

# Examiner's report

## P7 Advanced Audit and Assurance

### December 2017



#### General Comments

The examination consisted of two sections. Section A contained one question for 35 marks and one of 25 marks, both of which were compulsory. Section B contained three questions of 20 marks each, from which candidates had to answer two questions.

This examination requires a sound understanding of the syllabus and builds on the assumed knowledge from both F8 Audit and Assurance and P2 Corporate Reporting, reflective of what would be expected of an auditor in practice. Candidates must ensure that their knowledge is up-to-date and in line with the current versions of both auditing and financial reporting standards which are included as examinable documents. Although less frequent than last session, there are still candidates using outdated terminology from previous standards on revenue recognition and auditor's reports. This knowledge should then be developed into exam technique using question practice along with relevant technical articles published on the ACCA website and past examiner's reports. These will help candidates interpret requirements better and keep their answers relevant and mark focused.

This examination did not appear to be particularly time pressured with most candidates completing all the requirements. Overall candidates appeared to have correctly interpreted the majority of requirements although there was some evidence of candidates treating a given area as a repeat of a previous exam question and giving rote learnt answers on that topic rather than answering the requirement as set. This is particularly noticeable on group audit risks and other assurance assignments.

Candidates will benefit in terms of examination technique from practising for themselves the skills of time management, identifying the requirement and providing a concise answer before exam day – simply seeing someone else work through a question or reviewing the answers to past questions will not provide a good grounding for exam day.

From a technique perspective, candidates who started the examination with one of the optional questions rather than the compulsory questions tended to write disproportionately long answers for the number of marks available in their first response. In particular this strategy appears to attract the stating of rote learnt theory not required for the question. It is recommended that candidates take note of the marks available and tailor their responses appropriately.

However, overall there appeared to be fewer scripts containing unnecessary theoretical explanations than in the previous session which was pleasing.

#### Specific Comments

##### Question One

This question was set at the planning stage of an audit. The client was a clothing and jewellery group selling via different outlets and had acquired a new subsidiary during the year which was audited by another firm.

Candidates were asked to describe audit risks arising from the briefing notes provided by the audit

engagement partner. This area was generally well answered as the majority of candidates were able to pick out the key issues from the scenario and describe their impact on the financial statements. In general, candidates focused more on risks of material misstatement than on the detection risks but covered enough areas to attain good marks. However, control risks identified were often poorly described. Far fewer candidates quoted the audit risk model than in previous sessions and most of the technical areas such as consignment inventory and deferred consideration for the acquisition were well addressed.

As has happened in previous examinations the examiner flagged that there was a brand which was correctly not recognised in the statement of financial position because it was internally generated. A significant portion of candidates described this as their first audit risk, wasting time on an area that was clearly flagged as not a risk. Such candidates would do well to refresh on their knowledge of intangible reporting rules. The other area of weakness in financial reporting knowledge was regarding the fair values of assets and liabilities at the acquisition date. Almost universally candidates stated that recognising the value of research and development costs and a customer list as assets acquired with the purchase in the group accounts was incorrect and understated expenses.

Some candidates continue to speculate about potential risks rather than focusing on the information given and therefore unfortunately end up providing irrelevant answers. Such candidates speculated that foreign exchange issues could potentially arise if the group happened to be trading in foreign currencies despite there being no mention of this or that the client may not know how to deal with consolidating its existing subsidiaries despite the fact that they had been in the group for some time.

Candidates were also asked to provide audit procedures relating to consignment inventory held by third parties and this requirement was generally well answered with candidates explaining the procedures appropriately. Some candidates however did not read the specifics of the requirement and discussed procedures for inventory held by the client or in some cases brand valuations. Attention to the detail of the requirement is important for producing answers capable of attaining marks. Many candidates continue to provide procedures which do not detail a source and a purpose and therefore are not detailed enough to score full marks.

The final requirements asked for general considerations when relying on a component auditor and for candidates to appraise extracts of the component auditor's strategy. There were well addressed where the requirement was correctly interpreted however some candidates interpreted the first part as procedures or risks arising from an acquisition. Another error seen several times was candidates missing that this was an extract rather than the full strategy so focusing on what other elements should be included in a strategy document rather than weaknesses in the areas given.

## **Question Two**

This question focused on quality control and was comprised of two parts. Firstly candidates were asked for the benefits of monitoring quality control and actions to take if deficiencies were found and this was answered well by the majority of candidates. Common errors here were to either list out quality controls which should be in place or to discuss client systems and controls rather than those of the audit firm. These were misinterpretations of the requirement and candidates would benefit from taking the time to fully understand what is being asked before answering the question

A short answer with the right content will be worth more than a long answer which doesn't address the requirement.

Candidates were then presented with the outcomes of quality control reviews on a range of clients and subjects. Candidates who interpreted the requirement correctly and explained why those items raised were quality control deficiencies scored good marks. A common misunderstanding was to simply discuss the implication of those defects on the audit rather than explaining why they were breaches of quality control.

### **Question Three**

This question was set in a public sector environment and was broken down into two parts. One part examined procedures for assurance on a number of performance measures identified by the entity in the scenario and was generally interpreted correctly. Candidates found this a tricky requirement as the documents available would not be standard audit documents, however most candidates who opted for this question made a good attempt at describing where they might find the information. A minority of candidates did not address the requirement and instead discussed why the performance measures given had been chosen or where risks arise in auditing this type of information. This again suggests that a number of candidates failed to read the requirement carefully or were not confident addressing it, reverting to a preplanned answer for a given topic.

The other section was a matters and evidence question similar to that in Question two of the June 2015 examination. The requirement was set at the review/completion stage of an audit and candidates needed to discuss the contentious or risky items arising from the audit performed and explain what evidence should be on file to help determine if the issue is appropriately resolved. For matters, the sort of points a candidate is expected to raise here are the materiality of the issue, the accounting treatment that would apply and the risks within the information provided on that area. For instance a risk that a potential liability has not been provided in full or that an item might be recognised in the wrong period or with the wrong classification. Candidates would then be expected to describe the impact on the financial statements.

Candidates sitting this examination should have a good grasp of the principles of double entry and be capable of describing the direction of a risk. For example if a provision has been omitted from the financial statements candidates would score a mark for saying "expenses are understated and liabilities understated if the provision is omitted"

Candidates who do not describe the correct direction of the risk eg "liabilities will be under/over stated" or those who do not understand the impact of the double entry correctly (so assume every double entry has one under and one over statement) eg "liabilities will be understated and expenses overstated" do not attain credit.

Audit evidence was generally described well here but candidates too often rely on board approval and written representations for items which are simple to audit and not judgmental and as such are not appropriate.

Candidates were not asked to consider audit reporting implications in this question as the scenario is set at review stage not the reporting stage of the audit and again a number of candidates wasted time providing information which was not required.

#### **Question Four**

This question was an ethics and professional issues question based around three different scenarios similar to Question 4 from the Sample March/June 2016 Questions. Candidates can find detailed discussion on how to address such requirements in the recent ethics technique article on the ACCA website section for this examination. The description and identification of threats was generally well done with the majority of answers being focused and concise. The quality of answers was generally of a better standard than in previous sessions. The first two scenarios were well covered concerning self-review and acceptance procedures however candidates often missed either the conflict of interest or the listed status of the company in the third scenario.

#### **Question Five**

This was a reporting question and again was in two sections. Candidates who had read the examiner's article prior to the examination and who have a good understanding of materiality should have found this question straightforward.

Candidates were asked for a discussion on the three types of misstatement described in ISA 450 Evaluation of Misstatements Identified During the Audit. Candidates were expected to define the types of misstatement (factual, judgemental and projected) and could get full marks by describing how to address each of those with management or through further audit work.

The second part of the scenario had an example of each type of misstatement and required application of the knowledge demonstrated in the first part of the question, requiring candidates to cover what should be discussed with management and the effect on the audit opinion. This was well answered by well-prepared candidates however a significant portion of candidates failed to calculate materiality correctly and concluded an immaterial depreciation error was material. There was also a lack of appreciation that related party transactions are material by nature.

Candidates should note that the requirement specifically asked for the effect on the audit opinion not the full auditor's report so there was no credit available for describing the basis of opinion or Key Audit Matters. There are still a number of candidates who show a lack of understanding of misstatements and propose emphasis of matter paragraphs as an alternative to qualifying the report for factual misstatements or to explain immaterial/trivial items.

#### **Conclusion**

There was an improvement in performance in this session, particularly in relation to audit risk and ethics. However, it is clear that many candidates continue to not prepare properly for the exam and failed to learn the topics in sufficient depth. A large number have a narrow focus on the topic that they are studying and are not keeping up to date with changes to accounting standards, such as revenue recognition and auditing standards in relation to auditor reporting and in some instances are providing rote learned answers with little or no application to the specifics of the question.

Once again, candidates are urged to re-learn the basics of auditing – independence, ethics, robust third party evidence, audit risks and understanding the proper use of audit opinions – and are encouraged to use past questions to help them study and revise for the exam.