

EXAMINER'S REPORT**LEVEL III EXAMINATION - JANUARY 2021****(303) FINANCIAL CONTROLS & AUDIT**

Financial Controls and Audit comprises of 9 compulsory questions.

Section A includes 4 questions of 5 marks each, **Section B** includes 3 questions of 10 marks each and **Section C** includes 2 questions of 25 marks each.

It was noted that most of the candidates have written answers to all 9 questions within the given time. The overall performance of the paper was satisfactory.

Section A**Question No. 01**

This question tested the knowledge on business environment. Further, this question required candidates to relate changes in external environment due to COVID-19 pandemic. Majority of the candidates were able to understand the requirements of the question and performed well.

It was suggested that candidates should have knowledge on following areas to give successful answer for these types of questions:

- Identification of business environment (Internal environment, External environment)
- Forces of External environment. (Economic, Legal, Technical, Social)
- Factors of environment forces (Eg. For Economic force - Exchange rates, Interests rates, Taxation)
- Knowledge on recent local and global topics.

Overall performance of this question was at satisfactory level.

Question No. 02

Part (a) of the question required candidates to explain the meaning of Risk avoidance. Some candidates were able to explain the meaning accurately. However, there were irrelevant answers, for examples there were students who have explained the audit risk and kept on explaining how to avoid audit risk.

Part (b) of the question required candidates to identify two strategies used for Risk reduction. A few students mentioned risk reduction strategies and scored full marks. However, some students provided irrelevant answers such as, following accounting standards, follow rules and regulations, and prepare financial statements.

Overall performance of this question was at average level.

Question No. 03

Part (a) of the question required candidates to state three key aspects and requirements when accepting and managing an assurance engagement. Few candidates were able to provide the correct answer for this question. Significant numbers of candidates have given incorrect answers such as checking last year audit report, company and management structure, composition of shareholding etc.

Part (b) of the question required to state two elements of an assurance engagement. There are five elements of an assurance engagement and study text clearly states the elements with detailed explanations. However performance of the candidates was poor and students have provided irrelevant answers such as professional judgment, code of ethics, reasonableness, etc.

Overall performance of this question was not at satisfactory level.

Question No. 04

Part (a) of the question was required to identify two policies that need to be considered in quality control of an individual audit engagement. It was observed that only a few numbers of students have provided correct answer. Further, Some students have provided irrelevant answers such as:

- Should follow ethics.
- Following professional standards.
- Legal and regulatory requirements.

Part (b) of the question was required to state three matters to be included in a system of quality controls with regard to integrity of a client. Some students have provided irrelevant answers such as Professional skepticism, Human resources, Monitoring etc.

Overall performance of this question was not at satisfactory level.

Section B

Question No. 05

Part (a) of the question tested the application of accounting principles, and how it affects to the audit Opinion based on the materiality. Most of the students were unable to understand the accounting errors given in the question hence were unable to explain the impact to the audit Opinion. Majority of students have answered that all errors to be adjusted according to the LKAS-16 Property Plant & Equipment, and LKAS-2 Inventory, without explaining the impact of individual accounting errors to the Audit Opinion, based on the given materiality level.

When answering this type question, students should state the impact of individual items based on materiality. Then they should state the overall impact as a whole considering materiality if it exceeds the materiality level it affects to the auditor's report when management refuses to adjust in the financial statements.

Part (b) of the question required to state three elements included in the Auditor's report other than auditor's opinion. It was observed that most of the students has provided correct answer for this question.

Overall performance of this question was at an average level.

Question No. 06

Part (A) of the question required to assess three matters need to be considered before taking a decision to accept the audit of a company. It was observed that the students who have studied the study text understood the content of the scenario and were able to provide the correct answer. However, there were some candidates who failed to apply the facts given in the question when answering.

Part (B) of the question required to state circumstances / relationships that can be recognized as possible threats to independence. It was observed that most of the students have misunderstood the question and failed to give the correct answer. Further, it was observed that significant numbers of the students have mixed up with the threat to the independence with the threat of compliance, principle of professional ethics.

Overall performance of this question was at average level.

Question No. 07

Part (A) (a) of the question required to explain weaknesses in the external confirmation process adopted by the auditor. Though the question itself provided information relevant to weaknesses in the negative confirmation, some candidates have failed to provide the correct answer for this question.

Part (A) (b) of the question required to state two actions auditor can perform when management refuse to allow the auditor to send confirmation requests. The majority was unable to understand the question, and provided with wrong answers such as check the last year audit working papers, obtain the assistance from expert, inquire from last year statutory auditor, and internal auditors, etc.

Part (B) of the question required the candidates to identify four inquiries an auditor should perform on subsequent events in an audit of financial statements. The auditor can make many types of inquiries regarding subsequent events and study text also explained number of inquiries. However,

some students were unable to identify relevant inquiries and provide general answers such as inquire regarding assets and liabilities, inquire regarding internal controls, etc.

Overall performance of this question was at satisfactory level.

Section C

Question No. 08

Question consisted of 2 parts, Part (A) consisted of 4 sub parts as (a), (b), (c) and (d) and Part (B) had 3 sub parts as (a), (b) and (c). Overall, the question tested the candidates' ability to understand the concepts Business processes, Internal controls, Control environment and IT controls based on the given case study.

Part (A)

- (a)** This part of the question required candidates to identify three internal control weaknesses in the company based on the information given in the scenario. The answer could have been obtained from the scenario, where all such weaknesses have been highlighted. Most of the candidates were able to provide the expected answer. However, there were some unrelated answers such as absence of accounting system, absence of inventory system, etc.
- (b)** This part required to explain the operational, finance, and compliance controls with related examples applicable to the company given in the scenario. Performance was at average level. Most of the candidates have not understood the question. Further, it was noted some of the candidates have repeated the answer given under part (a) above. Further, some students have explained relevant controls but unable to give relevant example applicable to **BIO**.
- (c)** This question required to list four key business processes applicable to the company given in the scenario. Most of the students were able to provide the relevant processes accurately. However, there were students who have given the irrelevant processes of the business, such as operation, management, IT, and risk management processes ignoring the processes such as procurement, cash management, invoicing, inventory management etc.
- (d)** This question required candidates to differentiate of IT General Control, and IT Application Controls. It was observed that some students were unable to differentiate between general, and application controls. Further, it was also observed that there were candidates who have given examples of General and Application controls without differentiating the General and Application controls.

Part (B)

- (a)** This question required candidates to discuss the validity of the statement made on internal controls system, and this statement contained the fact that a sound internal control system could eliminate the frauds, and errors. Most of the candidates have mentioned that the statement is incorrect, and provided inherent limitation of internal controls.

- (b) This question required candidates to explain the meaning of internal control. It was observed that many candidates were able to provide the expected answer. However, there few candidates, have explained other controls without understanding the subject matter, such as quality control in business, and audit, operational controls, financial controls, compliance controls, etc.
- (c) This question required the candidates to state two component of internal control System as per COSO. Most of the students have provided correct answer while few students have provided some irrelevant answers such as:
- Segregation of duties
 - Physical controls
 - Quality Controls
 - Ethical Requirements

Overall performance for this part of the question was at satisfactory level.

Question No. 09

Question consisted of 2 parts, **Part (A)** had 5 sub parts as **(a), (b), (c), (d)** and **(e)** and **Part (B)** had 2 sub parts as **(a)** and **(b)**.

Part (A)

- (a) This part tested the ability of the students to identify areas that need special attention based on the scenario given. Most of the students were unable to provide the answers in audit perspective and written the general answers. Further, some students have provided irrelevant answers such as:
- Use of last year engagement letter.
 - Performance of CEO/Recruitment of CEO.
 - Efficiency of production plant.
 - Completeness of records
- (b) This question tested the knowledge of candidates, on the condition for revision of letter of engagement. Most of the students have answered matters to be included in the engagement letter instead conditions that should be considered by the auditor to revise the terms of engagement letter. Further, some students have provided some irrelevant answers such as:
- Audit fee.
 - Responsibility of the engagement letter.
 - Address of the client.

- (c) This question tested the theoretical knowledge of the students on areas of professional judgement in planning, and performing an audit. It was observed that most of the students have mentioned areas identified from question which are totally irrelevant for the question. Ex: Bonus, Sales revenue, CEO performance.
- (d) This question tested the knowledge of students in explaining the term significant risk based on the given scenario. Many students have failed to identify key risk areas and highlighted overstatement of sales as a risk of fraud but failed to explain the significant risk, those requires special attention, and finally the risk of fraud is a factor that indicates a risk be significant.
- (e) This question tested the knowledge of the candidates in applying audit procedure for sales. It was observed that many students have mentioned the verification of debtor balances without paying much attention to the sales. Further, it was observed that many students have provided general audit procedures such as:
- Inquiry.
 - Inspection.
 - Re- calculation.
 - Observation.

Part (B)

- (a) This question tested the knowledge of the students pertaining to Financial Indicators that may cast significant doubt on the going concern of an entity. It was observed that many students have mentioned about operating, and other indicators such as shortage of import supplies, pending legal cases instead of financial indicators.
- (b) This question required to state the audit procedure to be performed by the auditor when events or conditions related to going concerns are identified. It was observed that few candidates were able to provide the correct answer while most of the candidates have provided answers such as Inquiry, Observation, Inspection, etc.

Overall performance for this part of the question was not at satisfactory level.

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Suggestions to enhance the Competency Level of Candidates in order to Improve the Performance at the Examination:

- (1) Candidates must study the study text and understand its contents.
- (2) Refer articles, magazines in relation to this subject and other reading materials related to auditing.
- (3) Understand the definition of action verbs and practice to answer the questions based on the action verb list given at the end of the question paper.
- (4) Study the contents of the past papers and practice at least last 2-3 years' examination papers and try to understand the way in which the questions are being set.
- (5) The candidates should understand the relationship between the theory given in the question papers and examiner's expectation of its application at the examination.
- (6) The candidates should study and understand as to what areas in the study text have been tested in the past question paper and make short notes of those areas in the study text.
- (7) The candidates should work out the past paper questions on timely basis before the examination, it will improve the time management at the examination.
- (8) Write short notes of each study chapter given in the study text and study as and when you get free time to remember the contents of syllabus.
- (9) Candidates should write legible hand writing at the examination.
- (10) The candidates should carefully read the instructions given in the examination paper prior to start answering the questions in the paper.
- (11) The candidates should have a clear and balance mind set at the examination in order to understand the question and provide with appropriate and accurate answers required in the question.
- (12) The candidates should allocate the time for the questions based on the marks given and accordingly, the candidate should be able to answer all the questions given in the paper effectively.
- (13) Check twice whether all required questions were answered and appropriately numbered prior to hand over the answer scripts.