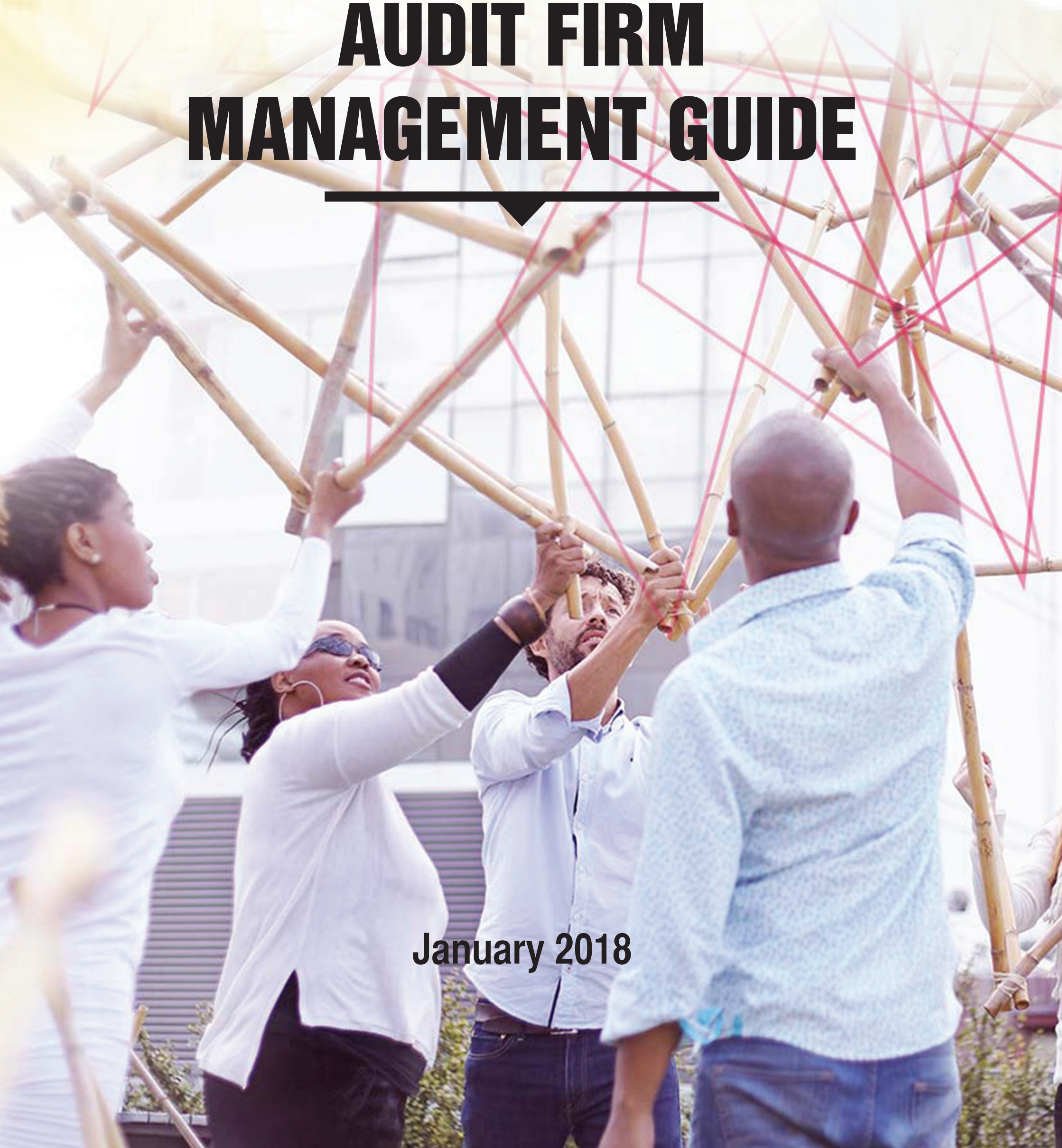
Uphold Public Interest

# AUDIT FIRM MANAGEMENT GUIDE



January 2018

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## ACKNOWLEDGEMENTS

This Guide was prepared by a team under the leadership and guidance of the Chief Executive Officer, CPA Edwin Makori. The Technical Team comprises of CPA Fredrick Riaga, CPA Nebart Avutswa, CPA Rahab Ntoiti, Hillary Onami, Elias Wakhisi, CPA Catherine Muema and CPA Patrick Ibuka.

We would like to express our gratitude to the Practitioners Development Committee (PDC) of the Institute and the select firms who helped in validation of the document.

The Institute acknowledges the valuable contributions and hard work from all individuals which led to the successful completion of this document.

Thank you.

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## ABBREVIATIONS

| | |
|---|---|
| CMA | Capital Markets Authority |
| CPA | Certified Public Accountant |
| IAASB | International Auditing and Assurance Standards Board |
| IASB | International Accounting Standards Board |
| ICPAK | Institute of Certified Public Accountants of Kenya |
| IESs | International Education Standards |
| IFAC | International Federation of Accountants |
| IFRSs | International Financial Reporting Standards |
| ISQC | International Standards on Quality Control |

## PREFACE

The purpose of this Firm Management Tool is to guide ICPAK practitioners in their day to day running of their firms. Professional accountants play a significant role in financial management which is one of the pillars to a country's growth.

The guide aims at honing the skills of Practitioners to be efficient in the ever-competitive global economy. It is hoped that through this Guide, practitioners will be able to conduct their businesses seamlessly. It will also enhance compliance to the professional requirements of practitioners during providing assurance services.

Moreover, it will improve the understanding of practicing members on their professional requirements. This in turn will lead to improved quality of services provided by practitioners.

## BACKGROUND

As the demand for assurance and non-assurance services continue to grow, the Institute has been on the forefront in building the capacity of its members. This ensures that they are in sync emerging global needs and trends of the practicing accountants.

Professional accountants play a crucial role in the country's economic development. They contribute to the credibility of the financial statements which in turn builds the confidence of the shareholders, regulators and financiers in financial reporting. As such, delivery of high quality work should be the guiding principle for a practitioner.
The International Financial Reporting Standards and International Standards on Auditing have shaped financial reporting and the auditing profession. It is needless to say that frameworks built on these technical accounting standards can only be delivered by persons with the technical know-how on the workings of these standards.

Moreover, the International Standards on Quality Control (ISQC 1) provides that the firm shall establish and maintain a system of quality control that includes policies and procedures that address each of the following elements: Leadership responsibilities for quality within the firm; relevant ethical requirements; Acceptance and continuance of client relationships; human resources; engagement performance; and monitoring.

In addition, the International Education Standard (IES) 8 prescribes the professional competence that professional accountants are required to develop and maintain when performing their duties.

Consequently, for a firm to fulfill and adhere to these standards and deliver good services to its clients competently, continued training and capacity building is pivotal. It's against the foregoing, that the Institute has developed this CPA Firm Management Guide to equip its members in practice to become effective and successful practitioners.

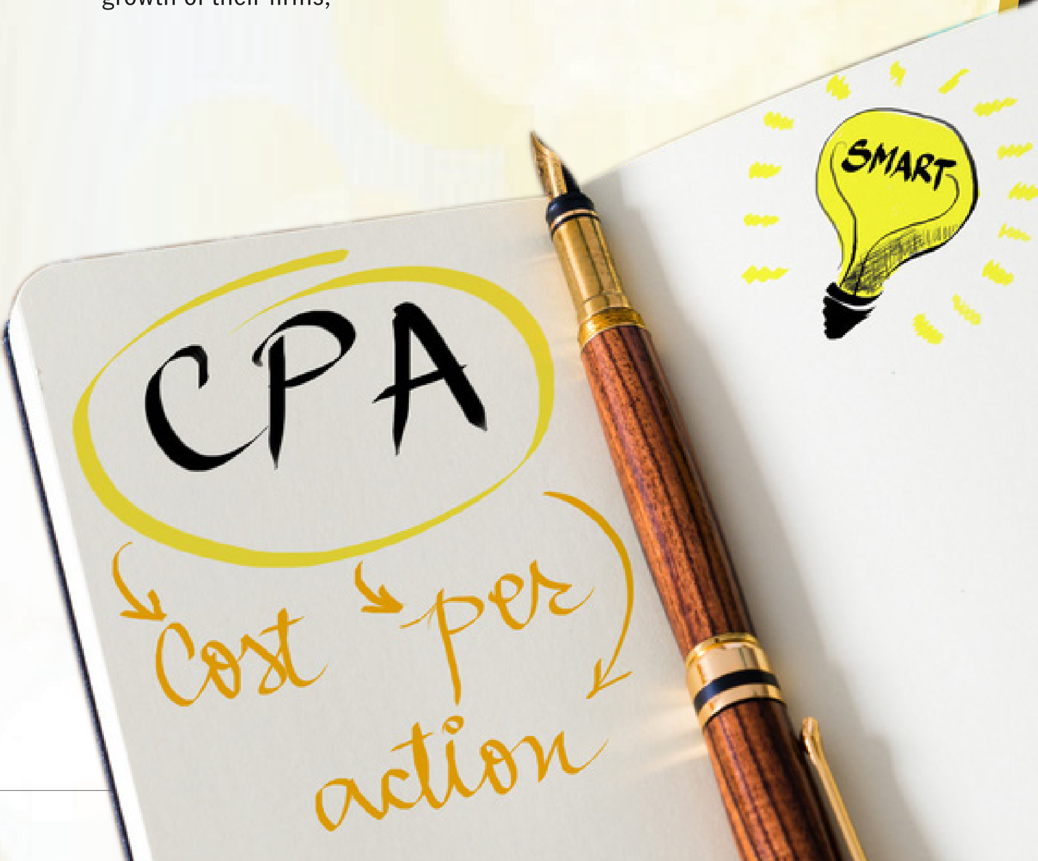
## SCOPE AND OBJECTIVES OF THE GUIDE

The guide provides an insight into various aspects that one needs to have in order to be a successful CPA firm. It outlines areas of specialization that one needs to venture into, set-up practices, audit specialization areas, branding and marketing, staffing and human resource, revenue management, work management, partnerships and compliance among others.

## OBJECTIVES

The main objective of this guide is to prepare practitioners for holistic professional growth. Specific objects include:

1. Equip ICPAK practitioners with technical skills and knowledge to be competent and efficient in the market;
2. Expose practitioners to soft career skills such as human resources development and retention, branding and marketingthatareessentialforthe growth of their firms;
3. Impart the professional accountant with practical knowledge on partnerships, mergers and acquisitions in the accountancy profession.
4. Leverage on partnerships with other professionals to complete the value chain to clients
5. Capacity build practitioners on important firm operational aspects such as revenue management, work flow management and utilization of audit techniques and tools.



## BENCHMARKING

Professional Accountancy organizations worldwide have developed guides on various topics to guide the members in professional growth. These are enumerated as follows:

### INTERNATIONAL FEDERATION OF ACCOUNTANTS (IFAC)


International Federation of Accountants (IFAC) in its quest to realize the mission to serve the public interest constantly develops guides aimed at promoting the value of professional accountants. In 2012, through the Small and Medium Practices Committee, IFAC developed a Guide to Practice Management for Small- and Medium-Sized Practices.

The Guide provides comprehensive guidance to help SMPs operate more proficiently in the increasingly complex global marketplace for professional services. The IFAC guide provides SMPs with knowledge of practice management principles and best practice guidance on strategic planning, managing staff, client relationship management, and succession planning among other topics.

For details: "Guide to Practice Management for Small and Medium-Sized Practices, Third Edition, IFAC @ 2012 *https://www.ifac.org/system/files/publications/files/SMP-PMGUserGuide.pdf*

### CPA AUSTRALIA

In 2014, CPA Australia developed a guide on "Client Relationship". The objective of the publication was to guide members through issues that must be considered or may arise when accepting a new client or fare-welling an existing client. The guide references legislative

and ethical requirements particularly for members in Australia, though members in other jurisdictions may also find the contents of the guide useful.

For more details, see:
*https://www.cpaaustralia.com.au/~/media/corporate/allfiles/document/professional-resources/practice-management/client-relationship-guide.pdf?la=en*

**SOUTH AFRICAN INSTITUTE OF CHARTERED ACCOUNTANTS**


SAICA has recently produced and acquired several practice management products like succession planning, leadership, taxation, compliance, management etc. to assist in running the practice more effectively, efficiently and most of all profitably.

*https://www.saica.co.za/About/MemberServices/Members in Small and Medium Practice.*

**THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND AND WALES (ICAEW)**


ICAEW, has developed a practice management guide for practicing firms that requires them to comply with regulations covering areas such as clients' money and anti-money laundering. Firms are also guided to take account of the Code of Ethics and the Practice Assurance regulations and related Practice Assurance standards. in addition the ICAEW guides members on how they can manage the client's documents.

For details *www.icaew.com*

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## THE PRACTICE OF ACCOUNTANCY

As a practitioner, one may venture into the following practices:

a) Statutory audits
b) Book Keeping services
c) Payroll Services
d) Tax filing, Tax Agency and consulting services
e) Management Consulting
f) Business Valuation
g) Investigations
h) Executors and Trustees
i) Insolvency Practitioners
j) Forensic Audit
k) IT and Systems Review
l) Outsourced Audit Services
m) Assurance Engagements
n) Reporting Accountants; Futures and Derivatives
o) Company Secretarial services
p) Executive recruitment
q) Attestation of documents

In the choice of the area of specialization, a practitioner should keep in mind the Institute's Code of Ethics and other relevant local legal requirements for the profession.


## BRANDING AND MARKETING

The issue of marketing and advertising of professional services offered to the public remains a contentious and challenging issue to professionals in Kenya and beyond. The Accountancy profession has for a long time perceived that advertising by members in public practice is prohibited.

However, the Accountants Act and the Code of Ethics for Professional Accountants provides for acceptable advertising and publicity. Section 30 (1) (e) of the Accountants Act provides that *"a member of the Institute shall be guilty of professional misconduct if such member solicits clients or professional work or advertises professional attainments or services by use of means which contravene the guidelines published by the Council".* The Council issued the 2010 *"Ethical Marketing and Publicity Practices in the Accounting Profession"* to provide guidance on ethical marketing for members.

**BRANDING PROCESS**
Branding is not just the use of a name, term, logo mark, or design to identify a product or service, but it is also the development of a personal relationship between the client and the product or service. Simply put, it is who people think you are, from the way a person answers the phone, to the way you do business, to the look of the invoice.

The ICPAK guidelines provide that a member shall not on behalf of himself, his partner or associate, or any other individual affiliated with him or his firm, use or participate in the use of any form of public communication containing a false, fraudulent, misleading or deceptive, thus not in public interest. Publicity not in the public interest shall include, but not be limited to, advertising or marketing that: —

(1) is false, fraudulent, deceptive, or misleading;
(2) guarantees any service based on discretionary decisions of regulatory authorities;
(3) makes any claim relating to professional services or products or the cost or price thereof which cannot be substantiated by the firm, who shall have the burden of proof;
(4) makes claims of professional superiority which cannot be substantiated by the firm, who shall have the burden of proof; or offers inducements in any form for a professional service or product.

Advertising or other forms of solicitation (communication, publicity etc.) that are false, misleading, or deceptive are not in the public interest and are prohibited. Such activities include (but not limited to) those that: — create false or unjustified expectations of favorable results; imply the ability to influence any court, tribunal, regulatory agency, or similar body or official; contain a representation that specific professional services in current or future periods will be performed for a stated fee, estimated fee or fee range when it was likely at the time of the representation that such fees would be substantially increased and the prospective client was not advised of that likelihood contain any other representations that would be likely to cause a reasonable person to misunderstand or be deceived.

Nonetheless, brand development is a strategy used increasingly by CPA firms globally because it can accomplish many important objectives such as: increase a firm's visibility in the marketplace; differentiate a firm from its competitors; deliver more consistent messages to clients, contacts, and staff; focus a firm's marketing program; enhance recruiting and retention efforts; and integrate marketing and communications after a merger.

The branding process starts with market research. First, survey your partners and staff and ask them questions, such as:

- What does our firm stand for?
- What are the unique strengths of our firm?
- What attracted you to work here?
- What differentiates our firm from its competitors?

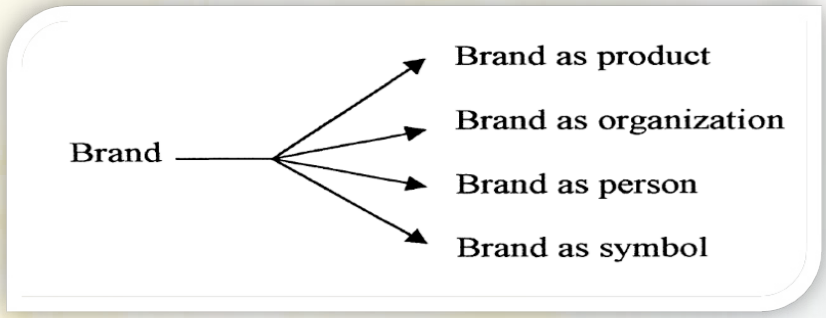
Survey your clients and ask:

- Why did you select our firm?
- What do you see as the major strength of our firm?
- What makes our firm unique?
- What does our firm offer that is superior to other accounting and consulting firms?

Survey your referral sources or centers of influence and ask:

- What do you see as the major strength of our firm?
- What do you see as the major weakness of our firm?
- If you could communicate a single message about our firm, what would it be?

Branding can thus be viewed through Aaker's Brand Identity Model as illustrated below:




## KEY MARKETING AND BRANDING TOOLS

### (a) Use of social media

Social media are the numerous forms of user generated content and the collection of websites and applications that enable people to interact and share information online.

These forms include but not limited to

- Social networking sites (Facebook, Twitter, Myspace, whatsapp, telegram)
- Blogs (Wordpress)
- Video sharing sites (YouTube)
- Photo sharing sites (Flickr, instagram)
- Crowdsourcing (Wikipedia)
- User reviews (Amazon, Yelp)
- Streaming sites (Ustream)
- Social bookmarking (Digg, del.icio.us)

Why is social media important in business and growth of a firm?

- It finds you customers and builds clientele
- It gives businesses the ability to find out what people are saying about them (and others) in their industries
- It introduces your brand
- It gives you feedback about your brand

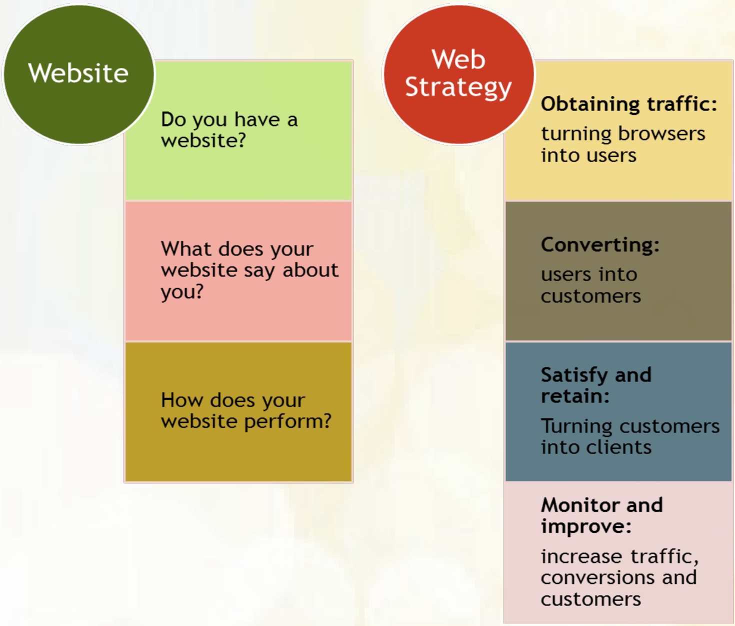
- Solidifies your reputation as a valuable and knowledgeable resource

It is imperative to note that the use of social media must be conducted within the confines of ICPAK guidelines on marketing and advertising and with respect to the Code of Ethics for Professional Accountants. This guards against individuals using the social media space to disparage other firms, create false or unjustified expectations of favorable results and other activities that violate the Code or ICPAK Guidelines.

**(b) E-Newsletters**

Firms usually send out external and internal newsletters, which contain partner's insights, key updates to motivate or educate clients, employees and the public at large.

**(c) Your Firms' website**




**(d) Other branding and marketing avenues**

- Online advertising
- Direct response e-mail,
- Sponsorships, and
- Internet advertising

## LIMITS FOR CPA FIRMS WHEN BRANDING AND MARKETING

It is important to note that branding and marketing for CPA firms has to done within the confines of ICPAK guidelines and Code of Ethics for Professional Accountants.

**ICPAK Guidelines**

The ICPAK guidelines provide that giving information on a member firm on a website is acceptable. Nevertheless, a member firm offering to perform professional services via the internet must include the following information: –

(a) member firm name;
(b) description of the firm, whether sole practice of partnership;
(c) principal place of business;
(d) business telephone;
(e) partner(s) name(s), registration number(s) and practicing certificate number(s); and
(f) a statement that the firm is licensed by ICPAK as a member firm and clearly separating from other businesses, with similar name
(g) registration number of the member firm, if it is a limited liability partnership

In the same regard, a member shall not provide the following information in an advertisement under the ICPAK guidelines: -

(a) the name or the identity of a client of the member's firm;
(b) a promise by the member or the member's firm to achieve an outcome for clients or prospective clients of the member or the member's firm or that failure to obtain that outcome shall constitute a waiver of the member or the member's firm fees.

## Code of Ethics for Professional Accountants

Furthermore, the Code of Ethics for Professional Accountants further stipulates that Marketing Professional Services should be done in a professional manner. When a professional accountant in public practice solicits new work through advertising or other forms of marketing, there may be a threat to compliance with the fundamental principles. For example, a self-interest threat to compliance with the principle of professional behavior is created if services, achievements, or products are marketed in a way that is inconsistent with that principle.

As such, a professional accountant in public practice shall not bring the profession into disrepute when marketing professional services. The professional accountant in public practice shall be honest and truthful, and not:

(a) Make exaggerated claims for services offered, qualifications possessed, or experience gained; or
(b) Make disparaging references or unsubstantiated comparisons to the work of another.

If the professional accountant in public practice is in doubt about whether a proposed form of advertising or marketing is appropriate, the professional accountant in public practice shall consider consulting with the relevant professional body. In this case, the Professional Accountant shall consult ICPAK.

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## CLIENT RELATIONSHIP

The auditor-client relationship differs from typical seller-buyer relationships primarily because the intended user of the audit service is not the client, but rather a third-party financial statement user.

According to IFAC's SMP Management Guide, each word in the term "Client-relationship Management" is important.

This is elaborated as follows:

- "Client" implies an ongoing, professional relationship. This means that once an initial relationship is established, both the firm and the client continue to deal with each other.
- "Relationship" implies that the association between client and firm is more than a simple transaction or a one-off time purchase of service

### HOW TO BUILD CLIENT RELATIONSHIPS

- Communicating to your client
- Be a useful resource to your customers
- Be honest at all times,
- Always meet your deadlines.
- Eliminate surprises
- Reward your loyal clients
- Become the Go-To Person
- Pay Attention to Feedback
- Pay Attention to Feedback
- Redefine Your Concept of "Client"
- Be patient in building new relationships.

"Management" implies that the relationship doesn't just happen, it needs to be managed. This means that there's an active involvement, more than just responding to client requests. The success of any firm hinges largely on strong client relationships, especially for a small or early stage firm. Provisional of exceptional client service should be a core value for the firm and always aiming to become a trusted partner of their clients other than viewing itself as a vendor of its services.

A firm is only as good as the clients it serves, and no business gets far after losing the clients it has. The key to success is building relationships that go beyond one-time projects and provide value to these clients on a consistent ongoing basis, make regular communications with your customers one of your top priorities.

**Challenges in maintaining Successful client relationships**

As much as building and maintaining client relationships is important for the firms, the firms are expected to ensure that the relationships are not so close as to lose their independence as required by the professional standards. The auditor-client relationship is a concern for those interested in auditor independence. Long-term firm-client relationships have been blamed for causing auditors to acquiesce to client demands, resulting from reduced auditor independence (Shafer et al. 2004). Acquiescence to client requests may result from auditors not wanting to lose the client before recuperating costs invested in building and maintaining the relationship (i.e., start-up costs) (DeAngelo 1981), or wanting to please the customer (Shafer et al. 2004).

Firms as providers of assurance services are supposed to have ethical obligations in client relationships. They have to maintain secrecy and confidentiality of private information gathered from clients during the course of conducting audit. The auditors must also follow professional standards as a basis for providing an opinion on whether the financial statements are in conformity with generally accepted auditing standards (Joshi et al., 2009).

In order to be able to perform their role, auditors often need to resolve issues which clients have clearly preferred positions (Stefaniak et al., 2012). Whereas, tension often results when auditors and their clients encounter situations, where regulatory standards allow for different judgments about the appropriate treatment of accounting transactions (Johnstone and Muzatko, 2002). The desire to maintain client relationships can influence external auditor's objectivity (Stefaniak et al., 2012).

Therefore, all members of the audit team (i.e. partners, managers, seniors and other staff) may alter their behavior throughout the audit process in response to competitive pressures. Hellman (2011) argued that auditors have to make trade-offs between having a close relationship with the client and at the same time maintaining enough distance to the client.

**Mitigations to challenges**

Although maintaining close relationship with client is necessary for firm growth, ICPAK members are required to comply with IFAC code of conduct to avoid threats to independence.

Threats fall into one or more of the following categories:

a) Self-interest: According to the Code, examples of circumstances that may create self-interest threats for a professional accountant in business include, but are not limited to:
   - Financial interests, loans or guarantees.
   - Incentive compensation arrangements.
   - Inappropriate personal use of corporate assets.
   - Concern over employment security.
   - Commercial pressure from outside the employing organization.

b) Self-review: These include business decisions or data being subject to review and justification by the same professional accountant in business responsible for making those decisions or preparing that data.

c) Advocacy: When furthering the legitimate goals and objectives of their employing organizations professional accountants in business may promote the organization's position, provided any statements made are neither false nor misleading. Such actions generally would not create an advocacy threat.

d) Familiarity: Examples of circumstances that may create familiarity threats include, but are not limited to:

- A professional accountant in business in a position to influence financial or non- financial reporting or business decisions having an immediate or close family member who is in a position to benefit from that influence.
- Long association with business contacts influencing business decisions.
- Acceptance of a gift or preferential treatment, unless the value is clearly insignificant.

(e) Intimidation: Examples of circumstances that may create intimidation threats include, but are not limited to:

- Threat of dismissal or replacement of the professional accountant in business or a close or immediate family member over a disagreement about the application of an accounting principle or the way in which financial information is to be reported.
- A dominant personality attempting to influence the decision-making process, for example with regard to the awarding.

The ICPAK Code of conduct section 290 TO 291 requires auditors to maintain independence in the following:

- Independence of Mind- The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.
- Independence in Appearance- The avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit team's, integrity, objectivity or professional skepticism has been compromised.

**Other safe guards to overcoming challenges**

Long Association

- To avoid familiarity threat attributed with long association with the client, the firm should have rotation for clients (rotation of the firm and the people within the firm/ engagement partners and key team members) in accordance with the relevant statutes and regulations

- Always comply with the client's regulators on auditor appointment and rotation
- Ensure that engagement team members are independent.
- Mandatory auditor rotation / formal hand-over)
- Exit and separation of clients

ICPAK members are required to comply with IESBA Code of conduct section 290 to avoid the following actions that compromise independence;

- Financial Interests
- Loans and Guarantees
- Business Relationships
- Family and Personal Relationships
- Employment with an Audit Client
- Temporary Staff Assignments
- Recent Service with an Audit Client
- Serving as a Director or Officer of an Audit Client
- Holding of client's assets
- Long Association of Senior Personnel (Including Partner Rotation) with an Audit Client
- Provision of Non-Assurance Services to an Audit Client

**FEES**

How do firms deal with clients calling for a fee cut – cost assignment based on input

**What client considers when choosing an audit firm**

- Fees
- Business Specialties
- Certification
- Advice
- Level of Service
- Depending on the services that are availability
- Personal Connection
- Goal Setting
- Audit Support
- References

**What firm should do?**

- Demonstrate knowledge and experience specific to client
- Provide reasonable fee
- Equip staff with right tools to perform work
- Deliver efficient and quick service integrate technology


RESPONDING TO NON-COMPLIANCE WITH LAWS AND REGULATIONS
IESBA
International Ethics Standards Board for Accountants®

## Notes

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# STAFFING AND HUMAN RESOURCE

## AN OVERVIEW OF STAFFING IN AUDIT FIRM

Attracting and retaining qualified staffs has been a big snag for firms however big or small they are. Firms have tried several strategies ranging from instituting graduate programmes meant to tap highly talented students, giving competitive rewards.

This issue is worsened by the fact that pattern of audit work is not spread evenly. For example, in Kenya a large proportion of companies have 31 December year-ends whose audits tend to take place in the first half of the year, as a consequence, the latter part of the year is a quiet period for audit firms. This may be compensated by the ability to use staff interchangeably on audit and non-audit engagements, although this may be limited by the requirement for specialized skills for non-audit engagements.

## STRATEGIES USED BY FIRMS TO ATTRACT AND RETAIN THE RIGHT STAFF

### (a) Recruitment

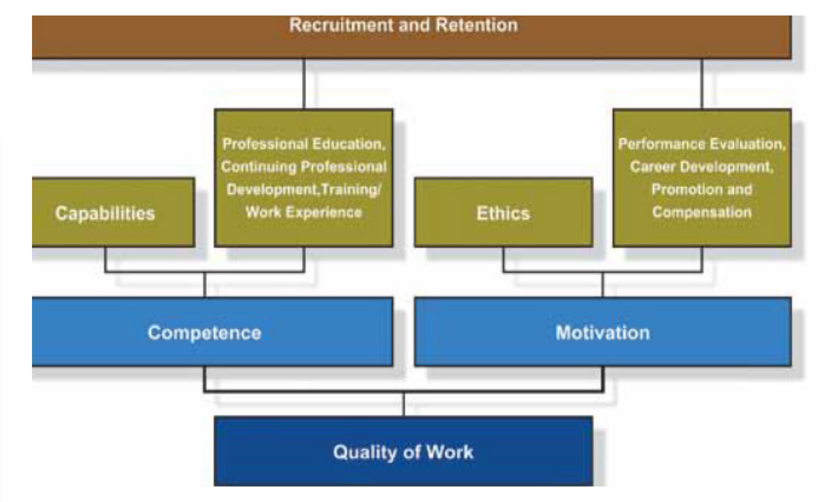
Apart from the traditional sources of recruitment, such as advertisement and the use of job portals, CPA firms can register on job websites as employers. This can help in attracting the best talent in the market and also enhance visibility of the firm. the firm should have a detailed effective training program to enable them recruit and retain qualified personnel.

Practical Experience framework and role of ICPAK

### (b) Documentation and employee records

It is best practice for a firm to maintain up to date employment records of its employees. Some of the vital records include- leave management records, attendance records, salaries and bills among others. Records can help assess other key aspect of human resources such as career progression and succession planning.

In this digital age, some firms can go further by creating a HR portal that can be of help in implementing biometric system especially on attendance, employees can track their salaries in the system. It can also help in tracking the number of approved leave days and holidays among others.




### (c) Planning and Job Allocation

It is of utmost importance that the right staff is assigned the right job. This will increase staff productivity and efficiency at work. Engagement allocation should be based on the competency, qualifications, knowledge and experience so as to ensure work of less experienced staff if reviewed by qualified staff.

### (d) Discussions and Training

For better understating of their duties and responsibilities, regular and timely meetings should be held to update staff of new happenings, get feedback on progress and opinions from them. The firm should periodically organize training sessions.

### (e) Continuous Professional Development

IES 7 states that firms should ensure that a continuous professional Development program is implemented so as to ensure that the staff have relevant competency to perform the audit work as required by IES8.

### (f) Assignment of engagement teams

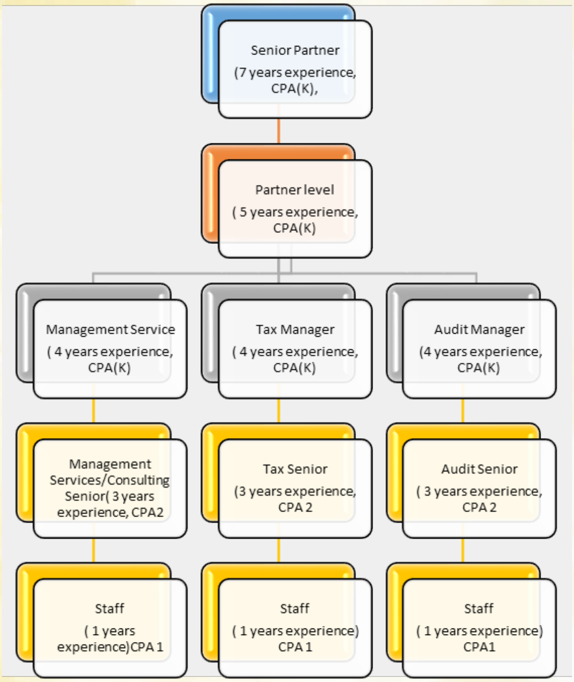
The firm should ensure the assignment of appropriate employees to the various engagements. ISA 220.14 states that the engagement partner should ensure that individuals assigned and the engagement team as a whole, have the necessary competencies to complete the engagement in accordance to the professional standards. The roles of various engagement team members should be communicated clearly to the team members.

**Sample Staff Requirements/competency in a Firm**

Audit is a technical and skilled profession that requires a competent and skilled manpower. See table below for a review of the best practices across the globe and the requirement of IES5 on practical experience framework as well as ICPAK requirements. On average, a partner of the firm should have at least five years' practical experience.

| | No. of years of practical Experience before administered as member | Admitted as a partner |
|---|---|---|
| IES 5-Practical Experience Framework | 3 years | None |
| ICPAK | 3 years | 5 years |
| Hong Kong | None | 5 years |
| American Institute of CPAs | None | 8 years |

The organogram below outlines the



**(h) Rewarding staff**

The firm should ensure commitment to high quality within the firm through positive reinforcement and recognition of compliance, leadership, innovation, training, development and coachingon. Performance appraisals could be used as a way of obtaining feedback on performance. ISQC1 29-30.

**(i) Succession Planning in Audit Firms**

For purposes of continuity of the firm ICPAK by-laws require firm partners to plan on succession of the firm in case the partner/partners are incapacitated. Appointment of an interim manager at a firm's capacity or at the individual practitioner level, is recommended.

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# MERGERS AND ACQUISITIONS

A merger is viewed as the situation where two or more companies or firms combine to form one larger business entity. The firms are usually of the same size. An acquisition on the other hand, involves outright purchase or purchase of controlling shares of another company or firm. In this case, the one firm takes over another and clearly establishes itself as the new owner. From the legal point of view, the target firm ceases to exist.

**TYPES AND FORMS OF MERGERS AND ACQUISITIONS**

- Outright sale
- Merger
- Two Stage Deal
- Cull Out Sale

## TYPES AND FORMS OF MERGERS AND ACQUISITIONS

The following types of deals make up the majority in current practice of mergers and acquisitions:

- Outright sale
- Merger
- Two stage deal and
- Cull Out Sale

In an *outright sale,* the owner of the firm being acquired normally turns over the practice to the buyer immediately and stays involved for a short period of time only to help in the transition. In some cases, the owner might be employed in the role of an experienced staff or non-equity partner. The buy-out payments for the practice normally start immediately.

Normally in a *merger*, an exchange of the equity interests in one firm occurs for the equity of the other firm or a newly combined firm. Most often, the partners of both firms become partners in the newly combined firm. The buy-out of equity is often handled through buy-sell agreements or partnership agreements that are designed to provide retirement benefits.

A *Two Stage* Deal is a technique that uses features of both a buy-out and a merger to address the unique needs of both parties in a specific situation. In a Two Stage Deal, the owner of the firm seeking succession remains in control of the clients and continues to work with the clients' full time or near full time for an agreed upon time frame. The owner's compensation is maintained at historical levels as long as the client base remains intact and the acquiring firm doesn't incur additional costs to provide back up and support. Then, at the earlier of the owner's discretion or at an agreed upon date (normally five or fewer years) the owner leaves or slows down to a part time role and the buy-out commences on terms that were agreed to at the beginning of the affiliation. Due the demographic issues many multiple partner firms face; it is not unusual for firms to have partners that are primarily interested in being bought out now or in a few years while other partners seek to extend their careers for a longer period or even indefinitely. A popular technique in these situations is to design a Two Stage Deal type of transition for the partners seeking near term succession and a merger type of transition for the other partners.

A cull-out sale involves segmenting a portion of the practice and selling it off. Examples are certain services, groups of clients, or an office. Normally, the sale is designed as an outright sale because the seller desires to cease providing services to a portion of the practice.

## WHY FIRMS MERGE OR ENGAGE IN ACQUISITIONS

Several factors in the accounting profession are behind the drive towards mergers and acquisitions. These include,

*a) Increasing staffing requirements:* The Audit environment is a highly contingent one. Auditors have to adapt to new physical locations and travel arrangements, different clients with associated different personnel and accounting systems including the tight audit deadlines. In addition, the pattern of audit work is not evenly distributed; in Kenya, most companies have their financial year ending December 31, meaning most audit work is conducted in the first half of the year with the rest of the year characterised as low season for audit work. Hence, smaller practitioners seeking a sale of their practice or an upward merger are sometimes driven to do so by an inability to attract the staff required to maintain their client base, or a fear they will face that problem in the near future. Larger firms often seek a merger or acquisition looking for quality staff, particularly at the partner and near partner levels. These factors make economic sense to seek for a merger and or acquisition.

*b) Practice Development:* The level of competition both within and outside the profession can be daunting. Practice development efforts can be expensive, time consuming and many practitioners

**ADVANTAGES OF MERGERS**

- Help eliminate redundancies thus increasing efficiency
- Leads to diversification and reduction of risks
- Ability to take advantage of additional clientele, products and services.
- Helps firms acquire existing technologies and business processes, which would otherwise be extremely expensive to develop as an individual firm.
- Brings about a broad skills mix through accessing talented managers and employees without the need to engage in an extensive search and hiring process.
- It increases fund raising ability thus ensuring larger pool of resources for optimal performance of the firm
- It encourages geographical spread.
- It gives the firm the muscle to take on bigger engagements

**DISADVANTAGES**

- Friction may arise between management of firms due to greed to maintain power.
- Possible clash of corporate culture between firms or the different cultures may take time to shed off to match the new entity culture
- Apprehension among employees of the firms. These employees may feel that their jobs may be in jeopardy during a consolidation (and their concerns may even be warranted)
- Dissenting staff from the bigger firm may work against the merger to protect their job
- Discomfort with share allocation, decision making and profit sharing

do not relish the prospects of spending a significant amount of their time growing their practice one client at a time. A merger or acquisition can lead to adding hundreds of clients all at once and much quicker growth. Smaller firms sometimes fear losing a portion of their client base to competition and seek a merger to alleviate this risk. Examples are firms that have concentrations of clients in certain industries like medical services or that have one or two clients that make up a significant portion of the practice.

*c) Quest for Firm Growth and Expansion:* The quest for growth can be achieved internally or externally. Internal growth may however take time to bear fruits as compared to external growth. Most of the big corporates at some point may have merged and then acquired other smaller entities. This is preferred because of the following:

- Firms want diversification to reduce risks
- A firm expects synergetic effect by merging with another
- A merger permits small firms to obtain superior management talent and or research capability
- The good will of a large firm is usually more acceptable than that of a small firm.
  This is a marketing strength to the firm.
- It is easier to finance a merger than to finance internal expansion.

d) Succession Planning: In other cases, firms merge to achieve succession and provide for the retirement of their owners.

There are several advantages highlighted for firms to merge including increase in efficiency, reduction of risk exposures and increase in financial muscle among others. Equally, merging of firms has had various disadvantages including management frictions and culture shifts between organizations, apprehension among employees among others listed in fig., This notwithstanding, with a good strategy and plan, the advantages of firms merging have outweighed the disadvantages.

**WHAT MAKES A FIRM MOST ATTRACTIVE TO A MERGER PARTNER (+VEs)**

- Reasonable profitability
- Talented people
- Partners who leverage and delegate
- Industry and/or service specialties Clients that will stay; age of clients
- Partners who will work for several years and not retire immediately after the merger.
- Special expertise that your firm could use
- A client base that is more business-oriented
- Firms use the same software
- Growth potential
- Willingness to accept change of leadership

**WHAT MAKES A FIRM MOST NON-ATTRACTIVE TO A MERGER PARTNER (-VEs)**

- Partners who want to retain full control
- Incompatibility of work ethic
- Dependence upon one huge client
- Unproductive/weak partners
- One firm's work standards far below other's;
- Poor or non-existent timekeeping
- Partners looking to sell out and leave without proper transition time
- Sloppy practice; office a mess, work goes out late, high levels of Work in Progress
- Low realization
- Poor malpractice history/exposure
- Obsolete technologies, attitude toward technology as well as the current hardware/software
- Unrealistic buyout expectations
- Ridiculous perks; excessive personal

Thus, on or before firms' merge, it is advisable for either party to conduct due diligence in the following areas:

- Operational policies and guideline
- Membership status with the Institute
- Operation structure of the firm(s)
- Human resource capital requirements
- Legal standing of the firm(s)
- Financial strength and obligations
- Nature of clients and risk portfolio

**Other Issues to Consider**

In addition to the due diligence measures above, a Practitioner should conduct a self-assessment and carefully consider the following questions.

**Table 1: Self-Assessment Questionnaire for those considering Partnership, Consolidations or merger**

| No | Question | Response / Comment |
|---|---|---|
| 1. | Do I really want to share decision making, control and profits with other people? | |
| 2. | What am I really getting myself involved in? | |
| 3. | Do I want to share ownership of the Firm? | |
| 4. | Does the upside of the shared ownership outway the downside? | |
| 5. | Can I trust my partners? | |
| 6. | Will they work as hard as I do? | |
| 7. | How much money will I make? | |
| 8. | Will I make more in the new structure, or less? | |
| 9. | What are the key reasons I am doing this? | |
| 10. | Have I considered the Advantages and Disadvantages of each option? What are they? | |

## RECOMMENDATIONS FOR REQUIREMENTS FOR MERGERS

For mergers to bear fruit, consider a binding agreement that will cover the details in the checklist below:

| # | Matter of Consideration | Response Date/ Timeline |
|---|---|---|
| 1. | Signing of confidentiality agreement | |
| 2. | New entity structure | |
| 3. | Management, dispute resolution, exit provisions, valuations formula and capital investment | |
| 4. | Services to be provided | |
| 5. | Decision making process | |
| 6. | Process for deciding on the management partner | |
| 7. | Develop partnership / shareholder’s agreement | |
| 8. | Partners remuneration | |
| 9. | Partners access to profits | |
| 10. | Charge out rates | |

| # | Matter of Consideration | Response Date/ Timeline |
|---|---|---|
| 11. | Target client profile | |
| 12. | Process for any existing client outside of the new client profile | |
| 13. | Period allowed and scope of due diligence on each other firms | |
| 14. | Valuation of each firms' interest at time of initial merger | |
| 15. | Valuation formula and process on partner exit | |
| 16. | Location and number of offices to be maintained | |
| 17. | Assess of office and office storage requirements | |
| 18. | Valuation of each firm's interest at time of initial merger | |
| 19. | Organization chart, partner responsibilities and staff structure | |
| 20. | Quality control, systems and procedures to be used | |
| 21. | Computer hardware and software platforms to be used and | |
| | firm database management | |
| 22. | Employment term for all staff and review of salary levels for equality | |
| 23. | Staff redundancies | |
| 24. | Working capital requirements and funding for the firm | |
| 25. | Firms bankers | |
| 26. | Firms lawyers | |
| 27. | Professional indemnity insurer and level of coverage required | |
| 28. | Firms name and logo | |
| 29. | Access to historic information on client base, fees by clients, and fees by service range for due diligence purposes | |
| 30. | Treatment of existing creditors and debtors | |
| 31. | Completion of work in progress and billing | |
| 32. | Commencement of drafting merger agreement or partner agreement | |
| 33. | Professional bodies to be advised on new entity and new registration | |
| 34. | Merger plan and timetable | |
| 35. | Merger compliance with the relevant statutes | |

**Notes**

# THE ROLE OF THE INSTITUTE IN MERGER & DEMERGER OF FIRMS

The Institute as a regulator of the profession is a key player in the merger and acquisitions of the accountancy firms. The Institute, in order to have an orderly and sustainable growth of the accountancy firms, is desirous that the firms begin with networking and then matures to mergers through a firm growth model. This is because networking enables the firms to develop working relationships with each other over time and avoid the pitfalls that are associated with most mergers. However, it is not to suggest that there cannot be mergers without networking.

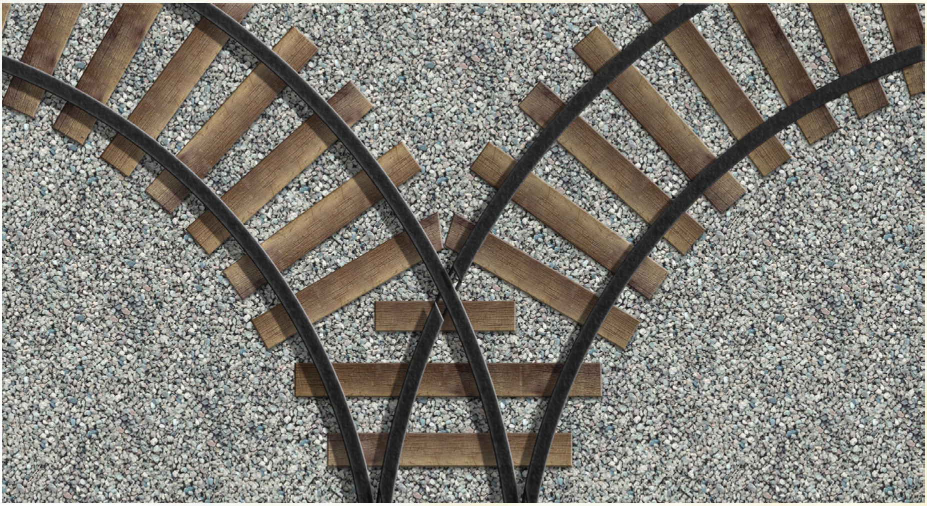
The mergers should be effected to develop core competencies and to render professional services of a larger range spread over bigger geographical area.

## THE ROLE OF THE INSTITUTE IN A MERGER

- To effect merger, a form as shall be outlined by ICPAK shall be completed and filed with the Institute within 30 days from the date of the agreement. The re-constitution agreement/partnership deed shall be filed with the registrar of companies as stipulated by the Companies Act 2015.
- Upon the merger of the firms, the Institute will freeze the names of the merging firms and shall not allow their separate practice.

## THE ROLE OF THE INSTITUTE IN A DEMERGER

- The merger has to precede the demerger. The merger agreement itself shall contain the terms and conditions for demerger. Therefore, no concurrence/ acceptance is required from the continuing partners. The merger agreement shall stipulate that in case 75% or more of the continuing partners of one of the erstwhile firm(s) are willing to demerge then they can do so after giving due notice in a form as prescribed by the Institute to the other partners and to the Institute.
- In case 75% or more of the continuing partners of one of the erstwhile merging firm have demerged after giving due notice to the other partners, then in such case, the merger shall come to an end and if the remaining erstwhile merging firms/partners of the erstwhile merged firm decided to continue, then they should enter into a fresh Merger/ Partnership Agreement.
- The Demerged Firm is entitled to practice in its old trade name, which existed at the time of merger.
- The practice certificate issued by the Institute to the demerged firm shall state the original date of establishment, the date of its merger and the date of the demerger. For the purpose of computing the seniority of the firm, the total period will be reckoned from the original date of establishment.
- The demerger cannot be done before 5 years are up from the date of merger.



**Notes**

# REVENUE AND COST MANAGEMENT

Revenue management is the process of enhancing a firm's revenues through the management of operational overheads. This process can also result in stabilizing a firm's cash flow throughout business cycles. It is therefore essential for firms to apply various tools and techniques to accurately forecast future cash flow needs.

Proper revenue management relies on accurate record keeping. This therefore implies that firms need to invest in appropriate financial tools to monitor their periodic records of incomes and expenses.

**Revenue Generation**

A firm's financial sustainability relies on reliable and consistent cash inflows, otherwise called revenue. Firm revenues are generated through fees charged for professional services, therefore a firm should explore innovative avenues generate continuous revenues. This can include but are not limited to:

1. Bidding:
The bidding process requires adequate capacity in proposal preparation, submission and follow up to improve a firm's likelihood of award. Where firms have limited resources to engage on the bidding process, firms should consider engaging in partnerships to amalgamate their resources and strengthen their capacity to deliver.

2. Diversification of professional services for assurance and non-assurance:
To steady cashflows it is paramount for firms to engage in other non-assurance services such as tax consultancy, forensic audit, payroll management and bookkeeping.

3. Networking and referrals
This gives firms a good opportunity for interact with new and potential clients whenever they meet in forums and events. It is important for firm partners and employees to have business cards with them always. Firm profile and interactive websites are also a good avenue. Firm domain names provide professional image for the firm.

4. Sourcing for new business and clients
Firms can consider advertising their services in professional accountancy publications and other media as guided by the Institutes guideline on acceptable advertising.

5. Maintaining existing clients
Client mobility is influenced by the quality of services provided as well as charging appropriate fees for services rendered. Firms should therefore endeavor to build long term business relationships with their clients.

**Recording of Revenue**
Firms should embrace a good system for recording all their revenues and keeping track of client payments. Follow up of on delayed payments can be done where there is a means of tracking receipts by clients. Proper recording enables the costing of jobs to be done comparing revenue vis a vi the input expended on a job.

## CONSIDERATIONS IN CHARGING FEES FOR AUDIT AND NON-AUDIT ENGAGEMENTS:

At the point of bidding the engagement partner should demonstrate proper understanding of what the job entails i.e. technical aspects, scope of the work should be well stipulated and defined from the onset.

Various factors can be considered when determining the audit fees to be charged i.e. time to be spent in the engagement, skills and experience of the team, complexity and nature of the engagement, internal control environment of the client, size and composition of the engagement team, establish and agree on the charge out rate for each member of the team.

The following are some of the factors that a firm would need to consider when determining the charge rate for professional services.

## COMPLIANCE WITH CODE OF ETHICS

The IESBA Code of Ethics for professional accountants recommends that when entering into negotiations regarding professional services, a professional accountant in public practice may quote whatever fee is deemed appropriate. The fact that one professional accountant in public practice may quote a fee lower than another is not in itself unethical. Nevertheless, there may be threats to compliance with the fundamental principles arising from the level of fees quoted. For example, a self-interest threat to professional competence and due care is created if the fee quoted is so low that it may be difficult to perform the engagement in accordance with applicable technical and professional standards for that price (IFAC, 2016).

The existence and significance of any threats created will depend on factors such as the level of fee quoted and the services to which it applies. The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level.

Examples of such safeguards include:

- Making the client aware of the terms of the engagement and the basis on which fees are charged and which services are covered by the quoted fee.
- Assigning appropriate time and qualified staff to the task.

## TIME SPENT ON THE AUDIT AND VALUE DERIVED BY THE CLIENT FROM THE SERVICE

There are two bases for computation of fee, namely time-based and value-based.

### Time-based approach

Time based billing has been very useful in assisting the practitioners in charging the clients. This involves the use of timesheets to monitor chargeable hours. However, this method of computing professional fee has its flaws, namely:

- Arbitrary fixing of charge-out rate; the erroneous recording of time sheets and the provision of non-assurance advice given in the course of providing the assurance service.
- The differences in fixing charge-out rate between practitioners give rise to accusation of 'fee under-cutting'.
- Fixing of artificially low charge-out rates and erroneous time sheet results in under valuing professional fees being billed to the clients.
- Time-based billing pre-supposes all information and knowledge is of equal value to all clients.
- It also discounts the value of research needed to satisfactorily discharge an assignment and the knowledge accumulated by the firm.

As an alternative to time-based billing, practitioners can also consider value-based billing.

### Value-based Principle

The computation of an appropriate fee for services involves value judgment. It should consider the value of advice rendered by the practitioner and the benefit, tangible and intangible, derived by the client.

Value-based billing takes cognizance of the knowledge and skills that a practitioner brings to bear on the assignment and the professional judgment that he is called upon to make.

In applying value-based billing, a practitioner must uncover the value drivers of his service. Value drivers are those elements that assist the practitioner in satisfactorily and professionally discharging his


professional obligation. Generally, express and inferred knowledge, information technology hardware, quality of internal processes and others can and are the drivers of value.

During his professional work, the practitioner should and must impress upon his client the 'value' that is being 'delivered' and the 'value-drivers' that have been brought to bear in satisfying the client's objective.

## COST MANAGEMENT

The firm cost can be classified into two:

- Professional cost-staff costs for both audit and non-assurance costs
- Non-Professional costs comprising administrative expenses and operational costs

The partner/firm should keep records of the direct costs incurred in the execution process of the audit and monitor the time spent on the assignment against budgeted costs to determine the variance.

The partner/firm should also strive to maintain separate fund accounts for the assurance and non-assurance services so that there is a clear demarcation of revenue generated from audit and non-audit assurance. Bills are to be sent out promptly for the component of work that has been delivered and an aging analysis on pending bills maintained.

Any assignment outside the earlier agreed scope of work should be underpinned on a separate agreement and billed separately.

**Notes**

## Notes

## WORK FLOW MANAGEMENT

Workflow management system provides an infrastructure for the setup, performance and monitoring of a defined sequence of tasks arranged as a workflow application from the initial point through the process to final stage. It helps the firm take control of the routine processes and help in better management.

Objectives of Good Work Flow Management Scheme

a) Allows automation on repetitive business processes
b) Automatically follow up on uncompleted tasks in the process
c) Gives an overall picture of the workflow along with performance metrics
d) Maintenance of client details
e) Track teams involved in engagements and work assignments to relevant resources
f) Share files within the teams assigned to execute the work.

The following chart illustrates a sample audit process work flow

**Figure 1: Sample audit process work flow**

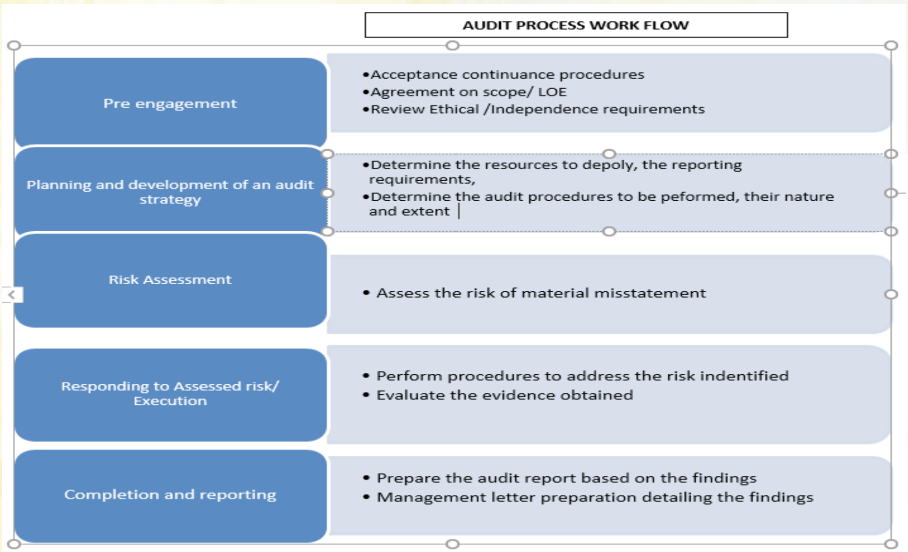
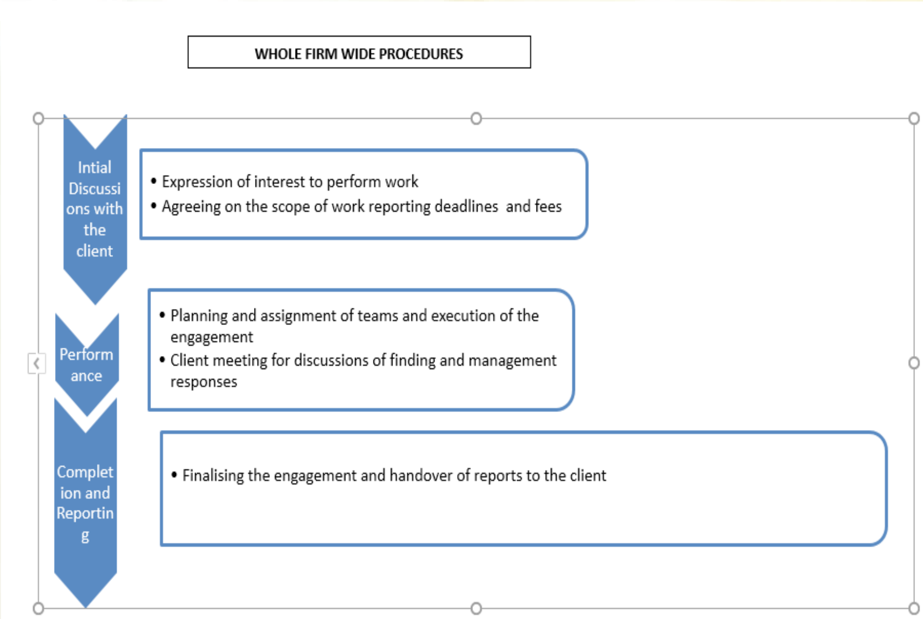


**Figure 2: Whole Firm-wide procedures and processes**



## Notes

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## DOCUMENTATION AND AUDIT EVIDENCE

ISA 230 requires an auditor to prepare audit documentation that is sufficient and appropriate to support the basis for the Auditor's report. It further requires the Auditor to confirm that the audit process was planned and performed in accordance to ISAs and applicable legal and regulatory requirements. Where a professional accountant is offering accounting services he/she should ensure that the accounts are prepared in accordance with the required reporting framework (IFRS, IFRS for SME, IPSAS, IAS, ISSAI) (IFAC, Handbook of International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements, 2015).

As per ISA 230 Audit documentation serves several purposes, including the following: -

a) Assisting the engagement team to plan and perform the audit.
b) Assisting members of the engagement team responsible for supervision to direct and supervise the audit work, and to discharge the review responsibilitiesin accordance with ISA 220.2
c) Enabling the engagement team to be accountable for its work.
d) Retaining a record of matters of continuing significance to future audits.
e) Enabling the conduct of quality control reviews and inspections

in accordance with ISQC1 or national requirements that are at least as demanding.

f) Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.

**GOOD DOCUMENTATION PRACTICE REQUIRES CONSIDERATION OF ASPECTS OUTLINED BELOW:**

**CLIENT FILE: MANAGEMENT AND RETENTION**

For audits that are recurring or continuing there are two types of audit files that are maintained: -

- Permanent file
- Current file/Working file

**PERMANENT FILE**

The permanent file contains the following:

- Professional clearance letter and response from the outgoing auditor
- Copy of resolutions for re appointment of the auditor
- The Engagement letter
- Copies of previous years audited financial statements
- Statutory information about the firm
- Client company background and history
- Client company's certificate of incorporation/registration
- Memorandum and Articles of Association


## CURRENT FILE/WORKING PAPERS

The current Audit file is mainly made up of the Auditor working papers which contains the following: -

- Correspondence relating to acceptance of annual reappointment.
- Extracts of important matters in the minutes of Board Meetings and General Meetings as relevant to audit.
- Evidence of the planning process of the audit and audit programme
- Analysis of transactions and balances
- A record of the nature, timing and extent of auditing procedures performed, and the results of such procedures.
- Evidence that the work performed by assistants was supervised and reviewed by the partner
- Copies of communication with other auditors, experts and other third parties (creditors, debtors).
- Letters of representation or confirmation received from the client and copies of any other evidence collected.
- Conclusions reached by the auditor concerning significant aspects of

the audit, including the way exceptions and unusual matters, if any, disclosed by the auditor's procedures were resolved or treated.

- Copies of the financial information being reported on and the related audit reports.

## FEATURES OF GOOD WORKING PAPERS

The working papers should clearly identify the audit objective, procedures and the assertions being tested. The various assertions that may be used are as below: -

**a) Assertions under classes of transactions and events for the period being audited;**

- Occurrence: The transactions and events that have been recorded have occurred and pertain to the entity
- Completeness: Every transaction that should have been recorded has been recorded
- Accuracy: The amounts and other information are correctly recorded
- Cutoff: The transactions and events have been recorded in the right /correct accounting period
- Classification: To ensure that items are properly classified and adequate disclosure is given

**b) Assertions about Account balances at period end**

- Existence: To test the existence of assets, liabilities and that they are in physical existence
- Rights and obligations: Confirming that the entity holds and controls the assets and liabilities
- Completeness: Confirming That all assets, liabilities that were to be recorded were recorded
- Valuation and allocation: That the assets and liabilities are properly valued

**c) Assertions Regarding Presentation and disclosure**

- Occurrence: This means that transactions and events took place
- Rights and obligations: Confirming that the company has a right to its assets and owns them Completeness: That all transactions have been recorded in the financial statements
- Classification and understandability: This means that Items are properly classified and disclosure given
- Accuracy and valuation: Accuracy means that amounts and other data relating to transactions and events have been recorded at the correct amounts – ie at the amounts appearing in the source documents
- The period should be clearly stated 'Year or period ended'

**Other Important Requirements**

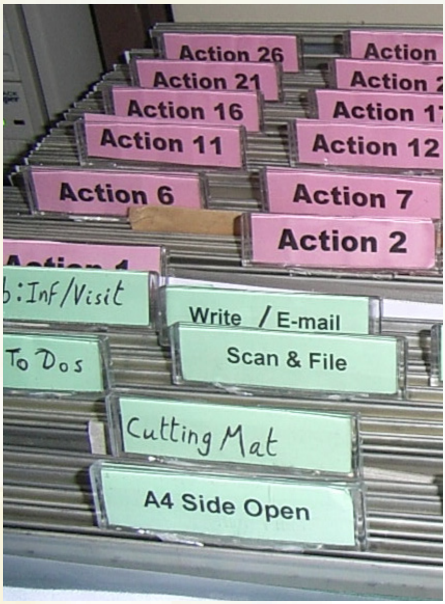
- Extent of tests or procedures carried out for example how many items were tested and how was the number for testing determined (materiality, random etc.)

- Proper and clear referencing where evidence is presented in another working paper. For example, circularization was done for so and so debtors and the confirmation received from the debtor is in working paper.
- The working paper should clearly and objectively state the results of the tests conducted.
- The conclusions arrived at after the audit procedures should also be disclosed and need to be consistent with the findings of the test carried out.
- The working paper should be signed by the person who prepared them and be dated.
- The reviewer of the work should also sign and date the work (The reviewer should not sign before the preparer because the latter is meant to review the work done and give comments and draw conclusions

## FORMS OF FILING

Documents should be filed in a secure place that is accessible which can either be manually or automated (electronic). Filing can be both physical or electronic as elaborated below:

- Physical Filling - This is where physical hardcopy files are kept. They need to be kept in an orderly manner
- Electronic Filing – These are in the form of soft and can be stored in cloud storage and should be secured.



## CLIENT FILE RETENTION

Once the Audit assignment is completed the Auditor is required to retain files for some length of time. ISQC1 58 'The firm shall establish policies and procedures that require retention of documentation for a period sufficient to permit those performing monitoring procedures to evaluate the firm's compliance with its system of quality control, or for a longer period if required by law or regulation'

File retention can be in two forms: -
a) Returning files to the Audit client
b) Retaining files for a given duration after the audit is completed as required by ISAs or national laws (KRA and Companies Act).

- **KRA –** The Tax Procedures Act 2015 provides the retention period of records for tax purposes to be 7 years from the end of the reporting period to which it relates to unless a shorter period is specified in a tax law.
- **Kenya Companies Act-** Accounting records retention for a period of 7 years
- **ISAs-**ISA 230.15 After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period. ISQC 1 requires firms to establish policies and procedures for the retention of engagement documentation. The retention period for audit engagements ordinarily is no shorter than five years from the date of the auditor's report, or, if later, the date of the group auditor's report'' (IFAC, Handbook of International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements, 2015)

The files should be retained for the maximum period to to comply with the requirements and allow for any legal proceedings that may arise. This implies that the firm should be careful to review the enabling statutes and adhere to the relevant document retention provisions.

**Confidentiality of the Working Papers**
The Audit firm has an ethical responsibility to ensure confidentiality of the client documents and information and can only be shared when there are legal proceedings required by law.

**Audit Quality Review by the Institute**
The Audit Quality Review process is carried out by the ICPAK in compliance with the IFAC SMO 1 (Quality Assurance). The review is based on two approaches compliance at the engagement level and at the firm level to see whether the entity has a firm management guide or quality control manual in place and if the audit procedures are in line with ISA's requirement. Audit quality reviews are aimed at ensuring that the firm complies with the requirement of the profession as required by the professional standards.

## Notes

## Notes

## AUDIT TECHNIQUES AND TOOLS


The Audit landscape has changed considerably in the current years where we had auditors performing analysis of transactions manually on working papers using pencils and green pens into analyzing increasingly complex and voluminous data using modern techniques. With the increasing cases of corporate failure, there has been increased regulation where the auditor is being required to report on various matters that were not previously required.

These changes necessitate that auditors adopt new ways of performing their work to incorporate these changes in technology and environment. ISA 300 states that in establishing the overall audit strategy the auditor considers the availability of data and Computer Assisted Audit Techniques (CAATs).

CAATs can be defined as the use of technology to assist in the completion of an audit. This (broad) definition would include automated working papers and traditional word processing applications or the use of certain software.

### WHAT TO EXPECT FROM A GOOD AUDIT SOFTWARE?

As a minimum, audit software should have the following qualities:

- Be in-built with accounting standards
- Should conform and facilitate audit planning and clear work-flow management
- Should enable analysis and generation of reports
- Ease of document filing and retrieval
- Should have enhanced security features to facilitate confidentiality
- Should facilitate reduction in paper documentation

## TO CONSIDER WHEN SELECTING A GOOD AUDIT SOFTWARE

When considering the type of software to acquire, the practitioner should ensure that the soft-ware is:

- User friendly
- Should be cost effective
- Secure and reliable
- Compliant with Accounting Standards (IFRS, ISAs, IASs, IPSAS, ISSAI) and other regulatory requirements
- Continuously updated with the changes in accounting standard and other regulations
- Flexible to accommodate specific user requirements like data analytics, risk assessment, number of users etc

## KEY AREAS WHERE AUTOMATION IS NEEDED

The following areas in the process of audit can be considered for automation:

- Pre-engagement and Client Acceptance
- In pre-engagement and client acceptance the following can be automated; the correspondence on engagement letter, independent assessment and previous auditor clearance for new clients Planning in planning, the determination of materiality, risk assessment, role assignment and work-flow management, audit procedures to be performed can be automated
- Performing Audit Procedures and documenting: at this stage, evidence and results of procedures performed can be automated and file compiled.
- Audit Reporting – Here, the analysis of the final financial statements, client response and comments, audit opinion and sign-off details may be automated.

Skeptism and judgement are key and crucial in the audit process even with the introduction of audit software. The auditors and accountants' judgement remain relevant. The auditor needs to keep up to date with new developments in the audit and accounting field to remain relevant and acquire clients. The value of data analytics facilitated by the software lies in the quality of analyses and judgments thereby facilitated, in the audit evidence extracted from the conversations and enquiries that the analytics generates.

**Notes**

## Notes

# AUDIT PROGRAMMES FOR SMES, PUBLIC LISTED COMPANIES, GENERAL PURPOSE AND REGULATED INSTITUITIONS

Practitioners and their audit firms are required to comply with appropriate professional standards and other regulatory requirements. These include;

i. The ICPAK Code of Ethics
ii. IFAC's Code of Ethics
iii. International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB)
iv. International Financial Reporting Standards Interpretations (IFRICs) developed by the International Financial Reporting Standards Interpretation Committee of the IASB
v. International Standards on Auditing (ISAs) and other engagement standards issued by International Auditing and Assurance Standards Board (IAASB)
vi. International Education Standards (IESs) issued by the International Accounting Education Standards Board of IFAC
vii. The Professional Code of Ethics issued by the Internationals Ethics Standards Board for Accountants (IESBA)
viii. Provisions of the Companies Act and other relevant Acts, (CMA Act, Banking Act, RBA Act, Insurance Act)

## Notes

## SELECTED REGULATORY FRAMEWORKS

The following regulatory frameworks are outlined in brief:

**SACCOs**

Regulators expect the cooperative societies to comply with set standards and expect high level of accountability. Examples of requirement under Sacco Societies Act, 2008 include:

a) Monthly returns (capital adequacy, liquidity, and deposits)
b) returns, financial performance)
c) Annual Quarterly returns (risk classification of assets and loan loss provisioning, investment returns (audited financial statements:
   - Have their financial statements audited three months after the end of each financial year.
   - Appoint external auditors through the general meeting from a list approved by SASRA and are to be changed or rotated after three years using a competitive bidding process.
   - Hold their annual general meeting within four months after the end of financial year.
   - Employ internal auditors to work with Audit Committee.
d) Report on any lending to insiders and credit advances exceeding limits of its core capital.
e) Make disclosures on individual shareholding exceeding 25% of core capital

**Accountability**

To enhance accountability, the Board of Directors should:

- Present a balanced and understandable assessment of the Cooperative's position and prospect in the financial statements which should comply with international standards on disclosure.
- Establish effective structures for communicating with the members.
- The Board should meet regularly. The number of Board and Board Committee meetings held in a year, as well as attendance of every Board member at the meetings should be disclosed in the annual report.
- Information to members should be sent early enough to allow time for deeper understanding to be able to have effective meetings and engagement with members.

## THE RETIREMENT BENEFITS AUTHORITY

Retirement Benefits Authority is the body mandated with the regulation, supervision and promotion of retirement benefits schemes, the development of the retirement benefits sector and any other connected purposes.

The Act under Part IV, regulation and supervision of retirement benefits schemes requires that retirement benefit schemes trustees shall within a period of three months after the end of each financial year, shall cause to be prepared in respect of the scheme fund:

a) a statement of assets and liabilities;
b) a statement of income and expenditure;
c) a statement of the assets and liabilities of the scheme as on the last day of that year;
d) such other documents as may be prescribed.

The accounts of the scheme fund in respect of each financial year shall be audited by an auditor appointed by the trustees with the approval of the Board if the appointed auditor shall not be a member, trustee or sponsor of the scheme.

The Act also under Section 42 requires the auditor among others to where an inspection of the scheme is being conducted by an inspector appointed by the authority

a) give to the inspector all reasonable assistance in connection with the inspection; or

b) appear before the inspector for examination concerning matters relevant to the inspection; or
c) produce any books or documents relating to the affairs of the scheme being inspected.

## INSURANCE INSTITUTIONS

The revised Insurance Act 2015 states that the Commissioner may, by notice in writing require a member of the insurance industry to supply him with information relating to his insurance business, the information if the notice so requires, may be certified also by an auditor.

Section 56 of the Insurance Act 2015 states that

1. The accounts of every insurer shall be audited annually by an auditor.
2. The auditor shall in a certificate relating to the accounts and statements in respect of a financial year of an insurer, state whether-

a) The accounts and statements to which it relates appear to him to be in accordance with the Act and give particulars of any matters that do not appear to be so in accordance;
b) The accounting records of the insurer in respect of that year appear to him to have been properly kept and to record and explain correctly the transactions and financial position of the insurer and give particulars of accounting records that appear to him not to have been so kept and of transactions that appear to him not to be so recorded;
c) In respect of that year, he has obtained the information and explanations that he requested and give particulars of information and explanations he requested but did not obtain;
d) He is satisfied that the accounts and statements referred to in paragraph (a) agree with the accounting records of the insurer and appear to him truly to represent the transactions and financial position of the insurer in respect of the financial year to which they relate and, if any of them appear to him to fail so to represent the transactions and financial position, give particulars of the failure;
e) Amounts required by section 53 to be apportioned have been equitably apportioned and if they have not been so apportioned give particulars of the failure;
f) All management expenses wherever incurred in respect of the insurer's business, whether directly or indirectly, have been fully debited in the revenue account or profit and loss account as expenses and, if they have not been so debited, give particulars of the amount not so debited;
g) Every reserve has been calculated in accordance with the method approved for the reserve by the Commissioner and, if they have not been so calculated, gives particulars of the reserves not so calculated.

Part 15 of the Act states that the client account of a broker shall be audited annually by an auditor qualified under section 161 of the Companies Act, who shall issue a certificate to the Commissioner certifying whether or not the account is managed in accordance with the provisions of the Act. The Act also provides for the establishment of a Policyholders' Compensation Fund which shall be managed and administered by a Board. Every insurer shall submit to the Board, in the prescribed form an annual return signed by its auditor showing the total annual contribution payable to the Board, within three months of the end of the financial year of the Board.

## BANKING INSTITUTIONS

When carrying out audit of Banks the Auditor shall check to see that the client complies with the Banking Act and CBK Prudential Guidelines and carry out procedures that will test if compliance has been done. Some of the key issues to be considered are: -

- Books of accounts will be prepared and kept in the required language
- The financial statements to be prepared in accordance with the appropriate reporting framework
- An auditor in conducting his work shall comply with the Banking Act, if not CBK may remove him from office
- Ensure that auditor appointment, re-appointment and resignation comply with the requirements of the Banking Act
- Board committee members and directors will be evaluated annually and this fact is to be disclosed in the annual report
- The key compensation for the directors will be disclosed in the annual report
- Proper Classification of loans is to be done in compliance with the CBK guideline and where an institution uses its own internal risk rating system there will be a proper process to map the internal rating to classification provided by Central Bank.
- When auditing write off for bank loans the auditor shall ensure that all credit policies and write-off procedures are adequately disclosed.

GENERAL PURPOSE ENTITIES For General purpose entities that are not subject to regulatory requirements, the auditor can refer to the model audit file for guidance.

The model file can be accessed at *https://www.icpak.com/resource/model-audit-file/*

## Notes

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**Notes**

## Notes

## QUOTES FOR CONSIDERATIONS

Our deepest fear is not that we are inadequate. Our deepest fear is that we are powerful beyond measure. It is our light, not our darkness, that most frightens us. We ask ourselves, Who am I to be brilliant, gorgeous, talented, fabulous? Actually, who are you not to be? … Your playing small doesn't serve the world. There is nothing enlightened about shrinking so that other people won't feel insecure around you. We are all meant to shine, as children do. We were born to make manifest theglory within us. It's not just in some of us; it is in everyone. And as we let our own light shine, we unconsciously give other people permission to do the same. As we're liberated from our own fear, our presence automatically liberates others.**– Marianne Williamson**

'The future is not some place we are going to but one we are creating. The paths are not to be found, but made, and the activity of making them changes both the maker and the destination.'
***– John Schaar***

When people get old and look back over their lives, what is important to them is not prestige or the amount of money in the bank, but whether or not they feel that their lives have been useful. If they have been able to contribute, even in some small way, to making it possible for people to live lives that are more satisfying to them than they might otherwise have been, that, it seems to me, is probably the most meaningful of all life's satisfactions.
***– John A. Hannah***

I have only to let myself go! … I am in full possession of accumulated resources – I have only to use them, to insist, to persist, to do something more – to do much more than I have done. The way to do it … is to strike as many notes, deep, full and rapid, as one can. All life is… in one's pocket. Go on, my boy, and strike hard…. Try everything, do everything, render everything – be an artist, be distinguished to the last.
***– Henry James***

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