



Think Ahead

# Foundations in Audit (FAU) December 2022 Examiner's report

The examining team share their observations from the marking process to highlight strengths and weaknesses in candidates' performance, and to offer constructive advice for those sitting the exam in the future.

## Contents

General Comments.....	2
Section A .....	3
Example 1 .....	3
Example 2 .....	4
Example 3 .....	5
Example 4 .....	5
Section B .....	6
Question .....	6
Suggested solution.....	8
Conclusion .....	10



## General Comments

The examination comprised two sections and all questions in each section were compulsory. Section A consisted of 15 multiple choice questions (MCQs) carrying a total of 30 marks. All of these questions carried two marks each. Section B consisted of eight questions with two questions carrying 15 marks, two carrying 10 marks and four carrying five marks each. These knowledge and scenario based questions tested candidates' ability to identify and apply relevant knowledge and auditing techniques.

MCQs allow the testing of candidates' knowledge of a broad range of topics in the syllabus and the questions in Section A achieved this objective. The performance of candidates across the range of questions was mixed with pleasing pass rates on some, disappointing rates on others and a disappointing average pass rate for the MCQ questions overall. Generally, candidates fared better in the Section A questions than in Section B, with all fifteen questions in the section being attempted by all candidates. While, inevitably, candidates will have found some questions to be more challenging than others, all of them are considered to be a fair challenge for reasonably well prepared candidates.

For Section B it was pleasing that some candidates were well prepared for the exam – reflected by a number of outstanding answers submitted to most of the questions. However, given the quantity of weak submissions, as for Section A, it does seem that a sizeable proportion of the candidates were inadequately prepared for the exam. Common weaknesses in answers, displayed in Section B were:-

- Answers which were simply far too brief - giving markers very limited scope to award anything other than a minimal mark due to the brevity of content.
- Limited, overly simplistic explanations and commentary.
- Answer content which bore little relevance to the question.
- Poor structuring of answers and longwinded, muddled points.
- Answers which addressed issues in the syllabus area to which the question related, but which weren't pertinent to the issues raised in the question.

Auditing is a technical subject, and it's generally accepted that auditing students, at any level, need to apply themselves diligently to a carefully programmed course of study and revision, to achieve success in the assessment process. There is no easy route to passing the FAU exam, it is broad ranging and to achieve success candidates need to ensure, at the very least, they have sound knowledge of all the core topics in the syllabus and a basic appreciation of the application of auditing techniques and procedures.

## Section A

As indicated above, the standard of responses was mixed. With the exception of a question about audit risk, average times taken to answer were well within the expected 2.4 minutes for each question – assuming 1.2 minutes per mark for the whole exam. Deeper analysis of this data revealed that the average time taken for the five least well-answered questions was only 1.25 minutes; and for the three least well-answered questions it was only 1.1 minutes. For these questions, candidates were, on average taking around 50 % of the expected time to answer – leading to the obvious concern as to whether they gave themselves sufficient time to consider the answer options and choose correctly.

A commonly held perception amongst some students is that MCQ questions are easier than essay style questions – because “*answers are given to you*”- and that substantial time gains can be made by answering the questions quickly. In reality this is often not the case. MCQ questions are often every bit as challenging as essay style type questions, sometimes more so and time is needed to carefully consider all the options. As with essay style questions the way to improve exam performance is to learn, learn and learn the material; and practice, practice and practice again answering questions to test knowledge and the ability to apply the same to answer questions correctly. Many candidates did not appear to adopt the above approach (or similar) prior to attempting the exam, resulting in disappointing performances. There is no easy remedy to improving on a disappointing performance in either Section of this exam - the above approach has been tried, tested and proven to work and is recommended to future candidates.

Examples of Section A questions and explanations of the answers are as below.

### Example 1

The least well answered question in this section tested candidates’ knowledge about the audit of bank balances. It was phrased as follows:-

**Which of the following items are included in a standard bank confirmation letter for an audit client?**

- (1) Details of authorised signatories on each bank account held by the client.**
- (2) Details of any unusual payments made out of bank accounts held by the client during the accounting period.**
- (3) Details of accounts closed during the accounting period.**

**A 1, 2 and 3**

**B 1 only**

**C 2 and 3 only**

**D 3 only**

Of the three items stated, only that at (3) - details of accounts closed during the accounting period - are included in a standard bank confirmation letter, so D is the

correct answer. Providing confirmation as to the matters at (1) and (2), respectively, is not the purpose of a standard bank confirmation; and careful consideration of the fact that the primary objective of sending the letter is to obtain verification of bank balances (accounts held) at the reporting date, should have enabled candidates to realise that only option 3 could be correct.

## **Example 2**

Another question not well answered was on tests of controls, presented as follows:

**Which of the following statements is TRUE in the context of tests of controls?**

**A The nature of a particular control does NOT influence the type of audit procedures required to obtain evidence about whether the control was operating effectively**

**B Tests of controls should be designed to detect material misstatements at the assertion level**

**C Tests of controls should be performed ONLY on those controls designed with the SOLE objective of preventing a material misstatement in an assertion**

**D Auditors should NOT focus on the monetary values of the transactions when carrying out tests of controls over the processing of transactions**

D is the correct answer. Monetary values are not relevant when an auditor is carrying out tests of controls over the processing of transactions, the auditor should focus on the effectiveness in achieving systems' objectives in the processing cycle. Audit testing, in terms of both tests of controls and substantive procedures, are areas which a lot of candidates for the FAU exam find particularly challenging and this question was no exception. It's only by deep learning of the concept of tests of controls and their of application on an audit engagement - a reasonable expectation given the core nature of the topic – that candidates can have a realistic chance of answering questions like this correctly.

### **Example 3**

A third question not well answered, was presented as follows:

**Which of the following matters is relevant when an auditor assesses the COMPETENCE and CAPABILITIES of a management's expert engaged to assist in preparing a company's financial statements?**

**A Significant assumptions and methods used by the expert**

**B Whether or not the expert is an employee of the company**

**C Books written by the expert**

**D The nature, scope and objectives of the work carried out by the expert for the company**

The option at (A) is relevant in evaluating the adequacy of the expert's work as audit evidence i.e. if the auditor believes the expert's assumptions to be flawed, then the auditor should have doubts about relying on the work. At (B), the point is relevant to the objectivity of the expert, and at (D) the matter is strictly relevant to the auditor needing to obtain an understanding of the expert's work as a basis for evaluating whether it is appropriate for the purpose of the audit. At (C), due consideration of books written by the expert should most certainly be relevant in the assessment of the expert's competence and capabilities, as seen in ISA 620 Using the Work of an Auditor's Expert.

### **Example 4**

The final example of a Section A question which was not well answered was:

**Which of the following statements about International Standards on Auditing (ISAs) is TRUE?**

**A ISAs need only be followed when auditing the financial statements of large international companies.**

**B ISAs override national regulations governing the audit of financial statements in a particular country.**

**C A copy of each ISA is contained in ACCA's Code of Ethics and Conduct.**

**D All ISAs have the same structure and style**

D is the correct answer. All ISAs do have the same structure and style. At A and B, ISAs should be followed on all financial statement audit engagements irrespective of company size, but they don't override national regulations applying to audits. At C, while auditors must comply with the foregoing requirements, as applicable on audit

engagements, and not to do so would be a breach of the implicit requirements of ACCAs Code of Ethics and Conduct, the code does not contain copies of any ISAs.

## **Section B**

This section contained a broad range of knowledge and application based essay and short commentary type questions. As for Section A, it was apparent that a number of candidates did not possess sufficient levels of basic knowledge in core areas of the syllabus.

Typical of candidates' performance across the Section B questions was the range of responses to the requirements of the following 15 mark question.

### **Question**

Cutter Co is a manufacturing company with 220 production employees. The company's accountant heads a large finance department, allowing for adequate segregation of duties throughout. The assistant accountant, cashier and the wages supervisor report to the accountant together with several other supervisors.

The following internal controls are exercised over the company's weekly wages system for production employees:

- The production manager and the human resources manager interview applicants for production roles.
- On their first day of employment, new employees report immediately to the production manager and he completes, authorises and forwards a new employee wages master file update form to the wages department.
- On receipt of the update form, a wages clerk responsible for preparing the weekly payroll uses the information provided on the form to create a new employee record in the wages system's master file. She then downloads a master file update report which provides full details of additions and amendments to employee records entered in the system and confirms the number of live employee records in the system. The update report is then filed with others previously produced.
- The company uses a secure clock card system to record daily hours worked by employees and wages are paid weekly in arrears. At the end of each working week the clock cards are checked and authorised by the production manager or, in his absence, the deputy production manager. During this process, the manager checks to ensure that the hours recorded for all employees are as agreed by him, adds up the authorised daily totals for each employee and then writes the total number of hours to be paid on each card.

- On receiving the clock cards, two wages clerks begin their weekly payroll procedures by simply keying in the total hours worked for each employee into the computerised wages system. The accuracy and completeness of the hours input is facilitated by the existence of a comprehensive range of information processing controls, incorporated in the wages software programme used, alongside similarly comprehensive controls over processing and output.
- In addition to providing gross pay, deductions and net pay data by employee, the weekly payroll shows similar information for each production section and for the production department in total. Downloading two hard copies of the payroll, the wages clerks retain one in the wages department and forwards the other to the production manager for his review and retention.
- After downloading the copies of the weekly payroll, one of the wages clerks runs the system to provide a weekly wages general ledger posting summary and a list of the bank payments to be made to employees to settle net wages liabilities. Each of these is checked for reasonableness by both wages clerks prior to distribution to the company's assistant accountant and the cashier respectively, for posting and payment.

## **Requirement**

**(a) Identify and explain THREE deficiencies (weaknesses) in the control exercised over Cutter Co's weekly wages system.**

**(ii) For each deficiency (weakness) identified above, explain the implications of it for Cutter Co.**

**(9 marks)**

**(b) Identify THREE pieces of standing data which should be included on Cutter Co's wages master file for each production employee.**

**(3 marks)**

**(c) Identify and describe TWO information processing controls in addition to format checks and check digit verification which may be incorporated in Cutter Co's wages software programme to ensure the accuracy and completeness of input and the processing of wages.**

**(3 marks)**

**(15 marks)**

## Suggested solution

(a)

(i) Deficiency	(ii) Implications
<p>There is inadequate control over the activity of the Production Manager in the recruitment of employees. He has sole responsibility for completing and authorising wages master file update forms without the existence of appropriate independent checks and approval.</p>	<p>Undetected errors on wages master file forms could be entered resulting in inaccurate data on the master file.</p> <p>The production manager could fraudulently raise master file update forms for non-existent employees or over state authorised pay rates with the intention of embezzling monies from Cutter Co.</p>
<p>There are no authorisation controls in place or segregation of duties over updating the wages master file and the preparation of the weekly payroll. A wages clerk responsible for preparing the weekly payroll has access to the wages master file and sole responsibility for updating it with new employee details</p>	<p>Errors made when keying in data could remain undetected on the wages master file.</p> <p>The wages clerk could fraudulently enter details for non-existent (ghost) employees on to the wages master file, and then key in hours worked when preparing the weekly payroll with a view to embezzling monies from Cutter Co. The clerk could also erroneously or fraudulently amend standing data on the master file.</p>
<p>There are no independent checks by appropriate responsible officials/ the accountant on the validity of additions and amendments made to the wages master file, including the number of live employee records in the system.</p>	<p>Erroneous or fraudulent payments could be made to employees or in respect of non-existent (ghost) employees' details on the master file.</p>
<p>There is no independent arithmetical check of the total number of hours as computed by and entered on the clock cards by the Production Manager or the Assistant Production Manager.</p>	<p>The total of hours recorded on each clock card could be erroneous, resulting in over/under payments of wages.</p>
<p>The weekly payroll is not checked independently for reasonableness (including sample checking to clock card data) and evidenced as such by the accountant, prior to distribution for management review and production of the weekly wages general ledger posting summary and the list of bank payments to be made to employees.</p>	<p>There is a significant risk of inaccurate and incomplete posting of wages transactions in the accounting records.</p> <p>Undetected errors either by the way of oversight or fraudulent manipulation will result in the over/under payment of wages.</p>



The weekly wages general ledger posting summary and the list of bank payments to be made to employees are not checked and authorised by the accountant, prior to distribution to the assisted account and the cashier for posting and payment.	Incomplete, inaccurate and unauthorised entries could be made in the company's accounting records and unauthorised wages payments could be made by the company.
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9 marks (3 items required).

(b) Standing data for each production employee should include:

- Full name
- Gender
- Date of birth
- Home address
- Full-time or part-time employee classification
- Production department cost centre
- Standard hours contracted
- Basic rate of pay
- Overtime rate of pay
- Statutory tax information
- Deductions data

3 marks (3 items required)

(c) Appropriate information processing controls incorporated may include:

- Reasonableness/range checks – checking whether or not data contained in a field is reasonable or within an authorised range and reporting exceptions where applicable.
- Exception checks – automatically rejecting data input where it is outside set parameters and providing an exception report detailing rejected input.
- Dependence or compatibility checks – comparing related fields searching for logical discrepancies and bringing these to the attention of the user.
- Control totals – established to check for compatibility with previously established user-input controls.
- Sequence checks – to ensure completeness of sequences input or ensure that prescribed sequences of data records are preserved.
- Documents counts – to ensure completeness of input of all prescribed documents.
- Screen warnings – to prevent user logout before processing is complete
- Other.

3 marks (2 items required)

The question tested candidates' knowledge of internal control and the ability to apply the knowledge in the context of controls exercised over wages. At part (a), it was pleasing that a number of candidates were able to identify a requisite three deficiencies in the controls exercised over the company's weekly wages system. However, it was disappointing that instead of explaining the implications of the deficiencies identified, a significant number of candidates proceeded to set out recommendations to address the deficiencies. This was neither an express nor an implied requirement, so no marks could be awarded for these answers and a failure to answer in line with the requirements of the question meant that candidates who didn't miss the opportunity to obtain any of the four and a half marks available. Irrespective of the very good quality of such recommendations by a number of candidates, no marks could be awarded because recommendations weren't a requirement of the question.

At (b), the majority of candidates demonstrated strong knowledge of standing data and the requirements for a wages master file.

However at (c), only a small minority demonstrated sufficient knowledge of the information processing controls which may be incorporated into a wages software programme, to ensure the accuracy and completeness of input and the processing of wages. Even though there was a strong steer in the requirement as to controls which should be incorporated, many candidates were unable to provide any examples; and some proceeded to focus on the two example controls provided in the requirement - contrary to what was asked for.

## **Conclusion**

Auditing is a highly technical subject and to pass the FAU exam candidates need to have a reasonably sound level of understanding of the full range of topics in the FAU syllabus. It is not an easy exam to pass, but questions are set at a level representing a fair challenge to candidates who have prepared diligently, such that they do have a reasonably sound knowledge of all the syllabus areas – particularly of the core areas.

The standard of submissions in this exam varied significantly. It was apparent that high-scoring candidates had reasonably deep-learning knowledge, evidenced by presenting well-structured answers with adequate levels of detailed, relevant and (where appropriate) incisive commentary and explanations. This level of knowledge should be the aim of all future candidates for this exam.

It is important that future FAU exam candidates work to a structured study programme over a time period which gives them the opportunity to assimilate and properly understand the learning material. Timing should allow for a period of revision, question practice and at least one mock examination prior to sitting for the exam.