

KC4 – Corporate Governance, Assurance and Ethics December 2019

Examiner’s Comments

General Comments

This examination consisted of two sections. Section 1 contained two compulsory questions for 25 marks each, and section 2 contained one question carrying 50 marks which is based on the common pre-seen.

The overall performance in this sitting is disappointing. Candidates were required to ensure that they devote sufficient time for preparing for this exam. This examination seems to have been more time pressured than some other sitting. It was noted that candidates seemed to spend more time answering question 3 than the other two questions. Candidates are reminded of the need to allocate their time appropriately. It is an obvious point to make, that attempting two questions makes it more likely that candidates will fail.

A number of common issues arose in candidates’ answers that contributed to their poor performance.

- Reproducing points from the question with minimal additional facts, and not taking into account the action verbs
- Lost focus on the questions’ requirements or failed to appreciate it fully.
- Poor planning of answers and time management

For candidates preparing for this exam it is especially important to focus on tailoring the number of points written to the marks available and to take note of areas that are not essential. The candidates are advised to read the question and plan the answer without being hasty to write the answer.

It was noted that the candidates demonstrated a lack of subject knowledge and poor exam techniques. It is vital with this type of exams to spend adequate time on reading the information provided and think how the information can be applied when answering the questions. Candidates are also advised to be mindful of the action verb, and in this case it was to “analyse”.

Specific comments

Section 1

Question 01

Requirement (a) for 4 marks it was required to explain the role of an internal audit manager in the risk management process of THG. This requirement was well attempted and answered fairly well. Most of the candidates have identified that it is one of the objectives of the internal auditor to monitor overall risk management policy to ensure that the company operates effectively. Weaker answers tended to write the objectives of the internal auditor without paying attention to the questions' requirement. Some have wasted time in writing lengthy answers explaining the concept of risks.

Part (b) For 10 marks, it was required to analyse five risk areas that should be included as part of the internal audit plan.

There were some candidates who have not understood the requirement to ensure that the areas where the affairs of the company have been affected be specific to the scenario rather than listing business risks as political, compliance, fraud etc.

Some candidates without understanding the questions' requirement recognised audit risks such as related party transactions, going concern, management override as risk areas which are areas to be assessed by the external auditor.

The candidate who lacked subject knowledge ignored the fact that the internal auditor is within the organisation and assists management in achieving the corporate objectives.

Part (c) This part carried 5 marks. It was required to propose key internal audit procedures for the identified risk areas. This part was generally well attempted with most answers taking full note of the information given in the scenario.

There were some answers which lacked the technical knowledge detailing audit procedures that should be carried out by the external auditor such as calling for confirmation from third parties, obtain bank confirmation, obtain clarification from regulatory authorities etc.

A significant number of candidates have written general audit procedures such as inquire from management, examine board minutes etc., without specifying the relevant issues in the scenario. Some candidates who have not understood the requirement had written controls to be implemented and recommendations as audit procedures. The examiner tried to test the knowledge of the candidates on audit procedures taking account of the risk is in achieving the objectives of the company.

Part (d) This part carried 6 marks and the candidates were required to propose three procedures that could be implemented in embedding risk awareness to comply with the franchise agreement. Some candidates who had the subject knowledge wrote relevant answers. Some candidates had misunderstood the requirements of the question and wrote general procedures such as to obtain a legal opinion, review the agreement, review the service provided etc., without any relevance to the questions' requirement.

Question 02

Part (a) of the question was also based on the scenario; carried 6 marks and candidates were required to advise Hadrain the Senior Partner of Hadley & co, on six possible root causes of quality issues in the audit engagement.

The examiner expected to test the knowledge of the candidates on the auditor's considerations on improving the quality of the firm. Many candidates have understood the questions' requirement but they demonstrated poor knowledge in analysing the issues in the given scenario. The examiner expected the candidates to apply the theoretical knowledge according to SLSQC1 and evaluate the given scenario accordingly. Most of the candidates just copied the elements of the systems of quality control, such answers tended to be either too brief, or were little more than a list of bullet points.

Part (b) For 4 marks, required the candidates to identify four additional information that may be obtained to understand the root causes of quality control. Almost all the candidates failed to produce relevant answers for this part of the question.

Part (c) of the question carried 10 marks, and required the candidates to recommend five quality improvements that H&C could implement to overcome its quality issues. Some candidates who were with sound subject knowledge had recommended quality improvements for each quality issue. Many candidates had ignored the action verb and just copied the elements of the quality control system. Some candidates had explained the deficiencies in the firm without making any recommendations.

Part (d) of the question carried 5 marks, and required the candidates to assess the independence of H&C in accepting the group audit. Although almost all candidates had attempted this part of the question only a small number of candidates were able to obtain satisfactory marks. Majority failed to evaluate the issues in the given scenario and just copied the section on independence of the Code of ethics. Some candidates who lacked subject knowledge identified irrelevant threats as self-interest, advocacy, without assessing the issue properly.

Question 03

Question 3 was for 50 marks, which was based on the common pre-seen. The client was a plantation company.

Part (a) This part of the question carried 10 marks, was based on the Code of Best Practice on Corporate Governance. The candidates were required to advise the client on enhancing the effectiveness of the board of directors.

Majority of the candidates ignored the requirements' of the question and did not focus on advising measures that should be taken, but merely copied responsibilities of the directors from the Code of best practice on corporate governance. The candidates are advised that although this is an open book exam, they should not just copy the facts given in the Code but should relate to the role of the directors in the given scenario and address the questions' requirement which was to enhance effectiveness.

Part (b) (1) of the question carried 5 marks. It was required to evaluate whether having a corporate code of ethics would be sufficient to have a positive impact on promoting ethics in the business operations of the client.

Majority of the candidates who had subject knowledge had written relevant answers as this area was covered in the text book. Some candidates used their general knowledge and wrote general answers. Others who had misunderstood the questions' requirement wrote that the code applies to auditors and other professionals and wrote completely irrelevant answers.

The candidates who were not prepared for the exam wrote the advantages and disadvantages of having a code, and copied the fundamental principles of the code of ethics which was irrelevant.

Part (b) 11 of the question carried 5 marks, and it was required to evaluate the ethical issues faced by Daniel and advise him on the safeguards. Majority of the candidates understood the questions' requirement which is on ethical behaviour but ignored the action verb which is to "evaluate". The candidates wrote how to eliminate or reduce the threat to an acceptable level.

Part (c) which carried 5 marks required the candidates to propose audit procedures that Pedris & co., could perform in auditing the "impairment assessment" made by UEL's management. Although the candidates understood the questions' requirement they failed to address the following;

- Develop point estimation or range to evaluate management estimates
- Assess the sensitivity of the assumption used in computation

Most of the answers were limited only to an evaluation of the estimate, growth rate, discount rate, cash flows. Most of the candidates demonstrated poor knowledge in impairment assessment. Many candidates who lacked technical knowledge wrote answers such as to obtain an independent valuation, obtain a letter of representation which are not adequate for an impairment assessment. The candidates are advised to refresh their knowledge on LKAS 36, and are expected to apply technical knowledge and write extensive audit procedures.

Part (d) carried 10 marks and required to advise Pedris & co. the extent to which reliance can be placed on the work of internal auditor in determining the audit procedures. The candidates with a sound subject knowledge managed to write relevant answers. Some candidates just copied SLAuS 610 without linking it to the pre-seen.

Part (e1) carried 3 marks and required to advise the Finance Director on the applicability of KAMs in the audit report of UEL for the year ended 31st March 2019. Majority of the candidates understood the questions' requirement and produced relevant answers. The candidates who had not comprehended the questions' requirement wasted time in writing lengthy answers defining and explaining KAMs.

Part (e11) carried 7 marks and required to propose three KAMs with reasons that the auditor may report in the audit report on the financial statements. The only relevant KAM written by most of the candidates was the value of biological assets. A few candidates had proposed revenue recognition and impairment assessment. Most of the candidates who had not read the pre-seen properly identified irrelevant KAMs such as employees' benefits, related party transactions, going concern and just described it. Most of the answers did not include an explanation to be communicated in the auditors' report as per the questions' requirement.

Part (f) carried 5 marks and required to advise the impact of a modification to the audit report. As per the information the inventory was incorrectly valued at 90 million rupees and the external auditor has expressed a modified opinion for the year ended 31/03/18. In the end of year 2019, the management had valued the inventory according to the company policy.

The issue was that the opening balance of the inventory was not corrected. Although the candidates were expected to address the significance of the error, a majority of the candidates failed to do so. Most of the answers were confined to verify limited area of advising either modify or not. Some candidates who lacked the technical knowledge suggested to change the policy on valuing inventory.

Conclusion

The question paper may test any part of the syllabus therefore, the candidates should study the whole syllabus. Selective study will definitely limit the number of questions that the candidates could attempt.

Candidates are requested to apply the principles and rules from their previous studies to more complex scenarios and demonstrate their ability to handle different issues in the common pre seen. They should keep abreast of current developments in the economy in order to understand the issues easily.

Candidates are expected to have a broader technical knowledge and be able to link it to the appropriate audit issues in a practical situation. Candidates are advised to practise past exam papers and review the model answers together with examiners reports.

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