Accountancy Board

Quality Assurance

2014 - ANNUAL REPORT

Quality Assurance Oversight Committee

(issue date - March 2015)

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CHAIRMAN'S STATEMENT

I am pleased to present the eighth annual report of the Quality Assurance Oversight Committee ('QAOC'), my first as Chairman. The annual report is presented in accordance with the requirements of Article 7 (19) (20) of the Accountancy Profession Act, Cap 281. The report sets out the principle findings arising from the inspections of sole practitioners and audit firms carried out by the Quality Assurance Unit ('QAU') during the year to 31 December 2014.

The QAOC exercises judgment in determining the findings to include in this public report on each inspection, taking into account their relative significance in relation to audit quality, both in the context of each individual inspection and in relation to any areas of particular focus in our overall inspection programme for the relevant year. In this document, we have commented on themes arising or issues of similar nature identified across more than one inspection.

The review of individual audit engagements and policies and procedures supporting audit quality are not restricted to compliance with the requirements of relevant International Standards of Auditing and local regulatory requirements. Reviews of individual audit engagements place emphasis on the appropriateness of the key audit judgments made in reaching the opinion together with the sufficiency and appropriateness of the audit evidence obtained. The quality assurance inspectors seek to identify areas during the visits where improvements are, in their view, needed to safeguard audit quality and comply with regulatory requirements. Accordingly the reports issued to the audit firms and practices after the visits place greater emphasis on weaknesses identified requiring action rather than areas of strength.

The quality review inspections are not designed to discover all deficiencies and weaknesses which may exist in the design and/or implementation of the firm or practice policies and procedures. Moreover the engagements file review selection process is risk based on a limited number of files selected.

We acknowledge the co-operation and assistance extended to our reviewers from compliance principals of audit firms, sole practitioners and staff in the conduct of our 2014 inspections. A number of practices continue to be receptive to the findings. However, in our second cycle of visits we are coming across a number of repeat breaches. Timely and effective remedial action is critical to the Quality Assurance process and one augurs that in future, one will demonstrate more rigour and commitment to the remediation of findings noted in the QAOC reports.

The focus in this report is on matters where the Committee believes that improvements are required to safeguard and enhance quality standards on audit engagement files reviewed by the QAU. We set out our key findings to the profession in this regard in Section 3.4. While this report is not intended to provide a balanced score sheet, we highlight certain matters which we believe contribute to audit quality.

2014 will undoubtedly be remembered as the year where the European Commission implemented tougher regulations on statutory audits particularly in relation to the audits of public interest entities[1]. The new Directive and Regulations governing audit policy will give rise to changes in audit methodologies. With these new rules, the European Commission has created a framework to restore investor's confidence in audits, safeguarding auditors' independence, promote better governance and more transparency in financial reporting. This framework will provide better mechanisms to safeguard the Public Interest. The QAOC remains committed to deliver its responsibilities in an efficient and effective manner in line with the new regulations.

From a local perspective, these reforms will undoubtedly affect stakeholders in different ways. PIEs will need to reinforce their corporate governance structures particularly in relation to audit rotation, the provision of non audit services and more onerous roles of audit committees. SMEs will also be impacted by the audit reforms but probably to a lesser extent. .

I would like to acknowledge the hard work and commitment of the members of the QAOC, and the QAU team led by Mr Marcel Coppini. It is with their concerted effort that we are able to demonstrate the full value of the quality assurance process.

I firmly believe that, whatever the changes brought about by regulatory reform, the QAOC and its agents will continue to play a vital role in maintaining the quality of the audit profession.

Mr. Peter J Baldacchino M.Phil (Lough), FCCA, FIA, CPA, CSA
Chairman – QAOC & member of the Accountancy Board

31 March 2015

[1] Public interest entities – entities whose transferable securities are admitted to trading on a regulated market within the meaning of point 14 of article 4 (1) of Directive 2004/39/EC, a credit institution as defined in point 1 of Article 1 of Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions (1) and insurance undertakings within the meaning of Article 2 (1) of Directive 91/674/EEC and such other entities as may be prescribed by the Board.

HEAD OF QUALITY ASSURANCE UNIT'S REPORT

The audit profession in Malta is one profession which has moved away from self regulation and one which has been subjected to independent Public Oversight and Quality Assurance ever since Directive 4 to the Accountancy Profession Act was introduced in 2007. With the expectations gap on auditor reporting widening the need for audit practices to have robust systems of internal quality controls, and adequate risk management procedures are today more pronounced than ever before. Moreover, the financial and the banking crises which wreaked havoc across the globe in recent years were undoubtedly two of the main reasons for the need to step up audit regulation worldwide.

Since February 2007, when inspection visits to audit practices were introduced, the QAOC through its duly appointed agents, the QAU, has been monitoring the audit profession, not only to safeguard the Public Interest but also to ensure that audit quality standards and Ethics applied by all audit practitioners are in line with internationally accepted auditing standards, as indeed with any other regulatory framework pertinent to statutory audits.

The Accountancy Board and the Quality Assurance Unit participated in meetings at EU level on the ongoing debate of the Audit Reform proposals. The consultation process lasted four years and it was not until June of 2014 that the finally agreed proposals were given the green light by the European Parliament. The changes brought about by these reforms will be transposed into our legislation by June 2016.

The QAU plays an active role within the European Audit Inspections Group (EAIG), whose primary purpose is to create an awareness of important issues and promote cooperation and consistency amongst European audit regulators on inspections. The group today shares inspection practices and findings amongst its members and facilitates discussions on topics related to audit inspections, with third parties such as standard setters (IAASB, IESBA)[2], the larger international audit networks and other stakeholders (including other European supervisory authorities (ESMA, FSB, BCBS)[2] and other professional organisations such as the ECG, EFAA, EGIAN, and FEE. The main scope of this dialogue with these organizations is that of promoting audit quality.

An important milestone for EAIG was the Common Audit Inspection Methodology (CAIM) project which, as its name suggests, seeks to harmonise inspection methodologies amongst all 27 EU member states and other EEA countries. Malta formed part of an eight member committee set up by the EAIG to oversee the realisation of this project. The first phase of the project was officially launched by

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2 For a list of acronyms used please refer to page 31 of this report

EAIG at its meeting in Madrid in November of 2014. This seeks to synchronise ISQC 1 methodologies being applied by European audit regulators to assess the propriety of the whole firm quality control procedures adopted by audit firms auditing Public Interest Entities.

Malta has also been a member of the International Forum of Independent Audit Regulators (IFIAR) since 2008. IFIAR brings together independent audit regulators from 51 jurisdictions across the globe. IFIAR is a member of the Monitoring Group which Group oversees audit and accounting related standard setting activities of the International Federation of accountants (IFAC) and monitors the activities of the Public Oversight Board (POB). IFIAR convenes annual plenary meetings to discuss issues and shares views relating to international audit quality, regulatory and market developments which could impact on the auditing profession.

Upholding the public interest is a prized goal which is closely shared by audit regulators, and investor groups alike. Our commitment to audit quality is reflected in the number of monitoring visits carried out since QA kicked in, and our active participation in fora, locally and abroad, to promote audit quality.

However, apart from safeguarding the Public Interest the QA process seeks to oversee the accountancy and audit profession which form an integral part of our dynamic and well-functioning financial services sector. Over a period of 13 years Malta established itself as an international financial centre of repute which today is contributing directly and indirectly to some 13% of our GDP and has the potential to grow even further. Public Independent Oversight of the profession serves to safeguard Malta's reputation in the field of Financial Services.

In spite of all the efforts by audit regulators worldwide, in its press release of the 3 March 2015, IFIAR reported, in its publication of its survey of inspection findings submitted by its members in 2014, a recurrence of high levels of deficiencies in key areas of public company audits around the world. This demonstrates the need for audit firms, to further improve audit quality.

Our report for 2014 not only seeks to highlight a number of the findings we came across during our monitoring visits, but also seeks to analyse the root causes of poor audit quality. Of particular concern is the increasing number of repeat breaches we have been coming across during our second cycle of visits to audit practices. This, in itself, is an indication that remediation procedures are not always timely and effective.

The larger international network firms' attention in 2014 has been directed to root cause analysis and remediation of findings from their own as well as external monitoring reviews.

The extended auditor reporting, now required for financial statements with a financial year on or after the 15 December 2016, (ISA 701) renders the auditor's reporting responsibility that more onerous. Only time will tell the extent to which this new reporting regime will impact on the audit profession, both locally and abroad.

Looking forward, we have set ourselves new goals including that of creating more awareness and more dialogue amongst all stake holders of the importance of Audit Quality, and to focus more closely in the areas of governance, enforcement and compliance.

Undoubtedly, 2015 will be another challenging and exciting year for the whole of the audit profession in Malta. The transposition of the EU Single Accounting Directive as indeed the new EU Statutory Audit Directive and the new EU regulations pertaining to PIEs will certainly bring about changes to the QAU's existing methodologies and procedures. We will also be implementing the first phase of the Common Audit Inspection Methodologies for all PIE audit firms as from 2015. The recently pronounced changes to the Ethics Code, the Continued Professional Directive as indeed the subtle changes to the Anti Money Laundering provisions will also be on the QAU's radar in the current year.

We all look forward to the new challenges ahead of us, and with the appropriate support and better dialogue from all stakeholders concerned, we are confident that these new emerging demands will be met.

Marcel Coppini FCCA, FIA, CPA
Head of Quality Assurance Unit and Secretary to the QAOC

31 March 2015

QUALITY ASSURANCE OVERSIGHT COMMITTEE| SECTION 1- COMPOSITION AND FREQUENCY

The supervision of the system of quality assurance is delegated by the Accountancy Board to the Quality Assurance Oversight Committee ('QAOC'). The day to day management of the system is delegated to the Quality Assurance Unit whose members act as agents to the QAOC. As at the date of the report, the composition of the QAOC was made up of the following five Committee members:

Chairman

Mr. Peter J Baldacchino M. Phil (Lough), FCCA, FIA, CPA, CSA; (Appointed on 12 February 2015);

Mr. Charles Rapa FCCA, FIA, CPA, MBA (Brunel/Henley); (Resigned on 12 February 2015)

Members

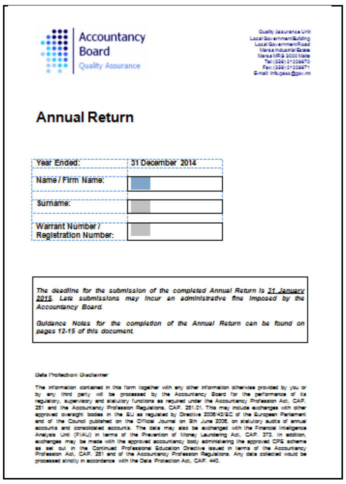
Ms. Heather Briers FCA; (Director CARB);
Mr. Alfred Lupi FCCA, BSc Econ, FIA, CPA;
Mr. Guido Mizzi FCCA, FIA, CPA; and
Mr. Peter Paris FIA, CPA

Secretary

Mr. Marcel P.Coppini FCCA, FIA CPA

The Committee held four meetings during the year – these were held in March, August, November and December 2014.

SECTION 2- THE QA PROCESS



Accountancy Board
Quality Assurance

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Local Government Road
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Tel: (356) 21239970
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E-mail: info.qaoc@gov.mt

Annual Return

Year Ended:	31 December 2014
Name / Firm Name:	
Surname:	
Warrant Number / Registration Number:	

The deadline for the submission of the completed Annual Return is 31 January 2015. Late submissions may incur an administrative fine imposed by the Accountancy Board.

Guidance Notes for the completion of the Annual Return can be found on pages 12-15 of this document.

Data Protection Disclaimer

The information contained in this form together with any other information otherwise provided by you or by any third party will be processed by the Accountancy Board for the performance of its regulatory, supervisory and statutory functions as required under the Accountancy Profession Act, CAP. 281 and the Accountancy Profession Regulations, CAP. 281.01. This may include exchanges with other approved oversight bodies in the EU as regulated by Directive 2006/43/EC of the European Parliament and of the Council published on the Official Journal on 9th June 2006, on statutory audits of annual accounts and consolidated accounts. The data may also be exchanged with the Financial Intelligence Analysis Unit (FIAU) in terms of the Prevention of Money Laundering Act, CAP. 373. In addition, exchanges may be made with the approved accountancy body administering the approved CPE scheme as set out in the Continued Professional Education Directive issued in terms of the Accountancy Profession Act, CAP. 281 and of the Accountancy Profession Regulations. Any data collected would be processed strictly in accordance with the Data Protection Act, CAP. 440.

The Quality Assurance Oversight Committee ('QAOC') is responsible for ensuring that professional services provided by practicing auditors, registered audit firms are of the highest possible standard by monitoring compliance in line with Audit Directive number 4 issued in terms of the Accountancy Profession Act (Cap 281) and of the Accountancy Profession Regulations 2009.

To achieve this, the Quality Assurance (QA) process comprises:

- An evaluation of the Annual Return submitted by all warrant holders, audit firms and accounting firms; and ;
- The carrying out of cyclical inspection visits to audit firms and sole audit practitioners.

The above processes are delegated to the QAU, whose reviewers are the duly appointed agents of the QAOC to carry out inspection visits.

As at 31 December 2014 there were 2,222 warrant holders. This included 1,227 holders of practising certificates in auditing and 163 of these provided statutory audit services. Of these, 77 operate on a full-time basis, while 86 provide audit services on a part-time basis. The number of full-time and part-time sole practitioners remained practically the same when compared to the previous year. There are 61 audit firms registered with the Accountancy Board.

Profile of audit firms and sole audit practitioners

	Total number of firms/ practitioners
PIE Audit firms	9
Non – PIE audit firms	52
Full – time sole practitioners	77
Part – time sole practitioners	86

All firms and sole practitioners carrying out statutory audits fall within the QA process are therefore subject to an independent monitoring to ensure that audit entity's compliance, not only with the International Standards of Auditing but also with the accounting and auditing regulatory framework. . The Quality Assurance Unit ('QAU') is committed to carry out inspection visits to audit firms and practices providing audit services on the basis as set out in Directive 4 to the APA i.e.

a) Auditors carrying out statutory audits of PIEs , at least once every 3 years; whilst;
b) All other statutory auditors are to be visited at least once every six years

Other than the established visit cycles noted above, the QAU also adopts a risk based approach in its selection the audit entities to visit. In this regard, it resorts to desk top monitoring of data emanating from annual returns submitted and inputted into the QAU's operating system.

In most cases, following reports submitted to it by the QAU, the QAOC meets to discuss and approve these reports. Following a monitoring visit, the QAOC may request audit firms or sole practitioners to address a number of issues that arise during the visit by requesting a number of undertakings to remedy any shortcomings noted during the visit. Depending on the gravity of findings, the audit firms or sole practitioners may be required by the QAOC to submit an external audit compliance review (including a review of audit engagement files), performed by an independent professional auditor. In certain circumstances the QAOC may impose a follow up visit by the QAU itself. In those instances where the findings are far reaching but the QAOC is of the opinion that the audit entity has the necessary resources and abilities to address all of the inspection findings raised the practice will be subjected to a hot file audit review restriction. This means that the audit practice will be unable to sign the audit report of pre-selected audited financial statements pertaining to the audit practice on which a hot file restriction has been imposed, before the audit file is externally reviewed by an independent warrant holder holding a practicing certificate and clearance given to the QAOC by the external independent reviewer.

Depending on the extent and nature of the findings raised by the QAU, the Committee may opt for a follow up visit by the QAU, within a relatively much short period (normally six months) to ensure the remediation of the findings raised.

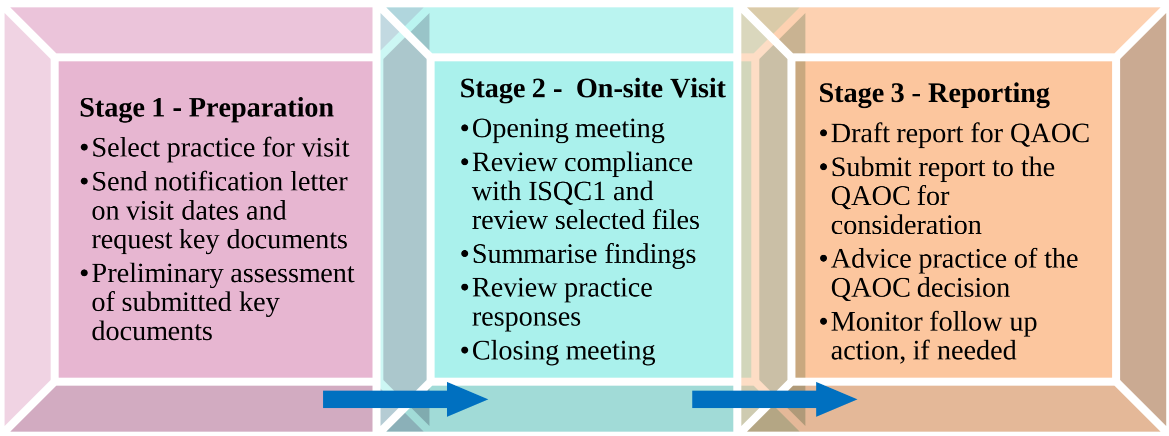
Other possible courses of action are available to the QAOC where it has serious concerns regarding the audit entity's ability to conduct a proper audit in line with International Standards of Auditing and /or fails to comply with the Accountancy Profession Act and its subsidiary legislation. These courses of action will include a recommendation to the Accountancy Board to:

(a) suspend the practitioner's practising certificate or
(b) withdraw the practitioner's practising certificate.

An important part of the risk based Quality Assurance Review process is the capturing of key audit quality indicators from returns submitted by audit practitioners in regard to their practices on an annual basis. Apart from visit cycle criteria, set out in Directive 4 to the Accountancy Profession Act, the selection of practices to be visited is risk based and emanates from Desk Top Monitoring (DTM) process of annual returns submitted along with media reports or complaints on practitioners made to the Accountancy Board. The main scope of the DTM process is to allow the QAU to identify potential risks at an early stage.

The Inspection Methodology

The practice monitoring process can be divided into three stages:-



Resources

Fully resourced, the Quality Assurance team comprises a Head of QAU and the inspection team which consists of 5 people, 4 quality review inspectors and an administrative clerk. The QAU had a back office administrator until the end of September 2014. To date, this post remains vacant

The reviewers as well as the Head of Unit are all qualified and hold practicing certificates in auditing. The QAU reviewers are bound by confidentiality and independence declarations which are reviewed on a year on year basis.

SECTION 3- OVERVIEW OF QUALITY ASSURANCE INSPECTION VISITS

3.1| QUALITY ASSURANCE VISITS

To date the, the Quality Assurance Unit ('QAU') carried out a total of 283 visits as indicated below.

Number of Audit Entities and Sole Practitioners visited since 2007

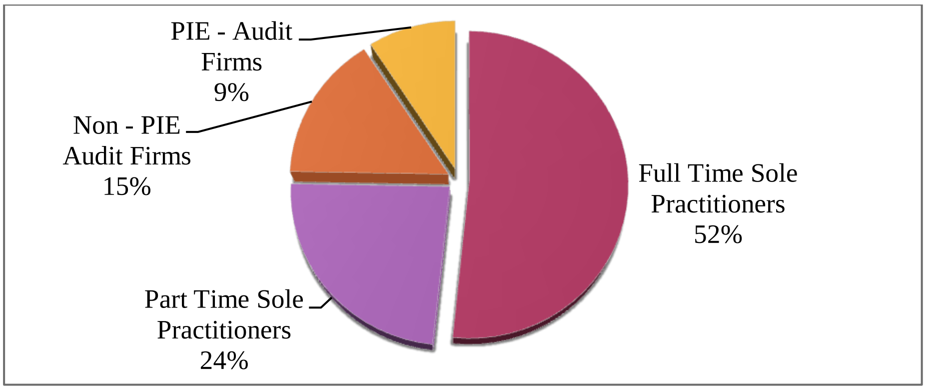
	Cycle 1	Cycle 2	Cycle 3 (PIE Auditors)	Total
PIE – Audit Firms	11	9	7	27
Non PIE – Audit Firms	27	22	-	49
Sole Practitioners	131	76	-	207
Total	169	107	7	283

Throughout 2014, the QAU carried out 39 visits. This represents a 100% increase when compared to the 19 visits carried out in 2013 (13 in 2012). The increase was attributed to the doubling of QA reviewers in 2014.

Once a quality assurance visit has been concluded and reviewed internally by the QAU, reports are passed to the Quality Assurance Oversight Committee ('QAOC') for their consideration. The number of visits closed down by the QAOC during 2014 amounted to 27 by the date of this report. Some other reports pertaining to visits carried out in 2013 were discussed and approved in 2014. The findings approved by the QAOC were reported in the contents included in this report.

During 2014 the QAOC met on four occasions. It reviewed and closed down 36 visits including those pertaining to 2013 bringing the total visits closed down by the QAOC since 2007 to 271.

Profile of practices visited by the QAU since 2007



3.2| OVERALL REVIEW OF THE 2014 VISITS

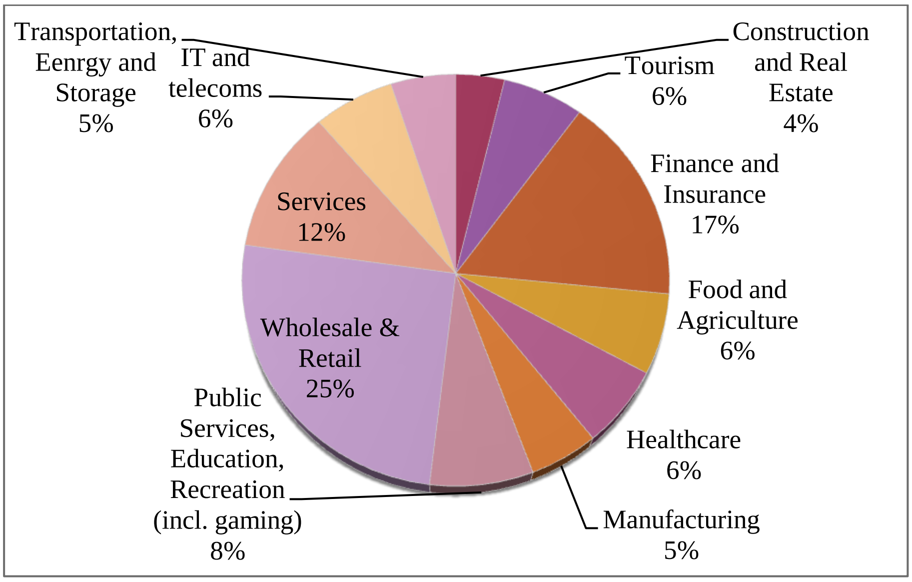
During 2014, based on the Quality Assurance Oversight Committee ('QAOC') reports issued, a total of 79 audit files were reviewed (of which 5 related to public interest entities).

The QAU adopts a risk based approach in the selection of audit files for review. Amongst other things, one looks at inherent industry risks related to the file reviewed, as well as other possible risks emanating from ethical and independence issues, audit report modifications, as well as the stature of the entity whose file is to be reviewed. These risk audits are identified from the client lists presented by the practice to the QAU on the first day of the visit. One also ensures that all audit engagement partners have at least one audit file reviewed during the inspection. Furthermore, throughout the year the QAU based its review on files which exceed the small company audit exemption thresholds as laid down in article 185 (1) (b) of the Companies Act.

Audit files of Government owned entities and those of public corporations which fall within the remit of the National Audit Office are not selected for review by the QAU during their monitoring visits at audit practices.

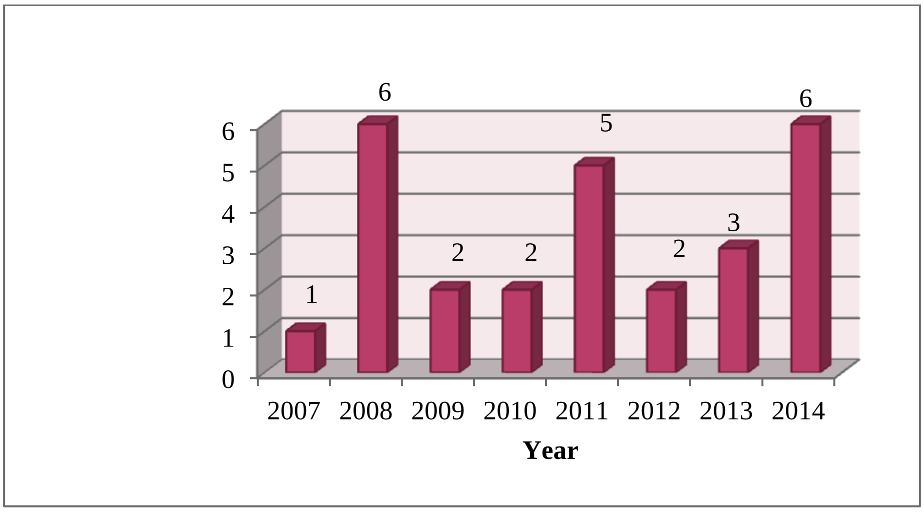
The analysis of audit files selected by industry during the inspection visits reviewed by the QAOC during the four QAOC meetings performed in 2014 is shown below:

Audit Files analysed by Industry sector reviewed by the QAU in 2014



During 2014, there were 9 audit firms auditing financial statements of public interest entities. Only the findings of four audit firms auditing public interest entities are being highlighted in this report since two of the big four firms visited in 2014 were not yet approved at the time of preparation of this report.

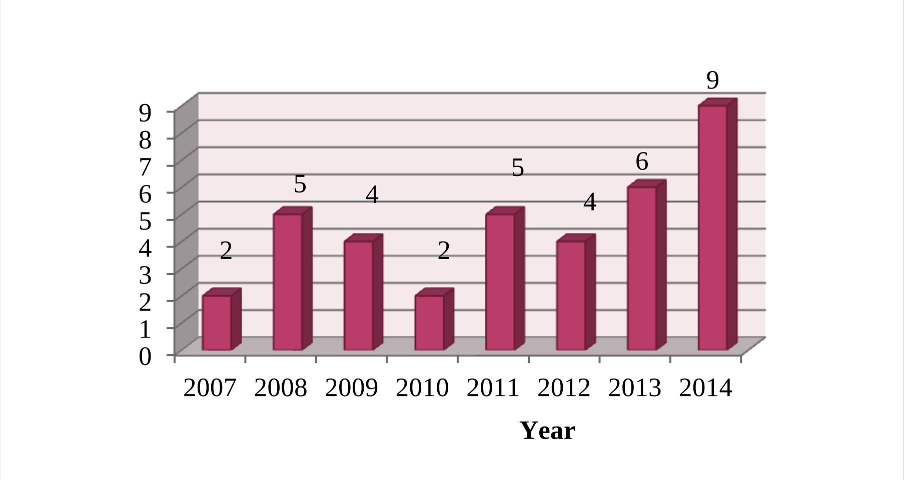
QAU Visits to PIE Auditors



Twelve inspection reports of visits (including 2 PIE auditors – both big 4 firms) carried out by the QAU in Quarter 4 were not yet approved by the QAOC, at the time of presentation of this report. During 2014, the QAU reviewed 9 audit engagement files of public interest entities as can be seen below. Audit files pertaining to public authorities or corporations which fall within the remit of the National Audit Office are not selected for review by the QAU when visiting practices which may be auditing such entities.

Since 2007 the QAU has reviewed a total of 37 statutory audits of public interest entities. These account for 7% of the total number of files reviewed to date. In 2014, the QAU visited 6 audit firms carrying out statutory audits of PIEs. Since 2007, 27 visits to PIE auditors having being carried out. Visit to PIE auditors account for 10% of all QAU visits carried out since 2007.

Audit files of PIEs Reviewed by the QAU since inception



3.3| OVERVIEW OF THE 2014 INSPECTION REPORTS

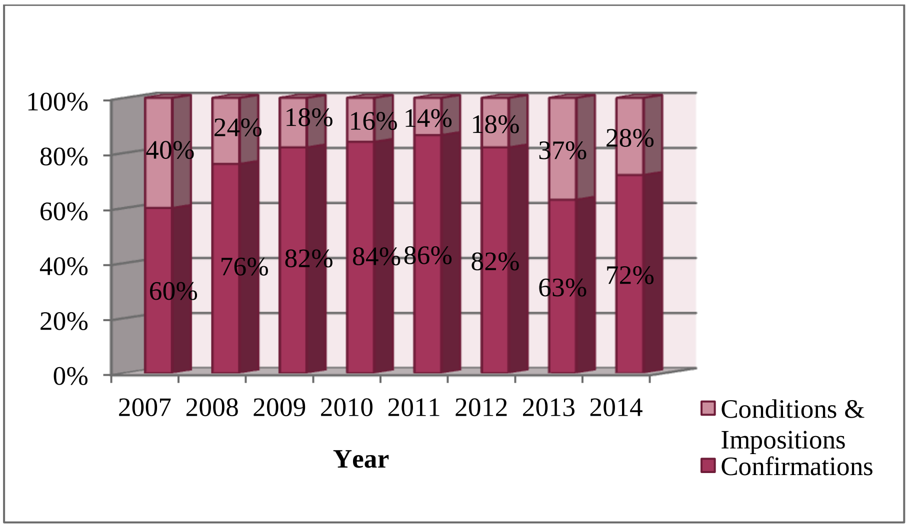
As in previous years, reports are assessed on the basis of the incidence, magnitude and gravity of visits findings, as well as the level of commitment and ability of the firm and sole practitioner to address the problems identified during a QA visit. In its closing down letter to the practitioners, the QAOC communicates the sanctions, impositions or any other corrective action, if any, which the QAOC deems appropriate.

The QAU is presently in its second cycle for non PIE auditors, and well into the third cycle of visits to firms carrying out PIE audits. Based on the visits carried out in 2014, we have noted a significant number of repeat breaches. This lack of rigour and commitment by certain practitioners to address the findings identified during the QAU visit is of concern to the QAOC. This explains the increasing number of sanctions being imposed by the Committee. In fact, since the second cycle of visits, conditions and impositions on audit practitioners increased from an average of 22% between 2007 and 2012, to 37% in 2013 and 28% in 2014.

The timely and effective remediation by audit practitioners of findings noted in QAOC visit reports and closing down letters is of critical importance to the whole of the QA process, and the QAOC will spare no effort to ensure that Audit Quality is improved.

An analysis of the courses of action taken by the QAOC since 2007 is illustrated in the diagram below:-

Analysis of Course of Action Taken

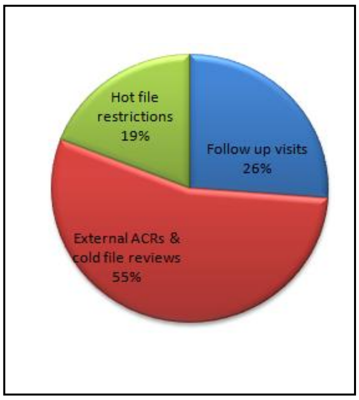


Based on the QAOC reports issued during 2014, the sanctions imposed on poorly performing audit practices consisted of external audit compliance reviews including cold file reviews, or follow up visits by the QAU. In fact 50% of the sanctions imposed during 2014 referred to a follow up visit by the QAU and 50% to an external ACR (including cold file review).

The number of conditions and impositions imposed since 2007 amounted to 42 and these can be analysed as follows:

Analysis of Sanctions Issued by the QAOC since 2007

	Follow up visits	External ACRs & cold file reviews	Hot file restrictions
PIE – Audit Firms	2	0	1
Non PIE –Audit Firms	3	7	0
Full-time Sole Practitioners	4	11	4
Part-time Sole Practitioners	2	5	3
Total	**11**	**23**	**8**



On average, 15% of the inspection visits carried out to date were subjected to one form of sanction or other. Of this, 3% related to auditors of PIEs which is equivalent to 10 % of the total PIE inspection visits carried out to date.

3.4| KEY OBSERVATIONS OF THE 2014 INSPECTION FINDINGS

It was noted that in the majority of cases, smaller audit practitioners and firms make use of the ACCA audit programme. It has been noted however that certain applicable sections of this audit programme were not being completed. As a result, pertinent ISA requirements were not being addressed on a number of the audit engagements files reviewed – particularly at the planning and completion stage of the audit.

Findings identified during the 2014 predominantly fell into three broad categories – Audit Engagement File Findings, Auditor Reporting issues and Whole Practice Matters. Those findings pertaining to non PIE audit practices have been reported separately from findings we have come across on visits to entities auditing PIEs.

3.4.1 – AUDIT FILE FINDINGS NOTED ON THE VISITS TO "NON PIE" AUDIT PRACTICES

ISA 230 – AUDIT DOCUMENTATION, ISA 500 – AUDIT EVIDENCE & ISA 501 – AUDIT EVIDENCE – SPECIFIC CONSIDERATIONS FOR SELECTED ITEMS

Documentation and evidence issues continue to be raised on a number of QA visits. The golden rule to audit documentation is that documentation must be sufficient to enable an experienced (third) auditor to understand the audit procedures performed, the audit evidence obtained and any significant judgment applied.

During our 2014 visits the more common documentation issues noted were in the following particular areas:

Inventories – Issues invariably arise mostly in relation to existence as well as valuation. Audit work carried out on inventories was particularly lacking on the verification of existence with a few instances where audit practices were simply accepting valuations (with no supporting documentation) given to them by management without carrying out any audit work on these management representations. There were also a number of instances where the year end stock count was not attended by the auditor, and this was neither because there was a limitation of scope imposed by management, nor because it was impractical to carry out the physical count. It was noted that the auditor, in these circumstances chose not to carry out alternative audit procedures, even where a perpetual stock taking system was in place. In most of these instances the auditor chose to modify the audit opinion on the basis of his inability to attend the stocktaking. Impairment of inventory items was also another major area of concern.

Accounts receivable and payable – Very little documentation was available on a number of audit files we reviewed in regard to debtor and creditor balances particularly in relation to possible impairment of debtor balances. Many practitioners tend to rely solely on audit tests they carry out in regard to payments and receivables after year end. Cut off tests and independent confirmation of debtor balances or reconciliations to suppliers' statements were few and far between;

<u>Bank confirmation letters</u> – Audit testing performed on bank balances is usually limited with verification of year end bank balances to the bank statements. In a number of instances independent direct bank confirmation letters were not requested by the audit practice. Direct bank confirmation letters not only confirm the existence of the balance at year end but also bring to light any potential contingent liabilities, the banking facilities made available to the company including their respective terms and conditions, as indeed other relevant information relevant to the audit which is not available on statements of account sent by banks. ;

<u>Completeness of income and cost of sales</u> – Audit testing of these two areas continues to be weak. In a number of instances, audit practices simply resort to reconciliation of nominal ledger figures to VAT returns when it comes to validating sales and cost of sales and nothing more. This gives very little audit comfort. Cut off test on both purchases and sales to ensure that both revenue and expenditure streams are taken in the appropriate accounting period at the year end were particularly lacking. Analytics, per se, do not uncover situations where the entity being audited has knowingly or otherwise anticipated revenues or deferred expenditure or vice versa. ;

<u>Professional skepticism – Impairment, fair values</u>. In a number of instances we noted that reliance is being placed solely on representations made by management or experts appointed by management. Very often audit files are laden with endless documents, with very little documentation as to what work was carried out by the auditor to assess the competence, integrity and independence of experts in order to dispel any management bias on such accounting estimates. Moreover, very often, there is very little evidence on file as to whether these valuations were challenged on the propriety of the assumptions applied in the financial models used for this purpose.

ISA 240 – THE AUDITOR'S RESPONSIBILITY RELATING TO FRAUD IN AN AUDIT OF FINANCIAL STATEMENTS, ISA 250 – CONSIDERATION OF LAWS & REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS, ISA 560 – SUBSEQUENT EVENTS

The assessment of fraud, laws and regulations and events after year end considerations continue to be a weak area both at the planning stage and completion stage of the audit for a number of the smaller audit practices. Although in many practices, audit programmes addressing these topics were found on audit files, in some instances these sections of the audit programme were either discarded or not adequately completed.

ISA 260 – COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

During the course of the QAU's visits, it was noted that in a number of instances a management letter was not issued. Furthermore although the auditor would indicate that the audit issues had been discussed, no minutes were kept on file evidencing this discussion and the responses received. A number of situations were noted when the auditor included an audit report modification, and yet no documentation was found on file of the auditor's communication of this matter with those charged with governance.

ISA 315 – IDENTIFYING AND ASSESSING THE RISKS OF MATERIAL MISSTATEMENT THROUGH UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

It was also noted that on a number of files reviewed, the key elements to the proper understanding of the entity and the environment, within which the entity being audited operates, are being overlooked. These procedures as set out under this ISA are intended to enable one to assess the risks of material misstatement of the financial statements, the sources of information from which the understanding was obtained and the risk assessment procedures identified. In some instances even where significant risks were identified, procedures to be applied at the fieldwork stage of the audit to mitigate the risks were not always identified.

Moreover, for those practices which involved a number of people on the engagement team, the engagement partner failed to document his discussion with the engagement team regarding the susceptibility of the entity's financial statements to material misstatement due to error or fraud, and the significant decisions reached.

ISA 320 – MATERIALITY IN PLANNING AND PERFORMING AN AUDIT

The calculation of materiality and especially performance materiality is an area which requires improvement. The documentation on audit files is lacking in respect of any thresholds applied or the basis for determining the appropriate benchmark for audit materiality computation at the planning stage of the audit engagement.

It was noted that on a number of audit files reviewed, performance materiality was not calculated. Revisions to such materiality calculations should be made if during the audit the auditor comes across information which could impact on such calculations. Moreover, in a number of instances, materiality thresholds were not re-considered after passing audit adjustments. Conclusions did not identify whether further audit work needed to be carried out.

ISA 520 – ANALYTICAL PROCEDURES

In some instances, preliminary analytical procedures were not carried out during the planning stage of the audit. There were other instances where preliminary analytical reviews were carried out but explanations of material fluctuations to identify potential risk areas which would require further consideration at the fieldwork stage of the audit were not always documented.

ISA 550 – RELATED PARTIES

Documentation on the work carried out to identify related parties at planning stage and any related party transactions, and the completeness and accuracy of these transactions was particularly lacking on many of the audit files reviewed. In addition, documentation of related party testing and evidence of audit work carried out needed improvement.

ISA 570 – GOING CONCERN

This is one of the more commonly breached ISAs noted during the course of the QA visits. The documentation of ISA considerations both at the planning and completion stage of the audit continues to be weak.

During the planning stage, as part of the auditor's understanding of the entity, the auditor should consider if the going concern assumption is appropriate or whether there are events or conditions and related business risks which may cast significant doubt on the entity's ability to continue as a going concern. As in prior years, although some practitioners have invariably stated that the material uncertainty considerations had been addressed at planning, fieldwork and reporting stage, this was either inappropriately documented or not documented at all.

Although management is responsible to assess its ability to continue as a going concern, it is the auditor's responsibility to obtain sufficient appropriate audit evidence about the appropriateness of management's assertion of the going concern assumption and to conclude whether there existed a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern at the time of signing of the audit report. The emphasis here is on the words "material" and "significant". When either or both do not prevail, the auditor should issue a clean auditor's report.

ISA 570 is very prescriptive in the audit procedures which are required to be performed by the auditor in respect of going concern. These may be summarized under two broad main headings:

• An evaluation of the means by which management has assessed the appropriateness of the going concern basis, including the performance of additional procedures when events or conditions are identified which may cast significant doubt on the entity's ability to continue as a going concern.

• An assessment of whether the financial statements contain adequate disclosures relating to going concern.

In order to assess whether adequate disclosure was made ISA 570 requires the auditor to determine whether the financial statements include the following required disclosures:

(i) a description of the principal events or conditions that give rise to the significant doubt on the entity's ability to continue in operation and management's plans to deal with these events or conditions; and

(ii) state clearly that there is a material uncertainty related to events or conditions which may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

From our review of the notes to the financial statements, a number of the above disclosures were not made. In this regard, the auditor failed to modify the auditor's report for inadequate disclosure made in the financial statements.

Although the QA reviewers are conscious of the fact that this is an area of professional judgment and that the auditor would have an in-depth understanding of their audit client, the audit files in a number of instances did not contain sufficient documentation to support the audit opinion given. Moreover it is important to re-iterate that even when it comes to professional judgment, auditors are still required to document the basis on which they have arrived to the professional judgment reached on Going Concern.

ISA 580 – WRITTEN REPRESENTATIONS

Although in most instances it was noted that a signed representation letter was obtained, from review of the letter of representation it was noted that a number of representations as set out in ISA 580 were not incorporated in the letter.

3.4.2 – WHOLE PRACTICE MATTERS NOTED DURING VISITS OF "NON PIE" AUDIT PRACTICES

ISQC 1 - QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF FINANCIAL STATEMENTS, AND OTHER ASSURANCE AND RELATED SERVICES ENGAGEMENTS

A significant number of practitioners and firms had documented policies and procedures in accordance with the requirements found in ISQC 1. On an overall basis, documentation of ISQC 1 requirements is satisfactory. However, instances were noted where number of practitioners failed to put into practice what they themselves set out in their own manuals. As in the past, the main weaknesses noted by the QAU reviewers in regard to the implementation of this document were in two main areas:

- the setting of criteria for engagement quality control reviews 'EQCR'. EQCRs is an area which is generally not looked with rigour and commitment; and
- the carrying out of cold file reviews. It was noted that a significant number of practitioners had carried out cold file reviews on audit engagements on which they had acted as an audit engagement partner. The guidance note on compliance reviews under 'clarified' ISQC 1 issued by the Quality Assurance Oversight Committee requires sole practitioners to conduct cold file reviews either by an externally suitable independent qualified person or internally by qualified staff not involved in audit or EQCR.

Article 153 of the Companies Act requires that: 'an auditor must at all times adhere to the rules of independence and professional ethics set out in the Code of Ethics and any other regulations, directives or guidelines issued from time to time in terms of the Accountancy Profession Act.' However, as in past years, the QAU encountered a number of instances where breaches of the Code of Ethics were noted, particularly in the area of auditor's independence. The more common breaches noted related to the provision of non-assurance services and long association with clients. Typical familiarity threats uncovered by the QAU included instances when immediate family members or siblings of an engagement partner were appointed directors in businesses of audit clients of the practices visited. Potential independence threats arising from a close business relationships, which an audit entity may have with its audit clients is one other area which is often overlooked at the acceptance and continuance stage of an audit engagement.

Maintaining competence is one other area considered by ISQC 1. It is indeed sad to note that a number of audit practitioners did not comply with the minimum required CPE hours as set out in Directive 1 of the Accountancy Profession Act. Moreover, many of those who have complied with Directive 1 have chosen to attend CPE events which do not focus on statutory audit related matter.

3.4.3 – AUDIT REPORT ISSUES NOTED ON OUR VISITS TO NON PIE AUDIT ENTITIES PRACTICES

ISA 700 – FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS.

The form and content of a number of audit reports reviewed by the QAU during the year did not conform to ISA 700 requirements. The main breaches noted in this area resulted from out of date wording being used and the exclusion of appropriate headings and paragraphs in the audit report itself. More care is required in this regard and practitioners are reminded that ISA 700 includes illustrative audit reports for their guidance.

ISA 570 – GOING CONCERN

Upon concluding whether the auditor concurs with the view of management of their assessment of the appropriateness of the going concern and on the adequacy of disclosures made, the auditor is required to determine the implications, if any, on the auditor’s report. In many instances it was noted that an emphasis of matter paragraph was included in the audit report, but adequate disclosures, as required by ISA 570 were neither included in the financial statements nor was an emphasis of matter paragraph included in the auditors' report itself. As explained in the audit file findings ISA 570 is very explicit as to what information needs to be disclosed in the financial statements. If the appropriate disclosures are not made the audit report needs to be modified on this basis.

ISA 705 – MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR’S REPORT

Small practitioners are still struggling with the ISA 705 qualification – particularly in relation to qualifications relating to limitation of scope, and its materiality and pervasiveness to the financial statements. The impact of year on year qualifications of this kind on the auditor’s ability to continue the engagement is an area which smaller practices do not quite grasp. The auditor’s inability to attend the year end stock take is one qualification which features frequently under this heading, more often than not, the auditor choosing to resort to modifying the audit opinion, even when no alternative audit procedures are applied. In a number of instances it is abundantly clear that alternative audit procedures could have been carried out. The inability to attend the year end stock take more often than not results when the auditor is appointed after the year end, The auditor is expected to attend year end counts, and can only do away with this procedure if it is impractical to attend, The word "impractical" is being used rather loosely within the profession.

On number of occasions, those practitioners who did not have the option to switch to GAPSE and reported under the IFRS regime, the identity of the ultimate controlling party was not disclosed in the auditor's report as required by IAS 24 & ISA 705. Moreover, in a number of instances, audit practices did not modify their audit reports on this basis, as required by ISA 705.

Attention is drawn to Guidance notes issued by the Malta Institute of Accountants on the 20 September 2012 which state "*ISA 705.19(a) requires the auditor to discuss the non-disclosure with those charged with governance. Should the appropriate disclosures not be made in the audited entity's IFRS financial statements, the auditor would need to issue a modified report in accordance with ISA 705, and as required by ISA 705.19(c), the report would have to include, amongst others, the omitted disclosure of the identity of the ultimate controlling party.*"

3.4.4 – FILE FINDINGS NOTED ON THE VISITS OF AUDIT FIRMS CARRYING OUT PIE AUDITS

THE CAPITAL MARKET AND OTHER REGULATED ENTITIES

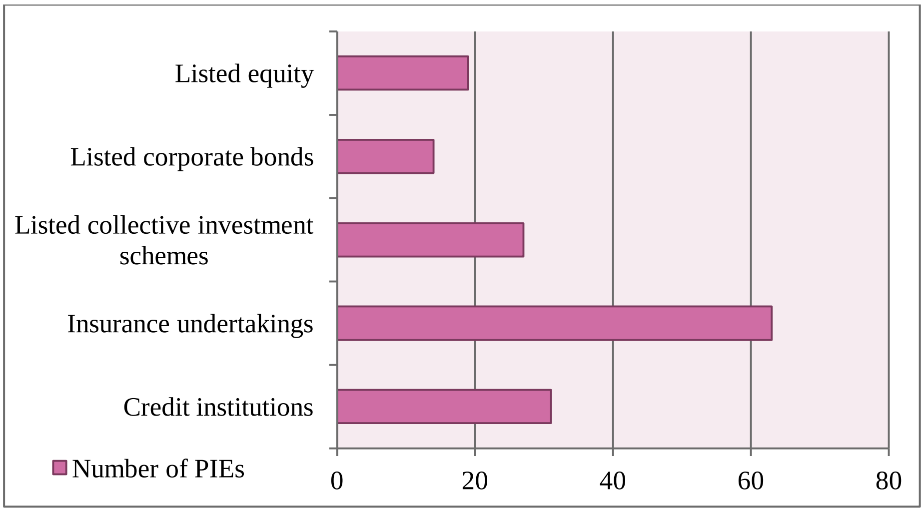
Apart from Government Bonds and Treasury Bills, there are 145 recognised listings on the Malta Stock Exchange with a total market capitalisation of circa € 4.3 Billion spread over some165,000 private and corporate investors. The listed corporate Bonds market is dominated by private investors (83%), whilst circa 65% of the listed Equity market is owned by financial institutions and other incorporated entities. HSBC and BOV jointly account for circa € 1.5 Billion (i.e. 35%) of the total listed market capitalisation.

Public interest entities are entities whose transferable securities are admitted to trading on a regulated market within the meaning of point 14 of article 4 (1) of Directive 2004/39/EC, a credit institution as defined in point1 of Article 1 of Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions (1) and insurance undertakings within the meaning of Article 2 (1) of Directive 91/674/EEC and such other entities as may be prescribed by the Board.

For this reason, therefore, other than those entities listed on the Malta Stock Exchange, regulated entities such as banks and insurance undertakings are deemed to be Public Interest Entities as indeed collective investment schemes.

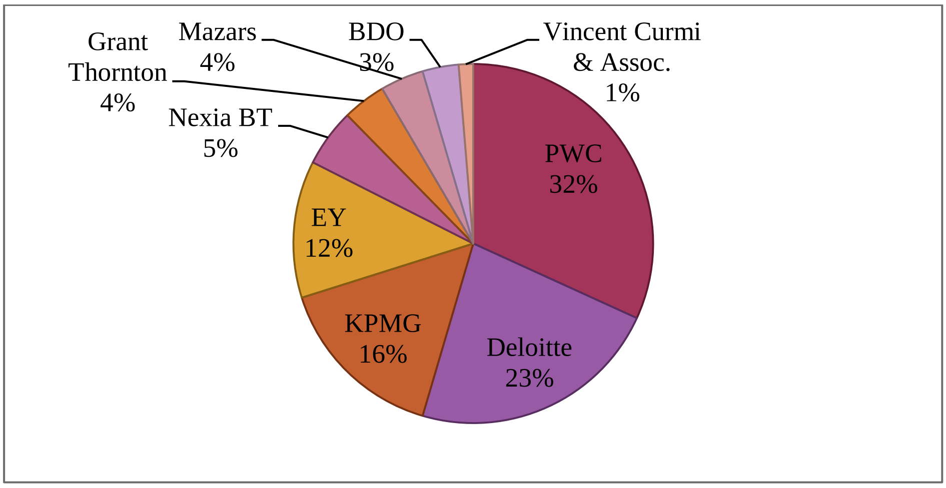
An illustrative segmentation of all types of entities which are deemed to be of a public interest is noted below.

Segmentation of Public Interest Entities



83% of the audits of all PIEs are conducted by the Big 4, international network firms. The audits of the remaining 17 % are carried out by other mid tier firms, all of which, other than one, form part of an international network.

Share of market of PIE Audits.



The inspection findings emanating from the QAU's visit to 6 audit entities carrying out PIE audits in 2014 are noted below. These include findings pertaining to both PIE and non PIE entities

ISQC 1 - QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF FINANCIAL STATEMENTS, AND OTHER ASSURANCE AND RELATED SERVICES ENGAGEMENTS

There were three instances where the archiving date exceeded the permitted 60 day period after the date of the auditor's report for the timely assembly of the engagement file.

One of the safeguards in place according to the firm ISQC 1 manual of a PIE audit firm when there is long association with client is an annual evaluation of the independence threat, which should be documented on file. In the independence questionnaire on file the consideration questioning whether the client was a client of the firm for more than ten years was inadvertently marked as ‘no’. As a result, the evaluation of the independence threat was not carried out. Consequently, no documentation of the safeguards adopted to mitigate the familiarity threat was found on the file reviewed.

During the visit of a particular PIE audit firm it was noted that the criteria for carrying out Engagement Quality Control Reviews had not been included in the ISQC1 policies and procedures. Furthermore, Annual Compliance Reviews including cold file reviews were not being carried out on an annual basis. The same firm did not have formal partner appraisals in place nor were staff appraisals formally documented.

In another PIE audit firm the firm’s ISQC1 manual included policies and procedures to address the provision of non – audit services to audit clients. On two of the files reviewed the audit firm of a PIE provided assistance in the preparation of the financial statements to non PIE companies. However it did not document the related independence considerations and the safeguards adopted to mitigate the independence risk

ISA 210 - AGREEING THE TERMS OF AUDIT ENGAGEMENTS

On the audit files of a PIE of a particular audit firm, the engagement letters did not identify the reporting framework (IFRS). On one other particular audit file, the engagement letter was dated after the audit work had been completed.

ISA 220 – QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS

The audit engagement partner’s review of the PIE audit files we selected was by way of electronic sign-off. On one of the PIE audit firms visited, a number of audit planning and completion procedures were signed off by the engagement partner two days before the commencement of the QAU visit. On another file the client acceptance form was signed off fifteen days after the firm signed the audit engagement letter. On another file the engagement partner’s file review was signed off after the audit report date.

ISA 230 – AUDIT DOCUMENTATION

A number of other documentation issues were noted at the audit fieldwork stage. The findings noted on the files reviewed were as follows:

- On a number of files reviewed during our visits of PIE audit firms the engagement team’s consideration and compliance with laws and regulations were not always adequately documented.

- The documentation to support the professional judgment reached in regard to the existence of material uncertainty was lacking on audit files reviewed across a number of PIE auditors.
- On one of the PIE audit files reviewed, group intangible assets were tested for impairment but documentation of audit work carried out required improvement.
- No documentation was found of the audit engagement’s team consideration of audited entity’s breach of a franchise agreement, nor were the consequences of such a breach assessed or evaluated.
- Material fluctuations identified from an analytical review carried out in respect of revenue and prepayments were not adequately explained.
- There was no adequate documentation as to whether the custodian and the broker of the entity being audited were of a good standing and of a solid financial strength. On the same file there was no documentation that the company met the qualifying criteria for investment tax credits.
- On a non PIE audit file there was no documentation of the sampling methodology used to identify the number of units to be tested during the inventory count.
- On a file of a gaming company the documentation of risks associated with revenue recognition, fraud, related parties, going concern, and company internal control system were not adequate.
- On another non-PIE audit file, an audit firm chose to qualify the audit opinion on the basis that it was unable to satisfy itself as to the inventory quantities at balance sheet date as it was appointed after year end. There was no documentation as to why no alternative procedures could be adopted by the audit firm to verify existence and reasonableness at which inventory was stated at year end. Moreover, there was no evidence on file in regard to the audit work carried out to test the possible impairment of inventory at year end.
- On another two non-PIE audit files, there was no evidence on file of the audit procedures adopted by the firms concerned to dispel any management bias on the fair value of investment property. On another audit engagement file an architect’s valuation was obtained subsequent to the audit report date.

ISA 260 - COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

On a particular file, a management letter was not prepared even though the audit report was qualified.

ISA 320 - MATERIALITY IN PLANNING AND PERFORMING AN AUDIT

On the audit file of a particular PIE there was no documentation as to how performance materiality was calculated.

ISA 520 – ANALYTICAL PROCEDURES

On two audit engagement files of non PIEs the firms' preliminary analytical procedures were not performed at the planning stage of the audit. On another separate audit file the analytical review procedures at the completion stage of the audit engagement were not carried out.

ISA 580 - WRITTEN REPRESENTATIONS

On two occasions both relating to non PIE audit engagements, the letter of representation did not include representations that management had fulfilled (rather than acknowledged) its responsibility for the preparation and fair presentation of financial statements. On one other file the firm did not include in its management representation letter any reference to the effects of uncorrected financial statements misstatements.

ISA 600 - SPECIAL CONSIDERATIONS—AUDITS OF GROUP FINANCIAL STATEMENTS (INCLUDING THE WORK OF COMPONENT AUDITORS)

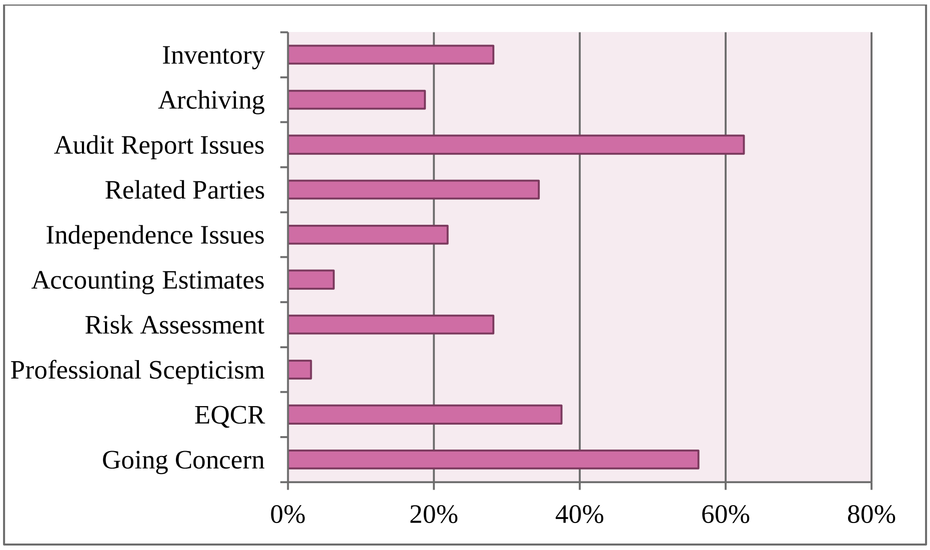
On a file of an unlisted major group of companies it was noted that the auditor was the component auditor of the parent company. A group audit engagement letter was not obtained from the parent company. Moreover, there was no engagement letter between other components of the group and no specific terms of reference in regard to the group audit were drawn up and formally agreed to. In particular the following specific ISA 600 requirements were not addressed.

- An overall audit strategy and audit plan;
- The identification of significant components;
- Understanding the component auditor (including consideration of the component auditors' independence and competence);
- Calculation of group materiality and component materiality;
- A group risk assessment and procedures to address those risks;
- An understanding of group-wide controls and the consolidation process and procedures on the consolidation process;
- Consideration of subsequent events of components; and
- Communication with component auditors'.

3.5| SYNOPSIS OF 2014 AUDIT FINDINGS

Due to the size, structure and the very nature of small, medium and micro entities our visit findings on these type of entities tend to be more basic and fundamental than those findings normally found in the audits of the larger entities, some of which may or may not be PIEs.

A summary of the main findings emanating from all files reviewed by the QAU during 2014 are presented below:



SECTION 4 - ROOT CAUSE ANALYSIS OF POOR AUDIT QUALITY PERTAINING TO SMALL AND MEDIUM SIZED PRACTICES

In the QAU's opinion, some of the root causes of the difficulties being encountered by a number of SMPs stem from the combination of one or more of the following:

a) The use of non ISA compliant audit programmes or excessive tailoring of ISA compliant programmes. In the latter case, it was noted that certain applicable sections of this audit programme were not being completed and as a result of which, certain pertinent ISA requirements were not being addressed on a number of the audit engagement files reviewed by the QAU.

b) The difficulty to attract and retain experienced audit staff – thereby impacting on the quantity and quality of resources spent on audits. This coupled with inadequate levels of supervision and review by senior members of the engagement team impact negatively on the quality of audit work. The lack of adequate inadequate supervision often results in directing one's resources to less significant parts of the audit rather than focusing on the more critical risks areas of the entity being audited. This shortage of experienced audit personnel poses a number of challenges to all audit practices – large and small.

c) The CPE culture is one which needs to be bolstered. Many practitioners find it difficult to attend CPE events. Moreover, it was noted that many audit practitioners prefer to attend non audit related CPE events While one recognizes the shortage of "audit" focused CPE events being held locally, globalisation has rendered the task of keep oneself technically up to date much more manageable, and professional websites do provide continuous professional development programmes and webinars;

d) Coping with multi-disciplinary services is no enviable task to a number of sole practitioners, particularly those operating on a part time basis. These bring with them endless deadlines, thereby alienating their attention from more pressing audit needs. Insufficient resources allocated to audit engagements, due to staff shortage or turnover, give rise to audit procedures being compromised to meet deadline pressures and this, at the expense of audit quality;

   The inability to balance the cost of increased regulation and pressures to lower audit fees, can often result in poor audit quality.

e) Failure to apply appropriate levels of professional skepticism, at the various stages of the audit.

SECTION 5- SUMMARY OF ACTIVITIES CARRIED OUT BY THE QUALITY ASSURANCE UNIT DURING 2014

5.1| TEAM MEETING

A local team meeting was held in June. This full-day meeting which is chaired by the Head of the QAU enables reviewers to discuss emerging issues arising from the more recent visits. In his presentations at this meeting, Mr Coppini not only dealt with new regulatory developments within the EU, but also discussed with the reviewers a number of the more common pitfalls noted during the QAU's own internal review process. This is to ensure that the whole of QA process is consistently applied by all QA reviewers across all audit practices visited.

5.2| REVIEW OF TRANSPARENCY REPORTS PUBLISHED BY AUDITORS OF PUBLIC INTEREST ENTITIES

The deadline of the publication of transparency reports by auditors of public interest entities which was due by 31 March 2014 was met by the majority of auditors of public interest entities. However one firm had not published their transparency report by the required date. By the end of April 2014, all transparency reports were in place.

5.3| MAINTAINING A CLOSE WORKING RELATIONSHIP WITH THE MALTA INSTITUTE OF ACCOUNTANTS

Over the years, the Malta Institute of Accountants ('MIA') and the QAU have fostered a close working relationship. The QAU in collaboration with the MIA held a session in February on SME Audits - QAU Findings, the SMP Perspective and a Simplified Audit Approach. During this session, MIA President, Ms Maria Micallef engaged with QAU Head, Mr Marcel Coppini in a question and answer exchange that sought to uncover the more common SME audit pitfalls.

On May 2014 Mr Coppini was also instrumental in bringing over the Association of Chartered Certified Accountants (ACCA) to Malta to participate in a joint event with the MIA. After a presentation by the ACCA's Head of Technical, Mr John Davies, who was then responsible for ACCA's work on technical policy matters affecting the accountancy profession, the event discussed the European developments affecting accountants.

During the year the Head of the QAU contributed to the winter issue of the MIA journal - the Accountant. This article was entitled "SME Audits and difficulties faced by their SMP auditors" Furthermore, during 2014, the QAU provided the MIA with a number of weaknesses identified during QAU visits.

The QAU was also represented on a number of MIA committees dealing with areas such as Continued Professional Education, Ethics, Accounting and Auditing.

5.4| FOSTERING A CLOSE WORKING RELATIONSHIP WITH THE UNIVERSITY OF MALTA

During September and October 2014, the Head of the Quality Assurance Unit lectured on Quality Assurance and Public Oversight, at a course held by the Accountancy Board in collaboration with the University of Malta. The course was mainly intended for persons with audit experience, to obtain recognition to practice on a freelance basis as officially approved Accountancy Board external reviewers, to be appointed by audit practitioners, when sanctions are imposed on them by the QAOC.

5.5| ATTENDANCE AND PARTICIPATION AT EUROPEAN AUDIT INSPECTION GROUP ('EAIG') AND INTERNATIONAL FORUM OF INDEPENDENT AUDIT REGULATORS ('IFIAR')

Our representation and active participation in the European Audit Inspection Group ('EAIG') has helped us to keep abreast of audit developments within the European Union. These meetings at European level ensure smooth and efficient co-operation amongst public oversight bodies within Member States. The Group meets on a quarterly basis. EAIG's milestone in November of this year was the launching of the first phase of Common Audit Inspection Methodology (CAIM) project. A suite of programmes addressing ISQC 1 requirements have been developed for implementation by all member states auditing PIEs in 2015.

The Head of the Quality Assurance Unit attended an inspection workshop held by IFIAR in London on the 3rd and 4th March 2015.

5.6| REVISION OF DIRECTIVE 1 CONTINUED PROFESSIONAL EDUCATION AND DIRECTIVE 2 CODE OF ETHICS FOR WARRANT HOLDERS

During December 2014, amendments to the Continuing Professional Education Scheme, which was the fruit of an MIA subcommittee set up for this purpose was approved by the Accountancy Board in terms of Sub-Rules (3) and (4) of Rule 4 of Directive Number 1, issued under the Accountancy Profession Act (Chapter 281 of the Laws of Malta). The new scheme became effective from 1 January 2015.

The Accountancy Board considered and approved the long awaited changes to Directive 2 to the APA – The Code of Ethics. The Code obtained ministerial approval and was published on the 13 March 2015 and became effective as from the same date.

5.7| CARRYING OUT OF A NUMBER OF INITIATIVES WITH THE MFSA

These initiatives will focus on ensuring that proper and complete declarations are made by the warrant holders when submitting their annual return. It is the QAU's intention to work more closely with the MFSA in regard to Audit Committees of PIEs, which committees, are presently supervised by the MFSA.

5.8| FEEDING LOCAL PIE INSPECTION FINDINGS TO A EUROPEAN DATABASE ON AUDIT INSPECTION FINDINGS

The European Audit Inspection Group ('EAIG') maintains a common database to collect and exchange findings of its member organizations from their local inspections of audit firms. The group maintains a database on inspection findings from its members to share knowledge and to identify any recurring issues from inspections that should be discussed with individual firms. The database contains inspection findings in relation to the ten of the largest European networks of audit firms. These findings are summarized and discussed with representatives of the large Global networks by members of the EAIG at the college of auditors. The database is confidential and restricted only to members of the EAIG. Malta participates in two of these colleges of Auditors, namely PwC and Deloitte.

5.9| DESK TOP MONITORING PORTAL PROJECT

This project has been in progress for a number of years, but one augurs that by mid 2015 the QAU would have fully developed the desk top monitoring system. This software enables QA reviewers to identify at an early stage of the QA process, which audit practices could be up for review. This is based on key Audit Quality Indicators generated by the system from information submitted by audit practitioner in their Annual Returns of the previous year.

5.10| CORPORATE SOCIAL RESPONSIBILITY EVENT

For the first time ever, the Quality Assurance Unit organized a corporate social responsibility event. The QAU paid a visit to the elderly people at St Vincent De Paul Residence, Luqa over the Christmas period. Those residents visited at this home were also given a small gift during the event.

SECTION 6 - OUTLOOK FOR 2015

Undoubtedly the Audit Reforms which are presently in the process of being transposed into our legislation will impact on the whole of the QA process. Moreover, the new regulations pertaining to PIEs will also require closer scrutiny on auditor rotation, and non assurance services being provided by the auditor to the PIE. The Audit reforms also require a closer check on the function and governance of Audit Committees of PIEs and their interaction with the external auditor.

The transposition of the Single Accounting Directive will also bring changes, albeit small, to the QA methodologies and procedures.

The QAU, through the support of the QAOC and the Accountancy Board embraces the challenges ahead of it as a result of new audit and financial reporting regulation which need to be transposed into our legislation by the 16 June 2016. This it will achieve by:-

- Working closely with other stakeholders within the educational sphere to assist audit practitioners in their Continued Professional Education needs;
- Working closely with the MIA in the area of quality assurance not only to maintain but also improve audit quality standards;
- Continuing to work closely with its European counterparts entrusted with Public Oversight and Quality Assurance;
- Working more closely with other local financial services regulators, financial supervisors as well other stakeholders within the field of audit and financial reporting regulation;
- Advise and make recommendations to the Accountancy Board in regard to enforcement and compliance mechanisms;
- Create more public awareness of the Quality Assurance process;
- Advise the QAOC and the Accountancy Board on key issues in regard to audit regulation and other legislative changes; and
- Maintain and further develop the existing methodologies, the Accountancy Board portal, and other tools at its disposal.

ACRONYMS USED

AB - Accountancy Board

ACCA - Association of Chartered Certified Accountants (UK)

AuRC - Audit Regulatory Committee

BCBS - Basel Committee Banking Supervisors

CPE - Continued Professional Education

CAIM - Common Audit Inspection Methodology

EAIG - European Audit Inspections Group

ECG - European Contact Group

EEA – European Economic Area

EFAA – European Federation of Accountants and Auditors for SMEs

EGAOB - European Group of Audit Regulators

ESMA - European Securities and Markets Authority

FEE - Federation Experts Comptables Europeens

GAPSE - General Accounting Principles for Smaller Entities

IAASB - International Auditing and Accounting Standards Board

ICAEW - Institute of Chartered Accountants of England and Wales

IFAC – International Federation of Accountants

IFIAR - International Forum of Independent Audit Regulators

ISAs - International Standards on Auditing

ISQC 1 - International Standards on Quality Control

MIA - Malta Institute of Accountants

PIE - Public Interest Entity

QA - Quality Assurance

QAU - Quality Assurance Unit

QAOC - Quality Assurance Oversight Committee

SME /SMP - Small and Medium Entity / Small & Medium Practices

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Quality Assurance

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