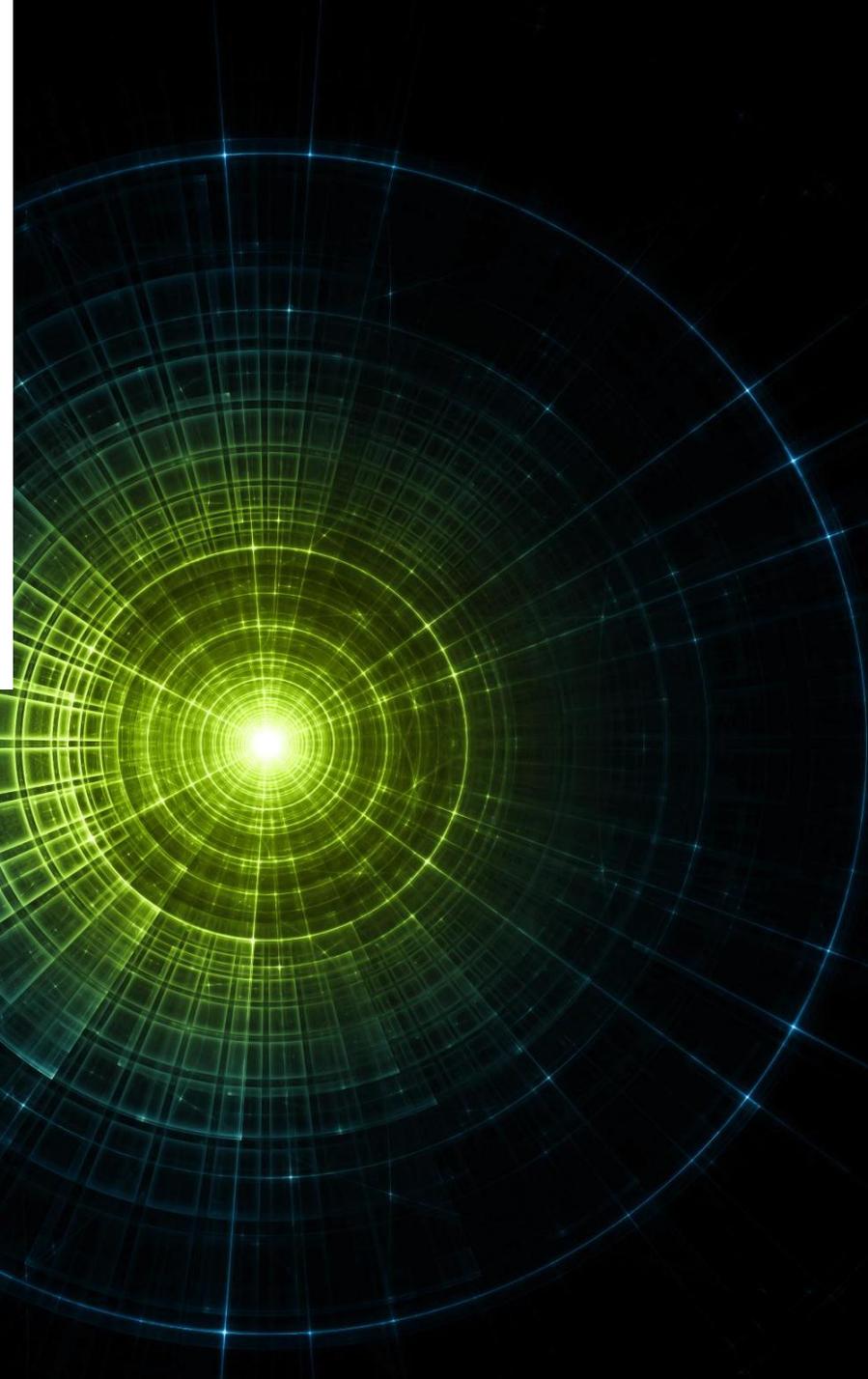


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Improving audit quality to
manage risk

LACPA 19th International
Scientific Congress

Roger Nasr, November 26, 2014



What is audit quality
and how is it defined?

Key talking points on audit quality

Audit quality is a complex subject and there is no analysis of it that has achieved universal recognition

The audit quality framework issued by IAASB, provides an insight into the key elements that create an environment for audit quality

Commitment to pursue professional excellence and achieve the highest audit quality on a consistent basis.

Efficiency is not the opposite of audit quality

A negative quality event can damage the entire audit firm brand

Together, all professionals own audit quality and need to hold each other accountable for the its execution

What is audit quality?

Audit quality means many things

Unwavering focus on **professional excellence** including implementing the **audit imperatives**, addressing client-specific audit **risks**, and leveraging **best-in-class** resources and **innovative** solutions to address the challenges and complexities of clients' businesses and provide them with meaningful **insights**

Outstanding **talented, skilled and experienced** professionals serving clients with **objectivity, integrity and professional skepticism**

Audit quality is exhibited through the audit firm's **organization values, attitude and culture** committed to **excellence**. It is built on the foundation of strong **ethics, independence and professional standards, system of quality control and audit approach**. It means not only delivering audits in **compliance** with relevant laws, regulations and standards but **excelling** at everything we do

Markets, media and investors judge audit quality through **financial reporting failures and fraud**.

Regulators define and judge audit quality in large part based on the outcome of their **inspection process and remediation efforts**

Importance of audit quality

Today, the market, clients and regulators are demanding audit quality and raising the bar



U.S. Securities and Exchange Commission

“Audit committee members believe relationships and a culture of professional skepticism are essential (for audit firms). ... They (Audit Committees) value the breadth and knowledge of global networks... A high-quality audit is the price of protection for Audit Committee members.”

Interviews with 10 leading Canadian Audit Committees, by University of Texas

.....”I worry that audit committees may be focusing too much on the amount of the fee, and not focusing enough on the expected audit quality.”
... “I believe focusing on audit quality is completely consistent with making good business decisions.”

Paul Beswick, SEC Chief Accountant, December 2013

“I want to see the audit profession compete on quality more than price. I imagine you wish for that as well... Standards that give audit committees and the public tools to distinguish on the basis of quality may help you get there.”

James R. Dooley



threadneedle

Regarding EU push for mandatory audit rotation, “the financial crisis has really given impetus to some of the longstanding concerns there have been about audit quality and the audit market.”

Iain Richards, head of governance and responsible investment at Threadneedle Investments, 2014

THE CARLYLE GROUP

“We think (audit) quality needs to be a key metric...when evaluating partner performance or compensation. Firms shouldn't rate audit personnel higher than their audit quality rating.”

Curtis Buser, managing director Carlyle Group, October 2013

With mandatory rotation “we are going to see a lot of activity where the second tier poach partners from the Big Four, possibly with the help and encouragement from the Chinese government. The Big Four is going to have a tougher time keeping their quality up with these low fees”

Paul Gillis, an accounting expert at the Peking University school of management



“Audit firms that broadly monitor and analyze the development of industry risks and use this knowledge to review, compare and challenge the risk classification of individual audit engagements have a strong instrument to monitor the (audit) quality of individual engagements.”

Netherlands Authority for the Financial Markets

Deloitte.

“By putting a substantial emphasis on quality, we primarily focus on stakeholders' needs. This is what auditing is all about... a strong focus on the public interest in everything we do. Good quality is here to stay.”

Practitioner, Member of Young Professional Audit Quality Board, Netherlands

Need for focus on audit quality (Cont'd)

... and looking for increased consistency of global audit delivery and coordination across regulators



International Forum of Independent Audit Regulators (IFIAR)

IFIAR brings together independent audit regulators from a total of **46 jurisdictions**. 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
- Providing a **platform for dialogue with other international organizations** that have an interest in audit quality.

“One of the ways the PCAOB shares experiences and its knowledge with other audit regulators is through its work in IFIAR. An organization like IFIAR is important because it provides individual regulators a better view of the global landscape of audit practice and financial reporting.”

Lew Ferguson, IFIAR Chair / PCAOB Board Member, April 30, 2013

“Audit firms need to do more to improve the consistency of performance on individual audit engagements, including remediating the inspection findings and determining the possible root causes underlying these findings.”

Paul George, IFIAR Chair (former) and Executive Director of Conduct at the UK's Financial Reporting Council, Dec 19, 2012

Priorities for FY14

Audit quality

Growth

Innovation

Talent

Importance of audit quality

Delivering quality audits provides a competitive advantage

Meeting expectations and enhancing trust

- Enhance investors' trust in financial reporting
- Provide consistent global services of the highest quality
- Respond to regulators' expectations

What's in it for the audit firm?

- Lead the profession
- Grow business and win more clients, across all functions
- Generate revenues / profitability
- Develop functional and industry expertise
- Enhance brand, reputation and legacy
- Attract and retain best talent

Value added to clients

- Provide valuable business, market and industry insights
- Bring consistent global expertise with local delivery
- Offer cross-functional and industry expertise to address client needs
- Ensure timeliness of deliverables
- Proactively communicate all potential issues

**Public /
Markets**

**Audit
Firms**

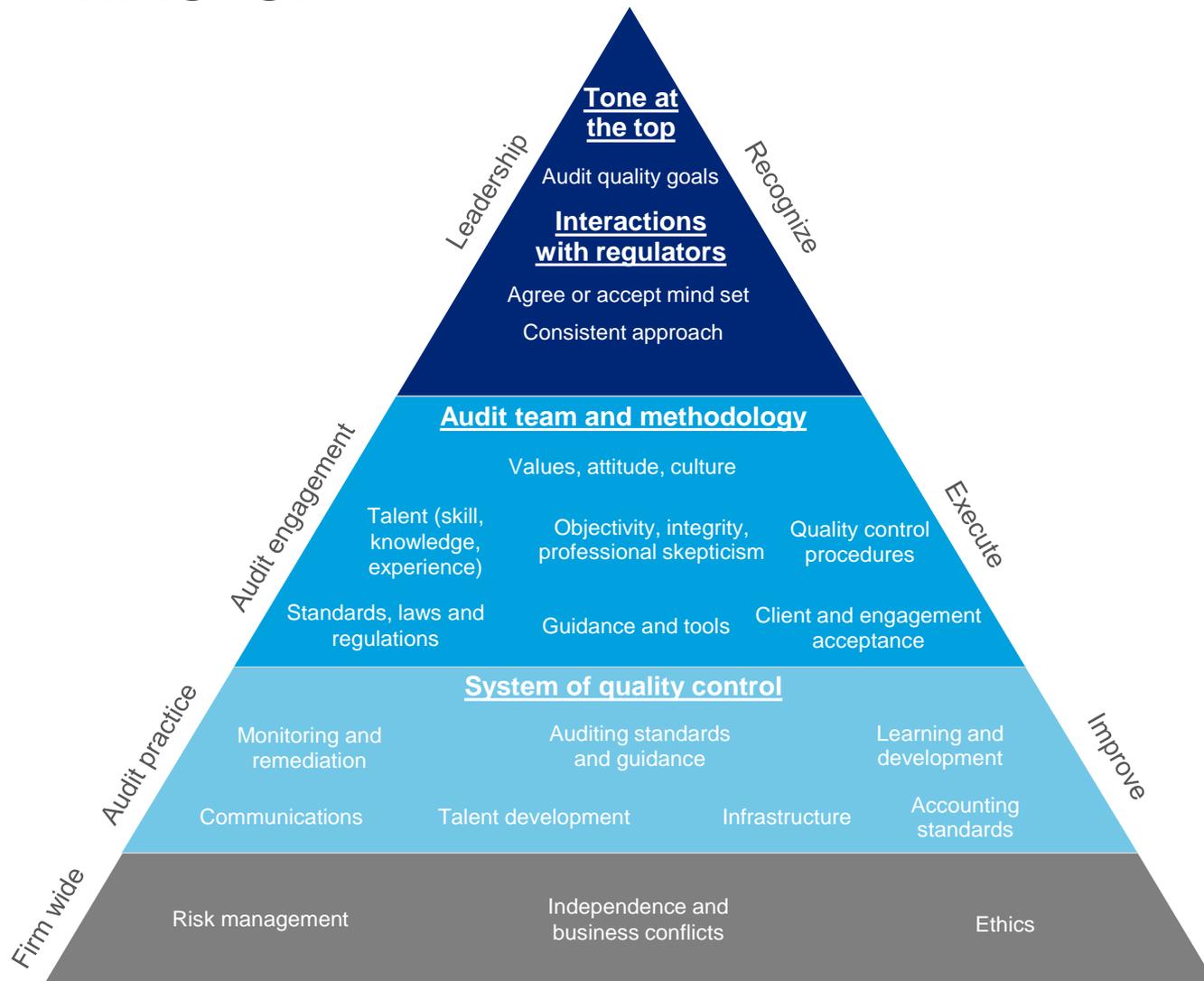
Clients

Enhancing trust in financial reporting and the capital markets

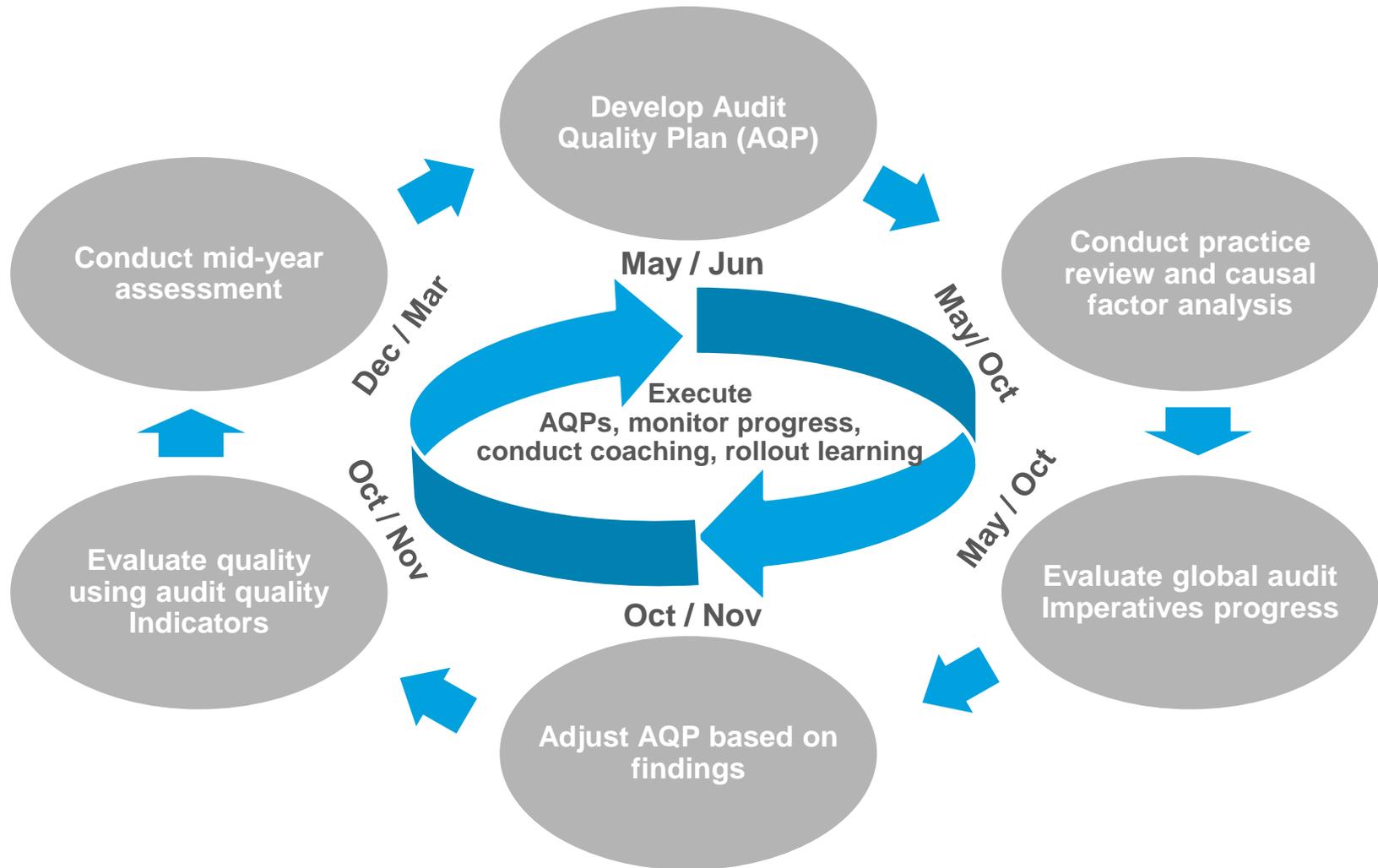
How to achieve audit
quality?

Foundational elements of audit quality

Audit firm level



Audit firm activities to improve audit quality



Professional excellence

Core components

Professional excellence =
Skill + Will

Standards

Judgment

Objectivity

Skepticism

Global audit imperatives

Core to supporting the audit quality agenda and delivering the highest quality audits



Global audit imperatives (Cont'd)

Importance of imperatives

A large percentage of Practice review findings relates to areas that align with the global audit imperatives

Global audit imperatives

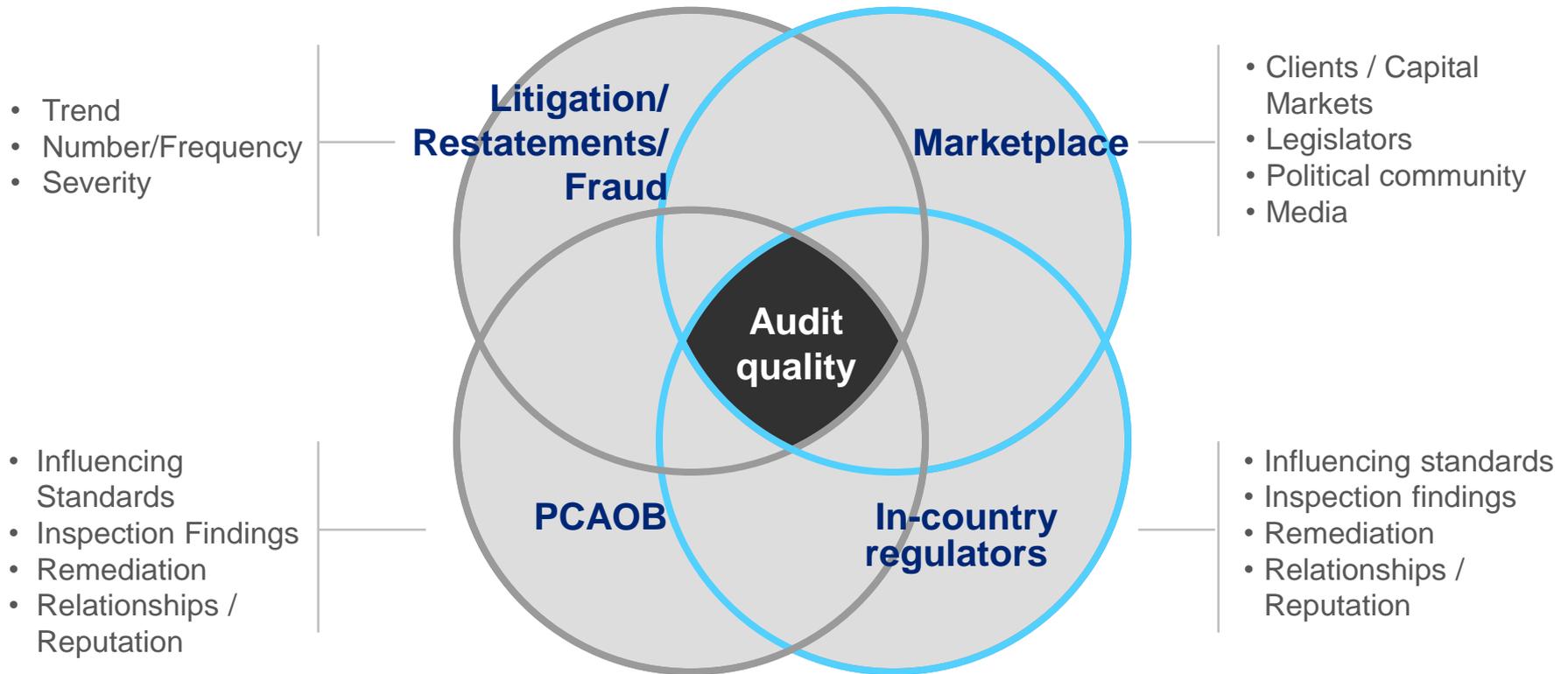
1. Audit procedures must clearly reflect acting as an evaluator with an attitude of professional skepticism
2. Demonstrate expertise in understanding internal controls, including understanding process flows and testing internal controls where applicable
3. Audit procedures and documentation must clearly reflect application of the guidance and relevant tools
4. Own the work performed by internal specialists and involve specialists in planning and concluding
5. Supervise and review the work of the component auditor
6. Improve expertise in audit skills – yours and those of others
7. Obtain deep understanding of the entity and its environment and improve application of the risk assessment procedures
8. We all own quality – individually and together

Effectively implementing the global audit imperatives has the potential to significantly reduce inspection findings

How to measure/assess
audit quality?

Audit quality

What, where and by whom is it judged?



Recognize our regulators define and judge quality in large part based on the outcome of their inspection process and our remediation efforts

Practice reviews

Regulatory inspections...

Internal practice review

- Within the firm
- By other member firms

Peer review

- By other firms
- Professional associations

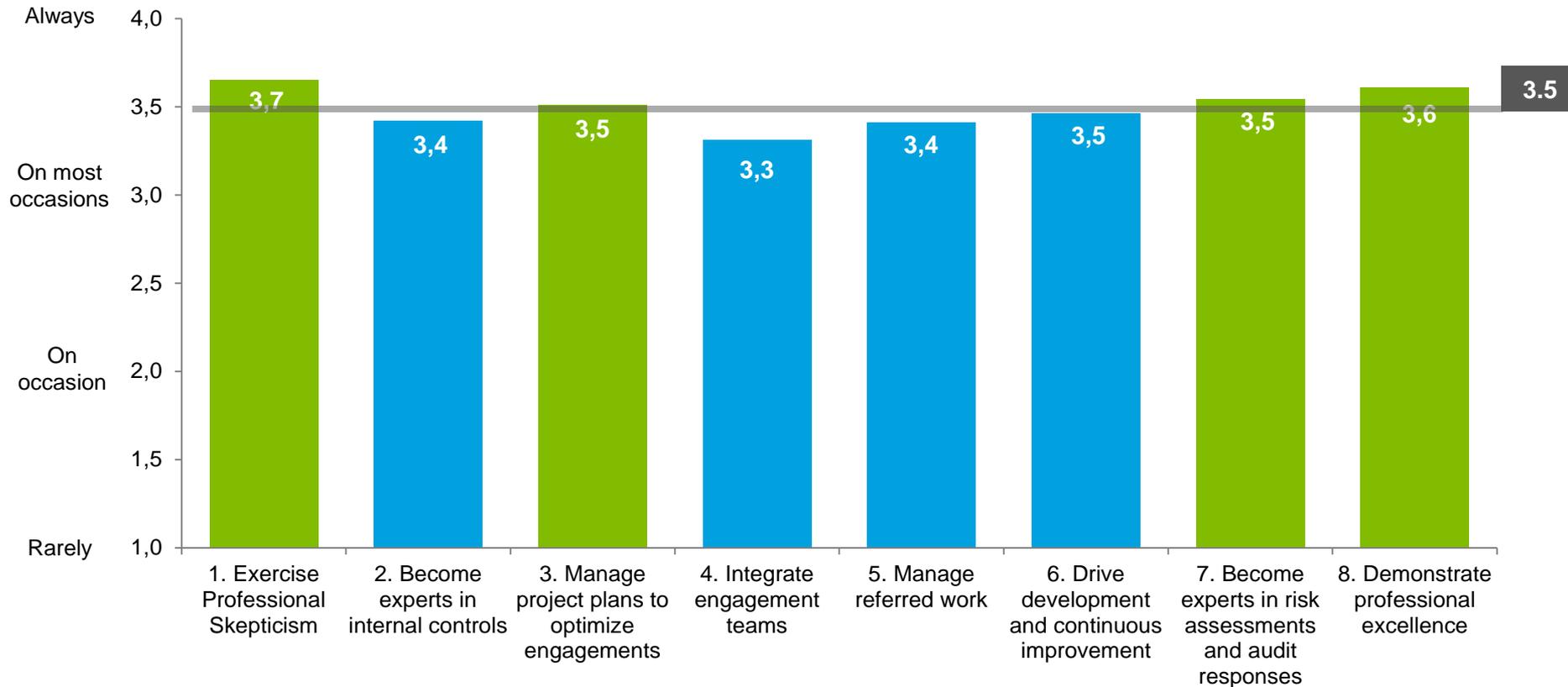
Assessment by clients' regulators

- Central banks
- Stock exchanges

Inspection by audit regulators

- Local
- International

Internal staff surveys on audit quality initiatives



Audit quality indicators

Audit quality indicator	
Engagement team	Partner / manager involvement in engagements
	Expert (specialist) involvement in engagements
	Culture of consultation
	Implementation of global audit imperatives
Firm	Tone at the top
	CEO / Audit business leader and audit partners measured against goals that reflect quality as a priority
	Reward for high quality audit and/or disciplinary action related to negative quality events
	Technical resources in national office
	Tenure of audit partners, directors, managers
	Staff turnover
	Delivery of (sufficient/appropriate) learning to audit practitioners
	Culture of on-the-job coaching
	Practice review and external inspection results
Nature of interactions with regulators and substance of communications with regulators	
External factors	Corruption – Perception of corruption in the market
	Culture – Cultural impact on decision-making and professional skepticism
	Regulatory environment (maturity of independent audit regulator)
	Rate of change in Gross Domestic Product (GDP)



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