

Annual Audit (ISAs) update

Presenter: Bronwyn MacCallum CA(SA)

30 SEPTEMBER 2021

Annual Audit (ISAs) Update

Changes in and updates to the Profession, the Auditing Standards and Ethics

Presenter

Bronwyn MacCallum CA(SA)

Bronwyn qualified as a CA(SA) in 2004 and has spent time in private practice as a partner and later director of small and medium firms as well as a tenure at the Auditor-General of South Africa as a Senior Manager and SAICA Training Officer. Her current professional focus is on the design, implementation and monitoring of systems of quality control in the auditing profession for firms and for engagements.

Bronwyn has also spent many years lecturing Auditing, IFRS and Public Financial Management at undergraduate, post-graduate and professional levels, both face to face and in the design and implementation of blended and on-line learning platforms. Bronwyn has played active roles at both SAICA and IRBA in board sub-committees related to professional practical training and development, and in various public sector governance structures and audit committees.

Bronwyn has significant experience in auditing in the public and private sectors in South Africa, with a focus on audit quality management and auditing and accounting technical considerations. Bronwyn develops and presents CPD and firm-specific training on the auditing standards for South African professionals and for the international profession.



COURSE OUTLINE

Session Objectives

By the end of this event the participant should:

- Conceptually understand the Quality Management Standards and ISAs.
- Be familiar with the new structure of standards.
- Understand the contents of the newest standards on audit quality and identifying and assessing the risk of material misstatement and the auditing of estimates.
- Understand recent amendments to existing ISAs.
- Understand recent publications by the IESBA affecting ethical requirements.

Table of contents

- Overview of IAASB's projects in 2020 and 2021.
- ISQMI, ISQM 2 and ISA220(R) – The new suite of Quality Management Standards
- ISA 315(R) – Identifying and assessing the risk of material misstatement through understanding the entity and its environment
- ISA540(R) – Auditing Accounting Estimates and Related Disclosures
- Unpacking the elements of IRBA's Public Inspections Report and related global trends in quality control review findings
- New pronouncements by the IESBA and their impact on practice management and ethics

INTERNATIONAL STANDARDS ON QUALITY MANAGEMENT

International Standards on Quality Management

- Began in June 2014 in response to various reports and calls for revision relating to audit quality
- Gathered information 2014 – September 2016
- Project proposal in December 2016 - ENHANCING AUDIT QUALITY: PROJECT PROPOSAL FOR THE REVISION OF THE IAASB'S INTERNATIONAL STANDARDS RELATING TO QUALITY CONTROL AND GROUP AUDITS
- Exposure draft approved in December 2018 and published in February 2019
- Comments were due by 1 July 2019
- Standard approved in September 2020
- Pronouncements published in December 2020
- Effective 15 December 2022
- First evaluation by 15 December 2023

International Standards on Quality Management

- The suite of standards comprises:
 - ISQMI: Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements (replacing extant ISQCI)
 - ISQM2: Engagement Quality Reviews (new)
 - ISA220(R): Quality Management for an Audit of Financial Statements (replacing extant ISA220)

ISQM 1: Why?

- Results of the ISA Implementation Monitoring projects
- Declining global audit quality results
- Changes to financial reporting
- The length of time lapsed since ISQCI
- Enabling compliance
- Driving leadership responsibility
- Aligning with projects in ethics, professional scepticism



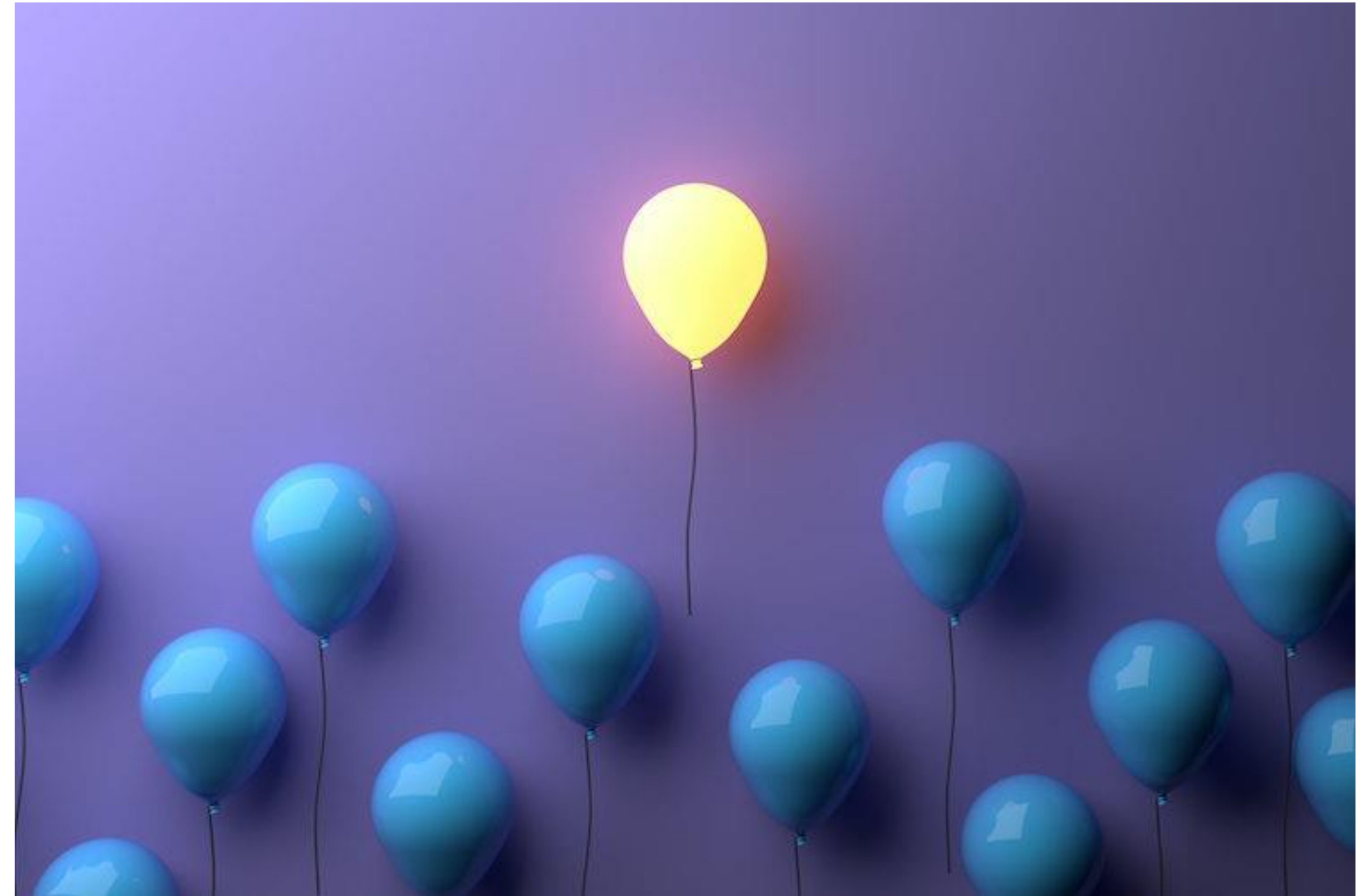
ISQM 1: What?

- Design, implement and operate a system of quality management (SOQM)
- Applicable to audits, reviews or other assurance or related services engagements performed by the firm
- SOQM provides the firm with reasonable assurance that:
 - Firm and personnel fulfil their responsibilities (prof stds, legal & re ethical and independence etc)
 - Engagement reports issued are appropriate in the circumstances
- Enables consistent performance of quality engagements (by achieving the quality objectives)
- Enables serving public interest (through consistently quality engagements)



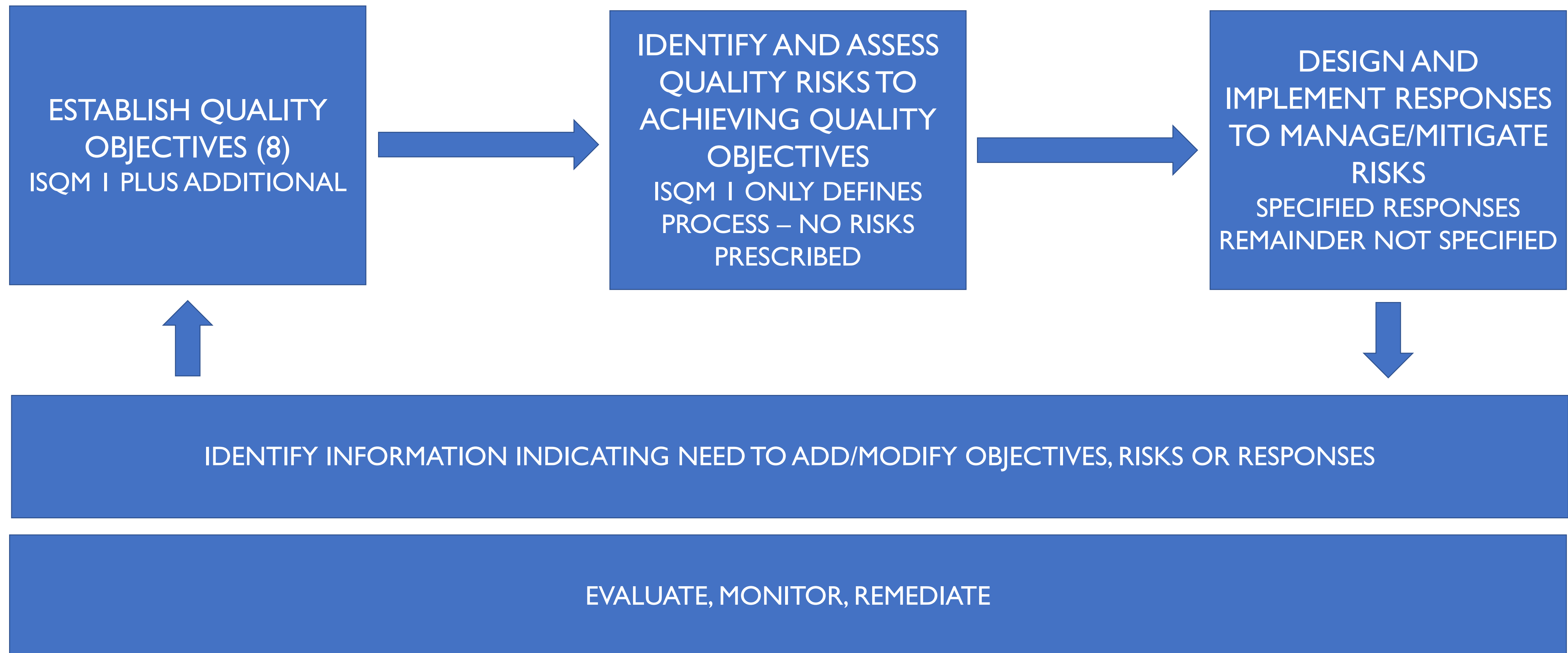
ISQM 1: What?

- Quality **Management** vs Quality Control
- **System** of quality management
- Proactive, **risk-based approach** vs linear, compliance driven approach
- **Scalability**
- **Integrative** (vs stand-alone P&P)
- **Iterative** (management)
- More **robust** requirements for:
 - Leadership and governance
 - Resources (expanded)
 - Service providers
 - Monitoring and evaluation

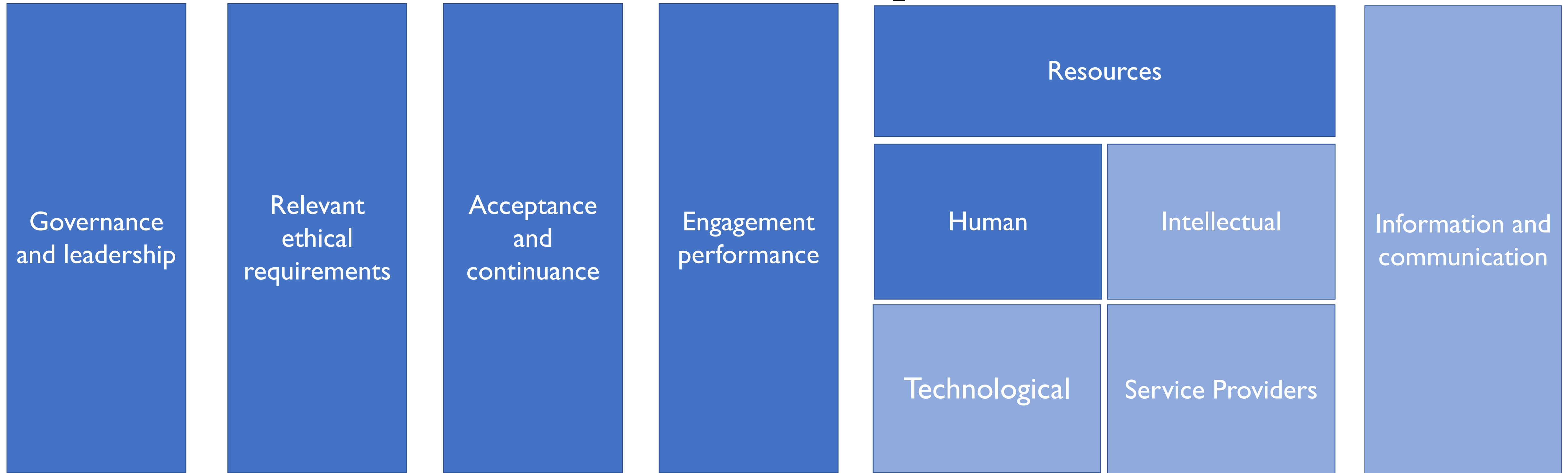


ISQM 1: System of Quality Management

Risk-based approach to quality management



ISQM 1: Components



CONTINUAL, ITERATIVE, INTERRELATE, OVERLAP

EG GOVERNANCE AND LEADERSHIP AND RELEVANT ETHICAL REQUIREMENTS / EG RECOURCFES AND ENGAGEMENT PERFORMANCE

RESPONSES TO RISKS IN ONE COMPONENT MAY CREATE A RISK IN ANOTHER

ONE TO ONE, ONE TO MANY, MANY TO MANY RELATIONSHIPS BETWEEN OBJECTIVES, RISKS AND RESPONSES

Risk assessment process

A process established by the firm as part of the SOQM

1: Establish quality objectives

2: Identify quality risks

3: Assess quality risks

4: Design risk responses

5: Specified responses

6: Implement risk responses



1: Relevant quality objectives

2: Events, circumstances, conditions and actions

3: Possibility of occurrence; adverse effect on objectives

4: Policy, procedure, time, responsibility, POE

5: Incorporate into responses

6: SOQM and evidence of implementation

Quality Objectives

- **Firm objective:** Design, implement and operate a SOQM
- **SOQM objective:** personnel fulfil their responsibilities, engagement reports are appropriate
- **Quality objective:** The desired outcomes in relation to components of the system of quality management to be achieved by the firm
- **Outcome based**
- Assist in the proper **identification and assessment of quality risks** (more focused consideration of “what can go wrong”)
- Establishing quality objectives includes consideration (and documentation) of when a quality objective might not be relevant
- Comprehensive and relevant descriptions of objectives (SMART principles – quality of implementation)
- Establishment of sub-objectives (optional) (eg for “operating units” and related resources/independence requirements/engagement performance requirements)
- Establishment of **additional objectives** (uncommon, but responsive to the nature and circumstances of the firm)

Governance and leadership

Establishes the environment in which the SOQM operates

Examples of objectives

The firm demonstrates a commitment to quality through a culture that exists throughout the firm...

- Serving public interest by consistently performing quality engagements
- The importance of professional ethics, values and attitudes
- The responsibility of all personnel for quality relating to the performance of engagements or activities within the system of quality management, and their expected behaviour; and
- The importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities.

The organizational structure and assignment of roles, responsibilities and authority is appropriate to enable the design, implementation and operation of the firm's system of quality management.

Resource needs, including financial resources, are planned for and resources are obtained, allocated or assigned in a manner that is consistent with the firm's commitment to quality.

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Relevant ethical requirements

Specific topic fundamental for engagement performance
Personnel and others fulfil relevant ethical requirements

Examples of objectives

The firm shall establish the following quality objectives that address the fulfilment of responsibilities in accordance with relevant ethical requirements, including those related to independence:

- (a) The firm and its personnel: (and others – networks, service providers)
 - (i) Understand the relevant ethical requirements to which the firm and the firm's engagements are subject; and
 - (ii) Fulfil their responsibilities in relation to the relevant ethical requirements to which the firm and the firm's engagements are subject.

Acceptance and continuance

Specific topic fundamental for engagement performance
Judgments about whether to accept/continue a
relationship/engagement

Examples of objectives

Judgments by the firm about whether to accept or continue a client relationship or specific engagement are appropriate based on:

- (i) Information obtained about the nature and circumstances of the engagement and the integrity and ethical values of the client (including management, and, when appropriate, those charged with governance) that is sufficient to support such judgments; and
- (ii) The firm's ability to perform the engagement in accordance with professional standards and applicable legal and regulatory requirements.

The financial and operational priorities of the firm do not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement.

Engagement performance

Specific topic fundamental for engagement performance

Promoting consistent quality engagements

Supporting professional judgment and scepticism

Examples of objectives

Engagement teams understand and fulfil their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement.

The nature, timing and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement teams, and the work performed by less experienced engagement team members is directed, supervised and reviewed by more experienced engagement team members.

Engagement documentation is assembled on a timely basis after the date of the engagement report, and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, or professional standards.

Resources

Enables operation of other components

Obtaining, developing, using, maintaining, allocating and assigning
resources

Human Resources

Examples of objectives:

Individuals are obtained from external sources (i.e., the network, another network firm or a service provider) when the firm does not have sufficient or appropriate personnel to enable the operation of firm's system of quality management or performance of engagements.

Engagement team members are assigned to each engagement, including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements.

Individuals are assigned to perform activities within the system of quality management who have appropriate competence and capabilities, including sufficient time, to perform such activities.

Technological Resources

Objective:

Appropriate technological resources are **obtained or developed, implemented, maintained,** and used, to enable the operation of the **firm's system of quality management** and the **performance of engagements.**

Intellectual Resources

Objective:

Appropriate intellectual resources are obtained or developed, implemented, maintained, and used, to enable the operation of the firm's system of quality management and the consistent performance of quality engagements, and such intellectual resources are consistent with professional standards and applicable legal and regulatory requirements, where applicable.

Resources: Service providers

Objective:

Human, technological or intellectual resources from service providers are appropriate for use in the firm's system of quality management and in the performance of engagements, taking into account the quality objectives in paragraph 32 (d),(e),(f) and (g). (Ref: Para.A105–A108)

- Leadership responsibilities cannot be outsourced

Information and Communication

Enables operation of other components

Obtaining, generating or using SOQM information

Communication – internal and external stakeholders

Examples of objectives:

The **information system** identifies, captures, processes and maintains **relevant and reliable information that supports the system of quality management**, whether from internal or external sources.

The culture of the firm recognizes and reinforces **the responsibility of personnel to exchange information** with the firm and with one another.

Relevant and reliable **information is exchanged** throughout the firm and with engagement teams,

Monitoring and remediation process

A process established by the firm as part of the SOQM
Provides information about the design, implementation and
operation of the SOQM
Addresses taking appropriate actions to respond to deficiencies
and remediate on a timely basis

Identification and assessment of quality risks

Risks that may adversely affect the achievement of quality objectives

AND HAS BOTH a reasonable possibility of

- Occurring
- Individually, or combined, adversely affecting the achievement of one or more quality objectives

Not all risks are quality risks – hence threshold above
Quality risks are assessed at an OBJECTIVE level (not a sub-objective level)

Identification and assessment of quality risks

Risk identification and assessment:

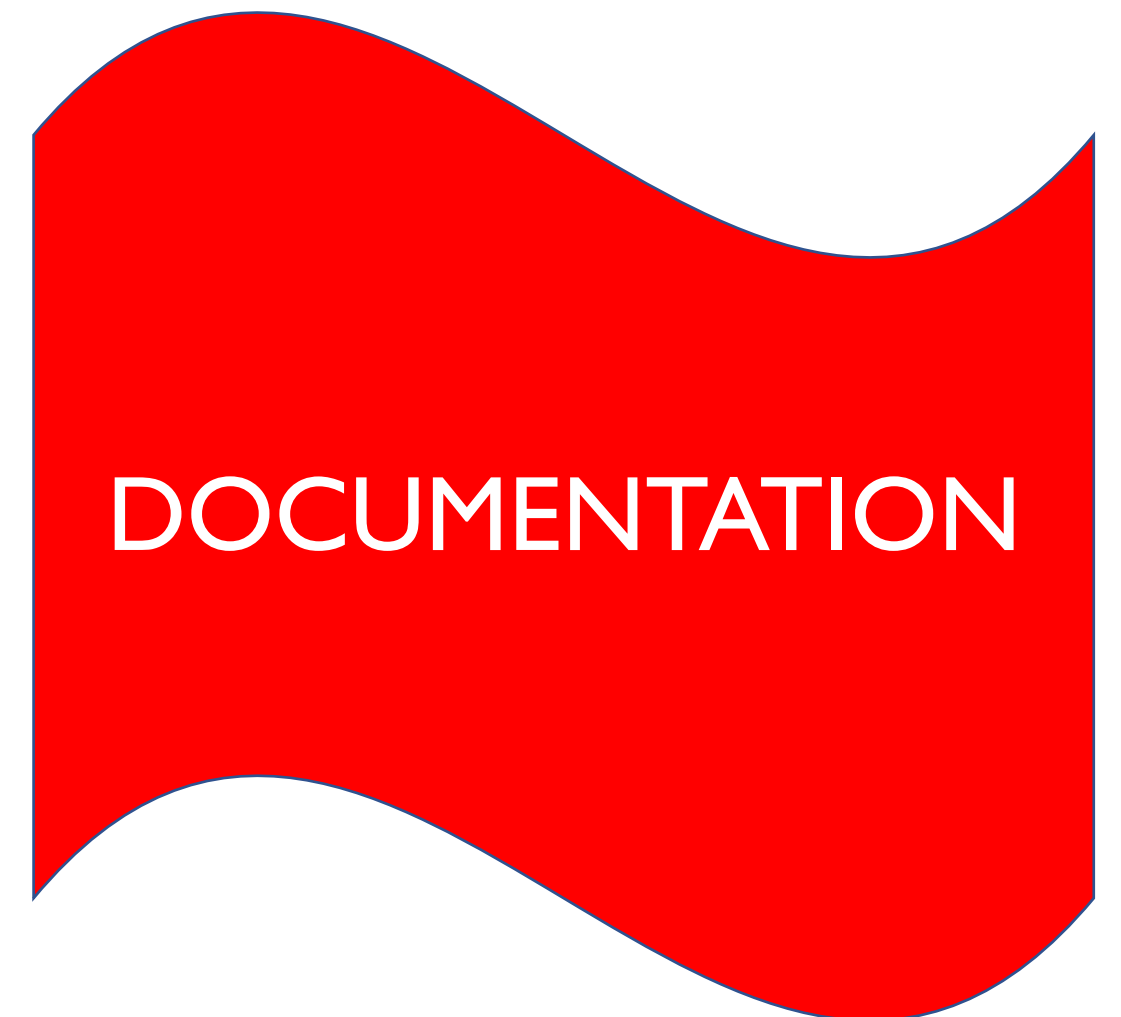
1. Obtain an **understanding** of the **conditions, events, circumstances, actions or inactions** that may adversely affect the achievement of quality objectives
2. Identify and assess quality risks
 1. Which risks have a reasonable possibility of
 1. Occurring
 2. Individually, or in combination, adversely affecting the achievement of one or more quality objectives

Taking into account **how, and the degree to which**, the conditions, events, circumstances, actions or inactions may adversely affect the achievement of quality objectives
3. = Quality risks that have been assessed (ito occurrence and effect)

Identification and assessment of quality risks

Conditions, events, circumstances, actions/inactions: (at least)

- The strategic and operational decisions and actions, business processes and business model
 - The firm's overall financial goals and how these are achieved (professional services provided)
 - Operating complexity (branches, mergers etc)
- Characteristics and style of management and leadership
- Resourcing, including resources provided by service providers
- Law, regulation, professional standards and the environment in which the firm operates
- Nature and extent of network requirements and network services
- Types of engagements performed and the reports to be issued
 - Audit/Review/Compilation/AUP/ISAE3000
- Types of activities for which engagements are undertaken
 - Nature of the clients and the client base (PIEs, complexity, specialist fields, other legal and regulatory reporting requirements, management integrity risks)



Identification and assessment of quality risks

How, and the degree to which...

1. HOW the (C,E,C,A/I) would affect the achievement of the quality objective
2. HOW FREQUENTLY it is expected to occur
3. HOW LONG it would take after occurrence to have an effect
4. WHETHER the firm would have time detect and to mitigate
5. HOW LONG the (C,E,C,A/I) would affect the quality objective for once occurred



DOCUMENTATION

Designing responses

Mitigate the possibility that a quality risk occurs

Responds to and addresses in the nature, timing and extent of the response:

- **How, and the degree to which,** the conditions, events, circumstances, actions or inactions may adversely affect the achievement of quality objectives
- The possibility of **occurrence**

Designing responses

NATURE

- Preventative
 - Detective
- Use of technology
- Resources required
- Responsibility level (firm/engagement)

TIMING

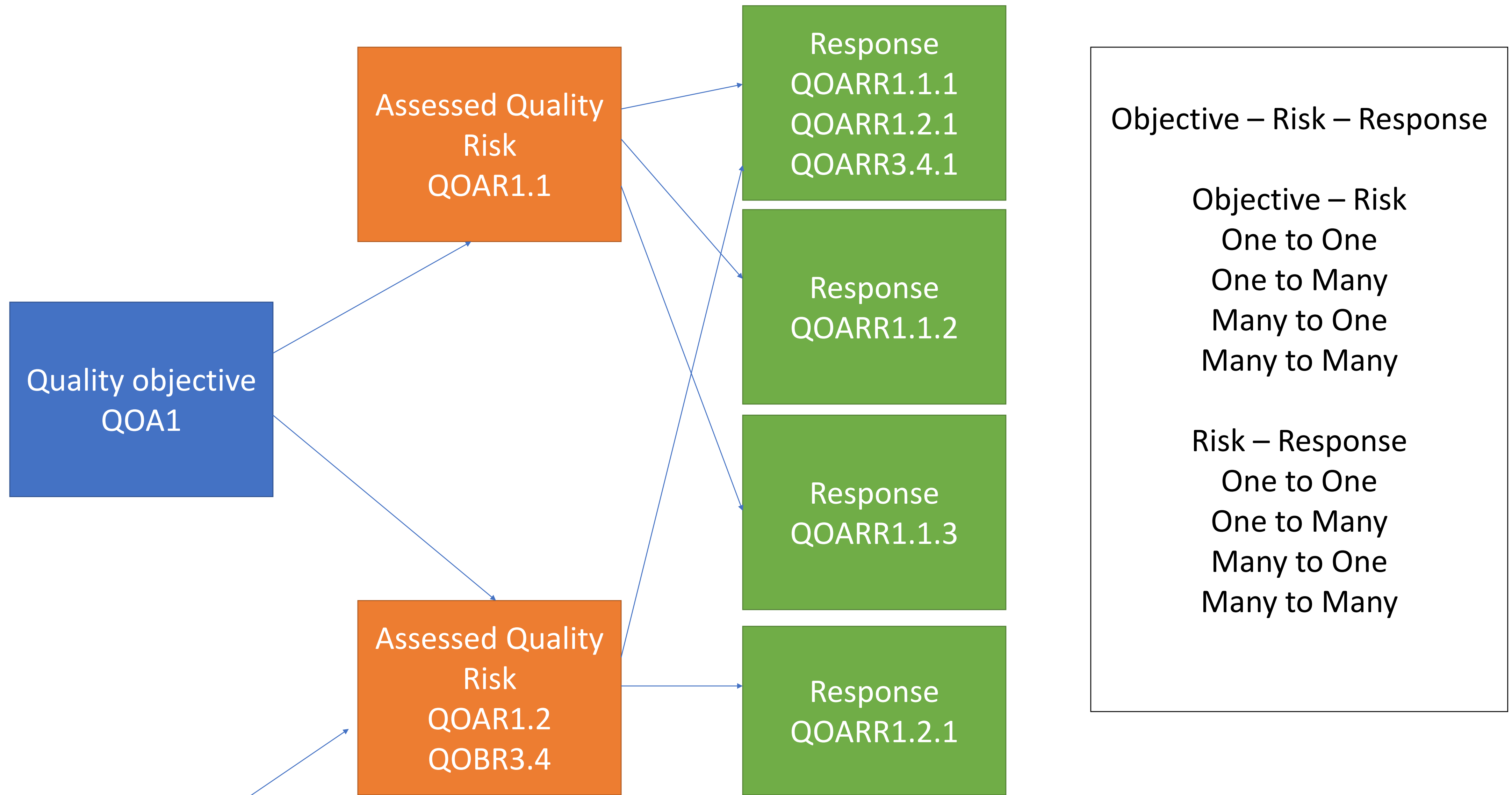
Periodic
Ongoing
Frequency (to mitigate)

EXTENT

All events
Selection of events
Specific events

SUFFICIENCY OF RESPONSE (ALONE OR IN COMBINATION)

Designing responses



Specified responses

Responses mandated by ISQM 1:

The firm shall establish policies and procedures for:

- Threats to compliance with relevant ethical requirements
- Breaches of the relevant ethical requirements and appropriately responding to the causes and consequences of the breaches in a timely manner
- At least annually, a documented confirmation of compliance with independence requirements
- Complaints and allegations
- Reconsidering the engagement acceptance/continuance decision after the fact based on new information
- Communication with TCWG of listed entity audits and other external communications on the SOQM
- EQRs to ISQM2 and which engagements these are required for (listed, by law and by firm's determination)

ISQM 2: Engagement Quality Reviews

- EQR (vs EQCRs) are a specified response to ISQMI
- Previously, ISQC 1 and ISA 220 included references to ECQRs, and implementation was inconsistent and not providing the intended results
- Now incorporated in detail into a specific QM standard: ISQM2
- Same effective dates as ISQMI, and implementation of a SQQM is only complete when all 3 QMS are implemented
- ISQM 2: Clarifies, strengthens relevant requirements (engagements, eligibility, EQR responsibilities) – more robust EQ Reviews
- Enhances focus on significant judgments made by the team (responsive to ISA540(R), ISA 315(R), IFRS changes etc) and professional judgement and professional scepticism
- Addresses in more robust detail, EQR's responsibilities at appropriate times in an engagement: Planning, Performing, Reporting
- Requires a “stand back” approach from EQRs on whether ISQM2 requirements have been achieved
- Requires a firm to develop P&P for EQR – EQ accountability, documentation, specifies engagements, may specify focus areas or working papers

ISA 220(R): Quality Management for an Audit of Financial Statements

- Replaces ISA220: Quality Control for an Audit of Financial Statements
- Same effective date and implementation requirements
- Amendments in line with the intention of changes in ISQMI
- Significant focus of the changes relate to the role of the engagement partner in managing and achieving quality on an audit engagement and in reinforcing quality messages to the engagement team
- Engagement partner's responsibilities enhanced to include:
 - Managing and achieving quality at engagement level
 - Determining the nature, timing and extent of direction, supervision and review
 - Be sufficiently and appropriately involved to provide a basis for taking overall responsibility
- "Take responsibility for" vs "Shall" (delegation vs performance)
- Amendments to enhance responsibility for properly resourcing a team (in line with ISQMI iro resources, including TIME)
- More explicit requirements about what an engagement partner needs to review

Monitoring and remediation of SOQM

Relevant, reliable, timely information: D, I and O of the SOQM

Take appropriate action to respond to deficiencies/remediate timely

Monitoring is not the same as maintaining and “internal controls” built into the SOQM

- Design monitoring activities: NTE: Iterative, non-linear
- Perform monitoring activities: POE
- Evaluate findings
- Identify deficiencies
- Evaluate deficiencies – root cause analysis
- Respond to deficiencies – remedial actions
- Evaluate remedial actions – design, implementation and effectiveness
- Modify remedial actions
- Ongoing communication – timely, to those assigned ultimate responsibility
 - Monitoring activities performed
 - Identified deficiencies – severity, pervasiveness
 - Remedial actions

Monitoring and remediation

Deficiencies: Evaluated from Findings

- Professional judgment
- Whether the finding indicates a deficiency (not all findings are deficiencies)
- A quality objective is not established
- A quality risk (or combination) is not identified / not properly assessed
- A response (or combination) is not properly designed
- A response (or combination) is not properly implemented
- A response (or combination) is not operating effectively
- Other aspects of the SOQM are absent/ not properly designed/implemented./operating effectively

Networks

- Network requirements
- Network services
- Structures vary
- Includes component auditors from another network firm
- The firm is ultimately responsible for its own SOQM and must take this into account when placing reliance on network requirements or services and whether these need to be enhanced/adapted or supplemented
- Network monitoring – also vary
- Monitoring and remediation process applies to firm requirements and services as well (deficiencies and responding)

Evaluating the SOQM

Person assigned ultimate responsibility must, at least annually:

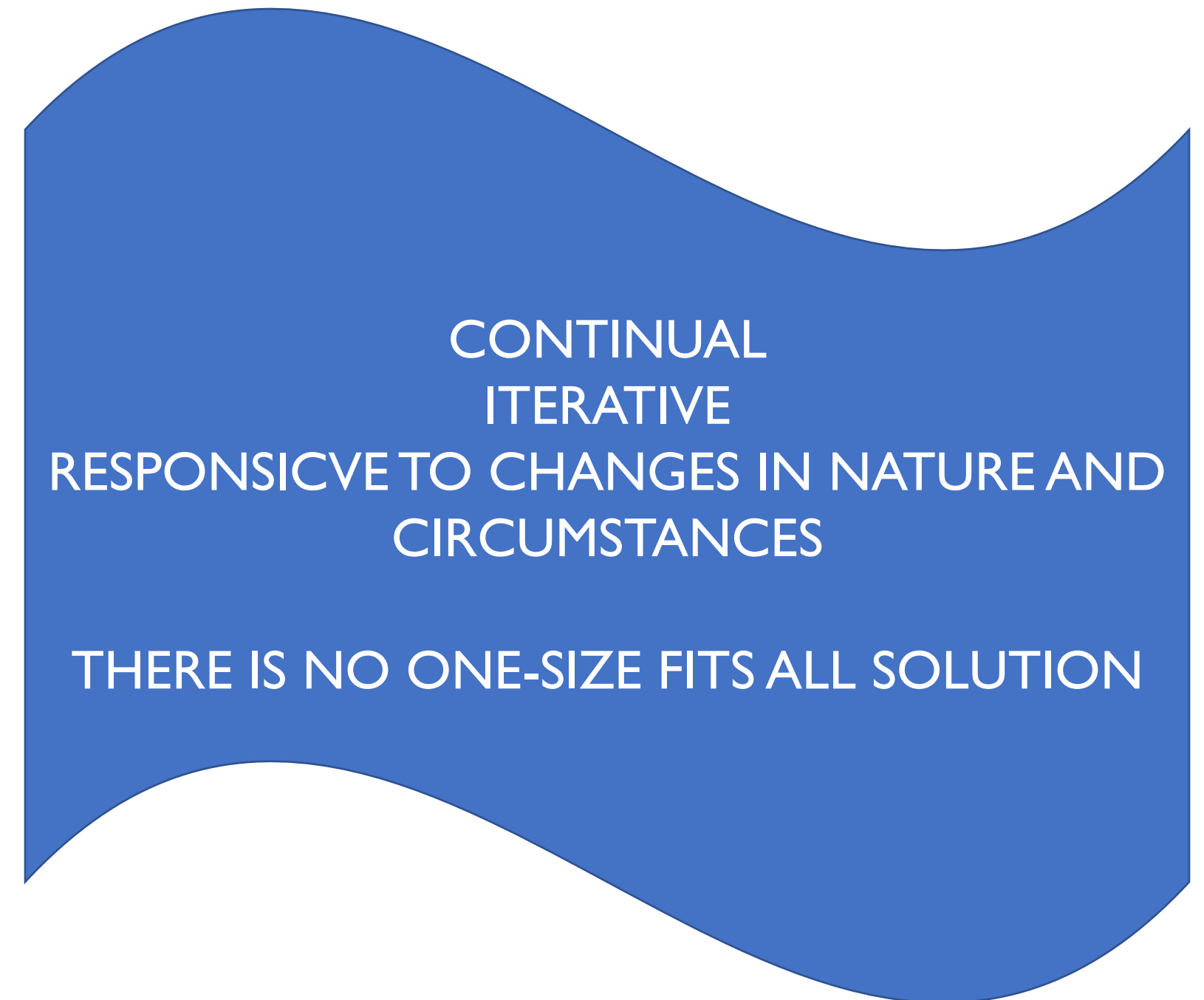
- Evaluate the SOQM (internal – “self-assessment”)
 - Information from monitoring and remediation
 - The severity and pervasiveness of deficiencies and impact on the achievement of SOQM objectives
 - Whether remedial actions were designed and implemented
 - Whether they were effective
 - Whether the effects of the deficiencies have been appropriately corrected
- Conclude on whether the objectives of the SOQM are being achieved
- Conclude on whether the SOQM provides reasonable assurance on the firm objectives
- Take appropriate action based on one of three Conclusions:
 - Provides reasonable assurance that objectives of the SOQM are being achieved
 - Except for...
 - SOQM does not provide reasonable assurance

ISQM: Practical implementation

- **Assigning** responsibilities: (governance and leadership, resources, communication)
 - Ultimate responsibility **and accountability** for the SOQM (CEO / Managing partner / Board)
 - Operational responsibility for the SOQM
 - Operational responsibility for aspects of the SOQM
 - Compliance with independence requirements
 - Monitoring and remediation
- **Appropriate experience, knowledge, influence and authority and time**, proper understanding of R&R (resources)
- **Direct line of communication** to person with ultimate responsibility and accountability (governance and leadership, communication, resources)

ISQM: Practical implementation

- SOQM Designed and implemented by 15 December 2022
- Monitoring activities commence 15 December 2022
- First evaluation of SOQM by 15 December 2023 (at least annually)
- Implementation: planned approach:
 - Early adoption (all three standards)
 - all-in
 - phased in (phasing in not considered “early adoption”)
 - Testing/piloting
- Scalability
 - Network firms – e.g. network level, individual firm level and engagement level
 - Larger firms – e.g. firm level and engagement level
 - Small firms (eg sole practitioners) – e.g. some aspects may operate concurrently with engagement level
- Review and adaptation of existing policies and procedures from ISQC I



CONTINUAL
ITERATIVE
RESPONSIVE TO CHANGES IN NATURE AND
CIRCUMSTANCES
THERE IS NO ONE-SIZE FITS ALL SOLUTION

ISQM: Practical implementation

- Develop your implementation plan
 - Establish your quality objectives
 - Conduct your understanding activities – business strategy, performance, financial analysis, business model articulation, client analysis, resources and capacity analysis, internal environment and leadership style analysis, interviews, previous monitoring results etc
 - Identify and assess the quality risks
 - Design responses
 - Map to exiting P&P and evaluate
 - Design responses for gaps
 - Map resources and timing for all responses
 - Procure/update systems for documentation of SOQM and POE and architecture, job descriptions etc
 - Engage service providers
 - Training
 - Launch



ISA315(REVISED 2019): IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT

ISA315(R 2019) – Why?

- To address challenges and issues with the current ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*
 - Inconsistency in application
 - Lack of clarity in implementation (what, why and how)
 - Risk assessments and responses not responsive to real risks as identified in global inspections findings trends

ISA315(R 2019) – What?

- Applicable to audits of financial periods beginning on or after **15 December 2021**
- Revised, reorganised and enhanced
 - **Requirements – focus on the what**
 - **Application material – focus on the why and the how**
- More **robust** risk assessment process
- Enabling **better responses** to identified risks
- Principle-based requirements enable **scalability**
- Easier to use
- Easier to apply to all environments, including changes to **technology**
- **THE AUDIT RISK MODEL HAS NOT CHANGED**
 - **Application, implementation, process and documentation has been clarified/enhanced/reorganised**

ISA315(R 2019) – Significant changes

- Clarity and enhancements on [professional scepticism](#)
- Separated process for understanding the applicable [financial reporting framework](#)
- Clarity and enhancements on the nature and extent of the understanding of entity's [system of internal control](#)
 - Extent of work needed for direct and indirect controls
 - Determining which controls to identify for evaluating design, and determining implementation (D&I)
- New considerations included for the use of automated tools and techniques, and for impact of technology on the control environment
- New terms and concepts:
 - [Significant COT, AB and Discl](#)
 - [Spectrum of inherent risk and revision of definition of significant risk](#)
 - [Inherent risk factors](#)
 - [Separate assessment of IR and CR](#)
 - [Stand back provision](#)

ISA315(R 2019) – Definitions

- Relevant assertions: An assertion (about a COT/AB/D) is relevant when it has an identified ROMM before considering controls
- Significant COT/AB/D – A COT/AB/D for which there is one or more relevant assertion
- Inherent risk factors – characteristics of events/conditions that affect susceptibility of an assertion about a COT/AB/D to misstatement, whether due to fraud or error:
 - BEFORE THE CONSIDERATION OF CONTROLS
 - QUANTITATIVE OR QUALITATIVE
 - Complexity (nature of information or the way information is prepared)
 - Subjectivity (objectivity in preparation)
 - Change (when changes in events/conditions affect economic, accounting, regulatory, industry, other aspects, when those changes are reflected in required information)
 - Uncertainty (vs precision, vs verifiable through direct observation)
 - Susceptibility due to management bias or other fraud risk factors insofar as they affect inherent risk

ISA315(R 2019) – Risk Assessment

PROFESSIONAL JUDGMENT AND PROFESSIONAL SCEPTICISM

Acc and Cont

Prior year audit

Eng team discussion

OBTAIN AN UNDERSTANDING OF

ENTITY AND ITS ENVIRONMENT

APPLICABLE FRF

IDENTIFY ROMM
FS LEVEL
ASSERTION LEVEL

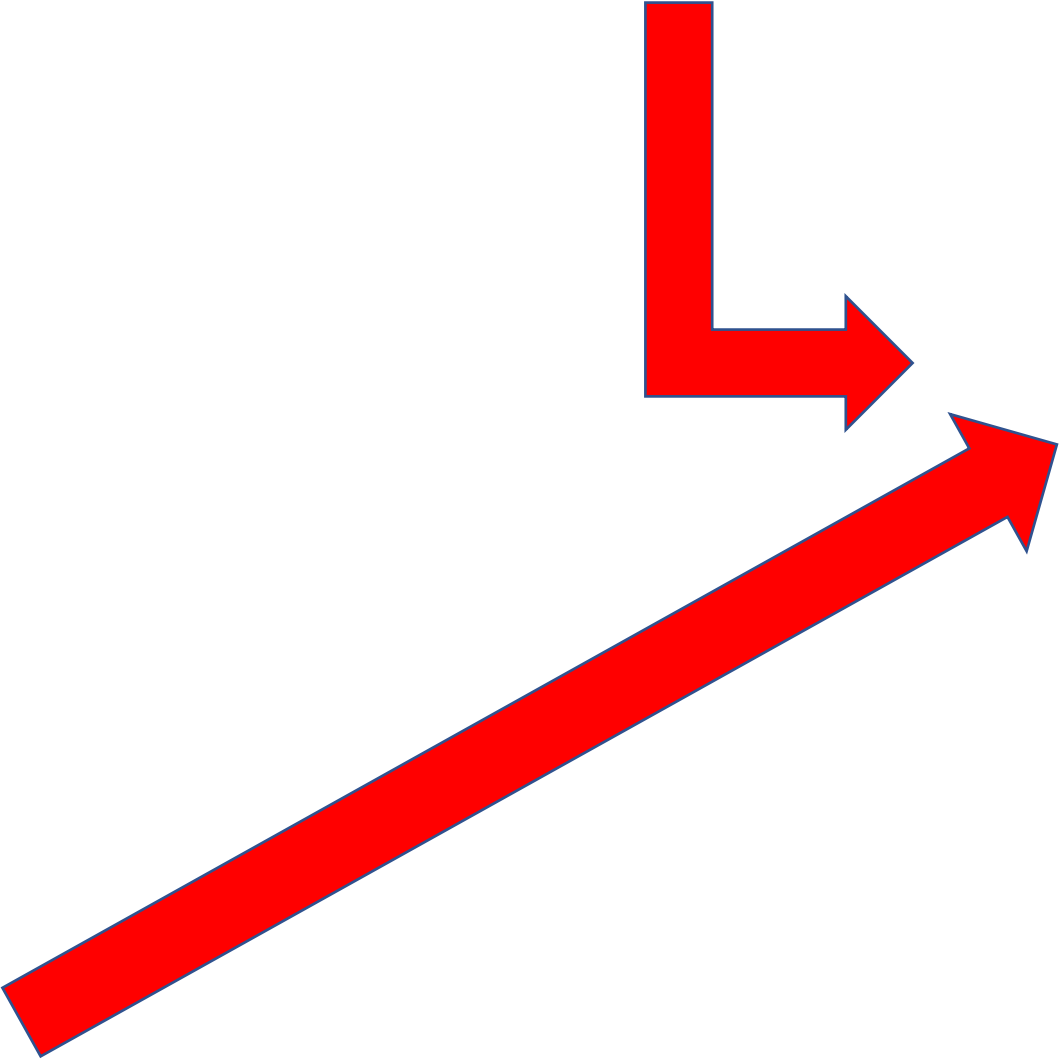
IR FACTORS

RELEVANT ASSERTIONS

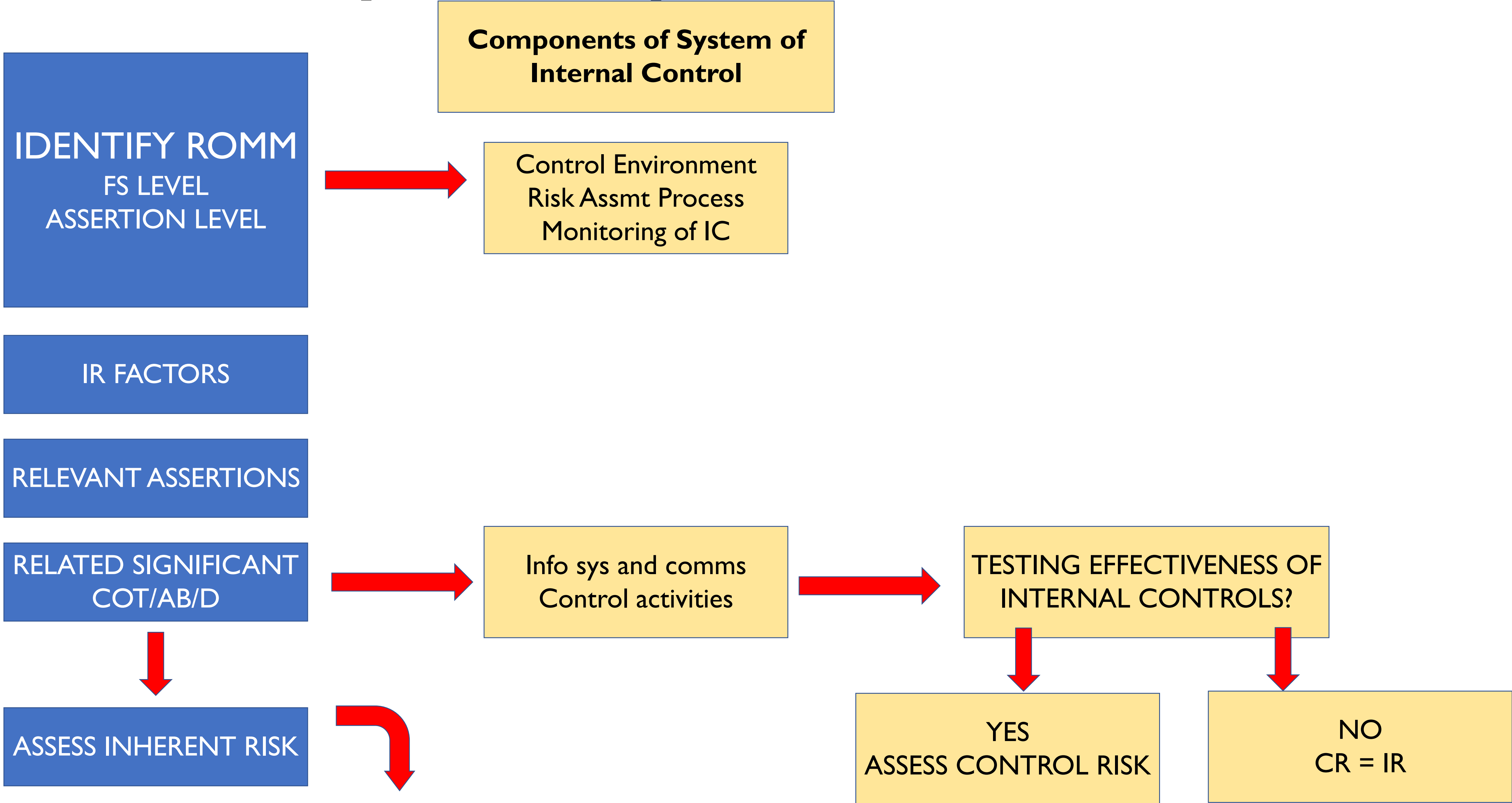
RELATED SIGNIFICANT
COT/AB/D

Info sys and comms
Control activities

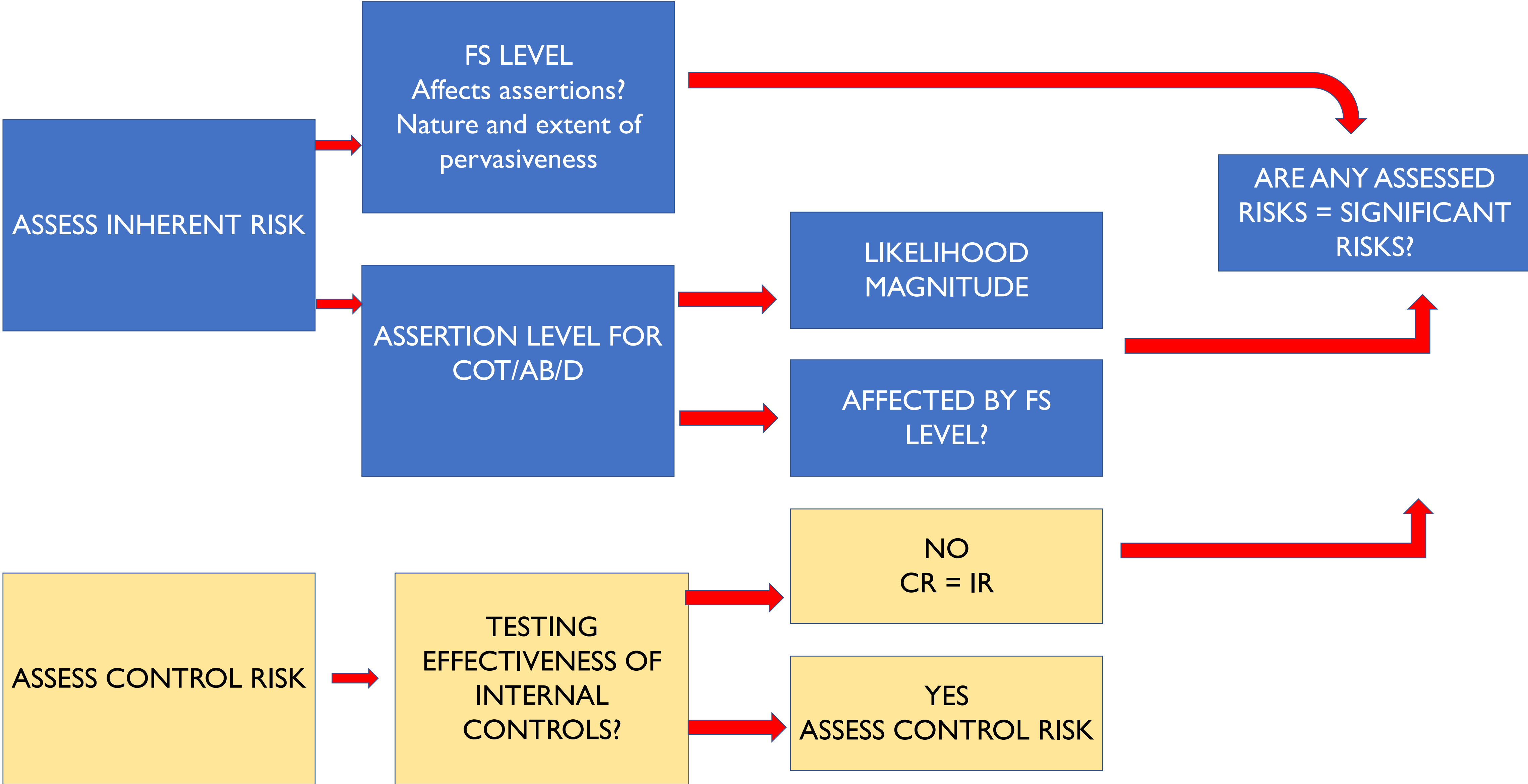
Control Environment
Risk Assmt Process
Monitoring of IC



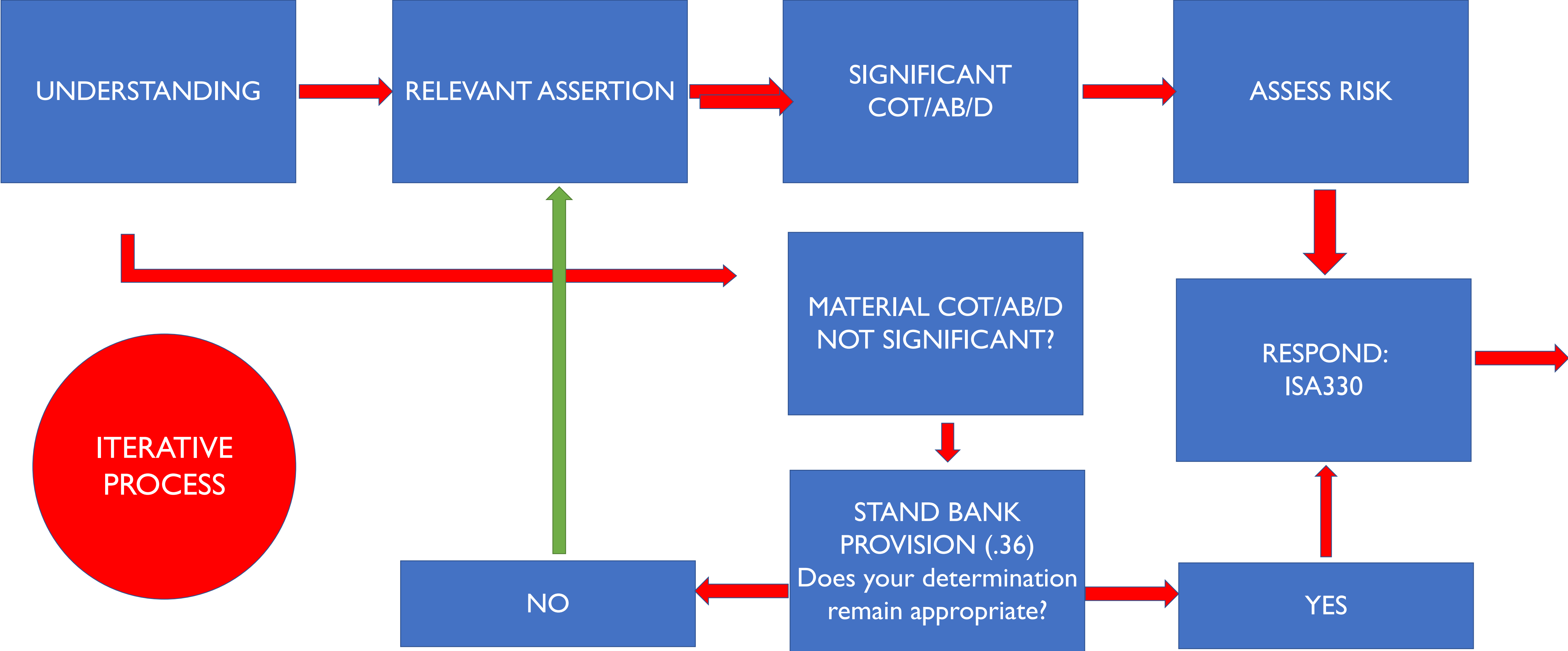
ISA315(R 2019) – Risk Assessment



ISA315(R 2019) – Risk Assessment



ISA315(R 2019) – Risk Assessment



ISA330 – Responding to ROMM

- Conforming amendments – terminology (eg significant COT/AB/D, relevant assertions etc)
- Clarity on controls addressing the ROMM and planning to test effectiveness
- No change to: “irrespective of assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material COT/AB and D



ISA315(R 2019) – Professional S & J

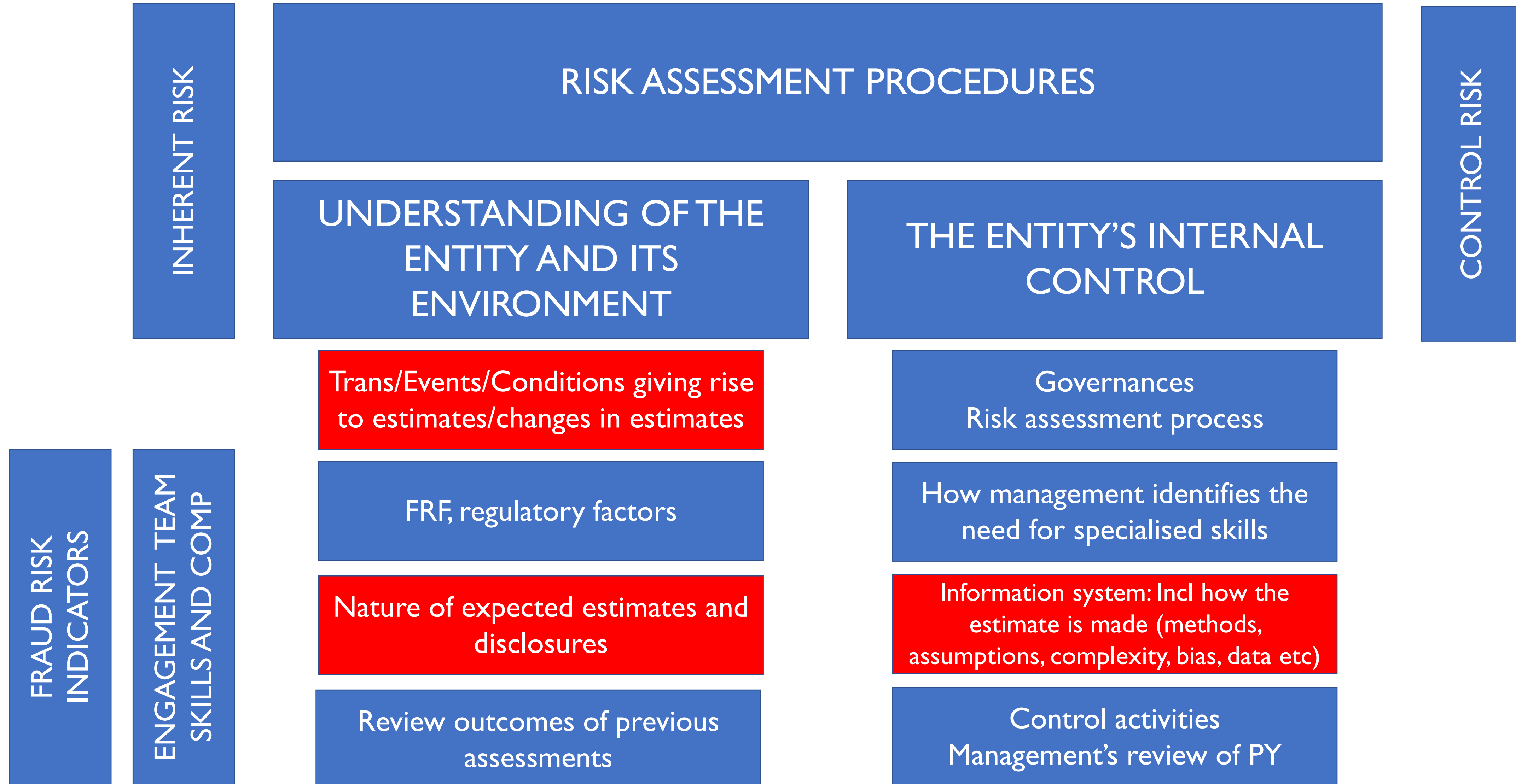
- The auditor shall design and perform risk assessment procedures **in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory.**
- (Stand back) For material classes of transactions, account balances or disclosures that have not been determined to be significant classes of transactions, account balances or disclosures, the auditor shall evaluate whether the auditor's determination remains appropriate.
- Documentation: rationale for significant judgments made

ISA540(R): IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT

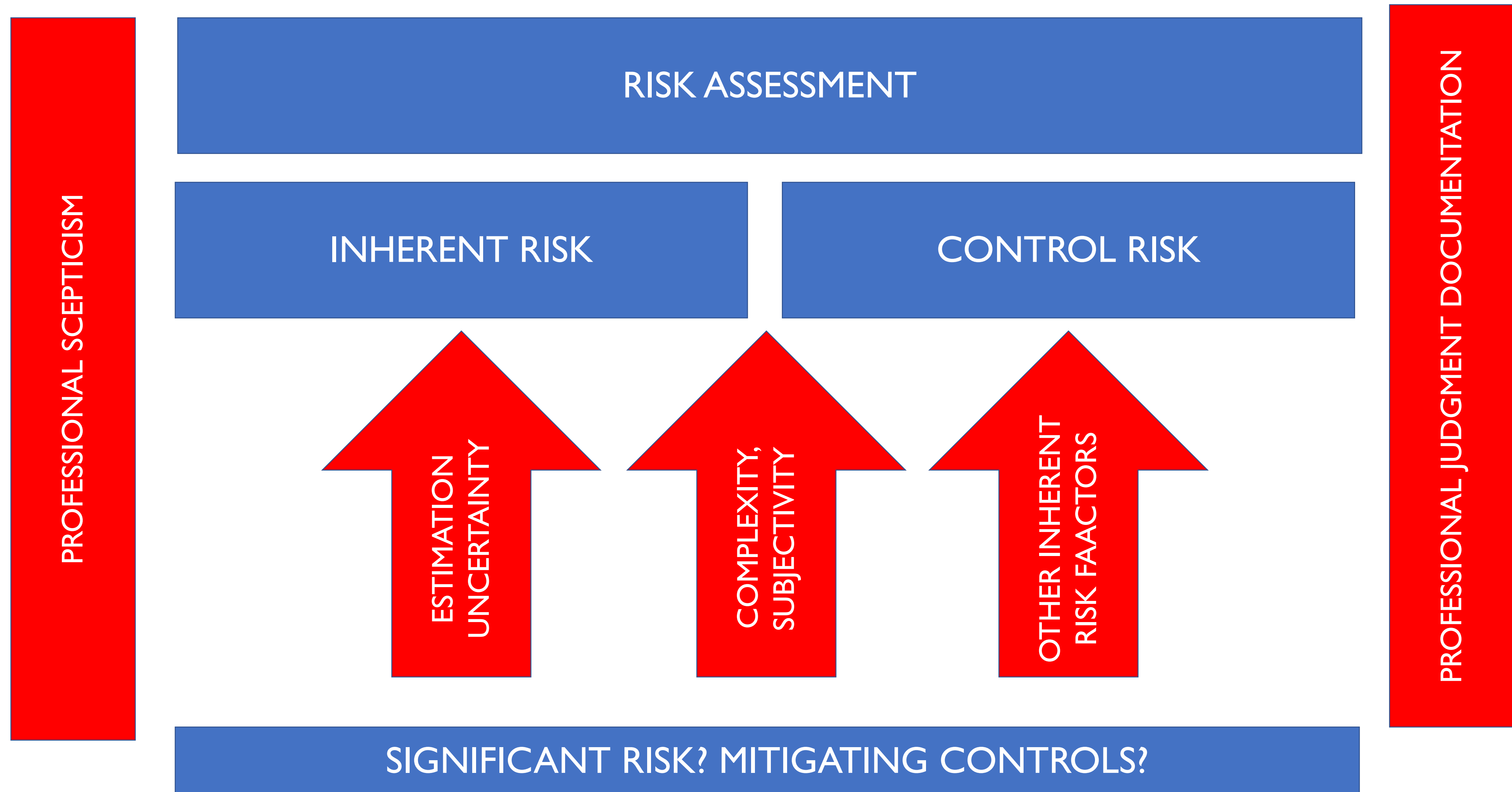
ISA540(R) – Auditing Accounting Estimates and Related Disclosures

- Applicable for audits of financial periods beginning on or after 15 December 2019
- Requirements are now applicable to most audits being undertaken now
- Key concepts in ISA540(R):
 - Separate IR and CR assessments
 - IR: for the purpose of assessing the ROMM at the assertion level for estimates
 - CR: Can ONLY be reduced if the auditor plans to test the effectiveness of controls.
- Further audit procedures need to be responsive to the ROMM
 - Taking into account the nature of the estimate, the making of the estimate, the accounting, the underlying data etc
- Specific documentation of professional judgment, specific application of professional scepticism
- Emphasis on persuasive evidence and challenging management's estimates

ISA540(R) – Auditing Accounting Estimates and Related Disclosures



ISA540(R) – Auditing Accounting Estimates and Related Disclosures



ISA540(R) – Auditing Accounting Estimates and Related Disclosures

RESPONDING TO THE ROMM
MUST BE **RESPONSIVE**, AND INCLUDE 1 OR MORE OF...

EVIDENCE FROM
EVENTS OCCURRING UP
TO THE DATE OF THE
AUDITOR'S REPORT

TESTING HOW
MANAGEMENT MADE
THE ESTIMATE

Specifically designed
Method
Assumptions
Inputs
Data
Calculation
Bias
Experts (500/620)
Documentation

DEVELOPING AN
AUDITOR'S POINT
ESTIMATE OR RANGE

PROFESSIONAL SCEPTICISM, INDEPENDENCE, OBJECTIVITY

ISA540(R) – Auditing Accounting Estimates and Related Disclosures

PROFESSIONAL SCEPTICISM, INDEPENDENCE, OBJECTIVITY, PROFESSIONAL JUDGMENT

HIGHER THE ROMM,
MORE PERSUAIVE
EVIDENCE NEEDS TO BE

DESIGN AND PERFORM
PROCEDURES SO THAT
NO BIAS TOWARDS

- Obtaining corroborative evidence
- Excluding contradictory evidence

ADDITIONAL
PROCEDURES ON:
DISCLOSURES
MANAGEMENT BIAS
CONTEXT OF AFS
MGT
REPRESENTATIONS
COMM TCWG

DOCUMENTATION: ISA540, ISA230.08, .09, .10

UNPACKING REGULATOR INSPECTIONS REPORTS

IRBA: Quality trends

Firms:

Firms where no further action required: Decreased to 0% (from 22%)

Firms where some improvement required: Decreased to 0% (from 7%)

Firms where significant improvement required: Increased by 23%

Firms referred for investigation: Increased by 7%

IRBA: Quality trends

Firms: Deficiency spread:

Engagement performance: 62% (declined from 58%)

Ethical requirements: 13% (declined from 5%)

Leadership: 10% (declined from 8%)

Human resources: 10% (declined from 8%)

Monitoring: 3% (improved from 20%)

Acceptance and continuance: 2% (improved from 3%)

IRBA: Quality trends

Engagement file reviews:

Files with no further action required: Stayed at 17%

Files where some improvement required: Decreased by 1%

Files where significant improvement required: Decreased by 2%

Referrals for investigation: Increased by 3% (In PIE segment, referrals increased by 5%)

IRBA: Quality trends

Top 15 Engagement Themes

Financial statement presentation and disclosure (23%)

Revenue (18%)

Significant auditor judgment (10%)

ROMM (6%)

PPE (6%)

Auditor's report and opinion (3%)

Goodwill (3%)

Inventory (3%)

COS (2%)

Evaluation of misstatements 2%

Journal entry testing: 2%

Trade and other receivables: 2%)

File archiving (2%)

Intangible assets (1%)

Independence and ethics (1%)

IRBA: Quality trends

Top 15 Engagement Themes

Financial statement presentation and disclosure (23%)

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Evaluation of misstatements 2%

Journal entry testing: 2%

Trade and other receivables: 2%)

File archiving (2%)

Intangible assets (1%)

Independence and ethics (1%)

IRBA: FS P&D

- Presentation not in accordance with SAAPS3 (eg missing responsibility paragraphs)
- Omission of key descriptors (consolidated and separate)
- Tenure disclosures (either non disclosure or incorrect disclosures)
- Deficiencies in KAMs:
 - Procedures reported not supported by evidence
 - Boilerplate language
- Material non-cash items in the CFS
- Inadequate disclosures relating to restatements
- Current v Non-Current classifications (especially related parties)
- Inadequate/incorrect IFRS 7 disclosures
- Inadequate/incorrect IFRS 13 disclosures (hierarchy) or evidence
- Insufficient disclosures for goodwill impairment assessments
- Numerous directors' emoluments findings – disclosures, audit evidence, entity v group not disclosed)

IRBA: Revenue

Completeness of revenue

- Completeness of revenue evidence for all material revenue streams either not included or insufficient
- Inappropriate source documents/data used for completeness testing
- Population not assessed for completeness and accuracy before testing
- Analytical reviews inappropriately used to test completeness

Occurrence of revenue

- No or insufficient testing on occurrence
- Incorrect source documents used to test occurrence (indicating insufficient understanding of system)
- Tests not achieving the occurrence objective

IRBA: Significant auditor judgment

- Evaluation of uncorrected misstatement inappropriate
- Inappropriate reliance on the work of experts
- Insufficient documentation on file relating to the auditor's assessment of the reasonableness of management's inputs and assumptions into critical valuation calculations (goodwill, financial instruments, investment property valuations)
- Significant deficiencies in the auditing of:
 - Going concern
 - Impairment of goodwill and intangible assets
 - Debt/equity classification
 - Subordination agreements
 - Breach of debt covenants
- No or insufficient assessment of the appropriateness of management's assessment of the EUL and RV of PPE (re the requirement to assess useful lives and residual values annually)
- No or insufficient independent assessment of whether management had appropriately determined depreciation

IRBA: Success factors

- Apply adequate levels of professional scepticism on areas of judgement – able to challenge management’s estimates and assumptions
- Being sufficiently independent of the audit client results in being less likely to allow management’s assumptions and estimates to go unchallenged
- Sufficient invest in training their audit staff to perform audits in accordance with standards and ensuring all professionals comply with CPD results in consistent high audit quality
- Proper, thorough understanding of the entity, its environment and information systems results in appropriately identifying the source documents to test for revenue
- Review of the AFS by an appropriately senior person more likely to detect disclosure deficiencies
- Investing in training to enable staff to review AFS instead of contracting this review out to external consultants more likely to achieve consistent quality
- Putting quality ahead of commercial interests results in more resources being made available and thus more consistent high quality audits and putting public interest first

IRBA: Remedial Action Plans

Adequacy of root cause identification: Improved by 9%

Adequacy of remedial action plans: Improved by 6%

IRBA continues to review RCA and RAPs

ISQM suite has a significant focus and enhancement on remediation as part of the monitoring process.

IRBA: Future Outlook

- Evolving auditing standards:
 - ISQMs
 - ISA600
 - Joint Audit Engagements Guide
- IRBA Guidance on COVID-19
- IESBA Publication on navigating ethical issues resulting from COVID-19
- Significant accounting developments
 - IFRS16 first time application will be monitored in the next cycle
 - IFRS17 possible early adoptions
 - IFRS9 and 15 remain focus areas for inspections (IRBA Staff Practice Note – audit implications of IFRS15)
 - Auditing of presentation and disclosure
- Focus on technology (IRBA inspections)
- IRBA CPD Policy

IESBA PRONOUNCEMENTS: IMPACT ON PRACTICE

Revisions to the Fee-related Provisions of the Code

Differentiating between PIEs and non-PIEs

Threats created by fees paid by an audit client

- Application material added relating to the level of self-interest threat created by fees paid by an audit client
- Additional factors for firms to consider when evaluating the level of threats created by fees paid by an audit client:
 - Whether the fees are paid for services provided by the firm or a network firm to the audit client
 - The operating structure and compensation arrangements of the firm and network firms
 - The relationship of the client to the related entities to which other services (other than audit) are provided
 - The level of the fee in the context of the service to be provided

Revisions to the Fee-related Provisions of the Code

Level of audit fees

- Audit fee should be a standalone fee, i.e. prohibition for fees not to be influenced by the fact that fees are earned for other services
 - Unless the firm can appropriately demonstrate the cost savings achieved as a result of the experience derived from the provision of other services

Fee dependency on PIE audits

- In considering an additional safeguard when fees exceed 15% for 2 consecutive years, recognising it may not be determined that fees exceed 15% until a later stage of the audit and therefore it may not be operable to follow ISQM 2 for an EQR, amendment will refer to “a review consistent with the objective of an EQR” as an appropriate action to reduce threats to an acceptable level (Pre-issuance review)
- Requirement to cease being the auditor if fee-dependence continues for a period of 5 consecutive years, with additional considerations (compelling reasons etc)

Fee dependency on non-PIE audits

- 30% and 5 years
- Pre-or post issuance review

Revisions to the Fee-related Provisions of the Code

Proportion of fees paid for services other than audit, to audit fees

- Acknowledgement of the threat to independence created when large proportion of fees come from non-assurance services
- Guidance included

Transparency of fee related information of PIE Audit Clients

- Inclusion in the communications with TCWG of the identified threats and safeguards and on-going fee dependency considerations
- Disclosure to public – approach is flexible, applies to information that is essential from perspective of the firm's independence

Revisions to the Non-Assurance Services Provisions of the Code

- Refinements emphasising the **self-review prohibition** in the general provisions and that the **conceptual framework must be applied** when specific requirements or application material are not included
- **Clarifying firm responsibilities before undertaking NAS** (the firm shall apply the conceptual framework to identify, evaluate and address any threat to independence that might be created by providing that service)
- New provisions to determine whether an identified threat relates to self-review and related new **prohibitions relating to PIEs** (prohibitions because threats CANNOT be eliminated or reduced to an acceptable level)
- Refinement of terminology – **will create vs might create**
- **Materiality** is NOT a factor in determining whether a proposed NAS creates a self-review threat
- Inclusion of **new factors relevant in identifying threats** (degree of reliance on the outcome of the service, fees)

ENVIRONMENTAL SCANNING

IAASB

New auditing standards

- ISQM standards: ISQM 1, 2 and ISA220R – applicable from 15 December 2022 and replacing ISQC 1 and extant ISA220
- ISRS4400 (Agreed Upon Procedures) – applicable for engagements where the LOE is signed on or after 1 January 2022
- ISA315 Revised (Identifying and assessing the risk of material misstatement) – applicable for audits of financial periods beginning on or after 15 December 2021 (IRBA has yet to issue guidance on the adoption/implementation of this standard, and I am not sure that the benefits envisaged by the IAASB as a result of the revision will necessarily be the same for the South African RAs)

Exposure drafts – auditing standards

- ISA600 – feedback on the ED has been given, is being processed and standard will be published, expected December 2021, will probably only be applicable in 2023
- Audits of less complex entities – ED has been issued for comment, with comments due by 31 January 2022 – this will likely take at least another 2 years before being ready for publication

Workplan projects

- ISA500 review
- ISA240 Fraud
- ISA570 Going concern

IESBA

New pronouncements

- Final pronouncement on fees - effective for audits and reviews of financial statements for periods beginning on or after 15 December 2022
- Final pronouncement on non-assurance services - effective for audits and reviews of financial statements for periods beginning on or after 15 December 2022

Exposure drafts

- ISQM conforming amendments to the Code – ED currently out for comment

Current projects

- eCode
- Technology
- Definitions of PIE and listed entities
- Engagement Team – group audits independence
- Tax planning and related services

IRBA - CFAS

- Data Protection
- Quality Management Standards - Local Laws & Regulations
- System of Quality Management Transitional Guidance
- Conforming Amendment to CFAS Pronouncements: Quality Management Standards
- Auditor's Report Disclosures
- ISA Plus
- Conforming Amendments - ISRS 4400 Agreed Upon Procedures
- Regulation 46 Banking Industry Reports
- Debt Collectors Trust Account Assurance Reports
- Social and Ethics Committee Report (awaiting legislation | 5)
- Financial Conglomerates (awaiting legislation | 6)
- Collective Investment Schemes Report (awaiting legislation | 7)

Other issues to watch

- Implementation of the new ISRS4400 Agreed Upon Procedures Standard
- Growing emphasis on and use of ISAE3000 for non-financial information and EER

RECAP

- ISQM: Proactive, iterative, risk-based approach to quality management: 442 days
- ISA315(R 2019): More robust planning procedures, better risk assessment, better responses – guidance on South African implementation still awaited
- ISA540(R): Applicability, change in approach and requirements, focus area for IRBA
- IRBA Inspections report: findings align with the changes to the standards above
- IESBA new pronouncements – impact on QCMs and ISQM processes
- Environmental scanning – IAASB – Audits of LCEs
- Environmental scanning – IESBA – Continuing enhancements to sections of the Code
- Environmental scanning – IRBA and the South African context

QUESTIONS

**Thank you
for your participation**