

# **Oversight and Profession of Auditing in Georgia**

Launch Event –

Service for Accounting, Reporting and  
Auditing Supervision

21 June 2017

# Agenda

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- ▶ Oversight and Profession of Accounting in Georgia
  - ▶ Global trends and best practices
  - ▶ A bit of history
  - ▶ Key opportunities and challenges for Georgia
  - ▶ Current status of cooperation

# Global trends and best practices

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- ▶ A starting point for a current approach, which assumes a public oversight of the audit profession, can be traced to adoption of a Sarbanes-Oxley Act in 2002. Until those times, audit profession was mostly self-regulated.
- ▶ It is widely accepted that audit profession cannot efficiently self-regulate due to incentives which are inherent in the conduct and set-up of audit services, such as:
  - ▶ Conflict of interests inherent in “client-auditor” relations;
  - ▶ Audit quality may not be sufficiently incentivised by market forces only;
  - ▶ In unregulated market, decision makers may place more value on price and ‘agreeability’ than audit quality;

# Global trends and best practices

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- ▶ Audit professions is one of the most difficult and complex professions to regulate and supervise.
- ▶ Properly conducted audit is based on complex judgments, which auditor should make based on the analysis of large volume of evidence collected during the conduct of the audit regarding the audited entity and its business, its system of internal controls and financial reporting.
- ▶ In addition, the auditor should possess in-depth knowledge of the industry sector and wider economic conditions which influence the audited entity,
- ▶ and have deep knowledge and experience in the auditing standards and relevant accounting framework.
- ▶ Audit is not a routine repetition of certain procedures, following the pre-defined schedules and ticking-off of relevant checklists.

# Global trends and best practices

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- ▶ Therefore it is of utmost importance that people engaged in the audit supervision have profound knowledge of the audit process and have vast experience of conducting audits in the capacity of a persons responsible for the delivery of the audit.
- ▶ Resources of both the auditors and the supervisor are limited. Only sufficient professional expertise of the supervisor can warranty risk based approach to regulation, which best serves the public interest.
- ▶ Lack of sufficient professional expertise at regulator may skew the supervision process into undue emphasis on the formalities, while loosing a sight of risks. Forcing auditors to spend extended time and resources on formal compliance, provision of information and disclosures, reporting and other formalities, while taking away the resources from performance of real and important purpose of the auditors' work.

# Global trends and best practices

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- ▶ The supervision bodies perform monitoring of the audit quality and ensure its improvement by utilizing following approaches:
  - ▶ Regular review of the quality control process at the auditors;
  - ▶ Regular review of the specific audit engagements;
  - ▶ Development of rules and regulations which incentives improvements in the quality control process of the auditors;
  - ▶ Performance of investigations and introduction of sanctions in the cases of material deficiencies, including right to withdraw the auditor from the market if its unable or unwilling to follow professional standards

# Global trends and best practices

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- ▶ Difficulties inherent in the regulation of the audit profession pose significant challenges to organization, funding, staffing and efficient operation of supervision bodies.
- ▶ It is generally agreed, that the supervision body should be independent of the audit profession.
- ▶ In most of the cases, the supervision body is an independent organization. In rare cases, it is part of the other regulator or the Ministry of Finance.
  - ▶ In countries where auditing profession is relatively small and newly established, it may make sense to combine the audit supervision body with other established regulator, which could benefit from such a synergy and allow a new regulator time to grow;
  - ▶ Existence of the supervision body at the Ministry of Finance, makes it more prone to political risks. Therefore actions should be taken to warranty relative independence of the supervisor, for example, by introducing longer terms for its management, establishment of an independent board, establishment of budget allocation rule, which is not dependent on the change of the leadership at the Ministry, etc.

# A bit of history

## Phase I – the 90's

Mandatory reporting and audit introduced by the law

Accounting and audit supervision authority created under the Parliament of Georgia

Audit became licensed activity.

Mandatory auditing and reporting requirements introduced based on the 'best practices' considerations, without adaptation to then current state of economy, needs and public interest.

Supervising authority not adequately funded and staffed.

Birth of, so called, "200 Lari audit opinions"

Discrediting of the audit profession

Discrediting of the supervision authority



# A bit of history

## Phase II – the 2000's

Mandatory reporting and audit abolished and discretion given to relevant regulators to introduce reporting and auditing requirements in the areas of their supervision

Supervision authority not formally abolished, however its authority fully eliminated due abolishment of license requirements for auditors (de-facto deregulation)

Free market allowed to regulate the audit profession.

Audit services acquired by clients only on needs basis, thus selecting trust-worthy auditors with international credentials.

Return of the trust to profession, but concentrated in few larger firms

Difficulties for the Government in selection of audit firms, resulting in "Chapter 360"

# Key opportunities and challenges for Georgia

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- ▶ Opportunities:
  - ▶ Positive impulse for the development of corporate governance in the corporate sector
  - ▶ Growth of audit quality in smaller/local auditors and growth of public confidence in smaller/local auditors
  - ▶ Improvement of investment climate through growth of transparency
  - ▶ Stimulus for the growth of audit business

# Key opportunities and challenges for Georgia

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## ▶ Challenges

- ▶ Insufficient market incentives, resulting in additional reporting and auditing requirements being viewed by market participants as simply a growth of cost of doing a business
- ▶ No depth in the audit profession, high competition on professional resources and no retired audit partners
- ▶ Small size of the audit market and small size of the audit firms.
- ▶ Continuous strengthening of SARAS

# Current status of cooperation

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- ▶ The Board
- ▶ Open discussions
- ▶ Consultations
- ▶ Perspectives



**Thank you!**