

Faizal Ali - 25 June 2018

ACCA/BICA Practice Monitoring Reviews – Overview of Findings

AGENDA

1. Practice monitoring programme
2. The audit monitoring process
3. Assessing the outcome of an audit file examination
4. Assessing overall outcome of a monitoring visit
5. Underlying causes of unsatisfactory outcomes

AGENDA

6. Common breaches of the IESBA Code of Ethics
7. Common deficiencies on ISQC 1 compliance
8. Common deficiencies found in audit work
9. Action plans
10. How firms should prepare for an audit monitoring visit

ACCA/BICA Practice Monitoring Reviews – Overview of Findings

PRACTICE MONITORING PROGRAMME

PRACTICE MONITORING PROGRAMME

- Audit monitoring visits undertaken by ACCA on behalf of BICA and started in January 2016
- Primary purpose – to verify compliance with International Standard on Quality Control No. 1 (ISQC 1), International Standards on Auditing (ISAs) and the IESBA Code of Ethics
- Firms with PIE audits are monitored on a three year cycle while the rest continue to be monitored on a six year cycle
- All firms including part-time practitioners, with at least one audit client are subjected to monitoring

PRACTICE MONITORING PROGRAMME

- Early follow-up visits are carried out to firms with unsatisfactory outcomes after two years (one year for firms with PIE audits) or four years (two years for firms with PIE audits), depending on severity of non-compliance with ISAs
- Monitoring visits have been carried out to about two thirds of the firms – The remaining third with only a very few non-PIE audit clients will be monitored over the next two years
- All visits undertaken to date are first visits
- Early follow-up visits to firms with unsatisfactory outcomes at first visits in 2016 to commence soon

ACCA/BICA Practice Monitoring Reviews – Overview of Findings

THE AUDIT MONITORING PROCESS

THE AUDIT MONITORING PROCESS

- Arranging the visit:
 - Firm contacted by telephone
 - Requested to complete PVQ and audit clients discussed
 - Date of visit agreed and confirmed in writing
- Undertaking the visit
 - Opening meeting - background /quality controls procedures
 - Examination of audit files
 - Closing meeting - discuss and agree the findings and overall outcome and provide guidance on improvements



THE AUDIT MONITORING PROCESS

- Post-visit procedures
 - Report on visiting findings, conclusion and guidance drafted
 - Internal quality control of review of report/visit papers
 - Report, and action plan template sent to the firm with unsatisfactory outcomes
 - Firm's response including action plan reviewed for adequacy
 - Report and firm's response /action plan sent to BICA with comments
- The audit monitoring report
 - The report concentrates on areas on weakness rather than strength
 - Gives recommendations for future action



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION

ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION

- Based on whether the audit opinion is adequately supported by sufficient appropriate audit evidence obtained and recorded in the audit files
- Not expecting to see perfect audit files
- Number of deficiencies does not necessarily determine whether audit is unsatisfactory
- Key concept is “reasonable assurance” that financial statements are free from material misstatement (ISA 200.5)
- The “test” is whether there is a significant risk that the financial statements could contain an undetected material misstatement as a result of the deficiencies found in the audit work
- An audit file may only have one deficiency and be considered unsatisfactory if significant in a key area

ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION - EXAMPLE 1

- Inventories are material
- No continuous inventory system and auditor does not attend client's physical inventory count
- No alternative procedures to obtain reasonable assurance that stock count was undertaken reliably and results were recorded accurately
- No other serious deficiencies noted on file and clean report issued
- Failure to verify inventory could mean a material misstatement remains undetected
- Conclusion: Unsatisfactory audit

ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION - EXAMPLE 2

- Inventories form a substantial part of the assets
- Auditor attends physical inventory count but is unable to verify quantities
- Audit report qualified “except for” valuation of stock and related cost of sales
- No consideration of whether the limitation on scope is so material and pervasive that the auditor is unable to express an opinion (ISA 701)
- Conclusion: Unsatisfactory audit



ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION EXAMPLE 3

- Audit client is a large manufacturing company
- Value of plant and machinery represented a significant proportion of the net assets of the company
- Large proportion of the value of plant and machinery related to a few items of machinery
- Auditor did not verify the existence and condition by physical inspection

ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION EXAMPLE 3

- Outcome may be considered unsatisfactory
- However:
- Auditor may have considered that the continuance of the manufacturing company's trade provided adequate indication of existence and condition of key pieces of machinery. If auditor has recorded these alternative procedures, including its going concern review, outcome may be considered satisfactory.



ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION EXAMPLE 4

- Indicators of financial difficulty and cash flow problems
- Auditing standard on going concern (ISA 570) not followed
- Conclusion: Unsatisfactory audit



ASSESSING THE OUTCOME OF AN AUDIT FILE EXAMINATION EXAMPLE 5

- No indication of financial difficulty and profit and surplus cash generated
- Auditing standard on going concern (ISA 570) not followed
- Conclusion: Deficiency, but not sufficiently serious to render outcome unsatisfactory



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

ASSESSING OVERALL OUTCOME OF A MONITORING VISIT

ASSESSING THE OVERALL OUTCOME OF A MONITORING VISIT

- Outcome satisfactory if all audit files examined are satisfactory
- Outcome satisfactory if half or more audit files examined are satisfactory subject to the following two conditions:
 - None of the unsatisfactory audit files are seriously deficient with little evidence of audit work; and/or
 - None of the unsatisfactory audit files are in respect of public interest entities or large clients of the firm
- Outcome unsatisfactory if serious ethical breaches found even if outcome of audit file examinations is satisfactory



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

UNDERLYING CAUSES OF UNSATISFACTORY OUTCOMES

UNDERLYING CAUSES OF UNSATISFACTORY OUTCOMES

- Serious breaches of the IESBA Code of Ethics
- Little awareness of requirements of auditing standards
- Lack of understanding of:
 - Approach to audit
 - How to plan the audit
 - How to identify audit objectives
 - How to develop or tailor proprietary audit programmes
 - How to execute audit procedures and document the audit work
 - How to supervise, control and review the audit
- Lack of documentation - audit tests, results and conclusion



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

COMMON BREACHES OF THE IESBA CODE OF ETHICS



COMMON BREACHES OF THE IESBA CODE OF ETHICS

Significant breaches

- Undue financial dependence on audit clients
- Immediate or close relationship with audit clients
- Long association with PIE audit clients

Less significant breaches

- Long association with non-PIE audit clients
- Providing book-keeping and accounting services to non-PIE audit clients



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE



COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE

OVERVIEW OF ISQC 1

- Applies to firms which perform assurance engagements such as audits
- Requires audit firms to document and implement firm-wide policies and procedures to ensure compliance with ISAs
- Covers leadership, ethics, acceptance and continuance, human resources, engagement performance, and monitoring

COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE

1. Leadership responsibilities
 - Policies and procedures not documented
 - No staff training
 - Staff not confirming have read and understood

2. Ethical requirements
 - Independence declarations not obtained
 - Undue financial dependence on audit clients
 - Long association with audit clients
 - No rotation policy – partners and senior personnel
 - Register of identified threats and safeguards not kept
 - Audit clients from unqualified accountants – little or no control over audit

COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE

3. Client acceptance and continuance
 - No formal procedures or inadequate procedures
 - No evidence of client identification and due diligence
 - Professional clearance not obtained
 - Engagement letters issued before above procedures completed

4. Human resources
 - References for new staff not obtained
 - Fit and proper and confidentiality declarations not obtained
 - No job descriptions
 - Staff appraisals informal or not done
 - Insufficient training and record keeping

COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE

5. Engagement performance

- Audit methodology non-existent or ineffective
- Lack of partner involvement in planning
- Lack of supervision, control and review
- Lack of policy on ECQR review (“hot” review)
- No formal consultation procedures
- No policy on file assembly, archiving and accessibility
- No policy on file destruction

6. Monitoring

- Periodic review of policies and procedures not done
- Periodic review of completed engagements not done
- No written policy to deal with complaints

COMMON DEFICIENCIES ON ISQC 1 COMPLIANCE

CORRECTING DEFICIENCIES IN ISQC 1 COMPLIANCE

- Familiarise with the requirements in the standard
- Review existing policies and procedures and amend as necessary with reference to ISQC 1
- Document amended policies and procedures by tailoring guidance provided by ACCA or using other sources, such as IFAC (ISQC 1 manual)
- Ensure staff read the firm's ISQC 1 manual and confirm in writing that they have done so
- Implement the policies and procedures adopted by the firm



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

COMMON DEFICIENCIES FOUND IN AUDIT WORK

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Planning

- Terms of engagement (ISA 210)
 - engagement letter not issued to client
 - signed engagement letter not obtained
 - engagement letter does not address all the matters required by ISA 210
- Understanding of the client business not documented (ISA 315)
 - business activities, the industry, key suppliers and customers, accounting systems and internal controls, related parties and key management, key personnel etc.

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Planning (continued)

- No risk assessment - Identifying risks from:
 - understanding of the client business (ISA 315)
 - non-compliance with laws and regulations (ISA 250)
 - consideration of fraud and error (ISA 240)
 - preliminary analytical review (ISA 315)
- Key audit areas not identified based on risk assessment / audit approach not identified
- Design of audit procedures - audit programme not developed or suitably tailored
- Overall and performance materiality not calculated
- Audit sampling not structured to ensure sufficiency of audit evidence

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Documentation of the audit plan should include:

- Understanding of the entity's business and inherent risks
- Consideration of fraud risk – discussions with the client and with the audit team
- Related parties and significant transactions and balances with them
- Consideration of compliance with applicable laws and regulations
- Preliminary analytical review
- Risks identified at financial statement level and at assertion level from the above
- Key audit areas and audit approach
- Tailored audit programme
- Overall and performance materiality
- Basis of sampling to be adopted
- Any modification to the plan during the course of the audit

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Documentation (ISA 230)

- Work performed but not (adequately) recorded/cross referenced
- Basis of sample size and selection not recorded
- Insufficient record of nature and extent of audit work – source of audit evidence and samples tested not recorded
- No summary and evaluation of the results of audit tests to support the conclusion, including record of any professional judgments applied

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Supervision, control and review

- Audit work not allocated based on experience and competence of staff
- Staff are not clear on the objectives of the tests and how they should carry them out
- No on-going supervision to ensure audit is on the right track and contentious issues are being dealt with properly
- Final review of the audit file by engagement partner not done or not effective to ensure sufficient, appropriate audit evidence had been obtained and recorded to support the conclusions reached and for the auditor's report to be issued

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Fixed assets

- Existence and condition of plant and equipment not verified
- Ownership of property and motor vehicles brought forward from prior year not verified
- Valuation of property not considered – No impairment review

Investments

- Title to investments not verified (particularly those brought forward from previous year, including investments in subsidiaries and associates)
- Valuation of investments not considered (particularly unquoted shares and investments in subsidiaries and associates)

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Inventory

- Physical count not attended or procedures observed not recorded and assessed
- Test counts not carried out or recorded (including direction of count) and not traced to final stock valuation
- Unit cost not verified (including allocation of direct labour and production overheads in respect of manufactured goods)
- Net realisable value not verified based on after date selling prices and no assessment of impact from slow moving, obsolete and damaged inventory
- Goods in transit not verified by cut-of work, and tracing to after date delivery-in records and payments

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Trade and other receivables

- Validity, based on structured sample which takes into account performance materiality, not verified
- Inadequate or no alternative testing for all balances circularised where no reply received
- Recoverability of receivables not adequately tested – results of subsequent receipts test not summarised and evaluated and no effective review of older, still outstanding balances
- Validity, recoverability and classification of balances due from directors and related companies not (adequately) verified

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Cash at bank

- No testing of bank reconciliations
- Bank confirmations not obtained or not from all of the banks used by client

Trade and other payables

- Completeness of payables not tested – suppliers' statement reconciliation, cut-off work and review of after date invoices and payments
- Validity not verified based on structured sample which takes into account performance materiality
- Inadequate or no alternative testing for all balances circularized where no reply received
- Validity, recoverability and classification of balances due from directors and related companies not (adequately) verified

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Borrowings

- Amounts and terms not verified
- Verification of classification of borrowings between current and non-current not documented

Revenue

- Completeness of income not tested i.e. that all goods delivered and services provided have been invoiced and recorded. For example, there is no testing from delivery or services records to sales invoices and the accounting records

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Cost of sales

- Validity and completeness not tested, including substantive analytical review of gross profit margins

Expenses

- Basis of selection of non-payroll expenses for testing and source documents tested not documented
- Wages and salaries not verified to payroll records
- Existence of employees not verified



COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Dividends declared

- Validity and completeness not verified e.g. with Board resolution

Contingencies and commitments

- No work recorded to identify possible contingencies and commitments

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Credit unions – members' loans, deposits and shares

- Audit approach not explained – fully substantive VS controls testing and reduced substantive
- Where circularization performed, (adequate) alternative testing not done for those balances where no reply received
- Adequacy of loan loss provision not tested based on the requirements of IAS 39/IFRS 9

Construction contracts

- Validity and completeness of income based on the allocation of the contract price to performance obligations (IFRS 15)
- Verification of costs allocated to the correct contract
- Estimate outcome of contracts in progress

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Initial engagements (ISA 510)

- Professional clearance not requested and obtained
- Opening balances not tested to ensure they contain no misstatements which can impact the current year

Relying on work of management's expert (ISA 500)

- Qualifications and independence of expert not assessed
- Source data used by expert not tested
- Reasonableness of expert's methodology, assumptions and conclusion not assessed

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Analytical review (ISA 520)

- Preliminary and final analytical review not performed
- Substantive analytical review not adequate

Subsequent events (ISA 560)

- Subsequent events review not performed or inadequately documented

Going concern (ISA 570)

- No going concern review
- Where there are going concern indicators, evidence not obtained to justify the going concern assumption and no disclosure of the matter, including management plans, in the financial statements and material uncertainty not highlighted in the audit report

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Management representation letter (ISA 580)

- Management representation letter not obtained
- Management representation letter dated either after audit report date or long before audit report date
- Management letter does not contain some of the minimum information stipulated in ISA 580

Communicating with those charged with governance

- Scope and timing of the audit not communicated to those charged with governance (ISA 260)
- Not recorded whether any deficiencies found in internal controls and if so, that they are communicated to those charged with governance (ISA 265)

COMMON DEFICIENCIES FOUND IN AUDIT WORK

Deficiencies in audit evidence

Review of financial statements (ISA 330.24)

- Financial statements not reviewed for presentation and adequate disclosures

Reporting

- Audit report format do not always comply with ISA 700, 701, 705 and 706
- Balance sheet not always signed & dated prior to the date of the audit report
- Other information contained in annual reports (e.g. of credit unions), not reviewed for consistency with the audited financial statements



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ACCA/BICA Practice Monitoring Reviews – Overview of Findings

ACTION PLANS

ACTION PLANS

- Firms required to provide details of the action taken to address the deficiencies found at monitoring visits
- In case of firms with unsatisfactory or mixed file inspection outcomes, firms are required to provide an action plan in a prescribed format
- Action plan template together with written instructions enclosed, when monitoring visit report issued to the firm
- Guidance on how to complete the template also given at the monitoring visit
- Submitted action plans reviewed to ensure provide a reasonable basis for rectifying the deficiencies
- Where action plan not generally adequate, firm required to provide revised plan after further guidance provide
- A copy of the action plan enclosed when the report is sent to BICA
- Firms are expected to implement the action plan and ensure that a satisfactory outcome is achieved at the next monitoring visit

ACCA/BICA Practice Monitoring Reviews – Overview of Findings

HOW FIRMS SHOULD PREPARE FOR AN AUDIT MONITORING VISIT

HOW FIRMS SHOULD PREPARE FOR AN AUDIT MONITORING VISIT

- Ensure appropriate policies and procedures established and documented (ISQC 1)
- Ensure effective compliance with ISAs
- Ensure effective planning leading to use of an effective audit programme
- Record all audit work and reasoning in detail to support the conclusions
- Undertake review of current compliance by reference to report from the previous visit (follow-up visits)
- Ensure action plan submitted after the previous monitoring visit is effectively implemented (follow-up visits)
- Ensure all files and other records are readily available at the visit
- Get the most out of the visit by listening carefully to what is said



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Questions?





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THANK YOU