

Impact of the Independent Review on SAICA Audit Training Offices

Date: 5 September 2011 (original publication date)
20 May 2014 (revision)
2 May 2018 (revision)

Prepared by: Graeme O'Reilly CA(SA) of NSOA Learning (Pty) Ltd

Table of contents:

| | Page |
|--|------|
| Background | 2 |
| Approach to the exercise | 3 |
| Summary of findings | 4 |
| Conclusion | 6 |
| Appendix A: Impact of the Independent Review on the Audit & Assurance Elective tasks | 7 |
| Appendix B: Impact of the Independent Review on the Audit & Assurance Residual tasks | 17 |

Background:

SAICA requires an understanding of the extent to which the performance of an Independent Review by a trainee accountant will meet the requirements for the Auditing & Assurance subject competencies and tasks.

Independent reviews are not "audits". The level of assurance provided by an Independent Review is limited and is based primarily on evidence obtained through inquiry and analytical procedures. Independent reviews are not conducted in terms of the International Standards on Auditing (ISA) but rather in terms of a stand-alone standard, ISRE2400 (the International Standard on Review Engagements).

Having said this, the process followed in conducting both an audit and an independent review is similar. Both engagements require engagement acceptance procedures, engagement planning procedures, the gathering of sufficient acceptable evidence to reach conclusions, engagement finalisation procedures and then engagement reporting procedures.

It is therefore probable that, given these similarities, the performance of an independent review will provide trainee accountants with **some** opportunities to demonstrate various abilities set out in the tasks pertaining to the Auditing & Assurance subject.

Reasons for updating the document:

When this document was originally published in September 2011, ISRE 2400 was undergoing a revision. A proposed ISRE 2400 was published for comment in January 2011 with comments due by the end of May 2011. As of the date of the original publication, the revised ISRE 2400 had not yet been issued.

The revised ISRE 2400 was subsequently published and became effective for reviews of financial statements for periods ending on or after 31 December 2013. This document was therefore reconsidered in terms of the revised ISRE 2400 and was amended in May 2014, where necessary, to reflect this revised ISRE 2400.

The latest change to this document updates the SAICA Training programme competencies and tasks to reflect the current version of this programme – i.e. the January 2016 Training programme - and reconsiders the appropriateness of the revised ISRE 2400 in this light. The 2016 Training programme incorporated several new tasks into the AA elective, significantly amended the wording for most of the AA tasks, and significantly changed the AA residual tasks.

Approach to the exercise:

Independent reviews are required to be conducted in terms of ISRE 2400 by the Companies Regulations, 2011 (Regulation 29(3)).

The following documents therefore currently direct the performance of an independent review in South Africa:

- ISRE 2400 (Revised) (The International Standard on Review Engagements)
- The Companies Regulations, 2011

For each of the individual tasks required of the Auditing & Assurance subject (both as an elective and as a residual) this document considers the degree to which the conducting of an independent review by a trainee accountant in terms of ISRE 2400 (Revised) would be capable of satisfactorily demonstrating an ability to perform these tasks.

The detailed assessment is documented in Annexure A (for the Elective tasks) and Annexure B (for the Residual tasks).

Summary of findings

Elective tasks:

Based on the summary contained in annexure A, of the total number of 30 Auditing & Assurance tasks, the following 13 *Elective* tasks will generally **not** be able to be adequately demonstrated during the performance of an independent review:

| Task | Description |
|----------|---|
| AA(E)2.3 | Obtains an understanding of and documents the entity's internal control. |
| AA(E)3.1 | Evaluates the adequacy of the design of control activities in the prevention or detection of material misstatement, and suggests improvements where appropriate. |
| AA(E)3.2 | Evaluates the risk of material misstatement at an overall financial statement level (including an evaluation of the appropriateness of the going concern assumption). |
| AA(E)3.3 | Evaluates the risk of material misstatement at the assertion level for classes of transactions, account balances and disclosures. |
| AA(E)3.4 | Evaluates the risk of material misstatement due to fraud. |
| AA(E)3.5 | Evaluates the risk of material misstatement due to non-compliance with laws and regulations. |
| AA(E)3.6 | Identifies and evaluates the significant risks that could result in material misstatement. |
| AA(E)5.1 | Designs or selects appropriate tests of internal control (including IT internal controls, where appropriate), including the determination of sample sizes and methods of selection. |
| AA(E)5.2 | Designs or selects appropriate substantive tests of detail, including the determination of sample sizes and methods of selection. |
| AA(E)5.5 | Evaluates the need to use computer assisted audit techniques to gather suitable audit evidence. |
| AA(E)6.1 | Performs the planned tests of internal control and identifies situations where follow-up/extended work is required. |
| AA(E)6.2 | Performs the planned substantive tests of detail and identifies situations where follow-up/extended work is required. |
| AA(E)7.2 | Performs a subsequent events review to identify potential adjusting subsequent events. |

Trainee accountants will generally be capable of demonstrating the remaining 17 Elective tasks during the performance of an independent review.

Residual tasks:

Based on the summary contained in annexure B, of the total number of 5 Auditing & Assurance tasks, the following *Residual* task will generally **not** be able to be adequately demonstrated during the performance of an independent review:

| Task | Description |
|----------|---|
| AA(R)2.1 | Prepares information for, or responds to requests by, the external auditors |

Trainee accountants will generally be capable of demonstrating the remaining 4 Residual tasks during the performance of an independent review.

Conclusion:

The performance of an independent review purely in terms of ISRE 2400 (Revised) does provide opportunities for trainee accountants to demonstrate the majority of the Auditing and Assurance Elective tasks.

It should be emphasized however that although the performance of an independent review may provide trainee accountants with **the opportunity** to demonstrate Auditing & Assurance tasks, the quality of the work delivered and the competence with which it is performed by the trainee will always need to be considered by the Reviewer when rating competence.

The Reviewer will also need to consider whether the evidence presented by the trainee while performing an independent review constitutes basic or advanced evidence (dependent on the complexity of the task at hand). *Under no circumstances would it be appropriate to presume that an independent review provides only basic evidence of competence.*

In addition to this, it would be very important for Evaluators to consider the sufficiency of evidence presented by trainees for Auditing and Assurance elective tasks where the majority of this evidence arises from the performance of independent reviews.

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|--|--|---|----------------------------|
| <u>AA(E)1:</u> Performs pre-engagement activities | <u>AA(E)1.1</u> Evaluates the nature, scope, standards and legislation applicable to a particular engagement. | Trainees need to be able to identify the appropriate nature of the engagement - that an independent review is required as opposed to an audit, for example. They also need to be aware of the scope of the independent review (conducted i.t.o. ISRE 2400 (Revised)); the financial accounting standards that are applicable to the engagement (the appropriateness of the accounting framework must always be considered – para 30(a)); and of any legislation that may be applicable to the engagement; and ISRE 2400 (Revised) specifically requires that inquiries are made to determine the extent of compliance with laws & regulations having a direct effect on material balances (para 48(d)(ii)) - this will require prior identification of these laws & regulations by the trainee. | Able to meet requirements. |
| | <u>AA(E)1.2</u> Identifies the factors to be considered in accepting or continuing with an engagement. | ISRE2400 (Revised) requires detailed client acceptance and continuance procedures to be followed (para 29 to 32). | Able to meet requirements. |
| | <u>AA(E)1.3</u> Drafts or evaluates an appropriate engagement letter for an engagement or outlines the appropriate content for such a letter. | ISRE 2400 (Revised) requires that practitioners "shall" agree the terms of the engagement with management (para 36). In addition to this, para 37 requires that these terms be recorded in an engagement letter or other suitable form of written agreement. | Able to meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|--|---|--|---|
| <u>AA(E)2</u> Obtains an understanding of the entity and its environment | <u>AA(E)2.1</u> Obtains a qualitative understanding of the entity and its environment and documents this information in an appropriate format. | Para 45 of ISRE 2400 (Revised) requires practitioners to obtain an understanding of the entity (and its environment) that they are reviewing. Para 46 provides the detail in terms of what needs to be understood... | Able to meet requirements. |
| | <u>AA(E)2.2</u> Identifies and documents the major classes of transactions and balances for an engagement entity. | ISRE 2400 (revised) requires practitioners to obtain an understanding of the entity that includes an understanding of its accounting system and accounting records. It further requires that the practitioner, when applying their judgement to the design of required procedures, shall consider all material items in the financial statements. (para 47). Major classes of transactions and balances will thus need to be identified when performing an independent review. | Able to meet requirements. |
| | <u>AA(E)2.3</u> Obtains an understanding of and documents the entity's internal control. | While ISRE 2400 (Revised) does require an understanding of the accounting system and accounting records, there is no specific requirement to obtain an understanding of the entity's internal control. | Not able to adequately meet requirements. |
| <u>AA(E)3</u> Identifies and evaluates the risk of material misstatement. | <u>AA(E)3.1</u> Evaluates the adequacy of the design of control activities in the prevention or detection of material misstatement, and suggests improvements where appropriate. | Because ISRE 2400 (Revised) does not require any understanding of the entity's internal control, it would not be possible to evaluate the design of control activities during an independent review. | Not able to adequately meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|------------|--|---|---|
| | <u>AA(E)3.2</u> Evaluates the risk of material misstatement at an overall financial statement level (including an evaluation of the appropriateness of the going concern assumption). | <p>There is no reference to the evaluation of risk of material misstatement at an overall level in ISRE 2400 (Revised). The standard does require that the engagement is planned in such a way that a sufficient understanding of the entity is obtained in order to identify <i>areas in the financial statements</i> where material misstatements are likely to arise (para 45).</p> <p>This however does not adequately evaluate risk at a <i>financial statement level</i> (in the context of that required of external auditors in terms of ISA315 para 25(a)).</p> <p>Thus, while a review does require consideration of risk of material misstatement, it appears to be largely at an account balance / transaction level and not at an overall financial statement level.</p> | Not able to adequately meet requirements. |
| | <u>AA(E)3.3</u> Evaluates the risk of material misstatement at the assertion level for classes of transactions, account balances and disclosures. | <p>As referred to for AA(E)3.2, the independent review does require the identification of areas in the financial statements where there is perceived to be a risk of material misstatement. ISRE2400 (Revised) however makes no specific reference to risk assessment in terms of the <i>financial statement assertions</i> specifically.</p> <p>An independent review conducted purely in terms of ISRE 2400 (Revised) would thus not be able to demonstrate this task.</p> | Not able to adequately meet requirements. |
| | <u>AA(E)3.4</u> Evaluates the risk of material misstatement due to fraud. | <p>ISRE 2400 (Revised) only requires practitioners to inquire as to the existence of fraud (para 48(d)) and then, only where there is an indication that fraud may have taken place, take action in terms of para 52.</p> <p>There is no requirement in the ISRE to specifically consider the risk of material misstatement due to fraud as is required for an audit in terms of ISA 240.</p> | Not able to adequately meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|--|---|--|---|
| | <u>AA(E)3.5</u> Evaluates the risk of material misstatement due to non-compliance with laws and regulations. | <p>Similarly to the risk of fraud, practitioners performing independent reviews are only required to inquire as to any actual, suspected, or alleged non-compliance with laws and regulations (para 48(d)) and then, only if suspected to have taken place, perform the procedures in para 52.</p> <p>This is unlikely to adequately demonstrate an evaluation of the risk of material misstatement due to non-compliance with laws and regulations.</p> | Not able to adequately meet requirements. |
| | <u>AA(E)3.6</u> Identifies and evaluates the significant risks that could result in material misstatement. | <p>Significant risks are risks of material misstatement that require special audit consideration (ISA315 para 27 – 29).</p> <p>ISRE 2400 (Revised) does not require that practitioners identify such risks of material misstatement. It is therefore unlikely that the risk assessment process followed during an independent review will adequately identify and document "significant risk" as envisaged by ISA315.</p> | Not able to adequately meet requirements. |
| <u>AA(E)4</u> Calculates and justifies planning materiality | <u>AA(E)4.1</u> Identifies and evaluates the factors that affect planning materiality. | ISRE 2400 (Revised) requires that practitioners “shall determine materiality for the financial statements as a whole, and apply this materiality in designing the procedures and evaluating the results obtained from those procedures” (para 43). | Able to meet requirements. |
| | <u>AA(E)4.2</u> Calculates a justifiable level of planning materiality for an engagement. | Refer AA(E)4.1. | Able to meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|--|---|--|---|
| AA(E)5 Designs effective & efficient audit procedures | AA(E)5.1 Designs or selects appropriate tests of internal control (including IT internal controls, where appropriate), including the determination of sample sizes and methods of selection. | Given that there is no need to obtain an understanding of an entity's internal control, and nor to evaluate the design of control activities put in place by the entity, an independent review will be very unlikely to provide an opportunity to demonstrate an ability to perform this task. | Not able to adequately meet requirements. |
| | AA(E)5.2 Designs or selects appropriate substantive tests of detail, including the determination of sample sizes and methods of selection. | <p>The primary procedures conducted during an independent review are inquiry and analytical procedures. Substantive tests of detail (usually incorporating the inspection of documentary evidence) will not normally be performed in an independent review.</p> <p>The only time where this might happen is where a potential misstatement is identified and the practitioner is required to perform further procedures in response to this. It should however be noted that even under these circumstances those further procedures do not <i>need to</i> incorporate substantive tests of detail.</p> <p>An independent review will therefore be unlikely to provide the opportunity to demonstrate an ability to perform this task.</p> | Not able to adequately meet requirements. |
| | AA(E)5.3 Designs or selects appropriate substantive analytical review procedures. | Analytical review procedures form an integral part of the evidence gathered during an independent review. Para A90 and A91 of ISRE 2400 (Revised) provide direction regarding the development of these procedures and trainees who design analytical review procedures in terms of these paragraphs would be able to demonstrate their ability to perform this task. | Able to meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|---|--|--|---|
| | <u>AA(E)5.4</u> Evaluates the need for using the work of others in conducting the audit, for example experts, internal auditors or component auditors, etc. | ISRE 2400 (Revised) suggests that when a practitioner performs an independent review, it may be necessary to use work performed by another practitioner or by an expert, and if so, that the practitioner should be satisfied that the work is adequate for the purposes of the review (para 55). It would thus be possible to evaluate the need to use the work of others. | Able to meet requirements. |
| | <u>AA(E)5.5</u> Evaluates the need to use computer assisted audit techniques to gather suitable audit evidence. | <p>Computer assisted audit techniques (CAATS) involve the use of computers to perform procedures that would otherwise be done manually. CAATS are most often associated with the use of software to interrogate entity information. This is generally most appropriate in the performance of tests of control or substantive tests of detail.</p> <p>In the context of an independent review, the only opportunity to incorporate the use of CAATS would be during the performance of analytical review procedures. While these analytical review procedures would most likely be performed using computers (excel, for example), the opportunities to use them to “gather suitable audit evidence” may however be limited given that they are unlikely to involve the extraction and review of entity information. It is thus unlikely that a trainee would be able to demonstrate that they have used CAATS sufficiently in the gathering of suitable evidence through performing an independent review.</p> | Not able to adequately meet requirements. |
| <u>AA(E)6</u> Executes the work plan, documents and evaluates results. | <u>AA(E)6.1</u> Performs the planned tests of internal control and identifies situations where follow-up/extended work is required. | An independent review does not normally encompass the performance of any tests of control and would therefore not provide trainee accountants with any opportunities to demonstrate this task. | Not able to adequately meet requirements. |

Annexure A: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as an **Elective** subject.

| Competency | Task | Commentary | Conclusion |
|------------|---|---|---|
| | <u>AA(E)6.2</u> Performs the planned substantive tests of detail and identifies situations where follow-up/extended work is required. | The independent review does not normally encompass the performance of any substantive tests of detail and would therefore not provide trainee accountants with any opportunities to demonstrate this task. | Not able to adequately meet requirements. |
| | <u>AA(E)6.3</u> Performs the planned substantive analytical review procedures and identifies situations where follow-up/extended work is required. | The independent review does incorporate the performance of analytical review procedures. As already indicated, provided these analytical reviews are predictive in nature, the design and performance of analytical review procedures can be demonstrated during the performance of an independent review. It would be important that analytical reviews used as evidence for this task should be designed to provide <i>substantive evidence</i> about account balances or classes of transactions, and should not be planning (risk-identification) analytical reviews, for example. | Able to meet requirements. |
| | <u>AA(E)6.4</u> Evaluates whether the procedure meets the stated objective. | Because there is no reference in the task description to any specific procedures, the independent review could be used by a trainee accountant to demonstrate the ability to draw conclusions following the performance of procedures such as inquiry and analytical procedures. | Able to meet requirements. |

| Competency | Task | Commentary | Conclusion |
|---|---|---|----------------------------|
| | <u>AA(E)6.5</u> Recommends modifications to the audit plan, where necessary, in response to the results of procedures performed. | <p>Although there is no specific reference to an "audit plan", ISRE 2400 (Revised) does require practitioners to design procedures that, in their judgement, provide them with sufficient evidence to support their conclusions (para 47).</p> <p>The substance of this task should therefore be seen in the context of a trainee's ability to respond to the findings arising from originally planned procedures.</p> <p>ISRE 2400 (Revised) requires that where the practitioner has reason to believe that the information subject to review may be materially misstated, that they carry out additional or more extensive procedures as they deem necessary (para 66).</p> <p>Therefore a trainee accountant who performs planned procedures during an independent review, and finds reason to believe that there may be a material misstatement, would have an opportunity to demonstrate that they are able to modify the plan in response to these findings.</p> | Able to meet requirements. |
| <u>AA(E)7</u> Completes the engagement | <u>AA(E)7.1</u> Evaluates the impact of identified misstatements against final materiality (quantitative and/or qualitative) and evaluates the need for additional work. | <p>ISRE 2400 (Revised) requires practitioners to consider the impact of any unadjusted misstatements identified during the review on their report (para 70).</p> <p>This task should form part of the finalisation of any independent review and a trainee accountant performing this requirement would be able to demonstrate this task.</p> | Able to meet requirements. |

| Competency | Task | Commentary | Conclusion |
|------------|---|--|---|
| | <u>AA(E)7.2</u> Performs a subsequent events review to identify potential adjusting subsequent events. | <p>ISRE 2400 (revised) only requires that practitioners should inquire of management about events subsequent to the date of the financial statements that may require adjustment or disclosure (para 48(e)). Furthermore, the practitioner is only required to respond to adjusting subsequent events if they become aware of them (para 58).</p> <p>There is no requirement that the practitioner performs procedures (other than the inquiry referred to already) to identify adjusting subsequent events.</p> <p>A trainee will therefore not be able to adequately demonstrate their ability to perform this task during an independent review conducted in terms of ISRE 2400.</p> | Not able to adequately meet requirements. |
| | <u>AA(E)7.3</u> Evaluates the appropriateness of the going concern assumption. | <p>Para 53 of ISRE 2400 (Revised) requires that a practitioner considers the entity's ability to continue as a going concern when performing an independent review of financial statements.</p> | Able to meet requirements. |
| | <u>AA(E)7.4</u> Evaluates the management representation letter and recommends modifications, where applicable. | <p>Para 61 of ISRE 2400 (Revised) requires that a practitioner requests a written representation that management has fulfilled its obligations and furthermore, para 62 requires a number of specific representations to be disclosed. Trainees will thus be able to demonstrate this task during an independent review.</p> | Able to meet requirements. |

| Competency | Task | Commentary | Conclusion |
|--|--|---|----------------------------|
| <u>AA(E)8</u> Prepares information for meetings with stakeholders. | <u>AA(E)8.1</u> Prepares the report to management on findings arising from the engagement. | ISRE 2400 (Revised) requires practitioners to communicate with management or those charged with governance of the entity all matters that are deemed to be of sufficient importance to merit their attention (para 42). Should the practitioner issue a report to management on the findings arising during the independent review, then the trainee will certainly have the opportunity to prepare this report for the engagement. | Able to meet requirements. |
| <u>AA(E)9</u> Identifies and responds to reportable irregularities. | <u>AA(E)9.1</u> Evaluates whether there are potential unlawful acts or omissions and whether or not they may constitute a reportable irregularity and, if appropriate, inform the supervisor of the potential irregularity. | Independent reviewers are not regarded as performing an assurance engagement that requires them to report irregularities as required by section 45 of the Auditing Professions Act, 2005 (IRBA Revised Guide on Reportable Irregularities in terms of the AP Act (May 2015), para 6.1.5). The Companies Regulations, 2011 do however require that should an independent reviewer be satisfied, or have reason to believe, that a reportable irregularity (<i>as defined in the Companies Regulations</i> as opposed to the AP Act) has taken place, then there is a duty to report it to the Commission (regulation 29(6)). Although not identical to the AP Act reportable irregularities, the definition and reporting process are sufficiently similar that a trainee accountant who identifies and communicates a reportable irregularity during the performance of an independent review would adequately demonstrate their ability to perform this task. | Able to meet requirements. |

| Competency | Task | Commentary | Conclusion |
|---|---|--|----------------------------|
| <u>AA(R)1</u> Demonstrates a basic appreciation and awareness of the practical considerations of the external audit function | <u>AA(R)1.1</u> Evaluates the scope and the appropriateness of the terms of engagement, including the responsibilities of management and the responsibilities of the auditors. | <p>For an independent review, trainee accountants would need to be able to identify the appropriate nature of the engagement - that an independent review is required as opposed to an audit, for example. They would also need to be aware of the scope of the independent review (conducted i.t.o. ISRE 2400 (Revised)).</p> <p>ISRE 2400 (Revised) requires that practitioners "shall" agree the terms of the engagement with management (para 36). In addition to this, para 37 requires that these terms be recorded in an engagement letter or other suitable form of written agreement. This engagement letter sets out responsibilities of both the practitioner and management.</p> | Able to meet requirements. |
| | <u>AA(R)1.2</u> Evaluates the impact of identified misstatements on the financial statements in the context of materiality | <p>ISRE 2400 (Revised) requires practitioners to consider the impact of any unadjusted misstatements identified during the review on their report (para 70).</p> <p>This task should form part of the finalisation of any independent review and a trainee accountant performing this requirement would be able to demonstrate this task.</p> | Able to meet requirements. |

Annexure B: Consideration of the degree to which the independent review demonstrates the Auditing & Assurance tasks as a **Residual** subject.

| Competency | Task | Commentary | Conclusion |
|--|---|--|---|
| | <u>AA(R)1.3</u> Evaluates the appropriateness of the management representation letter | Para 61 of ISRE 2400 (Revised) requires that a practitioner requests a written representation that management has fulfilled its obligations and furthermore, para 62 requires a number of specific representations to be disclosed. Trainees will thus be able to demonstrate this task during an independent review. | Able to meet requirements. |
| <u>AA(R)2</u> Prepares information requested by the external auditors | <u>AA(R)2.1</u> Prepares information for, or responds to requests by, the external auditors | This task would not be applicable in an independent review as the trainee accountant would be unlikely to be working with external auditors. | Not able to adequately meet requirements. |
| <u>AA(R)3</u> Communicates with external audit | <u>AA(R)3.1</u> Communicates effectively with external audit stakeholders, for example identifying issues regarding the audit strategy, describing internal controls and financial systems used, any material issues identified during the course of the audit, etc. | ISRE 2400 (Revised) requires practitioners to communicate with management or those charged with governance of the entity (similar to “external audit stakeholders”) all matters that are deemed to be of sufficient importance to merit their attention (para 42). Should the practitioner issue such a report on the findings arising during the independent review, then the trainee will certainly have the opportunity to prepare this report for the engagement. | Able to meet requirements. |