



International Forum of Independent Audit Regulators Report on 2013 Survey of Inspection Findings April 10, 2014

Executive Summary

This report summarizes the results of the second survey conducted by the International Forum of Independent Audit Regulators (IFIAR) of findings identified in Members' respective inspections of audit firms, primarily those firms that are affiliated with the largest international audit firm networks. The survey, conducted in 2013, indicates the persistence of deficiencies in important aspects of audits and that there is a basis for ongoing concerns with audit quality. Thirty-eight IFIAR Members contributed to the 2013 survey.

This survey is a follow up to IFIAR's first survey of its membership regarding findings from their inspection programs, conducted in 2012. That survey provided support for what had become evident to IFIAR Members through interaction in IFIAR's various working groups and meeting discussions: Members' individual inspection programs reveal common areas of deficiencies in, and concerns about, audit performance.

IFIAR Members' findings collected in the 2012 and 2013 surveys relate to deficiencies in audit procedures that indicate the audit firm did not obtain sufficient audit evidence to support its opinion; this may include a failure to identify or address a potentially material error in application of an accounting principle. Accordingly, the persistence of inspection findings raises concerns about auditors' satisfactory fulfillment of their role in providing assurance on financial statements. Audit quality is an integral component in investors' and other financial statement users' confidence in the reliability of financial reporting.

The nature of the survey does not provide an adequate basis for quantitative, year-over-year comparison of the quality of audit performance; thus IFIAR cannot conclude from the survey that audit quality has either improved or deteriorated since the previous survey was conducted. Nonetheless, commonality in the types of inspection findings and their significant levels as reported in this survey are of concern to IFIAR Members, individually and collectively. Audit regulators seek improvements in audit performance that would lessen the frequency and severity of inspection findings. Complementary to the efforts of individual Members, IFIAR is engaged with the senior leadership of the largest

international audit firm networks, emphasizing to the firms the need to identify the root causes of the deficiencies identified and the specific actions required to achieve the necessary improvements.

The general approach to the 2013 survey is consistent with that followed for the survey conducted in 2012. Members reported findings from inspections of three categories of audit firm activities—audits of listed public interest entities (PIEs); audits of systemically important financial institutions (SIFIs), including global systemically important banks (G-SIBs); and internal systems for firm-wide quality control. In each category, the survey results generally revealed similarities in the nature and extent of inspection findings as compared to the results of the survey conducted in 2012.

For audits of listed PIEs, the three inspection themes with the highest number of findings were:

- Fair value measurement,
- Internal control testing, and
- Adequacy of financial statements and disclosures.

The first two themes above had the highest number of findings in both the 2013 and 2012 surveys.

For audits of SIFIs and G-SIBs, the three inspection themes with the highest number of findings, consistent with the 2012 survey, were:

- Audit of allowance for loan losses and loan impairments,
- Internal control testing, and
- Audit of the valuation of investments and securities.

Inspections of quality control systems revealed the same three themes with the highest number of findings in both the 2013 and 2012 surveys:

- Engagement performance,
- Human resources, and
- Independence and ethics requirements.¹

The results of this survey will inform IFIAR's collective efforts, described in further detail in this report, to promote audit quality globally, complementary to individual regulators' audit firm inspection and oversight regimes. The recurrence of inspection findings suggests that audit firms should take steps to develop a robust root cause analysis to gain a clearer understanding of the factors that underlie these findings and take appropriate remedial actions.

¹ See Appendix B for a description of these and other elements of a system of quality control, as set forth in international standards.

IFIAR intends to continue monitoring developments in audit quality, including by conducting inspection findings surveys and engaging with the largest international audit firm networks, and expects audit firms to take actions that result in demonstrable improvement in audit performance. By continuing to conduct and publish the results of this survey, IFIAR seeks to inform regulators, investors, others in the financial community, and the public at large of audit oversight activities, as regulators pursue improvements in the reliability of audit firms' work and, consequently, of the opinions they express on financial statements.

Apart from data regarding inspection findings, the 2013 survey also collected general information about Members' oversight inspection regimes. While the nature of the survey does not enable detailed comparisons of Members' regulatory mandates and approaches, the information gathered indicates that most Members require audit firms to register with the regulator and also impose accreditation of audit professionals as a requirement for such registration. A number of Members also require registration of foreign audit firms. A clear majority of Members have enforcement or investigation responsibilities.

I. Introduction

IFIAR is an organization of audit regulators (Members) from around the world that are independent from the audit profession.² At the time of the survey, IFIAR's membership included 46 Members from jurisdictions in Africa, the Americas, Asia, Europe, the Middle East and Oceania. IFIAR focuses on the following activities:

- Sharing knowledge of the audit market environment and practical experience of independent audit regulatory activity with a focus on inspections of auditors and audit firms,
- Promoting collaboration and consistency in regulatory activity, and
- Providing a platform for dialogue with other international organizations that have an interest in audit quality.

In 2012, IFIAR conducted its initial survey (hereafter, the "2012 Survey") of findings resulting from IFIAR Members' inspections of firms affiliated with the largest international audit firm networks.^{3,4} The 2012 Survey demonstrated commonality in the types of deficiencies observed by IFIAR Members in their respective programs to oversee audits of listed PIEs. Recognizing the value of monitoring the nature of inspection findings across IFIAR Members' oversight programs, IFIAR decided to continue to survey

² More information on IFIAR and its activities can be found at <https://ifiar.org/Home.aspx>.

³ For purposes of this survey, a "finding" was defined as an observed audit and/or accounting deficiency that was communicated in writing to an inspected firm in a formal inspection report; a deficiency is a matter with respect to which the firm did not obtain sufficient audit evidence to support its opinion, including a failure to identify or address a potentially material error in an accounting principle. A finding, however, does not necessarily indicate that the financial statements are misstated. This report uses "findings" and "deficiencies" interchangeably.

⁴ See <https://ifiar.org/IFIAR-Global-Survey-Media-Coverage.aspx>.

Members' inspection findings periodically. This report summarizes the results of IFIAR's second inspection findings survey, conducted during 2013 (hereafter, the "2013 Survey").

II. Summary of Survey Methodology

The following is a summary of the methodology followed for the 2013 Survey. Appendix A contains more comprehensive information on methodology.

All IFIAR Members are asked to respond to IFIAR's inspection findings surveys. The 2013 Survey solicited data on Members' findings from inspections of:

- audits of listed PIEs;
- audits of SIFIs, including G-SIBs⁵; and
- audit firms' quality control systems.

Respondents reported findings categorized into 16 inspection themes for audits of listed PIEs. Separately, the survey solicited data on findings from inspections of audits of G-SIBs and other SIFIs, reported using thirteen inspection themes relevant to audits of financial institutions. Findings from inspections of audit firms' quality control systems were reported using six themes. Quality control systems relate to processes and procedures applicable to the overall firm subject to inspection, rather than to specific audit engagements.

Responses primarily, though not exclusively, reflected findings in reports on inspections of the six largest audit firm networks,⁶ as issued during the twelve-month inspection reporting period most recently completed as of the survey response date. In 2013, Members reported data on the number of firms inspected for each inspection theme, whether or not there was a finding.

⁵ SIFIs defined by the Financial Stability Board (FSB), are "listed and non-listed financial institutions whose distress or disorderly failure, because of their size, complexity, and systemic interconnectedness, would cause significant disruption to the wider financial system and economic activity"; financial institutions generally are designated as SIFIs at the national level. As of the time the survey was conducted, the FSB had identified 28 banks as G-SIBs (see http://www.financialstabilityboard.org/publications/r_121031ac.htm).

⁶ The six largest audit firm networks are BDO, Deloitte Touche Tohmatsu, Ernst & Young, Grant Thornton, KPMG and PricewaterhouseCoopers. In certain cases, Members provided data on inspections of those firms, and also of additional firms considered significant in the reporting Member's jurisdiction.

III. Survey Results

A. Respondents

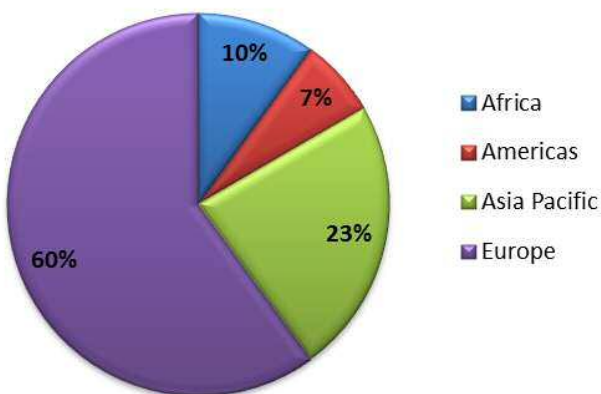
Thirty-eight Members responded to at least one area of the 2013 Survey, an increase from 32 respondents in 2012.



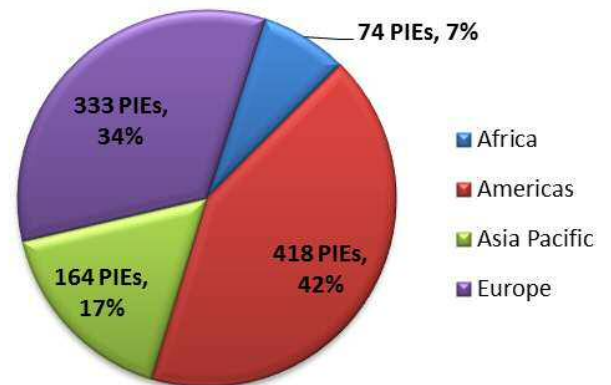
Of the 38 Members providing information, 30 reported data on the number and themes of findings from inspections of audits of listed PIEs and audit firm quality control systems. This is an increase from the prior year’s 22 responses regarding audits of listed PIEs and 23 responses regarding audit firm quality control systems.

Respondents providing data on inspection findings offer representation from all geographic regions with IFIAR Members.

Geographic Distribution of Members Providing Data on Findings from Inspected Audits of Listed PIEs and Firms' Quality Control



Geographic Distribution of Listed PIE Audits Inspected



B. Inspection Findings

Inspection findings are summarized below in line with three inspection categories used for the survey: 1) audits of listed PIEs, 2) audits of SIFIs, including G-SIBs, and 3) audit firm quality control systems.

IFIAR advises readers to consider the survey's information in light of the following limitations. A strictly quantitative, year-over-year analysis of the survey results is not appropriate, for various reasons. There were differences in which Members responded between the 2012 and 2013 Surveys, and the size and extensiveness of inspections programs included or excluded from collected survey data could influence changes in reported findings. Moreover, any individual Member's inspection activities can vary significantly from one year to the next, depending, for example, on its cycle for inspecting firms, choices to focus inspection resources in particular areas, or other unique characteristics of the Member's inspection methodology. The aggregate impact of such variations in individual Members' inspection programs for the year reported could yield misleading indications of trends.⁷ Finally, while individual and aggregate responses are reviewed for reasonableness, IFIAR does not validate the information received, nor does it represent that the data is complete.

Despite these limitations, the recurrence and level of inspection findings themes demonstrated by the survey provide a useful point of reference for discussions about areas for improvement in audit performance. The survey findings support the importance of continued national and international regulatory efforts in pursuit of necessary improvements in audit quality. Section IV of this report summarizes the relevance of the survey results to efforts currently underway within IFIAR.

1. Audits of Listed PIEs

The 2013 Survey revealed similarity in the themes most commonly cited in the 2012 Survey for deficiency. In particular, the three inspection themes individually composing more than 10% of total reported findings in 2013 – fair value measurement, internal control testing and adequacy of financial statements and disclosures – were found with similar relative frequency in 2013 and in 2012.

As described above, the nature of the survey is not conducive to a year-over-year assessment of changes in the quality of auditors' collective performance. However, the recurrence of considerable numbers of findings in key areas of an audit supports the importance of measures underway within IFIAR (discussed further in section IV below) and by national audit regulators to seek improvements in audit quality.

For the 2013 Survey, 30 Members reported findings from inspections of 989 audits of listed PIEs at 113 audit firms (compared to audits of 961 listed PIEs by 98 audit firms for the 2012 Survey). The findings, with comparisons to those reported for the 2012 Survey, are summarized below (**note:** three new categories of inspections findings were added to the 2013 Survey—audit committee communications, fraud procedures, and risk assessment; accordingly, the corresponding information for 2012 is marked "Not Applicable" in the table):

⁷ To note: The survey is not indicative of trends in inspection findings or audit quality in any individual Member jurisdiction.

Listed PIEs: Findings by Inspection Theme

Inspection Themes	Number of Findings Related to Listed PIEs	
	2013	2012
Fair Value Measurement	217	169
Internal Control Testing	156	117
Adequacy of Financial Statements and Disclosures	120	109
Revenue Recognition	104	86
Group Audits	89	75
Engagement Quality Control Review	78	116
Inventory	76	57
Fraud Procedures	65	Not Applicable
Risk Assessment	59	Not Applicable
Adequacy of Review and Supervision	58	115
Audit of Allowance for Loan Losses and Loan Impairments	55	43
Substantive Analytical Procedures	55	75
Use of Experts and Specialists	42	41
Audit Committee Communications	34	Not Applicable
Related Party Transactions	28	44
Going Concern	24	25
	1,260	1,072

A new feature of the 2013 Survey was that Members were asked to report the number of firms for which each theme was inspected, and the number of firms with at least one finding. The following table summarizes the 2013 Survey responses by inspection theme:

Listed PIEs: Number of Audit Firms Inspected and with Findings

Inspection Themes	Number of Audit Firms in which the Topic was Inspected	Audit Firms with at Least One Finding	
		#	%
Fair Value Measurement	98	70	71%
Adequacy of Financial Statements and Disclosures	107	49	46%
Group Audit	98	42	43%
Revenue Recognition	99	42	42%
Internal Control Testing	95	40	42%
Engagement Quality Control Review	86	37	43%
Inventory	91	32	35%
Risk Assessment	98	32	33%
Adequacy of Review and Supervision	86	31	36%
Fraud Procedures	104	29	28%
Substantive Analytical Procedures	92	27	29%
Audit of Allowance for Loan Losses and Loan Impairments	73	25	34%
Use of Experts and Specialists	83	25	30%
Related Party Transactions	86	20	23%
Audit Committee Communications	83	20	24%
Going Concern	89	17	19%

The survey format enables Members to report data on other notable themes identified in their respective oversight programs. The area cited most frequently by Members outside of the surveyed topics was procedures for auditing provisions / reserves.

2. Audits of SIFIs, including G-SIBs

IFIAR’s discussions about audit quality, among Members as well as with the largest audit firm networks, typically address audit matters without distinction by industry. The inspection findings surveys, however, request information specific to SIFIs and G-SIBs as part of IFIAR’s effort to assist the FSB in its consideration of the external audit function in the context of systemic risk in the financial services sector. While findings from financial institution audit inspections are captured in the listed PIE inspection results, IFIAR also separately collects and reports information specific to audits of financial institutions, as summarized herein. While certain themes overlap with those used in the collection of data about listed PIE audits, the survey also includes certain themes with particular relevance to audits of financial institutions.

Thirteen Members provided data for the 2013 Survey on inspections of audits of 95 financial institutions deemed SIFIs or G-SIBs, conducted by 29 firms (compared to audits of 108 SIFIs or G-SIBs by 28 audit firms for the 2012 Survey). The table below categorizes the findings by theme (*note*: five new categories of inspection findings for SIFIs and G-SIBs were added to the 2013 Survey—audit committee communications, use of experts and specialists, substantive analytical procedures, fraud procedures, and risk assessment; accordingly, the corresponding information for 2012 is marked “Not Applicable” in the table).

SIFIs and G-SIBs: Findings by Inspection Theme

Inspection Themes	# of Findings Related to SIFIs and G-SIBs	
	2013	2012
Audit of Allowance for Loan Losses and Loan Impairments	42	15
Internal Control Testing	39	33
Valuation of Investments and Securities	26	32
Insufficient Challenge and Testing of Management’s Judgments and Assessments	21	12
Substantive Analytical Review Procedures	12	Not Applicable
Risk Assessment	10	Not Applicable
Adequacy of Financial Statements and Disclosures	9	4
Group Audits	8	2
Use of Experts and Specialists	8	Not Applicable
Fraud Procedures	7	Not Applicable
Testing of Customer Deposits and Loans	3	10
Audit Committee Communications	2	Not Applicable
Audit Methodology Including Programs and Tools	1	9
	188	117

As with reporting on listed PIE audit inspections, in 2013 Members provided information on the number of firms at which each theme was inspected. The new information supplied provides further insight into the frequency of deficiencies in inspected audits. The following table summarizes finding frequency by inspection theme.

SIFIs and G-SIBs: Number of Audit Firms Inspected and with Findings

Inspection Themes	Number of Audit Firms in which the Topic was Inspected	Audit Firms with at Least One Finding	
		#	%
Audit of Allowance for Loan Losses and Loan Impairments	29	13	45%
Internal Control Testing	28	13	46%
Insufficient Challenge and Testing of Management's Judgments and Assessments	23	10	43%
Valuation of Investments and Securities	22	10	45%
Substantive Analytical Review Procedures	23	7	30%
Risk Assessment	21	7	33%
Fraud Procedures	29	5	17%
Adequacy of Financial Statements and Disclosures	18	3	17%
Use of Experts and Specialists	20	3	15%
Group Audits	17	3	18%
Testing of Customer Deposits and Loans	17	2	12%
Audit Committee Communications	17	2	12%
Audit Methodology Including Programs and Tools	15	1	7%

The survey format enables Members to report data on other notable themes identified in their respective oversight programs. Few Members provided such information. The audit topics not already included in the survey and most frequently submitted include Engagement Quality Control Reviews, independence considerations (e.g., the audit firm providing prohibited non-audit services to an audit client), and provisions / reserves.

3. Systems of Quality Control

Thirty Members provided information relating to their inspections of the audit firms' systems of quality control. The findings are organized using the six defined elements of a system of quality control as outlined in the International Auditing and Assurance Standards Board's International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*.⁸ Appendix B provides the definitions from ISQC 1 of each of these aspects of quality control.

The 30 Members responding to the survey inspected a total of 134 audit firms and reported 844 findings. These findings, compared to 767 findings reported in the 2012 Survey associated with inspections of 109 audit firms, are as follows:

⁸ See IFAC, *2012 Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*, ISQC 1 at <http://www.ifac.org>.

Quality Control: Findings by Inspection Theme

Inspection Themes	Number of Findings	
	2013	2012
Engagement Performance	380	261
Human Resources	146	166
Independence and Ethical Requirements	104	130
Monitoring	93	77
Client Risk Assessment, Acceptance and Continuance	78	100
Leadership Responsibilities for Quality within the Firm (i.e., Tone at the Top)	43	33
	844	767

In 2013, Members provided information regarding the number of firms inspected for each listed aspect of quality control. The following reflects the frequency of findings among firms inspected.

Quality Control: Number of Audit Firms Inspected and with Findings

Inspection Themes	Number of Audit Firms in which the Topic was Inspected	Audit Firms with at Least One Finding	
		#	%
Engagement Performance	134	72	54%
Independence and Ethical Requirements	134	53	40%
Monitoring	134	53	40%
Human Resources	134	50	37%
Client Risk Assessment, Acceptance and Continuance	134	38	28%
Leadership Responsibilities for Quality within the Firm (i.e., Tone at the Top)	134	30	22%

IV. Relevance to IFIAR’s Work

The two IFIAR inspection findings surveys confirm the need for further targeted actions by audit firms to achieve the necessary improvements in audit quality. Individual IFIAR Members take action locally to address issues identified from their specific inspection findings; individual Members have the primary responsibility for improving audit quality and determining the adequacy of remedial actions taken by firms over which they have jurisdiction. IFIAR collectively meets regularly with the leadership of the major firms individually and as a group.⁹

The objective of these meetings with the networks is to provide feedback on specific audit quality issues that IFIAR Members believe require network attention, obtain a better understanding of the networks’ global and/or regional policies and processes that impact audit quality at a national level, and discuss policy matters directly related to audit quality.

⁹ Members of IFIAR’s Global Public Policy Committee (GPPC) Working Group meet to discuss audit quality matters together, as well as with representatives of the six largest audit firm networks. The GPPC Working Group meets at least three times annually with these six network firms on a collective and individual network basis. In addition, the network firms’ respective global CEOs participate in a portion of IFIAR’s annual plenary meetings.

In 2010, through its GPPC Working Group, IFIAR agreed to focus discussions with the audit firms on the networks' efforts to improve the application of professional skepticism,¹⁰ the effectiveness of engagement quality reviews, and the quality with which audits of revenue and group financial statements were executed. The networks responded by developing action plans in 2010; subsequent meetings include updates from the network firms on implementation of, and updates to, the action plans.

Results of IFIAR's inspection surveys allow for a more targeted discussion, calling for more focused responses, on recurring areas of inspection findings. For example, the survey's reported extent of findings related to fair value measurement is relevant to discussions with the firms regarding professional skepticism, whereas deficiencies in testing of internal controls or performing substantive analytical procedures issues could adversely affect audits of revenue recognition, for example. After considering the results of the 2012 Survey, the GPPC Working Group and the six largest international audit firm networks further refined the specific items that the audit firms address in meetings with IFIAR, to also include reporting on their efforts to improve performance in these three areas. In the meetings, IFIAR expects the audit firms to provide information about the results of their root cause analysis, the performance measures used to assess progress, and whether measurable improvements are being made.

IFIAR has challenged the networks to identify and address the root causes of quality issues and to consider how their business processes, models and structures may influence the consistency with which audits are conducted. A common approach for firms' reporting to IFIAR the results of their internal inspection programs is under discussion with the audit firms. Such reporting, together with the results of future IFIAR inspection findings surveys, will assist consideration of the effectiveness of actions taken by the networks to improve audit quality.

IFIAR's Inspection Workshop Working Group organizes and convenes an annual workshop of inspectors involved in IFIAR Members' respective auditor oversight programs. The surveys conducted to date have been featured in these inspection workshops, providing valuable information to inspectors about common themes of inspection findings across Members' programs.

In addition to these examples of the relevance and utility of the survey to IFIAR's current work, the survey may prove useful to other IFIAR activities in the future. For example, understanding the frequency of inspection findings in a particular area may inform IFIAR's Standards Coordination Working

¹⁰ Professional standards require the auditor to exercise professional skepticism when planning and conducting an audit of an entity's financial statements and related disclosures. Professional skepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and performing a critical assessment of evidence. See International Federation of Accountants (IFAC), *2012 Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*, Glossary of Terms, at <http://www.ifac.org>. Individual IFIAR Members may define, and communicate expectations of, professional skepticism in varying ways.

Group’s consideration of projects undertaken by international standard setters to develop or revise auditing or ethics standards.

IFIAR plans to conduct inspection findings surveys periodically in the future, and to continue deepening its dialogue with the largest audit firm networks on measures to improve audit quality.

V. Additional Information

Separate from details of inspection findings, the 2013 Survey collected information regarding various aspects of Members’ respective oversight programs. The results are summarized below.¹¹

Members were asked how frequently they inspect the four largest audit firm networks (the “Big Four”); the next two largest audit firm networks network firms (“Other GPPC Firms”); and other firms.¹² The following table summarizes the frequency of IFIAR Members’ inspections of these three categories of firms.

Type of Firm	Number of IFIAR Members				
	Annually	Every 2 years	Every 3 years	Once every 4 or more years	Do Not Inspect
Big Four Firms	17	7	10	1	4
Other GPPC Firms	8	4	16	4	5
Other Firms	4	0	18	10	4

¹¹ The majority of this information was not collected in the 2012 Survey. Accordingly, comparable information for 2012 is not available.

¹² “Big Four” firms include Deloitte Touche Tohmatsu, Ernst & Young, KPMG and PricewaterhouseCoopers. The next two largest audit firm networks are BDO and Grant Thornton; these audit firms are referred to in the table above as “Other GPPC Firms”, reflecting their membership, together with the Big Four firms, in the Global Public Policy Committee.

The following summarizes responses to questions about Members' regulatory requirements.

Members' Audit Regulatory Requirements

Regulatory Requirements	Yes	No
Do audit firms need to be registered with you?	31	6
Do you impose accreditation or certification requirements of audit professionals as a condition of registration with you?	27	11
Do you require a specific registration exam for auditors beyond general qualifications for accountants?	23	15
Do you require that foreign auditors of PIEs located in your jurisdiction register with you?	10	7
Have you performed inspections of foreign auditors outside your jurisdiction?	5	32
Do you have other requirements before audit firms are allowed to be registered?	22	14
Are you responsible for enforcement?	36	2
Do you have an enforcement division?	26	10
Are sanction determinations publicly disclosed?	24	12
Have you observed standards that have auditability and enforceability issues?	11	23
Do you conduct outreach efforts with constituents (e.g., audit committees, academics, investors, other professionals)?	27	9

In the 2013 Survey, Members provided the following information regarding the number of investigations into possible auditor misconduct that were being conducted in 2012, apart from regular inspections.

Members Reporting Investigations Being Conducted in 2012

Investigation Conducted in 2012	#	%
1-5 Investigations	10	22%
6-10 Investigations	5	11%
11-15 Investigations	0	0%
16-20 Investigations	3	7%
21-50 Investigations	4	9%
>50 Investigations	6	13%
Did Not Respond	18	39%
	46	100%

The 2013 Survey also requested the number of investigations completed during 2012 that resulted in a sanction.

Members Reporting Investigations Resulting in Sanctions in 2012

Investigations Resulting in Sanctions	#	%
1-5 Investigations	27	59%
6-10 Investigations	4	9%
11-15 Investigations	1	2%
>15 Investigations	6	13%
Did Not Respond	8	17%
	46	100%

VI. Conclusion

Two consecutive years’ surveys of IFIAR Members’ inspection findings indicate that auditors still need to improve performance in certain areas for audits of listed PIEs, including major financial institutions. The extent of findings across jurisdictions in the various audit areas demonstrates that audit firms should continue to improve their auditing techniques and also their oversight policies and procedures. The persistence of findings in the same inspection themes suggests that audit firms should take steps to develop a robust root cause analysis to gain a clearer understanding of the factors that underlie the related findings and take appropriate actions to remediate the underlying causes.

Members intend to continue inspecting audits of listed PIEs, including SIFIs and G-SIBs, and to work closely with the audit firms in their jurisdictions to improve audit quality. Members also intend to continue to follow up with the audit firms to evaluate and monitor the audit firms’ remedial actions in response to their respective inspection findings. In addition, IFIAR will continue to work with leadership of the largest audit firm networks to discuss inspection findings and the firms’ strategies and actions to improve audit quality.

The results of this survey will contribute to IFIAR Members’ ongoing work in promoting audit quality through their regulation and inspection of, and engagement with, auditors on both a national and international basis. IFIAR believes that the survey results will be informative to other regulators and policy makers and to those setting standards for auditors. For example, IFIAR will continue to interact with International Auditing and Assurance Standards Board and others, as appropriate, on issues raised through inspections findings.

Finally, IFIAR plans to continue conducting inspection findings surveys periodically, to monitor changes in these findings, with the goal of allowing Members to identify those areas that need improvement and to share experiences about what practices seem to be most effective in reducing audit deficiencies.

Appendix A Survey Methodology

The following describes the methodology followed for the 2013 Survey.

All current IFIAR Members may participate in inspection findings surveys. The 2013 Survey solicited data on Members' findings from inspections of:

- audits of listed PIEs;
- audits of SIFIs, including G-SIBs¹³; and
- audit firms' quality control systems.

Responses generally were limited to findings from inspections of the six largest audit firm networks.¹⁴ Recognizing that an audit firm not affiliated with these six networks may be significant in a jurisdiction, respondents could elect to provide data on findings from inspections of up to three other audit firms.

Member responses were based on findings from inspection reports issued during the most recently completed twelve-month period ended on or before June 30, 2013. Members generally track inspection cycles by twelve-month period; however, their inspection cycles vary. Therefore, while Members' responses reflected inspections that had taken place between October 2010 and July 2013, the findings reported by individual Members should not exceed more than one year's inspection reporting activity for a single audit firm. As a further measure to avoid duplicative reporting of findings, referred work audit engagements performed in support of a group audit were not included in the scope of the survey. Respondents were instructed to exclude from their 2013 data any information provided for the 2012 Survey.

For purposes of the survey, a finding is an observed audit and/or accounting deficiency communicated in writing to an inspected firm through a formal inspection report. A deficiency, for purposes of the survey, is a matter with respect to which the firm did not obtain sufficient audit evidence to support its opinion, including a failure to identify or address a potentially material error in application of an accounting principle.

The 2013 Survey collected data on inspection findings related to audits of listed PIEs, categorized into 16 inspection themes (see section III.B. of the report). Thirteen of these themes are consistent with themes reported in the 2012 Survey. Those themes were included in the 2012 Survey due to their recurrence in reporting by and discussions among IFIAR Members. In the interest of continuity and due to their relevance as affirmed by the 2012 Survey, these themes were repeated in the 2013 Survey.

¹³ *Id* 5. Subsequent to commencement of the 2013 Survey, the FSB published an updated list of G-SIBs that included the addition of one G-SIB and also published a list of nine global systemically important insurers (G-SIIs) (see http://www.financialstabilityboard.org/publications/r_130718.htm); the survey did not separately collect data on audits of these entities.

¹⁴ *Id* 6.

Appendix A Survey Methodology

Three additional themes were added to the 2013 Survey's section on inspections of audits of listed PIEs: audit committee communications, fraud procedures and risk assessment. Members responding to the 2012 Survey were able to provide information on findings for topics other than the thirteen listed, in the event the thirteen designated topics omitted an area of frequent occurrence in a Member's inspection programs. These "write-in" topics in the 2012 Survey resulted in identification of three new themes in the 2013 Survey for audits of listed PIEs. With respect to audits of SIFIs and G-SIBs, the survey collected data on findings for 13 inspection themes, including eight themes used for the 2012 Survey and five new themes for 2013. The six inspection themes for firm-wide systems of quality control were consistent between the 2012 and 2013 Surveys.

The information presented should not be interpreted to imply that each inspection theme was selected by Members for inspection of every audit firm or for every inspected audit engagement. Not all audit engagements inspected had findings; others had multiple findings. Members' individual experiences vary with respect to the frequency of inspected engagements with findings, as well as the relative frequency of findings by inspection theme.

A. Other Information Collected

Separate from data on inspection findings, the 2013 Survey solicited information about Members' oversight program, such as the number of listed PIEs, SIFIs and G-SIBs audited by an audit firm subject to Member oversight; regulatory requirements; and the scope of the Member's regulatory mandate. Section V summarizes information learned from Member responses.

B. Comparison to Prior Survey Methodology

The approach taken to compile the data for the 2013 Survey corresponded closely to that followed for the 2012 Survey. A key change with respect to inspection findings was the addition of three inspection themes for listed PIEs and five for SIFIs and G-SIBs, based on recurring themes that were reported by Members in the 2012 Survey as "other" areas of findings. Further, the survey requested more information on the frequency of inspections of each topic and the number of audit firms associated with findings. Finally, the 2013 Survey expanded the nature of information collected regarding Members' inspection programs, to include information regarding regulatory requirements and the scope of Members' regulatory mandates.

IFIAR intends to reassess its approach for future surveys, to determine whether improvements to the survey would be beneficial.

Appendix B Elements of a System of Quality Control

The 2013 Survey requested data on findings from inspections of audit firms' quality control systems. The categories, or themes, of inspection findings align with the six defined elements of a system of quality control found in the International Auditing and Assurance Standards Board's International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*.¹⁵ However, as Members' inspections are based on their respective requirements and standards, findings reported in the 2013 Survey may be based on definitions or understandings of these themes that are not necessarily based on the exact definitions of the elements of ISQC 1, but may be based on analogous definitions or themes utilized in their respective inspection programs. ISQC1's elements of a system of quality control are summarized below.

Leadership responsibilities for quality within the firm: Each accounting firm is required to establish policies and procedures designed to promote an internal culture recognizing that quality is essential in performing engagements. Such policies require the accounting firm's Chief Executive Officer or Board of Partners (or equivalent) to assume ultimate responsibility for the firm's system of quality control.

Relevant ethical requirements: Each accounting firm is required to establish policies and procedures to provide it with reasonable assurance that the firm and its personnel comply with the relevant ethical and independence requirements.

Acceptance and continuance of client relationships and specific engagements: Each accounting firm is required to establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide the firm with reasonable assurance that it will only undertake or continue those engagements where the firm is competent to perform the engagement and has the capabilities, including time and resources, to do so; can comply with the relevant ethical requirements; and has considered the integrity of the client, and does not have information that would lead it to conclude that the client lacks integrity.

Human Resources: Accounting firms are required to establish policies and procedures designed to provide reasonable assurance it has sufficient personnel with appropriate technical competence, capabilities and commitment to ethical principles to perform engagements in accordance with professional standards and applicable legal and regulatory requirements, and enable the firm or the engagement partner to issue reports that are appropriate in the circumstances.¹⁶

Engagement Performance: Each accounting firm is required to establish policies and procedures designed to provide it with reasonable assurance that engagements are performed in accordance with professional standards and applicable legal and regulatory requirements, and that the firm or the engagement partner issue reports that are appropriate in the circumstances.¹⁷

¹⁵ See IFAC, *2012 Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*, ISQC 1 at <http://www.ifac.org>.

¹⁶ Survey respondents were provided the following examples of Human Resources findings: assignment of the engagement team (e.g., technical competence and expertise); training; evaluation of audit quality as part of partner admissions or partner performance evaluations; and partner remuneration.

¹⁷ Survey respondents were provided the following examples of Engagement Performance findings: consultations; engagement quality control review; and audit methodology and guidance.

Appendix B Elements of a System of Quality Control

Monitoring: Each accounting firm is required to establish a monitoring process designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively.