BAOA

Botswana Accountancy Oversight Authority

SUMMARY OF AUDIT PRACTICE & ANTI-MONEY LAUNDRING REVIEWS 31 DECEMBER 2020

Enhanced International Confidence in Financial Reporting, Audit and Corporate Governance

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BAOA MANDATE

Botswana Accountancy Oversight Authority (BAOA) is responsible for provision of oversight to accounting and auditing services and promotion of the standard, quality and credibility of providing financial and non-financial information by entities, including Public Interest Entities (PIEs), through standard setting, financial reporting monitoring, audit practice reviews, corporate governance reviews, enforcement of compliance and oversight over Professional Accountancy Organisations; and education and training of professional accountants in Botswana.

DISCLAIMER

The Botswana Accountancy Oversight Authority does not accept any liability to any party for any loss, damage or costs howsoever arising, whether directly or indirectly from any action or decision taken (or not taken) as a result of any person relying on or otherwise using this document or arising from any omission from it.

Foreword from Board Chairperson

On behalf of the Audit Practice Review Committee and the Board of the Authority, I have the pleasure of presenting the summarized report on audit practice reviews for the year ending 31 December 2020, as well as the second review cycle (2018-2020).

The report also summarises the Special Investigations that the Authority carried out in 2020 on Certified Auditors in accordance with Section 6 (1) of the Act which states that the Authority may conduct investigations and where necessary, impose relevant sanctions on certified auditors and officers of public interest entities as well as the public interest entities.

The Authority believes that this report will serve as a valuable tool for audit firms of all sizes in developing, enhancing, and evolving their audit practices and contributing to their own processes of continuous improvement; and thereby further demonstrating their ongoing commitment to enhancing audit quality.

Board Chairperson
March 2021

1. INTRODUTION

In accordance with the Financial Reporting Act, 2010, Section 57, the Authority is mandated to undertake audit practice reviews of Certified Audit Firms and Certified Auditors of Public Interest Entities (PIEs) at least once every three years. In addition, the Authority has a Memorandum of Understanding with the Botswana Institute of Chartered Accountants (BICA), which requires that the Authority undertakes audit practice reviews of Certified Audit Firms and Certified Auditors of Non-Public Interest Entities (Non-PIEs) until such a time that the Rules and Regulations are amended to give force and effect to the provisions of the new Act.

The Financial Reporting (Amendment) Act, 2020 was passed by Parliament at its July 2020 session, and after receiving Presidential Assent, was published in the Government Gazette on 13 November 2020 as an Act of Parliament. The amendment of the Act introduced several major changes and various consequential amendments to the Rules and Regulations. One of the major changes was the transfer of the registration of Certified Audit Firms and Certified Auditors of Non-PIEs to the Authority. The Authority is in the process of amending the Rules and Regulations to incorporate these changes and to give force and effect to the provisions of the new Act. The effective date of the Act will be communicated through a Statutory Notice in the Gazette.

Audit practice reviews consist of a firm (quality control) review and a review of selected assurance engagements carried out and signed off by each firm's Certified Auditors.

A firm review consists of an inspection of the six elements of a firm's system of Quality Control Policies and Procedures namely: Leadership Responsibilities for quality within the firm; Relevant Ethical Requirements; Client Acceptance & Continuance of client relationships and specific engagements; Human Resources; Engagement Performance; and Monitoring. The aim of the review is to ensure that the system conforms in all material respects to the requirements of the International Standard on Quality Control (ISQC)1.

An engagement review aims to obtain reasonable assurance that audit engagements are performed in accordance with the applicable Assurance Standards including International Standards on Auditing; International Financial Reporting Standards; Code of Ethics; and applicable Laws and Regulations, and that the engagement Partners issue audit opinions that are appropriate in the circumstances.

The Authority completed its second audit practice review cycle on 31 December 2020. This report discusses hereunder the results of the reviews for the year 2020; and the second cycle in summary. The report highlights significant themes arising from firm reviews and individual assurance engagement file reviews that were carried out in 2020 and reported in the second cycle.

The Authority is also identified as a supervisory authority under Schedule II of the Financial Intelligence (FI) Act, 2019. The Authority's responsibilities are as per section 44 of the FI Act, 2019. These include among others ensuring that specified parties or accountable institutions regulated by BAOA comply with the FI Act, 2019.

2. PROCESS OF APPROVAL OF AUDIT PRACTICE REVIEW REPORTS

After carrying out an audit practice review, the Technical Department of the Authority prepares and submits audit practice review reports to the Audit Practice Review Committee (APRC), a subcommittee of the Authority's Board, for their consideration.

The final results of audit practice reviews are determined in terms of the audit practice review methodology. The Audit Practice Review Committee's final decision on a Certified Audit Firm or Certified Auditor would be one of the following:

Risk	Type of Finding	Overall Rating Consequence
➢ Low	Documented non-compliance with standards, codes, legislation, or policies and procedures but risk of inappropriate audit opinion is unlikely	Low risk. Review in the next cycle.
➢ Medium	Significant issues of non-compliance, and appropriateness of audit opinion could not be determined.	Review in the next cycle if the weighted rating is Low risk to Medium risk OR Re-review or Re-review and refer to Enforcement if the weighted rating is Medium risk to High risk.
➢ High	Significant issues of non-compliance or fundamental none or inadequate documentation and risk of inappropriate audit opinion is very likely or has probably been expressed.	High risk to Very High risk. Refer to Enforcement for final decision (re-review or immediate strike off).

3. AUDIT PRACTICE REVIEWS UNDERTAKEN IN 2020

3.1 Overview

In 2020, the Authority reviewed a total of 13 Certified Audit Firms with a total of 19 Certified Auditors. 4 of these were Certified Audit Firms of PIEs with a total of 10 Certified Auditors, and 9 were Certified Audit Firms of Non-PIEs with a total of 9 Certified Auditors. The results of the reviews of the 13 audit firms undertaken during 2020 were as follows:

Risk Rating	Number of Certified Firms		Total	Recommendation	
	PIE	Non-PIE		PIE	Non-PIE
Low	3	6	9	Review in the next cycle	
Medium	1	1	2	A warning and review in the next cycle.	Re-review in 18 to 24 months
High	0	2	2	One was recommended for immediate striking off. However, the Authority is still awaiting BICA's final response on this review. The other firm was recommended to be re-reviewed in 18 to 24 months. However, BICA has since withdrawn the practicing certificate for this firm.	
TOTAL	**4**	**9**	**13**		

The High-risk ratings on the 2 Certified Audit firms were due to the following significant issues:

- One firm provided both non–assurance services and assurance services to some of its clients; the non-assurance services provided included setting up accounting systems, preparation of management accounts and financial statements. The firm also provided the audit services to the same clients. The other issues noted included Quality control review of the firm not performed, engagement files not archived within 60 days as required by ISQC 1 and various findings that were recurring from the previous review and had not been addressed indicating that the firm did not take reasonable steps to address the review findings that were noted and highlighted in the previous review.

- The other firm issued Independent Auditor's Reports that were not compliant with several International Standards on Auditing requirements. The Independent Auditor's Reports had an 'Emphasis of Matter' paragraph on the same matters that led to the modification of the audit opinions. This is contrary to the requirements of ISA 706 *(emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report)*. Matters communicated under the Key Audit Matters section of the auditor's report were also the same matters that led to modification of the audit opinions. This is contrary to the requirements of ISA 701 *(Communication of Key Audit Matters in the Independent Auditor's Report)*. There were also a number of issues noted which included the Monitoring Quality Control reviews not undertaken as required by ISQC 1 and Client acceptance procedures not operating effectively.

During the second cycle, 34 firms were reviewed. 17 Certified Audit Firms (8 PIEs & 9 Non-PIEs) attained a Low-risk rating (satisfactory); 15 Certified Audit Firms (3 PIEs & 12 Non-PIEs) attained a Medium risk rating (unsatisfactory) while the remaining 2 Certified Audit firms of Non-PIE attained a High-risk rating (unsatisfactory).

Overall, the quality of the firms' system of quality control is of concern to the Authority as only 50% of the Certified Audit Firms reviewed during the second cycle were considered to be Low risk (satisfactory) while 50% were considered Medium to high risk (unsatisfactory).

The performance of the 19 Certified Auditors reviewed in 2020 were as follows:

Risk Rating	**Number of Certified Auditors**		**Total**	**Recommendation**
	PIE	**Non-PIE**		
Low	3	2	5	Review in the next cycle
Low to Medium	1	2	3	
Medium	1	0	1	Re-review in 18 to 24 months
Medium to High	5	1	6	Re-review in 18 to 24 months (2 were referred to Enforcement Committee of BAOA).
High	0	3	3	Re-review in 18 to 24 months and refer to Disciplinary Committee of BICA. • BICA has since withdrawn the practicing certificate for 1 the 3 Practitioners. • For the other 2, the Authority is awaiting the final decision from BICA.
Very High	0	1	1	Struck off with immediate effect.
Total	**10**	**9**	**19**	

The review performed on one of the two Practitioners that were rated Medium to High risk and also referred to the Enforcement Committee was a follow up review. However, the majority of findings that were noted on this review were recurring, having been raised in the previous review on the same engagement file, therefore raising the concern that the Practitioner did not take reasonable steps to address the review findings that were noted and highlighted in the previous review. The other Practitioner had a number of findings rated as High risk on one of the two engagement files reviewed that pointed to the fact that an incorrect audit opinion had been issued.

The three Practitioners that were rated as High risk were new entrants. The reviews indicated that the Practitioners did not appear to understand the International Standards on Auditing primary requirements or had challenges in applying the technical aspects of both the International Standards on Auditing and International Financial Reporting Standards. Such results, therefore, require a revision in the registration of certified auditors to ensure that the individuals that are registered as certified auditors have the right competence and capabilities to provide reasonable assurance on the audit of financial statements as required by International Standards on Auditing.

The review that was performed on the Practitioner who was rated as Very High risk was a re-review. The majority of the significant findings noted on this review were recurring findings. This raised the concern that the Practitioner did not take reasonable steps to address the review findings that were noted and highlighted in the previous review.

For the second cycle, out of the 55 Certified Auditors reviewed, 25 Certified Auditors (16 PIEs & 9 Non-PIEs) were Low to Medium risk (satisfactory) while 30 Certified Auditors (10 PIEs & 20 Non-PIEs) were rated Medium to High risk (unsatisfactory).

Overall, the quality of the Engagement reviews is of serious concern to the Authority as only 45% of the Certified Auditors reviewed during the second cycle were considered to be Low to Medium risk (satisfactory) while 55% were considered Medium to High risk (unsatisfactory).

A summary of the issues that led to such ratings on both the firm (ISQC 1) review and the engagement reviews are discussed below under Firm Reviews and Engagement Reviews. The Authority is a member of the International Forum of Independent Audit Regulators (IFIAR) and, therefore, participates in the Survey of Inspection Findings in which member countries are required, among other things, to classify findings into audit practice review/inspection themes provided by the IFIAR. All findings arising from both the firm and engagement reviews have been classified into the IFIAR Inspection Themes.

3.2 Firm Reviews

All the key elements of each firm's system of Quality Control Policies and Procedures were reviewed on a sample basis and were then compared to the standard requirements of ISQC 1. All deviations from the requirements of ISQC 1 were noted as "findings" and were allocated to their respective ISQC 1 element as provided at Table A below.

Table A: Firm Review Findings

	2020						SECOND CYCLE					
	CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS		CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS	
SYSTEM OF QUALITY CONTROL IFIAR Inspection Theme	#	%	#	%	#	%	#	%	#	%	#	%
Leadership Responsibilities for Quality within the Firm (i.e., Tone at the Top)	0	0	4	8	**4**	**8**	3	2	8	6	**11**	**8**
Independence and Ethical Requirements	2	4	5	10	**7**	**14**	5	4	14	9	**19**	**13**
Client Risk Assessment, Acceptance and Continuance	0	0	1	2	**1**	**2**	0	0	5	3	**5**	**3**

	2020						SECOND CYCLE					
	CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS		CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS	
SYSTEM OF QUALITY CONTROL IFIAR Inspection Theme	#	%	#	%	#	%	#	%	#	%	#	%
Human Resources	4	8	2	4	**6**	**12**	7	5	5	4	**12**	**9**
Engagement Performance	5	10	13	27	**18**	**37**	10	7	54	38	**64**	**45**
Monitoring	4	8	9	19	**13**	**27**	8	6	23	16	**31**	**22**
Total Findings	**15**	**30**	**34**	**70**	**49**	**100**	**33**	**23**	**109**	**77**	**142**	**100**
Number of Audit Firms	**4**		**9**		**13**		**11**		**23**		**34**	
Average Findings Per Audit Firm	**4**		**4**		**4**		**3**		**5**		**4**	

15 (31%) of the 49 total findings for 2020 were for Certified Audit Firms of PIEs and the remainder of 34 (69%) were for Audit Firms of Non- PIEs. A total of 142 findings were noted during the second cycle. 33 (23%) of the findings were from the Certified Audit Firms of PIEs and 109 (77%) were from Certified Audit Firms of Non- PIEs.

Two themes, Engagement Performance and Monitoring emerged with a higher contribution to the total findings of 37% and 27%, respectively, which is also consistent with the second cycle statistics of 45% and 22%, respectively. Major issues noted under these themes are discussed further below.

a) <u>Engagement Performance</u>

The Engagement Performance theme made the largest contribution to the total findings; 37% in 2020 and 45% in the second cycle. Certified Audit Firms of Non-PIEs accounted for 27% of the findings, while Certified Audit Firms of PIEs accounted for the remainder of 10% in 2020. In the second cycle, 38% was contributed by Certified Audit Firms of Non- PIEs and 7% by Certified Audit Firms of PIEs. The significant and common findings noted in this theme included the following:

i) *Inappropriate Audit Opinions issued*

ISQC 1 requires firms to establish policies and procedures designed to provide them with reasonable assurance that engagements are performed in accordance with professional standards and applicable legal and regulatory requirements, and that the firm or the engagement partner issue reports that are appropriate in the circumstances.

The audit reports that were issued by some practitioners were not in compliance with the International standards on Auditing. It was also noted that when Practitioners issue modified opinions, the ISA 705 *((Revised) Modifications to the Opinions in the*

Independent Auditor's Report) requirements were no complied with. This area continues to be a challenge as this has previously been highlighted in our previous annual reports as an area of concern. The issues that were noted included the following:

- Qualified audit opinions issued instead of adverse audit opinions or disclaimer of audit opinions. ISA 705 gives guidance as to how a Practitioner arrives at a decision to whether the audit opinion is a qualified, adverse or a disclaimer of opinion.

- Insufficient disclosures made in the Independent Auditor's opinion, such as the quantification of the financial effects of the misstatement and inadequate disclosure of the description of matters giving rise to the modification.

- The financial statements of reporting entities not accounting for the business transactions for branches/departments and the auditor 's opinions not reflecting this significant fair representation issue. In some cases, Practitioners issued audit opinions on branches and did not highlight in the audit opinions through an emphasis of matter that the Financial statements were of a branch alone as required by ISA 805 *(Special Consideration-Audits of Single Financial Statements and specific Elements, Accounts, or Items of Financial Statements)*.

Inappropriate audit opinions are further discussed under Engagement Reviews; however, Practitioners are encouraged to familirise themselves with the requirements of ISA 705.

ii) *No documented evidence that Audit Files were archived / insufficient archiving procedures performed*

ISQC 1 requires firms to establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalised. It further indicates that such a time limit would ordinarily not be more than 60 days after the date of the auditor's report.

In our reviews it was noted that firms either did not have any evidence that the engagement files were assembled timely as required by ISQC 1 or the evidence provided was considered to be insufficient as it did not indicate the dates the engagement files were archived and also dates when the audit opinions were signed. It therefore became difficult to determine if the assembling of files was done within the 60 days.

Upon a sample of a few engagement files, it was noted that firms generally did not archive the engagement files within the stipulated 60 days as per ISQC 1 requirements.

It was further noted that, for the few firms that had a list of their archived files, the list only included files archived in the last twelve months despite the firms' retention periods being more than 5 years. The archived listing is therefore supposed to include all the files that have been archived to date and are not yet due for destruction.

b) Monitoring

The Monitoring theme accounted for the second highest contribution to total findings; 27% in 2020 and 22% for the second cycle. Certified Audit Firms of Non-PIEs contributed 18% of the findings compared to 8% contributed by the Certified Audit Firms of PIE in 2020. In the second cycle 16% was contributed by Certified Audit Firms of Non-PIEs and 6% Certified Audit Firms of PIEs.

The main area of concern was the Internal Monitoring Quality Control Reviews. For most of the firms, the Monitoring quality control reviews were either not performed or were considered to be insufficient.

ISQC 1 requires firms to establish a monitoring process designed to provide them with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively. This process shall include an ongoing consideration and evaluation of the firm's system of quality control including, on a cyclical basis, inspection of at least one completed engagement for each engagement partner.

For firms that performed the monitoring reviews, the following exceptions were noted:

- The individuals who performed the monitoring review of the firm did not have sufficient and appropriate experience and authority in the firm to assume that responsibility as required by ISQC 1, e.g., the individuals were neither Partners in the firm nor certified auditors.

- The inspection of at least one completed engagement was not performed for some of the Engagement Partners.

- Communication of monitoring procedures performed, conclusions drawn from the monitoring procedures to the engagement partner and other appropriate individuals within the firm were not evidenced as required by ISQC 1.

- Some of the ISQC 1 elements were not covered as part of the firm's system of quality control reviews and in other cases the elements reviewed were not documented.

3.3 Engagement Reviews

During 2020, a total of 21 engagement reviews under the responsibility of 19 Certified Auditors across 13 Certified Audit Firms were carried out. A total of 82 engagements under the responsibility of 55 Certified Auditors across 34 Certified Audit Firms were undertaken during the second cycle.

All deviations from the requirements of applicable Assurance Standards, International Financial Reporting Standards; Code of Ethics; and applicable laws and regulations were noted as "findings". Each engagement finding was allocated to the IFIAR themes as per Table B below.

Table B: Engagement Review Findings split by IFIAR Inspection Themes

	2020						SECOND CYCLE					
	CERTIFIED AUDITORS OF PUBLIC INTEREST ETITIES		CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ETITIES		TOTAL AUDIT ENGAGEMENTS		CERTIFIED AUDITORS OF PUBLIC INTEREST ETITIES		CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ETITIES		TOTAL AUDIT ENGAGEMENTS	
IFIAR INSPECTION THEMES	**#**	**%**	**#**	**%**	**#**	**%**	**#**	**%**	**#**	**%**	**#**	**%**
Internal Control Testing	1	0	0	0	**1**	**0**	3	0	0	0	**3**	0
Adequacy of Financial Statement Presentation and Disclosures	11	5	10	5	**21**	**10**	35	4	62	8	**97**	12
Use of Experts/Specialists	0	0	1	0	**1**	**0**	0	0	2	0	**2**	0
Substantive Analytical Procedures	2	1	2	1	**4**	**2**	3	0	2	0	**5**	1
Audit Committee Communication	0	0	0	0	**0**	**0**	1	0	0	0	**1**	0
Fraud Procedures	2	1	11	5	**13**	**6**	2	0	22	3	**24**	3
Risk Assessment	0	0	1	0	**1**	**0**	1	0	11	1	**12**	1
Audit Report	2	1	3	1	**5**	**2**	6	1	33	4	**39**	5
Accounting Estimates, including Fair Value Measurement	1	0	1	0	**2**	**1**	13	2	17	2	**30**	4
Revenue Recognition	2	1	4	2	**6**	**3**	2	0	8	1	**10**	1
Inventory Procedures	2	1	3	1	**5**	**2**	2	0	4	0	**6**	1
Related Party Transactions	4	2	5	2	**9**	**4**	6	1	30	4	**36**	4
Going Concern	0	0	0	0	**0**	**0**	2	0	3	0	**5**	1
Adequacy of Review and Supervision	58	27	83	39	**141**	**66**	132	16	364	45	**496**	61
Audit Sampling	3	1	3	1	**6**	**3**	7	1	25	3	**32**	4
Audit of Allowance for Loan Losses and Loan Impairments	0	0	0	0	**0**	**0**	1	0	0	0	**1**	0
Insufficient Challenge and Testing of Management's Judgement and Assessments	0	0	0	0	**0**	**0**	3	0	0	0	**3**	0
Testing of Customer Deposits and loans	0	0	0	0	**0**	**0**	7	1	0	0	**7**	1
Audit Methodology Including Programs and Tools	0	0	0	0	**0**	**0**	3	0	0	0	**3**	0
TOTAL FINDINGS	**88**	**41**	**127**	**59**	**215**	**100**	**229**	**28**	**583**	**72**	**812**	**100**
Total Number of Partners	**10**		**9**		**19**		**26**		**29**		**55**	
Findings per Attest Partner(average)	**9**		**14**		**11**		**9**		**20**		**15**	

88 (41%) of the 215 total findings for 2020 were from Certified Auditors of PIEs, the remainder of 127 (59%) were from Certified Auditors of Non- PIEs. A total of 812 findings were noted during the second cycle. These are made up of 229 (28%) contributed by Certified Auditors of PIEs and 583 (72%) by Certified Auditors of Non- PIEs.

The engagement files reviewed continue to show significant deficiencies mainly in the 'Adequacy of Review and Supervision' theme with 66%, split between Certified Auditors of PIEs with 27% and Certified Auditors of Non-PIEs with 39%. In the second cycle most of the findings also related to the same theme with 61%, split between Certified Auditors of PIEs with 16% and Certified Auditors of Non-PIEs with 45%. The significant issues noted under this theme which mainly led to the Practitioners being rated as either Medium to High Risk, High risk and Very High risk are discussed in detail below.

Adequacy of Review and Supervision Theme's contributions

Findings noted under this theme are mainly a result of failure of senior members of the audit engagement teams to properly supervise the audit work performed (e.g., insufficient time devoted to review or no evidence of review). The significant findings noted included:

a) *Insufficient Audit Evidence and Audit Documentation*

   Generally, the audit evidence obtained on material balances was considered to be insufficient to support the audit opinions issued as the audit documentation was either inadequate or was not documented altogether. In most cases, the Auditors documented on the working papers that the samples were traced to various supporting documents. However, the identifying characteristics of those supporting documents were not documented.

   ISA 230 *(Audit Documentation)* requires that the identifying characteristics of specific items or matters tested should be documented. The guidance on this standard further gives examples of the identifying characteristics that need to be documented, for example, for a detailed testing of entity generated purchase orders, the Auditor has to document the dates and unique purchase order numbers of the purchase order verified.

b) *Inventory valuation incorrectly tested*

   It has been noted that Auditors generally do not perform any audit work to test the inventory costing formulae or when the testing formula is tested, it is usually done incorrectly. Instead of recomputing either the weighted average costing or the First-in, First-out costing formula, Auditors tend to sample a number of inventory items and trace them to purchase invoices. This testing does not address the accuracy of the inventory values as required by IAS *(Inventories)* 2.

c) *Incorrect direction of testing performed on payables*

On most of the engagement files that were reviewed, it was noted that Payables were audited by tracing the year end balances to subsequent payments. This testing does not address the risk of completeness of payables which is a key risk for payables.

d) *Confirmations of balances not obtained*

Cash and cash equivalents, Bank Overdrafts, Loans, Finance Assets, Trade Debtors, government grants received were not confirmed. There were no alternative procedures performed or the alternative procedures were considered to be insufficient as they did not adequately address the specific risks of existence as at year end or completeness of transactions during the year.

e) *Expected credit losses Provisions incorrectly computed (IFRS 9).*

The Auditors either did not perform the 12-month expected credit loss impairment provisions as required by IFRS 9 or where it was performed the calculations did not take into account the consideration of the possible impairment of the actual cashflows using unbiased and a probability weighted amount determined by evaluating a range of possible outcomes as required by IFRS 9 *(Financial Instruments)*.A number of Practitioners incorrectly considered discounting for the time value of money to be the equivalent to expected credit loss computation.

f) *Opening balances not tested as required by ISA 510 (Initial Audit Engagements)*

On a number of engagement files that were reviewed, it was noted that there was no documented evidence on files that the auditors had tested opening balances despite the fact that it was the auditor's first year of auditing the entities.

ISA 510 requires the auditor to read the most recent financial statements, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures.

The auditor is required to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by:

i. Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated;

ii. Determining whether the opening balances reflect the application of appropriate accounting policies; and

iii. Performing one or more of the following:

- Where the prior year financial statements were audited, reviewing the predecessor auditor's working papers to obtain evidence regarding the opening balances;
- Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
- Performing specific audit procedures to obtain evidence regarding the opening balances.

The auditor is also required to obtain sufficient appropriate audit evidence about whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, and whether changes in the accounting policies have been appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

ISA 510 provides further guidance on what the auditor is required to do when the opening balances contain misstatements that could materially affect the current period's financial statements and when the prior period's financial statements had a modification to the audit opinion.

g) *Insufficient audit work carried out on Related Parties*

There was no documented evidence that the auditors had enquired from management the identity of related parties, nature of the relationships & type and purpose of the related party transactions. There was also no documented evidence that the auditors had considered the adequacy of control activities over the authorisation and recording of related party transactions as part of obtaining an understanding of the entities' internal controls as required by ISA 550 (*Related Parties)*. It was also noted that some related party balances/transactions were not disclosed at all in the financial statements as required by IAS 24 (*Related Parties Disclosures)* or were disclosed at various notes, not under the Related Parties note for easier reference.

h) *Restatements not audited and no disclosures made in the financial statements*

It was noted that some of the entities' financial statements were restated. However, there was no documented audit work performed on these material prior periods adjustments. There were also no disclosures made as required by IAS 8 *(Accounting*

Policies, changes in Accounting Estimates and Errors) in the financial statements. IAS 8 requires an entity to disclose the following in relation to prior period errors:

i. The nature of the prior period error;

ii. For each prior period presented, to the extent practicable, the amount of the correction:

- for each financial statement line item affected; and

- If IAS 33 *(Earnings per Share)* applies to the entity, for basic and diluted earnings per share.

iii. The amount of the correction at the beginning of the earliest prior period presented; and

iv. If retrospective restatement is impracticable for a particular period, the circumstances that led to the existence of that condition and a description of how and from when the error has been corrected.

i) *Rights and Obligations on Property, Plant and Equipment not addressed*

Property, Plant and Equipment were not physically verified for existence and were also not tested for ownership. There were instances where entities had land which was not recognised in the financial statements and the impact of this was not considered in the audit opinion that had been issued.

j) *Assessment of useful lives and residual values*

No documented evidence that the auditors had evaluated management's assessments, if any, of useful lives and residual values of Property, Plant & Equipment. IAS 16 requires that the residual value and useful life of an asset be reviewed at least at each financial year-end. The auditors are therefore required by ISA 540 *(Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*) to evaluate whether the accounting estimates in the financial statements are reasonable or misstated.

k) *Sampling*

It was noted in various engagement files that we reviewed that there was no documented evidence of the sampling plan which the auditors had used to determine sample sizes; and to select sample items for detailed testing.

ISA 530 *(Audit Sampling)* requires the auditor to determine sample sizes that are sufficient to reduce sampling risk to an acceptably low level and to select items for the sample in such a way that each sampling unit in the population has a chance of selection.

l) *Assets not tested for Impairment*

It was noted in some of the engagement files that assets were either not assessed for impairment as required by the various IFRSs *(IAS 36 Impairment of Assets, IAS 2 Inventories, IFRS 9, etc) or* the work that was performed was considered insufficient.

m) *Material misstatements not explained*

Material differences between the ledger and financial statements were not explained in a number of engagement files and there were also not accumulated in the schedule of misstatements as required by ISA 450 *(Evaluation of Misstatements Identified*). ISA 450 requires the auditor to:

i. accumulate misstatements identified during the audit, other than those that are clearly trivial.

ii. Determine whether the overall audit strategy and audit plan need to be revised:

- if the nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements exist that, when aggregated with misstatements accumulated during the audit, could be material; or

- the aggregate of misstatements accumulated during the audit approaches materiality determined in accordance with ISA 320 (Materiality in Planning and Performing the Audit).

n) *Testing of Journal Entries*

In some of the engagement files that were reviewed, it was noted that there was no documented evidence of any journal entry testing performed by the auditors to test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of financial statements as required by ISA 240 *(The Auditor's Responsibilities relating to Fraud in an Audit of Financial Statements)*.

Furthermore, on engagement files in which journal entry testing was performed, the auditors did not follow the requirements of ISA 240 in selecting the samples for journal entry testing. For example, when sampling, the auditors are supposed to consider characteristics of the fraudulent journals such as:

- Journals made to unrelated, unusual, or seldom used accounts;
- Journals made by individuals who typically do not make journal entries;
- Journals recorded at the end of the period or as post-closing entries that have little or no explanation or description;
- Journals made either before or during the preparation of the financial statements that do not have account numbers; or
- Journals containing round numbers or consistent ending numbers.

o) *Branches not accounted for in the financial statements of reporting entities*

The transactions of branches/departments to entities which form an integral part of the entity were not included in the Financial Statements of the reporting entity and the auditor 's opinions did not reflect this significant fair representation issue. In some cases, Practitioners issued audit opinions on branches and did not highlighted in the audit opinion that Financial statements were of a branch alone as required by ISA 805 *(Special Consideration-Audits of Single Financial Statements and specific Elements, Accounts, or Items of Financial Statements)*.

p) *Incorrect Modified Audit Opinions issued*

Audit opinions issued in some engagement files that were reviewed were considered to be inappropriate as the balances that were the subject of modification were considered to represent a substantial proportion of the financial statements and were also not confined to one area. Qualified audit opinions were issued in these engagement files instead of considering at a minimum either adverse opinions or a disclaimer of opinions as guided by ISA 705.

The table below illustrates how the auditor’s judgment about the nature of the matter giving rise to the modification, and the pervasiveness of its effects or possible effects on the financial statements, affects the type of opinion to be expressed.

Nature of Matter Giving Rise to the Modification	**Auditor’s Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements**	
	Material but Not Pervasive	**Material and Pervasive**
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

4. INVESTIGATIONS PERFORMED IN 2020

Two investigations were performed on three Certified Auditors of PIEs during 2020. The objective of the investigations was to provide the Authority with reasonable assurance that the three auditors complied with the professional standards and applicable legal and regulatory requirements and that the auditors' reports that were issued by the engagement Partners were appropriate in the circumstances.

Two of the three Certified Auditors investigated were referred to the Enforcement Committee for appropriate sanctioning following the Authority's conclusion that the audit opinions that they had issued on their respective engagement files were inappropriate.

In carrying out the audits of the specific entities, the auditors failed to identify non-compliance with the following International Financial Reporting Standards and International Standards on Auditing among others:

a) Significant non-compliances with IFRS 3 (*Business Combination*):

   - Recognising goodwill from business acquisitions under common control which is prohibited under IFRS 3.

   - Business acquisitions accounted for using contractual values instead of fair values as per the requirements of IFRS 3.

   - Businesses acquired and recognised on a provisional basis because of inadequate information were not subsequently updated when further information became available as required by IFRS 3.

   - Businesses acquired were incorrectly accounted for as Property, Plant and Equipment.

b) Impairments testing on goodwill was incorrectly assessed at a higher Cash Generating Unit (CGU) level rather than the lowest level as required by IAS 36 *(Impairment)*. IAS 36 requires that the identification of CGUs be done at the level of the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

c) The entity recognised the deferred tax assets relating to unused tax losses when the business did not reasonably appear to be able to recover the unused tax losses. This was contrary to the requirements of IAS 12 (*Income Taxes*) which states that the deferred tax asset shall be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax losses can be utilised.

d) In determining the cost of inventory held for trade, the entity did not account for the impact of rebates and discounts received from suppliers in connection with the purchase of inventory on the opening and closing stock values. These were netted off against the cost of sales. There was no allocation / capitalisation of the rebates and discounts to the opening and closing stocks. This was not in line with IAS 2 *(Inventories)* which states that trade discounts, rebates and other similar items are deducted in determining the costs of purchase of inventories.

e) Sales resulting from the entities acting as agents were accounted for as gross sales instead of commission. This was contrary to requirements of IAS 18 which states that revenue includes only the gross inflows of economic benefits received and receivable by the entity on its own account. Amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes are not economic benefits which flow to the entity and do not result in increases in equity. Therefore, they are excluded from revenue. Similarly, in an agency relationship, the gross inflows of economic benefits include amounts collected on behalf of the principal and which do not result in increases in equity for the entity. The amounts collected on behalf of the principal are not revenue, instead, revenue is the amount of commission.

f) Multiple physical inventory counts were performed by the Auditors which were not reasonably justified in accordance with International Standards on Auditing.

5. ANTI MONEY LAUNDERING REVIEWS UNDERTAKEN IN 2020

Four (4) audit firms were reviewed for compliance with the FI Act, 2019 by the Authority during the year ending December 2020. All Anti-Money Laundering (AML) exceptions are considered to be high risk; therefore, follow up reviews for weaknesses identified were done within a month after the review.

5.1 Summary of common findings

All the firms in 2020 were first time reviews. The following were the common findings noted across the four firms:

a) *Retention period for AML records kept by the Firms not in line with FI Act, 2019 requirement*

The retention period for records obtained through the customer due diligence process, account files and business correspondences, and from results of any analysis undertaken were stated as 5 years in most of the firms' manuals rather than 20 years as per FI Act,2019.

The FI Act, 2019 Section 28(1) requires that a specified party shall keep records obtained through customer due diligence measures, account files and business correspondences and results of any analysis undertaken for 20 years from the date a transaction is concluded and after the termination of a business relationship.

b) *Inadequate staff training on anti-money laundering*

The firms did not have training programs in place, to ensure that the required elements of AML/CFP (Countering the Financing of the Proliferation) were addressed, implemented, and executed as required by FI Act, 2019 Section 12(1c) which states that a specified party or accountable institution shall maintain an on-going employee training programme with regard to the specified party's obligations under this Act.

c) *Independent audit function and ongoing monitoring of AML not established*

The firms did not have independent audit functions and ongoing monitoring was not performed to examine and evaluate the effectiveness of policies, procedures and controls as required by FI Act, 2019 section12. (1)(d).

Specified parties or accountable institutions are required to develop and maintain an independent audit function to examine and evaluate policies, procedures and controls developed in accordance with the FI Act, 2019 Section 12(1)d to ensure compliance with measures taken by the specified party to comply with the Act and the effectiveness of those measures.

d) *No policies and procedures on screening of Prominent Influential Persons*

The firms did not have policies and programs on the identification of prominent influential persons as required by FI Act, 2019 Section 18(1), which states that a specified party or accountable institution shall in accordance with its risk management systems and compliance programme establish whether a prospective customer is a prominent influential person or beneficial owner of a prospective customer is a prominent influential person.

e) *Firm Risk Assessments insufficiently*

It was noted that the firms' risk assessment did not cover all the clients that the firms had, and also did not document the appropriate measures for managing and mitigating any identified risks relating to product/ service, delivery/ distribution channel, customer or country as required by FI Act, 2019, section 11 (1).

According to the FI Act,2019, a specified party or accountable institution shall conduct a risk assessment by identifying risks and mitigating measures relating to business relationships and transactions; pre-existing products, practices, and delivery mechanisms; development of new products, new business practices, new business procedures, new technologies and delivery mechanisms.

5.2 Follow up reviews

Follow up reviews that have been completed have shown a significant improvement on remedying the deficiencies that were previously noted.

6. MEASURES IN PLACE TO IMPROVE COMPLIANCE

The Authority continually engages in the following with the aim to improve audit compliance:

a) Issuing out a summary report annually to sensitise the Certified Firms and Auditors on the major and common issues noted each year. We encourage all Firms and Auditors to follow through these reports annually and make appropriate improvements to ensure compliance.

b) Close out meetings with the Firms' leadership and each Practitioner where exhaustive deliberations are held discussing all the issues that were noted, explaining what informed the exceptions and recommendations of how these exceptions can be remedied going forward.

c) The Authority issues ample thought leadership material on IFRSs, ISAs and other regulatory issues on its website.

The Authority is also considering doing the following going forward:

a) Increasing transparency in relation to annual reporting by disclosing the individual firm and engagement review findings and results by Firm name and Practitioner name.

d) Unsatisfactory performances will be referred to the Enforcement Committee for appropriate sanctions. These would be mainly firms or Practitioners rated at least as Medium to High risk.

7. CONCLUDING REMARKS

The Authority wishes to emphasise that the primary objective of the audit practice reviews is to raise the standard of audit and protect public interest. For that reason, the Authority's audit practice review reports are proactive and forward looking, contain detailed recommendations and guidance to enable audit practices to improve their performance and overall standard of audit, where such need has been identified. Although the Authority values developing the Certified Auditors to ensure the highest standards of compliance with applicable standards and code, the new emphasis will be towards sanctioning non-compliance in accordance with the amended Act. It is evident, based on the audit practice reviews carried out to date, that audit firms need to improve their systems of quality controls, particularly the quality of the work performed, and evidence obtained to support the audit opinions issued.

END