MARK PLAN AND EXAMINER'S COMMENTARY

The marking plan set out below was that used to mark this question. Markers were encouraged to use discretion and to award partial marks where a point was either not explained fully or made by implication. More marks were available than could be awarded for each requirement. This allowed credit to be given for a variety of valid points which were made by candidates.

General comments
The standard of answers to the short-form questions (SFQs) was consistent with that in the previous examination sessions in 2015. The answers to SFQs 1 and 2 were particularly disappointing given that SFQ 1 has been examined in previous sessions and SFQ 2 could be answered by reference to the Open Book. A significant number of candidates failed to make use of the facility to present their answers to SFQs in note form and wasted time writing lengthy answers thereby leaving themselves short of time for the long-form questions. Candidates performed well on most areas of the syllabus although many answers to questions 7b were very disappointing and highlighted a lack of familiarity with ISA 600 Special considerations – audits of group financial statements (including the work of component auditors).

Question 1
Total Marks: 4

Reasons it is important for an external audit firm to assess the integrity of a prospective client's management
Required by ISA220/ISQC1
Reduces engagement risk
Reduces risk of:
- investigations by regulatory bodies
- claims for damages
- loss of firm's reputation
- inappropriate opinion

Lack of integrity may indicate:
- aggressive interpretation of accounting standards/window dressing/bias/ inappropriate judgements/audit risk
- weak control environment/override of controls
- inappropriate limitation on scope of work/intimidation
- criminal activities/money laundering/fraud/breach of laws and regulations
- aggressive tax avoidance/evasion
- unreliable management representations

Answers to this question were disappointing given that this topic has been examined on a number of occasions. The majority of candidates were able to cite several points but not enough to score full marks. The points most commonly identified were those relating to management bias, fraud, reputational risk and the unreliability of management representations. The points most commonly overlooked were those relating to engagement risk, such as exposure to claims for damages and regulatory investigations. Furthermore, only a minority of candidates cited that ISA 220 and ISQC1 require the assessment of management integrity.

Total possible marks	6
Maximum full marks	4

Question 2
Total Marks: 3

Purposes of the review of work performed by audit junior

To consider if:

- work performed in line with audit strategy/plan
- work performed in accordance with professional standards/regulatory requirements
- significant matters have been raised for further consideration
- appropriate consultations have taken place
- work adequately documented
- there is a need to revise nature/timing/extent of audit procedures
- work performed supports conclusions reached
- sufficient and appropriate evidence obtained
- objectives of audit procedures achieved

To provide feedback for audit junior's development

Answers to this question were of a mixed standard. Those candidates who were familiar with the contents of para A17 of ISA 220 tended to score full marks. Candidates who did not make use of the Open Book struggled to identify more than two or three relevant points. The points most commonly identified were those relating to performance in accordance with professional standards, procedures carried out properly and sufficient appropriate evidence. The points most commonly overlooked were those relating to work carried out in line with the audit plan and the need to revise audit procedures. A minority of weaker candidates confused the review of an audit junior's work, which is required on every audit, with an engagement quality control review and consequently identified inappropriate purposes.

Total possible marks	5
Maximum full marks	3

Question 3
Total Marks: 3

Procedures to address potential conflict of interest

Separate engagement teams

Brief staff/clear guidelines on confidentiality issues/procedures

Information barriers:

- physical separation/use staff from different offices
- confidential/secure data filing

Procedures in place for dealing with any need to disseminate information beyond barrier

Staff to sign confidentiality agreements

Regular review of the application of safeguards by a senior individual not involved in the engagements

This question was generally well answered and many candidates scored full marks. Most candidates were able to provide a range of relevant points such as separate teams, information barriers and confidentiality agreements. A number of candidates appreciated that there should be an independent review but failed to specify that the review should cover the application of safeguards. A significant number of candidates wasted time citing the need to obtain informed consent from the respective clients, failing to appreciate that the scenario stated that this had already been obtained.

Total possible marks	5
Maximum full marks	3

Question 4
Total Marks: 4

Matters to consider

Reasons why milk powder became contaminated

Whether it resulted from breach of regulations, as may
- indicate inadequate internal controls/weak control environment
- indicate lack of management integrity
- result in fines/penalties from regulators
- result in suspension of licence/closure

Whether any other areas/items affected

Whether any babies have been harmed by contamination which may result in:
- legal claims against Squid
- potential significant uncertainty

Potential negative impact on Squid's reputation/bad publicity resulting in loss of revenue

Increased risk of material misstatement:
- refunds for returns
- irrecoverable trade receivables
- inventory to be written off
- provisions/contingent liabilities for legal claims/fines
- squid may no longer be a going concern/doubts over going concern (GC):
  - GC basis of preparation may not be appropriate/break-up basis required
  - uncertainty over GC may not be adequately disclosed

Answers to this question were of a mixed standard. The majority of candidates identified the potential legal and regulatory proceedings and that provisions may be required for damages or fines. Although many candidates identified the going concern risk, many of these candidates failed to consider the potential impact of this issue on the financial statements, i.e. inappropriate basis of preparation or absence of a disclosure of an uncertainty in the notes to the financial statements. Furthermore, a significant number of candidates failed to consider the need for provisions in respect of refunds, irrecoverable trade receivables and inventory write-downs.

Total possible marks	10
Maximum full marks	4

Question 5
Total Marks: 3

Actions firm should take

Assess whether misstatements are material in aggregate/by nature

Consider whether there are any other misstatements

Revise audit plan/perform further procedures

Communicate misstatements to management/request misstatements corrected

Perform audit procedures on any changes made

Document:
- amount below which misstatements considered trivial
- accumulated misstatements
- conclusion regarding materiality of uncorrected misstatements

Obtain written representation from management that the effect of uncorrected misstatements is immaterial

This question was well answered as most candidates identified that the individually immaterial items should be aggregated to determine whether they were material in aggregate and that they should be communicated to management. However, few candidates considered whether this was indicative of other misstatements and whether the audit plan needed revision. Only a minority of candidates identified the need for a written representation that the effect of uncorrected misstatements is immaterial. A number of candidates strayed beyond the requirement and wasted time describing the various audit opinions that might be provided, failing to appreciate that the requirement related to actions to be taken before reaching the audit opinion.

Total possible marks	9
Maximum full marks	3

Question 6
Total Marks: 3

Conclusion following review of financial statements Expressed negatively 'Nothing has come to our attention……..' **Opinion expressed in audit report** Expressed positively 'In our opinion the financial statements…'/true and fair view Properly prepared in accordance with CA06 Consistency of information in directors' report with FS Matters on which required to report by exception **Reasons** Limited/moderate assurance for review engagement compared to reasonable assurance for external audit Scope defined by management/ISRE 2400 for review engagement but by ISAs/CA06 for external audit Review is limited to inquiry/analytical/other review procedures whereas audit work includes tests of detail
This question was very well answered with the majority of candidates scoring maximum marks. Most candidates correctly identified the different levels of assurance and the manner in which they are expressed. Furthermore, most candidates identified that the scope of the work is greater for an audit than for a review engagement. Weaker candidates wasted time writing about the differences between the reports as a whole instead of the conclusions within the reports. These candidates often described the addressees of the reports and to whom they were distributed. There were no marks for these points.

Total possible marks		7
Maximum full marks	½ mark per point	3

Question 7
Total Marks: 35

General comments This was the least well answered of the long-form questions. Part (a) was generally well answered with the majority of candidates providing justifications of the key risks along with suitable audit procedures. However, a significant minority of candidates failed to appreciate that Haskett was a newly-formed company and wasted time citing procedures in relation to opening balances and obtaining prior year working papers from the previous auditor, which were not relevant. Answers to part (b) were disappointing, particularly in relation to the implications of Haskett being a component of the MT group.
(a) Justify why the items listed as (1) to (3) in the scenario have been identified as key areas of audit risk and, for each one, describe the procedures that should be included in the audit plan in order to address those risks.

Revenue **Justification** Draft revenue is 20.5% higher than budgeted revenue and draft gross profit is 20% higher than budgeted gross profit of 17%. These results are inconsistent with delays in the start of the bus service and suggest revenue is overstated.	**Procedures** Discuss with management the reasons for the variance between actual and budgeted figures. Obtain a breakdown of revenue by stream/month to identify any anomalies.
Cash There is a risk that revenue is understated due to: - potential for misappropriation of cash receipts - delays in banking receipts at year end.	**Cash** Ascertain and test controls over the collection and recording of cash on buses Reconcile amounts recorded on the buses with cash book and bankings. Review after date bank statements for cash banked after year end which relates to pre-year end journeys and check such income is appropriately accrued.
Contactless card There is a risk of misstatement of revenue due to: - lack of experience in the use of such	**Contactless card** For a sample of daily remittances from Dolphin: - compare amounts received to journey

systems - no checks on the amounts recorded/remitted by Dolphin - revenue from Dolphin being incorrectly recorded net of the 12% commission - internal control deficiencies in the newly-formed company, Dolphin - potential delays in the transfer of funds from Dolphin at year end. There may be issues regarding obtaining sufficient appropriate evidence if there are problems gaining access to Dolphin's systems. **Season tickets** There is a risk of inappropriate revenue recognition where season tickets span the year end due to: - incorrect revenue recognition (i.e. recognition in full on receipt) - errors in calculating the proportion of revenue to defer.	volume data recorded by card reader/sales reports for reasonableness - check that revenue is recorded before deduction of 12% commission. Perform tests of controls at Dolphin or seek assurance from Dolphin's auditor. Ascertain that any other auditor relied on is: - independent of Dolphin and Haskett - professionally competent. Ensure that remittances for journeys taken just before the year end are received and included in the accounting records. Inspect bank statements for remittances, which relate to pre-year end journeys, received from Dolphin after the year end. **Season tickets** Trace bank receipts to revenue/deferred revenue account. Ascertain the basis for calculation of revenue/deferred revenue and consider reasonableness. Re-perform the calculation.
Property, plant and equipment (PPE) – buses **Justification** The PPE (buses) balance is 40% above budget suggesting PPE (buses) is overstated or depreciation is understated. Refurbishment costs capitalised may not meet the relevant criteria, for example, repairs may be incorrectly capitalised. The estimated useful life of buses may be inappropriate because: - both refurbished and new buses are being depreciated over ten years but new buses would be expected to have a longer useful life - buses may have no use at the end of the eight-year contract. Buses have not been owned by Haskett for the full year, therefore depreciation may not have been pro-rated correctly. Buses may not have been depreciated when ready for use if they were ready before 1 February. The residual value of buses may have been over-	**Procedures** **New buses** Vouch costs capitalised to invoices/contract with EchoBus. Ensure that any purchase costs that do not meet capitalisation criteria are excluded. **Second hand buses** Vouch purchase cost to agreement with MT subsidiary/bank statement. Vouch to ownership/registration documents. Select a sample of buses from the asset register and physically inspect and assess their condition. Inspect management's impairment reviews. Obtain a schedule of refurbishment costs: - ensure costs included are capital in nature/meet IAS 16 criteria - vouch time spent on refurbishment by employees to timesheets - vouch materials costs to purchase invoices. Compare the value attributed by Haskett to second-hand buses with similar-aged buses on the market. Compare the useful life of buses to other buses in MT group/other similar companies. Consider whether significant profits/losses arise on disposal of buses in the group. Enquire of directors: - the basis of estimated useful life - the reason why refurbished buses have the same useful life as new buses - reasons the useful life extends beyond the length of the eight-year contract - the basis of estimates of residual value. Recalculate depreciation ensuring that charges are pro-rated correctly.

or under-estimated.	
Legal claim **Justification** The £250,000 claim represents 2.8% of revenue and 46.5% of profit before tax and is therefore material. The absence of a provision or disclosure may be inappropriate. If the claim is probable to succeed a provision should be recognised. If the claim is possible to succeed a disclosure should be included in the financial statements. A contingent asset may not be offset against a liability as this does not comply with accounting standards.	**Procedures** Ascertain from the directors of Haskett the reason for not including a provision/disclosure in the financial statements. Review the contracts between Haskett and the government body and EchoBus to ascertain the terms/penalties for any breach. Review correspondence with Haskett's legal advisers to determine the likely outcome of the claim(s). Review correspondence with the Government body and EchoBus to determine the likelihood of settlement. Review board minutes regarding any developments surrounding the claims, such as an out of court settlement. Obtain a written representation from management regarding its intention to settle/fight the claim against Haskett.

It was pleasing to note that the majority of candidates attempted to make use of the financial information provided in the scenario, appearing to have taken on board points raised in previous examiners' commentaries. Whilst the majority of candidates appreciated that budgeted information was provided (in the absence of prior year figures) a significant minority of candidates wasted time citing procedures to test the accuracy of the budgeted figures.

Revenue

Most candidates provided a number of reasons to justify why revenue was a key area of audit risk, including making use of basic analytical procedures. However, only stronger candidates identified that the actual figures presented were inconsistent with the delay in starting the bus service. Candidates who structured their answers around the three revenue streams (cash, contactless cards and season tickets) tended to produce better answers than those who took a scattergun approach. The most commonly overlooked justifications were in relation to the contactless card - that there may be issues for the auditor in gaining access to Dolphin's system and that revenue may have been incorrectly recorded net of the 12% commission deducted by Dolphin. The most commonly overlooked audit procedures were those relating to reliance on Dolphin's auditor to gain assurance over the contactless system and the independence and professional competence of that auditor. The majority of candidates correctly identified that revenue recognition issues may arise in relation to season tickets. However, fewer candidates appreciated that cut-off issues might arise in relation to cash and contactless payments if amounts were banked or remitted to Haskett after the year end.

Property, plant and equipment (PPE) – buses

Most candidates provided a number of reasons to justify why PPE - buses was a key area of audit risk and made use of basic analytical procedures. The most commonly overlooked justifications were:

- the risk of buses being assigned an inappropriate useful life given both refurbished and new buses were depreciated over the same ten-year period and that buses may not have any use at the end of the eight-year government contract; and
- the possible over- or under-estimation of residual values.

The most commonly overlooked procedures were:

- vouching of ownership documents
- inspecting management's impairment reviews
- comparing the useful life of the buses to those used by similar companies and consideration of whether there were significant profits or losses on the disposal of buses in the group
- enquiring of management why refurbished buses have the same useful life as new buses and why the useful life of ten years extended beyond the eight-year government contract, and
- enquiring of management the basis of the estimated residual values.

In respect of the audit procedure for testing the existence of the buses, a number of candidates lost marks by incorrectly stating that the sample of physical buses should be selected and traced to the asset register instead of selecting a sample from the asset register and verifying the buses existence.

The majority of candidates correctly identified that some costs may be inappropriately capitalised as part of the refurbishment of buses acquired from other MT subsidiaries. However, fewer candidates earned the

marks for vouching the capitalised costs to invoices and timesheets.

Legal claim against Hackett
Most candidates recognised that the legal claim was material but only stronger candidates were able to provide further reasons to justify why the legal claim was a key area of audit risk. The most commonly overlooked justifications were relating to whether the claim should be disclosed or provided for depending on whether the outcome was either possible or probable. Generally, most candidates identified some appropriate audit procedures to address the risk. A number of candidates cited, in general terms, a relevant audit procedure (e.g., review board minutes) but didn't earn the marks available for explaining the relevance of that procedure (i.e., a review of board minutes would provide information on developments such as an out of court settlement). A number of candidates wasted significant amounts of time discussing the going concern implications of the legal claim which was outside the scope of the requirement.

Total possible marks	61½
Maximum full marks	25

(b) Set out the matters you should consider, as part of your audit planning, arising from: (i) the ownership of Dolphin by Clay McCarthy; and (ii) Haskett being a component of MT group

(i) the ownership of Dolphin by Clay McCarthy
Dolphin appears to be a related party of Haskett as it is controlled by Clay McCarthy who is a key manager at Haskett. Transactions between Haskett and Dolphin are material by nature and therefore require disclosure in the financial statements. There may be a risk of non-disclosure if Haskett's management is unwilling to disclose such transactions. The 12% commission charge appears high and transactions may not be on an arm's length basis.

The auditor will require a written representation from management that disclosure of related party transactions is complete and it will need to include audit procedures in the audit plan to verify the adequacy of related party disclosures. The component auditor will need to disclose such transactions to the group auditor.

Sufficient, appropriate evidence over transactions may be difficult to obtain given the need to rely on information from Dolphin in light of Haskett's internal control deficiencies surrounding transactions with Dolphin.

There is an increased risk of fraudulent behaviour and consequently a need for increased scepticism which must be discussed by the engagement team during planning.

(ii) Haskett being a component of MT Group
The component auditor will need to involve the group auditor in its risk assessment at the planning stage as there may be additional risks identified by the group auditor. Instructions will be issued by the group auditor setting out its requirements and the materiality thresholds relevant to the group audit. The component auditor may need to carry out additional audit procedures to address any risks identified by the group auditor and will need to confirm to the group auditor that its instructions have been followed.

The group engagement team may be involved in the work of the component auditor and the timing of audit procedures will need to take into account the timetable for reporting set by the group auditor.

The form of communications/report required by the group auditor must be confirmed and the component auditor will need to report significant issues/risks to the group auditor, such as:

- evidence of management bias
- any non-compliance with laws/regulations or suspected fraud
- related party transactions (i.e. amounts received from Dolphin)
- intra-group transactions (i.e. sale of buses to Haskett)
- information regarding the legal claim(s)
- a list of uncorrected misstatements.

The component auditor should also consider whether its subsequent events review will need to be extended to cover any gap between signing the audit report on Haskett's financial statements and the date of the audit report on the group financial statements.

Answers to part (b) were disappointing with answers to section (i) being of a higher standard than section (ii). A number of candidates did not attempt section (ii) or presented very short or irrelevant answers and therefore failed to score any marks for this section.
In respect of section (i), those candidates that correctly identified that Dolphin was a related party of Haskett then went on to score reasonably well. However, a significant minority of candidates failed to identify the related party issue. The points most commonly cited, having identified Dolphin as a related party, were that related party transactions are material in nature and therefore disclosures are required in the financial statements. Stronger candidates were then able to set out some further matters to consider as part of the audit planning such as the need to obtain written representations. The points most commonly overlooked were those relating to the difficulty in obtaining evidence for related party transactions, the need for the audit team to increase professional scepticism and appropriate discussion of issues by the engagement team during audit planning.
In respect of section (ii), the points most commonly identified by stronger candidates were those relating to risks identified by the group auditor, materiality thresholds, the timetable for the audit and the need to report significant issues to the group auditor. However, few candidates were able to provide examples of the significant matters that need to be reported to the group auditor. The point most commonly overlooked was that relating to the extension of the subsequent events review to cover any gap between signing the audit report on Haskett's financial statements and the audit report on the group financial statements.
Weaker candidates were often unable to set out any matters to consider as part of audit planning arising from Haskett being a component of MT Group. A significant number of weaker candidates wasted time setting out irrelevant ethical threats (e.g., conflict of interest, self-interest, familiarity and self-review) and safeguards to mitigate those threats (e.g. information barriers) failing to appreciate the nature of the relationship between the component auditor and the group auditor, including the fact that the audit teams were part of the same audit firm. Candidates who had an awareness of the contents of ISA 600 produced significantly better answers to this part of the question.

Total possible marks	10
Maximum full marks	28

Question 8
Total Marks: 25

General comments
This was the second best answered long-form question. However, the quality of candidates' answers varied significantly between the four scenarios presented. A number of candidates wasted time presenting information relevant to engagement performance whereas the requirement asked candidates for matters to consider and steps to take **before** acceptance.

For each of the four prospective audit engagements, identify the matters that your firm should consider, including any professional and ethical issues arising, and any steps it should take before deciding whether to accept the engagement.

Clymene
Matters to consider
The reduction in the number of employees in Clymene's accounts department may make obtaining audit evidence more difficult, especially if key employees have left before any audit work commences. It may result in an increase in the risk of misstatement.
The additional engagement to prepare financial statements will require additional resources and may present a threat to objectivity due to:

Familiarity threat
- the firm has been acting for Clymene for a number of years and may be too trusting of the client's management

Self-review threat
- the results of accounts preparation work will be reflected in the financial statements that are the subject of the external audit. The audit team may be insufficiently questioning of the work performed to prepare the financial statements or may be unwilling to highlight any deficiencies identified in that work

Management threat
- the team preparing the financial statements may be expected to make decisions/ judgements about the amounts included, whereas these should be made by management. Their views may become too closely aligned with the views of management

Self-interest threat

- the firm may place too much reliance on the fee income generated from Clymene and may be unwilling to modify its opinion on the financial statements due to fear of losing the client
- fees will increase to £750,000 which may be on a recurring basis if the firm prepares the financial statements each year. The firm's gross income from Clymene will then be £7,150,000 which represents 10.5% of gross practice income. This is below the 15% threshold for unlisted companies but above the 10% threshold. Therefore, safeguards will be required.

As Clymene is not a listed company, an engagement to prepare financial statements is permitted.

Steps

Ensure that adequate resources and expertise are available within the firm.

The engagement partner should be rotated if necessary to mitigate any familiarity threat

Determine if the firm is able implement the following safeguards:

- preparation of the financial statements to be performed by a separate team that is not involved in the external audit
- arrangement of an external independent quality control review.

Ensure the client understands that the firm cannot make management decisions and that the service to prepare the financial statements is of a technical and mechanical nature, i.e.:

- no authorisation/approval of transactions
- no preparing originating data
- no determining/changing journal entries

The firm must document the existence of informed management.

Ascertain if Clymene requires the firm to prepare the financial statements on an on-going basis and disclose the fact that fees are above the 10% threshold to the firm's ethics partner and to those charged with governance at Clymene.

Dusky

Matters to consider

Whether the level of assurance required is limited or reasonable. There may be a risk of an expectation gap given that any system has inherent limitations. The firm cannot provide absolute assurance that the system is free from control deficiencies. The system may include control deficiencies not identified in the firm's report to management and are therefore unlikely to have been addressed by the recent system changes.

The scope of engagement, including the period or point in time to be covered and nature of the report required.

There is a potential threat to objectivity due to a self-review threat as the assurance report on the systems may be used as part of the external audit. The audit team may be insufficiently questioning of the assurance work or may be unwilling to highlight deficiencies in the work.

Steps

Discuss the scope of the engagement and the level of assurance required with the directors to ensure their expectations are appropriate.

Determine if the firm is able to put appropriate safeguards in place, i.e.:

- a separate team for the assurance engagement whose members are not involved in the external audit
- an independent partner review to assess whether the systems are rigorously reviewed as part of external audit work

Ensure that adequate resources and are expertise available within the firm.

Risso

Matters to consider

There is a potential threat to professional competence and due care. Risso operates in the marine biology industry, a highly specialised sector, in which the firm may not have sufficient expertise. The firm may also be unaware of the same set of facts as the incumbent auditor.

The directors appear to be "opinion shopping" which may call into question the integrity of management and the firm may not wish to be associated with the client due to reputational risk.

A self-interest threat exists if the firm is tempted to give the opinion the client desires in order to obtain future work from Risso.

Ethical issues, such as conflicts of interest, may exist and, if so, will need to be addressed.

Steps

Seek permission to contact the incumbent auditor. If the management of Risso refuses, the firm should consider declining the engagement. If permission is obtained, contact the incumbent auditor to ensure the firm is apprised of all the facts relevant to the issue at the time the opinion was modified.

Perform searches/background checks on Risso's management.

Ensure adequate resources and expertise are available within the firm.

Irrawaddy
Matters to consider
There is high engagement risk due to reliance by the bank on the firm's assurance report and the firm should consider the level of the liability cap it should put into place.
The firm lacks cumulative knowledge of the business and its management and it is unclear why the current auditor was not offered the assurance engagement. It may indicate a potential management integrity issue if management is hiding something from the external auditor. The firm may not wish to be associated with Irrawaddy due to reputational risk.
The current year audit is not complete and it is unclear whether the audited figures for the year to 30 June 2015 will be available to provide opening balances for the prospective financial information.
Whether management accepts that it is responsible for the preparation of the prospective financial information and whether it understands that an engagement to examine prospective financial information provides a limited level of assurance.
Ethical issues, such as conflicts of interest, may exist and, if so, will need to be addressed.
Steps
Ascertain if permission will be given to communicate with/inform the incumbent auditor.
Ascertain from management why the incumbent auditor was not offered the engagement to examine the prospective financial information.
Perform searches/background checks on Irrawaddy's management.
Ensure adequate resources and expertise are available within the firm.

Clymene
This part of the question was generally well answered as the majority of candidates identified the self-interest, self-review and, to a lesser extent, management threats and provided plausible explanations of each threat. The familiarity threat, arising from acting for a number of years, was often overlooked by many candidates. A small number of candidates wasted time discussing whether there were any going concern issues (due to the reduction in employee numbers) when there was no evidence of this. The most common omission was the failure to specify that the independent review should be an external review. Candidates generally cited appropriate steps in relation to the matters they identified. However, a significant minority of candidates continue to incorrectly cite information barriers in relation to a self-review threat when this is only appropriate where there are confidentiality issues. Some candidates also wasted time discussing fee monitoring procedures that should be in place when these would only be relevant after the engagement had been accepted. A small minority of candidates stated, incorrectly, that the engagement should only be accepted in an emergency failing to appreciate that this safeguard only applies to listed entities.
Dusky
Answers to this part of the question were very disappointing. The vast majority of candidates failed to appreciate that an engagement to provide assurance on the effectiveness of internal controls could be a reasonable or limited assurance engagement. Most candidates assumed that it could only be a limited assurance engagement. However, a significant number of candidates did appreciate that absolute assurance could not be given and that there was an expectation gap on the part of management. A significant minority of candidates assumed, incorrectly, that the engagement was an internal audit engagement and consequently identified, incorrectly, a management threat. A number of candidates also identified a self-interest threat in relation to fee income. This was not appropriate as the engagement was likely to be non-recurring.
Risso
This part of the question was generally well answered as the majority of candidates identified that the prospective client was opinion shopping and that this had implications for management integrity and the fundamental principle of professional competence and due care. Many also identified the significant self-interest threat and the need to obtain client consent to discuss the reason for the modification with the incumbent auditor. The point most commonly overlooked was that relating to the need to be aware of the same facts as the incumbent auditor.
Irrawaddy
Answers to this part of the question were very disappointing. The points most commonly identified were those relating to the reason why the incumbent auditor was not offered the non-audit service and the implications for management integrity. The points most commonly overlooked were those relating to engagement risk associated with the bank's reliance on the assurance report. A number of candidates wasted time listing irrelevant threats to objectivity, such as an advocacy threat, or seeking clarification on the intended use of the information when this was clearly stated in the scenario. A small number of candidates wasted time discussing going concern, believing, incorrectly that a company seeking finance must be in financial difficulty.

Total possible marks	57½
Maximum full marks	25

Question 9
Total Marks: 20

General comments
This was the best answered long-form question with candidates scoring higher marks on parts (a) and (c) compared to part (b). A significant minority of candidates' answers for this question were very short suggesting that time management had been an issue for them.

(a) For each internal control deficiency identified in (1) and (2) above, draft points for inclusion in your firm's report to the trustees. For each deficiency, outline the possible consequence(s) of the deficiency and provide recommendations to address it.

(1) Collection boxes used during street collections were not sealed or numbered and collectors were responsible for counting and recording proceeds from their own collection boxes.

Consequences	Recommendations
Cash donations are susceptible to misappropriation and errors in the counting proceeds may not be identified. If a collection box is not returned, Rescue24 will be unable to determine which one is missing or to hold collectors accountable for specific collection boxes. Rescue24 will be unable to identify which are the most effective collectors or collecting locations. This will have a negative impact on revenue and cash flows.	Collection boxes should be sealed with a tamper-proof seal and sequentially numbered. Collectors should sign for a numbered collection box when taken. A record should be kept of which collector has which box and in which location and all collection boxes should be checked in when returned at the end of the collecting period. Proceeds should not be counted by collectors but should be counted and recorded by two people in the presence of the collector who should be given a receipt for the amount collected. Proceeds should be banked promptly and an independent reconciliation of amounts recorded and amounts banked should be undertaken.

(2) Veterinary drugs were not stored in a secure lockable container, in contravention of the requirements of the Veterinary Medicines Directorate.

Consequences	Recommendations
There is an increased risk of theft of drugs and Rescue24 may be unable to treat animals if drugs run out unexpectedly. Contravention of the requirements of the VMD may lead to fines or disciplinary action including loss of licence or closure. This will have a negative impact on profits and cash flows.	Install a lockable secure container which is fixed to the floor/wall. Keys or security codes should only be made available to those with authority to use drugs and the keys should be stored securely or security code changed on regular a basis. A record of drugs in/out should be maintained and any movements signed for. Regular inventory checks should be performed comparing the quantity of drugs in the container with the records.

Deficiency (1)
This part of the question was generally well answered as most candidates identified that donations may be stolen or collection boxes could be lost and that these risks could be mitigated by sealing and numbering the buckets. It was pleasing to note that the majority of candidates appreciated the need for dual control during counting and segregation of duties between collecting and counting/recording. The points most commonly overlooked were those relating to the negative impact on revenue and cash flow and the need to reconcile amounts recorded with amounts banked.

Deficiency (2)
Most candidates identified that drugs could be stolen and that the entity could face fines or even lose its licence to operate as a result of the breach in regulatory requirements and that these risks could be mitigated by storing the drugs in a lockable container with restricted access. The points most commonly overlooked were those relating to the adverse impact on profits and stockouts. A number of candidates merely stated that Rescue24 should comply with VMD requirements and consequently failed to earn the marks available for describing how the procedures might work.

Total possible marks	15
Maximum full marks	7

(b) Identify and explain the factors which give rise to an uncertainty about the going concern status of Rescue24.

Resuce24 is in a net liability position posing the risk that it may be unable to meet debts as they fall due. Expenditure exceeds income resulting in an inability to generate cash to cover Rescue24's activities. Rescue24 has faced difficulties raising funds through traditional activities as well as suffering from a decline in government funding which means it is unlikely to be able to rely on these sources of funding in future.

The trustees failed to promote a crowdfunding campaign or recruit any employees with crowdfunding experience. Consequently, the campaign was unsuccessful and no funds were raised. It appears unlikely that new sources of funding will be identified quickly.

Rescue24 is reliant on its overdraft facility which is repayable on demand and could therefore be withdrawn. An overdraft is an expensive form of funding and interest payments will put a strain on cash flow.

The bank loan is secured on Rescue24's only premises. If Rescue24 defaults on the loan payments or breaches covenants the bank may call in the loan and seize the property. The charity will be left with no base for its operations.

Three of the five trustees and the fundraising manager resigned. There may be insufficient expertise to continue with Rescue24's activities and there may be a possible breach of its constitution. There is no fundraising expertise left in the organisation and it may be difficult to recruit new employees in view of the present difficulties.

As a result of non-compliance with the VMD requirements, Resuce24 may be at risk of losing its licence and any resulting fines will exacerbate its present cash flow issues.

This part of the question was generally well answered as the majority of candidates provided a range of factors that indicated uncertainty about the going concern status. However, many candidates were unable to provide plausible explanations as to why those factors indicated an uncertainty about the going concern status. For example, the vast majority of candidates identified the reliance on the overdraft facility as a factor but only a minority appreciated that this was an expensive form of funding which would have an adverse impact on cash flow and that the facility could be withdrawn at any time. A number of candidates incorrectly cited that the overdraft (rather than the bank loan) was secured on the premises.

Total possible marks	13½
Maximum full marks	7

(c) Assuming your firm concludes there is an uncertainty about the going concern status of Rescue24, explain the potential implications for the audit opinion on the financial statements of Rescue24 for the year ended 30 June 2015 if the trustees:

(i) make appropriate disclosures

There is no material misstatement and no limitation on scope, therefore an unmodified audit opinion with a modified audit report will be issued. An emphasis of matter paragraph will be included immediately after the opinion section to draw users' attention to the matter disclosed in the financial statements as the issue is fundamental to users' understanding of the financial statements. A statement that the opinion is not modified in respect of the uncertainty should be included.

(ii) do not make any disclosures

There is a material misstatement due to the lack of appropriate disclosure and therefore a modified opinion/report is required. If the matter is considered material (but not pervasive) a qualified opinion ('except for') will be issued. If the matter is considered material and pervasive an adverse opinion will be issued. The audit report will include a section headed "basis for qualified opinion"/"basis for adverse opinion", describing the matter giving rise to the modification.

Although many candidates scored maximum marks on this part of the question, a significant number of candidates' answers were very disappointing. This stemmed from the fact that these candidates did not read the question carefully. The question was based on the assumption that the firm had concluded that there was an uncertainty about the going concern status. However, these candidates assumed that the financial statements had been prepared on an inappropriate basis and consequently reached

inappropriate conclusions in respect of the audit opinion. In part (i), a significant minority of candidates demonstrated that they are not clear on the difference between a modified report and a modified opinion which meant they scored fewer marks. In addition, many candidates failed to point out that the uncertainty surrounding going concern was fundamental to the users' understanding of the financial statements and did not score the mark available for this point. In part (ii), weaker candidates were not able to deal with the fact there were two potential options for the audit opinion depending on whether the absence of the disclosure was considered material or material and pervasive. Consequently, answers became muddled and difficult to follow resulting in fewer marks being awarded.	
Total possible marks Maximum full marks	8½ 6