



The Institute of
Chartered Accountants
of Pakistan

CA
PAKISTAN

REPORT 2016

QUALITY
ASSURANCE
BOARD

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Message from the Chairman

I take pleasure in presenting the report of the Quality Assurance Board (QAB) for the year 2016. The regulatory bodies play a pivotal role in promoting audit quality to increase public confidence in the audit process and in financial reporting.

I firmly believe that quality control plays a crucial role in enhancing users' confidence in the services provided by a chartered accountant firm. A robust system of quality control addresses quality control with respect to leadership responsibilities for quality within the firm, compliance with relevant ethical requirements, acceptance and continuance of client relationships and specific engagements, human resources engagement performance and monitoring.

The QAB with the assistance of Quality Assurance Department (QAD) has been continuously striving to improve quality of audit and assurance service in Pakistan.

This year marked the formation of Audit Oversight Board as an independent audit regulator with the collaboration of the Institute and Securities and Exchange Commission of Pakistan.

In order to reduce subjectivity, enhance transparency and to ensure that audit quality continuously improves, the QAB has developed criteria for assigning weightages to various observations noted during QCR which ultimately helped QAB to conclude overall rating of a firm.

The report provides an overview of the QCR program, QAB activities and a summary of the significant and or frequent observations noted during the period July 01, 2015 to June 30, 2016. In the interest of transparency and confidentiality, only aggregated data, trends and issues arising from the findings are being reported. Though the quality of audit has improved since the QCR program commenced, still there are areas of audit where firms require more serious attention.

I would like to extend my gratitude and appreciation to all those firms and their staff who cooperated with our reviewers throughout the QCR process. I also would like to thank all members of the QAB and QAD team without which it would not have been possible to run our quality control program effectively.

Sohail Hasan

Chairman

Quality Assurance Board

April 11, 2017

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1. Introduction

This Report provides an overview of the activities of the Quality Assurance Board (QAB) and Quality Assurance Department (QAD) of the Institute of Chartered Accountants of Pakistan (the Institute) for the year ended June 30, 2016.

Section 2 provides salient features of Audit Oversight Board established through an amendment to the Securities and Exchange Commission of Pakistan Act, 1997.

Section 3 recommends list of documents and records required for QCR

Section 4 highlights the reviews conducted during the period and an analysis of the audit engagements which were Satisfactory and those Unsatisfactory to assess the overall quality of the audit.

Section 5 of this Report provides a summary of the key observations noted during the review. The findings represent challenges faced by the audit firms in interpreting complex requirements of International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA).

It is important to ascertain that the information contained in this Report is not intended to set out how the firms should structure their audit working paper files, policies and practices, as there is no "one-size-fits-all" approach. Practicing members are encouraged to seek guidance from the observations summarized in the Report in the light of their facts and circumstances.

2. Formation of Audit Oversight Board

The Audit Oversight Board (AOB) has been established through amendments to the SECP Act, 1997 at the initiative of ICAP, SECP and other regulators and stakeholders.

Salient features of the Audit Oversight Board are as follows:

Members of AOB

AOB shall comprise seven members including its chairman. The members and the chairman of AOB shall be appointed by the Federal Government on the recommendation of the nominating committee.

Functions of AOB

- To register and deregister audit firms that intend to audit accounts of public-interest companies and carry out oversight and review of the quality assurance board.
- To ensure that the auditing standards adopted by the Institute conform to the international standards as issued by International Auditing and Assurance Board.
- To conduct inspections and inquiries.

Registration and deregistration of audit firm

An audit firm shall be entitled to be registered on the recommendation of QAB in accordance with the quality control review framework. All the firms having satisfactory QCR rating at the time of commencement of this Act shall be deemed to be registered.

AOB, on its own motion or on the recommendation of QAB, may order deregistration of the audit firm from the register. For this purpose AOB shall rely on the work and inspections carried out by QAB or its own inspection.

Inspection and proceedings by AOB

AOB on a complaint, suo moto or on reference made by the Commission or State Bank of Pakistan may conduct inspection of records of QAB, in respect of an audit firm registered, to ensure compliance with the regulations made. If AOB is not satisfied with the work of QAB, it may directly conduct inspection of records of audit firm and the public interest company.

Penalty, sanctions or revocation of registration

If an audit firm fails to comply with the requirement of any regulation, or if so recommended by the QAB based upon its findings, AOB may after providing opportunity of hearing:

- a) impose penalty which may extend to five million Rupees;
- b) impose following sanctions;
 - i. such audit firm may be barred from engaging itself as an auditor of the public interest companies for a minimum period of six months or for such higher period not exceeding five years as may be decided by AOB; or
 - ii. revoke registration and remove name from the register of auditor of public interest companies;
- c) reprimand, issue warnings or such other sanctions as deemed necessary or appropriate under the circumstances; or
- d) publish or place its findings of inspections of registered firms on its website.

3. Guidelines for recommended list of documents and records required for QCR

To assist the firms in preparing for a quality control review the QAB has developed a guideline for quality control visit by ICAP reviewers. The objective of the guideline is to make the firms prepare themselves for the review and what is expected of them by the reviewer. This guideline will be sent to the firm before a reviewer visits the firm.

These guidelines address the documentation expected in the archive work files such as but not limited to:

- Engagement letter
- Planning – Understanding the entity and its environment
- Audit Programs
- Working Papers
- Audit Evidence
- Analytical Review
- Subsequent events
- Going Concern
- Management Representations
- Disclosure checklist for Review of Financial Statements
- Quality Control for an audit of financial statements
- Quality Control of firms – ISQC 1

All the audit procedures performed and conclusion reached must be recorded in audit documentation. All the working papers should be initialed and cross-referenced and must contain:

- (a) Objective of the work done
- (b) What item was tested?
- (c) Conclusion of audit procedures
- (d) If the results were not satisfactory, what additional work was done
- (e) The firm's conclusion on all audit tests i.e. did the test confirm the audit objective? If not, is there a record of consideration of the implication for the audit opinion.

It is important to note that the auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

- (a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements;
- (b) The results of the audit procedures performed, and the audit evidence obtained; and
- (c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

4. Summary of Activities

Introduction

This section provides a summary of the review activities undertaken during the year 2015-16.

Scope of Review

In reviewing an audit firm, all locations of the firm and at least 50% of audit partners of the firm are covered. The frequency of review varies depending upon the result of last review and decision of QAB.

Audit engagements reviews conducted

During the year 50 audit firms were reviewed as compared to 52 audit firms in the previous year. The reviews comprised as follows:

Year	2015-16	2014-15
Audit firm's reviewed	51	52
Number of engagements reviewed	228	133
Number of locations covered	88	72
Reviews for compliance with the requirements of ISQC-1	27	15

Out of 51 firms reviewed, 46 firms were found to be "Satisfactory" while 5 firms were rated as "Unsatisfactory".

During the year six (6) new firms offered themselves for review and one firm was removed from the list of QCR Rated Firms.

Review of Firms under ISQC 1

During the period under review, 27 firms were reviewed for compliance with the requirements of ISQC-1 under the framework for QCR program 2015.

Summary of engagement reviews

The following chart summarizes individual audit engagements reviewed over the last five years:

Year	Listed		Other than listed		Total
	Satisfactory	Unsatisfactory	Satisfactory	Unsatisfactory	
2015-2016	88	8	107	25	228
2014-2015	20	21	61	31	133
2013-2014	37	9	57	20	123
2012-2013	43	8	57	14	122
2011-2012	18	9	35	13	75
2010-2011	56	6	41	7	110

5. Summary of observations

5.1 Deferred Taxation

IAS 12 Income Taxes continued to be a perplexing issue while accounting for future tax consequences of the recovery (settlement) of the carrying amount of assets (liabilities) that are recognized in an entity's financial statements. Observations noted with respect to recognition of deferred tax were as follows:

- Non-provisioning of deferred tax
- Incorrect calculation of deferred tax
- No evidence to support utilization of unused tax losses
- Non-apportioning of temporary difference when part of the income of company is chargeable under PTR

5.2 Valuation of Biological Assets

During review it was observed that companies recognized and measured the biological asset such as chicks at historical cost instead of the fair value in accordance with IAS 41.

5.3 Amortization of interest free loan

Similar to previous years during the year it was also noted that interest free long term loans and liabilities from related parties were not measured at amortized cost using effective interest rate and auditors did not modify the report where amount was above materiality level.

To provide guidance the Institute issued Technical Release 'TR – 32: Accounting Directors' loan' which specifies the accounting treatments and the related disclosures of loan according to the terms of the loan.

5.4 Ijarah financing

During review instances were noted where the entities i.e. lessors/lessees entered into an Ijarah agreement but the transactions were accounted for as finance lease in accordance with IAS 17. The auditors neither asked the management to rectify the transactions nor modify the report where the impact on the financial statements was material.

5.5 Retirement Benefit Obligation

In some cases it was observed that the companies did not operate any retirement benefit plan for its employees and no audit evidence was available to conclude whether provision for retirement benefit was required in accordance with Industrial and Commercial Employment (Standing Orders) Ordinance, 1968.

5.6 Audit Sampling

In many instances it was observed that while verifying account balances and classes of transactions using samples, conclusions were drawn on whole population solely on the results of the sample test of details. In determining the sample size, the auditor has not carried out any assessment of the likely risk of a material error in the concerned account balances or class of transactions. Such assessment is usually based on the nature of balances and the adequacy of the control environment. This assessment is usually based on a test of controls which were not carried out. The risk assessment and confidence level that the auditor intends to seek that there is no material error in the population determines the sample size. In the absence of this documentation it is not possible to determine whether the sample size selected is adequate to form an opinion on the population as a whole.

Moreover in a sample test there is always a sampling risk – a risk that the conclusion drawn from the sample is incorrect. To mitigate this risk, sample tests are usually supplemented by target test of details and analytical reviews to reduce the audit risk to an acceptable level.

It was also observed that auditor did not verify the sample completely and concluded on the fair presentation of the account balances and transaction without obtaining sufficient appropriate audit evidence.

5.7 External Confirmation

During reviews instances were noted where the auditor did not maintain control over confirmation requests and did not perform alternative audit procedures in case of non-response of confirmations.

5.8 Going concern assumption

Following observations with respect to going concern assumption were noted during the year:

- Instances were noted where events or conditions that may cast significant doubt on the entity's ability to continue as going concern were identified; however no further audit procedure was performed to determine the existence of material uncertainty.
- In cases where use of going concern assumption was appropriate but material uncertainty existed it was observed that disclosure for going concern was not made in accordance with paragraph 18 of ISA 570. Moreover the auditor also did not qualify the audit report on inadequacy of disclosure in accordance with paragraph 20 of ISA 570.

5.9 Evaluation of work of expert

There were instances where firms did not apply adequate procedures to comply with the requirements of ISA 500 with regard to gathering audit evidence on work of management's experts.

Quality Control Review Process

Step wise review process followed by QAD for review of files is as follows:

- Step 1 – Submission of list of audit engagements on prescribed format.
- Step 2 – Fixation of QCR date with mutual agreement.
- Step 3 – Reviewer visits the firm for review.
- Step 4 – Selection of audit engagement(s) from the list provided, at the time of reviewer's visit.
- Step 5 – Review of working paper of audit engagements and firm's system of quality control under ISQC-1.
- Step 6 – Reviewer notes the observation(s) and obtains comments of engagement partner on "Review Findings Form (RFF)", which is signed by both the reviewer and the engagement partner.
- Step 7 – Draft QCR report is prepared and sent to the firm for comments.
- Step 8 – After incorporating comments of the firm, if any, the draft QCR report is presented to QAB for approval.
- Step 9 – After QAB approval, the final QCR report is issued to the firm informing the overall conclusion of the QCR.

Quality Assurance Board

The QAB performs its functions and discharges its responsibilities in accordance with the Framework. During the year 2015-16, the Board held ten meetings. QAB membership comprises:

1. Sohail Hasan (Chairman)

Sohail Hasan is a Chartered Accountant and a member of the Institute of Chartered Accountants in England and Wales and The Institute of Chartered Accountants of Pakistan. He was a partner in A. F. Ferguson & Co. for over 35 years and also served as its Senior Partner.

2. Ahmed Ali Mitha

Ahmed Ali Mitha is a Chartered Accountant. He is the CFO of Pakistan Stock Exchange Limited.

3. Ali Azeem Ikram

Ali Azeem Ikram is a Chartered Accountant. He is head of the SECP Insurance Division.

4. Amer Aziz

He is Managing Director of the National Institute of Banking & Finance. By profession, Mr. Amer Aziz was a banker.

5. Ayaz Ahmed

Ayaz Ahmed is a Chartered Accountant. He was the CFO of a large commercial bank.

6. Etrat Hussain Rizvi

He has over 31 years' experience of working in private and public sectors in the fields of banking, development financing, manufacturing, utility and regulatory organizations.

7. Mohammad Almas

Mohammad Almas is a practicing chartered accountant and partner of M. Almas & Co.

8. Mohammad Naeem

Mohammad Naeem is a practicing chartered accountant and partner of Mohammad Naeem & Co.

9. Muhammad Lukman

Muhammad Lukman is a Chartered Accountant. He has twenty five years of diversified experience with national and multinational companies.

10. Syed Ahmed Abid

Syed Ahmed Abid is a Chartered Accountant with a vast experience of over 40 years. He worked as CFO of a petroleum sector listed company and also worked as a Financial Advisor/Consultant for the Ministry of Petroleum and Natural Resources.

11. Zulfikar Ali Causer

Zulfikar Ali Causer is a practicing chartered accountant and partner of BDO Ebrahim & Co.

Quality Assurance Department

Quality Control Reviews are performed by chartered accountants employed on a full time basis by the Institute. Currently, the Quality Assurance Department has the following staff strength:

- | | |
|--------------------------------|-----------------|
| 1. Shahid Hussain, FCA | Director |
| 2. Ajlal Hyder, ACA | Deputy Director |
| 3. Muhammad Asad Iqbal, ACA | Manager |
| 4. Muhammad Fahad Parvaiz, ACA | Manager |
| 5. Mahmood Ahmad | Manager |
| 6. Arsalan Malik | Officer |

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