Chartered Accountant SINGAPORE

SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER'S REPORT

MODULE: Assurance (ASF)

EXAMINATION DATE: 13 June 2019

Section 1
General comments

It is encouraging to see an improvement in Candidates' quality of answers. There was a general improvement across the scripts and this was reflected in the increase in overall pass rate. There were less scripts with incomplete answers, reflecting better time management. There were also more Candidates who passed with distinctions. However, the number of passes with merit reduced.

Section 2
Analysis of individual questions

Question 1

Part (a) of this question required Candidates to compare engagement letter and representation letter in terms of four characteristics:
- Preparer and addressee
- Date
- Purpose
- Frequency

Candidates generally did well in differentiating the preparer/addressee of engagement letter and representation letter. However, a small number of Candidates showed a lack of knowledge of the purpose and frequency of the letters. For example, there were answers stating that representation letters were required whenever necessary during the audit and thus could be dated at any time during the audit. According to *SSA 580 – Written Representations, Paragraph 14*, the date of the written representations shall be as near as practicable to, but not after, the date of the auditor's report on the financial statements.

Some Candidates misunderstood that the engagement letter had to be issued every period for the same audit client. According to *SSA 210 - Agreeing the Terms of Audit Engagements, para A23,* it is in the interests of both the entity and the auditor that the auditor sends an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the audit. With reference to *SSA 210, para A29*, the auditor may decide not to send a new audit engagement letter or other written agreement each period. The paragraph also listed situations when it may be appropriate to revise the terms of the audit engagement or to remind the entity of existing terms.

For **part (b)**, a list of business risks was provided. Candidates were required to describe the risk of material misstatements (RMM) associated with the business risk. This question is based on the principle in *SSA 315 (Revised) - Identifying and*

Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment. It was stated in *para A39*, "An understanding of the business risks facing the entity increases the likelihood of identifying risks of material misstatement, since most business risks will eventually have financial consequences and, therefore, an effect on the financial statements." *Para A41* provides examples of RMM that are associated with business risks: "A business risk may have an immediate consequence for the risk of material misstatement for classes of transactions, account balances, and disclosures at the assertion level or the financial statement level. For example, the business risk arising from a contracting customer base may increase the risk of material misstatement associated with the valuation of receivables."

Some Candidates showed a lack of understanding of the difference between business risk and RMM. For example, a business risk given in the case was "Management believes that the company needs to secure a loan of significant amount from the bank to finance its working capital." A few Candidates brought up points on the inability to repay loan amounts and the impact on the company's cash flow and reputation. The answers described the negative business consequences (business risk) instead of the RMM required in the question.

Part (c) required Candidates to compare interim audit and final audit in terms of their timings. Most Candidates correctly stated that the interim audit was performed prior to the entity's financial year end whilst the final audit was performed after the entity's financial year end. However, there were some who did not know the timings.

The final part of **part (c)** required Candidates to discuss whether interim audit was mandatory and the circumstances when an interim audit was useful. Most Candidates were able to provide relevant factors such as volume or complexity of transactions to be audited. Some Candidates showed a lack of understanding of the interim audit (in relation to the RMM and the frequency of interim audits) and thus the answers did not receive any mark.

Part (d) provided a list of different audit procedures and required Candidates to state when each audit procedure was typically performed, i.e. during interim audit or during final audit. The answers to this question were satisfactory except for the performance of final analytical procedures (audit procedure (vi)). Analytical procedures may be performed in three different stages of audit:

- During the planning stage, as risk assessment procedures [see *SSA 315 – Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment, para A14*], commonly known as preliminary analytical procedures.

- During the testing stage, as substantive procedures [*see SSA 520 – Analytical Procedures, para A4*]

- During the final review stage, as required by *SSA 520 – Analytical Procedures, para 3b* - To design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.

The analytical procedures provided in the question part were used to assess whether the financial statements were consistent with the auditor's understanding of the company. Thus, the procedure would be done in the final audit stage, nearing the completion of the audit. Many Candidates did not get this correct.

Question 2

For **Part (a)**, five business processes were provided. Candidates were required to identify internal control procedures from the business processes and describe the test of controls to verify their effectiveness. Candidates' performance was satisfactory except for the business process relating to the accounts payable staff performing checks on the sequentially numbered goods received notes (GRN) (business process 4). Many Candidates were able to identify that the sequentially numbered GRN is an internal control. Sequentially numbered documents on their own would not be internal control. It is the sequence check performed by the accounting staff that is the control that ensures completeness of documents.

Part (b) required Candidates to discuss the follow up and conclusion after the performance of the test of controls (TOC). **Part (b)(i)** required Candidates to conclude if any deviations were detected from the TOC. Candidates' performance for this is satisfactory. **Part (b)(ii)** required Candidates to describe the further procedures to be perform on the control deviations that were detected from the TOC performed. Many Candidates did not provide the correct answer. *SSA 530 – Audit Sampling, para 12* requires the auditor to investigate the nature and cause of any deviations identified. *Para 13* states that "In the extremely rare circumstances when the auditor consider a misstatement or deviation discovered in a sample to be an anomaly, the auditor shall obtain a high degree of certainty that such misstatement or deviation is not representative of the population. The auditor shall obtain this degree of certainty by performing additional audit procedures to obtain sufficient appropriate audit evidence that the deviation does not affect the remainder of the population." Thus, the further procedures to be performed is to investigate the cause of the control deviation to confirm whether the deviations are anomalies or not.

Part (c) was based on the principles found in *SSA 265 – Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*. The question required Candidates to describe the factors to consider when deciding whether the control deficiencies should be communicated:

- Those charged with governance and management; or
- Management

SSA 265, para 9 and 10a require auditors to communicate in writing, significant deficiencies in internal control identified during the audit to those charged with governance and management on a timely basis.

SSA 265, para 10b require auditors to communicate other deficiencies (i.e. not significant) in internal control to management.

The performance for this question part is mixed. This indicated that Candidates lack knowledge of *SSA 265*.

Part (d) required Candidates to explain THREE key areas that should be included in a management letter on control deficiencies. The performance for this question was satisfactory.

Question 3

Part (a) provided four different methods of selecting trade receivables for further audit procedures. Candidates were required to explain whether a sampling approach was used for each of the selection methods and explain the reason for selection.

According to *SSA 530 – Audit Sampling*, sampling is the application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population. From the above definition, there are two salient features of sampling:

- All sampling units have a chance of selection;
- Sampling provide a basis to draw conclusions about the entire population.

Most Candidates used the first feature and correctly determined whether the stated selection method used a sampling approach. However, the explanation for some selection methods were not adequate. For example, one selection method was to select all major customers (method 2). Most Candidates correctly pointed out that this was not a sampling method without offering adequate explanation on why the receivables of major customers were selected. They were selected because the balances were expected to be material. In cases where the recorded outstanding balances of major customers were not significant, there could be a risk that they were understated.

Part (b) required Candidates to describe FIVE types of details in relation to the outstanding loans that an auditor would normally request in their bank confirmations. Most Candidates answered this well although there were some who indicated answers such as “the name of the loan” and “description of the loan”.

Part (c) required Candidates to explain TWO errors that could be detected from the performance of monthly bank reconciliation. The performance for this question part was satisfactory.

Part (d) required Candidates to describe the TWO reconciling items, unpresented cheques and uncleared deposits, in a bank reconciliation. Most Candidates provided satisfactory answers. However, there were some Candidates who provided the same answers for both **Part (c)** and **(d)**. These Candidates did not know the difference between errors and timing differences giving rise to reconciling items.

Question 4

Part (a) required Candidates to explain ONE significant ethical threat if the auditor also provided tax services (tax computation and filing) to its audit client. **Part (b)** is related to **part (a)** and required Candidates to explain TWO safeguards that the audit firm could implement to mitigate the threat (assuming that the entity was not a listed company).

Most Candidates answered these questions satisfactorily except a few Candidates who discussed whether the self-review threat was significant. Additionally, some Candidates identified the wrong ethical threats such as advocacy threat or familiarity threat.

Part (c) required Candidates to explain THREE reasons that could result in a downward revision of the materiality. Candidates' performance was satisfactory. However, there were answers that were too general or showed lack of understanding of setting materiality. For example:

- "Materiality revision may occur if there are new information that comes to light."
- "A decrease in materiality could mean a stricter approach on the accounts as the testing of details at a higher materiality was not sufficient to draw a sufficient opinion of the financial statements."

Part (d) involved an issue encountered during audit, i.e. unrecorded supplier invoices. Candidates were required to explain whether the issue was a misstatement or a limitation. The issue was a misstatement as the auditor was able to obtain evidence to confirm that there were unrecorded invoices. Surprisingly, some Candidates concluded that this was a limitation.

Part (e) provided the materiality of $100,000 and required Candidates to evaluate the issue of unrecorded supplier invoices against the materiality to determine whether the issue was material, pervasive and the impact on auditor's opinion. Some Candidates had the wrong concept that the issue was pervasive because the amount exceeded materiality. Otherwise, Candidates' answers were satisfactory.

Part (f) provided a development of the unrecorded supplier invoices issue in **part (d)** and **(e)**. The case stated that the finance manager agreed to record the unrecorded supplier invoices after year end. Candidates were required to discuss whether the finance manager's proposed action was appropriate. Many Candidates correctly stated that it was still a misstatement. Very few Candidates were able to explain that the proposed action would result in a cut-off error.

