequately disclosed in the financial statements.

To be awarded the mark for discussing the issue, candidates should not just copy and paste the information from the question but must explain the impact. In this case the issue is that renewal of the overdraft facility will be decided after the auditor's report has been signed. This is a material uncertainty (½ mark) and the effect on the auditor's report depends on the adequacy of the disclosure (½ mark). Many candidates still do not attempt this part and therefore cannot be awarded the 1 mark available.

Knowledge of ISA 570 Going Concern will help in considering the next part of the requirement which is the impact on the auditor's report of both adequate and inadequate disclosure. Answers should be clearly split into adequate and inadequate disclosure. In this session candidates that structured their answers in this way tended to generate more relevant answers and ensured that they considered both parts.

Those who did not split out the two possible outcomes often failed to consider adequate disclosure, and it was difficult to see which points related to which outcome, resulting in difficulties allocating marks.

If the going concern issue has been adequately disclosed, then the auditor's report would contain an unmodified opinion (½ mark) as the financial statements are true and fair (½ mark). However, to score well, candidates should consider whether any additional communication would be required in the auditor's report. A material uncertainty relating to going concern paragraph would be required (½ mark) which is cross referenced to the disclosure note in the financial statements (½ mark). A clear statement that the auditor's opinion is not modified would also be necessary.

Inadequate disclosure of the contingent liability will result in a modification of the opinion and therefore this part of the requirement is more typical of standard questions on auditor's reports. When considering the impact of the modification, answers must clearly state the type of opinion required e.g. qualified opinion, adverse opinion, disclaimer of opinion, and whether this is due to a material misstatement or due to an inability to obtain sufficient and appropriate audit evidence.

In respect of Everest Co, if the disclosure is inadequate then there is a material misstatement which is likely to be material not pervasive and therefore a qualified opinion is appropriate. It should also be remembered that a modified opinion will affect the basis for opinion paragraph. For example, it will include an explanation of why the opinion is modified.

When attempting questions on auditor's reports, it is important to ensure that the correct terminology is used. No credit is awarded for recommending an unqualified opinion as it should be an unmodified opinion. Additionally, candidates should note that an emphasis of matter paragraph is not relevant for going concern uncertainties.

This session a minority of candidates did not attempt this requirement. However, it is important that candidates adequately prepare themselves for questions relating to all types of auditor's reports as well as any other part of syllabus area E. A good example to practice is Jasmine Co from the September/December 2018 sample exam.