

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN	
EXAMINERS' COMMENTS	
SUBJECT Audit, Assurance and Related Services	SESSION Certified Finance and Accounting Professional (CFAP) Examination - Winter 2017

General:

The overall performance in this attempt was much below expectation as the passing percentage was only 11.2% as compared to 16% in the previous attempt. The disappointing factor was that the overall performance remained poor in all the questions. The major reason for the poor performance was lack of knowledge, failure to give due attention to the requirement of the question and answering in light of the given scenario and poor writing skills.

Question-wise comments:

Question 1

This question required identification of audit risks in a given scenario and the key audit steps to be performed to address the identified risks. Though it was a standard question which is tested in almost the same manner in every examination, the performance remained poor as only 15% of the candidates secured passing marks. The only consolation was that a further 40% of the students scored 7 to 9 marks.

Major errors were as follows:

- Majority of the candidates could not identify more than three or four risks. Mostly, the risk related to installments receivable, write down of inventory, impairment of plant and proper segregation of revenue between revenue from sale of cars and services revenue could not be identified.
- Issue of going concern and deferred tax were identified as the risks which was inappropriate as the company was still earning substantial profits.
- In respect of audit procedures, the requirement was to specify key audit procedures whereas a number of students identified the simpler procedures such as casting, agreeing with ledger, etc.
- Audit steps aimed at obtaining evidence to support completeness assertion were mostly missed. For example, most of the students specified steps to verify the list of litigation and claims but did not specify steps which could ensure that all litigations and claims are recorded on the list.

Question 2

This question consisted of two parts. The overall performance was below average as only 25% of the candidates secured passing marks. However, like in question 1, a further 30% of the students scored more than 40% marks. Performance in each part is discussed below:

Part (a)

According to the scenario given in this question, an audit team member had discovered a draft report issued by a valuer appointed by the company. In the draft report, the value assigned to the buildings was lower than the amount which was mentioned in the final report. It was also noted by the auditor that in case of valuation as per draft report, certain loan covenants may have been breached. The requirement was to specify the steps to be taken in the given situation and the possible impact on the audit report.

The overall performance was satisfactory. However, very few students scored full or high marks. The major issues observed were as follows:

- The issue of overall materiality was ignored in most of the cases. Despite the fact that materiality limit mentioned in the question was Rs. 80 million and the amount in doubt was only Rs. 20 million, which was much below the materiality level, most of the candidates stated that the matter is material and pervasive and discussed the possibility of giving an adverse opinion. In such cases, the auditor considers the impact of all material misstatements in aggregate, in order to decide the impact on audit report. This aspect was rarely mentioned.
- Breach of loan covenant usually entitles the bank to demand an immediate repayment and therefore the loan is converted into a short-term liability. Moreover, other terms of loan may also change requiring revision in certain disclosures. In such situation, in case of disagreement with the management, auditor has to qualify the report despite the amount not crossing the materiality threshold, because, such disclosure is qualitatively material. This aspect was seldom discussed.
- While discussing the issue of management integrity, only two alternatives were mostly discussed i.e. disclaiming an opinion and withdrawal. These are relevant but extreme steps. An important step which the auditor takes in such situations i.e. where there is a doubt but no conclusive evidence is to reassess the risk of material misstatement due to fraud and its impact on nature, timing and extent of audit procedures. This aspect was not covered by many candidates.

Part (b)

The performance in this part was quite poor. Only about 50% of the students were able to explain correctly that matter discussed in the scenario was qualitatively material and should be disclosed. However, very few could specify the impact on audit report if the client refuses to make the disclosure (For details, refer ICAP's suggested answer). Moreover, the fact that if the disclosure is given, the matter may form part of the Key Audit Matter section of the audit report was rarely mentioned.

Question 3

The overall performance in this question was very poor as only 6% candidates secured passing marks, though a further 30% of the candidates scored more than 40% marks. The requirement was to specify key audit procedures related to two issues as discussed below:

- (i) This contained a short scenario whereby a subsidiary had been acquired during the relevant accounting year. According to the given information, three issues should have been addressed i.e. measurement of goodwill, impairment of goodwill and inter-company transactions. The major reason for poor performance was that majority of the students ignored either one or both of the last two issues. Other common mistakes were as follows:
- Verification of discount rate used to discount the purchase consideration received after one year of the acquisition and the methods / assumptions used to determine the fair value of the assets and liabilities were mostly ignored.
 - Many students only mentioned that impairment of goodwill should be tested. No further steps were specified in this regard.
 - While discussing steps related to inter-company transactions, reversal of profit on intercompany stocks was mostly missed.
- (ii) This part was based on a very simple scenario whereby a company had changed its accounting policy for property, plant and equipment from historical cost to revaluation model. The overall performance was average as most of the students mentioned about inquiring the reasons for change and whether it was free from bias and ensuring proper disclosure. However, only few students mentioned about modifying the opinion paragraph to mention about the change and whether the auditor concurs with it or not. Moreover, while discussing the accounting treatment and the disclosure requirements, it was mentioned that being a change in accounting policy, the effect would be taken retrospectively which was incorrect as change in accounting policy from historical cost to revaluation method does not require restatement of financial statements.

Further, the question explicitly stated that routine verification steps of property plant and equipment were not required but many students kept wasting their time on these steps.

Question 4

According to the scenario in this question, the auditor had been asked to report on compliance with internally developed safety standards related to disposal of waste chemicals and the report was to be issued to the customers of the company. The key issue was that the government had also issued its own safety standards which were more comprehensive and stringent.

The performance remained below average as only 19% candidates secured passing marks. Moreover, about 40% of the candidates were totally unaware of the related auditing standard and scored less than 25% marks.

Some of the better students who scored passing or near passing marks made two types of errors which resulted in loss of marks, as discussed below:

- They failed to offer any comments regarding the use of internally developed standards in the presence of more comprehensive standards issued by the government.
- It was mentioned that the auditor should assess that the standards to be applied are suitable but failed to specify how the auditor would ensure them.

Question 5

This question was based on Key Audit Matters (KAM) section of the audit report. According to the question, the auditors had identified three matters for inclusion in the KAM section. The requirement was to draft the relevant KAM section. The overall performance was below average as only 20% candidates could secure passing marks. The major errors were as follows:

- About 50% of the candidates were totally unaware of how to handle this question and obtained four or less marks. Answers of most such students were restricted to specifying the audit verification steps.
- While discussing the reasons for inclusion of a particular matter in the KAM section, many candidates only discussed materiality of the matter. Other reasons such as high level of judgment involved and existence of risks, etc. were not mentioned.
- Many key steps which the auditor performs were not listed. Especially, in the case of related party transactions, only the audit procedures related to verification of transactions listed by the client were mentioned, whereas procedures for ensuring completeness of the disclosure were not stated.

Question 6

This question contained two independent scenarios and the candidates were required to identify the threats involved and the possible course of action to be adopted in each case. Though this should have been an easy question as this part of the syllabus is regularly tested, yet the performance was even worse as only 18% of the candidates secured passing marks. Comments on each scenario are given below:

- (i) According to this scenario, a client which was in a weak financial position had failed to pay the audit fee for review of half yearly accounts and the management had also requested the audit firm to give some relief as regards audit fee of current year.

The performance remained below average mainly because the students could not give appropriate comments on some of the main issues as discussed below:

- With regard to non-payment of audit fee, the candidates generally could not specify an important step that the auditor should bring the matter to the knowledge of the audit committee and/or those charged with governance. Moreover, it was also important to assess the significance of the threat which was also missed by the majority. Furthermore, many candidates mentioned about declining the engagement whereas according to the scenario it had already been accepted.

- With regard to reduction in fee, many students did not make any comment on the management's contention that work would reduce as a result of closure of plants. On the other hand, many students were completely in agreement with the management's view in this regard. They did not consider the other aspect of the situation i.e. closure of factories is also an indication of weakening financial position because of which the auditor may have to face more challenges such as risk of intentional misstatement and more issues involving professional judgment, such as impairment of assets and going concern and therefore it was not necessary that closure of plants may result in reduction in work.
- A large number of students were of the incorrect view that audit fee cannot be reduced under any circumstances.

Question 7

This question was based on a simple scenario according to which a not-for-profit organisation required a report of factual findings about its projects, in order to receive certain grant from the federal government. However, since the trustees want to distribute the report to other donors also, they have requested the auditor to not to include any condition in the report regarding its non-distribution to parties.

The performance in this question was poor and only 12% of the candidates secured passing marks. Almost 11% of the candidates had no idea whatsoever and preferred not to attempt the question altogether. A further 27% of the candidates scored zero marks as they believed that the request of the trustees cannot be accepted.

(THE END)