Accountancy Board

Quality Assurance

2011
ANNUAL REPORT

(issue date - March 2012)

CONTENTS

CHAIRMAN'S STATEMENT

I am pleased to present the Accountancy Board's Annual Report for the year ended December 2011.

2011 will undoubtedly be remembered as the year where the current statutory audit methodologies across the globe were put under the spotlight following the aftermath of the financial crisis. So much has been written and debated in this regard and yet there still seems to be no consensus by the stakeholders concerned, on the renewed expectancy gap.

The European Commission issued a Green Paper to open up the debate on the role of the auditor, the governance and the independence of audit firms, the supervision of auditors, the configuration of the audit market, the creation of a single market for the provision of audit services, the simplification of rules for Small and Medium Sized Enterprises (SMEs) and Practitioners (SMPs) and the international co-operation for the supervision of global audit networks. In this debate, the Commission took a proactive approach in seeking comments from the broadest possible base of stakeholders such as investors, lenders, management, employees, government authorities, auditors, tax authorities, credit rating agencies, equity analysts, regulators, business counter-parties and SMEs. As part of this process, the Accountancy Board provided its feedback to this consultative paper in March and November 2011.

After almost 12 months of consultation with the respective stakeholders the Commission presented its proposals on audit policy to the European Parliament in December 2011 and it is expected that Comissioner Barnier will have new Directives governing Audit Policy entrenched in the respective Member State's legislation governing the audit profession.. This will undoubtedly change audit methodologies, particularly in relation to those carrying out audits of Public Interest Entities. For more information in this regard please refer to Section 3.4 of this report.

Furthermore, the European Commission is also looking at the Professional Qualifications Directive to bring into line with today's requirements. The EU recognised that restrictive regulation of professional qualifications found in individual Member States has become a fundamental stumbling block towards the concept of a Single Market. For this reason, the Professional Qualifications Directive needs to set out clear and simple rules for the mutual recognition of professional qualifications. At the same time, the rules must ensure that the high quality of services provided is maintained without this becoming an obstacle to mobility. With this aim in mind, the EU during June 2011, issued the Green Paper to bring this directive on professional qualifications in line with emerging realities. The Accountancy Board actively partcipated in dialogue to address this.

On a more local scenario, the Accountancy Board has taken steps to review certain sections of the Accountancy Profession Act and is also focusing in more closely, in collaboration with the Malta Institute of Accountants, on a number of Continued Professional Education issues. While one recognises that enforcement in this regard could be stepped up, the legislative and CPE regulatory framework needs to be revamped, to provide the necessary tools to the Accountancy Board to sanction defaulting warrant holders.

The accountancy and audit profession in Malta accounts for over 1,850 registered individuals and firms. The profession has experienced significant growth over the last decade. In spite of an annual increase of circa 150 - 200 warrants and practising certificate holders, one is still experiencing a dire shortage in qualified and experienced audit personnel. This emanates from the fact that the local supply of accountants is being directed towards the ever growing financial services sector. This leaves many of the local audit firms and sole practitioners with a major recruitment problem, many of them having to recruit suitably qualified and experienced audit personnel from abroad, to help them meet local demand.

Although the Accountancy Board had its own website, it was felt that the functionality of its web pages was somewhat limited. In past years the Board had appointed IT developers to create a bespoke IT platform to meet the needs of the Accountancy Board. Unfortunately, this project could not be brought to fruition for a number of reasons. At the start of 2011, new software developers were called in to take full responsibility of this IT project. I am pleased to inform you that, in spite of the tight deadlines, the new system is now up and running and the Accountancy Board prides itself that an interactive portal is now available. Warrant holders can now submit their annual return and settle their fees and access other useful information regarding the profession on-line. The public at large too, can now obtain information pertaining to warrant and practising certificate holders, as well as registered accounting and audit firms via the Accountancy Board's registers which are now on line and can be accessed on a real-time basis. It is pertinent to point out that the manual submission of the Annual return will be phased out during 2012.

Presently the Board regulates a total of 218 audit practices of which, 74 are full-time sole practitioners, 90 part-time sole practitioners and the remainder being 54 audit firms. As Chairman of the Quality Assurance Oversight Committee (QAOC) I am pleased to inform you that up until November, the QAOC since its inception has concluded 208 quality assurance visits, of which 37 pertain to visits finalised during 2011. The QAOC has also agreed that the visit cycle of statutory auditors who do not audit public-interest entities should be extended from a cycle spanning to not more than four years to one spanning a period of not more than six years.

During the year, the QAU has continued its second cycle of visits to practitioners and firms. In some cases, a number of repeat breaches were noted during our second visits. One cannot but emphasise the fact that Quality Assurance (QA) is an ongoing process in so far as statutory audits are concerned. Firms and practitioners must not only ensure that reported breaches reported during earlier visits are remedied in the least possible time but must ensure that the highest form of QA policies and procedures are fostered by the audit profession at all times. Amongst others, these procedures must include clearly set policies in relation to professional ethics, particularly those relating to auditor's independence, professional scepticism and adherence to international standards on auditing and accounting.

The Chartered Accountants Regulatory Board of Ireland confirmed its intention to resume its support to the Accountancy Board in 2012, once its present assignment of looking at and reporting on audits of banking institutions in Ireland following the financial crises is completed, which assignment left CARB with very little time to support the QAU in 2011.

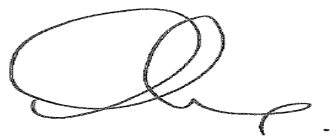
During 2011, the Board held discussions with representatives of the Institute of Chartered Accountants in England and Wales (ICAEW) on possible areas of co operation. Two officials from the ICAEW visited Malta in December 2011 to assist the QAU on a scheduled Big 4 visit.

I take this opportunity to thank all members of the committees which I chair for the constant support they have given the Accountancy Board throughout 2011. My heartfelt thanks also go to the Quality Assurance Unit, which Unit, in spite of an acute shortage of personnel has not only carried out 37 inspections throughout the year under review, but has also given a high level of back office support to the Accountancy Board including that of bringing to fruition the IT project. This latter project has taken circa 10% of the Unit's total available time.

Looking ahead, I envisage that 2012 will pose another challenging and exciting year for the Board and for the accounting profession. Undoubtedly 2012, which has started off with a focus on the Euro zone crisis, will bring with it even more regulation within our field - particularly audits, where securing independence in audit judgement and the promulgation of high quality statutory audits remain high on the agenda.

I have no doubt in my mind that the continued reputation that the Board has built is largely dependent on the integrity and high standards we strive for in the services we offer. While accountants and auditors may complain that, unlike other professions, regulatory compliance has become a laborious and onerous task, it is pertinent to point out that other professional bodies seek to emulate the regulatory process which the Accountancy Board has gone through over the last six years, as today all professionals across the globe move away from self regulation.

To conclude, it is pertinent to point out that one of the more important roles of the Accountancy Board and the Quality Assurance Oversight Committee play remains that of protecting the public interest. As regulators, we seek to strengthen accountability and reinforce trust and confidence in financial reporting and corporate governance.



Charles Rapa
Chairman – Accountancy Board

INTRODUCTION & OVERVIEW

The Board is pleased to present its fifth annual report set out in accordance with the requirements of Article 7(19 & 20) of the Accountancy Profession Act, CAP 281. Enclosed in this report, one will find details of the Board's:

- annual work programme;
- activity reports;
- a description of the work carried out by the disciplinary committee;
- a summary of the work carried out in respect of quality assurance; and
- such other things which the Board deems relevant.

This annual report is set out in the following manner:

- *Sections 3 to 8* – give a brief overview of the composition, frequency of meetings, review of activities carried out during 2011 and plans for 2012 pertaining to the Accountancy Board, Disciplinary Committee, Quality Assurance Oversight Committee, Legislative Clarifications Committee, Investigative Committee and CPE Committee respectively; and
- *Section 9 - Profile of the audit and accounting profession* provides an overview of the audit and accountancy profession in Malta and of the new warrant holders, practising certificate holders and firm registrations issued during 2011.

ACCOUNTANCY BOARD

3.1. COMPOSITION

During the year under review, the Accountancy Board was composed of the following members:

Chairman
Mr. Charles Rapa FCCA, FIA, CPA, MBA(Brunel/Henley), MIM

Members
Mr. Peter J. Baldacchino M.Phil (Lough), FCCA, FIA, CPA;
Dr. Bernice Buttigieg LL.D, B.A., M. Jur (EU & Comp. Law);
Mr. Simon Flynn FCCA, BA(Hons)Accty., FIA, CPA;
Mr. Mario P. Galea FCCA, FIA, CPA;
Ms. Elvia George BA(Hons) Accty., FIA, CPA;
Ms. Angele Grech BA(Hons) Accty., CPA;
Mr. Godfrey Leone Ganado FIA, CPA;
Ms. Helen Meli Attard FIA, CPA, CSA, MIM, MIT, B.A.(Hons Acc.), M.A. (Financial Services);
Mr. Benjamin Rizzo ACMA, FIA, CPA; and
Mr. Bernard Scicluna FCCA, FIA, FMIT, CPA

Technical Advisors
Mr. Anthony Zarb FCCA, FIA, CPA, MBA(Warwick); and
Mr. John Zarb FCCA, CPA, FIA

Secretary
Mr. Joseph Croker (until 31st January 2011)
Mr. Martin Spiteri IEng., MIIE, MBA (Leicester) (as from 1st February 2011)

3.2. FREQUENCY OF MEETINGS

The Board held twelve meetings during the year – once per month.

3.3. COMMITTEES

In accordance with Article 7(2) of the Accountancy Profession Act, the Board is empowered to appoint Committees, of which the Chairman must be a member of the Board for the carrying out of such duties or other work as the Board may assign to them.

The Accountancy Board appointed five Committees to assist it in discharging its functions and responsibilities:

- Disciplinary Committee;
- Quality Assurance Oversight Committee;
- Legislative Clarifications Committee;
- Investigation Committee; and
- CPE Committee.

The structure and activities of such Committees can be found in Sections 4 to 8 of this report.

3.4. SUMMARY OF ACTIVITIES CARRIED OUT DURING 2011

During 2011, the Board carried out a number of activities to fulfil its obligations under Article 7 of the Accountancy Profession Act. These are summarised as follows:

- ***Issue of CPA warrants, practising certificates in auditing and registration of firms.***

  During the course of year, the Board carried out a number of application evaluations for CPA warrants, practising certificates in auditing as well as accounting and audit firm registrations.

  On the basis of such evaluations the Board recommended to the Minister of Finance, the Economy and Investment the approval of 85 CPA warrants. Furthermore, 39 practising certificates in auditing were granted. Certificates awarded to these warrant holders were conferred during June and December 2011.

  In addition, as a result of a concerted effort made by the Board in respect to corporate entities providing accounting services, a number of accounting firms which were previously not registered with the Board have now been duly registered. By the end of 2010, a total of 6 new accounting firms had been registered.

  For more information pertaining to the issue of CPA warrants and practising certificates in auditing, please refer to Section 9 of this report.

- ***Responding to the Green Paper on Audit Policy Proposals: Lessons from the Crisis.***

  During the year, following a conference held by the EU Commission in this regard in February 2011, the Board was asked to provide Malta's position in respect of the proposals included in the Green Paper. The Board was also involved in discussions held to consider the views put forward by other Member States on this matter.

  The Commission's subsequent legislative proposals were launched in November 2011 in the form of a draft Regulation that will shortly commence the relevant approval processes by Council and by the European Parliament. The draft Regulation deals with the audits of Public Interest Entities (PIEs). It makes a number of important suggestions regarding the governance of the audit profession, communication with audit regulators, adoption of International Standards on Auditing by the EU, and the form and content of the audit report itself. The proposed Regulation also makes other more radical proposals such as mandatory rotation, the abolition of the provision of any non-audit services to PIE's and the creation of audit only audit firms (whereby large firms would be prohibited from offering any services whatsoever apart from statutory audit).

  Reservations have been expressed on certain of the more radical proposals by a number of EU Member States, including Malta. The debate on the draft Regulation is therefore likely to be a protracted one. It is too early to foresee at this stage what measures will be included in the final Regulation, but the ongoing debate will undoubtedly impact on PIE audits across Europe in coming years.

- ***Provision of comments in respect to the Green Paper on Modernising the Professional Qualifications Directive.***

  The EU recognised that restrictive regulation of professional qualifications found in individual Member States has become a fundamental stumbling block towards the concept of a Single Market. For this reason, the Professional Qualifications Directive needs to set out clear and simple rules for the mutual recognition of professional qualifications. At the same time, the rules must ensure that the high quality of services provided is maintained without this becoming an obstacle to mobility. With this aim in mind, the EU during June 2011, issued this Green Paper to bring this directive on professional qualifications in line with emerging realities. The Accountancy Board actively participated to address this.

- ***Monitoring and action taken against corporate entities providing accounting services not duly registered with the Board.***

  During 2011, the Board continued its identification of a number of companies providing accounting services which had not been registered with the Board, and thus were in breach of the Accountancy Profession Act.

  On the basis of such identification, notification letters were sent out to the relevant entities for action to be taken. A number of accounting firms have been duly registered in 2011 and others will be registered in 2012.

- ***Amendments proposed for legal regulatory framework.***

  Throughout the year, a number of amendments were proposed and agreed upon by the Board. These changes will effect the following legislation:
  - The Accountancy Profession Act, Cap 281;
  - Accountancy Profession Regulations, 2010 (LN 111 of 2010);
  - Accounting Profession (General Accounting Principles for Smaller Entities) Regulations, 2009 (LN 58 of 2010);
  - Directive 1 – Accountancy Profession (Continued Professional Education) Directive;
  - Directive 2 – Accountancy Profession (Code of Ethics for Warrant Holders) Directive;
  - Directive 3 – Accountancy Profession (Annual Return and Registration Fees) Directive; and
  - Directive 4 – Accountancy Profession (Quality Assurance) Directive.

  These changes will become effective in 2012.

- ***Review of transparency reports published by auditors of public interest entities.***

  During the year, the Board ensured that transparency reports were issued by auditors of public interest entities by the end of March deadline as set out in law.

  The Board vetted such documents to ensure that the requirements set out in the Accountancy Profession Act were duly detailed in the published transparency report. The Board discussed the need for more disclosures to ensure consistency in the information disclosed in these reports.

- ***Issuing of information disseminations.***

  The Board, in 2011, sent out by email, four information disseminations to warrant holders – in March, August, November and another in December. These take the form of short bulletins sent electronically to all warrant holders to bring to their attention any changes in regulatory procedures.

- ***Dealing with complaints against warrant holders.***

  The Board was presented with two complaints during the year. One case was referred to the Investigative Committee and subsequent to its assessment the Board ruled that there was no case against the warrant holder referred to in the compliant.

  The other case is still being considered by the Board.

- ***Launch of the first phase of the Accountancy Board warrant holder portal.***

  As a result of a number of issues that arose in the past in regard to the development of the Board's web portal, in January 2011 new software developers were engaged to bring to fruition this long awaited warrant holder portal. The first phase of this project was launched on the 29th December 2011, in time for the electronic submission of the 2011 Annual Return.

  This system provides a platform from which information can be easily accessed on the Board's website and includes an up-to-date online register of the Board's warrant holders, holders of a practising certificate in auditing, audit firms and accountancy firms. The major development which has resulted from such platform is that warrant holders are now able to fill in and submit the Board's annual return online. Furthermore, annual registration fee payments can now all be made electronically through the Board's website. Warrant holders who are MIA members are no longer required to pay such dues with the MIA. Warrant holders who are not members of the MIA are now also, as part of the annual return itself be required to fill in a detailed log of CPE activities attended during the year. In addition, the lists of registers, which were in the past updated on the website every couple of months, are now on line and can be accessed on a real time basis.

  Furthermore, the online submission of applications for warrants and practising certificate has also been developed through E-forms.

- ***Attendance and participation at European Group of Auditors Oversight Board (EGAOB), Accounting Regulatory Committee (ARC), Audit Regulatory Committee (AuRC) and the European Audit Inspections Group (EAIG) meetings held in Brussels.***

  Two plenary meetings of the EGAOB and two AuRC meetings were held during 2011. The more predominant issues discussed at these meetings were the Green Paper proposals on audit policy, equivalence assessment of and co-operation with competent authorities entrusted with the oversight of auditors in third countries, governance of the audit profession across Europe, and the adoption of ISAs amongst all Member States. Mr. Marcel Coppini, as Head of the Quality Assurance Unit (QAU) attended these meetings. One EAIG meeting in London was attended by Mr. Paul Borg – a QAU reviewer. Mr. John Zarb attended Accounting Regulatory Committee meetings on behalf of the Board.

- ***Corresponding with the EU on matters effecting the accounting and audit profession.***

  The Accountancy Board participated in a number of surveys carried out by the EU throughout 2011 which amongst others included the impact of the Statutory Audit Directive on Member States, the audit market and its evolution, funding and legal structures of oversight bodies, retirement age of auditors and limitation of auditors' liability across Europe.

- ***Attendance and participation at the plenary meeting held by the International Forum of Independent Audit Regulators (IFIAR) in Berlin.***

  Mr. Marcel Coppini attended one plenary meeting held in Berlin in April 2011. The other plenary meeting held in Bangkok was not attended due to budgetary constraints. The meeting focused on close international co-operation amongst audit regulators.

  This organisation brings together top people from no less than 38 different jurisdictions (large and small) across the globe to discuss key issues impacting the audit profession.

- ***Attendance and participation on a number of Malta Institute of Accountants Committees.***

  Members of the QAU sit on a number of Committees of the Malta Institute of Accountants, amongst which, are the Committees dealing with Ethics, Education, CPE and Money Laundering.

- ***Provision of an advisory role with Government on all issues relating to accounting and auditing.***

  These are issues which mainly relate to governance pertaining to the accounting and audit profession in Malta. Amongst other things, areas of significant importance during the current year related to the proposed changes to the 4th and 7th EU Directive, which proposed changes to reduce burdens on smaller entities, by significantly reducing disclosure requirements in financial statements. This will adversely impact the existing accounting regulatory framework pertaining to SMEs (GAPSE) not to mention audit concerns which these proposed reduced disclosure requirements bring with them.

  The Board also had a meeting with the Commission of Inland Revenue in regard to the anomaly which presently exists regarding audit exemption. Whilst statutory audit exemption is contemplated under Section 185 (1) (b) of the Companies Act, business entities filing accounts with the Inland Revenue, under the provisions of the ITMA, are still required to have these financial statements audited – irrespective of their size. One augurs that a solution to this inconsistency which has impacted incorporated small businesses over a number of years is found in the near future.

3.5. PLANS FOR 2012

During the current year, the Accountancy Board intends to undertake a number of initiatives and continue others that were underway which include:

- ***Completion of the second phase of the Accountancy Board warrant holder portal.***

  In the coming year, any difficulties found by warrant holders with the implementation of the first phase of the portal project will be ironed out. Furthermore, the system will be further developed to include additional functionality both for front-end users as well as for back-end processes.

- ***Revision of legislation.***

  During 2011, a number of changes to the Board's existing legislation were proposed. In 2012, these will be adopted to implement the changes recommended by the Board as well as by its Committees.

- ***Recruitment of staff with the QAU.***

  Although the Board has sought to recruit additional staff members with the QAU, these attempts so far have been unsuccessful. As a result, in 2012, a Steering Committee was appointed to identify ways in which staffing issues can be adequately addressed to meet the needs of the QAU. This may include utilising audit staff from other firms for this purpose.

- ***Continuation of the identification and registration process of companies providing accounting services which, to date, have not been registered with the Board.***

  The Board will seek to ensure that providers of accounting services are duly registered with the Board.

  The identification and registration of all providers of accounting services is expected to be a laborious task. This monitoring will be carried out an ongoing basis.

- ***Maintaining close work relationships with other stakeholders.***

  As in previous years, the Accountancy Board will work closing with the Malta Financial Services Authority in a number of areas particularly relevant to the profession and its warrant holders. The Accountancy Board will also foster its relationship with the Malta Institute of Accountants, CARB and the ICAEW.

DISCIPLINARY COMMITTEE

4.1. COMPOSITION

The composition of the Accountancy Board's Disciplinary Committee, as set out in Article 7(16) of the Accountancy Profession Act is made up of five members, two of which are appointed from a list of not less than ten persons submitted to the Board by the Malta Institute of Accountants (MIA) and of the three remaining members at least one person must be a warrant holder. Furthermore, the Board appoints one of the members who held a warrant, to act as Chairman.

As in the prior year, the composition of the Disciplinary Committee was made up of the following members:

Chairman
Mr. Godfrey Leone Ganado FIA, CPA

Members
Dr. Bernice Buttigieg LL.D, B.A., M. Jur (EU & Comp. Law);
Mr. Marcel Cassar MBA (Manchester/Wales), FIA, CPA;
Ms. Helen Meli Attard FIA, CPA, CSA, MIM, MIT, B.A.(Hons Acc.), M.A. (Financial Services); and
Mr. Martin Said FCCA, FIA, CPA.

Secretary
Ms. Karen Sultana B. Accty (Hons), MIA, CPA

4.2. FREQUENCY OF MEETINGS

During the year, the Committee met twice, in November and December.

4.3. SUMMARY OF ACTIVITIES CARRIED OUT DURING 2011

The Disciplinary Committee met to discuss a number of warrant holders who had not adhered to the requirements of Directive 1 addressing continued professional education as well as the CPE Scheme issued by the Board's approved body – the MIA. Such non-compliance was a result of CPE returns not being submitted by warrant holders, CPE declarations not complying with annual and cumulative requirements as well as other CPE related matters.

Based on these meeting the following was agreed:

- Warrant holders not submitting their annual CPE returns would incur a fine of €50 for each annual CPE return not submitted. For those who still choose not to regularise their position in this regard without any just cause will be subject to further disciplinary action which may lead to the suspension of one's warrant and/or practising certificate withdrawal. The Board may also recommend to the Minister the withdrawal of the person's warrant.
- Warrant holders who did not comply with annual CPE requirements would incur a fine of €50 for each year of default. Furthermore, warrant holders will be required to

compensate for the shortfall in CPE activities by attending CPE activities equivalent to the shortfall identified by no later than 31 December 2013. Further disciplinary action, as noted above, can be taken against those who remain in default.

These letters will be sent out to defaulters during 2012.

4.4. PLANS FOR 2012

- ***Amendments to disciplinary procedures***

  In the coming year, it is the intention of the Board, in conjunction with the recommendations made by the Disciplinary Committee, to revise the law to facilitate disciplinary action which may be taken against annual return, annual registration fee and quality assurance regulatory fee defaulters. Such revision in the law will result in more timely action being taken against defaulting warrant holders and practising certificate holders as well as firms.

- ***Following up of disciplinary matters identified during 2011***

  The Disciplinary Committee will periodically meet to revisit the progress made by defaulters to come in line with the requirements set out in the law. This process may lead to further disciplinary action.

QUALITY ASSURANCE OVERSIGHT COMMITTEE

5.1. COMPOSITION

The Quality Assurance Oversight Committee (QAOC) as set out in Directive 4 of the Accountancy Profession Act is composed of five individual members appointed for a period determined by the Board which shall not exceed three years.

During 2011, the QAOC was made up of five Committee members who were as follows:

Chairman
Mr. Charles Rapa FCCA, FIA, CPA, MBA(Brunel/Henley), MIM

Members
Mr. Peter J. Baldacchino M.Phil (Lough), FCCA, FIA, CPA;
Ms. Heather Briers FCA;
Mr. Alfred Lupi FCCA, BSc Econ, FIA, CPA; and
Dr. Michelle Mizzi Buontempo LL.D., M.A. (Fin. Serv.)

Secretary
Mr. Marcel P. Coppini FCCA, FIA, CPA

5.2. FREQUENCY OF MEETINGS

The Committee held a total of four meetings during the year – in March, May, August and December 2011.

5.3. SUMMARY OF ACTIVITIES, VISITS AND FINDINGS DURING 2011

5.3.1. Quality assurance visits

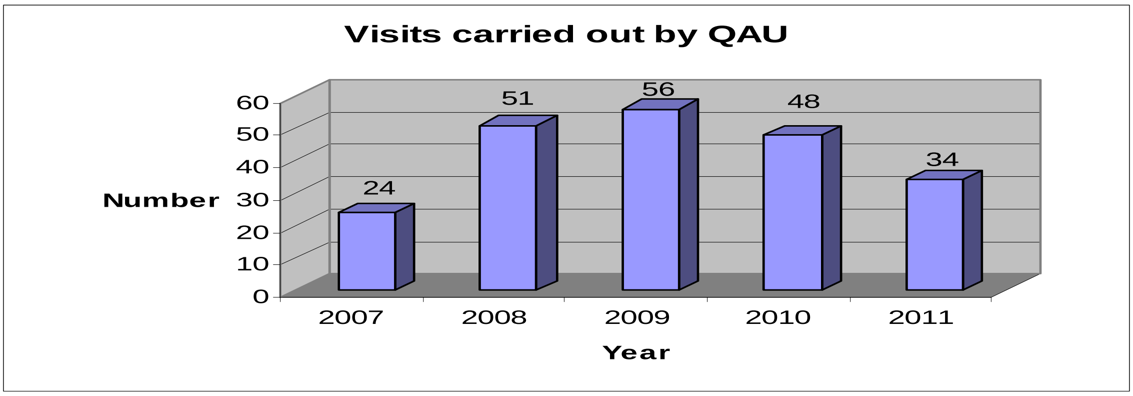
Based on declarations made in the Annual Returns covering the year ended 2010, locally there were a total of 164 sole practitioners providing statutory audit services. In addition up until year end there were 54 registered audit firms, of which 3 were newly registered and another 3 de-registered during 2011.

Since the first year of operations in 2007, the Quality Assurance Unit (QAU) carried out a total of 213 quality assurance visits covering all audit practitioners. This is illustrated in Chart 5.1. The unit is currently in the process of carrying out its second cycle of visits.

During the year, the QAOC has revised its visit cycle for auditors who do not audit public interest entities. The visit cycle for these practitioners has been extended from four years to six years. The visit cycle established by the QAOC for auditors of public interest entities has remained at three years in line with the requirements of the EU Statutory Audit Directive.

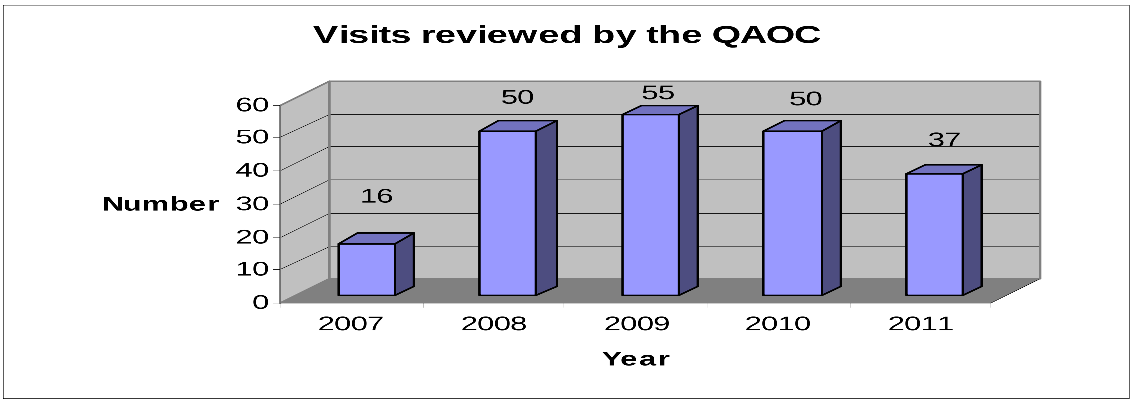
It is pertinent to point out that 39% of the QAU's total available time has gone to carrying out QAU visits in 2011. Further analysis indicates that only 57% of the reviewers' time was spent on inspection visits – whereas the rest (43%) has been dedicated to Accountancy Board matters. This is hardly surprising when one considers that of one of the three reviewers then available allocated 50% of her time solely on Accountancy Board matters. The average time spent on monitoring visits works out to 80 hours per visit.

Chart 5.1 – Visits carried out by the QAU



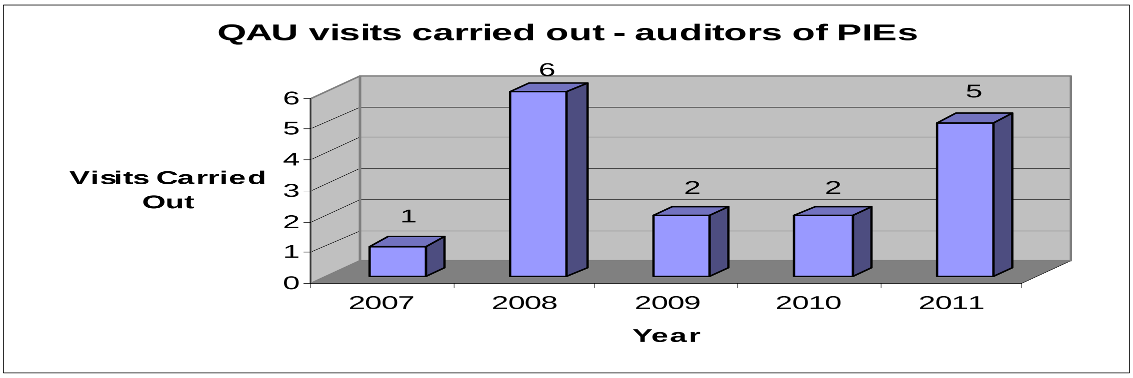
On completion of visit documentation prepared by QAU reviewers, visit work-packs are reviewed internally. Once the work-packs are finalised, the QAU passes on its recommendations based on its findings to the QAOC for its review. During the year 2011, the QAOC has reviewed and closed down 37 visits bringing the total visits reviewed by the QAOC to 208. This is illustrated in Chart 5.2 below.

Chart 5.2 – Visits reviewed by the QAOC



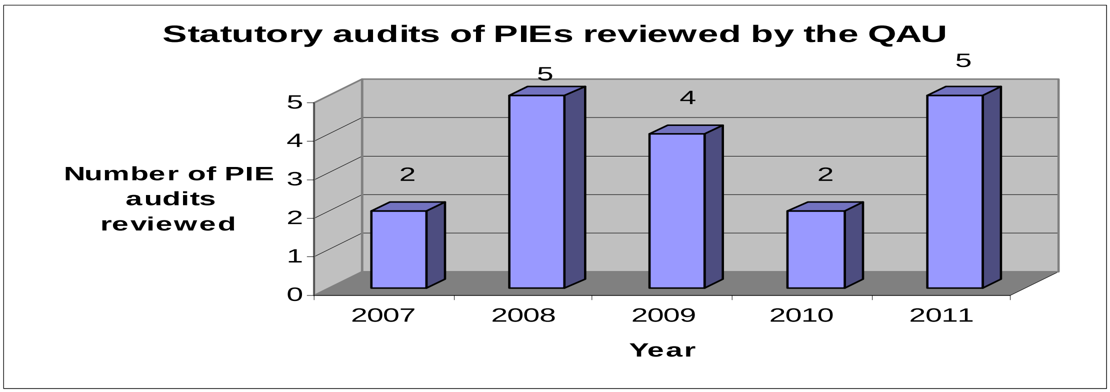
As per the 2010 transparency reports submitted, there were 11 auditors/audit firms auditing public-interest entities of which 5 audit firms were subjected to QAU visits in 2011. The number of auditors/audit firms visited by the QAU is shown in Chart 5.3.

Chart 5.3 – Visits to auditors of Public-Interest Entities



The QAU as part of its monitoring cycle reviewed a total of 5 audit files of public interest entities during 2011. Since it began its monitoring process in 2007, the QAU has reviewed a total of 17 statutory audits of public interest entities as illustrated in Chart 5.4.

Chart 5.4 – Public-Interest Entity Audits Reviewed by the QAU



On the basis of information submitted by audit entities carrying out PIE audits in their 2010 transparency report, there were 40 listed entities, 26 credit institutions (which 6 are listed) and 49 insurance companies (of which 1 is listed). 85% of the PIEs are audited by the Big 4 audit firms.

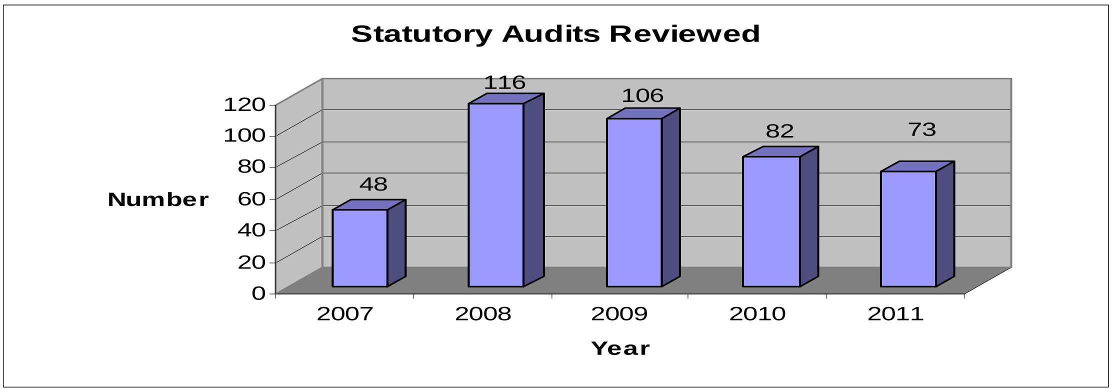
5.3.1.1 Conclusion of quality assurance reviews during 2011

During the course of 2011, the QAU carried out a total of 34 visits. This represents a decrease of 14 visits when compared with the prior year as depicted in Chart 5.1. This was the result of a reduced QAU staff compliment during 2011. The QAU also reviewed 5 practices carrying out audits of PIEs (of which two were Big 4 firms). More time was dedicated to these visits. The QAOC approved 37 reports as shown in Chart 5.2. These related to the following types of audit practices:

- 5 full-time sole practitioners;
- 22 part-time sole practitioners;
- 6 firms with less than five but more than two principals; and
- 4 firms with less than three but more than one principal.

The QAU has since its inception reviewed a number of audit files. This is depicted in Chart 5.5 and shows that in 2011, a total of 73 files were reviewed. The drop in audit files reviewed during 2011 is due to the fact that during the year the QAU based its reviews on files which exceed the thresholds laid down in article 185(1)(b) of the Companies Act dealing with exemptions for small companies, apart from the fact, that less visits were carried out during the year.

Chart 5.5 – Audit files reviewed by the QAU



5.3.1.2 Overview of reports

As in past years, reports are categorized for internal purposes into ratings which are determined by the instances and magnitude of non-compliance with the relevant regulations, the level of commitment and ability of the firm/sole practitioner to correct the problems identified and the regulatory action, if any, which the QAOC considers should be applied.

During the year, the QAOC reviewed a number of practitioners and firms which had already been visited during the first cycle. Practitioners and firms which had during the first visit undertook in their confirmations to address issues raised during the visit, but which remained unaddressed in the second cycle visit found that the QAOC took a less sympathetic view to breaches identified. This resulted in a number of practitioners and firms being faced with conditions and impositions made by the QAOC as a result of continued non-compliance.

In addition during the year, practices and firms have introduced clarified ISAs into their audit approach. However it was noted that in some cases further tailoring is required to established procedures.

However overall the findings noted indicate a relatively consistent level of report findings were noted.

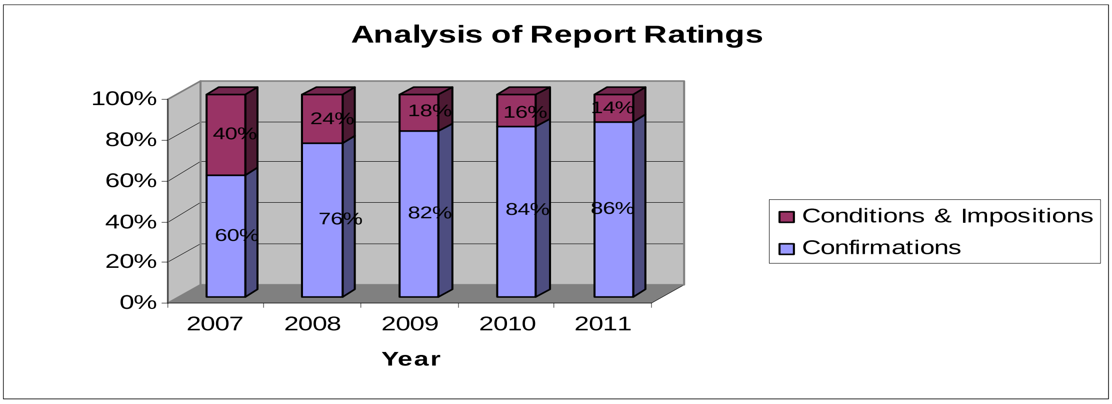
As a consequence by the end of the year, the QAOC had asked practitioners/firms on 86% of visits for just confirmations as opposed to 84% in 2010, 82% in 2009, 76% in 2008 and 60% in 2007.

Furthermore, conditions including impositions such as follow up visits, hot file reviews and external audit compliance reviews and external cold file reviews were sanctioned on 14% of practitioners/firms visited in 2011 when compared to 16% in 2010, 18% in 2009, 24% in 2008 and 40% in 2007. This is illustrated in Chart 5.6.

While this may indicate improved audit quality standards, there is still ample room for improvement – particularly in those areas noted later on in this section of the report. Perhaps more specifically, areas which remain of concern to the QAU are in relation to audit documentation, audit evidence, going concern and professional scepticism. The unit has also come across instances where inadequate safeguards were in place to address independence threats. This again is an area which needs to be look at more closely.

In December 2011, in line with Directive 4 to the Accountancy Profession Act, the QAOC referred a case to the Accountancy Board for consideration by its Disciplinary Committee. This case, refers to one practitioner, whose breaches, noted during one of the monitoring visits in 2011, were of significant concern to the QAOC. Other than breaches, pertaining to regulatory compliance, the QAOC was of the opinion that the practitioner's audit quality standards fall short of international standards on auditing. The QAOC awaits the outcome of this referral.

Chart 5.6 – Analysis of Report Ratings

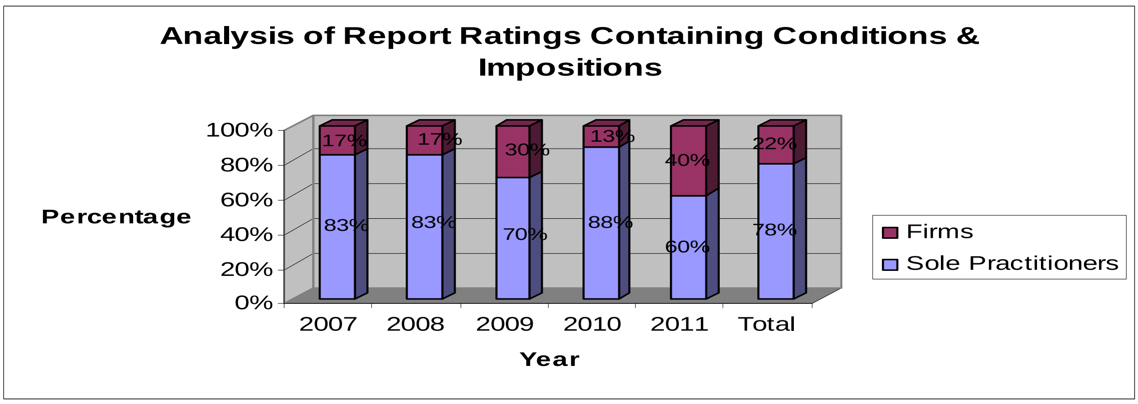


During 2011, conditions including impositions on practitioners/firms can be analysed as follows:

- 60% required external audit compliance reviews and cold file reviews to be conducted;
- 20% required follow up visits to be carried out; and
- 20% required hot file reviews to be carried out.

Furthermore, if one were to analyse the composition of reports issued featuring conditions & impositions one would note that the majority of conditions & impositions were sanctioned on sole practitioners. As can be seen in Chart 5.7, apart from 2009 and during 2011, this trend has remained fairly consistent during the last five years.

Chart 5.7 – Analysis of Report Ratings Containing Conditions & Impositions



The following list identifies the areas in which the most common weaknesses were noted and which require improvement based on the findings identified during the quality assurance visits carried out throughout 2011.

- *Code of Ethics – Provision of Non-Assurance Services to Non-Public Interest Entities*
  This topic continues to be encountered year-on-year during visits carried out by the Quality Assurance Unit. Although in most instances, it was found that firms and sole practitioners had established and documented policies and procedures to address circumstances in which non-assurance services are provided in addition to the audit of non-public interest entities, it was noted that documentation found in the audit file was lacking or not present.

  When the practice or firm assesses that after evaluating the significance of the threat and determines that safeguards can be introduced to mitigate the independence threat arising, these considerations should be appropriately documented.

- *Accountancy Profession Act – Professional Indemnity Insurance*
  Visits carried out during the year have revealed a number of issues arising from non-compliance with professional indemnity insurance requirements. Examples of such weaknesses can be summarised as follows:

  - in a few cases sole practitioners were not covered by a professional indemnity insurance policy as required by the Accountancy Profession Act;
  - it was noted that in some instances the professional indemnity insurance policy did not cover the practitioner against any losses or damages which a client or any person may suffer as required by the Accountancy Profession Act;
  - in a particular case a sole practitioner's cover was less than his total annual fees (in this case the practitioner had no connected undertakings) multiplied by three and was also less than €100,000;
  - in other cases although the practitioner/firm had a professional indemnity insurance cover this cover did not list connected undertakings. In addition, the amount covered in the policy did not ensure that the principals of the connected undertakings were also adequately covered as required by guidance issued by the Accountancy Board entitled 'Clarification of the definition of principal and the legal requirements for professional indemnity insurance and quality assurance regulatory fee'.

  On the basis of such findings, practitioners and firms if they have not done so already are requested to familiarize themselves with professional indemnity insurance requirements emanating from the Accountancy Profession Act, Accountancy Professional Regulations and from the clarification document issued by the Accountancy Board.

- *ISA 230 – Audit Documentation*
  Audit documentation requires that the audit file contains a record of the audit procedures performed, the relevant audit evidence obtained and should include the conclusions reached by the auditor. Ensuring that the right balance is maintained, continues to pose a challenge for firms and practitioners. However auditors are required to prepare audit documentation which is sufficient enough to enable an experienced auditor, with no previous connection with the audit to understand the audit procedures performed, the results and evidence of these procedures, as well as to be able to identify

significant matters arising during the audit and the conclusions reached on those significant matters.

- *ISA 240 – The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*
  Documentation of fraud considerations in accordance with ISA 240 remains an area of concern as in past years. Although assurances were given that such considerations had been addressed during the course of the audit, in such cases no documentation was found on file.

- *ISA 250 – Consideration of Laws and Regulations in an Audit of Financial Statements*
  During the course of the QAU visits it was noted that a number of firms and practitioners did not document their consideration of laws and regulations. However through discussion it was noted that in the most part, practitioners/engagement partners had gained a general understanding of the legal and regulatory framework within which the company operated and how the company adhered to such legal and regulatory requirements. Practitioners and firms are reminded that such considerations should be adequately documented on file.

- *ISA 260 – Communication with those Charged with Governance*
  In respect to this ISA it was noted that the major weaknesses noted arose when verbal communications were made instead of written ones. In a number of cases, the audit file did not include documentation of the significant findings arising from the audit. Such documentation did not also include when such oral communication occurred and to whom such matters were discussed with.

- *ISA 500 – Audit Evidence*
  Audit evidence is necessary to support the auditor's opinion and report. However our visits identified instances where sufficient audit evidence was not found on file. On this basis, QAU reviewers were unable to determine how the auditor drew conclusions on which the audit report was based.

- *ISA 530 – Audit Sampling*
  Compliance with ISA 530 dealing with audit sampling continues to be a standard where weaknesses were noted. Practitioners are reminded that although audit procedures can be applied to less than 100% of the items in the population, the auditor needs to ensure that the items tested provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

- *ISA 550 – Related Parties*
  From the audit files reviewed, it was noted that in a number of instances, the audit engagement team did not adequately identify and document related parties as part of the auditor's understanding of the entity being audited. This may lead to related party transactions not being identified during the course of the audit and company's management making inappropriate disclosures in the financial statements. Thus more effort is required in this regard.

- *ISA 570 – Going Concern*
  During the course of the 2011 reviews, a number of breaches were noted in respect to going concern. In particular, a number of instances were noted in which an emphasis of matter paragraph was included in the audit report when in the view of the QAOC, this emphasis of matter paragraph was not appropriate or not necessary.

The QAOC has noted that in some instances, based on the evidence obtained during the course of the audit, although the auditor has determined that a material uncertainty does not exist, an emphasis of matter paragraph is still used in the auditor's report to highlight a particular matter. In the view of the QAOC this is of concern, as it goes against the spirit of this ISA.

On the other hand when an emphasis of matter paragraph is necessary due to the fact that the going concern assumption is appropriate but a material uncertainty exists, the auditor should ensure that the financial statements adequately disclose the matters identified in ISA 570 and that the emphasis of matter paragraph is worded according to the requirements of this ISA.

- *ISA 580 – Written Representations*
  With the clarification of this ISA, revisions have been required to the letter of representation. To a large extent, we noted that, letters of representations did incorporate the new requirements. However it was noted that in a small number of instances the letter of representation did not include a list of the effects of the uncorrected misstatements as required by ISA 450.

- *Cold File Reviews and Audit Compliance Reviews*
  The carrying out of periodic cold file reviews as well as audit compliance reviews arise from ISQC 1 requirements and enable the firm to identify areas requiring improvement. From reviews carried out during the year, it was noted that in some cases such reviews were not carried out whilst in others it was noted that the frequency of such reviews were not carried out in accordance with ISQC 1 requirements.

  In this regard, the Accountancy Board issued guidance notes on its website under the heading: 'Guidance Note on Compliance Reviews under 'Clarified' ISQC 1'. A summary of the frequency of such recommended reviews is reproduced below:

<table>
<tr><th colspan="2" rowspan="2">Summary</th><th colspan="2">Audit Compliance Review</th></tr>
<tr><th>Whole Practice Review</th><th>Cold File Review</th></tr>
<tr><td rowspan="2">Sole practitioner – with no audit staff</td><td>Frequency</td><td>Once every 3 years (minimum)</td><td>Once every 3 years (minimum)</td></tr>
<tr><td>Reviewer</td><td>Internal or External</td><td>External (not EQCR reviewer)</td></tr>
<tr><td rowspan="2">Sole practitioner – with audit staff</td><td>Frequency</td><td>Annually</td><td>Once every 3 years (minimum)</td></tr>
<tr><td>Reviewer</td><td>Internal or External</td><td>Internal or external (reviewer not involved on audit/EQCR)</td></tr>
<tr><td rowspan="2">Firm – with no audit staff</td><td>Frequency</td><td>Annually</td><td>Annually (each partner once every 3 years - minimum)</td></tr>
<tr><td>Reviewer</td><td>Internal or External</td><td>Internal or external (reviewer not involved on audit/EQCR)</td></tr>
<tr><td>Firm – with audit staff</td><td>Frequency</td><td>Annually</td><td>Annually (each partner once every 3 years - minimum)</td></tr>
</table>

	Reviewer	Internal or External	Internal or external (reviewer not involved on audit/EQCR)

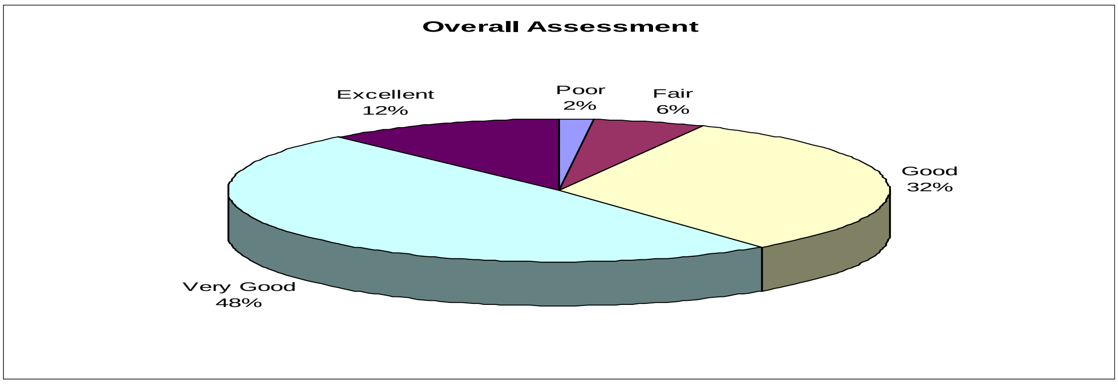
5.3.2. Evaluation forms – feedback from practitioners

Feedback from practitioners and firms has continued to be sought through Evaluation Forms sent once the QAOC report has been finalised. During the year, a number of evaluation forms were received. Out of a total of 37 visits concluded by the QAOC a total of 36 (97%) evaluation forms were received. Of this total 6 evaluation forms pertained to visits which were finalised by the QAOC in 2010. At year end, 7 evaluation forms pertaining to 2011 are still outstanding but the bulk relate to visits which were finalised towards the end of the year.

The percentage of evaluation forms received increased from 76% to 97% by year end.

As in past years, overall feedback received from practitioners and firms was very positive. Chart 5.8 provides a graphical illustration of the summary of results:

Chart 5.8 – Evaluation Form Summary



5.3.3. Chartered Accountants Regulatory Board of Ireland (CARB)

During 2011, the Chartered Accountants Regulatory Board of Ireland (CARB) through Ms. Heather Brier's presence and contribution at QAOC meetings has again been an invaluable aide to the QAU. For reasons beyond their control, CARB was unable to provide the QAU the same support given to it in previous years. It is envisaged that this support will be resumed in the coming year.

5.3.4. The Institute of Chartered Accountants in England and Wales (ICAEW)

In 2011, the Accountancy Board has asked for the assistance of ICAEW in respect of quality assurance matters primarily dealing with training focusing on banks and insurance companies.

The ICAEW had accepted to assist the QAU reviewers in this and during the year assisted in the carrying out one of the Big 4 visits. During this visit a local bank was selected for review and such review was carried out jointly with the local reviewers being trained on site with ICAEW.

Further training will be carried out in the coming year.

5.3.5. Team meetings

Although no team meetings were attended in Belfast, Northern Ireland with CARB as part of the Unit's continuous training programme, locally one team meeting was organised in June.

5.4. PLANS FOR 2012

- For the last three years, the QAU has been experiencing an acute shortage of qualified and experienced audit personnel to fill the role of QA reviewers. The problem has been further exacerbated by the resignation of one reviewer towards the latter part of the year, whilst another reviewer will be on maternity leave and reduced working hours for most of 2012. This leaves the Unit with just one full time reviewer. Whilst no effort is being spared by the Board to address this issue, until a solution is found to this impending problem it is envisaged that during 2012, with just one reviewer, the unit will conduct no more than 14 visits as noted below:

    - 3 full-time sole practitioners;
    - 4 part-time sole practitioners; and
    - 7 audit firms.

  The above numbers will be reviewed once new QA reviewers will be engaged.

- The biennial QAU workshop which is organised in collaboration with the Malta Institute of Accountants which was scheduled to be held in November 2011 had to be postponed until the 29th February 2012, for reasons beyond the Unit's control

- Resume technical and other working relationship with CARB

- Maintain and further develop the Accountancy Board portal

- Training of new recruits

LEGISLATIVE CLARIFICATIONS COMMITTEE

6.1. COMPOSITION

During the year, the Committee continued analysing legislative amendments referred to it by the Board and was made up of the following members:

Chairman
Mr. Bernard Scicluna FCCA, FIA, AMIT, CPA

Members
Mr. Marcel P. Coppini FCCA, FIA, CPA;
Ms. Angele Grech BA(Hons) Accty., CPA;
Ms. Karen Sultana B. Accty (Hons), MIA, CPA; and
Mr. Anthony Zarb FCCA, FIA, CPA, MBA(Warwick).

6.2. FREQUENCY OF MEETINGS

During 2011, the Legislative Clarifications Committee held three meetings.

6.3. SUMMARY OF ACTIVITIES CARRIED OUT DURING 2011

During the year, the Legislative Clarifications Committee discussed and drafted proposed changes in the Law as a result of the clarifications made in 2009 and 2010, following discussions with the Board's legal advisor. Unfortunately until the end of the year the amendments proposed had not yet been incorporated into Law. Apart from matters arising in prior years, the Committee also looked into the regulation of joint audits.

6.4. PLANS FOR 2012

It is envisaged that during 2012, the changes proposed by the Committee and approved by the Board will, where necessary be passed through Cabinet and subsequently be reflected in the Law.

Should there be any other matters arising during 2012, the Committee will look into these matters and based on its analysis, make suggestions to the Board on an ongoing basis.

It is pertinent to point out that a new Code of Ethics, will come into force in 2012. The existing Directive 2 is being revamped to bring it in line with IFAC's International Ethics Standards Board for Accountants' (IESBA) pronouncements on ethical standards.

INVESTIGATIVE COMMITTEE

7.1. COMPOSITION

This Committee is made up of three members and is formed on an ad hoc basis. During the year, the Investigative Committee was made up of the following individuals:

Mr. Simon Flynn FCCA, BA(Hons)Accty., FIA, CPA;
Ms. Elvia George BA(Hons) Accty., FIA, CPA; and
Mr. Benjamin Rizzo ACMA, FIA, CPA.

7.2. FREQUENCY OF MEETINGS

Throughout the year, the Investigative Committee met on two occasions.

7.3. SUMMARY OF ACTIVITIES CARRIED OUT DURING 2011

During the year, the Committee met to discuss a complaint lodged with the Accountancy Board. As a consequence of recommendations made by the Investigative Committee in respect to this complaint, the Board decided not to refer the case to the Disciplinary Committee.

Although another complaint has been lodged with the Board, this compliant has not yet been referred to the Committee as further correspondence is required before an assessment can be made.

7.4. PLANS FOR 2012

In the coming year, should the need arise, the Accountancy Board will appoint on an 'ad hoc' basis Committees to investigate complaints received by the Board before determining whether these should be referred to the Disciplinary Committee.

CPE COMMITTEE

8.1. COMPOSITION

During the year, the Accountancy Board's CPE Committee was made up of the following members:

Mr. Peter J. Baldacchino M.Phil (Lough), FCCA, FIA, CPA;
Mr. Simon Flynn FCCA, BA(Hons)Accty., FIA, CPA;
Ms. Maria Micallef B.A. Hons Accountancy, FIA, CPA;

and assisted by:

Ms. Catherine Mallia Bonavia B.Com (Hons.) Mgt; and
Ms. Karen Sultana B.Accty(Hons), MIA, CPA.

8.2. FREQUENCY OF MEETINGS

Throughout 2011, the CPE Committee held eleven meetings, once monthly except for the month of December when a meeting was not held.

8.3. SUMMARY OF ACTIVITIES CARRIED OUT DURING 2011

Throughout the year, the Committee discussed a number of CPE exemption applications lodged with the Board and made an initial assessment of these exemption requests for final approval by the Accountancy Board. Although warrant holders were informed that CPE exemption requests should be sent by warrant holders within one month after which the condition giving rise to the CPE exemption came into being, it was noted that in a number of cases this was not being adhered to. As a result warrant holders were informed that such late CPE exemption requests would only be considered by the Board and Committee if received by June 2011. After this date, warrant holders were informed that late exemption requests would not be allowed or if allowed would incur a fine imposed by the Board. As a result a number of warrant holders who filed CPE exemption forms after this date incurred a fine amounting to €50.

Also during the course of the year, the Committee assisted the MIA in the revision of its CPE scheme which all warrant holders must comply with. In particular, it provided its feedback in respect to the introduction of a procedure which must be followed by warrant holders who return from a period in which they were granted an exemption from CPE by the Board.

8.4. PLANS FOR 2012

The Committee intends to continue to meet to make initial assessments on the eligibility of warrant holders to be granted a CPE exemption.

It also intends to commence a monitoring process to determine whether warrant holders have complied with CPE requirements derived from Directive 1 as well as the CPE scheme over both an annual basis and over a three year rolling period.

PROFILE OF THE AUDIT & ACCOUNTANCY PROFESSION

Throughout the year, the Board has considered a number of applications for CPA warrants as well as practising certificates in auditing. On the basis of evaluations of these applications the Board recommended to the Minister of Finance, the Economy and Investment the approval of a number of CPA warrants. Furthermore the Board approved a number of practising certificates in auditing and registered a number of firms.

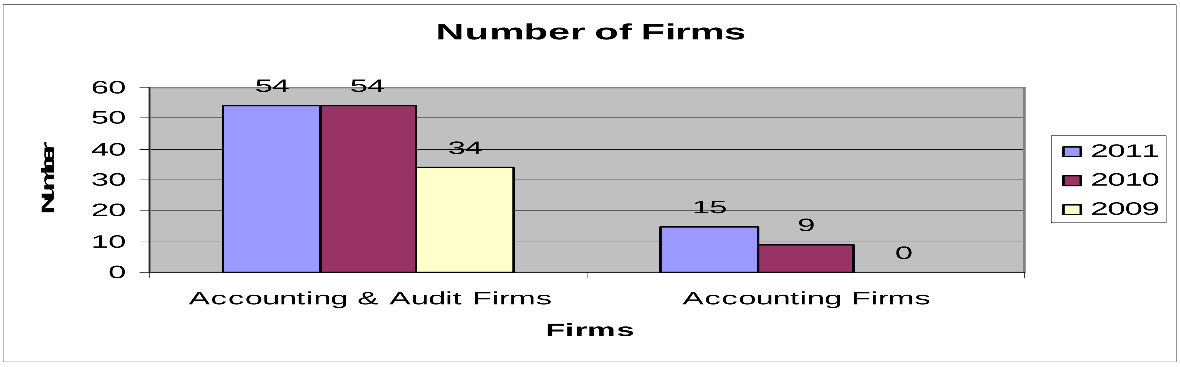
9.1. FIRMS

During the year, the number of audit firms remained consistent with that of the prior year, as three new audit firms were registered whilst during the same period three other firms were de-registered with the Board.

In regard to accounting firms, the number of registered firms rose from nine to a total of fifteen by the end of the year, as a result of the Board's work in identifying corporate entities providing accounting services.

These figures are depicted as follows:

Chart 9.1 – Number of firms registered with the Accountancy Board



The composition of principals making up the both accounting & auditing firms as well as accounting firms varies from one firm to another. However on a general basis, firms are composed of a few principals – with the majority of accounting firms having only one principal (Chart 9.3) whereas accounting & audit firms have 2 principals (Chart 9.2).

Chart 9.2 – Accounting and audit firms – analysis of principals

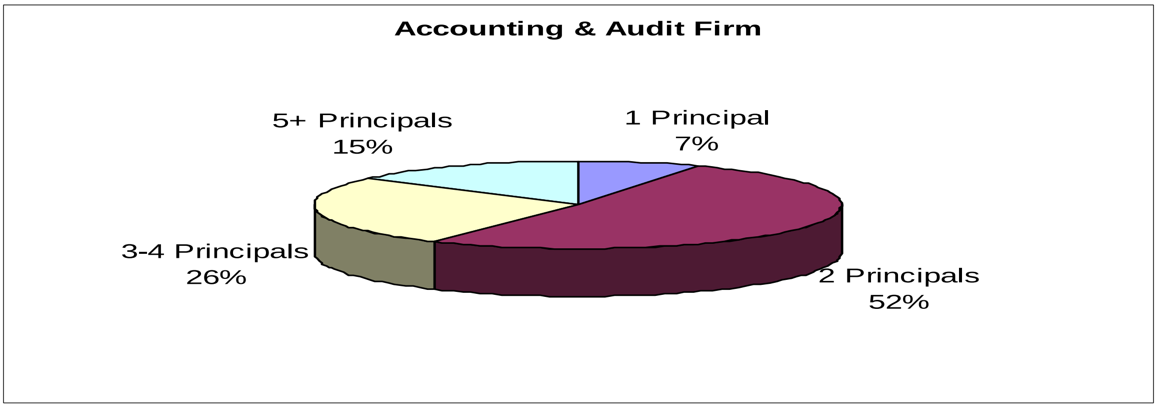
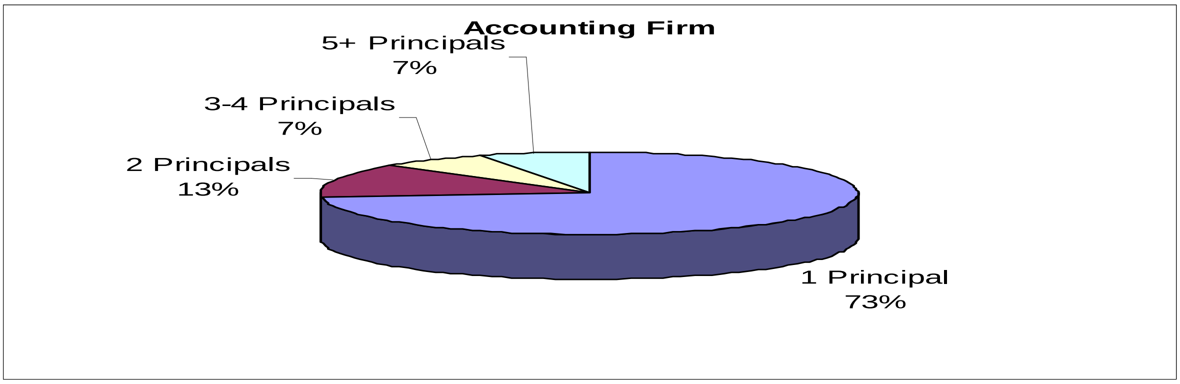
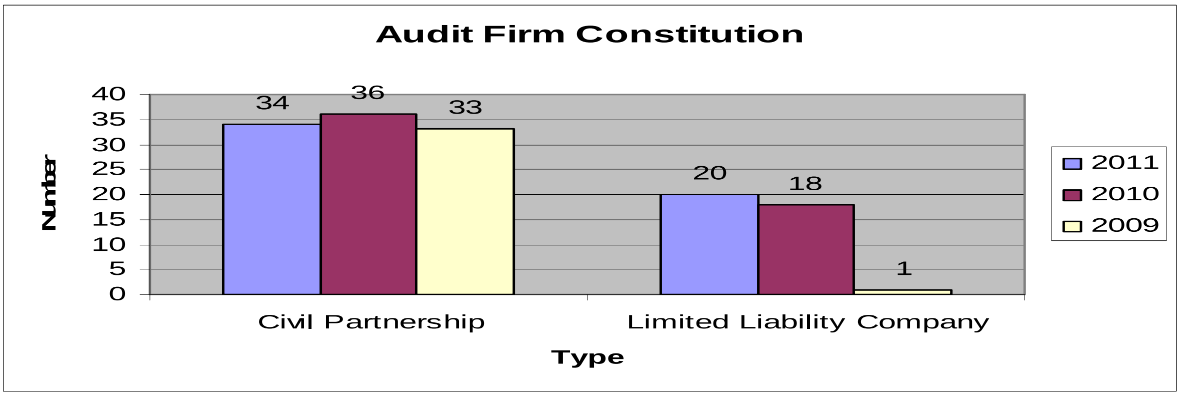


Chart 9.3 – Accounting firms – analysis of principals



From review of the constitution of both accounting firms as well as accounting & audit firms, it is of interest that all accounting firms are structured as companies. On the other hand accounting & audit firms are composed of both partnerships and companies structured in a manner such that the liability of its owners is directly or indirectly limited. At year end, the Board's registered audit firms (2011: 54; 2010: 54) were constituted as follows:

Chart 9.4 – Audit firm constitution



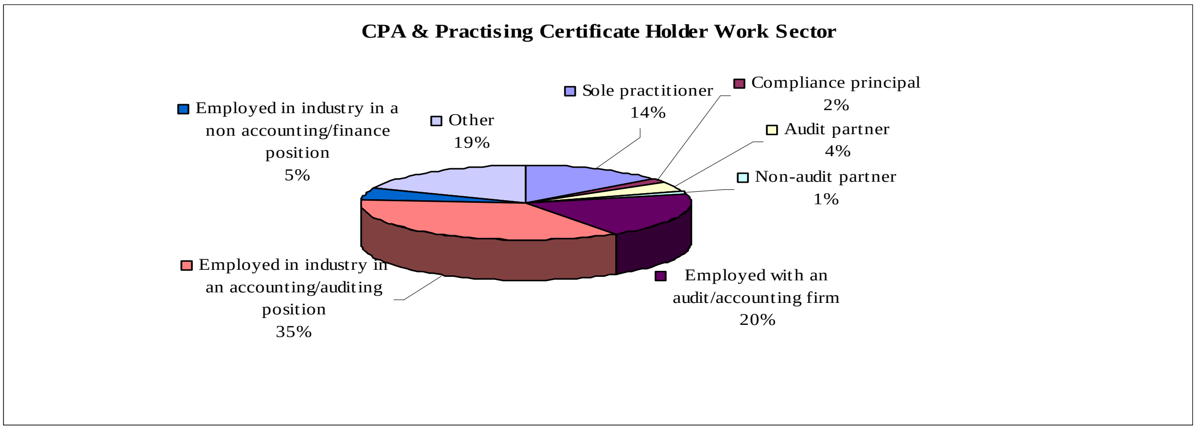
9.2. WARRANT HOLDERS AND HOLDERS OF A PRACTISING CERTIFICATE IN AUDITING

Throughout the year, applications were received for both warrants and practising certificates in auditing.

During the course of 2011, both warrant and practising certificates in auditing were approved on a monthly basis by the Board with certificates being presented on two separate occasions during the year. By the end of 2011, the Board regulated 1,785 warrant holders including 1,015 holders of a practising certificate in auditing. During the year under review, the Accountancy Board approved 85 warrants and 39 practising certificates in auditing to 93 individuals during 2 ceremonies, one held in June and the other in December.

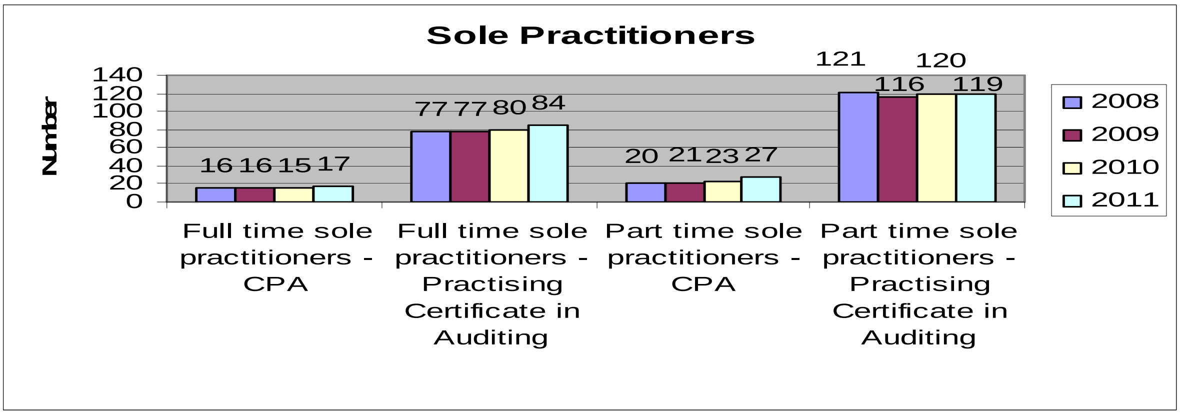
Based on the declarations made in the 2010 Annual Returns, Chart 9.5 illustrate warrant holders and holders of practising certificates employment status analysed by work sector.

Chart 9.5 – CPA & Practising certificate in auditing work sector



As illustrated in Chart 9.6, in regard to CPA warrant holders, during 2011 there were 17 full-time sole practitioners and 27 part-time sole practitioners. Furthermore, in regard to practising certificate holders in total there were 84 full-time sole practitioners and 119 part-time sole practitioners. No significant fluctuations were noted during the year.

Chart 9.6 – Analysis of sole practitioners practicing in Malta



Furthermore, practising certificate holders being subject to Quality Assurance Reviews can be analyzed as follows: 74 full-time sole practitioners; 90 part-time sole practitioners; and 54 firms as shown in Chart 9.7. The figures have remained fairly stable, with a small decrease noted in the part-time sole practitioners providing audit services.

Chart 9.7 – Sole practitioners & audit firms subject to a quality assurance review