Chartered Accountant SINGAPORE

SINGAPORE CA QUALIFICATION EXAMINER'S REPORT

MODULE: Assurance (AS)

EXAMINATION DATE: 7 June 2022

Section 1
General comments

The overall performance for the June 2022 exam was not satisfactory. Question 4 was the best performing question and Question 3 was the worst performing question. This exam covered the major stages in the auditing of financial statements, i.e., planning, field test (interim and final audit), review and finalisation, and reporting. As in previous exams, professional ethics was also tested.

A summary of the topics tested are as follows:

Planning stage
Candidates were tested on assessing risk of material misstatements in relation to the given accounting transactions. To perform well, Candidates need to know the correct accounting method so as to evaluate whether the audit client's accounting is appropriate. It is advisable for Candidates to revise their accounting knowledge in preparation for the AS exam.

Testing stage
Questions relating to substantive procedures and data analytics tested Candidates' ability to design audit procedures using the facts given in the case scenarios.

Review and finalisation stage
Candidates were tested on subsequent events, specifically on events that occurred after the financial statements were issued. Candidates are advised to be conversant with the guidelines in the Singapore Standards on Auditing (SSAs).

Auditor's report
This topic was tested in every exam, but the performance has not been satisfactory. Candidates should read real audit reports that are available from the Singapore listed companies to familiarise themselves with how misstatements and limitations on scope are handled in the auditor's report, including how the introduction paragraph of the Key Audit Matters section was impacted by these issues.

It is disappointing that Candidates' performance on questions relating to the topic on professional ethics has not improved even though professional ethics was tested in every AS exam. Candidates should be conversant with the guidelines in ISCA's EP 100, specifically paragraph 410 to paragraph 610.

Section 2
Analysis of individual questions

Question 1

Part (a) required Candidates to use data analytics to identify seven unusual transactions for further analysis.

There were some easily identifiable unusual items if Candidates recalculated some of the figures. For example:

(i) Item with negative book value, i.e., accumulated depreciation exceeding cost.

(ii) Items that were fully depreciated, (i.e., cost = accumulated depreciation) but still kept in the fixed asset register implying they could still be in used.

(iii) Newly acquired item (i.e., addition during the year) that was not depreciated. This could be due to the asset not being ready for use or due to error.

(iv) Useful life that could be too long given the nature of the items.

(v) Items whose depreciation did not follow the depreciation policy.

(vi) Prepaid expenses wrongly capitalised.

(vii) Depreciation method did not reflect the consumption pattern of the assets (i.e., the seats in the coaches were depreciated based on the distance travelled and were replaced after 3 years regardless of the distance travelled).

Most Candidates were able to identify the first four unusual transactions, but the explanations on why they want to investigate the items further were weak. For example, the newly acquired Robot Tester was not depreciated as it was not in the condition to be used, e.g., still under testing or it could be due error. Most Candidates did not discuss the possibility that the asset was not ready for use. Candidates who failed to provide reasonable explanations generally failed this question part as more marks were awarded for the supporting explanations than identification.

Many Candidates did not identify the potential error of capitalising prepaid maintenance expense. Instead, they commented that the depreciation charge of the prepaid maintenance was not accurately calculated.

Several Candidates incorrectly pointed out that the depreciation method was based on the distance travelled by the coaches was not allowed by the accounting standard. In fact, this method was a practical example of the unit of production method. This reflects their lack of knowledge of the relevant accounting principles.

For **part (b)**, most of the Candidates were able to score full marks. They were able to design the following two audit procedures to confirm that the coaches were not deployed during the year using the information from the case:

- Review the coach order book; and
- Review the mileage log.

Question 2

Question 2 tested Candidates on the auditor's report and written representations.

Part (a)(i) required Candidates to explain whether it is appropriate for an auditor to issue a disclaimer of opinion on the consolidated financial statements as a whole and also issue an unmodified opinion on certain components of the consolidated financial statements. Many Candidates correctly concluded it was not appropriate to do so. However, most of the Candidates were not able to provide a justification which can be found in SSA 705.15.

Part (a)(ii) required Candidates to consider whether it was appropriate for the auditor to issue a disclaimer of opinion given the issue in the case. Many Candidates were able to present a structured analysis of the issue at hand as follows:

- Disclaimer of opinion is appropriate when the auditor is not able to obtain sufficient appropriate evidence (i.e., limitation on scope) on accounts which are both material and pervasive.

- The issue at hand is that of misstatement rather than a limitation on scope.

- The relevant accounts are material but not pervasive, with justification.

Weaker Candidates were able to justify that the issue was material but were not able to explain why the issue was not pervasive.

For **parts (iii) to (v)**, Candidates were provided with a draft extract of an auditor's report for a listed entity. They were required to identify and explain the deficiencies in the draft audit report. Candidates were instructed specifically not to comment on the sections of the audit report that were not presented in the case, e.g., management responsibilities and auditor's responsibilities. However, there were still Candidates who commented on their omission as deficiencies. No mark was awarded for these answers. Candidates should read the instructions carefully to avoid providing irrelevant answers in the exam.

For **part (iii)**, many Candidates were not familiar with how the Introduction paragraph of the Key Audit Matters (KAM) section should be phrased when the audit opinion was modified. Thus, they presented the Introduction paragraph of the KAM section in an unmodified audit report.

Part (iv) was well addressed by most Candidates, and they were able to draw attention to the insufficient details of the KAM description such as the lack of description of how the KAM was addressed and why the matter was deemed as KAM.

For part (v), most Candidates correctly pointed that Material Going Concern Uncertainty (MUGC) should be specifically addressed as a MUGC section in the audit report and should not be included in the KAM section.

Part (b) required Candidates to evaluate the alternative dates proposed for the written representation letter and audit report given that the Directors planned to authorise the financial statements for issue on 28 June 20X2. The reference date should be 28 June 20X2, the date that the Directors authorised the financial statements. Candidates should have considered the appropriate date of the written representation and the appropriate date of the audit report in reference to 28 June 20X2. Many Candidates correctly compared the date of written representation to the date of audit report but did not consider the audit of audit report to the financial statements' authorisation date. Some Candidates commented that the authorisation date of the financial statements was too early and would create significant time pressure on the auditor. The question did not ask for an evaluation of the authorisation date of the financial statements.

Question 3

The case scenario provided that the auditor was notified by the Management that a fraud was uncovered after the audited financial statements were filed with the Accounting and Corporate Regulatory Authority (ACRA). The audit opinion was unmodified. The Management intended to issue revised financial statements that would take into account the implications of the fraud.

Part (a) required Candidates to consider two implications of the fraud on the financial statements. Only a handful of the Candidates correctly considered the legitimacy of the recorded revenue and deferred revenue. Many Candidates did not consider whether the recorded receivable was subsequently received.

Candidates' performance for **part (b)** was not satisfactory. The question required the Candidates to state the five audit procedures to be performed when Management decided to issue revised financial statements to replace the defective financial statements that were already issued. Many Candidates copied the procedures listed in SSA 560.14 without applying them to the case. For example, the first procedure in the SSA is to discuss with Management and those charged with governance what they intend to do. However, the case already stated that the Directors intend to issue revised financial statements. Furthermore, Candidates did not consider the implications of the lack of integrity of the Chief Executive Officer (CEO) in terms of re-evaluating the evidence obtained, especially the representation from the CEO and the contracts signed by the CEO.

Part (c) was the worst performing question part for the paper. Most Candidates answers focused on the audit procedures to be performed instead of the quality control procedures. This suggested that they either misunderstood the question requirements or they are unfamiliar with the concept of quality control procedures.

Part (d) required Candidates to discuss whether it is permissible under Singapore Companies Act for the Directors of GPL to voluntarily revise the Financial Statements.

There are two main parts to this answer:

1) The Companies Act provision relating to Directors voluntarily revising financial statements. Here, a key condition is that the original financial statements do not comply with the Act, (i.e., not true and fair), including non-compliance with accounting standards.

2) Candidates' application of the above condition to the case in GPL. i.e., whether the GPL situation met the condition required by the Act.

Many Candidates answers focused on the first requirement and only a few Candidates applied it to the case.

Part (e) required Candidates to explain why the auditor should include an "Other Matter" section in the auditor's report on the revised financial statements that GPL will issue. Many Candidates correctly stated that the reason was to highlight the fact that the audit report was on the revised financial statements and draw attention to reasons for GPL to issue revised financial statements. However, there are some Candidates who wrote the general reason for auditor to include the "Other Matter" section without applying to the case.

Question 4

Question 4(a) to (d) tested the concept of audit of leases by a lessee. It is the best performing question for the paper.

In the case facts, the company negotiated a reduction of the annual lease payments for the remaining three years. This reduction in lease payment was not provided for in the original lease agreement and did not qualify for the COVID-19 practical expedient accounting.

Part (a) required Candidates to evaluate whether the Management has accounted for the lease reduction correctly. This is the essence of an audit, i.e., to verify whether the financial statements are prepared in accordance with SFRS(I).

Part (b) required Candidates to describe the audit procedures to obtain evidence that:

(i) Verify the lease reduction; and

(ii) Verify the incremental borrowing rate used

Generally, Candidates performed better in **part (b)** than **part (a)**. There is a concern that Candidates know the audit procedures but do not know what they are auditing.

Many Candidates failed to identify that Management should have used a revised incremental borrowing rate to determine the present value of the remaining lease payment. Some did not know the reduction in lease liability should have a corresponding adjustment to the right-of-use (ROU) asset. Thus, Management recognising the reduction in lease payment as other income is wrong.

For **part (b)**, the quality of answer for **part (b)(i)** was better than **part b(ii)**. This was probably due to the fact that Candidates were not familiar with the concept of “incremental borrowing rate” (IBR). SRFS(I) 16 defines a lessee's incremental borrowing rate as: The rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. Thus, IBR is specific to the nature of the lease asset and specific to the entity. A common audit procedure in the Candidates answers was to compare the IBR used by Management to the interest rates published by the Monetary Authority of Singapore (MAS). The MAS website publishes the interest rates, such as interbank rates, SORA rates. These rates, unfortunately, do not provide sufficient evidence on what the entity’s IBR should be.

Part (c) required Candidates to compute the correct revised lease liability and ROU asset based on the lease reduction and a revised IBR. The answers by some Candidates showed that they were to answer Q4(a), i.e., what is the correct accounting treatment according to SFRS(I) – 16, but they were not able to apply the accounting principle in the actual computation.

Part (d) was the worst performing question part for this question. It required the Candidates to consider a risk of material misstatement to the ROU asset, besides the risk in the misstatement arising from the wrong accounting for lease payment reduction. Most Candidates did not identify the adverse business environment as an impairment indicator and thus Management should have performed an impairment analysis on the ROU asset and recognise an impairment loss if the recoverable amount is lower than the carrying value.

Part (e) was a qualitative question and it tested Candidates on the concept of professional ethics. In this case, the auditor was offered discount in buying goods from the audit client. It is pleasing to see that many Candidates considered whether the discounts were at commercial terms and whether the value of the discount was significant to determine whether self-interest threat was significant. However, there were some Candidates who considered the discount as a gift and thus failed to earn the marks allocated. A handful of Candidates wrongly identified advocacy threat as the main ethical threat in the case. These Candidates believed that when an auditor buys products from their audit clients, they would be promoting the interest of audit clients and thus their objectivity were compromised. The advocacy threat should have a clear linkage with the financial statements. For example, if an auditor helped an audit client to defend the tax position with the authority, then the advocacy threat would be significant.