



The Role of the Audit Oversight Board in Enhancing Audit Quality



Strategic Themes

Outcomes

Confidence in audited financial statements

Audit opinion based on sufficient and appropriate evidence

Externalisation of professional values and ethics

Resourceful and capable audit practices

High quality financial reporting practices by PIE

Support adoption and implementation of standards

- Ensure no significant gaps with international standards
- Promote substance over form implementation
- Monitor the effectiveness of the implementation of standards by audit firms

Promote high quality audit practices

- Enforce registration policy that promotes quality and capacity
- Drive quality audit practices through inspection and remediation of audit firms
- Set tone for quality through enforcement actions

Influence financial reporting ecosystem

- Collaborate with stakeholders in financial reporting ecosystem
- Promote research and discourse on audit quality

Leverage on stakeholders support

- Coordinate activities with other authorities in Malaysia and abroad
- Participate in international activities to gain knowledge and experience and promote confidence in Malaysian audit quality
- Obtain higher financial support from stakeholders

Services Areas

Standards setting and guidance

Registration

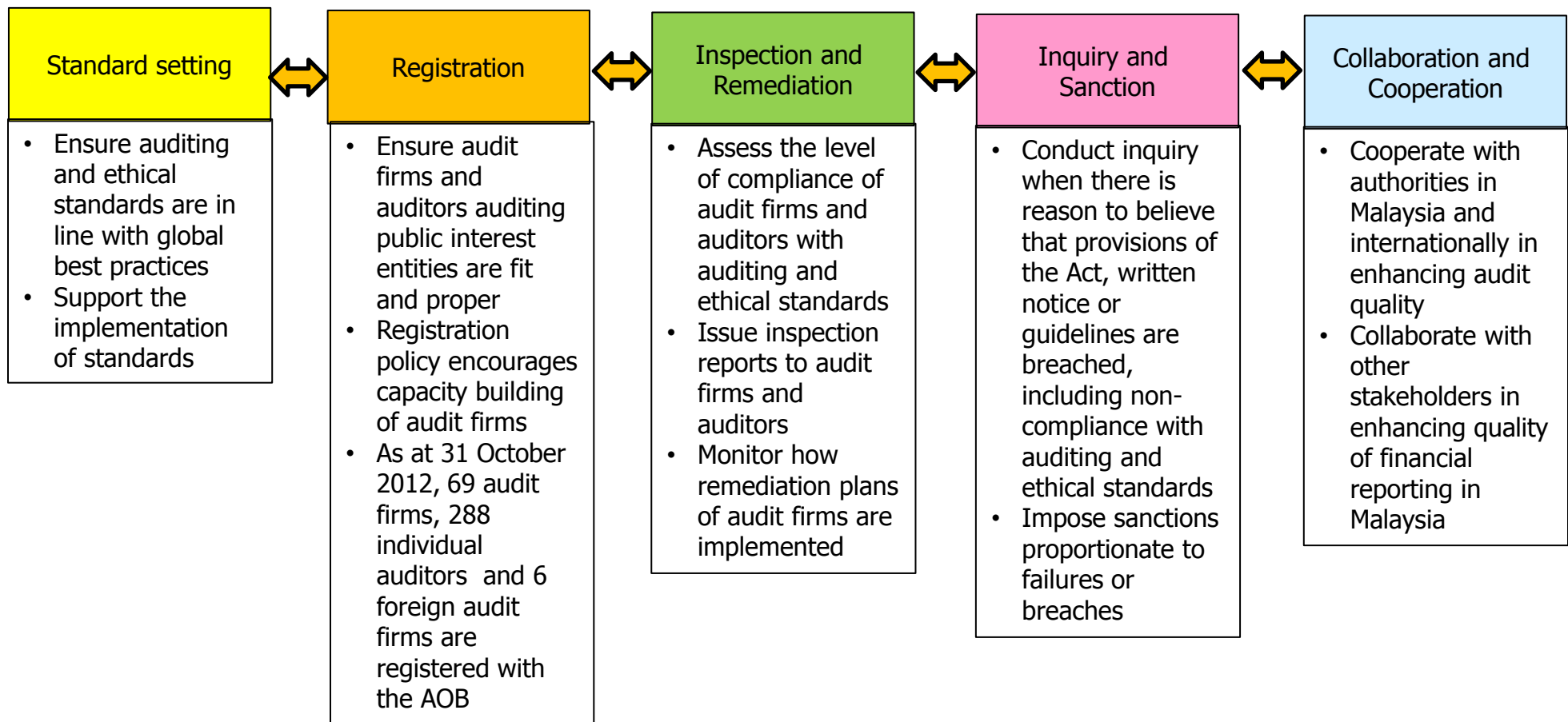
Inspection and Remediation

Enforcement of standards

Promotion of quality and Collaboration with stakeholders



Key service areas of AOB

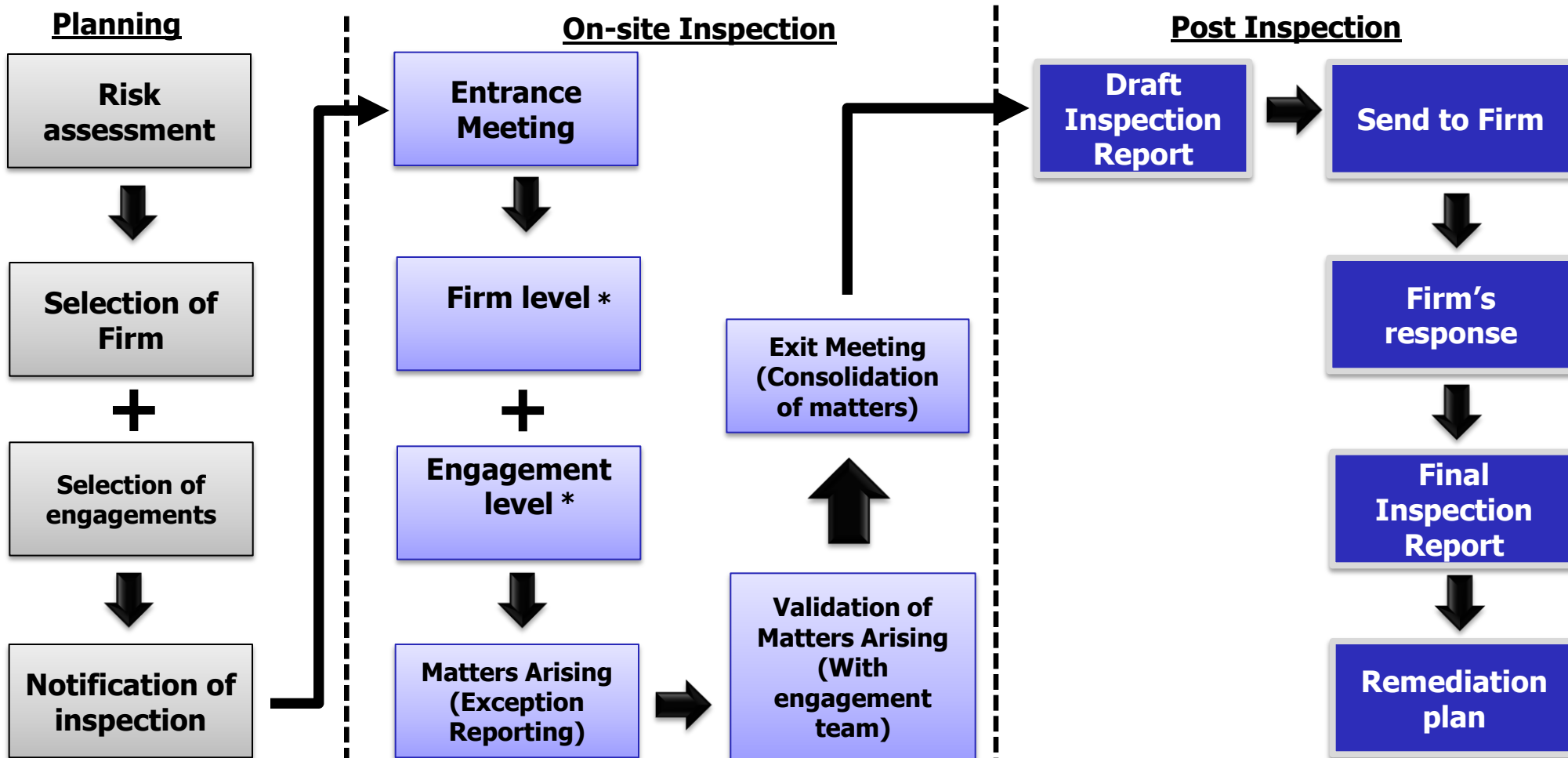


Quality Control

Firm level control (ISQC1)
Leadership
Ethical requirements
Client acceptance and continuance
Human resource
Engagement performance
Monitoring

Engagement level control (ISA 220)
Engagement partner's responsibility
Compliance with ethical requirements
Client acceptance And continuance
Engagement performance
Engagement Quality Control Review
Documentation

Inspection process (Firm Level)



Inspection process (ISQC1)

- **Leadership**
 - Arrangement amongst partners regarding quality
 - Partner and staff performance assessment and remuneration
 - Penalty for non-performance
- **Ethical Requirements and Client Acceptance**
 - Compliance with partner rotation requirement
 - Client acceptance process

Inspection process

- **Human Resource**
 - Staff recruitment policy
 - Training: Areas of training and timing
- **Engagement Performance**
 - Updated manual and guidance
 - Role and responsibility of EQCR
- **Monitoring**
 - Design and effectiveness of monitoring process

Firm Level		
	Major Audit Firms	Other Audit Firms
Tone from the Top	<ul style="list-style-type: none"> Balancing business strategy vs. audit quality Balancing capacity and risks 	<ul style="list-style-type: none"> Balancing business strategy vs. audit quality Balancing capacity and risks Absence of partnership agreements No holistic framework which defines, measures, monitors and rewards audit quality
Relevant ethical requirements	<ul style="list-style-type: none"> Familiarity threat and safeguards – senior personnel 	<ul style="list-style-type: none"> Monitoring of threats to independence and safeguards Familiarity threat and safeguards – partner rotation and EQCR, senior personnel Self review threat Mechanism to detect non-compliance with independence
Acceptance and Continuance of Client Relationships and Specific Engagements	<ul style="list-style-type: none"> Objective evaluation – Substance over Form 	<ul style="list-style-type: none"> Objective evaluation – Substance over form Timeliness of evaluation

Firm Level		
	Major Audit Firms	Other Audit Firms
Human Resources	<ul style="list-style-type: none"> Partners' workload High staff attrition rate 	<ul style="list-style-type: none"> Partners' workload Training in Clarified ISAs or applicable new and revised FRSs
Engagement Performance	<ul style="list-style-type: none"> EQCR effectiveness Professional Skepticism Thinking Audit Time spent at various stages of audit engagement Relevant documentation Late archival 	<ul style="list-style-type: none"> EQCR effectiveness Professional Skepticism Thinking Audit Consultation on contentious issue Investment in competent resources Audit Program/Audit Methodology Time spent at various stages of audit engagement Robustness of documentation Late archival
Monitoring	<ul style="list-style-type: none"> Effectiveness of follow up on internal/network audit quality review 	<ul style="list-style-type: none"> Absence of internal/network audit quality review

Engagement Review

	Major Audit Firms	Other Audit Firms
Planning and Risk Assessment	<ul style="list-style-type: none"> • Audit strategy fail to fit business model • Disconnect between audit planning, execution and conclusion 	<ul style="list-style-type: none"> • Robustness of risk assessment and planning • Understanding the regulatory framework and internal control framework • Planned audit procedures to response to risk at financial statement assertion level • Disconnect between audit planning, execution and conclusion

Engagement Review

	Major Audit Firms	Other Audit Firms
Revenue Recognition	<ul style="list-style-type: none"> • Revenue cut off – insufficient testing or inappropriate reliance on control testing • Audit strategy fail to understand transactions captured • Complexity of business model and processing systems – data captured cannot be easily traced and identified, traditionally • Communication between IT auditors and financial auditors • Drawing comfort from high level controls (entity level) and general IT control do not compensate for non testing of application control • Direct/indirect relationship of the controls • Assets Management Companies (“AMC”) – inherent limitation where AMC does not manage its own funds 	<ul style="list-style-type: none"> • No rebuttal of presumed fraud risk • Audit strategy fail to understand transactions captured • Direct/indirect relationship of the controls • Revenue cut off – insufficient testing or inappropriate reliance on control testing

Engagement Review		
	Major Audit Firms	Other Audit Firms
Going Concern	<ul style="list-style-type: none"> • Over-reliance on audit client's explanations and representations • Past history growth could not support future estimated growth with business case • Insufficient challenge despite existence of indicators of going concern • Various methods used in the calculation of terminal value • Wrong sensitivity analysis performed on the cash flow projections 	
Impairment of Goodwill, Assets and Other Intangibles	<ul style="list-style-type: none"> • Identification of Cash Generating Unit "CGU" not supported • Inadequate challenge why CGU can be larger than operating segment • Inappropriate assessment – not in compliance with accounting standards • Inadequate challenge of assumptions – key estimates used i.e. growth rate and discount rate • Value in use / PV of future cash flow was incomplete • Cash flow revealed thin margin of error but no further work done 	
Accounting Estimates	<ul style="list-style-type: none"> • Insufficient procedures to understand management's estimation process despite being significant • Not identified as key risks area in view of the nature of estimation 	

Engagement Review		
	Major Audit Firms	Other Audit Firms
Related Parties Transactions and Disclosures	<ul style="list-style-type: none"> Shortcomings in documentation 	<ul style="list-style-type: none"> No review performed to understand the management's control and process to identify RPT Undue reliance on management's representation
Use of Experts	<ul style="list-style-type: none"> Lack of coordination between IT expert and financial auditors Limitation clauses in the experts' report not appropriately resolved 	<ul style="list-style-type: none"> No evaluation of competence, objectivity and scope of experts Limitation clauses in the experts' report not appropriately resolved
Group Audit Arrangement	<ul style="list-style-type: none"> Limitation in the scoping process, consistency in work done based on threshold set No critical evaluation of work of component auditors 	
Sampling	<ul style="list-style-type: none"> Undue reliance placed in determining the completeness of population Untested population though amount above materiality No basis for sample size used 	

Engagement Review		
	Major Audit Firms	Other Audit Firms
Third Party Confirmations	<ul style="list-style-type: none"> Lack of follow / further work done 	<ul style="list-style-type: none"> Lack of follow up / further work done Reliance on photocopy and fax
Presentation and Disclosures	<ul style="list-style-type: none"> Insufficient rigour in the review of financial statements resulted in insufficient / omission of disclosures i.e. FRS 8 – Operating Segments, FRS 7 Financial Instruments : Disclosures, FRS 139 – Financial Instruments : Recognition and Measurement 	
Substantive Analytical Review	<ul style="list-style-type: none"> Insufficient work done to comply with Clarified ISAs 	
Materiality Concept	<ul style="list-style-type: none"> Overall materiality and performance materiality – lacking for smaller firms Limited to quantitative factors Inconsistent materiality used 	

Enforcement

- Enforcement actions taken by AOB so far:
 - An auditor has been sanctioned for his failure to comply with International Standards on Auditing in his audit work
 - An auditor has been sanctioned and fined RM 5,000 for his failure to comply with MIA By-Laws on professional independence and failure to comply with International Standards on Auditing in his audit work*

* Subject to appeal to Securities Commission within 30 days from the date of the notification of the decision

Building blocks of audit quality

- Tone from the top is very important in setting the tone for quality
- While firms have put in place systems and process of quality control, effective implementation of the process remains a concern
- Balancing the workload of partners and key audit staff would influence audit quality
- EQCR plays an important check and balance role in maintaining audit quality

Building blocks of audit quality

- Professional scepticism of auditors is critical in assessing audit risks and evidence obtained
- Need to balance between reliance on checklist and “thinking audit”
- Effectiveness of the monitoring by audit firms of their audit quality will reinforce the emphasis on quality

Building blocks of audit quality

- Risks need to be identified at the planning stage to ensure the auditor could design appropriate response and obtained sufficient and appropriate evidence to forming audit opinion
- Auditors need to understand business models and their associated risks especially when dealing with complex businesses and large groups of companies operation in many countries and jurisdictions

Building blocks of audit quality

- Professional scepticism need to be applied when auditing areas where judgment are exercised such as goodwill, asset impairment and estimates
- Achieving the objectives of audit procedures such as confirmation and sampling should be always ensured
- Auditing disclosures is becoming more challenging in view of the changes in IFRS

Audit Oversight Board Malaysia



Suruhanjaya Sekuriti
Securities Commission
Malaysia

