

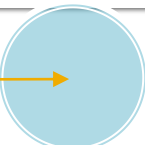
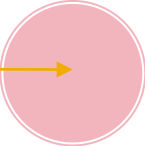

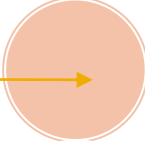
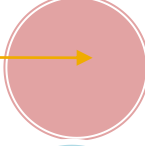
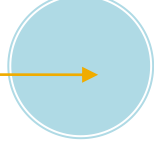
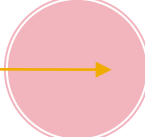


AUDIT ASSURANCE WORKSHOP

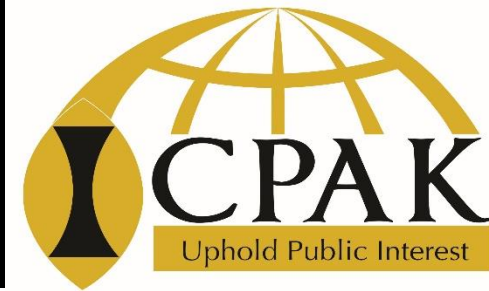
Gelian Hotel, Machakos

Saturday, 18 March 2017

OUTLINE

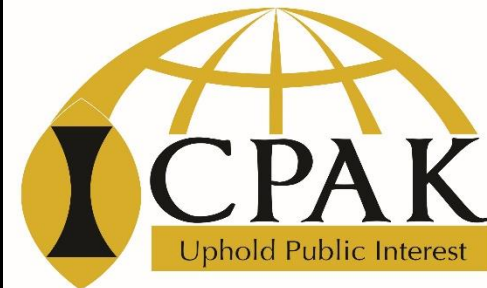
1.  OVERVIEW
2.  WHICH REPORTS ARE AFFECTED
3.  NEW AND REVISED STANDARDS
4.  KAM
5.  ISA 720 REVISED
6.  ETHICS
7.  COMPANIES ACT

Overview



- In January 2015, the IAASB issued the new and revised auditor reporting standards
- Contains a raft of changes including:
 - Changes to the format
 - Disclosure of auditor's independence
 - Enhanced disclosures of the auditor's responsibilities
 - Going concern (if there exist material uncertainty or in close call situations)
 - Key audit matters (For PIEs) – ISA 701.
 - Disclosure of reference to the terms of engagement (engagement letter)

Which audit reports are affected?

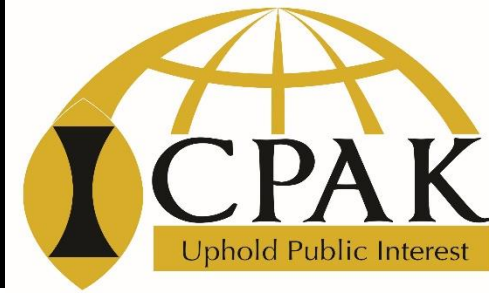


All International Standards on Auditing (ISA) audit reports, not just those for listed entities, will look different compared to current audit reports, for example:

- Opinion first;
- Affirmative statement about the auditor's independence and fulfillment of relevant ethical responsibilities;
- Enhanced description of the responsibilities of the auditor and key features of an audit;
- Enhanced description of the respective responsibilities of management and the auditor regarding going concern;
- Material going concern uncertainty reported in a separate section in the audit report; and
- Revised reporting requirements relating to “other information” included in an entity's annual report

In addition, audit reports on **listed entity** financial statements will include “key audit matters” (KAMs) – a significant change

New and Revised Auditor Reporting Standards



Overarching Standard for Auditor Reporting – ISA 700 (Revised)

New Key Audit
Matters section
ISA 701

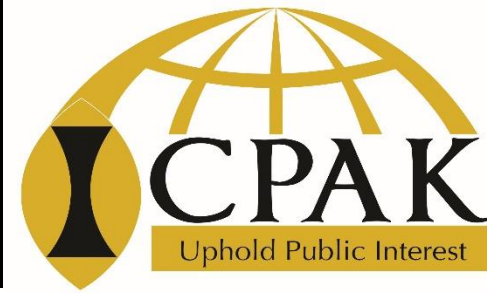
Modifications
to auditor's
opinions
ISA 705
(Revised)

Enhanced
auditor
reporting
related to going
concern
ISA 570
(Revised)

New auditor
reporting on
other
Information
ISA 720
(Revised)

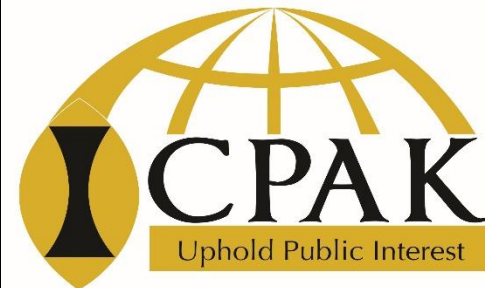
Revisions to **ISAs 260 and 706** as a result of ISA 701, and related conforming amendments to **ISAs 210, 220, 230, 510, 540, 600, 710**

What are KAM?



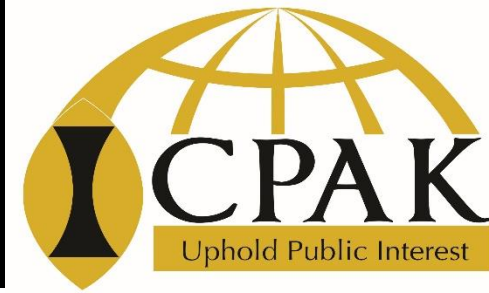
- KAM are defined as those matters that, in the **auditor's professional judgment**, were of **most significance** in the audit of the financial statements of the current period
- KAM are **selected from matters communicated with TCWG**
- **KAM are not the same as Management Letter Issues***

KAM section?



- **KAM are required** to be communicated in the auditor's report **for audits of financial statements of listed entities** in accordance with new ISA 701
- **Law or regulation may require KAM** for audits of entities other than listed entities (e.g., “public interest entities”, or public sector entities)
- **Auditors may voluntarily, or at the request of management or TCWG, communicate KAM** in the auditor's report for entities other than listed entities

When not to include KAM

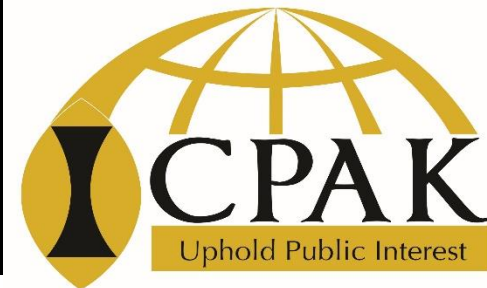


- There are some situations (for “sensitive matters”) in which the auditor would not be required to disclose a matter:
 - if law or regulation precludes it, or,
 - in extremely rare circumstances, where the adverse consequences of public communication of a matter would reasonably be expected to outweigh the public interest benefits

The IAASB has been very clear that the provisions should not be abused to avoid disclosing matters that do not firmly fit these circumstances

- KAM is prohibited for a disclaimer of opinion, but required for a qualified or adverse opinion
- In certain *limited* circumstances, there may be no KAM to be communicated

Decision-Making Framework for KAM



Starting population: all matters communicated with those charged with governance

The determination of matters that required **significant** auditor attention in performing the audit

The determination of which of those matters were of the **most significance** (the population of “key audit matters”)

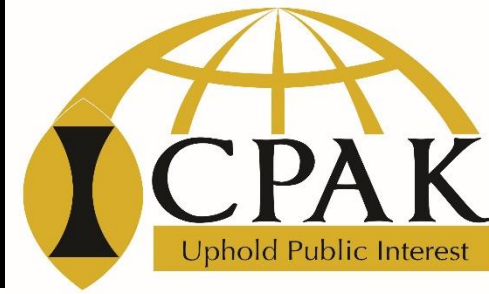
Key audit matters

Permission to **carve out** “sensitive matters”

Carve out in extremely rare circumstances

Key audit matters to be described in the auditor’s report

Initial step in determining KAM



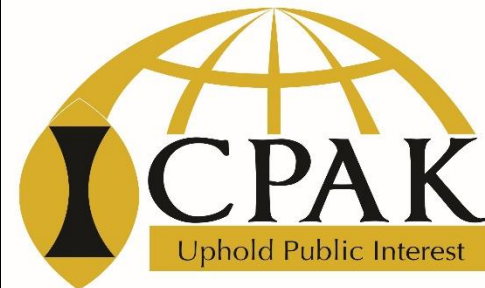
Matters communicated
with TCWG

Matters that
require significant
auditor attention

The auditor will always consider:

- Areas of higher assessed risks of material misstatements or significant risks (i.e., risks requiring special audit consideration) in accordance with the auditing standards
- Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty
- The effect on the audit of significant events or transactions that occurred during the period.

Determining KAM



Matters that require
significant auditor
attention

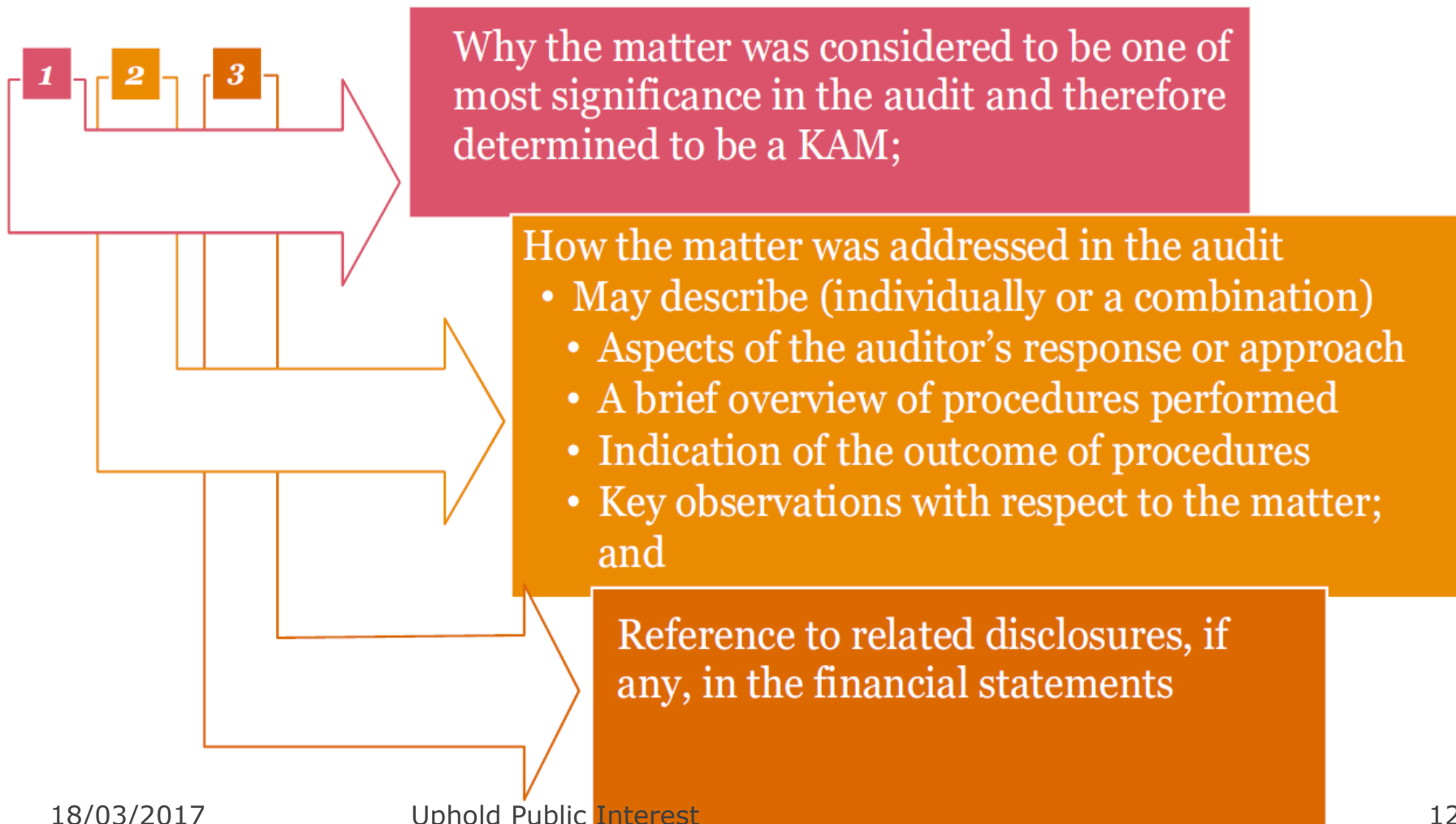
Matters of most
significance in
the audit

KAM are determined by the auditor's consideration of the:

- Nature and extent of communication with TCWG
- Importance to intended users' understanding of the financial statements
- Nature and extent of audit effort needed to address
- Nature of the underlying accounting policy, its complexity or subjectivity
- Nature and materiality, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements due to fraud or error (if any)
- Severity of any control deficiencies identified relevant to the matter (if any)
- Nature and severity of difficulties in applying audit procedures, evaluating the results of those procedures, and obtaining relevant and reliable evidence





Describing KAM

The description of a KAM in the audit report is required to include



Describing KAM (continued)

Guiding principles on the language used in the report

			
Relate the matter directly to the specific circumstances of the entity, while avoiding generic or standardized language	Take into account how the matter is addressed in the related disclosure(s) in the financial statements, if any	Imply that the matter has not been appropriately resolved by the auditor in forming the opinion	Contain or imply discrete opinions on separate elements of the financial statements

Describing KAM (continued)

How far will auditors go in describing findings in the auditor's report?

1

The auditing standards do not require the auditor to include findings on KAMs in the auditor's report.

2

While readers of the audit report might find KAM descriptions incomplete without the auditor's findings or outcome, there are questions around how this can be done meaningfully.

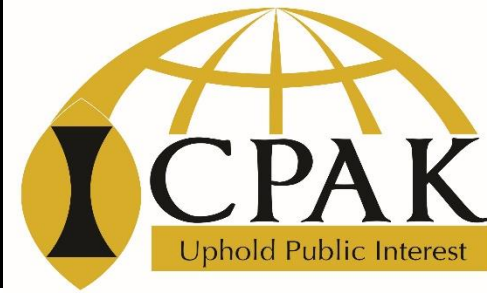
3

For example, might the auditor's view end up supplanting management or the directors' judgement?

4

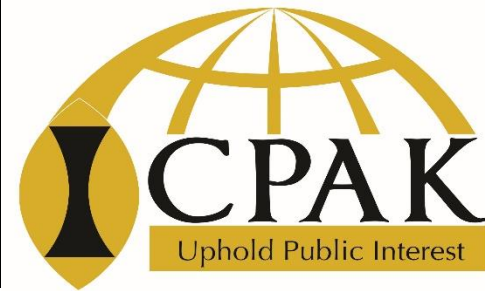
This will continue to be an area for discussion as experience with the new reports evolve.

How many KAMs will be reported?



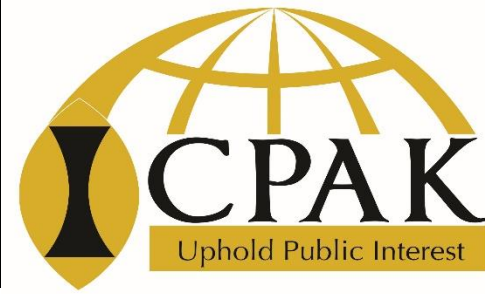
- The auditing standards neither prescribe the number of KAMs that should be reported nor provide a suggested range of number of KAMs
 - KAMs are selected based on the auditor's **professional judgment**
 - The standards state that the greater the number of KAMs that are initially determined, the more auditor should reconsider which of those matters were of **most significance** to the audit

If no KAM is identified?



- The relevant auditing standard envisages that this will be rare: The determination of KAMs involves making a judgment about the **relative importance** of matters that required significant auditor attention
- The audit report must still contain a “Key audit matters” section which must state that the auditor has determined that there are no key audit matters
- Audit documentation must include the rationale for the auditor’s determination that there are no key audit matters to communicate in the auditor’s report

Effect on Financial Reporting Process

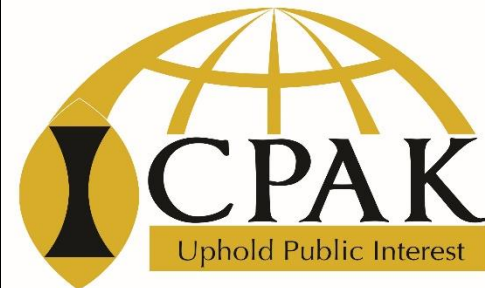


It remains **management's responsibility**, with the oversight of those charged with governance, **to communicate relevant information to users about the entity and its financial performance**, including providing adequate disclosures in accordance with the applicable financial reporting framework.

Auditor's report should not be the original source of information about the entity

The new style auditor's reports may result in enhanced disclosure by management in the financial statements

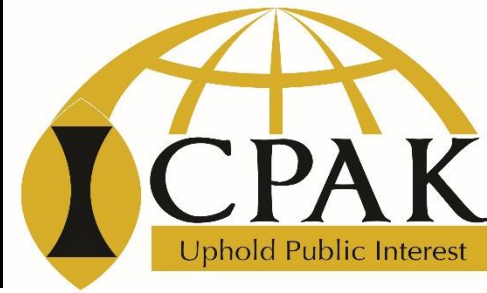
Effect on the Audit Process



The changes to the auditing reporting standards do not change the underlying work effort required in an ISA audit, but rather focus on increased transparency about the audit that was performed

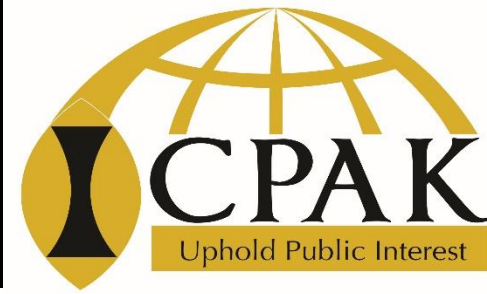
Time commitment will be required from senior members on the audit team and the firm's internal quality assurance functions with regard to the identification of KAMs and the articulation thereof in the auditor's report

What has changed regarding the auditor's consideration of going concern?



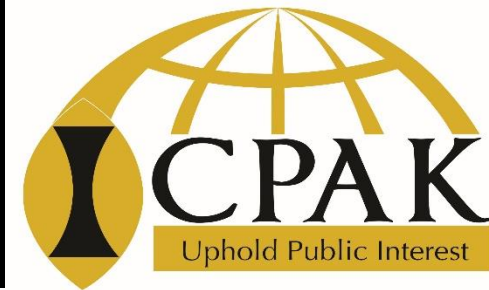
- Stakeholders have requested earlier warning of potential issues that may exist with respect of an entity's ability to continue as a going concern
- The auditor's work effort on going concern has been enhanced as follows in the revised auditing standard on going concern:
 - New guidance was added to support the auditor's evaluation of disclosures when **a material uncertainty exists**;
 - A new requirement has been added for the auditor to evaluate the **adequacy of disclosures in "close-call" situations**
- All auditor's reports will include descriptions of the responsibilities of the auditor and management in relation to going concern to provide an additional focus on going concern

KAM – Relationship to Emphasis of Matter (EOM) and Other Matter (OM) Paragraphs and Modified Opinions



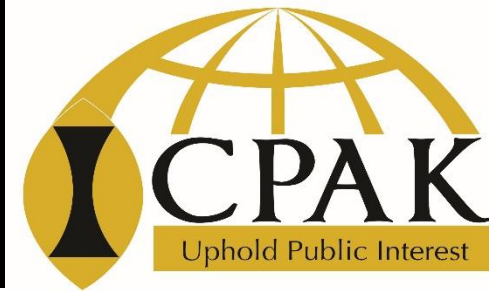
- Concepts of EOM and OM paragraphs are retained
- EOM and OM paragraphs cannot be used as a substitute for communicating a matter determined to be a KAM
- New requirement to use the term “Emphasis of Matter” in the heading in the auditor’s report when an EOM paragraph is included
- Modified opinion are KAM by their nature but are described in the Basis for Opinion section

ISA 720 (Revised 2015)



- This ISA provides for the auditor's work effort with respect to other information
- The auditor is required to read the other information and:-
 - consider whether there is a **material inconsistency** between the **other information** and the **financial statements**; and
 - consider whether there is a **material inconsistency** between the **other information** and the **auditor's knowledge** obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit

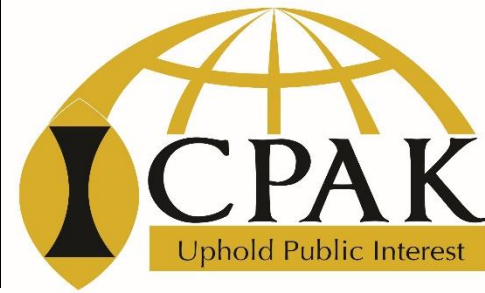
ISA 720 (Revised 2015)



Using the heading “Other Information” or other appropriate heading, the auditor’s report will include:

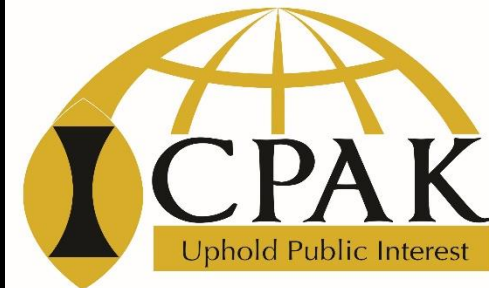
- A statement that **management is responsible** for the other information.
- **Identification** of the other information obtained prior to the date of the auditor’s report.
- A statement that the auditor’s opinion does not cover the other information and, accordingly, that the auditor does not express (or will not express) an audit opinion or any form of assurance conclusion thereon.
- A description of the auditor’s responsibilities relating to reading, considering and reporting on other information.

ISA 720 (Revised 2015)



- When other information has been obtained prior to the date of the auditor's report, either :
 - i. A statement that the auditor has nothing to report; or
 - ii. If the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information

Example



Other Information [or another title if appropriate, such as “Information Other than the Financial Statements and Auditor’s Report Thereon”]

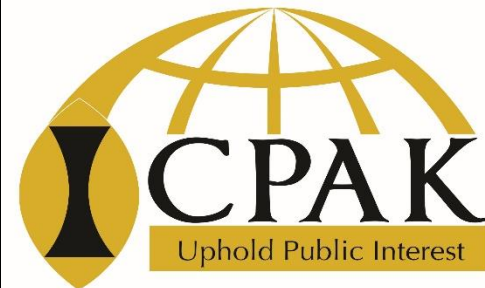
Management⁶ is responsible for the other information. The other information comprises the [information included in the X report,⁷ but does not include the financial statements and our auditor’s report thereon.]

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

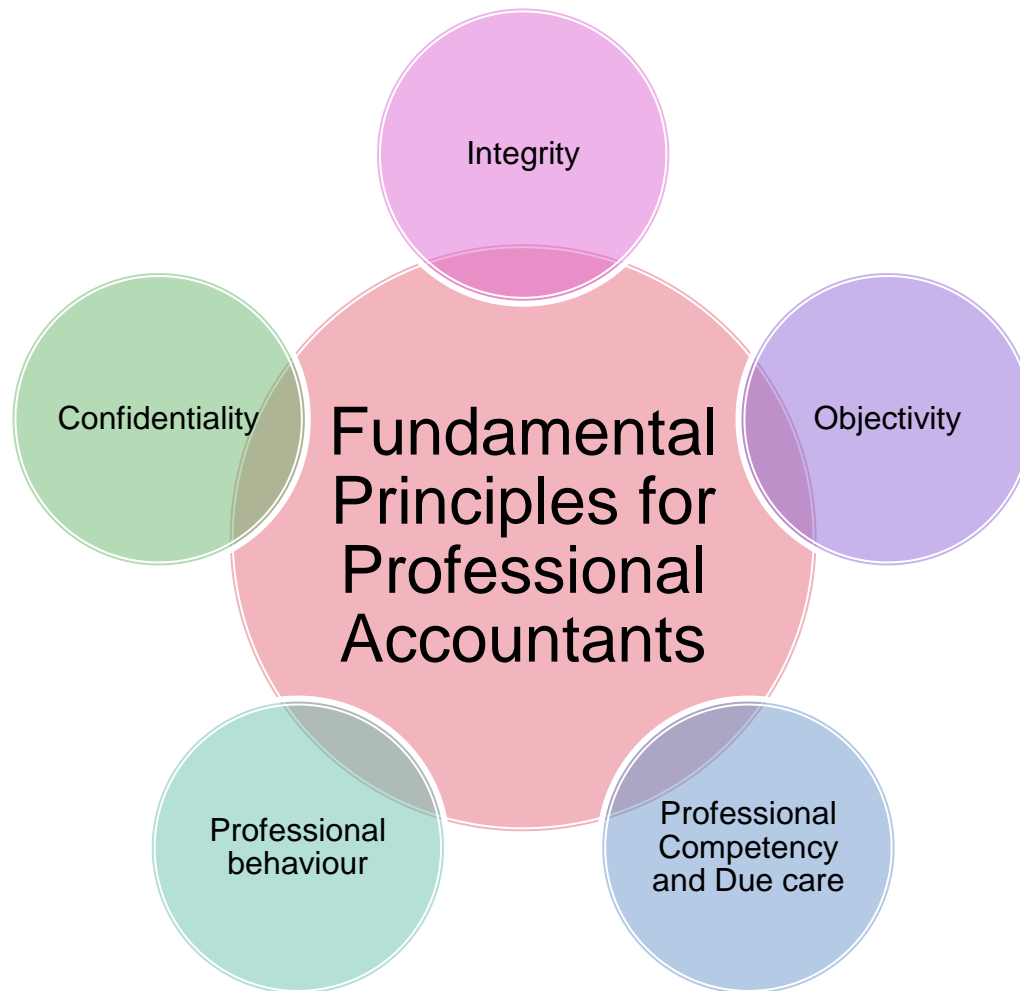
In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

- See ISA 720 (Revised, 2015) for more examples

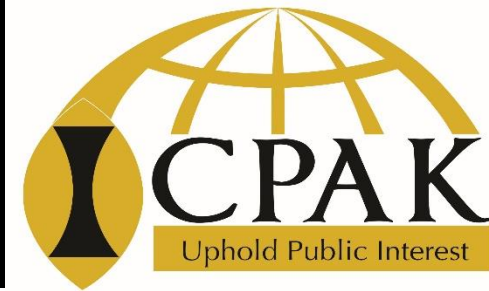
Kenya's case



- The Institute adopted the new and revised standards, in April 2015, *as issued by the IAASB taking into account the provision to extend the scope of key audit matters...*
- Engagement with regulators
 - CBK to issue circular for mandatory inclusion of KAM for banks
 - Insurance Regulatory Authority – engagements
 - Capital Markets Authority – extend KAM to all issuers of securities to the public and its licensees
 - OAG – phased approach with large state corporations to be included in phase I.
 - SASRA – engagements in progress...
- The ISAs permit early application of the standards, as long as the entire suite of new and revised standards is applied.
- Sensitisation and training of practitioners on the new and revised standards.

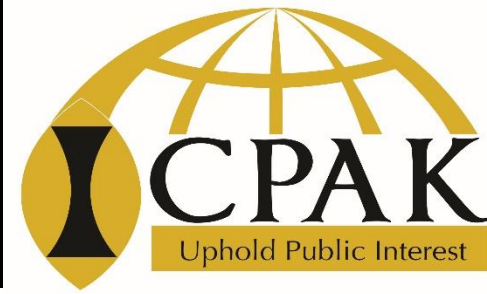


Responding to Non Compliance with Laws and Regulations (NOCLAR)



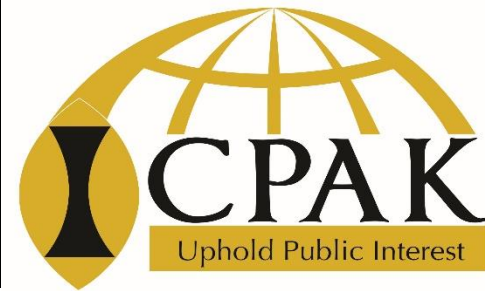
- NOCLAR refers to “any act of omission or commission, intentional or unintentional, committed by a client or employer, including by management or by others working for or under the direction of the client or employer, which is contrary to prevailing laws or regulations”.
- The laws and regulations covered, violations of which are acts of NOCLAR, are those that **directly affect the client’s or the employing organization’s financial statements or its business in a material or fundamental way.**
 - FRAUD
 - TAX AND PENSION LIABILITIES
 - BRIBERY
 - PROCEEDS OF CRIME
 - TERRORIST FINANCING
 - FINANCIAL PRODUCTS & SERVICES
 - SECURITIES MARKETS
 - DATA PROTECTION
 - ENVIRONMENTAL PROTECTION
 - SECURITIES TRADING
 - PUBLIC HEALTH AND SAFETY
- Personal **misconduct unrelated to the business activities** of the client or employer and matters that are clearly inconsequential, are outside the scope of NOCLAR

Why was NOCLAR developed?



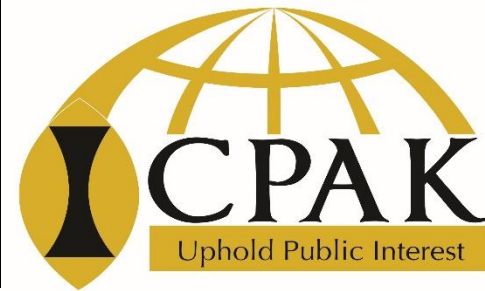
- NOCLAR responds to the following key public interest concerns:-
 - i. that professional accountants have “used” duty of **confidentiality** in the Code as a barrier to the disclosure of potential NOCLAR to public authorities in the appropriate circumstances;
 - ii. that auditors simply resigning from client relationships without NOCLAR issues being appropriately addressed; and
 - iii. there is a lack of guidance to help PAs in working out how best to respond to potential NOCLAR, a situation that may often be difficult and stressful.

Intended Outcomes



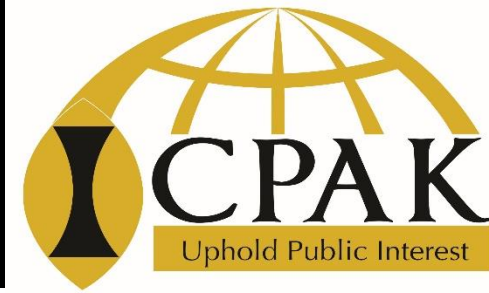
- i. Ensuring that PAs respond in a timely way to identified or suspected NOCLAR
- ii. Rectifying, remediating, or mitigating the adverse consequences of identified or suspected NOCLAR to stakeholders and the general public
- iii. Deterring the commission of NOCLAR
- iv. Stimulating increased reporting of identified or suspected NOCLAR where required by law or regulation, or where determined appropriate under the Code in the public interest

Who will be affected?



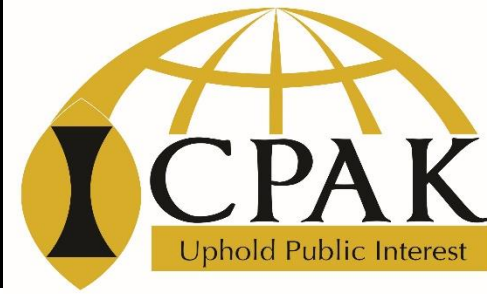
- The standard applies to all PAs.
- However, it stipulates a different but proportionate approach for the following four categories of PAs:-
 - i. Auditors
 - ii. Other PAs in public practice
 - iii. PAs in business who are in senior-level *roles—directors, officers, or senior employees in their employing organizations*
 - iv. Other PAs in business
- Those with whom PAs may raise NOCLAR matters will also be directly affected—including those in management positions or on boards of directors, and regulators or other public authorities.

What Is Required of Auditors?



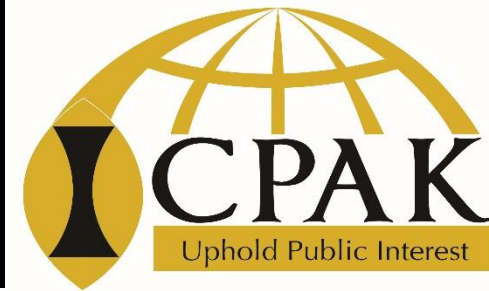
- **Raise the identified or suspected NOCLAR with management/TCWG**
 - To clarify their understanding of the matter, to substantiate/dispel their concerns, and to enable management/TCWG to investigate it
 - To advise management/TCWG to (i) address the consequences, (ii) deter the NOCLAR, or (iii) disclose the matter to an appropriate authority where required by law or regulation or where necessary in the public interest
- **Fulfil professional responsibilities**
 - Understand and comply with applicable laws and regulations, including requirements regarding reporting to an appropriate authority and prohibitions against “tipping off”
 - Comply with applicable auditing standards; and communicate the matter appropriately
- **Determine if further action is needed**
 - Assess appropriateness of the response of management/TCWG
 - In light of that response, determine objectively if further action needed in the public interest
- **Imminent breach**
 - In exceptional circumstances, may immediately disclose the matter to an appropriate authority if imminent breach of a law or regulation that would cause substantial harm to stakeholders
- **Document, among other matters, courses of action considered, judgments made, and decisions taken**

What Is Required of Senior-Level PAIBs?



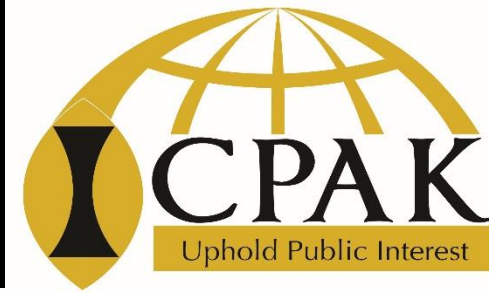
- **Overarching expectations**
 - Set the **right tone at the top** within the organization
 - Establish **appropriate policies and procedures** to prevent NOCLAR, including whistleblowing procedures as a necessary part of good internal governance
- **Fulfil professional responsibilities**
 - Take appropriate steps to: (i) raise the identified or suspected NOCLAR with a superior/TCWG, (ii) understand and comply with applicable laws and regulations, including requirements to report the matter to an appropriate authority, (iii) rectify, remediate, or mitigate consequences, (iv) reduce the risk of re-occurrence; and (v) seek to deter the NOCLAR
 - Also determine whether disclosure to the external auditor, if any, is needed.
- **Determine if further action is needed**
 - Assess appropriateness of the response of superiors, if any, and TCWG
 - In light of that response, determine objectively if further action needed in the public interest
- **Imminent breach**
 - In exceptional circumstances, may immediately disclose the matter to an appropriate authority if imminent breach of a law or regulation that would cause substantial harm to stakeholders
- **Documentation is encouraged**

What Is Required of Other PAs in Public Practice and Other PAIBs?



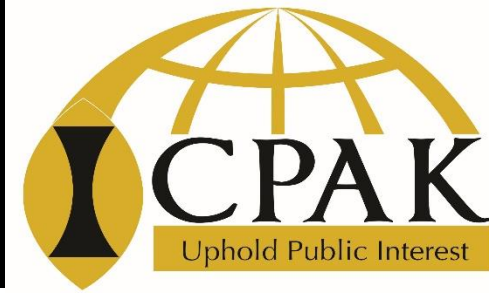
- **PAs in public practice other than auditors**
 - Discuss the identified or suspected NOCLAR with management and/or TCWG
 - If the client is also an audit client of the firm, communicate the matter within the firm
 - For any other client, consider communicating the matter to the firm that is the external auditor, if any
- Stand back and consider whether further action is needed in the public interest; which may include:-
 - Disclosing the matter to an appropriate authority even if not required by law
 - Withdrawing from the engagement and client relationship
- **Imminent breach - disclose to appropriate authority.**
- **PAIBs who are not senior PAIBs**
 - Escalate the identified or suspected NOCLAR to the immediate superior or next higher level of authority; or
 - Use established internal whistle-blowing mechanism

Value of NOCLAR Standard



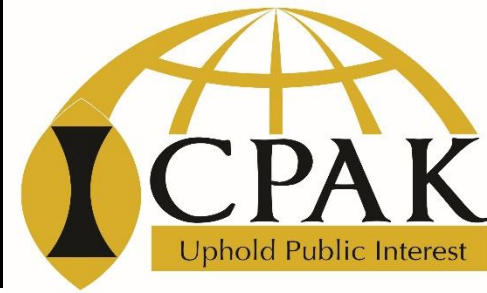
1. A holistic and balanced model – *focus on desired outcome in public interest*
2. A proportionate approach – *recognises different capabilities and spheres on influence*
3. A renewed emphasis on “tone at the top” – *importance of right culture as instilled by top leadership*
4. Expanded auditors’ “toolkit” – *disclosure pathway for auditor*
5. Complementing laws and regulations – *guidance to Pas in complying with laws and regulations.*

Companies Act of 2015



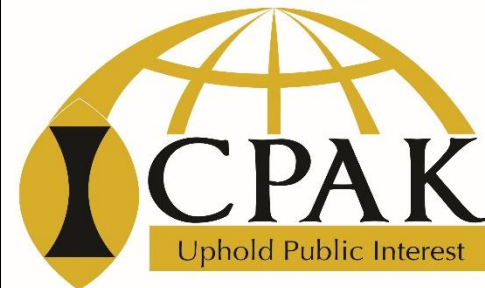
- The Companies Act No. 17 of 2015 comes with raft of changes affecting financial reporting and auditing.
- Key provisions include: -
 - Codification of directors' responsibilities
 - Additional disclosures on business review
 - Directors remuneration report, including provision for the auditor to audit and report on the auditable part of the director's remuneration report
 - Electronic mode of communication
 - Language
 - Disclosure of the auditor's terms of engagement
 - Directors' attestation on the accuracy of the financial information presented to the auditor
 - Introduction of regimes and stratification of companies
 - **Audit exemption for companies qualify as small companies**
 - Inclusion of the audit committees (for quoted companies)
 - Statutory auditor – qualification and attestation of independence = FIT AND PROPOER

Accountants as Reporting Persons



- The Proceed of Crime and Anti Money Laundering Act (POCAMLA) 2009, established the Financial Reporting Centre (“FRC”) - the competent authority for supervising financial institutions and designated non-financial businesses and professions.
- Casinos, real estate agencies, dealers in precious stones and metals and **accountants** are designated as *Designated Non-Financial Businesses or Professions (“DNFBP”)* under POCAMLA, for compliance with AML obligations.
- The FRC became operational in April 2012.
- *Professional accountants in public practice are therefore reminded to read the act and its regulations and consult the Institute and the FRC to ensure compliance. These provision including reporting to the FRC, designating Money Laundering Reporting Officers (MLRO) etc.*
- *The Institute’s practice monitoring program has also been reviewed to monitor compliance with the Act.*

Penalties



- Natural person – fine ranging from **KES <500,000 to KES <5 million** or the amount of the value of the property involved in the offence, whichever is the higher; or to imprisonment for a term ranging from **<2 years to 14 years** or both.
- Body corporate - a fine ranging from **KES <5 million to KES <25 million**, or the amount of the value of the property involved in the offence, whichever is the higher.
- *Where any offence under this Part is committed by a body corporate with the consent or connivance of any director, manager, secretary or any other officer of the body corporate, or any person purporting to act in such capacity, that person, as well as the body corporate, shall be prosecuted in accordance with the provisions of this Act.*

Thank You!

