

# Quality Control Reviews in Slovenia

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## How often the quality of the work of audit firms is inspected:

- audit firms which perform audits of public-interest entities are supervised at least every 3 years,
- all other audit firms are supervised at least every six years.

The Agency perform approximately 25 inspections of key audit partners per year.

Number of inspections of audit firms per year varies and depends on the size and complexity of the operations of the audit firms under inspection in a particular year.

Agency uses the Common Audit Inspection Methodology (CAIM) and the CEAOB Guidelines for the selection of audit files and review areas. ([CEAOB - Common Audit Inspection Methodology \(CAIM\) | European Commission \(europa.eu\)](#))

# PREPARATION FOR INSPECTION-PLANING STAGE

The selection of audit firms and the number of key audit partners (KAP) to be inspected in a certain year is based on our annual plan of inspections. When determine the plan of inspections we also take into consideration (beside the mandatory cycles) offices with poor inspection results in previous years and offices that were recently opened, to be inspected earlier, to include element of unpredictability.

## **SELECTION OF KEY AUDIT PARTNERS AND NUMBER OF FILES FOR INSPECTION**

Factors which we take into consideration are :

- number of auditor's report signed by each KAP,
- number of PIE's in portfolio of each KAP,
- nature of the clients or engagements in portfolio of each KAP,
- expertise of the KAP in different industries.

## Example of selection- BIG 6

KAP	number of signed reports in 20XX	% in total	number of PIE's	% in total	sample of engagements
KAP - A	1	0,4%	0	0,0%	0
KAP - B	43	18,9%	2	11,1%	2
KAP - C	78	34,2%	8	44,4%	2
KAP - D	67	29,4%	8	44,4%	2
KAP - E	20	8,8%	0	0,0%	0
KAP - F	11	4,8%	0	0,0%	0
KAP - F	8	3,5%	0	0,0%	0
<b>Total</b>	<b>228</b>	<b>100,0%</b>	<b>18</b>	<b>100,0%</b>	<b>6</b>

*Differences in the selection of KAP for large audit firms (BIG 6) and other audit firms*

When we perform inspection of one of the BIG 6 audit firm:

- all partners who signed the auditor's reports of public interest entities are always under review in each 3 year cycle,
- other partners are reviewed at least every six years (taking into account element of unpredictability).

## Example of selection- small audit firm

KAP	number of signed reports in 20XX	% in total	number of PIE's	% in total	sample of engagements
KAP - A	20	49%	2	100%	1
KAP - B	18	44%	0	0%	1
KAP - C	3	7%	0	0%	0
<b>Total</b>	<b>41</b>	<b>100,0%</b>	<b>2</b>	<b>100,0%</b>	<b>2</b>

*Differences in the selection of KAP for large audit firms (BIG 6) and other audit firms*

When we perform inspections of smaller audit practices we usually perform inspection of:

- all KAP,
- unless individual KAP signed only few auditor's reports.

## SELECTION OF AUDIT FILES

We prepare in-depth analysis of the portfolio of each key audit partner selected for inspection and document analysis and our decision (excel format).

### **Our approach for selecting audit files (using CAIM guidance):**

- risk-based selection approach for selecting audit files (it is biased towards a greater likelihood of encountering audit quality issues (for example higher-risk audit areas of more complex PIEs, areas with elevated risk profiles or areas where the audit firm or KAP may have less expertise).
- other selection criteria, audit engagements with a lower risk profile, maintain an element of unpredictability.

The sample is determined based on o **combination** of **risk-based characteristics** and **other selection criteria**.

## Selection criteria taken into consideration when selecting audit files for inspection:

### 1. Risk based characteristics:

- Nature of the client and/or engagement:
  - Large, multi-location or complex entities;
  - Engagements in specific industries/sectors with known risks, including risk of fraud (e.g. banks, insurance companies or other regulated industries);
  - Information resulting from 3rd party notifications (“Whistleblowing”), including notification from other regulators.
  - Initial Public Offerings;
  - Engagements perceived as highly exposed (high number of employees, political sensitivity, etc);
  - Communication and notes from the relevant Stock Exchange market;

# PREPARATION FOR INSPECTION-PLANING STAGE

- Topical financial news (profit warnings, going concern issue, corporate restructuring, tax issues, money laundering issues, management / key personnel change, governance issues, other significant transactions).
- Audit and auditor characteristics
  - Initial audit engagements, rotation of audit firm, audit engagement leader and audit engagement team;
  - KAP with no experience in the specific industries/sector (banks, insurance companies, etc);
  - Known and potential threats to auditor independence;
  - Number and nature of internal or external inspection findings in prior years.
- Review of the financial statements
  - Auditor's reports with modifications to the opinion and/or with emphasis of matter paragraph included (legal claims, illiquid assets, etc);



# PREPARATION FOR INSPECTION-PLANING STAGE

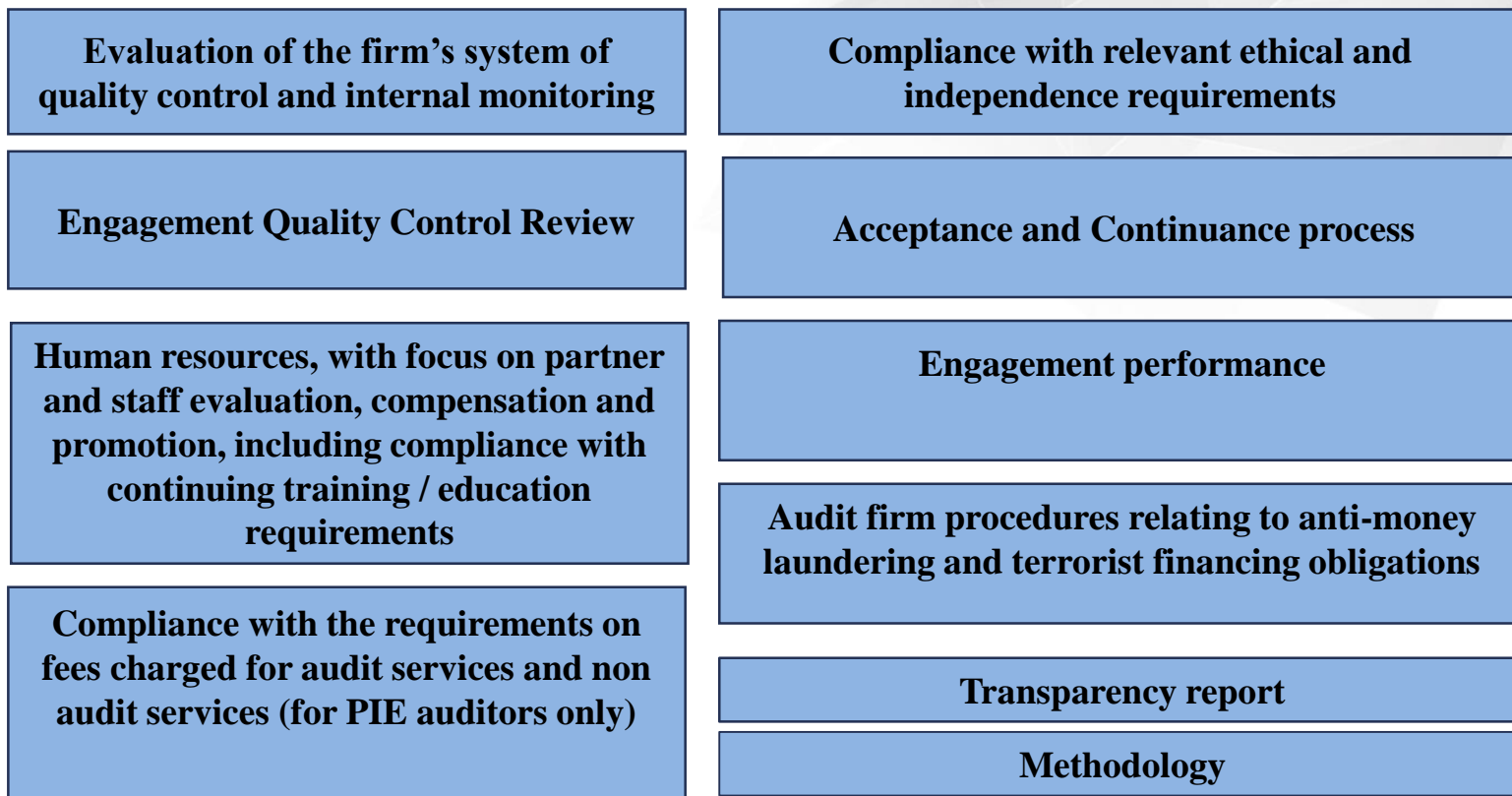
- Key audit matters included in the audit report;
- Key Client Data: revenue, material inventories, net assets or debt and other key client data (e.g. meeting one or several criteria such as Goodwill > 50% of revenues or losses 10% of revenues);
- Magnitude of assets and liabilities measured at fair value that involve high level of judgement or with high degree of estimation uncertainty (goodwill, financial assets and liabilities classified as level 3, provisions);
- Company prepare financial statements in accordance with IFRS (extended notes to FS vs. local SAS);
- Significant unusual or complex transactions described in the notes of the financial statements;
- Significant variations with corresponding comparative figures.

# PREPARATION FOR INSPECTION-PLANING STAGE

## 2. other characteristics:

- audit engagements with a lower risk profile, applying element of unpredictability, with no specific risks identified, middle sized companies, random selection of audit file

**Inspection of firm's system of quality control is focused mainly on the following areas:**



Programs used for documenting the inspection procedures performed in respect of review of internal quality control :

- For BIG 4 audit firms we use CAIM work programs for all focus areas ( procedures performed are documented in excel),
- For small audit firms we use simplified work program, which include all areas of quality control, as determined in ISQC 1.

## Selection of inspection areas for audit files:

**Identification and risk assessment  
(assessing the Risks of Material  
Misstatement)**

**materiality**

**The auditor's responses to  
assessed risks**

**Auditing of accounting estimates in  
connection with the using of the  
work of Auditor's Expert**

**appropriateness and sufficiency of audit  
documentation of the auditor's procedures  
performed, for certain account balances,  
selected implementing risk based approach  
and taking into account also the  
unpredictability element**

**Other areas selected based on risk  
approach – consolidation process, journal  
entries testing, related parties, post balance  
sheet events,**

**Auditor's review of adequacy of disclosures  
in annual report**

**Appropriateness of auditor's report and  
compliance with ISA**

Programs used for documenting the inspection procedures performed in respect of review of audit files:

- CAIM review programs: ISA 540 accounting estimates, ISA 600 Special considerations –Audits of group FS (including the work of component auditors and revenue work program;
- UK file review work programs implemented in our methodology such as engagement management, materiality, audit report, planning and risk assessment;
- we developed our own work programs for review of account balances and also for areas such as JET, related party transactions, post balance sheet events.

All findings which we identify during inspection are noted as deficiencies in meeting requirements of ISA, quality control, audit regulations or other applicable laws and regulations.

We divide them on significant findings and findings.

## Significant firm-wide finding:

- Relevant requirement in an auditing, quality control or ethical standard (or in a firm policy) was not met,
- circumstances indicate that there is a pervasive or systemic issue (rather than a one time deviation or isolated issue), and
- not only remote likelihood that the deficiency could affect the audit firm's independence or the quality of audits performed by the firm.

## Firm –wide finding:

other deficiency identified, which does not affect the independence of the audit firm and does not significantly affect the quality of the audit and is mostly the result of a one-off event.

## Significant file review finding:

- procedures of substance required by a standard were not performed and relate to a material account balance, class of transaction or disclosure,
- certified auditor failed to obtain sufficient and appropriate audit evidence for a key assertion.
- Significant deficiencies in documenting auditor's procedures

## File review finding:

- certified auditor did not perform procedure required by a standard, but we assessed that he still obtained sufficient audit evidence for key assertion,
- minor deficiencies noted in documenting auditor's procedures.



## Examples of significant Firm –wide findings:

### ➤ Engagement quality control review (EQCR):

Audit firm didn't establish and implement sufficient policies and procedures on documentation of the engagement quality control review, therefore work performed by EQCR was not properly documented.

### ➤ Rotation of key audit partner KAP:

The firm didn't establish policies and procedures, requiring, for audits of financial statements, the rotation of the engagement partner and the individuals responsible for engagement quality control review and others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements and local legislation. Therefore, KAP breached the rotation requirement set in local audit legislation (max. 7 years)

### ➤ Appointment of a key audit partner (KAP)

The firm didn't establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to perform engagements in accordance with professional standards and applicable legal and regulatory requirements. Therefore persons/partners without appropriate licence and authorisation were appointed as KAP in several engagements.

## ➤ Engagement performance

The firm didn't establish policies, procedures and specific guidance to promote consistency in the quality of engagement performance and processes to comply with applicable engagement standards and appropriate document the work performed and the timing and extent of procedures. Therefore KAP's failed to appropriate document risk assessment procedures, select appropriate samples to perform test of details etc.

## ➤ Completion of the assembly of final engagement files

The firm didn't establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized.

## ➤ Auditor's report

The firm didn't establish policies and procedures that the firm or the engagement partner issue reports that are appropriate in the circumstances. Therefore number of misstatements were identified in different parts of the auditor 's report.

## Examples of Firm –wide findings:

### ➤ Assessment of the internal quality control system

Audit firm didn't establish policies for documenting the assessment and evaluation of the firm's system of quality control and findings of that assessment therefore didn't keep the record of such assessment and their findings

### ➤ Additional report to the audit committee

Audit firm didn't include all information required in additional report to audit committee, but omissions were not significant

### ➤ Acceptance and Continuance of Client Relationships

Audit firm didn't establish policies and procedures for documenting their consideration of the integrity of the client and how the consideration and also supporting documentation for conclusion should be documented.

### ➤ Disclosure checklist

Audit firm didn't establish policies and procedures for documenting review of completeness and adequacy of financial statements disclosures by using relevant disclosure checklist

## Examples of audit file significant findings:

### ➤ Materiality

The basis for determining materiality is not adequately documented on the audit file. The factors that auditor has considered in determining an appropriate benchmark for materiality, justification of percentage used in calculation, factors considered in determine performance materiality, are not documented on the audit file.

### ➤ Audit Procedures Responsive to the Assessed Risks of Material Misstatement at the Assertion Level

- Auditor failed to obtain sufficient and appropriate audit evidence with regard to the valuation of inventories. The firm failed to obtain appropriate audit evidence with respect to the lower of cost and net realisable value test,
- Auditor failed to obtain sufficient and appropriate audit evidence with regard to revenue recognition,
- Auditor failed to test the design and implementation of the relevant internal controls relating to revenue recognition,
- The firm failed to obtain sufficient appropriate audit evidence regarding the risk of fraud through its journal entry testing.

## ➤ Group audit engagements

Auditor failed to perform required audit procedures for consolidation process and failed to properly document them. From audit documentation is not clearly evident which procedures have been performed, the group audit instructions to the component auditors were not sent, completeness of the consolidation scope is not documented engagement team did not evaluate the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications, the auditor did not evaluate whether the financial information of that component has been appropriately adjusted for purposes of preparing and presenting the group financial statements.

## ➤ Omission of disclosures to financial statements

Auditor failed to identify significant omissions of disclosures to financial statements in annual report.

## ➤ Accounting estimates

The auditor failed to perform adequate procedures to be able to conclude that accounting estimates are reasonable.

## ➤ Using the work of an Auditor's expert

The auditor failed to evaluate whether the external experts engaged to perform part of the audit work had the necessary competence, capabilities and objectivity and failed to evaluate the adequacy of the auditor's expert's work for the auditor's purposes.

## Examples of audit file findings:

### ➤ Omission of disclosures to financial statements

Auditor used a disclosure checklist to check the completeness and accuracy of disclosures, however he didn't identify or properly document omissions of some disclosures which were not significant.

### ➤ Written representations

Auditor failed to obtain written representations from management whether they believe significant assumptions used in making accounting estimates are reasonable.

### ➤ Information to Be Used as Audit Evidence

Auditor failed to test the accuracy and completeness of IPE key reports used during the audit.

### ➤ Additional report to audit committee

Auditor failed to include all information required in additional report to audit committee, but omissions were not significant

### ➤ Sampling

Auditor failed to document how he selected items for the sample.

Based on inspection performed, the Agency present all its findings to the audit firm in Report on inspection. In Report we also present a final assessment of the compliance of the audit firm's work with applicable requirements, using one of the four quality categories.

All KAP which were inspected also receive separate Report on inspection, where all the findings are presented together with the final assessment of the quality of work performed.

In Report on inspection we also include:

- legal basis for performing inspection
- basic information about the audit firm inspected
- presentation of the selection of key audit partners and audit files
- an indication of the inspectors who performed the inspection

- focus areas of inspection for both firm wide controls and for audit file review
- a description which finding is considered significant

Reports of inspection are not published.

The Reports of inspections are the basis for potential measures of inspections taken. The measures are taken when the quality of the audit is rated as unsatisfactory.



# GRADING DESCRIPTION

GRADING DESCRIPTION	FIRM –WIDE	AUDIT FILE
GOOD	Small number of findings (less than 6)	Small number of findings (less than 6)
	Audit firm is compliant with all requirements	Good performance, KAP ensured compliance with all requirements
SATISFACTORY WITH MINOR IMPROVEMENTS NEEDED	very small number of significant findings (less than 3) and small number of findings (less than 6), minor improvements are needed	very small number of significant findings (less than 3) and small number of findings (less than 6), minor improvements are needed
	Audit firm ensures compliance with the applicable requirements on major part of the quality control system	Good performance with minor improvements needed, KAP still ensured compliance
PERFORMANCE IMPROVEMENT NEEDED	Small number of significant findings (less than 6) and large number of findings (less than 10)	Small number of significant findings (less than 6) and large number of findings (less than 10)
	Audit firm is not compliant with requirements in all parts of quality control system	Performance improvement need, it depends –professional judgment needed to evaluate if the KAP ensured compliance
UNSATISFACTORY	Large number of significant findings (more than 6) and large number of findings (more than 10)	Large number of significant findings (more than 6) and large number of findings (more than 10)
	Audit firm is not compliant with requirements of quality control system	Unsatisfactory performance, significant improvements needed, KAP is not compliant

**QUESTIONS?**