SINGAPORE CA QUALIFICATION EXAMINER'S REPORT

MODULE: Assurance (AS)

EXAMINATION DATE: 20 June 2018

Section 1
General comments

There has been an observable improvement in the quality of answers, which resulted in an increase in pass rate. There was also a considerable variance in the quality of answers across Candidates. Candidates generally did not perform well for Question 2 and 3.

Candidates should be focused and relevant in their answers of the theoretical components in the paper. Merely extracting from the standards and other sources will receive little or no marks.

Section 2
Analysis of individual questions

Question 1

The main focus of question 1 is reliance on internal auditor's work.

Part (a)(i) requires Candidates to state four factors that could affect the extent of reliance on internal auditor's work. This part was generally well answered. **Part (a)(ii)** is an extension of **part (a)(i)** requiring Candidates to apply the four factors to the case. Candidates' performance varied as stronger candidates were able to use the information in the case to justify the reliance on internal audit while some Candidates did not attempt to answer this question part at all. As part **(a)(i)** and **(a)(ii)** are related, the learning point for the Candidates is that the factors written for **part (a)(i)** should be factors that can be applied in **part (a)(ii).**

Part (b) tested the Candidates' ability to identify specific areas from the case where reliance on internal audit can be placed. This question is generally well answered as most Candidates referred to the internal control documentation, the internal audit work done for the year-end inventory count and review of the data transfer testing. However, half of the Candidates did not refer to the review of the internal audit report produced by the internal audit team, as well as the internal audit test results which can be used to identify effectiveness and completeness of internal controls.

Part (c) focuses on ethical issues arising from audit staff having a personal relationship with the audit client's personnel. This question sets out to test Candidates' ability to evaluate whether the ethical threats are significant and apply safeguards that are appropriate in relation to the severity of the threat.

Most candidates did well for **part (c)(i)** as they could identify the familiarity threat. Only a handful of Candidates failed to mention the lack of objectivity due to the

familiarity threat and missed out on the full marks for this part. For **part (c)(ii)**, most Candidates correctly pointed out the fact that both the auditor and the accountant held junior positions. Many Candidates suggested a complete removal of the junior audit staff as the easiest way to avoid any independence issue for **part (c)(iii)**. Only a quarter of the Candidates correctly suggested assigning the auditor to another area not handled by the related accountant.

Question 2

This question focuses on the audit procedures and objectives relating a number of assets.

Part (a) required the Candidates to explain the audit objectives of verifying the owners and directors of the two companies, where a significant amount of prepayment was made by the audit client to the potential acquisition target. While prepayment is a common business practice, a huge prepayment is less, and auditor should be alert to such prepayment made to related parties. Most candidates were able to state the objectives of identifying possible related parties and related party transactions required in **part (a)**.

Part (b) is to explain the objectives of possible acquisition. Understanding the management's reasons for investment helps auditor to confirm whether the classification of investment is appropriate, such as investment in subsidiary, associate or financial investment. Professional scepticism should be raised if management was not forthcoming with their explanation. Candidates' performance varied as some Candidates did not attempt to provide an answer.

Part (c) requires Candidates to explain the audit procedures to be performed to verify the various assets in the case. The answers provided by the Candidates were satisfactory. However, some audit procedures provided by the Candidates were impractical, such as inspecting bank statement to confirm the payment was received by the payee. As the identity of payees made by cheques do not appear in bank statement, such answers were not given any credit.

Part (d)(i) required Candidates to state the audit procedures to verify the cost of components that can be capitalised in self-constructed assets. The performance of Candidates varied as some Candidates wrongly thought that the components were intangible assets and they had completely missed the point.

In **part (d)(ii),** Candidates needed to state the audit procedures to verify staff cost capitalised in self-constructed assets. Candidates' performance was satisfactory. However, weaker candidates failed to mention verifying of the source documents or supporting documents that provides evidence on these costs.

Part (d)(iii) required Candidates to explain the potential misstatement in the self-constructed assets. Candidates did poorly for this part as the majority of the Candidates failed to notice the non-capitalisation of borrowing cost was a potential misstatement.

Question 3

This case involves the restructuring of a large listed company. The restructuring activities included:

- discontinuing helpdesk service for customers,
- early termination of office lease,
- termination of staff,
- disposal of property, plant and equipment, and
- restructuring of an existing loan.

Part (a) focuses on audit procedures to be performed on the above restructuring activities.

Part (a)(i) required Candidates to obtain evidence to confirm affected employees have been notified (timing) and the compensation cost (measurement). Most candidates did well for this question. In **part (a)(ii),** the audit procedures relating to the termination payment would confirm the occurrence of the event and the accurate measurement. Thus, the notification letter on the termination of the lease and the offer letter from the landlord on the compensation for the lease termination are the main audit evidence to obtain. Candidates' performance varied widely. Whilst most Candidates correctly stated the proposal to obtain written agreement on the lease termination arrangement, some Candidates' answers are too general to be awarded full credit, e.g. review management worksheet.

For **part (a)(iii)**, few candidates spotted the key word in the requirement, i.e. "planned" disposal of property, plant and equipment (PPE). This was further explained in the case that the associated PPE were not disposed as at year-end. Thus, the audit procedures should be focused on gathering evidence to support whether the PPE should be reclassified as held for sale. Furthermore, the audit procedures should aim at acquiring evidence that support the recognition criteria in SFRS (I) 5 *Non-Current Assets Held for Sale and Discontinued Operations*, such as, whether there will likely be future sales or whether the assets have been written down to fair value less cost of disposal, etc. However, answers given were related to the actual disposal of PPE. Answers such as ensuring the disposed PPE are removed or updated in the fixed asset register did not earn any marks.

Part (a)(iv) focused on audit evidence that prove whether the help desk service ceased before year end or after year end. The timing of cessation affects when the operations can be considered as discontinued operations. This question is not well answered.

Part (a)(v) focused on evidence that supports if the loan has been restructured. Most Candidates did well by indicating the review of bank correspondence and the revised agreement as the evidence to confirm the existence and details of the restructured loan.

Part (b) continued from part (a) which focused on the accounting treatment of the restructuring activities. Candidates are required to provide the reasons and purpose of the audit procedures provided in part (a). Audit evidence is needed to evaluate whether financial statements are prepared in accordance with SFRS. For example, do the financial statements complies with the recognition rules, measurement rules and disclosure requirements. Generally, the Candidates did not answer **part (b)** as well as for **part (a)**. Candidates have displayed understanding on the audit procedures but less understanding on the linkages between the audit procedures and purposes.

Majority of the Candidates correctly stated the timing and criteria relating to recognition of provision for redundancy in SFRS (I) 1-37 *Provision, Contingent Liabilities and Contingent Assets* for **part (b)(i)**. Very few Candidates correctly identified the termination of the lease as an onerous contract as required in SFRS (I) 1-37 *Provision, Contingent Liabilities and Contingent Assets*.

Some Candidates wrongly applied SFRS (I) 1-17 *Leases*, misinterpreting the termination of lease would result in a new lease and the risk of non- compliance with FRS 116. Such answers were not awarded any mark.

For **part (b)(iii)**, Candidates did not realise that the risk is whether the assets are correctly classified as for held for sale and thus the performance for this question is generally poor.

Very few candidates demonstrated the knowledge in SFRS (I) 15 *Revenue from Contracts with Customers* in **part (b)(iv)** whereby discontinued operations in the helpdesk can only be considered as discontinued operations upon cessation of the operations. Therefore, the answer did not attract high marks.

Only a handful of candidates correctly cited SFRS (I) 1-1 *Presentation of Financial Statements* for **part (v)** to support the risk of classifying current loan as short term loan. Candidates' answers in **part (v)** indicated the correct procedures to perform but lack the appropriate reasons for the audit procedures.

Question 4

The case is about a chain of convenience stores experiencing inventory shortages and control issues. A public accounting firm has been approach to help investigate the issues.

Part (a) tested the Candidates' ability to use the information provided in the case to help a single store from the chain of convenience stores in the investigation. Candidates demonstrated business acumen by selecting the store with the highest shortages or with the highest shortages in relation to the revenue or total inventories in the store. Random selection of stores for investigation is not appropriate here.

Part (b) required Candidates to recommend five internal controls to address the issues. Generally, Candidates were able to recommend control procedures targeted at the issues on hand and use the information in the case well.

Part (c) required Candidates to state the assurance level provided by the internal control report to be submitted to the management. The quality of answers to this question is unsatisfactory. Many Candidates failed to recognise that this is not an assurance engagement and thus no opinion is sought by the client. There is no assurance provided by the report. Some Candidates incorrectly concluded that this is an agreed-upon-procedures when no procedures were agreed with the management prior to the engagement.

Part (d) on the ethical issues related to the proposed fee arrangement is well answered with many Candidates correctly identified the self-interest threat arising from the contingent fee arrangement. However, some Candidates suggested the wrong safeguards in reducing the threat. This threat has to be avoided.

Part (e) focused on the opening balances relating to an initial audit engagement, which included implications on the audit report if the issues cannot be resolved. This part was poorly answered with many Candidates copying the auditing standards without explaining the application to the context. Extracting from the audit standard do not contribute to the answers and do not earn any credit for the Candidates. This is because this question is about the application of the principles in the auditing standards and not what the standards say. Only a handful of the Candidates were able to use information from the case, such as the company's financial statements were never audited, as a significant risk affecting opening balances.