

2018-2019 Professional Inspection Review

Highlights and analysis



About the Professional inspection committee

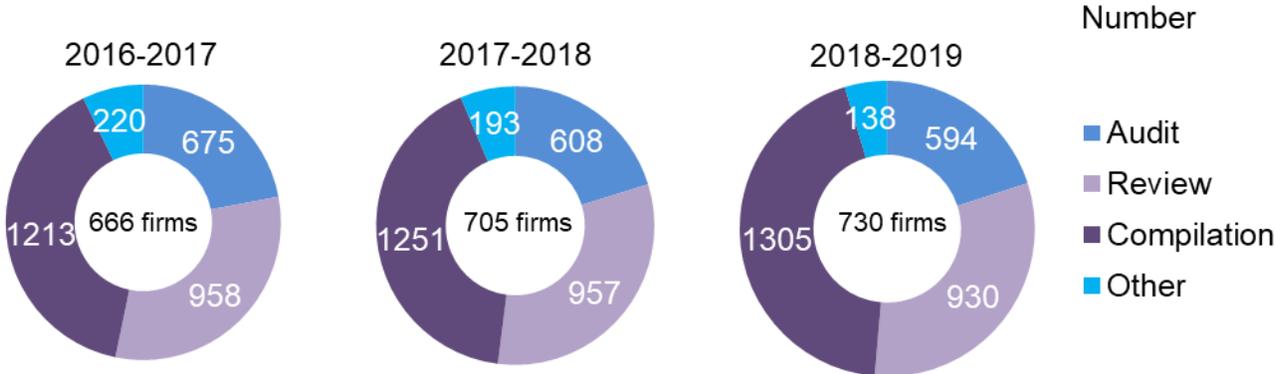
The primary mission of the Professional inspection committee is to protect the public while ensuring Quebec CPAs meet the highest standards of quality. Every visit is an opportunity to guide members in their pursuit of excellence by helping them better comply with the standards of the profession as well as perfect their work methods.

The Professional inspection committee (“the Committee”) has therefore prepared an annual report on the inspection results, including:

- Highlights of 2018-2019 inspection results
- Analysis of areas for improvement
- Practical advice from the Committee
- Tools to assist you in your commitment to excellence

Overview of inspection results

During the 2018-2019 inspection period, we inspected 730 firms compared to 705 firms in the prior period.¹ The number of firms inspected varies from year to year depending on the inspection cycle and the client portfolios of firms inspected.



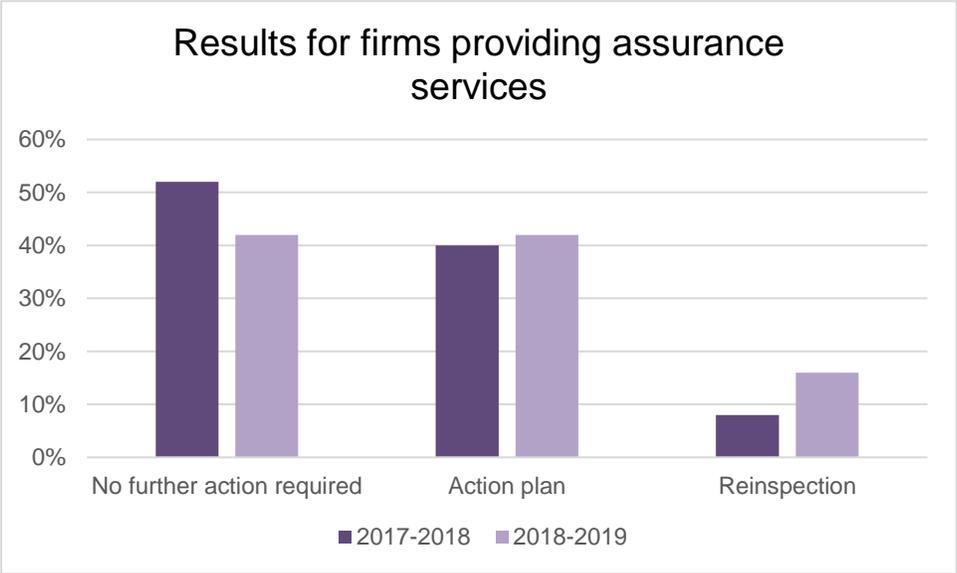
In an evolving context where, among other things, review engagement standards have undergone substantial changes, inspection results continue to illustrate that our members are dedicated to providing high-quality services and deeply committed to continually improving their practice.

¹ The population referred to in this article includes only practising units for which an inspection report has been issued and a decision has been ratified.

Highlights

Ninety-one (91%) percent of the inspected firms met the requirements of the professional inspection program, i.e. a 3% decrease from the prior period. Below is the rate of compliance with the supervision program requirements by type of firm:

- 98% for the 239 firms providing only compilation or other services, i.e. a result similar to the prior period.
- 84% for the 491 firms providing assurance services.
 - 42% met the requirements (52% in 2017-2018)
 - 42% required an action plan (40% in 2017-2018)
 - 16% did not meet the requirements (8% in 2017-2018)



This decrease in the rate of compliance is primarily due to the following factors:

- The implementation of the new review standard CSRE 2400, *Engagements to Review Historical Financial Statements*.
- An increase in the number of significant deficiencies related to insufficient procedures for validating complex or non-recurring transactions.
- An increase in the number of re-inspected firms that failed to meet the requirements. The compliance rate among these firms was 76% compared with 90% the previous year.

Overview of areas for improvement

Several findings recur across multiple inspection reports. In this overview, the Committee presents the deficiencies that most strongly affect quality of work and that generally led to the conclusion that an inspected firm did not meet the requirements or required an action plan. The Committee will continue to work with its collaborators, especially the Continuing Education team, to determine how to assist members in addressing deficiencies identified.

Financial accounting

The Committee is especially sensitive to accounting and financial reporting issues since a significant deficiency can result in issuing false or misleading financial statements. The Committee asks that practitioners be especially vigilant in the presence of the following items.

Complex and/or non-recurring transactions

In this respect, the major challenges facing members are:

- issue identification and assessing the appropriate accounting treatment;
- designing appropriate procedures to obtain a sufficient level of assurance based on the identified risk;
- insufficient expertise and lack of consultation with a quality control reviewer.

Financial liabilities classified as non-current

The misclassification of financial liabilities continues to be one of the most common weaknesses. A number of financial liabilities were classified as non-current, even though reimbursement may have been required within 12 months after the reporting period in circumstances where there were:

- covenant violations;
- loans repayable on demand, including related party loans;
- intended short-term refinancing.

In these circumstances, practitioners must include a waiver from the lender in order to continue supporting the presentation of the liability as non-current.

Assurance engagements

Certain significant deficiencies have been recurring for several years, in both audit and review engagements.

Understanding of the entity and its environment

Audit file documentation, like review engagement documentation, must evidence that the practitioner has acquired an adequate understanding of the entity and its environment to assess the risks and develop sufficient and appropriate procedures to mitigate them.

This understanding must extend to the terms and conditions of contracts the entity has entered into with its customers and suppliers. The unique features of these contracts can have a substantial impact on the recognition of transactions arising from them.

The benefits of a thorough understanding an entity and its environment cannot be overstated. It:

- helps with identifying risk areas;
- assists in developing appropriate audit and review procedures to mitigate the risks;
- serves as a basis for establishing more specific expectations when performing certain analytical procedures.

Practitioner's knowledge of specialized industries

Performing assurance engagements for entities in specialized industries requires a sufficient understanding of the industry in which the entity operates. Among other things, the member must understand the specific legal and regulatory requirements that can impact financial reporting or raise the inherent risk over certain types of transactions.

In general, the deficiencies noted in files involving entities in specialized industries related to insufficient or inappropriate procedures relating to revenue recognition and liabilities, including provisions.

Assessment of the entity's ability to continue as a going concern

The Committee frequently raises deficiencies in files that include events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern. The deficiencies can be addressed by:

- better documenting the assessment of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern;
- performing procedures to assess management's plan of action;
- including appropriate disclosure in the report or ensuring that the notes to the financial statements adequately reflect the situation.

Audit engagements

Sampling

During the period, special attention was paid to the sampling methods used by firms. Sampling was an important issue, as a high proportion of firms do not document whether the sample:

- is representative of the population being tested;
- provides sufficient audit evidence concerning the relevant assertions.

Hence, firms are often unable to demonstrate whether their sample size reduces the sampling risk to an acceptable level. An appropriate sampling method is key to mitigating audit risks, especially in situations where auditors do not place reliance on the controls. Sample size established based on professional judgment does not, in and of itself, relieve the auditor from

documenting how the number of tests provides sufficient evidence based on the characteristics of the population, the risks and materiality.

Review engagements

The main findings specific to review engagements can be grouped into two broad categories:

Implementation of the new review engagement standard – CSRE 2400

Although most firms adequately applied the new Canadian review engagement standard CSRE 2400, the application of the new standard constituted a significant challenge for some members this year. In certain cases, members had not modified their procedures to address the implications of the revised standard. In other cases, the nature and scope of documentation required was insufficient to meet the requirements of the standard.

Analytical procedures

Insufficient or inadequate analytical procedures on income statement items are one of the most common and recurring deficiencies in review engagements, including:

- Weak correlations between non-financial information collected as part of the understanding the entity and changes in financial statement balances.
- Insufficient analytical procedures performed for a new entity due to the lack of comparative information or because the practitioner had little information on the industry.
- Limited explanations provided where entities operated in volatile or unpredictable industries, such as construction.
- Limited analysis of interdependencies between types of transactions and account balances.

To be relevant and help assess the existence of material misstatement, analytical procedures must be sufficiently precise and adapted to the specific context of the entity. Key performance indicators (“KPIs”) the entity uses can provide important clues over account balances and may be worth examining.

Comparing the current year’s results with those of the previous year is generally insufficient to provide limited assurance over balances, especially if this comparison is not tied in with the

changes observed in the nature of the entity's transactions or with the economic trends of its industry.

When inquiry and analytical procedures provide insufficient evidence, further procedures must be performed. Audit procedures may therefore be required in certain circumstances.

Compilation engagements

Again this year, most weaknesses identified in compilation engagements related to the following:

- Incomplete implementation of AuG-16, *Compilation of a Financial Forecast or Projection*. The compilation of future-oriented financial information requires implementing specific procedures included in the guideline.
- The lack of documentation to support the figures and the assumptions and hypothesis underlying the forecast or projection.

Practical advice from the Committee

The Committee encourages members to review their inspection results in order to identify weaknesses in their quality control systems. This will help them establish and implement a personalized action plan and determine the root causes of deficiencies noted.

The Committee notes certain root causes that may explain why certain firms did not meet the requirements of the professional inspection program. The Committee encourages firms to give special attention to these:

- **Engagement acceptance procedures**

These procedures are an essential first step to meeting professional standards and providing quality services. Acceptance procedures should take into account the following factors:

- knowledge of the client, how it is managed and its industry;
- the availability of staff with an appropriate level of experience;
- the potential use of experts or other resources, if applicable;
- consideration of professional risk and engagement risk.

- **File review by the partner**

File review provides partners the perspective necessary to ensure file documentation is complete and sufficient to allow readers unfamiliar with the file to understand major issues and how these were addressed. As a result, it is critical to allocate sufficient time to this important step. Remember: If it isn't documented, it isn't done!

- **Consultation**

The most successful engagement teams regularly consult. Don't go it alone! Consult with your colleagues and the resources provided by the Quebec CPA Order or other experts to help you find answers to your questions.

- **Quality control review**

In general, firms do not sufficiently involve quality control reviewers or do so only superficially. When a quality control review is performed in a timely manner by a suitably qualified and experienced person, such reviews help the engagement team appropriately identify risks and provide an objective perspective on the sufficiency and appropriateness of the audit evidence obtained.

Risk management is the cornerstone of public practice of the CPA profession. The following risk factors related to human resources should not be underestimated:

- illness or disability of key staff members;
- departure of key engagement team members;
- acceptance of new engagements without access to sufficient resources;
- availability of specialized staff or experts.

As these factors have been identified as potential root causes of deficiencies highlighted during the professional inspection, practitioners should consider establishing a detailed plan for managing these contingencies.

Tools to assist you in your commitment to excellence

Maintaining high quality standards allows you to:

- optimize the client experience;
- lower legal and reputational risks;
- facilitate business development;
- consolidate your firm's success.

To assist you in providing quality services on an everyday basis, the Quebec CPA Order offers you a variety of resources, including training activities, tools, guides and templates. Consider the following valuable resources to enhance your knowledge related to some of the deficiencies raised during this inspection period.



GENERAL
RESOURCES

Quebec CPA Order's technical reference service

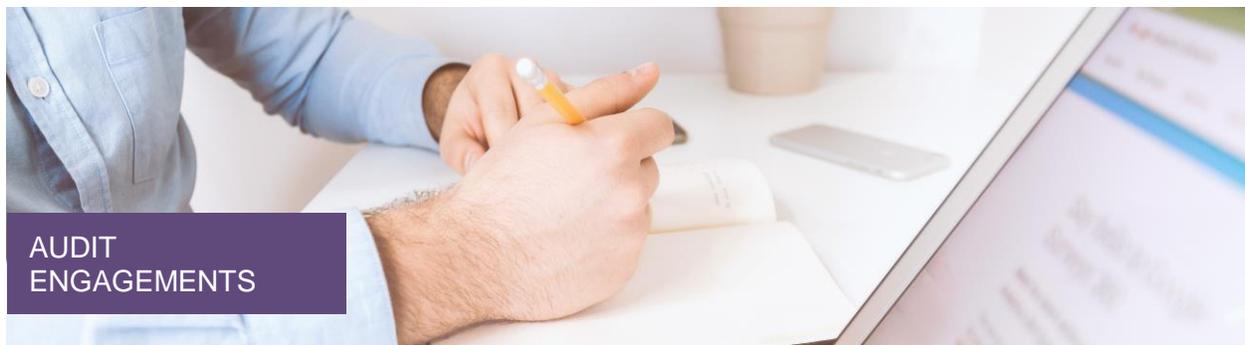
Have questions about accounting and assurance standards in the *CPA Canada Handbook*? We can help you! This service is free and easy to use.

Ethics-related questions

Have questions about the *Code of ethics*? Need guidance on a specific situation? Consult our team. It's easy and free!

CPA Canada's **Guide to Review Engagements** aims to help practitioners conduct review engagements in compliance with CSRE 2400, *Engagements to Review Historical Financial Statements*.

The CPA Canada guide **Reporting Implications of the Canadian Standard on Review Engagements (CSRE 2400)** is intended to promote consistency in practitioners' reports by providing guidance with respect to commonly occurring circumstances.



The Quebec CPA Order's **Atelier pratique – Échantillonnage** (French only) workshop provides best practices for performing audit sampling procedures and for understanding the impact of sampling on audit risk components.

CPA Canada's **Framework for Information Integrity Controls** can help you assess and document your organization's information integrity controls.

CPA Canada's **Implementation tool for auditors: CAS 315 – Understanding the entity through internal control** raises awareness of common pitfalls auditors might encounter when applying certain requirements of CAS 315 as it relates to obtaining an understanding of internal control.

The CPA Canada publication **Implementation tool for auditors: Designing and performing tests of relevant controls** alerts you to common pitfalls auditors might encounter when applying certain requirements of CAS 330, *The Auditor's Responses to Assessed Risks*, as it relates to designing and performing tests of relevant controls.

CPA Canada's **Guide for Auditors: Audits of Not-for-Profit Organizations: Risk Assessment under Canadian Auditing Standards** addresses key issues likely to arise when applying the risk assessment standards set out in CAS in an audit of an NFPO.

The CPA Canada publication **Audit and Assurance Alert: Revised CAS 540, Auditing Accounting Estimates and Related Disclosures** raises awareness about the impact to all auditors resulting from changes to CAS 540, regardless of the size or type of entity whose financial statements are being audited. These revisions are effective for audits of financial statements for periods beginning on or after December 15, 2019.

The *Implementation Tool for Auditors: Information Technology – Why Should Auditors Care?* discusses specific requirements of CAS 330 regarding relevant controls of the entity's information technology (IT) systems and designing and performing tests of their operating effectiveness.



Download CPA Canada's *Accounting Standards for Private Enterprises (ASPE): Summary Resource Guide* for a comprehensive listing of CPA Canada's ASPE resources.

Consult *Accounting Standards for Private Enterprises (ASPE) Briefing: A New Light on Accounting for Investments* for assistance in the application of Sections 1591, 3051 and 3056.

CPA Canada's *Guide to Accounting Standards for Not-for-Profit Organizations in Canada* will help you determine if your organization is a private or government-controlled NFP so you can apply the correct accounting standards.

Download *International Financial Reporting Standards (IFRS): Summary Resource Guide* for a comprehensive listing of CPA Canada's IFRS resources.

Consult the link *IFRS 9 Financial Instruments: External Resources*, where CPA Canada has compiled a list of useful external resources to help you understand and apply IFRS 9 *Financial Instruments*.

Questions?

To learn more about the inspection process, the program evaluation criteria and remedial actions, and access the tools and reference material available to members, please consult the *Professional inspection* section on the Order's website.

For all other inquiries, 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.