



ACA Tutor Conference 2019

AUDIT AND ASSURANCE



Introductions

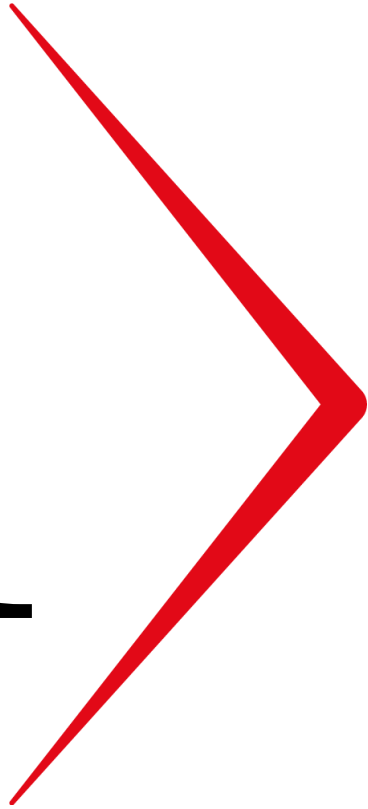


Agenda

1. Candidate performance in 2018
2. December 2018 script review
3. 2019 Syllabus and learning materials update
4. CBE
5. Questions?

Candidate performance in 2018

1



Pass rates

Average mark by question type

Average score by syllabus area

Non-attempts

Qualitative evaluation of performance

Pass rates

	2018 %	2017 %	2016 %	2015 %
March	78.8	87.1	80.9	87.1
June	83.9	81.6	82.7	82.0
September	87.2	86.1	90.5	87.5
December	78.2	70.2	81.6	74.9

December had the poorest performance for the 3rd time out of the last four sessions

- Some evidence of timing issues
- Highest incidence of non-attempts of question parts (see later slide)

September continues to exhibit strong performance

Average mark and % by question type

Question type	December 2018	September 2018	June 2018	March 2018
SFQ	12.3 61.4%	13.1 65.6%	13.4 66.9%	11.2 56.0%
LFQ	49.6 62%	54.9 68.6%	51.7 64.6%	51.3 64.1%
Total	61.8	68.3	65.3	62.5

- Students performed better in the LFQs in three out of the four sittings
- March SFQ performance was disappointing
- Lower LFQ performance in December relative to other sittings (same as 2017)
- September candidates excelled in the LFQs

Average % score by syllabus area

		December	September	June	March
1. Legal, Professional & Ethical	2018	61.9%	74.4%	64.5%	60.8%
	2017	62.7%	71.4%	63.3%	67.3%
2. Accepting & Managing Engagements	2018	62.0%	65.4%	61.6%	54.6%
	2017	54.6%	51.5%	47.3%	67.5%
3. Planning Engagements	2018	64.0%	72.4%	66.7%	63.6%
	2017	60.2%	66.1%	67.1%	58.9%
4. Concluding and Reporting	2018	63.9%	60.3%	68.5%	67.7%
	2017	62.2%	74.8%	72.4%	75.6%

Area 1: Generally the strong performance in this syllabus area has continued

Area 2: Improvements in most sessions with exception of M18

Area 3: General improvement in answers to planning questions across the sittings despite some trickier areas (Intangibles M18, WIP/warranties J18, Complex revenue S18, rebates D18)

Area 4: Noticeable decline in quality of answers to reporting questions in most sessions – historically the strongest syllabus area

Non-attempts

Session	Question	Marks available	% non-attempts	Syllabus area
March	1.5	3	3.9% (35)	3: Procedures re cyber-attack
	1.6	3	4.6% (41)	3: Analytical procedures re payroll
	2.4	3	5.9% (53)	3: Group audits
	4.3	2	5.3% (47)	4: Audit reports
June	2.4	1	7.2% (144)	1: Monitoring of external auditor by AC
	3.3	3	13.7% (275)	2: Money laundering regulations
Sept (best pass rate)	1.3	3	2.1% (34)	3: Data analytics routines (inventory)
Dec (worst pass rate)	1.1	2	4.9% (72)	3: Analytical procedures
	1.4	4	3.9% (57)	4: Audit reports
	1.5	3	3.9% (57)	2: Ethics partner responsibilities
	1.6	3	7.3% (108)	2: Money laundering suspicions
	3.3	6	3.3% (49)	3: Audit procedures re Going concern
	3.4	6	3.7% (55)	4: Audit reports (GC)
	4.4	3	4.9% (72)	1: Conflicts of interest

Qualitative evaluation of performance

General comments	
Good news	Bad news
	Lack of note form in SFQs
	Failing to tailor answers to scenario provided / generic
	Answering a different question (see eggs)
	Time management
Lower incidence of hidden text in cells, but...	...Still some scripts contain hidden text in cells
	Higher incidence of incorrect calculations (eg % changes on PY or fee thresholds, wrong decimal place)

Example M18, SFQ1.2

Question asked: factors considered by **prospective client** when evaluating your firm's tender and why important

Many candidates answered it from the firm's perspective. Eg: Factor = fees, importance = value for money

But candidates cited whether or not the engagement would be profitable as the reason for importance

Example J18, SFQ1.3

Question asked: actions to **assess credit controller's suspicions** that chief accountant is misappropriating funds

But candidates listed out steps with respect to firm's actions if money laundering is suspected

Qualitative evaluation of performance

Legal, ethical and current issues (20%)	
Good news	Bad news
Identification of relevant threats – especially threats to independence and objectivity	Weaker candidates struggle to explain the threats in the context of the scenario (eg self-review)
Procedures to address conflicts of interest	Less likely to identify other threats: professional behaviour, professional competence and due care, confidentiality
	Differences in ES for listed and non-listed entities
	Sitting on the fence (eg declining engagement)
	Applying information barriers when firm performs other engagements in addition to an external audit
	Factors used by AC to monitor external auditor (J18)
	Failure to recognise Money Laundering (SFQ1.6, D18)

Qualitative evaluation of performance

Accepting and managing engagements (15%)	
Good news	Bad news
Identifying issues related to management integrity / behaviour	Understanding of the different reviews of audit work (eg when an external independent CQ review is required – S18)
Factors to consider when deciding if to submit a tender (S18)...	...explanation of those factors
	Identifying deficiencies in audit work already performed (D18)

Qualitative evaluation of performance

Planning assurance engagements (40%)

Good news

- Justification of risks and relevant audit procedures
- Citing risk of over or understatement
 - Identifying when judgement is required
 - Making use of FS extracts (but we'd like more! Eg higher skills ratios)
 - Dealing with unusual scenarios

Identifying general justifications, such as new client, bank reliance

Bad news

Analytical procedures (M18, S18 – tests based on outcome of AP)

Addressing GC has been mixed (D18 poor, S18 good)

Consideration post year-end audit evidence

Not considering data analytics unless specifically asked for or citing procedures that are not data analytics routines

Group audits (eg communication between group and component auditor) – use the open book!!!!

Dealing with provisions v contingencies

Explaining why audit briefing meeting is required (D18)

Qualitative evaluation of performance

Concluding and reporting (25%)	
Good news	Bad news
Dealing with basic audit report scenarios (material misstatement and limitation on scope)...	... but if there is there are multiple potential outcomes weaker candidates find it more challenging
	... and tend to struggle more with non-audit reports (eg PFI and GHG statements – S18)
	Failing to consider matters to report by exception when there is limitation on scope
	Unable to distinguish between emphasis of matter and other matter paragraphs
Potential impacts on audit reports re GC....	...However, weaker candidates struggle re: <ul style="list-style-type: none"> - Material uncertainty para v EoM - Material v Pervasive
Differences between assurance and external audit	...However, some candidates do not read the question which may be about why the level of assurance differs or how the reports differ (also sometimes ask difference in planned procedures, S18)

Qualitative evaluation of performance

Concluding and reporting (25%) continued....

Good news

Actions following review of audit files (M18)...

Consequences of identified internal control deficiencies and relevant recommendations to address them (exception S18)

Bad news

...although many did not appreciate the context of the scenario.

... weaker candidates recommendations are often the converse of the weakness

December 2018 script review



*Example of marking from
December 2018 session*

2019 Syllabus and Learning Materials update



Assurance syllabus update

Assurance learning materials update

A&A syllabus update

A&A learning materials update

Assurance syllabus update

Changes to existing LOs

1. The concept and need for assurance

- LOg recognise the need to plan and perform assurance engagements with an attitude of professional scepticism **and the exercise of professional judgement;**
 - **clarification of LO – no change to how it is examined**

2. Internal controls

- LOf show how specified internal controls mitigate risk, **including cyber risks**, and state their limitations;
 - **Ch 5 Question bank – Q39 is an example of how it will be examined**

Assurance learning materials update

Chapter 5 Introduction to internal control

Section 2.4.3

New section on risks associated with cyber attacks and controls to mitigate the risks

Chapter 9 Internal audit

Section 1

Additional bullet point re ISA (UK) 610 prohibition of the use of IA to provide direct assistance to EA

Assurance learning materials update

Chapter 15 Integrity, objectivity and independence

Section 1.2 Integrity

New section on integrity

Chapter 16 Confidentiality

Section 3.2 Conflicts of interest

Expansion of existing section with examples

A&A syllabus update

Combination of syllabus areas 1 and 2:

1. Legal and other professional regulations, ethics, accepting and managing engagements and current issues – weighting 35%

Syllabus areas previously numbered 3 & 4 now become areas 2 & 3 respectively – no change to weightings

A&A syllabus update

Changes to existing L.O.s

2. Planning

LOc: recognise the circumstances under which it may be necessary to bring in expertise (including expertise in **cloud computing and** cyber security) from other parties to support assurance processes;

LOd: identify the risks arising from, or affecting, a given set of business processes processes (including risks associated with **cloud computing and** cyber security) and circumstances and assess their implications for the engagement;

LOf: assess significant business risks (including risks associated with **cloud computing and** cyber security) identified for their potential impact upon an organisation, in particular their potential impact on performance measurement;

A&A Learning materials update

- **Study Manual**
 - **Chapter 2 Responsibilities**
 - added new section 5.4 Future of audit
 - **Chapter 7 Planning**
 - added new section 6.5 Cloud computing
 - **Chapters 12 Completion/13 Reporting**
 - the auditor's responsibilities relating to other information moved from Chapter 12 to 13 and expanded for responsibilities relating to strategic report
 - **Chapters 2, 4, 9**
 - deleted some worked examples, interactive and exam style questions

A&A Learning materials update

- **Hard/Electronic Question Banks**
 - Most pre-2014 questions transferred from hard to electronic bank
 - However, non-assurance engagement style questions retained

CBE



Tips for candidates

SFQs

- We like new points on new lines!

9	1. 2	If this matter is likely to result in fines and compensation Nessie may have to recognise a provision at the year end.
10		The firm should ensure there is a provision for the legal case if necessary and ensure adequate disclosure.
11		Infringement of patents, if genuine, could suggest improper integrity of management. This should increase professional scepticism around the financial statements to identify potential misstatements elsewhere.
12		If the company failed to realise that their actions infringed patents it could suggest poor internal control reducing reliance on the controls of the firm meaning more substantive testing is required.
13		The firm may also have to consider further potential law suits and any impact on going concern.

LFQs

- As for 2018 no proforma answer areas will be set up in the CBE package
- Candidates should make use of the word processing tool in the CBE software to avoid the risk of text being “hidden” in cells
- Start each point in a new cell / line rather than including multiple points in a single cell
- Bullet points are still ok in the LFQs – just need to be full sentences

‘Justification of risks and procedures’ question

As in 2018:

- No longer required to answer question in columnar format
 - Can still use columns if they wish
 - However, beware of risk of “hidden text”
- Sub-headings to be used will be stipulated in the requirement
- Please encourage candidates to use their justification of risks to generate ideas for relevant audit procedures

Example layouts



- Writing is dense
- Headings not clearly visible
- Use of bullets is a plus

8	2 2
9	Volume-based supplier rebates
	issue : <ul style="list-style-type: none">- there is an increase in the level of the rebated of the company of 69.23% $((110-65)/65)$ which is not in line with the increase in the revenue of the company of 22.66% $(2885-2352)/2352$) and the increase in the cost of sales of 20.97% $((1194-987)/987)$, this may indicate possible overstatement of the rebates.- the level of the rebated to the purchases if the company increased to 9.2% from 6.56% which are between the 1-10% of the policy of the company but this too close to the limit which may indicate possible overstatement.- when the rebated are included the cost of sale the value of the rebated increased to 8.44% $= ((110000)/(1194+110))$ from 6.18% $B((65)/(987+65))$- the rebates are paid in arrears and therefore there is a risk of misstatement in the recognition of the rebates- the rebates are based on the supplies contracts and the amount included in the financial statements are based on the calculations of the company and the TR system of the company. this may increase the risk of material misstatement due to error in the system and window dressing activities- the old system was replaced in Sep 18 one month before the year end which may indicate possible misstatement in the financial statement due to the fact that the old system may not be reliable and the information may include errors and misstatements.- there is a risk of misstatement in case that the information may not be transferred correctly.- there is a risk of overstatement in the performance of the company since the statement would be used for the loan application i.e. window dressing
10	Procedures: <ul style="list-style-type: none">- discuss with the management the reason for the change in the rebates and the reason why this is not in line with the increase in the sales and the costs of sales.- compare the actual and the budgeted results to ensure that the rebates are not more overstated than expected- review the post year results to ensure that all the transactions and the information related to the year under review are recognised in the accounts- get a representative sample of the transactions and vouch to the supplies contracts to ensure that the calculation of the rebates were correct and accuracy and ensure that the level of the rebates are in line with the level of the purchases and the information in the contracts- vouch to the relevant contracts to the invoices and the cash receipts- reperform the relevant calculations to ensure accuracy- ascertain if there was a parallel running for the change in the system and if there was any, review the result of the parallel running- use test data to ensure that the new system is working effectively and efficiently.- discuss with the management the reason for the change in the old system to find out any problems- review the forecasts and assess the reasonableness of the assumptions and compare this with the post year results and the prior year results to ensure that they are reasonable and consider to carry out a sensitivity analysis- vouch the invoices to the cash receipts and the recognition of the rebated to ensure that they were correctly treated and recognised based on the fact that they were paid in arrears- carry out cut off test- review the post year results to ensure that only the rebated related to the year under review are included.- compare the revenue forecasts with the post year results to ensure consistency and ascertain any big differences, and assess the reasonableness of the assumption based on the change in the inflation and other macroeconomic factors- consider to carry out a sensitivity analysis when considering the reasonableness of the assumptions- from a representative sample compare the invoices to the contracts to assess the level of the rebate

Example layouts



- Spacing is good (ie new cells used)
- Some aspects have dense writing

8	Volume-based supplier rebates
9	<u>Justification</u>
10	Supplier rebates have increased by 69% year on year. Rebates were 3% of revenue in 2017 and 4% of revenue in 2018 and therefore materia for both years. Rebates range from 1-10% of purchases. Having removed rebates from the cost of sales figures for 2017 and 2018, rebates were 7.0% of cost of sales in 2017 and 10.1% of cost of sales in 2018. The latter is above the 10% rebate range. Therefore there is a risk of overstatement.
11	The contracts at at different times in the year. This increases the risk of misstatement of rebates as Dragon may recognised rebates early and therefore in the incorrect accounting period. Rebates are paid in arrears which further adds to the chance they are recognised early.
12	Risk revenue is overstated as the operations manger prepares the forecasts. Revenue increased by 23% year on year suggesting it may be over stated. The revenue is used to estimate the anual volume of purchaes, which then determines in turn, the amount of reabte. Overstatement of revenue would increase rebate payments. Early recognition for rebates when they may not exist would increase the overstatement of rebates.
13	The IT system was replaced so less audit testing has been done on the system icncreasing the risk of errors.
14	<u>Procedures</u>
15	Obtain the signed annual contracts for each of the 100 suppliers and use data analytics to confirm that the contracts state the 1-10% rebate range and that these have been signed by both the client and the supplier. Obtain the list of authorised signatories of the suppliers from management and compare the signature on the contract with the list of authorised signatories. For a sample of clients, obtain independent confirmation, in writing, from the supplier that their company agree with the terms in the contracts.
16	Review the dates in the contracts. Using data analytics, recalculate the rebates figure, per supplier. Confirm the rebates have been accounted for in the correct accounting period and that the overall rebate figure has not been overstated. For rebates that have been paid in this accoutning period but were due to rebates that fell in the previous accounting period (2017), confirm the rebates were not accounted for this year by confirming when the rebates were recognised in the financial statements. Perform cut off testing for any rebate payments that will be made in the next accounting perido but are due to be recognised in this accoutning period, to confirm correct rebate recognition.
17	Obtain communication with suppliers who are paying amounts in arrears and confirm that Dragon had exceeded the volumes of purchases stipulated in the contract. Compare the actual volume of purchases with the maxmium limits in the contracts to confrim Dragon was due a rebate.
18	Use data analytics to recalculate revenue per product and match this against the forecasts the manager prepared for the year. Confirm the figures match. For each rebate recognised in the finaicla statements, match the rebate with the actual volume of purchased goods and compare this with the contract limits for that customer. Confirm that every rebate recognised was owed.

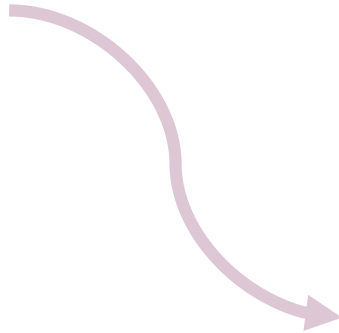
Example layouts



- Well spaced out
- Procedures match justification of risks
- Exercise caution re “hidden text”

26	2.2	Volume-based supplier rebates							
27		Justification						Procedures	
28		- Increased by 69.2% and have gone from 6.6% of cost of sales to 9.2% suggesting overstatement as has changed from last year and is at the top end of the rebate range. The increase is also not inline with the increase of 20.9% in cost of sales.						- Agree sample of rebates paid to the signed contracts to confirm existence of the rebate.	
29									
30									- Discuss with management reason for the increase from the prior year.
31									
32									
33		- Contracts end at different times of the year and are paid in arrears therefore there may be recognition errors if they straddle the year end and are recognised to early resulting in overstatement.						- Agree a sample of signed contracts that have end dates within the year and just after the year end and review the terms and volumes. Agree these to the amounts included in the rebate system and trace through to the financial statements to ensure that only rebates paid this year are included in the financial statements.	
34									
35									
36									
37									
38		- Rebates in the accounts are based on revenue forecasts by operations managers therefore include estimate and judgement. May also be element of bias if the forecasts are linked to salary incentives and bonuses. Also applied for a bank loan therefore forecasts may include management bias to support loan application.						- Discuss with operations manager the basis of the forecasts. Obtain working papers and perform recalculations of the projections. Also compare with prior year forecast with current year actual figures to determine the reasonableness of the assumptions made.	
39									
40									
41									
42									
43		- Rebate system was replaced in September therefore some of the data may not have been transferred properly resulting in misstatements. Also specialised IT system developed in house therefore as its bespoke it is inherently more risky than off the shelf packages.						- Perform a parallel run to ensure that all of the information was properly extracted into the new system.	
44									
45									- Confirm the closing balance of the old system and the opening balance on the new system agree to also confirm all data has been transferred.
46									

Example layouts



- Well spaced out
- New cell for each procedure

6	Volume Based Supplier Rebates:
	Volume based supplier rebates have been identified as a key area of audit risk as they are based on estimates made by management, and estimates are always considered to be high risk as they can lead to over/understatement of expenses.
	This year, cost of sales has increase from 987 to 1194, an increase of 21%, which is in line with the 22.7% increase in revenue, but supplier rebates have increased by 69%.
	Also, in 2017, supplier rebates attributed to $65/987 = 6.6\%$, but in 2018 this has risen to 9.2% ($110/1194$). This suggests that a larger number of supplier rebates have been recorded in 2018 and at the higher end of the rebate range and may be a sign that the rebates have been overstated in order to make the accounts appear healthier.
7	Another issue is that each of the rebates have individual terms associated, so it would be a complex working required to assess the potential rebates from each of the 100 suppliers. The system was designed internally (so there may be questions as to whether the staff had appropriate knowledge and testing completed), and there has been a new version implemented mid-year, which may create the potential for the calculations to not be working as they should be and could be leading to overstating the rebates due.
	Another potential issue is that they are annual contracts which all end at different times of the year. This could lead to cut-off issues and rebates being incorrectly recorded in the wrong period to enhance the appearance of the company. This is also an issue as the company are seeking finance from the bank, so there may be a potential for overstatement of profits and assets to ensure they obtain the financing.
8	Procedures:
9	- Enquire with management as to how the rebates have been calculated and discuss whether there has been a large increase in the rebates agreed/expected with key suppliers.
10	- Obtain a copy of the rebate workings to review the companies included. Reperform the calculations within the workings to ensure accuracy.
11	- Complete a controls walkthrough/testing to review the system used for the rebates to ensure understanding of how it operates.
12	- Review documentation relating to the upgraded system in year. Review results of testing completed and review the competence and expertise of the IT staff.
13	- Agree sample of suppliers included in rebate calculation and agree back to original contract to confirm terms have been recorded in the system correctly. Agree the estimated purchases with purchase invoices and any PO raised.
14	- Agree any post-year end supplier rebate payments received to the calculation to confirm the accuracy of the rebate.
15	- Review forecast method for purchases and review reasonableness of assumptions made.
16	- Review sample of purchases made after the year end and agree to estimated levels to provide assurance over the estimation basis.
17	

Example layouts



- New line for each new point
- Use of bullet points
- Short succinct sentences

6	Question 2.2																		
7																			
		Volume-based supplier rebates																	
		Justification																	
		1) The rebates have increased by 69%, while the revenue only increased by 23%.																	
		2) The volume-based rebates represent 3.8% in 2018 while in 2017 it presented on 2.8% of revenue.																	
		3) Dragon has individual terms with each supplier. And in total they have 100 suppliers.																	
		4) Rebates range from 1% to 10% of purchases.																	
		5) The contracts with suppliers are annual and may not be extended, or the terms can change annually.																	
		6) Rebates are paid in arrears, which may Dragon may recognise early creating a cut off error and thus overstating the rebates.																	
		7) The rebates payments depend on the volume of sales. Dragon may overstate revenue in order to recieve the rebates.																	
		8) Revenue forecasts are used to estimate rebates. Judgemental decisions are involved in estimates.																	
		9) Rebate management system was replaced in September 2018, during which data loss could occur or mistakes made.																	
		10) Sales are made online and the system may not compile correctly with revenue accounts.																	
	8	Audit procedures																	
		1) Inspect a sampe of contracts with suppliers to check the terms of the contracts.																	
		2) Match the revenue figures to the contracts terms and rebates received.																	
		3) Enquire of management about the increase in rebates which was not inline with the increase in revenue.																	
		4) Check post year end rebates recieved and check for cut off error.																	
		5) Test the reasonableness of revenue estimates, obtain explanation from management about the basis used for estimates and recalculate if necessary.																	
		6) Check the revenue for overstatement by matching against the invoices sent to customers.																	
		7) Test the new system's opening balances against the old system closing balances for errors in data transfer.																	
		8) Obtain suffiecent evidence about the opening balances of rebates, revenue by looking at previous auditor's files.																	
		9) Check the online system has bene appropriately synchronised with financial accounts.																	

Questions?



*Is there anything you would like
to ask the examiners?*

