



Hong Kong Institute of  
**Accredited Accounting Technicians**  
香港財務會計協會

# **Professional Bridging Examination**

## **December 2010 Session**

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### **Paper III PBE Auditing and Information Systems**

### **Questions & Answers Booklet**

The suggested answers are longer than what candidates are expected to give in the examination. The purpose of the suggested answers is meant to help candidates in their revision and learning. The suggested answers may not contain all the correct points and candidates should note that credit will be awarded for valid answers which may not be fully covered in the suggested answers.

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Published by Hong Kong Institute of Accredited Accounting Technicians Limited  
27/F, Wu Chung House, 213 Queen's Road East, Wanchai, Hong Kong

March 2011



Hong Kong Institute of  
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香港財務會計協會

# Professional Bridging Examination

## Paper III PBE Auditing and Information Systems

### December 2010 Session (Questions)

Time Allowed	3 hours
Examination Assessment Allocation	
• Section A – The One question is compulsory	40 Marks
• Section B – Answer 3 out of 4 questions	60 Marks

### PAPER III – PBE AUDITING AND INFORMATION SYSTEMS

This examination is divided into TWO sections.

- Section A (40%). This consists of ONE compulsory question. You should allocate approximately 1 hour 12 minutes in total for Section A.
- Section B (60%). This consists of four questions, of which you must answer THREE questions only. Each of these three questions is worth 20% of the total marks (making Section B worth 60% of the total marks). You should allocate approximately 36 minutes for each question (that is, 1 hour 48 minutes in total for Section B).

Suggested Time Allocation (by marks):

Marks	Approximate time (minutes)
1	2
2	3
3	5
4	7
5	9
6	11
7	12
8	14
9	16
10	18
11	20
12	21
13	23
14	25
15	27
16	29
17	30
18	32
19	34
20	36

## **SECTION A (COMPULSORY)** (Total: 40 marks)

Answer **ALL** questions in this section. Marks are indicated at the end of each question. Together they are worth 40% of the total marks for this examination.

### **CASE**

Daily Care Limited (DCL) is an online retailer of daily care products and cosmetics, such as skin care products, shampoo, shower foam, and cosmetic products. The company has a fixed mark up for different lines of products. There are 8 employees working in the company with fixed monthly salaries. Goods are sold to local customers only. Consumers select the category of products from a pull-down menu on DCL's Web-site. A variety of products are available for each category. For each listed product sold online, the Web-site provides a product description, picture, and price. The information is maintained in an inventory master file under a perpetual inventory system. Customers click on the product number of the items they wish to purchase. The following are control procedures DCL has established for its online sales:

1. All products shown on the Web-site can be purchased online if the inventory quantity is greater than zero. The online sales system is linked to the perpetual inventory system. The quantity of goods available for sale will be automatically updated when goods are purchased online by customers.
2. Before payment, the online screen shows the product name, description, unit price, and total sales price for the online transaction. Customers must click on the Accept or Reject Sales buttons to indicate approval or rejection of the online sale.
3. All transactions must be settled by credit card payment. DCL obtains credit card authorisation codes electronically from the credit card agency.
4. Once customers finalised the online sale procedures, the online sales system generates a Pending Sales file, which is an online data file that is used by a clerk to process delivery. A clerk is responsible for issuing the delivery notes to the warehouse for arranging the delivery of goods. The warehouse is operated by an unrelated third party. Online sales are not recorded in the sales journal until delivery note copies signed by customers are received from the warehouse personnel. The clerk will then enter the delivery note number and date of delivery into the Pending Sales data file.

Before the year ended on 31 December 2009, the company purchased a lot of products from a manufacturer at exceptionally low prices as the manufacturer closed down its business. The company has never bought any products from this manufacturer before. Some of these products were sold in December 2009. In January 2010, about half of the customers reported that they have skin problems after using these products. The company immediately stopped selling these products to customers.

**Required:**

**Question 1** (40 marks – approximately 72 minutes)

- (a) The understanding of the nature of the entity and the entity's selection and application of accounting policies enables the auditors to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.

What are the key matters of DCL's operations that are relevant to the auditor?  
(7 marks)

- (b) For control procedure 4 in the Case, identify the assertion(s) for the relevant classes of events and transactions being fulfilled if the control is in effect. Describe any potential misstatements that could occur if the control was not present.

(5 marks)

- (c) Suggest the control activities that should be present to ensure that the prices of the products included in the inventory master files are correct.

(3 marks)

- (d) Describe how audit software would assist the auditor in the audit of the sales transactions for DCL, assuming all of the information above is available to the auditor in a suitable format for the auditor to conduct audit testing using audit software.

(5 marks)

- (e) Auditors have to adopt CAAT to audit a client's computerised system because of the invisibility of the transactions trail and data in a computerised system. Explain the causes of invisibility of transactions trail and data in a computerised system.

(3 marks)

- (f) What are the procedures to control test data applications?

(2 marks)

- (g) What are the audit procedures that should be carried out for the inventory held by the third party warehouse? How does the materiality of the item affect your choices of audit procedures?

(5 marks)

- (h) Regarding the incidence of skin problems happening to customers after using the company's products, what procedures should the auditor perform in order to become aware of such incidents?

(6 marks)

- (i) Assuming you are the manager in charge of this audit. What is your assessment of the risk of material misstatement of the completeness of provision for liabilities?

(4 marks)

\* \* \* END OF SECTION A \* \* \*

**SECTION B (ANSWER THREE QUESTIONS ONLY) (Total: 60 marks)**

*Answer any **THREE** questions in this section. Each question carries 20 marks. Together they are worth 60% of the total marks for this examination.*

**Question 2 (20 marks – approximately 36 minutes)**

You are an audit manager of ABC & Co. You are responsible for the audits of several clients of ABC & Co. ABC & Co has focused their attention in conducting cost-effective audits by having adequate planning for every audit.

In the audit of year-end accounts receivable for Peter Limited, you ascertained that there are 3,200 active customer accounts. Of these, 200 accounts are \$50,000 and above and 3,000 are below \$50,000, including 180 accounts with zero balances and 20 accounts with negative balances. You intend to use stratified sampling and monetary unit sampling for the selection of 40 customer accounts for positive customer account confirmation purposes. You wish to have coverage of a large proportion of accounts receivable in terms of dollar values. You also wish to have a reasonable spread of other accounts.

In the audit of the sales transaction cycle for Stella Limited, you intend to test the postings of a sample of 20 credit notes to customer accounts. You ascertained that all credit notes used in the period are pre-numbered and the first credit note used in the period is numbered CN2701, while the last one is numbered CN3980. There were no credit note cancellations in the period. You intend to use interval sampling with random start as the basis for the sample selection.

**Required:**

- (a) Discuss the benefits of audit planning. (6 marks)
- (b) What is sampling risk? Explain sampling risk in both test of controls and substantive tests contexts. (3 marks)
- (c) What is the objective of stratification? Discuss how stratified sampling and monetary unit sampling can be used for the selection of the accounts receivable of Peter Limited for customer confirmation. (7 marks)
- (d) Provide two advantages of monetary unit sampling. (2 marks)
- (e) To test the postings of Stella Limited, and assuming that CN 2703 is the first sample item, list the sample of credit notes with credit note numbers smaller than CN 3000 that will be selected. (2 marks)

**Question 3 (20 marks – approximately 36 minutes)**

You have recently joined an audit firm as a trainee and attended an in-house auditing training programme. You have learnt that audit risk and materiality are two important factors in determining the amount of audit work performed by auditors in conducting audits of financial statements. You have also learnt that auditors should obtain sufficient appropriate evidence to support their audit opinion and that all work carried out by auditors should be properly documented.

Currently, you are involved in an audit engagement, the client's principal activities are the wholesaling and retailing of computers and accessories as well as various digital products. You are responsible for auditing the inventory section.

You found that there is an agreement signed by the client with a third party just after the year end date. A huge number of products were sold at a price lower than the total cost. The gross loss of all these products amounted to \$500,000. The management said that the goods were sold after the financial year end, therefore, no adjustment on the inventory value is required. Also, the total assets of the company are \$80 million and the profit before tax is \$1 million. Compared with the total assets, the amount of \$500,000 is clearly immaterial. The management will not consider any write down of the inventories.

**Required:**

- (a) The audit manager assessed the inherent risk in respect of the existence and valuation assertions of the inventory balance are not low. Please suggest the reasons for his assessments. (2 marks)
- (b) According to the audit risk model, both the inherent risk and control risk should be considered for determining the nature of further audit procedures and the audit approach. For the inherent risk discussed in part (a), what control activities do you expect to exist to lower the risks of material misstatement at the assertion level? (4 marks)
- (c) Evaluate the management's argument that the amount of \$500,000 is immaterial. (4 marks)
- (d) If the auditor disagrees with the management's argument and considers that the inventory value is overstated by \$500,000, what are the key elements that would be included in the opinion section of the auditor's report? (4 marks)
- (e) According to HKSA230 (Clarified), the auditor should prepare, on a timely basis, audit documentation that provides:
- A sufficient and appropriate record of the basis for the auditor's report; and
  - Evidence that the audit was planned and performed in accordance with HKSAs and applicable legal and regulatory requirements.

What are the purposes of preparing audit working papers?

(6 marks)



**Question 4** (20 marks – approximately 36 minutes)

HY Limited owns several (less than 10) expensive residential properties in Hong Kong and Mainland China, all are used for earning rental income. This is the major operating activity of HY Limited. The company is owned by six shareholders who engage two directors to operate the business. The directors plan to acquire more and more properties in the future, therefore, a lot of resources are allocated to set up a good internal control system for the collection of rental income.

**Required:**

- (a) Assess with reasons the inherent risk of material misstatement of the existence of HY Limited's investment properties.

(2 marks)

- (b) Assuming that the substantive approach is adopted, list four audit procedures that should be performed in addressing the existence assertion of investment properties.

(4 marks)

- (c) The company adopts the Fair Value Model for the accounting of the investment properties. The auditor has decided to use an expert's services regarding the fair value of the investment properties.

What matters should be agreed between the auditors and the auditor's expert?

(6 marks)

- (d) Assuming the substantive approach is adopted, what are the audit procedures to be performed for the rental income?

(6 marks)

- (e) Assuming the company maintained good internal control for the collection of rental income, is it appropriate for the auditor to adopt the substantive approach for the audit of rental income?

(2 marks)

**Question 5 (20 marks – approximately 36 minutes)**

ABC & Co carries out manufacturing and trading business in paper and metal products in Hong Kong and Mainland China. The company is undergoing a fast expansion plan. The number of salespersons will increase from 20 to 100 in three years time. The information system of an organisation affects the organisation's competitive advantage in the market and determines organisational performance and success.

**Required:**

- (a) Information is a key resource for an organisation and can serve an organisation's information needs in developing corporate strategy. What are the six stages of development of corporate strategy?  
(6 marks)
- (b) Information can serve the information needs of managers of different levels in their decision making. What are the four stages of the decision making process?  
(4 marks)
- (c) What are the information needs of managers for the following functions?  
(i) Accounting  
(ii) Production  
(6 marks)
- (d) Porter's value chain model is one of the tools that can assist identifying the information needs of different activities and functions of a company. An organisation's value chain consists of primary activities and four supporting activities. The primary activities include inbound logistics and outbound logistics. What are inbound logistics and outbound logistics?  
(4 marks)

\* \* \* END OF EXAMINATION PAPER \* \* \*

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# Answers

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Paper III  
PBE Auditing and  
Information Systems  
(December 2010 Session)

**SECTION A (COMPULSORY) (Total: 40 marks)**

**Answer 1(a)**

The key matters of Daily Care Limited's business operations are as follows:

- (i) nature of revenue resource – the company is a retailing company which provides daily care products to local customers through its website
- (ii) key customers – the company has a large number of customer accounts
- (iii) products or services and markets – the company has a rather high volume of transactions from the selling of daily care products with expiry dates and it is facing keen competition as many companies are selling daily care products everywhere in Hong Kong, obsolescence of products
- (iv) conduct of operation – the company sells products to customers through its website / on-line
- (v) alliances, joint ventures, and outsourcing activities – the warehouse and delivery function are outsourced
- (vi) employment – there are approximately 8 staff in the company, the monthly salaries are fixed
- (vii) research and development activities and expenditures – the company may need to further develop its website to cope with the fast changing technology, search for new products and carry out promotion activities. A computer expert team may be maintained within the organisation
- (viii) no debtors, except receivables from credit card issuing banks
- (ix) web trust certification
- (x) sales returns handling

**Answer 1(b)**

The two assertions are:

- occurrence – transactions recorded in the ledger represent events that have occurred
- cutoff assertions- transactions and events have been recorded in the correct accounting period

Without such control, there may be overstatement of sales for the goods recorded but not delivered.

### Answer 1(c)

Control activities include:

- authorisation of the price list by management.
- segregation of duties, input of price to the master file by a designated member of staff and the price inputted should be checked by senior staff
- performance review, gross profit margin by product analysis report should be generated and reviewed by management on a regular basis

### Answer 1(d)

The audit software can help the auditor to perform the following functions:

- reads and extracts data from client's computer system for further audit procedures
- selects transactions from client's data file which meet the criteria set by the auditor
- performs arithmetic calculations on selected transactions, files and databases
- performs statistical analysis to support various types of audit sampling
- generates various types of reports designed by the auditors
- verifies extensions and footings of the client's computations by calculating the information independently
- examines records for completeness, consistency and correctness by scanning all records using specified criteria and then prints out exception reports, e.g. missing delivery notes
- compares data on separate files to ensure consistency of information
- compares data obtained through other audit procedures with company records
- selects audit samples from any machine readable data in several ways, including at random
- prints the confirmation request forms by applying the information of the master files, e.g. print supplier name, address and account balance

### Answer 1(e)

Due to the invisibility of a data and transaction trail, auditors may not be able to perform substantive tests alone for the sales and receipts cycle. Data in computerised systems lead to the use of CAATs.

The causes of the invisibility of a data and transaction trail are as follows:

- some transactions are initiated by a computer program, for example, transactions with automated initiation and authorisation were processed with no visible evidence
- internal controls are implemented within a computer system without visible evidence
- source documents are often eliminated for a computer-based system, audit evidence is maintained in machine-readable form
- most of the underlying data in a computerised environment are stored in centralised electronic files
- a computerised information system retrieves data from various sources and processes various transactions simultaneously, transactions are complicated by the summarisation of the related details

#### **Answer 1(f)**

Audit procedures to control test data applications may include:

- controlling the sequence of submissions of test data where it spans several processing cycles
- performing test runs containing small amounts of test data before submitting the main audit test data
- predicting the results of the test data and comparing them with the actual test data output, for the individual transactions and in total
- confirming that the current version of the program was used to process the test data
- testing whether the programs used to process the test data were the programs the entity used throughout the applicable audit period

#### **Answer 1(g)**

When inventory is under the custody and control of a third party, the auditor would ordinarily obtain direct confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity.

Depending on materiality of this inventory the auditor would also consider the following:

- the integrity and independence of the third party
- observing, or arranging for another auditor to observe, the physical inventory count
- obtaining another auditor's report on the adequacy of the third party's internal control for ensuring that inventory is correctly counted and adequately safeguarded

- inspecting documentation regarding inventory held by third parties, for example, warehouse receipts, or obtaining confirmation from other parties when such inventory has been pledged as collateral

#### **Answer 1(h)**

The auditor should carry out audit procedures in order to become aware of any litigation and claims involving the entity which may result in a material misstatement of the financial statements. Such procedures would include the following:

- make appropriate inquiries of management including obtaining representations
- make appropriate review of the minutes of those charged with governance and correspondence with the entity's legal counsel
- review customers' complaints file
- review sales returns after balance sheet date
- direct confirmation from the company lawyer
- examine legal expense accounts
- use any information obtained regarding the entity's business including information obtained from discussions with any in-house legal department. The entity may not have a legal department as the size of the entity is small in this case

#### **Answer 1(i)**

Risk of material misstatement of the provision for liabilities at assertion level for completeness is medium to high. The customers may have sued the company for compensation. The company may need to make provision for liabilities or disclose the contingent liabilities in the financial statements.

Students may raise the going concern issue, but detail justification is required.

\* \* \* END OF SECTION A \* \* \*

**SECTION B (ANSWER THREE QUESTIONS ONLY)** (Total: 60 marks)

**Answer 2(a)**

According to HKSA300 (Clarified), adequate planning benefits the audit of financial statements in several ways, including the following:

- helping the auditor to devote appropriate attention to important areas of the audit
- helping the auditor to identify and resolve potential problems on a timely basis
- helping the auditor to properly organise and manage the audit engagement so that it is performed in an effective and efficient manner
- assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them
- facilitating the direction and supervision of engagement team members and the review of their work
- assisting, where applicable, in the coordination of work done by auditors of components and experts

**Answer 2(b)**

Sampling risk – The risk that the auditor's conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions:

- (i) in the case of a test of controls, that controls are more effective than they actually are, or in the case of a test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion.
- (ii) in the case of a test of controls, that controls are less effective than they actually are, or in the case of a test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect.

**Answer 2(c)**

Audit efficiency may be improved if the auditor stratifies a population by dividing it into discrete sub-populations which have an identifying characteristic. The objective of stratification is to reduce the variability of items within each stratum and therefore allows sample size to be reduced without increasing sampling risk.



In this case, the population of accounts receivable can be stratified by monetary value into four sub-populations. They can be stratified as follows:

- Group 1 - accounts with balance of \$50,000 and above
- Group 2 - accounts with balance below \$50,000 and above zero
- Group 3 - accounts with zero balance
- Group 4 - accounts with negative balance

This allows greater audit effort to be directed to the larger value items, as these items may contain the greatest potential misstatement in terms of overstatement.

For Group 1 & 2, monetary unit sampling can be applied to select particular items, for example, individual balances, that contain those monetary units.

#### **Answer 2(d)**

Advantages of monetary unit sampling are as follows:

- audit effort is directed to the larger value items because they have a greater chance of selection
- smaller sample sizes

#### **Answer 2(e)**

The sample items are CN2767, CN2831, CN2895, CN2959.

#### **Answer 3(a)**

The inherent risk in respect of the existence assertion of the inventories balance is not low as the computers and accessories and digital products are high value, small size items and therefore easily subject to misappropriation.

The inherent risk in respect of the valuation assertion of the inventories balance is not low as the industry is fast changing. The selling prices of products drop significantly once the products become obsolete.

#### **Answer 3(b)**

The company should maintain good physical control of the inventories. Also, segregation of duties should be maintained between the staff who are responsible for the physical inventories keeping and the staff who keep the inventories record.

The company should maintain a perpetual inventory system and a physical count should be conducted periodically to see whether there are any discrepancies and management should carry out follow up actions accordingly.

The company should maintain a perpetual inventory system. As slow moving items report should be generated periodically so that the management can carry out an appropriate selling strategy on time to reduce the chance of keeping obsolete inventories.

Sales analysis by items report should be generated by the sales system and inventories movement and outstanding reports should be generated by the inventory system. The management should carry out a performance review frequently to evaluate past performance and plan for the future trading strategy. The management has to determine the amount of inventories written off/down based on the available information.

### **Answer 3(c)**

To determine whether the amount is material or not, we need to consider whether its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements.

For the misstatement of inventory, which should be stated at lower of cost or net realisable value, we have to consider its effect on the misstatement of the statement of financial position as well as the income statement. The effect on the income statement is material. The income before tax of \$500,000 is misstated as \$1,000,000. The gross profit margin is misstated as well. Such misstatement could influence the economic decisions of users.

### **Answer 3(d)**

The qualified opinion should be expressed as being "except for" the effect of the overstatement of the inventory value to which the qualification relates.

A clear description of all substantial reasons giving rise to the disagreement and a quantification of the possible effects on the financial statements.

### **Answer 3(e)**

In addition to the mentioned objectives, audit documentation serves a number of purposes, including:

- assisting the audit team to plan and perform the audit
- assisting members of the audit team responsible for supervision to direct and supervise the audit work, and to discharge their review responsibilities
- enabling the audit team to be accountable for its work
- retaining a record of matters of continuing significance to future audits
- enabling the conduct of quality control reviews and inspections
- enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements

#### **Answer 4(a)**

The inherent risk of material misstatement of the existence of HY Limited's investment property should be low to medium.

The reasons are as follows:

- there is no indication of fraud
- investment property is not subject to misappropriation
- physical movements are usually rare as the major business is the leasing of the investment properties

#### **Answer 4(b)**

The audit procedures for the existence of investment properties are as follows:

- substantive analytical procedures, such as comparing this year's account balance with last year's account balance by taking into account the amount of rental income for both periods
- review minutes to identify purchase or disposal of properties and inspection of sale and purchase agreements
- inspection of title deeds
- physical inspection of the properties
- land search

#### **Answer 4(c)**

The auditor shall agree, in writing when appropriate, on the following matters with the auditor's expert:

- the nature, scope and objectives of that expert's work
- the respective roles and responsibilities of the auditor and that expert
- the nature, timing and extent of communication between the auditor and that expert, including the form of any report to be provided by that expert
- the need for the auditor's expert to observe confidentiality requirements

#### **Answer 4(d)**

The audit procedures of rental income are as follows:

- obtain the list of rental income
- agree the amount of the rental income list to the trial balance and general ledger
- check the calculation and casting of the list of rental income
- check the monthly income against the rental agreement
- for vacancy periods, confirm with the management and seek written representation if necessary
- perform analytical procedures, compare this year's rental income with last year's rental income by taking into account the additions and disposals of investment properties in the two years
- test check the cash receipts with the bank statements
- for early termination of rental agreement, obtain the termination agreement

#### **Answer 4(e)**

Even though there is good internal control system, it is still appropriate for the auditor to adopt the substantive approach as this is the most cost effective way of performing the audit work on rental income since the number of transactions is small.

#### **Answer 5(a)**

The six stages in the development of a corporate strategy are as follows:

Establish the mission based on the culture and developments in an organisation's environment.

Perform background situation analysis, based on results of past activities to evaluate different alternatives.

Set measurement objectives for the company's financial standards and requirements.

Develop strategies for achieving the objectives.

Develop tactics based on the direction of the strategies.

Develop operational plans for managers of different function areas.

#### **Answer 5(b)**

The four stages of the decision making process are as follows:

The trigger stage – which is an event or a piece of information that precipitates the need for a decision. The earlier the identification of the need for a decision driven by new information, the more timely the decision.

Information gathering stage – collecting information for decision making. The more timely the collection of information, the more timely the decision.

Design stage – the decision maker will consider a range of different courses of action and predict their likely results.

Evaluation stage – the manager will choose from among the possible courses of action.

#### **Answer 5(c)**

The accounting managers need to collect information such as sales, purchases, salaries and other transactions of the business. They need information for preparing financial statements for internal and external users. In addition, they need information to prepare regular, forward looking, flexible and non-routine reporting for managers of different levels.

Production managers require information for the production budget, production scheduling, product development and controlling the flow of products in order to ensure that resources are properly controlled and allocated during the production process. Examples of information needs, such as expected sales, materials and overheads required for producing finished goods, price and usage and variance of material, labor and overheads for production cost drivers, essential production activities, etc.

#### **Answer 5(d)**

In-bound logistics involve activities associated with receiving, storing and disseminating inputs to create products and services.

Outbound logistics are those activities associated with storing and distributing the products or services.

\* \* \* END OF EXAMINATION PAPER \* \* \*



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# Examination Panelist's Report

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Paper III  
PBE Auditing and  
Information Systems  
(December 2010 Session)

*(The main purpose of the following report is to summarise candidates' common weaknesses and make recommendations to help future candidates improve their performance in the examination.)*

### **General Comments**

The performance was not satisfactory as quite a number of candidates did not master the fundamental concepts of auditing such as different types of audit reports, purposes of audit planning, procedures for identifying subsequent events, usage of the audit software as a tool for auditing, application of audit sampling, and application of substantive procedures for different classes of transactions and account balances.

Many candidates failed to apply their knowledge to real-life issues in order to demonstrate the expected level of analytical thinking. In particular, they did not read the questions carefully.

Quite a number of candidates wrote illegibly and made spelling and grammatical mistakes. Illegible handwriting and poor English inevitably affected the assessment.

### **Specific Comments**

#### **Section A – Compulsory Questions**

##### **Question 1 – 40 marks**

This was a case of a practical scenario. Candidates were asked to apply their knowledge to practical auditing and information system issues. Most candidates were not able to link up their knowledge of information systems and auditing which required analytical thinking.

Part (a), many candidates did not read the requirements carefully; they copied the details of the information system for operation from the case instead of highlighting the specific matters of DCL's operation for the understanding of the business. Part (b), most candidates were not able to distinguish the differences between assertions for classes of transactions. Part (c), most candidates provided substantive procedures to be performed by auditors instead of control activities carried out by the client. Parts (d), (e) and (f), most candidates did not have a good understanding of the possible usages of audit software and the application of CAAT. Part (g), most of the candidates who attempted this part scored satisfactorily. However, a few candidates only provided general audit procedures for attending an inventory count. Part (h), quite a lot of candidates did not mention the procedures for identifying subsequent events but provided specific audit procedures to be carried out after identifying the event mentioned in the case. Part (i), most of the candidates who attempted this part scored satisfactorily. However, a few candidates were not able to justify their risk assessment.



## **Section B – Optional Questions**

### **Question 2 – 20 marks**

This question examined candidates' understanding of the purposes of audit planning and application of audit sampling.

Part (a), most candidates who attempted this part scored satisfactorily, but quite a number of candidates did not know the purposes or were not able to express their understanding in good English. Part (b), most candidates who attempted this part scored satisfactorily. Parts (c) and (d), most candidates did not have a basic understanding of stratified sampling and monetary unit sampling. Part (e), some candidates who attempted this part scored satisfactorily, but quite a lot candidates did not know how to apply interval sampling.

### **Question 3 – 20 marks**

This question examined candidates' knowledge of risk assessment, control activities, the concept of materiality, differences between different types of audit report and purposes of preparing audit working paper.

Part (a), some candidates who attempted this part scored satisfactorily, however, some candidates did not have a good understanding of inherent risk and therefore provided irrelevant answers. Part (b), many candidates mixed up control activities and substantive procedures. Part (c), most candidates who attempted this part scored satisfactorily. Part (d), some of the candidates who attempted this part scored satisfactorily, but some candidates were not able to distinguish between different types of audit opinion. Also, many candidates were not able to detail the key elements that would be included in the opinion section of the auditor's report. Part (e), most candidates who attempted this part scored satisfactorily, but quite a number of candidates did not know the purposes of preparing working papers and therefore provided irrelevant answers.

### **Question 4 – 20 marks**

This question examined candidates' knowledge of auditing an investment properties holding company.

Part (a), some candidates who attempted this part scored satisfactorily, however, many candidates did not have a good understanding of inherent risk and therefore provided irrelevant answers. Part (b), most candidates who attempted this part scored satisfactorily, but quite a number of candidates did not know the differences between the assertions and therefore only provided substantive procedures for addressing other assertions instead of the existence assertion. Part (c), a few candidates who attempted this part scored satisfactorily, most candidates could not provide relevant answers for this part. Part (d), most candidates who attempted this part scored satisfactorily, but quite a number of candidates only provided substantive procedures for auditing sales revenue instead of substantive procedures for auditing rental income.

Question 5 – 20 marks

This question examined candidates' knowledge of the corporate strategy for the development of a business and the information needs of the management for decision making.

Most candidates who attempted this question performed satisfactorily in Parts (c) and (d). The performance of the candidates for 5(a) and (b) was varied, some candidates did very well in these parts but some discussed information system development instead of the six stages of development of corporate strategy and the four stages of decision making.

\* \* \* END OF EXAMINATION PANELIST'S REPORT \* \* \*