



# Examiner's report

## Audit and Assurance (AA)

### June 2019

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.

#### **General comments**

The Audit and Assurance exam is offered in computer-based (CBE) format. The model of delivery for the CBE exam 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 case questions – here we look at the key challenge 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 were two sections to the examination and all the questions were compulsory. Section A consisted of three OT cases, each comprising five OT questions for a total of 30 marks, which covered a broad range of syllabus topics. In Section B candidates were presented with one constructed response question worth 30 marks and two constructed response questions worth 20 marks each; testing the candidates' understanding and application of audit and assurance in more depth.

In order 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 practicing questions are unlikely to be successful as the constructed response questions in particular aim to test candidates' application skills.

#### **Section A**

It was very pleasing to see that once again almost all candidates attempted all 15 questions, across the three OT cases. Candidates preparing for future sessions are advised to work through the past exams which are available and to carefully review how each of the correct answers were derived. Section A questions aim to provide a broad coverage of the syllabus, and future candidates should aim to revise all areas of the Audit and Assurance syllabus, rather than attempting to question spot. Section A in the June 2019 examination included, but was not limited to, questions on the following areas:

- Corporate governance
- Substantive procedures including analytical procedures, revenue, expenses, bank and cash and share capital
- Written representations
- Going concern
- Subsequent events

- Auditor's reports

### Sample questions for discussion

The following questions are reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific questions selected. Candidates are reminded that there will be a mix of application and knowledge questions in Section A and it is imperative that they ensure their knowledge of the International Standards on Auditing (ISAs), relevant financial accounting and important areas of the syllabus such as auditor's reports is at an appropriate level. Recent Examiner's reports have noted that performance on knowledge questions was poor and this continued to be the case in June 2019. Questions may test specific details of examinable documents including ISAs, ACCA's Code of Ethics and Conduct and the Corporate Governance Code, therefore candidates must ensure that they have studied these in sufficient depth.

### Example 1

X Co is a listed company and has an audit committee.

**Which of the following responsibilities should be included within the terms of reference for the audit committee?**

- (1) Reviewing and monitoring the external auditor's independence and objectivity
- (2) Appointing and removing the external auditors
- (3) Evaluating and monitoring the effectiveness of the internal audit function

- A. 1, 2 and 3
- B. 1 and 2 only
- C. 1 and 3 only
- D. 2 and 3 only

The correct answer is C.

This question tests knowledge of corporate governance responsibilities and in particular those of the audit committee and demonstrates the level of detailed knowledge which is required. It also demonstrates the level of care which must be taken when reading the question and thinking through the options. The audit committee makes recommendations in relation to the appointment and removal of the external auditors but it is the shareholders who are responsible for their appointment and removal. Candidates who rush through this type of question or who word spot without considering the whole of the context of the question are likely to answer incorrectly.

### Example 2

A & Co is the auditor of Z Co for the year ended 31 December 20X8. The detailed audit work is due to be completed by 30 June 20X9. The directors are planning to approve the financial statements on 31 July 20X9 and then issue them to the shareholders on 15 August 20X9. The management of Z Co has performed an assessment of the company's ability to continue as a going concern based on a cash flow forecast prepared to 31 December 20X9.

**To which date must A & Co's assessment cover when evaluating management's assessment of Z Co's ability to continue as a going concern?**

- A.** 30 June 20X9
- B.** 31 July 20X9
- C.** 15 August 20X9
- D.** 31 December 20X9

The correct answer is D.

As with the previous question, this question requires detailed knowledge, in this case of ISA 570 Going Concern. However, it also demonstrates the need to be able to apply knowledge to a practical scenario. In accordance with ISA 570, the auditor is required to review the same period as that used by management to determine whether the going concern basis is appropriate. This must be at least 12 months from the end of the reporting period. The management of Z Co has used a cash flow forecast for 12 months to December 20X9. As this is at least 12 months from the end of the reporting period, this is date to which A & Co's assessment must cover.

## **Section B**

The constructed response questions in Section B tested candidates understanding of the Audit and Assurance syllabus:

- Audit framework and regulation
- Planning and risk assessment
- Internal control
- Audit evidence
- Review and reporting

### **Audit framework and regulation**

This area of the syllabus requires; an understanding of the functions of an audit, and an understanding of both corporate governance and professional ethics.

Questions in this area may present candidates with a scenario-based ethics or corporate governance question. Candidates are generally asked to identify and explain a set number of issues from a given scenario and give relevant recommendations to address the issues identified. In this session candidates attempting ethics questions were able to identify the fact from the scenario, such as there being a family relationship. However, in order to gain the ½ mark for identifying the ethical threat the correct type of threat must also be stated. In this case there was a self-interest threat. In order to gain the other ½ mark available for the explanation of the threat, candidates needed to explain the implication of the ethical threat. Many candidates gave vague answers such as 'this reduces independence or objectivity'. This did not gain any credit. An appropriate explanation for the family relationship identified above, would have included the following: 'due to the family relationship the firm may be reluctant to give a modified opinion'. In addition, when making recommendations for ethics and corporate governance questions, candidates are reminded that the recommendation must be an action; often candidates provide objectives rather than actions. 'Hurling Co' from the 'Sample March/June 2017 Questions' is a

good scenario based question to practice the skill of explaining ethical issues and making relevant recommendations. 'Freesia Co' from the 'Sample March/June 2019 Questions' is a good scenario based question to attempt on corporate governance.

In addition questions in this area can include stand-alone knowledge based questions, covering areas such as confidentiality or assurance, that do not need to be applied to the scenario provided. In answering knowledge questions it is important to ensure that an adequate level of detail is provided, as often these questions are answered too briefly, almost in a note format. It is also important to identify the requirement verb, as 'describe' or 'state' require completely different levels of detail to be provided.

### Planning and risk assessment

This area of the syllabus requires an understanding of how the auditor obtains and accepts audit engagements, obtains an understanding of the entity and its environment, assesses the risk of material misstatement and plans an audit of the financial statements.

Questions on assessing audit risks tend to be scenario based; the candidates having to identify and explain the risks from a scenario and give an auditor's response to address the risks. Other questions in this area of the syllabus tend to be more knowledge-based questions and hence depend on the ability of students to recall their knowledge in the exam.

As noted in previous Examiner's reports a fundamental factor in planning and assessing the risks of an audit of an entity is an assessment of audit risk, and this remains a highly examinable area. Audit risk questions typically require a number of audit risks to be identified ( $\frac{1}{2}$  mark each), explained ( $\frac{1}{2}$  mark each) and an auditor's response to each risk (1 mark each). Typically candidates can be required to identify and explain in the region of six to eight risks and responses.

The scenarios usually contain more issues than are required to be discussed. It is pleasing that candidates planned their time carefully and generally only attempted to list the required number of issues. A point to note however is that there may be risk factors at the beginning of the scenario in the opening paragraph and also in the closing paragraph. Candidates are often missing these. In this session the opening paragraph of a risk question stated that this was a new audit client, many candidates failed to identify the increased detection risk for the current year.

As stressed in previous exam sessions, yet again a significant number of candidates did not explain how each issue could impact on the audit risk and therefore were not awarded the second  $\frac{1}{2}$  mark. To explain audit risk candidates **MUST** state the specific area of the financial statements impacted with an assertion (e.g. cut off, valuation etc.), or, a reference to under/over/misstated, or, a reference to inherent, control or detection risk. 'Misstated' was only awarded if it was clear that the balance could be either over or understated. A significant minority of candidates stated the risk was 'under/over stated' when it was clearly one or the other. They were not awarded credit and this scattergun approach is not recommended. Additionally, candidates must state the specific area of the financial statements impacted, as opposed to a general statement. As an example, a significant loss on disposal is indicative of an inappropriate depreciation policy resulting in 'property, plant and equipment being overstated or depreciation being understated'. No credit would be awarded just for stating 'assets are overstated' or 'profit is overstated'.

An auditor's response does not have to be a detailed audit procedure, rather an approach the audit team will take to address the identified risk. In common with previous sessions, auditor responses were sometimes too weak e.g. 'discuss with management' or 'obtain a breakdown and confirm it is reasonable'. In addition, it was noted that some candidates focussed on what management should do rather than the auditor, and/or, gave responses that were inappropriate to the scenario. For example, in this session a company had encountered significant fraud in its warehouse, some candidates recommended that 'the company install CCTV cameras'. This is an inappropriate auditor response and so would have gained no marks as it addresses the issue from the perspective of the company and not the audit. 'Peony Co' from the 'Sample March/June 2019 Questions' is a good scenario based question on audit risks and responses to practice.

Audit risks and response questions can also be linked with a knowledge question. Good examples of this are 'Cupid & Co' from the 'Sample September/December 2017 Questions' and 'Blackberry Co' from the 'Sample March/June 2018 Questions'.

It has been noticeable in recent sessions that candidates have not performed well in these knowledge questions and these should be straightforward marks to obtain. In this session it was disappointing that many candidates did not know the auditor's responsibilities under law and regulations and also the differences between the audit strategy and audit plan. Future candidates are reminded that they MUST revise all areas of the syllabus and spend adequate time learning knowledge areas in preparation for the exam.

Audit risk questions may be combined with a requirement to calculate ratios, these ratios then linking in to the risk and responses requirement. Alternatively as was the case in this session questions may contain pre-calculated ratios which are to be used in the risk and responses requirement. In both cases candidates are encouraged to make the connection between the results of the ratios and the other information in the scenario when identifying and explaining risks. 'Darjeeling Co' from the 'Sample September/December 2018 Questions' is a good question to practice the skill of calculating ratios and applying these to a risk and response question.

Candidates tend to score well in calculating ratios, however a few points to note are as follows:

- Do not calculate more than the required number of ratios as this wastes time
- Do not provide the formula for ratios, as no credit is available.

### **Internal control**

This area of the syllabus requires both an ability to describe and evaluate internal controls techniques and audit tests, and also an ability to make appropriate recommendations as well as being able to distinguish between the scope of internal and external audit.

Internal control questions typically require internal control deficiencies to be identified ( $\frac{1}{2}$  mark each), explained ( $\frac{1}{2}$  mark each), a relevant recommendation to address the control deficiency (1 mark), and, often a test of control the external auditor would perform to assess whether each of these controls, if implemented, is operating correctly (1 mark). Internal control questions can also include the identification ( $\frac{1}{2}$  mark each) and explanation ( $\frac{1}{2}$  mark each) of key controls as well as

tests of controls (1 mark) to assess whether the key controls are operating effectively. Further, answers may be required to be presented in the form of a report to management, in which case a covering letter (2 marks) is required.

Internal control questions often include a knowledge requirement. In common with planning and risk questions, these are relatively straightforward marks and candidates should be attempting to score maximum marks. In this session some questions focused on knowledge of control objectives, and it was disappointing to see once again that many candidates failed to score many marks. It is imperative that future candidates ensure that they devote adequate time to learning the knowledge areas of the syllabus as well as practicing this style of question. Good example questions to practice are 'Comet Publishing Co' from the 'Sample September/December 2017 Questions', 'Raspberry Co' from the 'Sample March/June 2018 Questions' and 'Freesia Co' from the 'Sample March/June 2019 Questions.'

Internal control questions remain a highly examinable area and performance in June 2019 was mixed. The scenarios included in exam questions contain more issues than are required to be discussed. It was pleasing in this session that candidates were generally able to identify (for ½ mark each) the required number of issues from the scenarios. However some candidates were unable to correctly identify the deficiency from the scenario. They were able to pick the relevant fact from the scenario but failed to spot what the actual deficiency was. For example, from the scenario candidates identified 'invoices have a unique number' but the actual issue was that the unique numbers were not sequential. Additionally, this session there was an increase in the number of answers with irrelevant deficiencies being given. This seems to stem from a lack of understanding of the scenario and possibly due to a lack of question practice.

In common with previous sittings many candidates did not clearly explain the implication of the deficiencies. It is important that the explanation fully details the impact to the company. As an example, for a deficiency of 'purchase invoices are not sequentially numbered' a suitable, well-explained implication would be 'this could result in the recording of purchases and payables being incomplete and suppliers being paid late'. Many candidates did not go on to explain the impact on the company in sufficient detail, for example just stating, 'this could result in invoices being missed'.

Most candidates were able to provide good recommendations to address the deficiencies they identified. However, some of the recommendations were either poorly described, did not clearly address the specific control deficiency identified or were impractical suggestions. Many candidates just repeated the converse of the deficiency and to obtain the one mark for the recommendation more detail is needed. For example, for the deficiency 'a lack of segregation of duties around inventory management' some candidates stated a recommendation of 'segregation should be introduced'. However, to obtain the full mark this recommendation needed to cover what elements of the role should be separated. Additionally, as with ethics and corporate governance questions, recommendations must be actions rather than just objectives.

'Equestrian Co' from the 'Sample March/June 2017 Questions,' 'Camomile Co' from the 'Sample September/December 2018 Questions' and 'Freesia Co' from the 'Sample March/June 2019 Questions' are good internal control deficiencies and recommendations questions to practice.

## Audit Evidence

This area of the syllabus requires a description of the work and evidence obtained by the auditor required to meet the objectives of audit engagements and the application of International Standards on Auditing.

A key requirement of this part of the syllabus is an ability to describe relevant audit procedures for a particular class of transactions or event. Overall performance in this key syllabus area in this exam session was once again disappointing.

The June 2019 exam session contained a number of questions in this syllabus section covering a variety of areas across both the statement of profit or loss and statement of financial position, illustrating that candidates must be prepared to tailor their knowledge of substantive testing to any area of the financial statements. In most cases candidates remain unable to tailor their knowledge of general substantive procedures to the specific issues in the question requirements, with many providing tests of controls rather than substantive procedures, or providing incorrect procedures, or concentrating on one type of test e.g. multiple examples of analytical review procedures. In particular, care must be taken to address the specifics of the question; often the requirement is to describe substantive procedures to address specific financial statement assertions, such as valuation, and any tests provided which do not test this assertion would not score any marks. For example, in this session a question asked for “substantive procedures in relation to the valuation of a company’s inventory”. Procedures focused on attendance at the inventory count were therefore not awarded credit. It was also particularly disappointing this session that relatively straightforward audit procedures, such as in the audit of receivables, were not well answered.

A good example to practice is ‘Dashing Co’ from the ‘Sample September/December 2017 Questions’ and ‘Hyacinth Co’ from the ‘Sample March/June 2019 Questions’.

In addition candidates should read the AA Technical Article ‘The Audit of Financial Statement Assertions’.

As addressed in previous Examiner’s reports candidates must strive to understand substantive procedures. Learning a generic list of tests will not translate to exam success – procedures must be tailored to the specific requirements of the question. Additionally tests must be sufficiently detailed noting clearly which source document should be used. As in previous sessions, a significant number of candidates suggested tests such as ‘review disclosures’ however this only scored ½ marks as they did not go on to detail what those disclosures were being reviewed for. Also recommending ‘obtain a written representation’ without explaining what for, e.g. to ensure completeness/reasonableness of a provision, will not generate any marks.

Other good examples of substantive procedures questions to practice are ‘Gooseberry Co’ from the ‘Sample March/June 2018 Questions’ and ‘Jasmine Co’ from the ‘Sample September/December 2018 Questions’.

There are many resources available on ACCA’s website which will help you prepare and reviewing these, along with past exam questions, is one of the best ways to help you cover the syllabus and get used to the style of the questions.

## Review and reporting

This area of the syllabus requires an understanding of how consideration of subsequent events and the going concern principle can inform the conclusions from audit work and are reflected in different types of auditor's report, written representations and the final review and report.

Questions in this area of the syllabus tend to be scenario based and may require candidates to describe required amendments to the financial statements and/or audit procedures in relation to going concern or subsequent events. Alternatively they can require an assessment of the impact on the auditor's report due to an unresolved accounting issue.

Performance in auditor's report questions this session was mixed. Candidates are often required to discuss an accounting issue, assess whether the error is material, consider the type of modification, if any, and lastly to discuss the impact on the auditor's report. Answers must clearly state the opinion to be issued (i.e. unmodified opinion or modified opinion), and if the opinion is to be modified, the type of modified opinion which is appropriate (i.e. qualified opinion, adverse opinion, disclaimer of opinion). Candidates are advised to ensure that they are as knowledgeable on modifications caused by insufficient evidence as they are for material misstatements.

This session there was an improvement in that some candidates provided a discussion of the issue, which scored up to 1 mark. In order to be awarded marks for discussing the issue candidates should not just re-write the issue from the question. Candidates need to explain the effect of the item being incorrectly recorded, for example, if this results in assets/liabilities/profit being over/understated.

While it is pleasing that candidates performed well calculating materiality for auditor's report questions, candidates should note that it is not necessary to show the workings of how materiality is calculated, as there is only ½ mark available for this calculation.

Unless stated otherwise in the question requirement, candidates should only include the type of modification required if the company does not adjust for the issue in the financial statements. Weaker candidates continue to discuss what the report will look like if the error is adjusted for and if it is not. This is not an efficient use of time and only responses which answer the question will generate marks.

In this session there was also a question focusing on key audit matters (KAM). Performance on this was very disappointing. In particular a number of candidates demonstrated a lack of understanding of the appropriate use of an emphasis of matter paragraph, suggesting that this should be used to communicate KAM. Other candidates just focused on materiality and modified auditor's reports. Candidates are reminded that they must revise all elements of the syllabus in relation to auditor's reports and not just assume that the questions will focus on modification of the auditor's opinion.

Auditor's reports are a core area of the syllabus and knowledge of the ISAs in this area is imperative. Good questions to practice are 'Airsoft Co' from the 'Sample March/June 2017



Questions', 'Gooseberry Co' from the 'Sample March/June 2018 Questions' and 'Jasmine Co' from the 'Sample September/December 2018 Questions'.

In addition candidates should read the AA Technical Article 'The Auditor's Report'.

### **Exam technique**

Good exam technique is vital for success in Audit and Assurance. It was pleasing to see that many candidates made effective use of the pre-formatted response areas provided which encourages answers to audit risk and internal control questions to be structured in columns. Not only does this make it easier to mark, it makes it easier for a candidate to review their answer and ensure they have covered all of the relevant areas, for example it is clearer to see if a control recommendation has been omitted. A minority of candidates are reproducing the questions in their answer, this is not necessary as it is not marked and it wastes time.

Additionally, it was pleasing that where a question asked for a specific number of issues to be addressed, such as risk and internal control questions, most candidates attempted to identify the required number demonstrating appropriate exam technique and time management.

Once again it was disappointing to see that some question requirements were not attempted. This tended to be in knowledge areas, substantive testing questions and key audit matters. This could have been due to a lack of knowledge or exam preparation.

Candidates need to ensure that their answers relate to the scenario given. In questions requiring a description of substantive procedures these were often too generic. Candidates need to ensure that substantive procedures and tests of control in particular are clearly described as to exactly 'how' the procedure should be performed. Also an adequate number of procedures must be provided; a five-mark question should have at least five well described procedures to maximise the candidate's mark.

### **Word processing technique**

It was pleasing to see that the depth of many answers has continued to significantly expand on previous sessions. However please note that when answering into a pre-formatted table, providing bullet points is acceptable, however answers must be sufficiently detailed and not 'note like' in order to maximise marks.

Very occasionally, the typed words in some candidates' answers were difficult to understand as the words were misspelt. Candidates are reminded that there is no automatic spelling checker tool available and to try and manage their time appropriately to allow for a review of their answers before submission. Also when reviewing answers look out for omission of key words, for example the omission of the word 'not' can completely change an answer.

There are resources on ACCA's website giving more guidance on how to use the word processing tools. A video introducing the main functionality and how to make best use of these in Audit and Assurance can be accessed via the website.

### **Guidance and Learning Support resources to help you succeed in your exam**

Preparing for the Audit and Assurance exam can appear challenging but there are many resources available to help you. You should refer to these throughout your studies.

You should make sure you have made use of all of the resources found [under technical articles for AA](#) – these include technical articles, study support videos and exam technique resources – all developed with you in mind.

Additionally [Examiner's reports](#) are available after each exam session. These are a valuable tool for understanding the exam, avoiding common pitfalls and developing exam technique. Work through the Audit and Assurance resource 'Examiner approach' and also 'A guide to using the examiner's report' if you are sitting the exam for the first time or 'A guide to reflection' if you are retaking your exam. Both of these interactive tools can be found under the [technical articles page](#) for Audit and Assurance. These have been developed to sit alongside the self-study guide and the [retake guide](#) respectively, and provide you with further pointers for using the Examiner's reports for previous sittings.

It is essential to practise as many exam standard questions as you can in the lead up to your exam, this is critical for Audit and Assurance as 70% of the marks are written. We strongly recommend that you use an up to date question and answer bank from one of our [Approved Content Providers](#) but if this is not possible then work through the most [recent past exams](#) on our website. However, please note if you are using the past exams that these are not updated for syllabus changes or changes to the exam format since September 2016 and so should be used with caution – so check the [latest syllabus and study guide for changes](#).