Botswana Accountancy Oversight Authority

SUMMARY OF AUDIT PRACTICE REVIEWS

FOR THE YEAR ENDED 31 DECEMBER 2018

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Foreword from Board Chairperson

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 Accounting Organisations; and education and training of professional accountants in Botswana.

On behalf of the Audit Practice Review Committee and the Board of the Authority, I have the pleasure of presenting the Audit Practice Review Committee summarized report on audit practice reviews for the year ending 31 December 2018 as well as the audit practice reviews for the first cycle (2015 – 2017).

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.

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Board Chairperson

March 2019

SUMMARISED AUDIT PRACTICE REVIEW REPORT
FOR THE YEAR ENDED 31 DECEMBER 2018

INTRODUTION

One of the major mandates of the Authority is to undertake audit practice reviews of Certified Audit Firms and their attest partners or practitioners.

Audit practice reviews consist of a firm (quality control) review and a review of selected assurance engagements carried out by each firm's attest (assurance) engagement partners (interchangeably referred to as practitioners).

A firm review consists of an examination of the six (6) elements of a firm's system of Quality Control Policies and Procedures, namely: Leadership Responsibilities; Independence & Ethical Requirements; Client Acceptance & Continuance; Human Resources; Engagement Performance; and Monitoring. The aim of the examination is to ensure that the system conforms in all material respects to the requirements of the International Standard on Quality Control 1 (ISQC 1).

An engagement review aims to obtain reasonable assurance that audit engagement partners in a Certified Audit Firm comply with the applicable Assurance Standards; International Financial Reporting Standards; Code of Ethics; and applicable Laws and Regulations, and that reports issued by the firm or engagement partners are appropriate in the circumstances.

In terms of its audit practice review mandate, the Authority is responsible for Certified Audit Firms and Certified Auditors of Public Interest Entities. However, the Authority has entered into a Memorandum of Understanding with 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 until such a time that the legislation is changed to give the Authority the responsibility to undertake inspections of all Certified Audit Firms and Certified Auditors in Botswana.

The Authority has adopted a three-year inspection cycle, which requires that all Certified Audit Firms and their practitioners be reviewed within the three-year cycle period. The Authority completed its first audit practice review cycle on the 31 December 2017 and the second cycle commenced on the 01 January 2018.

This report discusses in detail hereunder the results of the reviews for the year 2018; and for the first cycle (2015 to 2017) in summary.

PROCESS OF APPROVAL OF AUDIT PRACTICE REVIEW REPORTS

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

Final results of audit practice reviews are determined in terms of predetermined criteria applicable to the audit practice review cycle. The APRC's final decision would be one of the following:

- Satisfactory, meaning the next audit practice review will be carried out in the next cycle;

- Unsatisfactory, meaning some matters still require attention before a satisfactory result can be achieved and a follow-up audit practice review will be scheduled; or

- Referral to the Enforcement Committee, which could then attract possible sanctions by the Committee.

Audit practice review reports for Certified Audit Firms and Certified Auditors of Public Interest Entities will be examined by the APRC, who will then recommend a course of action to the Authority's Board.

In respect of Certified Audit Firms and Certified Auditors of Non-Public Interest Entities, the APRC will examine audit practice review reports prepared by the Technical Department and recommend a course of action to BICA, through the Authority's Board. BICA will then make the final decision and inform their members accordingly.

With regard to Certified Audit Firms and Certified Auditors of Public Interest Entities, the Authority has adopted a developmental policy which requires that an audit firm or audit practitioner will be deregistered if their performance in an audit practice review is unsatisfactory:

- three times in a row, with no prospect of making minimal improvements to attain the required performance standards in the short-term; or

- at first or second review; where it is determined that the performance is so bad that continued practice of the firm or practitioner could seriously harm public interest or the interests of those who rely on the reports of the firm or practitioner.

In respect of Certified Audit Firms and Certified Auditors of Non-Public Interest Entities, BICA has adopted a three-strike rule which requires that an audit firm or audit practitioner be deregistered if their performance in an audit practice review is unsatisfactory three times in a row.

AUDIT PRACTICE REVIEWS UNDERTAKEN IN 2018

Overview of Audit Practice Reviews

Nine (9) Certified Audit Firms with a total of thirteen (13) Certified Auditors were reviewed during 2018. One (1) of these, with a total of five (5) practitioners was a Certified Audit Firm of Public Interest Entities, and eight (8) with a total of eight (8) practitioners were Certified Audit Firms of Non-Public Interest Entities.

Overall the quality of the firms' system of quality control (firm reviews) has not improved in terms of average number of findings per audit firm. The average number of findings remained virtually static at five (5) findings for certified audit firms of PIEs and slightly decreased for certified audit firms of Non-PIEs from seven (7) to six (6) findings. (see Table A).

For the Engagement Reviews, the quality of the audits does not seem to be improving. As it will be noted at Table B, the average number of findings per attest partner increased in 2018 for certified auditors of PIEs to twenty-three (23) from eight (8) in the first cycle while for certified auditors of non-PIEs the average number of findings decreased slightly to twenty-four (24) from twenty-seven (27) in the first cycle. Clear distinctions can be noted for small audit firms which continue to record a high number of findings when compared to the "big" audit firms. Small audit firms find it difficult to resource their practices with adequately competent staff and engagement quality control structures to cope with the ever-changing audit and International Financial Reporting Standards (IFRS) landscape

The Authority has for the past four years been participating in the International Forum of Independent Audit Regulators (IFIAR) Survey of Inspection Findings in which member countries were 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 were classified into the IFIAR Inspection Themes.

Detailed analysis of the Firm Reviews and Engagement Reviews findings are provided in the following paragraphs.

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.

Provided in Table A below are the findings for 2018 and for the first cycle; allocated to each ISQC 1 element (IFIAR Theme), and split between Certified Audit Firms of Public Interest Entities and Audit Firms of Non-Public Interest Entities:

Table A: Firm Review Findings allocated to the ISQC 1 Elements of System of Quality Control (IFIAR "Inspection Themes")

SYSTEM OF QUALITY CONTROL IFIAR Inspection Theme	2018					
	CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS	
	Total findings	Total findings as a % of total findings for all firms	Total findings	Total findings as a % of total findings for all firms	Total findings	Total findings as a % of total findings for all firms
Leadership Responsibilities for Quality within the Firm (i.e., Tone at the Top)	1	2%	2	4%	**3**	**6%**
Independence and Ethical Requirements	0	0%	5	11%	**5**	**11%**
Client Risk Assessment, Acceptance and Continuance	0	0%	3	6%	**3**	**6%**
Human Resources	1	2%	2	4%	**3**	**6%**
Engagement Performance	2	4%	24	49%	**26**	**53%**
Monitoring	1	2%	8	16%	**9**	**18%**
Total Findings	**5**	**10%**	**44**	**90%**	**49**	**100%**
Number of Audit Firms	**1**		**8**		**9**	
Average number of findings Per Audit Firm	**5**		**6**		**5**	

SYSTEM OF QUALITY CONTROL IFIAR Inspection Theme	FIRST CYCLE (2015 -2017)					
	CERTIFIED AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDIT FIRMS OF NON - PUBLIC INTEREST ENTITIES		ALL CERTIFIED AUDIT FIRMS	
	Total findings	Total findings as a % of total findings for all firms	Total findings	Total findings as a % of total findings for all firms	Total findings	Total findings as a % of total findings for all firms
Leadership Responsibilities for Quality within the Firm (i.e., Tone at the Top)	5	3%	12	7%	**17**	10%
Independence and Ethical Requirements	8	5%	22	12%	**30**	17%
Client Risk Assessment, Acceptance and Continuance	0	0%	2	1%	**2**	1%
Human Resources	17	9%	37	21%	**54**	30%
Engagement Performance	14	8%	37	21%	**51**	28%
Monitoring	6	3%	19	10%	**25**	14%
Total Findings	**50**	28%	**129**	72%	**179**	100%
Number of Audit Firms	**10**		**18**		**28**	
Average number of findings Per Audit Firm	**5**		**7**		**6**	

The nine firms that were reviewed in 2018 recorded an average number of findings of 5 (five) per audit firm. For the first three-year (2015-2017) cycle twenty-eight (28) audit firms recorded an average number of findings of six (6) per firm.

The number of findings for the one (1) certified audit firm of public interest entities reviewed in 2018 was five (5). Over the first audit practice review cycle, the average number of findings for the ten (10) audit firms reviewed was five (5).

With regard to audit firms of Non-Public Interest Entities, the performance of the eight (8) audit firms reviewed in 2018 recorded an average number of findings of six (6); while for the first cycle, the eighteen (18) firms recorded an average number of findings of seven (7).

The findings as summarised at Table A above, split by Elements of the System of Quality Control (IFIAR Inspection Themes) are further analysed below, by each theme's contribution to the total findings:

a) *Engagement Performance Theme Contribution to Total findings: 53% in 2018 and 28% in the first cycle*

The Engagement Performance theme made the largest contribution to the total findings (53%) in 2018 and 28% in the first cycle. Certified Audit Firms of Non-Public Interest Entities accounted for 49% of the findings, while Certified Audit Firms of Public Interest Entities accounted for the remainder of 4% in 2018.

Common findings in this theme included the following:

i) Firms had no documented policies and procedures in their Quality Control Manuals guiding them on the destruction of old audit files.

ii) Firms were unable to provide us with lists of archived files as evidence that client documentation had been archived and securely stored for future reference.

iii) Procedures for ensuring that audit engagement files were backed up within 60 days of signing an audit report were not operating effectively as evidenced by most firms being unable to provide us with lists of archived files. In other firms, there were no systematic or documented procedure in place to verify/support that backups of electronic documentation, in particular engagement files, had been successfully done.

iv) Some firms did not have policies and procedures to address the following ISQC 1 requirements:

- The firm's review responsibility policies and procedures shall be determined on the basis that work of less experienced team members is reviewed by more experienced engagement team members;

- Engagement teams are to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized;

- That appropriate consultation takes place on difficult or contentious matters; and that sufficient resources are available to enable appropriate consultation to take place;

- That the firm shall establish policies and procedures setting out the nature, timing and extent of an engagement quality control review. Such policies and procedures shall require that the engagement report should not be dated until the completion of the engagement quality control review;

- The firm shall establish policies and procedures to address the appointment of engagement quality control reviewers and establish their eligibility through: the technical qualifications required to perform the role, including the necessary experience and authority; and the degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer's objectivity;

- For audits of financial statements of listed entities, the firm shall establish policies and procedures to require the engagement quality control review to include consideration of the following:

  - the engagement team's evaluation of the firm's independence in relation to the specific engagement;

  - whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, the conclusions arising from those consultations; and

  - whether documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached.

- The firm shall establish policies and procedures to require the engagement quality control review to include: discussion of significant matters with the engagement partner; review of the financial statements or other subject matter information and the proposed report; review of selected engagement documentation relating to significant judgments the engagement team made and the conclusions it reached; and evaluation of the conclusions reached in formulating the report & consideration of whether the proposed report is appropriate; and

- The firm shall provide for the replacement of the engagement quality control reviewer where the reviewer's ability to perform an objective review may be impaired.

b) *Monitoring Theme's contribution to total findings:* 18% in 2018 and 14% in the first cycle

The Monitoring theme accounted for the second highest contribution to total findings; 18% in 2018 and 14% for the first cycle. Certified Audit Firms of Non-Public Interest Entities contributed 16% of the findings compared to 2% contributed by Certified Audit Firms of Public Interest Entities in 2018.

Common findings in this theme included the following:

i) Most of the firms had not carried out reviews of their system of quality control, or cold reviews of audit files on a cyclical basis as required by ISQC 1. For some firms the internal quality control reviews were either undertaken by persons who did not have the appropriate authority to sign audit reports or were insufficient:

- the monitoring reviews only covered the engagement reviews and did not cover the review of the firm's system of quality control;
- there were no written procedures on how the engagement and quality control reviews were carried out;
- there were no recommendations on the engagement files reviewed;
- no documented evidence of any evaluation of the effects of the deficiencies noted by the monitor;
- no documented evidence that the findings noted on the review had been discussed with engagement partners & appropriate personnel within the firm; and
- there were no conclusions in the reports of the outcome of the monitoring review.

ii) Some firms did not have policies and procedures addressing the following ISQC 1 requirements:

- Those performing the engagement, or the engagement quality control review are not involved in inspecting the engagements;
- The firm shall evaluate the effects of deficiencies noted as a result of the monitoring process and determine whether they are either: instances that do not necessarily indicate that the firm's system of quality control is insufficient to provide it with reasonable assurance that it complies with professional standards and applicable legal and regulatory requirements, and that the reports issued by the firm or engagement partners are appropriate in the circumstances; or systemic, repetitive or other significant deficiencies that require prompt corrective action.

c) *Independence & Ethical Requirements Theme's contribution to total findings:* 11% in 2018; and 17% for the first cycle:

The Independence & Ethical Requirement element contributed 11% to the findings in 2018, and 17% for the first cycle. The entire11% were attributed to Certified Audit Firms of Non - Public Interest Entities.

Common findings in this theme included the following:

i) Some firms did not have documented policies and procedures on their Quality Control manuals on the following as required by ISQC 1:

- policy prohibiting the audit team members from making or assuming responsibility for management decisions for audit client

- policies and procedures to address the accumulation of relevant information on ethical and independence compliance.

ii) Firms provided non-audit services to audit clients, i.e. preparation of financial statements and tax computations and did not document how they managed the independence threat that arises from preparing and auditing the same financial statements.

Engagement Reviews

During 2018, a total of twenty-six (26) engagement reviews under the responsibility of thirteen (13) practitioners across nine (9) audit firms were carried out. During the first cycle a total of eighty-six (86) engagements under the responsibility of forty-five (45) practitioners across twenty-eight (28) audit firms have been undertaken.

The results of the review of practitioners and the total number of findings, split between Certified Auditors of Public Interest Entities and Certified Auditors of Non-Public Interest Entities are provided in Table B below:

Table B: Summary of Firm and Engagement Review Results for Certified Auditors of Public Interest Entities and Certified Auditors of Non-Public Interest Entities

DESCRIPTIONS	2018			First Cycle (2015 – 2017)		
	AUDITORS OF PUBLIC INTEREST ENTITIES	**AUDITORS OF NON - PUBLIC INTEREST ENTITIES**	**TOTAL**	**AUDITORS OF PUBLIC INTEREST ENTITIES**	**AUDITORS OF NON - PUBLIC INTEREST ENTITIES**	**TOTAL**
NUMBER OF FIRMS	**1**	**8**	**9**	**10**	**18**	**28**
Total Number of Partners	2	11	**13**	32	20	**52**
Total Number of Attest Partners Reviewed	2	11	**13**	27	18	**45**
Total Number of Attest Clients (Total practitioners client Portfolio)	70	255	**325**	1,358	387	**1,745**
Total Number of Attest (Assurance) Engagements Reviewed	4	22	**26**	52	34	**86**
Total Number of Findings	45	267	**312**	221	490	**711**
Average number of findings per Attest Partner	23	24	**24**	8	27	**16**
Attest Partner Rating:						
1. Satisfactory	1	5	**6**	24	6	**30**
2. Unsatisfactory	1	6	**7**	3	12	**15**
Total Attest Partners	**2**	**11**	**13**	**27**	**18**	**45**
Firm Ratings:						
1. Satisfactory	0	2	**2**	**7**	**6**	**13**
2. Unsatisfactory	1	6	**7**	**3**	**12**	**15**
Total Firms	**1**	**8**	**9**	**10**	**18**	**28**

As will be noted from Table B above, of the total of thirteen (13) Certified Auditors reviewed in 2018, the performance of one (1) Certified Auditor of Public Interest Entities and five (5) Certified Auditors of Non-Public Interest Entities were "Satisfactory" while the performances of the other Certified Auditor of Public Interest Entities and six (6) Certified Auditors of Non-Public Interest Entities were "Unsatisfactory". For the first cycle, of the total of forty-five (45) Certified Auditors reviewed, twenty-four (24) Certified Auditors of Public Interest Entities and six (6) Certified Auditors of Non-Public Interest Entities) were "Satisfactory". This meant that twelve (12) Certified Auditors of Non-Public Interest Entities and three (3) Certified Auditors of Public Interest Entities were "Unsatisfactory".

Engagement Review Results: Analysis by Audit Area (IFIAR Inspection Theme Findings)

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 one of the seventeen (17) Audit Inspection Themes (audit areas) provided by the IFIAR for the 2018 Survey. These were in turn split between Certified Auditors of Public Interest Entities and Certified Auditors of Non-Public Interest Entities. The results are provided in Table C below:

Table C: Engagement Review Findings split by IFIAR Inspection Themes

IFIAR INSPECTION THEMES	2018 — CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES: Total Findings	2018 — CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES: Total Findings as a % of findings for all Engagements	2018 — CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES: Total Findings	2018 — CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES: Total Findings as a % of findings for all Engagements	2018 — TOTAL AUDIT ENGAGEMENTS: Total Findings	2018 — TOTAL AUDIT ENGAGEMENTS: Total Findings as a % of findings for all Engagements	FIRST CYCLE (2015 - 2017) — CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES: Total Findings	FIRST CYCLE (2015 - 2017) — CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES: Total Findings as a % of findings for all Engagements	FIRST CYCLE (2015 - 2017) — CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES: Total Findings	FIRST CYCLE (2015 - 2017) — CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES: Total Findings as a % of findings for all Engagements	FIRST CYCLE (2015 - 2017) — TOTAL AUDIT ENGAGEMENTS: Total Findings	FIRST CYCLE (2015 - 2017) — TOTAL AUDIT ENGAGEMENTS: Total Findings as a % of findings for all Engagements
Group Audits	0	0%	0	0%	**0**	**0%**	1	0%	1	0%	**2**	**0%**
Internal Control Testing	0	0%	0	0%	**0**	**0%**	0	0%	1	0%	**1**	**0%**
Adequacy of Financial Statement Presentation and Disclosures	7	2%	28	9%	**35**	**11%**	65	9%	71	10%	**136**	**19%**
Use of Experts/Specialists	0	0%	0	0%	**0**	**0%**	0	0%	1	0%	**1**	**0%**
Substantive Analytical Procedures	0	0%	0	0%	**0**	**0%**	2	0%	8	1%	**10**	**1%**
Audit Committee Communication	0	0%	0	0%	**0**	**0%**	2	0%	0	0%	**2**	**0%**
Fraud Procedures	0	0%	4	1%	**4**	**1%**	7	1%	24	3%	**31**	**4%**
Risk Assessment	0	0%	8	3%	**8**	**3%**	5	1%	18	3%	**23**	**3%**
Audit Report	2	1%	17	5%	**19**	**6%**	8	1%	17	2%	**25**	**4%**
Accounting Estimates, including Fair Value Measurement	10	3%	7	2%	**17**	**5%**	1	0%	10	1%	**11**	**2%**
Revenue Recognition	0	0%	2	1%	**2**	**1%**	0	0%	5	1%	**5**	**1%**

IFIAR INSPECTION THEMES	2018					
	CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES		TOTAL AUDIT ENGAGEMENTS	
	Total Findings	Total Findings as a % of findings for all Engagements	Total Findings	Total Findings as a % of findings for all Engagements	Total Findings	Total Findings as a % of findings for all Engagements
Inventory Procedures	0	0%	1	0%	**1**	**0%**
Related Party Transactions	3	1%	15	5%	**18**	**6%**
Engagement Quality Control Reviewers ("EQCR")	0	0%	0	0%	**0**	**0%**
Going Concern	2	1%	2	1%	**4**	**1%**
Adequacy of Review and Supervision	45	14%	149	48%	**194**	**62%**
Audit Sampling	2	1%	8	2%	**10**	**3%**
Audit of Allowance for Loan Losses and Loan Impairments	N/A					
Other Areas/Topics	N/A					
TOTAL FINDINGS	**71**	23%	**241**	77%	**312**	**100%**

IFIAR INSPECTION THEMES	FIRST CYCLE (2015 - 2017)					
	CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES		CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES		TOTAL AUDIT ENGAGEMENTS	
	Total Findings	Total Findings as a % of findings for all Engagements	Total Findings	Total Findings as a % of findings for all Engagements	Total Findings	Total Findings as a % of findings for all Engagements
Inventory Procedures	1	0%	3	0%	**4**	**1%**
Related Party Transactions	16	2%	18	3%	**34**	**5%**
Engagement Quality Control Reviewers ("EQCR")	3	0%	0	0%	**3**	**0%**
Going Concern	4	1%	8	1%	**12**	**2%**
Adequacy of Review and Supervision	98	14%	263	37%	**361**	**51%**
Audit Sampling	5	1%	21	3%	**26**	**4%**
Audit of Allowance for Loan Losses and Loan Impairments	0	0%	2	0%	**2**	**0%**
Other Areas/Topics	3	0%	19	3%	**22**	**3%**
TOTAL FINDINGS	**221**	**31%**	**490**	**69%**	**711**	**100%**

Note: "N/A": In 2016, new themes were introduced, while others previously used in 2015 were either renamed or combined with others
"*" Total findings for all firms

241 (77%) of the 312 total findings for 2018 were for Certified Auditors of Non-Public Interest Entities, while the remaining 71 (23%) were for Certified Auditors of Public Interest Entities. In the first cycle, of the 711 findings, 490 (69 %) relate to Certified Auditors of Non-Public Interest Entities while 221 (31%) are for Certified Auditors of Public Interest Entities.

Most of the findings in the 2018 reviews were in the theme of 'Adequacy of Review and Supervision' (62%), split between Certified Auditors of Non-Public Interest Entities (48%) and Certified Auditors of Public Interest Entities (14%). This was followed by the 'Adequacy of Financial Statement Presentation and Disclosures' theme with (11%) of the findings, split between Certified Auditors of Non-Public Interest Entities (9%) and Certified Auditors of Public Interest Entities (2%).

This was also the case during the first cycle, as most of the findings related to the theme of 'Adequacy of Review and Supervision' (51%), split between Certified Auditors of Non-Public Interest Entities (37%) and Certified Auditors of Public Interest Entities (14%). This was followed by the 'Adequacy of Financial Statement Presentation and Disclosures' theme (19%), split between Certified Auditors of Non-Public Interest Entities (10%) and Certified Auditors of Public Interest Entities (9%).

The findings for the themes with the highest percentage contributions to the engagement review findings are further analysed below:

a) <u>Adequacy of Review and Supervision Theme's contributions: 62% in 2018; and 51% for the first cycle:</u>

Common findings noted under this theme included:

i) During the identification and assessment of the risks of material misstatement due to fraud, the auditors turn not to make a presumption that there is an inherent risk of fraud in revenue recognition as required by International Standards on Auditing (ISAs); nor do they document that this presumption was not applicable.

ii) No documented evidence that the auditors had evaluated the design of the related controls, including the relevant control activities, and the implementation thereof, in respect of the significant risks identified.

iii) Areas considered to be significant to the financial statements as a whole, not identified as such at planning stage and therefore no documentation of audit work undertaken to understand the information systems, including the related businesses processes, relevant to financial reporting for these classes of transactions.

iv) Inquiries of management and those charged with governance on fraud were not documented, i.e. their knowledge of any actual, suspected or alleged fraud; their assessment of fraud risk and processes to identify and respond to fraud risk; management's communications to those charged with governance regarding processes for identifying and responding to the risks of fraud in the entity; and management's communication, if any, to employees regarding its views on business practices and ethical behaviour.

v) No documented evidence of the audit procedures performed by the auditors to identify any litigation and claims involving the entity which may give rise to a risk of material misstatement.

vi) No documented evidence that the practitioners had determined the amount below which misstatements were regarded as clearly trivial.

vii) Evidence of audit work carried out on material balances stated in the financial statements was either inadequate or was not documented altogether. In some cases, the auditors had indicated on the working papers that the samples were traced to various supporting documents, however the identifying characteristics of those supporting documents were not documented.

viii) No documented evidence of the sampling plan which the auditors had used to determine sample sizes; and to select sample items for detailed testing.

ix) No documented evidence that the auditor had evaluated managements' assessments, if any, of useful lives and residual values of Property, Plant & Equipment.

x) Insufficient audit work carried out on Related Parties as there was no documented evidence that the auditors had enquired from management, the identity of related parties, nature of the relationship & type and purpose of the transactions. There was also no documented evidence that the auditors had considered the adequacy of control activities over the authorization and recording of related party transactions as part of obtaining an understanding of the entities' internal controls and it was further noted that some related party balances/transaction were not disclosed at all on the financial statements or were disclosed at various notes, not under the Related Parties Note for easier user reference.

xi) No documented evidence of audit work performed on dividends paid. There were no audit working papers on file confirming that the solvency test had been undertaken to ensure compliance with the Companies Act requirements and there were also no accounting policies on dividend payments disclosed in the financial statements.

xii) Financial assets not sufficiently and appropriately assessed for impairment.

xiii) No documented evidence that confirmations of related party balances, bank balances, long term liabilities had been requested and/or received.

xiv) No documented evidence of any journal entry testing carried out 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.

xv) Consideration of the effect of uncorrected misstatements, if any, related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements was not documented in the audit files.

xvi) Analytical procedures not performed at end of audit to assist in forming the overall conclusions on consistency of financial statements with the auditor's understanding of the entities.

xvii) No documented evidence of any subsequent events procedures carried out.

xviii) Documentation of some audit work undertaken by the auditors on some account balances were not assembled timely.

b) <u>Adequacy of Financial Statement Presentation and Disclosures: 11% in 2018; 19% for the first cycle:</u>

As a general observation, the quality of review of financial statements continues to be a matter of concern as practically all financial statements reviewed had numerous disclosure deficiencies of varying magnitudes; which could mislead the users of financial statements. These deficiencies included the following:

i) Material misstatements of disclosures in the financial statements, i.e. discrepancies between balances disclosed on the notes and balances disclosed on the face of the four main statements in the financial statements.

ii) Comparative disclosures for each class of Property, Plant and Equipment (PPE), i.e. a reconciliation of the carrying amount at the beginning of the period showing additions, disposals, depreciation and any other changes not disclosed in the financial statements.

iii) Disclosures in the financial statements of some entities showed that the entities held shares in subsidiaries, however, consolidated financial statements were not prepared and presented. There were no disclosures in the financial statements, as to why consolidated financial statements had not been prepared or whether the conditions for exemption from preparation of consolidated financial statements as per requirements of the International Financial Reporting Standards (IFRSs) had been met.

iv) Disclosures on inventories were not fully compliant with the disclosure requirements of IAS 2.

v) Balances in the financial statements were incorrectly classified.

vi) Disclosures for leases not made in accordance with the requirements of IAS 17.

vii) Incorrect/inadequate accounting policies:

- the accounting policies on financial instruments did not include a list of all the financial instrument categories for financial assets and liabilities the entities had, and the related accounting policies as required by IFRSs;

- no accounting policies on significant balances disclosed in the financial statements; and

- accounting policies that were considered not to be relevant based on the nature of the businesses were disclosed in some financial statements.

viii) Incorrect/no cross referencing between the main financial statements and the notes.

ix) Disclosures in the notes not casting to balances indicated as totals in the financial statements.

x) New standard and interpretations disclosures were incomplete and the impact the new standards would have on the financial statements not disclosed.

c) <u>Other areas of concern</u>

The following themes, even though they did not have the highest percentage contributions to the engagement findings were considered to be of concern:

i) *Going Concern*

Insufficient procedures appear to be carried out in this area especially when events or conditions exist that may cast significant doubt on the entity's ability to continue as a going concern. Additional procedures are required to be performed when such events or conditions are identified, these include:

- Where management has not yet performed an assessment of the entity's ability to continue as a going concern, the auditor should request management to make this assessment.

- Evaluating management's plans for future actions in relation to its going concern assessment.

- Where the entity has prepared a cash flow forecast, the auditor is required to interrogate the forecast:

  ~ Evaluating the reliability of the underlying data generated to prepare the forecast; and

- ~ Determining whether there is adequate support for the assumptions underlying the forecast.

- Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans.

- Based on the audit evidence obtained, the auditor shall conclude whether, in the auditor's judgment, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and:

  - ~ Ensure financial statements adequately disclose this fact and that the entity may be unable to realize its assets and discharge its liabilities in the normal course of business;

  - ~ The auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern and this should be referenced to the note in the financial statements that discloses the matters set out in this paragraph;

  - ~ If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall express a qualified opinion or adverse opinion, as appropriate, in accordance with ISA 705 (Revised).

  - ~ the auditor shall communicate with those charged with governance events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern.

ii) *Audit Report*

Practitioners continue to issue numerous modified audit opinions on audits of financial statements without fully following the audit procedures outlined in ISA 705 (Revised), "**Modifications to the Opinion in the Independent Auditor's Report".** These procedures include the following:

- Auditors are expected to quantify and disclose the amounts relating to misstatements in the 'Basis for *Modified* Opinion' section;

- If material misstatements relate to qualitative disclosures, an explanation of how the disclosures are misstated should be disclosed and if material misstatements relate to the non-disclosure of information required to be disclosed paragraph 23 lists procedures that need to be performed.

- If modification is due to the inability to obtain sufficient appropriate audit evidence, the auditor shall include in the 'Basis for *Modified* Opinion' section the reasons for that inability and also the fact that it was not possible to use alternative procedures.

- Auditors are also required to communicate with Those Charged with Governance the circumstances that led to the expected modification and the wording of the modification.

As this area seem to be a difficult and contentious matter, auditors should consider making appropriate consultations before making a decision to modify their audit opinions.

Summary of Audit Practice Review Findings and Decisions

The Engagement Performance element of an audit firm's system of quality control tends to have the most significant impact on the overall performance in a firm review. Therefore, all audit practices with engagement practitioners whose performance was "Unsatisfactory" in engagement review also attained an "Unsatisfactory" rating in the Engagement Performance element of the firm review; and consequently, attained an "Unsatisfactory" rating in the overall audit practice review.

In line with the Authority's audit practice review methodology, which is explained in more detail at page 5, issuance of a single inappropriate audit opinion, irrespective of the practitioner's or other practitioners' performances on other engagements, is indicative of serious deficiencies in the firm's overall system of quality controls. Therefore, in such circumstances, both the practitioner's performance and that of the whole firm is assessed to be unsatisfactory.

Of the nine audit firm reviews undertaken during 2018, two (2) (22%) attained a "Satisfactory" rating while six (6) (67%) attained an "Unsatisfactory" rating with a recommendation for a re-review; one (1) (11%) attained an 'Unsatisfactory' rating for the third time in a row and the certificate of the practitioner of this firm's is likely to be revoked in line with the BICA three strikes rule. (See table B above). Three (3) of these nine (9) firms were re-reviews and two (2) of the three (3) still obtained unsatisfactory results.

Twenty-eight (28) firms were reviewed during the first cycle. Thirteen (13) (46%) of these attained a 'Satisfactory' rating; eleven (11) (39%) attained 'Unsatisfactory' rating and were recommended to be re-reviewed; four (4) (15%) attained an 'Unsatisfactory' rating for the third time in a row and three (3) of the practitioners' certificates were revoked in line with the BICA three strikes rule while one (1) is pending the final outcome from BICA. (See table B above)

The Authority, however, wishes to emphasize that the primary objective of 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. Deregistration of an audit practitioner or firm is a last resort and will only be considered if an audit firm/practitioner fails three reviews consecutively, and it is determined that there is little prospect of an audit firm/practitioner improving in the short-term, in order to meet the minimum performance standards; or if the performance of a firm or practitioner, even if at first or second review, is considered so bad that continued practice would put public interest or those for whom the audit reports are intended, at significant risk.

Conclusion

Based on the results of the audit practice reviews undertaken by the Authority in 2018, it is evident that audit firms need to improve their systems of quality controls, particularly the Engagement Performance, Monitoring and Independence & Ethical elements.