

Examiner's report

P7 Advanced Audit & Assurance

December 2015



General Comments

The examination consisted of two sections. Section A contained two questions totaling 60 marks. Question 1 was worth 35 marks and question 2 was worth 25 marks. Section B contained three questions of 20 marks each, from which candidates had to answer two questions

In general, candidates managed their time well in the exam with the majority of submitted scripts being complete or substantially complete. Time management and presentation were generally well evidenced however some weaker candidates attempted to present answers in a columnar format. This typically scores fewer marks as these answers more often than not lack the depth and application that is required at this level. At this level candidates are required to apply their knowledge to specific scenarios rather than state a generic point.

A good understanding of both audit and financial reporting issues is required in order to perform well in this exam so candidates who are able to discuss both these elements demonstrate more effective application and analytical skills. Many of the weaker scripts indicated that candidates had limited knowledge of auditing principles and that candidates struggled to appropriately apply their knowledge to question scenarios.

A common reason for poor marks in this exam is failing to read and remain focused on the requirement in order to provide specific relevant answers. Of particular importance is the attention to the time-frame and the stage in the audit cycle and to the type of assignment being examined.

A number of common issues arose in candidates' answers that contributed to the disappointing pass rate:

- Writing too little for the marks available
- Failing to develop points beyond simple identification of facts given in the question. Answers often lacked the detailed evaluation and assessment of the issues identified that is required at this level.
- Lack of knowledge of certain fundamental syllabus areas such as audit reports.
- Lack of basic accounting knowledge – for example not understanding how transactions are recorded and whether accounting errors would lead to the overstatement or understatement of balances and transactions.

Specific Comment

Section A

Question One

This question followed the pattern of previous examinations and was set at the planning stage of the audit/assurance cycle and covered risks, audit procedures and other information required.

Candidates were required to provide an analysis of audit risks for a manufacturer of bespoke and generic machines. Performance on this requirement was good with the majority of candidates correctly describing audit risks rather than business risks. This is an area that most candidates are well prepared on, however stronger answers were able to develop and apply the relevant accounting treatment. Those able to identify specific areas of the financial statements which would be affected and to correctly identify whether the risk was over or understatement tended to score the strongest marks. A significant minority of candidates thought that the client was new to the firm as opposed to simply having a change in manager and spent time addressing opening balances and new client procedures which were not relevant to the question. Candidates are again reminded to read the question carefully and consider the context of the scenario both in terms of client history and timeframe before answering the question.

Candidates were further required to provide additional information needed to effectively plan the audit and candidates showed a marked improvement over previous sittings where this requirement has been examined. This type of question requires candidates to identify information that would be available in advance of the audit that would assist in the planning of the audit. Such information would generally help in the identification or evaluation of risks rather than the information available at the year-end for performing audit procedures. This is particularly relevant as the question was set almost a month prior to the year-end so financial statements and year-end balances would not yet be available.

Candidates were further required to provide audit procedures for the valuation of work in progress (WIP) and a government grant. With respect to the former, candidates often cited the need for an expert to value WIP rather than focusing on the components of cost and NRV in the machines. Similarly, there were a number of candidates who requested written representations from management on WIP despite the figure not being an issue where the knowledge was confined to management or one of management's intentions. Candidates are once again reminded that a written representation is not a suitable substitute for sufficient appropriate evidence. The audit procedures relevant to the grant were generally well described.

There were four professional marks available, and most candidates secured most of these marks by providing an introduction and using headings to create an appropriate structure for their answer. However, presentation was not always good and candidates are reminded to pay attention to determining an appropriate layout for their answer.

Question Two

Question two was a two-part question and presented information relating to two different clients. Initially candidates were required to identify indicators in the scenario which gave rise to going concern issues and then to state procedures to audit the going concern status of the company. In general, this was well attempted and candidates scored high marks, however those using a columnar approach tended to lack depth in their explanation of the factors identified in the question and overlooked some of the more encompassing audit procedures that did not arise from a specific scenario point.

The second part of the question differed between the International (INT) and Singapore (SGP) exams and the UK and Ireland (IRL) adapted exams. The INT and SGP exam focussed on the audit of performance information, a relatively new topic in the relevant syllabus, and required candidates to discuss the relevance and measurability of key performance indicators (KPIs) in respect of a University and to describe how they might be audited. Well prepared candidates were able to discuss the issues surrounding measuring and determining relevant performance information and were able to draw on the information included in the recent examiners article on this topic to the scenario. Some candidates did not focus on the question requirement and attempted to describe the theory of public sector KPIs. Many candidates were unprepared and left this requirement out altogether.

In the UK and IRL exam this requirement was set around alternatives to insolvency for a company in financial distress. Answers to this requirement were mixed. Many candidates provided good answers, showing that they understood this syllabus area and could apply their knowledge to the scenario. Weaker answers were too vague, and some clearly did know this syllabus area well enough to provide any reasonable advice.

Section B

Question Three

Question 3 was the least attempted question in the optional section. This followed a familiar format of addressing the matters arising and evidence expected to be found on three financial reporting issues. Candidates were faced with a sale of assets and redundancies relating to a move of distribution centres, a share purchase

and segmental reporting.

The issue surrounding the sale of assets was the best answered of the issues in this question, however candidates are reminded that dates and timelines in questions are of crucial importance in determining which events are adjusting and non-adjusting.

The second issue focused on an equity investment and candidates could score well either with a strong knowledge of accounting for financial instruments or could question the substance of the relationship in order to discuss accounting treatment for associates. In general answers to this section were very short and did not cover enough points to score well on the financial reporting aspects but marks for the audit procedures were generally good. Candidates are again reminded to use the mark allocation as a guide for the level of depth of analysis that is required to score the available marks.

The final part of this question looked at the concept of segmental reporting. Overall only the best candidates displayed an in depth knowledge of this area. Candidates preparing for this examination should bear in mind that a strong knowledge of financial reporting is crucial to the ability to audit financial statements and the ability to audit the appropriateness of disclosures made in the financial statements is a very topical issue.

Question Four

Question 4 was the most popular of the optional questions and was answered by a significant number of candidates. Performance on this question was generally strong and most candidates were able to identify and discuss the relevant issues. The question focussed on ethics and practice management, and candidates were required to critique the appropriateness of advertising being utilised by the firm. The majority of students were well prepared to answer this question with a format that has been used before, and were able to confidently identify and evaluate the ethical issues associated with the proposed advertisement

The second part of this question combined overdue fees with an intimidation threat and again was well answered. The final part dealt with a conflict of interest between two competing clients arising after an acquisition of another firm and candidates attempting this question tended to score well.

Question Five

This question examined audit reporting and corporate governance. Candidates were asked to analyse four issues set out in the scenario arising at a listed client and to discuss the appropriateness of including those issues in the report to those charged with governance. In addition candidates were also asked to consider whether the items would have an impact on the audit report.

Disappointingly a large number of candidates suggested including immaterial issues or those not affecting the annual report in a modified audit report. In particular, there was an overuse of the Emphasis of Matter modification. In addition, some candidates were unable to differentiate the impact of something on the business from the impact in the financial statements.

The second part of this question asked for role and benefits of an audit committee and this requirement was generally well answered with most students able to demonstrate sound knowledge of the role of the audit committee in the governance of a company.

Conclusion

As stated in the conclusion to the previous examiner's report, almost all candidates are able to identify at least some relevant issues to a particular requirement from the scenario, but not all can adequately explain, discuss or describe their points in sufficient depth or detail. Candidates must ensure that they answer the specific requirement which has been set, and focus their answer points on the scenario.

Candidates are also reminded that while it is important to have good knowledge of financial reporting, they must be able to link this to the appropriate audit issues that arise in the question scenarios. Candidates are encouraged, as always, to practise past exam questions and to carefully review the model answers and the examiner's reports that accompany the past exam questions. This is important to gauge the style of question requirement that regularly appears in this paper, and to gain an appreciation of what it means to explain an answer point rather than just identify an answer point