

# Audit (ISA) Update and Refresher

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# Programme

- ▶ Summary of all significant recent developments
- ▶ Feedback and comment from regulatory bodies
- ▶ Audit quality management

# Summary of all recent significant developments

# Changes to the ISAs - International and UK versions

- ▶ ISA 570 - Going Concern
  - ▶ FRC issued ISA in September 2019
  - ▶ Effective for periods commencing on or after 15 December 2019
- ▶ ISA 540 - Auditing Accounting Estimates and Related Disclosures
  - ▶ FRC issued ISA in December 2018
  - ▶ Effective for periods commencing on or after 15 December 2019
- ▶ ISA 315 - Identifying and assessing risk of material misstatement through understanding of the entity and its environment
  - ▶ Revised ISA issued July 2020 effective for 31 December 2022 year ends
  - ▶ Major changes and increased specific requirements

# Changes to ISAs

- ▶ ISA 240 - Auditor's responsibility in respect of fraud
  - ▶ Applicable for accounting periods starting on or after 15 December 2021 - early adoption is possible
  - ▶ Enhanced duties and requirements
- ▶ ISA 700 - audit reports
  - ▶ Applicable for accounting periods starting on or after 15 December 2019
  - ▶ Increased requirements for all audits
- ▶ ISA 600 - group audits
  - ▶ Updated and aligned with ISA 315 methodology
  - ▶ For year ends commencing on or after 15 December 2023

# Poll questions

1. Do you think that SME companies are audited:
  1. In too much detail
  2. In not enough detail
  3. The ISA requirements are about right
2. What do you think is the biggest issue that auditors have to face, at the moment?
  1. Lack of resource
  2. Too much regulation and compliance
  3. Cost pressure
  4. Something else

# ISA 315 (revised) - key changes

- ▶ 5 inherent risk factors specified
- ▶ Risk spectrum now defined
- ▶ More focus on IT based controls and environment
- ▶ Obtain 'sufficient appropriate' evidence of risk assessment
- ▶ More work required on controls relevant to audit
- ▶ Distinguishes
  - ▶ Inherent and control risks
  - ▶ Direct and indirect controls
- ▶ 'Stand back' review of financial statement aspects considered insignificant
- ▶ Contains considerable example including for smaller entities (scalability)

# Other ISA 315 issues to consider

- ▶ Stand back review
  - ▶ How and when to perform?
  - ▶ How document?
- ▶ Work needed on IT controls - direct and indirect?
- ▶ Maximise opportunity to reduce audit work on areas where risk of misstatement is insignificant - following Stand back
- ▶ Do more and good luck



# Poll questions

1. Do you ever place reliance on controls when auditing an SME client?
  1. Yes
  2. No
  3. Sometimes but not often
2. Do any of your clients use spreadsheets as part of their accounting system?
  1. Yes - they all do
  2. Some of them
  3. None of them

# ISA 240 Auditor's responsibilities in respect of fraud

- ▶ ISA has enhanced the requirements
  - ▶ No change to legal responsibilities so the 'audit product' does not need to change?
- ▶ Issued in response to criticisms raised about the audit market
  - ▶ Government and other regulatory bodies
- ▶ Definition of fraud now includes reference to 'deception' and 'suspected fraud'
- ▶ Need to consider if documents are authentic

# Summary of key changes in ISA 240

- ▶ Greater focus on audit team discussion
  - ▶ Exchange of ideas
  - ▶ 360 degree challenge
  - ▶ Keep discussion ongoing throughout the audit
- ▶ Use forensic expertise as and when needed - do you need a forensic accountant?
- ▶ Client systems and controls - do they have provisions for whistle blowers? Who are the owner managers' eyes and ears?

# Poll question

- ▶ Who do you ask, to meet the requirement to ask management and ‘others within the entity’ about the possibility of fraud within the organisation as required by ISA 240?
  - ▶ The directors
  - ▶ The shareholders and others charged with governance
  - ▶ The finance director and controllers
  - ▶ Other - please state

# Summary of key changes in ISA 240 - continued

- ▶ Requirement to encourage professional scepticism in audit team
- ▶ Must set aside beliefs that management and those charged with governance are honest and have integrity
  - ▶ Have discussions assuming that they are crooks (almost)
- ▶ Challenge the validity of documents
- ▶ Keep in mind related parties

# Poll question

- ▶ How would you identify the related parties if you were auditing Red Bull Formula 1 Racing?
  - ▶ Credit rating or companies house search
  - ▶ Check minutes of company meetings and other similar documents
  - ▶ Other - please state

# ISA (UK) 600: Auditing Groups

- ▶ Revised ISA issued April 2022 following revisions to IAASB - effective for accounting periods starting on or after 15 December 2023.
- ▶ Key changes
  - ▶ Scope and applicability - ISA 600 will apply to branches, divisions and shared service centres
  - ▶ Proactive risk based approach - ISA 315 aligned, top down risk assessment
  - ▶ Definition of component - now based on significance to the audit and auditor not the management reporting processes
    - ▶ Component auditor now part of the group audit engagement team.
  - ▶ More detailed 2-way communication required throughout the team
  - ▶ Test the consolidation process - likely to be significant and high risk
  - ▶ Assess component materiality relevant to each separate component
  - ▶ Enhanced documentation requirements linked to ISA (UK) 230

# Audit file monitoring reports



# Summary of findings

- ▶ 71% of firms visited scored satisfactory or better (UK QAD)
  - ▶ Down slightly from year before
  - ▶ More firms reported to Audit Registration Committee
- ▶ 3 main areas for improvement
  - ▶ Evidence
  - ▶ Documentation; and
  - ▶ Identification and assessment of risk
- ▶ Specific comments on findings
  - ▶ Evidence = support conclusions
  - ▶ Documentation = explain complex information
  - ▶ Identification and assessment of risk - evidence to support key judgements made by management



# QAD - areas identified of most concern

- ▶ Group audits
  - ▶ Stock and long term contracts
  - ▶ Valuation especially property valuations
  - ▶ Revenue
- 
- ▶ None of these are new issues

# Poll questions - to illustrate file review findings

- ▶ If you are testing revenue for completeness where would you start your audit test?
  - ▶ Sales day book listing of invoices issued
  - ▶ Reported revenue in financial statements
  - ▶ Sales orders generated by the organisation
  - ▶ Cash receipts from customers
- ▶ How would you define your population for an audit test of 'journal' entries?
  - ▶ Every item listed as a journal entry in the accounting ledgers
  - ▶ Year end and month end 'adjustments'
  - ▶ All accounting entries between ledgers not generated by day book entries - cash, invoices etc.

# Further poll questions

- ▶ How would you audit impairment of inventory if there are no recent sales invoices?
  - ▶ Require full provision to scrap value - always
  - ▶ Physical inspection
  - ▶ Understand why business needs to hold 'old' stock and what constitutes 'old or slow-moving' to them
  - ▶ Check to relevant purchase invoice
- ▶ What steps would you take before you decided to rely on a property valuation provided by an external, independent value?
  - ▶ Their qualifications?
  - ▶ Their independence?
  - ▶ The scope of their work
  - ▶ The assumptions and data used in their calculations

# Quality management

# ISQM 1 - key changes

- ▶ Requires proactive quality management procedures and policies
- ▶ Design, implementation and operation of a QM system to manage engagement quality
- ▶ Key steps
  - ▶ Establish quality objectives
  - ▶ Design and implement responses to risks of meeting those objectives
- ▶ Guidance more detailed and prescriptive including use of Root Cause Analysis (RCA)

# ISQM 1 - step 1 Identify Quality Risks

- ▶ Relate back to ISQM or add
- ▶ Perform a review of existing engagements
  - ▶ Internal Hot File Reviews
  - ▶ QAD and other inspections
  - ▶ Additional and specific
- ▶ Identify appropriate responses to risks and
- ▶ Resources needed
  - ▶ Obtained? Developed? Used? Maintained? Allocated and Assigned

# QAD report on audit quality 2022/23

- ▶ Root cause analysis of reasons for poor quality audit work
- ▶ Same as in previous year
- ▶ Lack of knowledge regarding ISAs and UKGAAP
- ▶ Poorly designed audit tests
- ▶ Inadequate review of work by audit manager or partner
- ▶ Lack of sufficient resource - especially since the pandemic



# Quality management - throughout the year

- ▶ What is your firm's objective for the audit 'product' that you deliver?
  - ▶ Perfection
  - ▶ Meets basic statutory requirements
  - ▶ Something else?
- ▶ Is this objective shared and understood by everyone within your organisation?
  - ▶ Yes
  - ▶ No
- ▶ What key steps are needed to achieve this objective? Every time. Throughout the year.
  - ▶ Detailed fixed prescriptive procedures?
  - ▶ Training and development?
  - ▶ Appraisal and reward structures?
  - ▶ Resources needed?

Thank you and any questions?

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