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THE IRBA INSPECTIONS STRATEGY AND PROCESS: EIGHTH INSPECTIONS CYCLE

2021/2022-2023/2024

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1. INTRODUCTION

The Independent Regulatory Board for Auditors' (IRBA) Inspections Department is committed to enhancing audit quality and promoting compliance with professional standards and rules. Primarily, we do this through our inspections programme.

Further, the department's functions support the IRBA's refocused five-year strategy that was adopted by the Board in February 2021 and approved by National Treasury and Parliament in March 2021.

To that end, this document provides an overview of the inspections process, and that includes changes in the 8th Inspections Cycle. Auditors may find this information valuable as they plan and perform current and upcoming audits. Audit committees and those charged with governance may also use this information to understand the inspections process as well as initiate and inform constructive dialogue with their auditors.

2. OBJECTIVE OF INSPECTIONS

The IRBA's vision is to be a pre-eminent and respected audit regulator that is also internationally and locally recognised, and whose purpose is to protect the public interest and safeguard the integrity of the South African financial markets by creating an enabling environment in which auditors can deliver high-quality audits.

The mission of the IRBA is to endeavour to protect the financial interests of the investing community by creating and enhancing regulatory tools and principles, to empower registered auditors to carry out their duties competently, independently and in good faith.

Part of this mission entails performing inspections, in terms of Section 47 of the Auditing Profession Act (APA), Act 26 of 2005, as amended.

Objective Statement of the Inspections Department

Inspections are a crucial regulatory function that gives effect to the IRBA's mandate and strategy to protect the public interest by monitoring compliance and influencing auditors and relevant stakeholders in pursuing consistent sustainable high audit quality that adheres to the highest standards, while maintaining good professional relationships. This is achieved by employing adequate and competent staff, and effectively deploying available resources, tools and technology to perform high-quality independent inspections of predominantly public interest entity (PIE) audits, but also smaller assurance engagements, selected on a risk basis. Furthermore, this is achieved through performing and reporting on the outcomes of inspections in an objective and fair manner that promotes transparency, accountability and remediation by auditors, where required; and helping drive broader proactive audit quality improvement strategies with relevant stakeholders on areas where these are most needed.

Inspections' Value Proposition

Restoring stakeholder confidence through measured audit quality.

3. INTERNATIONALLY RECOGNISED AUDIT REGULATOR

The IRBA is a founding member and board member of the International Forum of Independent Audit Regulators (IFIAR), an international body of more than 50 independent audit regulators. Our membership and representation on the board and its working groups, such as the Inspections Workshop Working Group, the Investor and Other Stakeholder Working Group, the Enforcement Working Group, the Standards Coordination Working Group and the Technology Task Force, allow the IRBA to keep up to date with international developments in audit regulation, including inspections. Also, our inspections process is benchmarked on an ongoing basis against the IFIAR core principles and inspection processes followed by other recognised independent audit regulators worldwide.

4. STRATEGIC FOCUS ON AUDIT QUALITY

One of the revised strategic focus areas of the IRBA's refocused five-year strategy relates to audit quality. This is because the improvement of audit quality is critical to restoring confidence in the profession. The IRBA will respond to this focus area by, inter alia, employing and developing the relevant skills to increase the coverage of inspections; strengthening the disciplinary and sanctions processes; and developing IT solutions that will enable it to work proactively and more efficiently in the dynamic audit environment.

In the 8th Inspections Cycle the Inspections Department has therefore aligned the inspections process to the IRBA's refocused strategy. As a result, the following key changes are introduced in the 8th Inspections Cycle:

- Comprehensive stakeholder engagement; (point 5)
- Guided proactive monitoring of remediation initiative (point 6)
- Theme-based inspections (point 7)
- Enhanced BI process (point 7)
- Enhanced reporting (point 9.7)

5. STRATEGIC FOCUS ON COMPREHENSIVE STAKEHOLDER ENGAGEMENT

Comprehensive stakeholder engagement is another focus area in the revised strategy. This is particularly important because the IRBA has a responsibility to respond to the concerns of its many and varied stakeholders, especially those who rely on the auditor's opinion that a company's accounts reflect fairly, as investment decisions are made based on the veracity of these opinions.

As such, with this Inspections Cycle strategy, the Inspections Department will focus on increasing its stakeholder relations and enhancing its communications plan. This will include engaging with audit firms on a proactive basis, while maintaining independence; assessing the need to engage with audit committees of listed entities; and engaging with other regulators and institutions.

In line with this strategy, the department will follow a broader stakeholder approach to audit quality improvement that requires enhanced transparency and accountability in the public interest. Audit firms

are therefore required to promptly share their latest inspection decision letters, formal reports (unredacted) and remedial action plans with audit committees of listed companies and other PIEs to facilitate robust dialogue on matters affecting audit quality.

6. GUIDED PROACTIVE MONITORING OF REMEDIATION INITIATIVE

Due to the concerning trend, over several inspections cycles, of recurring deficiency themes being reported to audit firms and practitioners, the Inspections Department is introducing a guided proactive monitoring process with audit firms, as part of the 8th Inspections Cycle remediation initiatives. This proactive monitoring process provides audit firms and their practitioners with an opportunity to commence with the remediation of the IRBA-identified deficiencies at an earlier stage in the inspections process.

An essential part of this proactive monitoring process, which is aimed at strengthening the current IRBA Remedial Action Process, relates to the effectiveness and reliability of the audit firm's internal monitoring controls. Therefore, the IRBA will monitor this through a dashboard/tool that will need to be completed by audit firms and supported by the relevant evidence of remediation.

Once the proactive monitoring process for a specific practitioner and audit firm has been completed, the Inspections Department will inspect the evidence compiled, to confirm the sufficiency of the remediation.

It is anticipated that through this process the IRBA will be able to provide further insights to relevant stakeholders on the remediation steps taken by the audit firm, and whether those steps are appropriate, in light of the findings initially identified, thereby addressing the risk of repeat findings. This initiative will be piloted on a voluntary basis in the first year of the 8th Inspections Cycle, with further rollouts anticipated as the cycle progresses.

7. RISK-BASED INSPECTIONS APPROACH

The IRBA has adopted the IFIAR¹ Core Principles, which state that audit regulators should ensure that a risk-based inspections programme is implemented. The purpose of the risk-based inspections approach is mainly to ensure that firms performing high-risk assurance engagements² are analysed, categorised and selected for inspections at the appropriate frequency, based on inherent and identified risk factors.

Firms providing assurance services are classified into categories, based on their size (per annual assurance fees declared); the number of registered auditors (RAs) performing assurance engagements; and the nature/type of assurance engagements. This is done to stratify the population and help determine the nature and extent of both firm level and engagement level inspections to be performed. Audit firms are categorised as:

- *High-risk firms*: Those that perform high-risk assurance engagements, as defined.
- *Low-risk firms*: Those that perform low-risk assurance work, as defined.

The Inspections Department focuses mainly on high-risk firms. For compliance monitoring purposes, the department inspects entities that require mandatory/statutory audits and prioritises the inspection of PIEs, as defined in the IRBA Code of Professional Conduct. This is in line with the IRBA's mandate and strategy to help protect the broader investing public from potential audit failures that could also affect a broader percentage of the public, and to protect the reputation of the auditing profession. The list of firm types classified as high-risk is reviewed and revised on an annual basis, as part of the annual fee declaration process, and is published in the Annual Return Explanatory Manual that is circulated every year to all RAs.

Low-risk firms may be inspected, where specific risks are identified, and selected on a random basis, at the IRBA's discretion.

Despite the focus on firms and audits with greater public interest exposure, our current mandate stretches beyond listed entities and PIEs. Therefore, small to medium-sized practices and firms that audit non-PIEs cannot be overlooked.

Risk factors may include the nature and complexity of the entity being audited; its industry and level of public interest; audit issues likely to be encountered; and the maturity of markets. Other risk factors considered are specific to the audit firm and include the type and range of its assurance engagements; prior reported inspection deficiencies; and reportable deficiencies from inspections of the firm's internal quality control and risk management processes.

The gathering and analysis of intelligence data form the basis of a comprehensive risk analysis that enables the Inspections Department to make informed decisions on audit firms and specific assurance engagements, or parts thereof, to select for inspection. Risk factors are generally assessed at the following three levels:

- Level 1 – Firm level.
- Level 2 – Specific assurance engagements of the firm.
- Level 3 – Scope of the inspection (specific areas within an assurance engagement).

¹ See www.ifiar.org.

² Entities that require statutory audits in terms of legislation or regulation and are categorised by the IRBA as high-risk assurance engagements.

Firm Selection

Factors considered to determine which firms to select for inspection include:

- Section 47(1)(b) of the APA (amended)
- Type and range of assurance work, i.e. High risk, special risk, or Low risk
- Firm size
- Firm specific risk indicators, including firm inspection results and relevant quality indicators
- Developments in the firm's assurance client profile and structures
- Assurance engagement portfolio and associated risks
- Prior firm review findings from the firm's own internal quality control and risk management processes
- Prior inspection findings raised by the IRBA at firm and engagement level and the remediation thereof
- Reports issued by other regulators to the firm
- Firm leadership's 'Tone-at-the-top' and governance
- Firm governance
- Audit failures and media articles

Assurance Engagement Selection

Factors considered to determine which assurance engagements to select for inspection include:

- Level of public interest inherent to the engagement entity
- Engagement partner specific risk indicators, including prior inspection results, client portfolio and engagement partner experience
- International and local developments, including accounting and auditing standards as well as market and industry indicators
- Selections include an element of random selection of assurance engagements
- Nature and knowledge of the industry risks and the nature of the client
- SENS announcements and media coverage

Scope of Selected Assurance Engagements

Factors considered to determine the scope of the inspection include:

- Nature and knowledge of the industry risks and the nature of the client
- Risk factors identified from a review of the audited Financial Statements
- Trends in areas of poor audit quality
- International and local developments, including accounting and auditing standards as well as market and industry indicators
- Planning and Completion sections
- Fieldwork scope based on identified risks and judgement
- Prior inspection findings at firm and engagement levels, including effectiveness of the firm's quality control system and remediation process

Figure 1: Risk-based selection and scope of inspection (the listed factors are not exhaustive).

Business Intelligence

To enable effective Business Intelligence (BI) and risk-based selections, additional information is obtained through declarations, Audit Quality Indicators (AQIs) and collaboration with other regulators as well as through conducting robust financial reporting reviews.

In 2021 and in preparation for the 8th Inspections Cycle, the BI function has been enhanced by the appointment of additional capacity and centralisation within the IRBA to enhance intelligence gathering and risk scanning capabilities, to support the organisation as a whole. Additionally, the IRBA's digital transformation journey is expected to automate

some of the manual environmental scanning and make information gathering more efficient. Furthermore, the IRBA will continue to engage with other regulators and relevant professional bodies through the strategic focus area of comprehensive stakeholder engagement, to further strengthen the regulatory oversight of the broader financial reporting and governance ecosystem.

Inspections approach

The inspections approach also includes elements of unpredictable and random selection of firms, engagement partners and assurance engagements, to complement its risk-based selections and scope.

The risk-based inspections approach is not intended to select a representative sample of a firm's assurance work. Instead, it is focused on higher-risk engagements and audit areas where deficiencies are likely; and areas that, if not appropriately responded to by the auditor, can create a risk of an inappropriate auditor's report being issued. This approach also means that inspection results should not be statistically extrapolated across the entire auditor population. Rather, inspections are designed to address inherent and identified risks and not to cover all RAs or assurance engagements in a cycle.

It should also be noted that an inspection is not designed to identify every deficiency that may exist; and the IRBA's scope, reportable deficiencies and reports are not necessarily exhaustive. Accordingly, the formal inspections report and the decision of the IRBA's independent Inspections Committee (INSCOM) do not provide any assurance regarding the firm's quality control system or assurance engagements. They rather describe reportable deficiencies that the IRBA wishes to bring to the auditor's attention, at a particular point in time, to prompt remediation across all offices and audits performed by the firm, as part of its quality improvement processes.

Theme-based inspections

The Inspections Department is introducing theme-based inspections during the 8th Inspections Cycle. The objective is to measure the extent to which audit firms or auditors implement appropriate remediation to address reported deficiencies (themes). The inspection of these themes will be performed on selected engagement files, in addition to those selected for inspection following the normal process highlighted above. The selected themes will be communicated to the firm leadership at the start of the inspection. The results of these theme-based inspections will be communicated to the audit firm leadership. Also, theme-based inspections, together with firm or engagement file inspections, will be performed concurrently for a specific audit firm. Themes could be specific to an audit firm, based on previous inspection findings and/or those reported by the IRBA through the public inspection's report and the IFIAR reports.

8. ANNUAL FEE DECLARATION INSPECTIONS

The Inspections Department performs standard procedures during selected inspections, to verify the completeness and accuracy of annual firm fee declarations. A separate specific fee declaration inspection can also be scheduled at any time, if the IRBA suspects that the firm's declaration is incorrect or incomplete.

Any errors or omissions in the declarations are regarded in a serious light, as they do not only adversely impact the scope of inspections but also the IRBA's fee base. These cases may result in reportable deficiencies in the formal inspections report and may be referred to the IRBA's Operations Department for correction and/or to its Investigations Department for an investigation, where negligence, dishonesty or failure to cooperate with the regulator is suspected.

9. INSPECTIONS PROCESS

Two types of inspections are performed, namely, firm-wide inspections and individual assurance engagement inspections. Inspections are performed over three-year cycles.

It is important that the inspections process be comparable to international best practice. To ensure this, the inspections approach, methodology, scope and procedures are benchmarked against those of other reputable international regulators on an ongoing basis.

The inspections process is also regularly updated in response to changes in the environment, and these may include new international standards of accounting and auditing, changes in relevant legislation as well as trends identified in the political and economic landscape.

Pre-planning

- Firm's Annual Declaration (Must be timely, accurate and complete)
- Cycle/Annual Themes and Scope
- Annual Risk & Capacity Budget
- Annual Performance Plan (Performance targets)
- Business Intelligence (BI) risk analysis and report
- Risk-based selection (Firm/Engagement partner/Assurance engagement)
- Financial Reporting Inspection and report
- Risk-based selection (Component/Focus areas) including file selections for theme-based inspections
- Planning and allocating appropriate resources to specialised areas

Planning & Execution

- Scheduling of selected Firm/ Engagement partner
- Complete and accurate preliminary information submitted to the IRBA in the specified time
- Performing inspections with technical support by a dynamic/multi-skilled team
- Discussion of findings with Firm/Engagement Partner/Team
- Team Leader supervision, review, and guidance
- Dedicated Team Leader at larger firms to liaise with firm leadership
- Robust internal and independent Quality Control Review
- Issue and discuss Preliminary Findings Report
- Firm/Engagement partner submit complete and succinct written comments, including relevant supporting evidence to the IRBA in the specified time
- Anonymous evaluation of inspections team by firm/engagement partner (optional but encouraged)
- Ongoing communication and consultation where deemed necessary
- Additional internal and independent Quality Control Review

Reporting and Submission to INSCOM

- Anonymised draft inspection reports with comment letters submitted to INSCOM
- Report includes reportable deficiencies that require remediation by firm/engagement partners to improve audit quality
- INSCOM meets four times a year on a quarterly basis
- INSCOM determines and communicates further action required (if any) to the firm:
 - Nothing identified that requires any action
 - Action/conditions required (See Remedial Action Process below)
- INSCOM determines if any specific re-inspection is required and the extent thereof
- Written formal inspections report issued to firm leadership (CEO or equivalent) and this includes INSCOM's decision on any further action/conditions required and special messages
- Reconsideration process available (evidence based only)

Remedial Action Process

- INSCOM requires a written undertaking within the specified time that appropriate action to remediate all reported findings will be implemented by the firm and its engagement partners
- General action/condition - INSCOM requires a Root Cause Analysis and Action Plan (RCAAP) to be submitted within the specified time, including any supporting evidence
- Specific action/condition – INSCOM may also require additional specific action/conditions to be met by the firm/engagement partner within a specified time, supported by evidence
- The IRBA evaluates the RCAAP and evidence received and engages with the firm/engagement partner where deemed necessary
- Guided proactive monitoring process commences and is implemented simultaneously with normal remedial action process.
- Continued non-compliance and failed remediation reported to INSCOM may lead to an investigation/disciplinary action
- Publish key inspection findings, e.g. The Annual Public Inspections Report
- Feedback to relevant stakeholders
- Drive broader proactive audit quality improvement strategy with relevant stakeholders on areas where it is most needed

Figure 2: An overview of the inspections and remediation processes.

Note: The INSCOM was established in terms of Section 20(2) of the Auditing Profession Act of 2005, as amended.

9.1 FIRM-WIDE INSPECTIONS

The objective of firm-wide inspections is to inspect the design and implementation of an audit firm's system of quality control/management, in terms of the applicable standards.

Until 15 December 2022, firm inspections will continue to monitor compliance with the following elements of International Standard on Quality Control (ISQC) 1: leadership responsibilities; ethical requirements (including independence); client acceptance and continuance; human resources; engagement performance; monitoring; and documentation thereof. Firm inspections also include a selection of assurance engagements to assess the implementation and effectiveness of the firm's system of quality control, and the overall sustainability, consistency and quality of assurance engagements by its engagement partners.

After 15 December 2022, or where firms formally adopted and implemented International Standard on Quality Management (ISQM) 1, the Inspections Department will monitor compliance with the components of:

- ISQM 1 – the firm's risk assessment process; governance and leadership; relevant ethical requirements; acceptance and continuance of client relationships and specific engagements; engagement performance; resources; information and communication; monitoring; and the remediation process.
- ISQM 2 (Engagement quality reviews) – applying and complying with relevant requirements; appointment and eligibility of engagement quality reviewers; performance of the engagement quality review; and documentation.

The new Suite of Quality Management Standards – ISQM 1, ISQM 2 and International Standard on Auditing (ISA) 220 (Revised) – become effective as per the dates stipulated in each respective standard. These effective dates³ occur during the Inspections Department's 8th Inspections Cycle. As part of our proactive monitoring approach, the department will be monitoring the implementation of these standards by audit firms. For our greater stakeholder engagement strategy, we will meet with relevant audit firms before the implementation date to assess their implementation plans and activities in relation to the adoption of these standards.

³The IRBA Board adopted the full Suite of Quality Management Standards. ISQM 1 is to be designed and implemented by 15 December 2022; and ISQM 2 and ISA 220 (R) are applicable to assurance engagements for periods beginning on or after 15 December 2022. Early adoption of these standards is permissible.

In the 8th Inspections Cycle, the IRBA will continue to focus on those who assume leadership responsibilities within the firm, i.e. the Chief Executive Officer or equivalent and assigned senior executives, whose primary responsibility is to operationalise the quality control system within the firm (firm leadership).

Logistical arrangements, including suitable office space for the inspectors, laptop computers, software licences, engagement file back-ups, must be arranged in advance; and all requested information must be provided to the Inspections Department by the specified time and before the commencement of, and during, the inspection. A mere offer or invitation to inspect information at a certain location will not be regarded as information provided, unless agreed to by the inspections team and the firm in advance.

Given the COVID-19 pandemic, we expect to continue to conduct inspections remotely, for the foreseeable future. However, the inspections process, as communicated in this document, will continue to be adhered to, where applicable. The Inspections Department will make use of relevant technology to communicate virtually with relevant stakeholders.

9.2 ASSURANCE ENGAGEMENT INSPECTIONS

The objective of individual assurance engagement file inspections is to monitor firms' and engagement partners' compliance with applicable standards, codes of conduct and legislation in performing assurance work of a consistent, sustainable high quality. The risk-based approach may result in the selection of one or more assurance engagements of the same audit firm and/or engagement partner in a cycle. Engagement performance quality on selected assurance engagements is used as an indicator of the effectiveness and consistency of the firm's quality control system.

9.3 LEADERSHIP RESPONSIBILITIES

In the 8th Inspections Cycle, there will be a continued focus on firm leadership, which is ultimately responsible for promoting a culture of quality that ensures consistent, sustainable high quality on all audits within the firm, including a responsibility that any reported quality control review or inspection reportable deficiencies are promptly evaluated, internally communicated and remediated, as part of the firm's ongoing quality improvement processes. This is in line with ISQC 1/ISQM 1, which requires the firm leadership to assume ultimate responsibility for the firm's system of quality control, including

consistency and the quality of engagement performance.

A dedicated Team Leader will be allocated to the selected network firms, to drive the IRBA's strategy with firm leadership to promote consistent, sustainable high audit quality within the firms.

Leadership and those delegated to manage quality control in the firm should at all times remain up to date on the inspections process and any possible reportable deficiencies. In addition, the firm leadership will be required to attend key meetings with the Inspections team during inspections, to avoid any unnecessary disagreements or delays in the inspections process. The Team Leaders remain aware of their independence at all times.

9.4 GENERAL INSPECTION AND REMEDIATION PROCESSES

The general inspection procedures followed by the Inspections Department include the following:

- a) The firm is normally notified of the planned dates of the scheduled inspection for logistical purposes by the Senior Administrator: Planning. However, in terms of Section 47 of the APA, the IRBA may, at any time, inspect or review the practice of an RA.
- b) Once the internal risk-based selection and planning process have been concluded by the team, pre-inspection information is requested from the firm/engagement partner. The firm/engagement partner must ensure that all relevant information and documentation are provided to the IRBA by the specified time and before the inspection commences. This includes all relevant electronic and hardcopy documents or working papers.
- c) Selected completed assurance engagement files are requested prior to the commencement of the inspection and should be promptly provided by the firm. This includes all relevant electronic and hardcopy documents or working papers.
- d) The inspections team performs the inspection, scheduling the necessary kick-off, progress and close-out meetings with the firm/engagement partner.
- e) During the inspections, the inspections team may request (or make) copies of any relevant documents and working papers.
- f) Inspectors may, at any time, interview firm staff, including members of the engagement team.
- g) Initial or potential draft reportable deficiencies (preliminary reportable deficiencies) are promptly communicated and discussed with the firm/engagement partner throughout the duration of the inspection.
- h) The draft reportable deficiencies are subjected to an internal quality control review, and a preliminary inspections report (PIR) is issued and discussed within the internal timeframes. The PIR is subject to change or, in some cases, additional reportable deficiencies may be raised later in the process.
- i) The inspections team obtains written comments on the PIR from the firm/engagement partner on the firm's letterhead (PDF version) together with a separate MS-Word version (to allow for anonymisation) within the specified timeframe.
- j) The inspections team assesses the written responses and prepares an anonymised draft formal inspections report (which includes the reportable deficiencies, comments received and conclusions, where applicable). Then, following a final internal quality control review, the inspections team submits the report to the INSCOM for a decision on any further action/conditions (if any).
- k) The INSCOM's decision, including any required action/conditions, an executive summary highlighting key inspection themes and risks, any special paragraphs and inspections report/s are all formally communicated to the firm leadership as one reporting pack.
- l) Where the formal inspections report requires further action/conditions, the firm/engagement partner is required to respond within 30 calendar days from the date of the formal inspections report. Further communication with the firm/engagement partner is initiated, where deemed necessary.
- m) In 2021, the Inspections Department will implement changes to the quality control process, to improve the turnaround time of inspections reports to audit firms, thereby allowing for prompt remediation by audit firms.
- n) As part of the 8th Inspections Cycle strategy, we aim to achieve enhanced reporting by affecting changes to stakeholder reports, including the Firm Executive Summary report and the formal inspections report (engagement file inspections report). These changes will result in a more user-friendly report and include relevant information that will, for instance, consist of trend analyses, thereby providing relevant stakeholders with meaningful information.

9.5 REPORTABLE DEFICIENCIES

There are two types of reportable deficiencies communicated to the firm/engagement partner in the formal inspections report, following an IRBA inspection. These are: (1) firm level – those related to the audit firm's system of quality control/management; and (2) engagement level – those related to the firm's individual assurance engagements.

A reportable deficiency at a **firm level** includes any significant or systemic deficiency related to the firm's conduct (including ethics and independence requirements); or its system of quality control/management that may have an impact on audit quality by creating a risk of inappropriate auditor's reports being issued by the firm, including failure to implement remedial/corrective action on all assurance engagements performed by the firm, resulting in recurring inspection reportable deficiencies.

A reportable deficiency at an **engagement level** includes any significant deficiency whereby the firm has failed to perform sufficient and appropriate audit procedures and/or has failed to obtain or document sufficient and appropriate audit evidence to support its auditor's report, including a failure to identify or address a material or likely potential material financial reporting/accounting related deficiency or error in the application of an accounting principle. Alternatively, this includes any non-compliance with applicable standards, codes of conduct (including ethics and independence requirements) and legislation, including a departure from the firm's adopted policies, procedures or methodology.

Reportable deficiencies on assurance engagements do not necessarily imply that the financial statements are materially misstated or the auditor's opinion is inappropriate, but may relate to a lack of documented procedures or sufficient and appropriate evidence that would have detected misstatements.

The purpose of communicating reportable deficiencies is to formally alert the firm/engagement partner to any identified deficiency of a significant or systemic nature that requires prompt remediation or corrective action to be implemented by the firm and its engagement partners, to promote consistent, sustainable high audit quality on all audits within the firm.

9.6 ACTION REQUIRED

The INSCOM assesses the nature and facts of the deficiencies, including the responses to the reportable deficiencies identified. The committee then comments on these reportable deficiencies and determines any further action it deems necessary, as follows:

- No further action required: When there are no pertinent reportable deficiencies identified during the inspection and requiring any action on the part of the firm/engagement partner, this will be reported as "no further action required".
- Where reportable deficiencies are identified and reported to the INSCOM, the firm will be required to, within the specified timeframe, submit a written undertaking that prompt remedial/corrective action will be taken to address the reportable deficiencies within the firm. This includes submitting a Root Cause Analysis and a Remedial Action Plan in the prescribed format to the IRBA for evaluation (general action/conditions). The firms are required to undertake these actions when the INSCOM concluded with one of the following outcomes:
 - Some improvement required: Where the nature and/or extent of the reportable deficiencies identified are not regarded as significant.
 - Significant improvement required: Where the nature and/or extent of the reportable deficiencies identified are significant.
 - Referral for an investigation with significant improvement required: Where the nature and/or extent of the deficiencies identified are regarded as a material non-compliance with the Code/ISAs. This includes instances where the audit opinion issued is incorrect, material misstatements were not identified by the auditor or there was even significant non-documentation of audit work performed.

The INSCOM, at any time, reserves the right to refer any firm/engagement partner to the Investigations Department, based on the significance, systemic nature or extent of the deficiencies reported, including recurring deficiencies of a similar nature being reported.

A referral for an investigation does not negate the responsibility on the part of the firm and/or its partners to implement prompt remedial/corrective action. The INSCOM may decide that a specific follow-up inspection be performed on a firm and/or an engagement partner, to determine if the firm/engagement partner remediated the previously reported deficiencies. However, follow-up inspections might not necessarily be performed on the same assurance engagement or engagement partner previously inspected at the firm. If during any inspection, including a follow-up inspection, previously reported inspection reportable deficiencies of a similar nature are raised with no or little improvement, this will be viewed in a serious light.

- Pending: The INSCOM may decide not to finalise its decision on the overall outcome of the inspection, and may request the firm/engagement partner to take specific actions or meet certain conditions before a final decision on the outcome of the inspection is made. This can be, for example, to submit supporting evidence or information on a specific matter within a

prescribed timeframe for evaluation by the committee (Pending Decision: Specific action/ conditions). Failure to meet any of the committee's requested actions or specific conditions may result in a referral to the IRBA's Investigations Department for an investigation, leading to possible further disciplinary action.

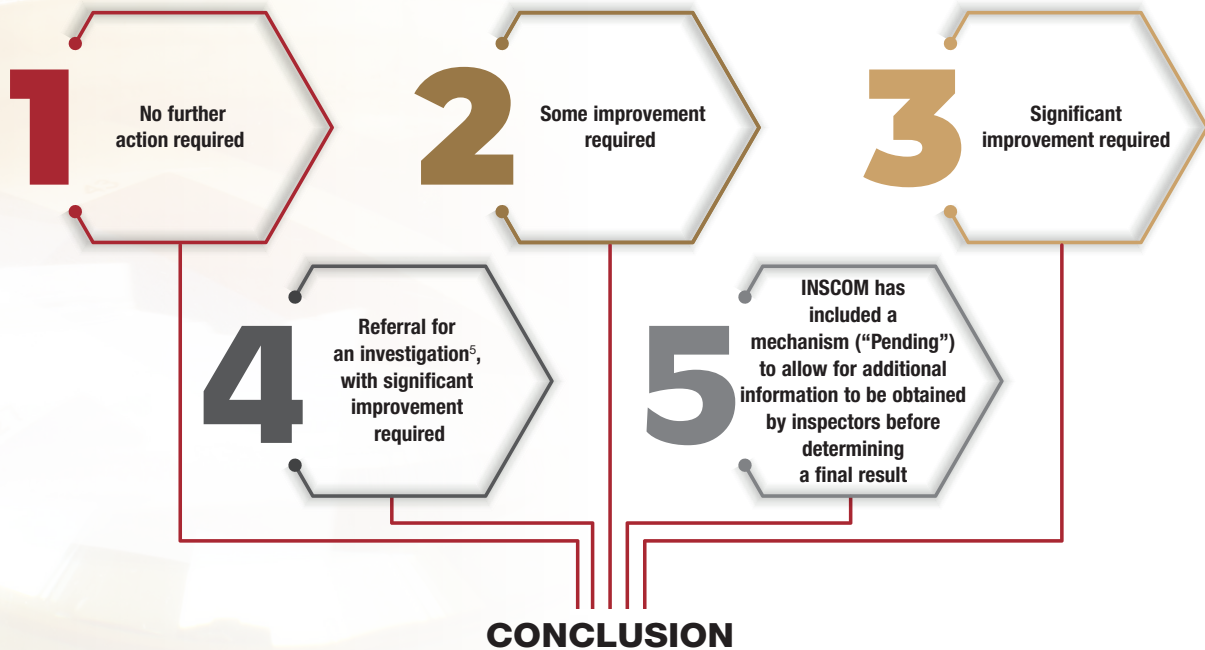


Figure 3: The committee's decision outcomes

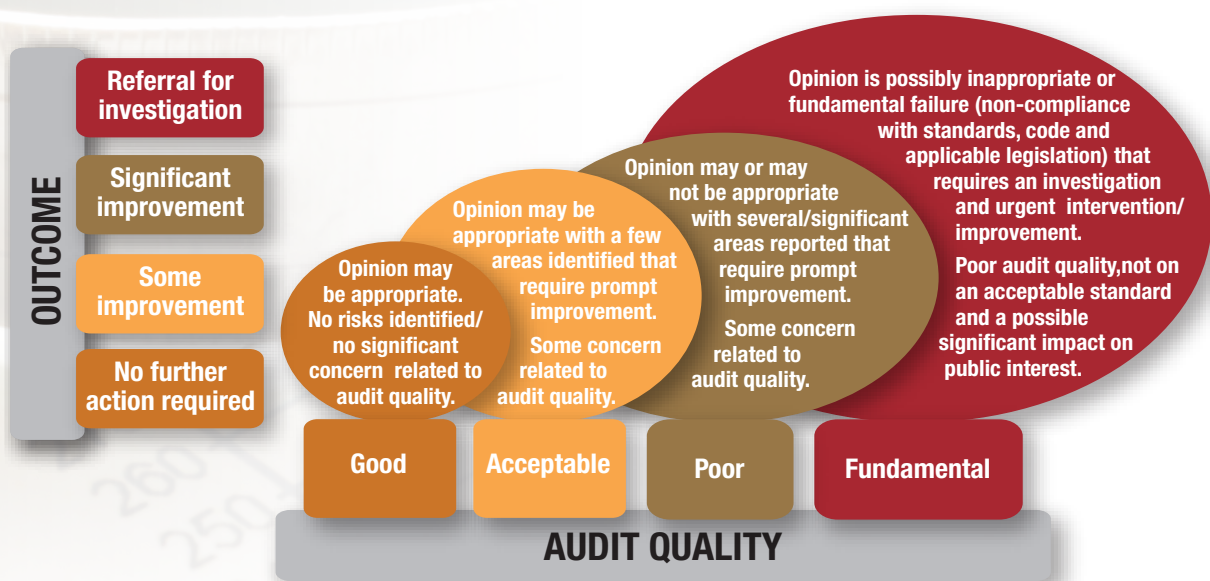


Figure 4: Outcome vs audit quality

In addition, the committee may implement more proactive and strict decisions, where deemed necessary, e.g. conditional results that require more specific proactive action by firms; being subjected to a more robust and focused remedial action process; or escalating poor performing firms with systemic failures to the Board for it to take appropriate action to protect the public interest. Such action from the Board may include withdrawing the firm's registration, escalating concerns to all structures of leadership, as well as requesting and monitoring the audit firm's turnaround strategies and plans on a quarterly basis.

9.7 REPORTING

9.7.1 Preliminary Inspections Report

A PIR is issued to the firm/engagement partner and discussed, followed by an opportunity to provide succinct and complete written comments (which must, as far as possible, be supported by accompanying documented evidence) and submit these separately on the firm's letterhead (PDF version) together with a separate MS-Word version (to allow for anonymisation) within the prescribed timeframe. Firms/practitioners should not wait for the final formal report before responding.

The written comments to the PIR are the only opportunity available to the firm/practitioner to formally respond in writing. The comment letter must be numbered exactly in the same way as the PIR reportable deficiencies and must be signed by the relevant engagement partner and the firm's appointed quality control representative (or equivalent). The firm/engagement partner's comment letter will then be attached to the formal inspections report and its content should, as far as possible, be anonymised.

The PIR is subjected to the IRBA's internal quality control process. While it is also subject to change, in some cases additional reportable deficiencies may be raised later in the process; and when that is the case, that will be duly discussed and communicated.

9.7.2 Formal Inspections Report

The final formal inspections report – including INSCOM's decision on any required action/conditions; the inspection scope; key themes and risks; any firm level reportable deficiencies; and any engagement level reportable deficiencies, with the firm/engagement partner's written comment letters attached – will be formally reported to the firm leadership by the Director Inspections. Since firm leadership is ultimately responsible for ensuring consistent, sustainable high-quality audits and the remediation of deficiencies at their firms, all

inspections reports will be directed to the firm's Chief Executive Officer (or equivalent).

The firm/engagement partner is expected to study the report and address any required action/conditions as soon as possible; and, where required, start the process to identify the root causes and implement remedial/corrective action on all subsequent audits and then monitor this. The report, which is anonymised as far as possible, is written with the users in mind, and these may include the firm leadership, engagement partner/team, the INSCOM and other relevant users that include audit committees or other regulators.

Since quality control and remediation is an ongoing process of the firm, a firm/engagement partner may receive multiple inspections at different times during a cycle. In addition, separate formal inspections reports will be issued to the firm/engagement partner after every visit and these will supersede or supplement any reports previously issued. Any issued report to the firm/engagement partner will clearly spell out the scope, assurance engagement/s, disclaimer, reportable deficiencies, responses and decisions by the INSCOM.

The scope of an inspection visit may not necessarily be the same every time and may or may not include a firm level quality control/management inspection; so, the formal report should be read in that context. As a result, any previous firm report (in particular the firm executive report) and the related INSCOM decision letter remain relevant to the extent that the previously reported deficiencies would have been subjected to the firm's internal quality improvement process and successfully remediated.

9.7.3 Special Paragraphs

The INSCOM, from time to time, deems it necessary to focus a firm/engagement partner's attention to specific matters, including matters that are not necessarily reported as a finding in the formal inspections report. These specific messages are communicated together with the formal inspections report in the form of special paragraphs. These specific messages do not constitute additional reportable inspection deficiencies, but are rather other matters or general observations that the committee deems important to bring to the firm's attention.

Reportable deficiencies (if any) are reported in the formal inspections report that forms the basis of INSCOM's decision on any required action/condition; and they should be read with any special paragraphs that are stated in the formal inspections report. Special messages to the firm/engagement partner will be considered in subsequent inspections and

might lead to reportable deficiencies, if not appropriately addressed.

9.7.4 Public Inspections Report

Annually, the Inspections Department issues a public inspections report that provides an analysis of key finding themes arising from inspections performed during a particular year. These reports are available on the IRBA website and auditors are encouraged to analyse them and proactively identify and address similar reported deficiencies that might exist in their respective firms.

The objective of the reports is to promote audit quality at a broader level by highlighting significant themes arising from firm-wide and individual assurance engagement file inspections reported on annually. Each report is aimed at auditors and those responsible for quality management systems within firms as well as other relevant stakeholders, such as audit committees, investors, oversight bodies, company directors and financial accountants, who are responsible for the integrity of financial information. The intention is to assist these stakeholders – audit committees, in particular – in their respective roles by encouraging robust discussions regarding matters that affect audit quality, and as reported by the IRBA.

The 2021 Public Inspections Report will reflect on observations made on audit quality during the entire 7th Inspections Cycle (1 April 2018 to 31 March 2021). In line with previous reports, the 2021 Public Inspections Report will detail audit quality deficiencies and themes identified on firm and engagement file levels, highlighting the impact that these deficiencies have on both the public interest and the efforts made in restoring confidence in the profession.

The IRBA encourages firms and practitioners to reflect on these results in order to strengthen their own audit quality processes, including proactive remediation initiatives to improve audit quality. Also, the IRBA will analyse the results to measure the effectiveness of audit firms' remediation processes, and enhance our firm level inspections reports in a manner that allows firms and stakeholders to be more responsive to inspection results.

9.8 EVIDENCE-BASED RECONSIDERATIONS

A firm/engagement partner that believes INSCOM's decision should be reconsidered, due to the committee's initial decision not being based on sufficient documented evidence or related information available at the time, may submit a written request to the Director Inspections for reconsideration. This

request must be clearly headed as a "request for reconsideration" and should be submitted within 30 calendar days from the date of the formal inspections report. Only if sufficient evidence-based documentation is presented that warrants a change to INSCOM's original decision will the anonymised request be tabled before the committee at its next meeting. The committee's final decision will be communicated to the firm/engagement partner in writing by the Director Inspections.

10. REMEDIAL ACTION PROCESS

In a continuous effort to meet the objectives of the IRBA and improve audit quality, as stated in point 1 above, the Inspections Department will continue to drive a formal Remedial Action Process during the 8th Inspections Cycle with firm leadership and relevant engagement partners. Inspected firms/engagement partners that have received inspections reports with reportable deficiencies are requested to analyse all the reportable deficiencies and submit to the IRBA a Root Cause Analysis and an action plan within 30 calendar days from the date of the formal inspections report, with a written undertaking that all deficiencies that were reported will be addressed by the firm, on all of its audits going forward.

After a reasonable time allowing for corrective measures to be implemented by the firm and engagement partners, an inspection, including a follow-up inspection, may be performed to look into previously reported reportable deficiencies and assess the effectiveness of the remedial/corrective action undertaken by the firm. This process can be highly effective and yield the necessary improvements, if firm leadership assumes ultimate responsibility for quality and approaches the remediation process constructively by developing and implementing appropriate remedial action plans and strategies based on effective root cause analyses.

Firms and engagement partners must recognise that remediation of inspection reportable deficiencies forms part of a firm's process of continuous improvement. Further, remediation should happen continuously on all internal and external reportable deficiencies and not only when deficiencies are identified during the IRBA inspections.

The IRBA's remedial action process feeds back into the Business Intelligence and inspections processes for follow-ups, to determine whether the firm remediated previously reported deficiencies in terms of its root cause analysis and remedial action plan. A failure to remediate reportable deficiencies throughout

the firm may indicate that the firm's system of quality improvement is ineffective, which may result in a firm level inspection finding. Such reportable deficiencies, which are seen in a very serious light by the regulator and stakeholders, may be raised based on a firm's failure to cooperate with the regulator, demonstrating an inability or reluctance to promptly and effectively remediate previously reported inspection reportable deficiencies, as required by the standards and the IRBA's remedial action process.

Therefore, it is critically important for firm leadership to set the correct tone at the top, promoting an internal culture of high audit quality that is supported by prompt and effective remediation of identified root causes and deficiencies, based on structured problem-solving principles.

11. INSPECTIONS COMMITTEE

The committee consists of a maximum of eight (8) suitably qualified and experienced members who are not directly or indirectly involved in public practice and are not members of the IRBA's Investigating Committee, Disciplinary Advisory Committee or Disciplinary Committee.

The committee's function is to independently participate in the inspections process by:

- Monitoring the progress of the inspections cycle;
- Considering whether the inspections reports and recommendations are consistent and of an appropriate quality (on an anonymous basis);
- Considering the recommendations made by the IRBA's Inspections Department and determining the outcome of inspections; and
- Providing guidance to and advising the Inspections Department on its strategy, challenges and contentious matters.

The committee meets at least four (4) times in a calendar year, and these meetings are closed to the public and RAs, without exception, due to confidentiality requirements.

12. FEES

Specific fees are charged, in addition to the normal fees charged by the IRBA, for the following:

- Any ad-hoc work performed by the Inspections Department to external stakeholders (not RAs), based on the actual time spent, and this is at an hourly rate that is determined and gazetted by the Board from time to time, and disbursements recovered at cost.
- Cancellation fees may be charged where scheduled inspections are cancelled at short notice by the audit firm/engagement partner without an acceptable reason that can be corroborated. The cancellation fee must be reasonable in relation to the size of the firm or the RA's assurance portfolio, and be subject to the Director Inspection's discretion and approval.

13. CONFIDENTIALITY

The confidentiality requirements of Section 47 of the APA are strictly respected and enforced by all staff within the Inspections Department.

14. OTHER

Given the pandemic and the greater focus on online learning and remaining up to date with Continuous Professional Development (CPD), the Inspections Department will collaborate with the IRBA's Education and Transformation Department to assess the RA's CPD compliance. The Inspections Department will also monitor the inspections outcomes at audit firms, to evaluate whether there is a need for CPD monitoring as part of the Human Resources pillar in ISQC 1 and the Resources component in ISQM 1.



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