



SUMMARY OF AUDIT PRACTICE REVIEWS

FOR THE YEAR ENDED DECEMBER 31, 2015

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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 first Audit Practice Review Committee summarised report on audit practice reviews covering the year ending December 31, 2015. This comes after more than two years of preparatory work following the launch of the Authority.

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 29, 2016

SUMMARISED AUDIT PRACTICE REVIEW REPORT FOR THE YEAR ENDED DECEMBER 31, 2015

AUDIT PRACTICE REVIEWS

INTRODUCTION

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

The Authority has adopted a three-year inspection cycle, whereby all audit firms and their practitioners should be reviewed within the three-year cycle period.

Each audit practice review consists of a firm review and an engagement review for each practitioner, intended to provide the Authority with reasonable assurance that the firm and its personnel comply with International Standards on Auditing (ISA) and applicable legal and regulatory requirements; and that reports issued by the firm or engagement partners are appropriate in the circumstances.

A firm or quality control review aims to ensure that a firm's Quality Control Policies and Procedures are operating effectively and comply with International Standard on Quality Control 1 (ISQC1).

An engagement review consists of a selection of audit engagements and aims to obtain reasonable assurance that attest engagement partners in the firm comply with International Standards on Auditing (ISA) and other relevant professional standards, in the performance of audits.

PROCESS OF APPROVAL OF AUDIT PRACTICE REVIEW REPORTS

In terms of its audit practice review mandate, the Authority is responsible for 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), whereby the Authority will undertake audit practice reviews of 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 audit firms and certified auditors in Botswana.

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 inspections are determined in terms of predetermined criteria applicable to the inspection cycle. The APRC's final decision would be one of the following:

- Satisfactory, meaning an inspection only in the next cycle;
- Unsatisfactory, meaning some matters still require attention before a satisfactory result can be achieved and a follow-up inspection will be scheduled; or
- Referral to the Enforcement Committee, which could then attract possible sanctions by the Committee.

Audit practice review reports for 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 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.

An audit firm or audit practitioner will be deregistered if their performance in an inspection 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.

AUDIT PRACTICE REVIEWS UNDERTAKEN IN 2015

Overview of Audit Practice Reviews

On the basis of the three-year audit inspection cycle adopted by the Authority, 8 audit firms and their certified auditors were reviewed during 2015, while 8 and 12 are planned to be reviewed in 2016 and 2017, respectively. 3 of the 8 firms reviewed in 2015 were Audit Firms of Public Interest Entities, while 5 were Audit Firms of Non-Public Interest Entities.

The Audit Practice Review Committee met three times during 2015 to review audit practice review reports submitted to it by the Technical Department on the 8 audit firms reviewed during the year. After reviewing the reports of the Technical Department, the Audit Practice Review Committee resolved that the performance of 5 audit firms was "Satisfactory", while that of 3 audit firms was "Unsatisfactory".

The Authority is a member of the International Forum of Independent Audit Regulators (IFIAR). Each year, members of the IFIAR, the Authority included, are invited to participate in the Forum's Survey of Inspection Findings in which member countries are required, among others, to classify findings into Inspection Themes provided by the IFIAR. The Authority participated in the 2015 Survey of Inspection Findings, and classified all findings arising from the firm review of the 8 audit firms into the 6 elements of the ISQC 1 System of Quality Control, which the IFIAR termed "Inspection Themes". Similarly, all findings arising from the audit practitioner engagement reviews were classified into 15 IFIAR Engagement Review Inspection Themes.

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

Firm Reviews

A firm review consists of an examination of the 6 elements of a firm's system of Quality Control Policies and Procedures, intended to ensure that the system conforms in all material respects to the standard requirements of the International Standard on Quality Control 1 (ISQC 1).

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 the International Standard on Quality Control 1 (ISQC 1).

All deviations from the requirements of ISQC 1 were noted as “findings” and were allocated to their respective ISQC 1 element.

A total of 8 audit firms were reviewed, of which 3 were Audit Firms of Public Interest Entities and 5 being Audit Firms of Non-Public Interest Entities. All 3 Audit Firms of Public Interest Entities attained a “Satisfactory” rating. However, of the 5 Auditors of Non- Public Interest Entities, two were “Satisfactory”, while 3 were “Unsatisfactory”. These ratings were based on the findings explained in more detail below.

There were a total of 30 Firm Review findings, of which 5 were in respect of Audit Firms of Public Interest Entities, while 25 were for Audit Firms of Non-Public Interest Entities.

Provided in Table A below are the findings allocated to each ISQC 1 element (IFIAR Theme), split between audit firms of Public Interest Entities and Audit Firms of Non-Public Interest Entities:

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

ELEMENT OF SYSTEM OF QUALITY CONTROL (IFIAR INSPECTION THEMES)	FINDINGS RELATING TO AUDIT FIRMS OF PUBLIC INTEREST ENTITIES		FINDINGS RELATING TO AUDIT FIRMS OF NON-PUBLIC INTEREST ENTITIES		FINDINGS RELATING TO ALL 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)	0	0	2	7	2	7
Independence and Ethical Requirements	0	0	5	17	5	17
Client Risk Assessment, Acceptance and Continuance	0	0	1	3	1	3
Human Resources	2	7	5	17	7	24
Engagement Performance	3	10	8	26	11	36
Monitoring	0	0	4	13	4	13
TOTAL FINDINGS	5	17	25	83	30	100

As will be noted in the Table A, the Human Resources and Engagement Performance elements (IFIAR Themes) recorded the highest number of findings in the firm reviews. These are further discussed below.

Common Firm Review Findings

Based on the analysis in Table A above, most findings were noted in Engagement Performance and Human Resources elements, albeit fewer for Audit Firms of Public Interest Entities. Details of the specific findings under these areas/themes are as follows:

a) Engagement Performance: 36% of total findings

The majority of the findings (36%) were recorded in the area of Engagement Performance. Audit Firms of Public Interest Entities accounted for 10% of the findings, while audit firms of Non-Public Interest Entities accounted for the remainder of 26%. This is an indication that all audit firms need to improve their quality control systems, particularly in this area, albeit in varying degrees. Some of the deficiencies noted included the following:

- i) non-compliance with relevant accounting and auditing standards;
- ii) insufficient or totally no consultation undertaken on contentious or difficult subject matters, prior to issuance of audit reports;
- iii) Engagement Quality Control Reviewer not having appropriate expertise and experience to perform the role of Engagement Quality Control Reviewer; and
- iv) firms not having documented policies and procedures on destruction/retention of engagement documentation.

b) Human Resources: 24% of total findings

The Human Resources element recorded the second highest number of findings, at 24%, with Audit Firms of Public Interest Entities contributing 7% of the findings; and Audit Firms of Non-Public Interest Entities contributing the balance of 17%.

Among the findings were the following:

- i) operational effectiveness of some of the firms' human resources policies were found to be weak mainly because the understanding of the firms' policies by their staff was inadequate;

- ii) no documented evidence that staff had been provided with adequate Continuous Professional Development (CPD) training to enable them to undertake their work effectively;
 - iii) policies and procedures that ensure that staff with the necessary competence and capabilities are allocated to engagements were not operating effectively; and
 - iv) there were no documented policies and procedures on clearing new employees for independence prior to joining the firm.
- c) Independence and Ethical Requirements: 17% of total findings

Practically all the findings identified in the Independence & Ethical Requirements IFIAR theme related to Audit Firms of Non-Public Interest Entities. Not only were these findings common in this category; they were also considered significant findings; as the firms involved provided accounting/taxation services to their audit clients whilst not demonstrating that they had put in place adequate safeguards against the self-review threat. They may, therefore, have been in breach of the Code of Ethics for Professional Accountants.

- d) Monitoring: 13% of total findings

2 Audit Firms of Non-Public Interest Entities did not carry out reviews of the firm's system of quality control, or cold reviews of audit files on a cyclical basis as required by ISQC 1. In the absence of such reviews, the firms were unable to detect areas of weakness in the system of quality controls that could contribute to the issuance of inappropriate audit reports.

Engagement Reviews

An engagement review consists of a selection of audit files designed to provide the Authority with reasonable assurance that applicable International Standards on Auditing have been complied with in undertaking audit work, and that audit reports issued by audit practitioners (interchangeably referred to as audit attest partners) are appropriate.

A total of 24 engagement quality reviews under the responsibility of 13 practitioners across 8 audit firms were carried out. 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 the Table B below:

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

DESCRIPTION	AUDITORS OF PUBLIC INTEREST ENTITIES	AUDITORS OF NON-PUBLIC INTEREST ENTITIES	TOTAL
Total Number of Partners (Including Non- Attest practitioners)	12	5	17
Total Number of Attest Practitioners	8	5	13
Total Number of Attest Clients	476	85	561
Total Number of Attest Engagements Reviewed	16	8	24
Total Number of Findings	46	79	125
Findings per Attest Practitioner(average)	6	16	10
ATTEST PRACTITIONER RATING:			
Satisfactory	8	2	10
Unsatisfactory	0	3	3
TOTAL ATTEST PRACTITIONERS	8	5	13

The performances of all 8 Certified Auditors of Public Interest Entities and 2 Certified Auditors of Non-Public Interest Entities were “Satisfactory” while those of 3 Certified Auditors of Non-Public Interest Entities were “Unsatisfactory”

Further analysis is provided below.

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

All deviations from the requirements of: International Standards on Auditing; 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 15 Audit Inspection Themes (audit areas) provided by the IFIAR for the 2015 Survey, split between Certified Auditors of Public Interest Entities and Certified Auditors of Non-Public Interest Entities, as provided in Table C below:

Table C: Engagement Review Findings split by IFIAR Inspection Theme

INSPECTION THEME		FINDINGS RELATING TO CERTIFIED AUDITORS OF PUBLIC INTEREST ENTITIES		FINDINGS RELATING TO CERTIFIED AUDITORS OF NON-PUBLIC INTEREST ENTITIES		FINDINGS RELATING TO 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
1	Group Audits	1	1	0	0	1	1
2	Adequacy of Financial Statement Presentation and Disclosures	18	14	19	15	37	29
3	Audit of Allowance for Loan Losses and Loan Impairments	0	0	2	2	2	2
4	Substantive Analytical Procedures	0	0	1	1	1	1
5	Audit Committee Communication	2	2	0	0	2	2
6	Fraud Procedures	2	2	5	4	7	6
7	Risk Assessment	0	0	1	1	1	1
8	Fair Value Measurements	0	0	5	4	5	4
9	Revenue Recognition	0	0	3	2	3	2
10	Inventory	1	1	1	1	2	2
11	Related Party Transactions	5	4	1	1	6	5
12	Engagement Quality Control Reviewers ("EQCR")	3	2	0	0	3	2
13	Going Concern	4	3	2	2	6	5
14	Adequacy of Review and Supervision	7	6	20	16	27	22
15	Other Areas/Topics	3	2	19	15	22	17
TOTAL FINDINGS		46	37	79	63	125	100

Of the 125 total findings, 46 (37 %) were for Certified Auditors of Public Interest Entities, while 79 (63 %) were for Certified Auditors of Non-Public Interest Entities.

The majority of the findings were in the theme of "Adequacy of Financial Statement Presentation and Disclosures" (29%), split between Certified Auditors of Public Interest Entities (14%) and Certified Auditors of Non-Public Interest Entities (15%). This was followed by the "Adequacy of Review and Supervision" theme with 22 % of the findings, split between Certified Auditors of Public Interest Entities (6%) and Certified Auditors of Non-Public Interest Entities (16%).

Further analysis is provided below:

a) Adequacy of Financial Statements Presentation Theme : 29% of total findings

Common findings in this theme included:

- i) incorrect disclosures of prior period errors; provisions for obsolete stocks and doubtful debts; directors fees; dividends declared after reporting date, which were not treated in accordance with accounting policy; and
- ii) inadequate or no disclosures altogether of, among others: bank securities and guarantees confirmed by banks; items in Statement of Changes in Equity; accounting policy relating to Estimation Uncertainty and material balances; adoption and impact of new standards and interpretations; and material future finance charge commitments on finance lease transactions, which were instead inappropriately recognised in the financial statements.

b) Adequacy of Review and Supervision Theme: 22% of total findings

Common findings in this theme included, among others:

- i) insufficient and/or inadequate audit work in the areas of Revenue, Cost of Sales, Expenditure, Payroll and Inventory;
- ii) insufficient documentation of audit work carried out on unresolved differences in the areas of Trade Payables, Accounts Payables, Related Party balances, and Cash Book/General Ledger;
- iii) no evidence that material accounting estimates relating to: provisions for doubtful debts; and provision for obsolete stock had been tested for reasonableness;
- iv) differences between the auditor's taxation working paper and the client's taxation computations were inconsistent with the auditor's conclusion;
- v) sample items tested were fewer than the sample size items determined as per audit firm's audit methodology;

vi) Related party loans were not sufficiently and appropriately assessed for impairment; and

vii) Loan balances were not directly confirmed with lenders, to enable verification of accuracy of balances, loan terms, as well as identification of contingent liabilities, if any.

c) Other Theme findings

The following findings, while not being common across engagements, were nevertheless considered major:

i) use of Incorrect Framework: On 2 engagements, incorrect frameworks were used; on one, International Standard on Related Services (ISRS) 4400, "Agreed-upon Procedures" was used on an assurance engagement that required use of International Standard on Assurance Engagements (ISAE 3000); while on another where International Financial Reporting Standards for Small and Medium Sized Entities (IFRS for SMEs) Reporting Framework was adopted, Full IFRSs were also applied without justification; and

ii) the Engagement Quality Control Reviewer (EQCR) findings were not documented: On 2 engagements, the EQCR documentation did not reflect details of discussion of significant issues with the engagement partner. On another engagement, there was no documented review by the EQCR of documentation relating to significant judgements made by the engagement team and conclusions reached, nor of evaluation of the conclusion reached by the engagement practitioner in formulating the audit report.

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.

2 practitioners and their firms, whose performance in the audit practice reviews was "Unsatisfactory" are pencilled in for a re-review sometime in 2017.

In accordance with the BICA guidelines, one practitioner and his firm, whose performances were “Unsatisfactory” were subsequently deregistered by BICA on account of their performances having been “Unsatisfactory” three times consecutively, and with little prospect that they could improve in the short term in order to meet the minimum performance standards required.

The Authority, however, wishes to emphasise 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

On the basis of the results of the audit practice reviews undertaken by the Authority in 2015, it is evident that audit firms need to improve their systems of quality controls, particularly the Engagement Performance and Human Resources elements (interchangeably referred to in this case as IFIAR themes). The IFIAR 2015 Survey of Inspection Findings Report also found that the Engagement Performance and Human Resources themes recorded the highest and third highest number of findings, respectively. Specific to the Botswana jurisdiction, it is evident that audit firms will need to significantly improve their quality control systems by, among others, establishing monitoring processes 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 as required by ISQC 1.

The Authority will continue to benchmark its performance standards with those of the IFIAR and its flagship members, in order to ensure that it maintains the highest standards of audit inspections.