

2016-2017 Professional inspection committee annual report

Journey to excellence

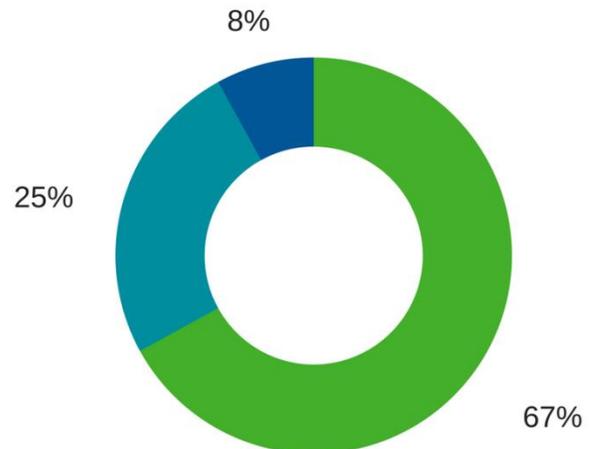
The Professional inspection committee (hereafter “the committee”) plays a key role in protecting the public in a constantly changing environment. Through the inspection process, the committee helps members excel to ensure they are consistently recognized for their integrity, skills and leadership.

Following the 2016-2017 inspection process, the information below was collected and compared to inspection results from previous years to highlight certain trends and provide practitioners with ideas on improving file quality.

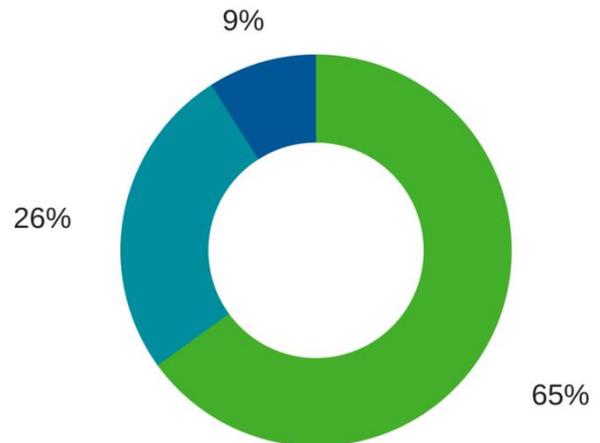
Key trends since 2013

- Little improvement required
- Some improvement required
- Significant improvement required

2016-2017



2015-2016



■ Little improvement required
 ■ Some improvement required
 ■ Significant improvement required

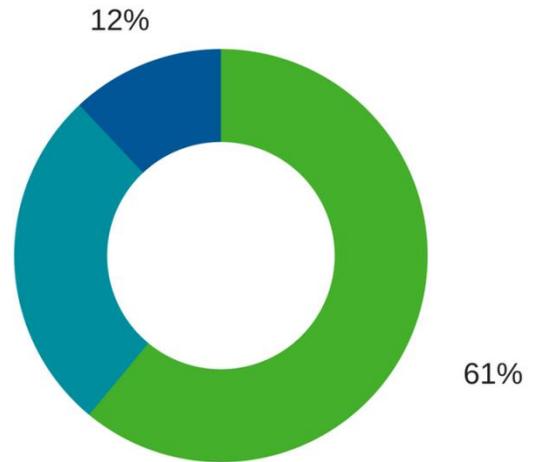
2014-2015


772
 firms inspected


3,076
 files inspected

AUDIT	619
REVIEW	1,124
COMPILATION	1,243
OTHER	90

27%

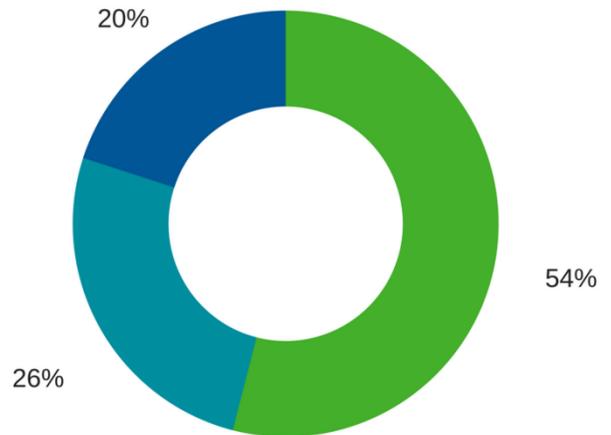


2013-2014


828
 firms inspected


3,326
 files inspected

AUDIT	754
REVIEW	1,217
COMPILATION	1,272
OTHER	83



Analysis of inspection results

The steady improvement over the years testifies to our members' remarkable efforts to provide their clients with high-quality services. The committee wishes to acknowledge this strong commitment to excellence.

Nonetheless, the inspections carried out in 2016-2017 revealed new and persisting deficiencies, as briefly summarized in the annual report below. See Appendix A for a comparative summary of deficiencies identified in 2016-2017 and 2015-2016.

Canadian Auditing Standards

With the advent of the digital age and a global economy, our members are faced with complex accounting situations such as understanding new business methods and governance structures, as well as the existence of significant accounting estimates. This new reality has given rise to several deficiencies in the application of the following standards:

- > **Application of CAS 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.**
Members should pay special attention to the ownership and governance structure, industry and regulatory factors, as well as the entity's objectives, strategies and performance factors. The emergence of new business models (e.g. online sales and electronic payments), new laws and organizational structures has made the work much more complicated. Which is why a good understanding of all these factors is key to performing an effective audit.
- > **Application of CAS 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*.**
Management accounting estimates have always existed and always will. However, business process diversification, complex contracts and market convergence make auditing these estimates much more difficult. Therefore, our members must go back to square one, ensure that they understand and document the client's accounting estimate process, determine the degree of uncertainty and risks, and identify indicators of possible management bias. To learn more, read the CPA Canada [alert](#) on the application of CAS 540 and participate in the [webinar](#) explaining upcoming changes to this standard.

In addition, there are **some recurring deficiencies**, including:

- > **Evaluation of the design and implementation of controls relevant to the audit.**
CPA Canada issued a [bulletin](#) explaining the concept of controls relevant to the audit and the function of a walk-through.
- > **Application of CAS 520, *Analytical Procedures and more specifically substantive analytical procedures*.**
Substantive analytical procedures are effective if the financial statement items to which they apply are sufficiently predictable, the reliability of the data used has been assessed and variances requiring additional procedures are appropriately corroborated.

Canadian Standards on Review Engagements

The most commonly reported deficiency in review engagements relates to inadequate documentation of analytical procedures, especially on income statement items where changes are calculated without any comments. This deficiency recurs year after year, often requiring significant remedial action. Remember that undocumented procedures are considered not to have been performed.

Documenting the plausibility of these items is not easy. Here, for example, is a list of potential analyses to facilitate documentation and help conclude on plausibility:

- > changes to key financial ratios and key performance indicators;
- > changes in sales (overall) and sales by function (e.g. product line, geographic region, etc.);
- > a comparison of sales by month and/or sales by customer to prior periods;
- > sales returns, credit memos, etc., as a percentage of sales;
- > gross margins (overall) and gross margins by function.

The effective date of new review standard CSRE 2400 *Engagements to Review Historical Financial Statements* is fast approaching and the standard is applicable to your clients with fiscal years ending after December 14, 2017.

To help you prepare for the application of this standard, we invite you to read the [guide](#) on performing review engagements in accordance with the new standard and to keep an eye out for training activities offered by the Order or other organizations in your area.

Compilation engagements

One of the most common deficiencies reported in compilation engagements is an undocumented agreement between a client and member. The best way to clarify engagement terms and avoid any misunderstanding is to make sure they are documented.

A [task force](#) is currently exploring possible changes to compilation engagement standards, so we encourage you to watch for developments in this area and issue your comments in due course.

Canadian Standards on Quality Control

The committee reminds you that the implementation of a cyclical inspection process is mandatory and must cover at least one completed assurance engagement for each engagement partner and cannot be performed by a member who worked on the engagement.

Financial reporting

One of the most common financial reporting deficiencies identified relates to the classification of liabilities as current or long-term on the balance sheet.

Advances from related companies or shareholders are subject to the same classification criteria as any other liability. For advances reported as long-term, the related company or the shareholder must have waived the right to demand repayment of the debt for a period of more than one year.

Root causes

The following are the causes of the main deficiencies identified that most concern the committee:

1. Acceptance of engagements when a firm does not have the required knowledge.

Before accepting an engagement, it is crucial to have a good knowledge of the standards, industry, laws and regulations and control environment of the entity that is the subject of the engagement (for instance, accepting a business valuation engagement without sufficient knowledge of the [related standards](#)).

2. Client familiarity or mismanagement of unexpected events resulting in less documentation of procedures performed.

We remind you that anything that is not documented cannot be considered as performed. In addition, for sound management, it is imperative to have a backup plan to cover the unexpected (illness, accident, etc.) and maintain the quality of the work, including compliance with filing deadlines.

3. Deficient quality control structure resulting in the issuance of inappropriate special reports.

Members are responsible for putting in place control structures and the necessary mechanisms to ensure that engagements meet the profession's standards.

In this regard, please read the [caveat](#) issued by the Order on requests to file special reports.

Watch for

1. Changes to standards on the independent auditor's report

The new auditor's report will usher in a new age of transparency. The standards will be adopted shortly—for more information, see the [update](#) issued by the Auditing and Assurance Standards Board (AASB).

2. The digital age

The use of new technologies and technology-based media is a significant challenge for the profession, particularly for regulatory and ethical aspects. This will bring changes to certain regulations and the profession as a whole. In its latest strategic plan, the Order prioritizes this new issue. Please use the [self-](#)

[diagnosis](#) tool prepared by the Order to assess whether your practices are current and watch for the impending release of a guide on IT good practices.

Conclusion

The inspection process is a public protection and member training and guidance mechanism. As the inspection results show, there has been a steady improvement in file quality. However, the pursuit of excellence is a long journey bringing one challenge after another, and we must continue to move forward together.

To learn more about the inspection process, the program's evaluation criteria, remedial actions, as well as the tools and reference material available to members, please consult the [Professional inspection](#) section on the Order's website.

Questions?

Please contact the Professional Inspection team by phone at 514 288.3256 [2565] or toll-free at 1 800 363.4688, or by email at inspection@cpaquebec.ca.

Appendices

Appendix A: List of most common deficiencies

Appendix B: Files forwarded to the syndic

Appendix C: Tools and reference material

Appendix A – Most frequent reportable items in 2016-2017

The most severe reportables that may result in follow-up or remedial action are identified by the symbol †.

FINANCIAL REPORTING

	Percentage of units for which reportable was recorded	Change vs 2015-2016
<p>The entity did not disclose the following information about its transactions with related parties: a description of the relationship between the transacting parties; a description of the transaction(s), including those for which no amount was recognized; the recognized amount of the transactions classified by financial statement category; and amounts due to or from related parties and the terms and conditions relating thereto.</p> <p><i>Part II 3840.51</i></p>	26%	↓3%
<p>† A debt payable on demand or within one year from the balance sheet date was classified incorrectly as a long-term liability.</p> <p><i>Part II 1510.10, 1510.12 et 1510.13</i></p>	19%	↓ 1%
<p>The entity issued preferred shares in a tax planning arrangement, but failed to present the shares as a separate line item in the equity section of the balance sheet, provide a suitable description indicating that they are redeemable at the option of the holder, and disclose on the face of the balance sheet, the total redemption amount for all classes of such shares outstanding.</p> <p><i>Part II 3856.23 et 3856.47</i></p>	9%	↓ 7%
<p>The entity did not disclose the following about issued share capital: a brief description of the shares for each class, dividend rates on preference shares and whether or not they are cumulative, and the redemption price of redeemable shares.</p> <p><i>Part II 3240.20</i></p>	8%	↓ 1%
<p>For financial liabilities, the entity did not disclose the carrying amount of assets pledged as collateral for liabilities.</p> <p><i>Part II 3856.44</i></p>	6%	↓ 4%

CANADIAN AUDITING STANDARDS (CAS)

	Percentage of units for which reportable was recorded	Change vs 2015-2016
<p>The auditor did not communicate with those charged with governance an overview of the planned scope and timing of the audit (mandatory for all audit engagements).</p> <p><i>CAS 260, para. 15</i></p>	20%	↓ 3%
<p>⚡ When obtaining an understanding of controls that are relevant to the audit, the auditor did not evaluate the design of those controls and determine whether they were implemented.</p> <p><i>CAS 315, para. 13</i></p>	20%	↓ 3%
<p>The auditor did not document the reasons for concluding that the presumption that there is a risk of material misstatement due to fraud related to revenue recognition is not applicable in the circumstances of the engagement.</p> <p><i>CAS 240, para. 47</i></p>	19%	↓ 1%
<p>The auditor's report was dated earlier than the date on which those with the recognized authority asserted that they took responsibility for the financial statements on which the auditor was reporting.</p> <p><i>CAS 700, para. 41 et A38-A41</i></p>	18%	↑ 7%
<p>⚡ The substantive audit procedures performed on the following material classes of transactions and account balances were not documented:</p>		
<p>a) revenues (completeness, occurrence, accuracy, cut-off);</p>	13%	↓ 3%
<p>b) expenses (completeness, occurrence, accuracy, cut-off);</p>	4%	↓ 5%
<p>c) accounts payable cut-off – search for unrecorded liabilities (completeness);</p>	9%	↑ 3%
<p>d) payroll (completeness, occurrence, accuracy);</p>	9%	↑ 3%
<p>e) loans/notes receivable – collectability (completeness, valuation);</p>	5%	stable
<p>f) GST and QST paid – procedures on amount received and paid in the year</p>	6%	↑ 1%
<p>g) inventory (existence, rights and obligations, completeness, valuation).</p>	3%	↓ 1%
<p><i>CAS 330, para. 18,25-28 and 30, and CAS 500, para. 6</i></p>		

CANADIAN REVIEW ENGAGEMENT STANDARDS

	Percentage of units for which reportable was recorded	Change vs 2015-2016
<p>‡ The enquiry, analytical procedures and discussion employed to establish the plausibility of the information being reported were not documented with respect to:</p> <p>a) revenue, direct costs, gross margin and expenses;</p> <p>b) GST and QST;</p> <p>a) subsequent events;</p> <p>b) inventory – the client’s count procedures, assessment and review of the lists (quantities, prices, calculations);</p> <p>c) loans/notes receivable – collectibility;</p> <p>c) sales (accounts receivable) and purchase (accounts payable) cut-off procedures.</p> <p><i>Para. 8100.15 et .19-.24, 8200.23 and AUG-20</i></p>		
	16%	↓ 5%
	17%	↓ 1%
	36%	↓ 9%
	12%	↑ 1%
	15%	↑ 3%
	11%	↓ 3%
<p>The date of the review engagement report was not documented in the file and, therefore, there was no indication of compliance with the requirements regarding approval of the financial statements by those with recognized authority.</p> <p><i>Para. 8100.30 and NOV-47</i></p>	36 %	↓ 1 %
<p>There was no documentation indicating that the review engagement was adequately reviewed by the engagement partner on or before the date of the report.</p> <p><i>Para. 5030.26, 5030.32, 5030.33 and 8100.15</i></p>	7%	stable
<p>The engagement letter did not cover all the matters required by Section 8200 or there was no indication in the file that the public accountant had come to a written agreement and understanding with the client as to the services to be provided.</p>	6%	↓ 5%
<p>The representation letter did not cover all the matters required by Section 8200 or no representation letter was obtained from the client.</p>	5%	↓ 5%

COMPILATION ENGAGEMENTS

	Percentage of units for which reportable was recorded	Change vs 2015-2016
The Notice to Reader was not worded in accordance with the requirements of Section 9200 (the former wording of the Notice to Reader was used, wrong terminology). <i>Para. 9200.25 and .26</i>	11%	↓ 4%
There was no indication in the file that the public accountant had reached an understanding and agreement with the client as to the services to be provided. <i>Para. 9200.16</i>	8%	stable

CANADIAN STANDARD ON QUALITY CONTROL (CSQC1)

	Percentage of units for which reportable was recorded	Change vs 2015-2016
‡ The firm's system of quality control did not include a cyclical inspection of at least one completed engagement for each engagement partner. <i>CSQC 1, para. 48</i>	15%	↓ 4%
The firm did not perform an ongoing consideration and evaluation of the firm's system of quality control. <i>CSQC 1, para. 48</i>	12%	↑ 2%

Appendix B – Files forwarded to the syndic

CODE OF ETHICS OF CHARTERED PROFESSIONAL ACCOUNTANTS AND CANADIAN HARMONIZED RULES OF PROFESSIONAL CONDUCT

Most common departures

- > Potential breach of section 22.1 of the **Code of ethics of CPAs** requiring a member who is responsible for issuing a report or an opinion in the practice of public accountancy, other than compilation engagement reports that are not intended solely for internal management purposes, to include his name or permit number on such report or opinion.
- > Potential breach of section 21 of the **Code of ethics of CPAs** stipulating that a member who performs a contract, in whole or in part, in the practice of his profession, assumes full personal civil liability arising therefrom, regardless of his status within the partnership or company, and is forbidden to include in such contract any clause to the effect of directly or indirectly, fully or partially, excluding this liability.
- > Potential breach of rule 204.8 of the **Canadian Harmonized Rules of Professional Conduct** requiring a member engaged in the practice of public accounting who provides a service not subject to the requirements of rules 204.1 to 204.7 to disclose any activity, interest or relationship which, in respect of the engagement, would be seen by a reasonable observer to impair the member's or firm's independence such that the professional judgment or objectivity of the member, firm or a member of the firm would appear to be impaired.
- > Potential breach of rule 204.4.23 of the **Canadian Harmonized Rules of Professional Conduct** requiring a member who performs an assurance engagement to obtain approval from management of the entity when preparing journal entries.

CHARTERED PROFESSIONAL ACCOUNTANT ACT

Most common departures

- > Potential breach of section 62 requiring that the member must use the title of "CPA, CA", "CPA, CGA" or "CPA, CMA" until May 16, 2022.
- > Potential breach of section 4 which provides specifics on the practice of the chartered accountancy profession, more specifically, the professional activity reserved to CPAs and how to report on the engagements performed (member's signature).
- > Potential breach of section 7 requiring members who hold a public accountancy permit and engage in the professional activity described in the third paragraph of section 4, except the performance of compilation engagements not intended exclusively for internal management purposes, to use the title "auditor." The title of auditor must be preceded by the title "chartered professional accountant" or the abbreviations or initials that refer to that title.
- > Potential breach of section 65 which stipulates that a member of the Ordre des CGA or the Ordre des CMA must use the title "auditor" in accordance with section 7 or sections 62 and 63, as applicable, adding an explicit indication that the practice of public accountancy is limited to the field in which the permit holder is authorized to practise.

Appendix C – Tools and references

Tools and reference material published by the Inspection and Professional Practice Vice-Presidency

- > [2016-2017 semi-annual report](#)
- > [2015-2016 annual report](#)
- > [2014-2015 annual report](#)
- > [Using Canadian Auditing Standards \(CASs\) to your advantage](#) (article)
- > [Audit of salaries](#) (article)

Other tools and reference documents (free)

QUEBEC CPA ORDER

cpaquebec.ca

- > [Expert advice and resources](#) (Financial accounting and assurance/Taxation, taxes and financial planning). Please note that the following CPA Canada publications are reproduced in this section:
 - Audit and assurance alert: [Significant revisions to CPA Canada's Joint Policy Statement \(JPS\)](#)
 - Audit and Assurance Alert: [Canadian Standard on Association](#)
 - Audit and Assurance Alert: [Comparison between CSRE 2400 and the 8000 series](#)
- > [Technical and ethics reference services](#)
- > Training activity: [L'inspection : Soyez-prêts!](#)
- > Webcast: [Regulation respecting trust accounting](#)

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Relevant publications:

- > [Summary comparison of ASPE and IFRS](#)
- > [ASPE briefing: Amalgamations of wholly owned enterprises](#)