

Accounting and Auditing Standards Community of Practice (A&A CoP) STAREP

**Audit oversight and quality assurance
in Georgia: current status**

Description of Background

- Georgia has adopted a law on accounting and auditing in 2012, which states the rules for the auditors to be listed in the registers of statutory or non-statutory auditors, BUT the law is not fully enforced, because certain important requirements have been deferred by the parliament of Georgia twice. This leads to audit firms being able to perform audits of financial statements without the obligation to be listed in the register, which itself leads to confusion.
- Current law requires auditors/audit firms to be members of the accredited professional organization.
- It also requires the accredited professional organizations to maintain a register of auditors/audit firms which are THEIR MEMBERS.
- The law also states, that audit can only be conducted if the audit firm is listed in the register, maintained by the professional organizations.
- However, the requirement for the audit firms to be members of the accredited professional organizations has been deferred.
- Therefore, accredited professional organization maintains the register of its members, however not all audit firms on the market are their members.
- The above mentioned auditors perform audits of financial statements without any barriers.

Description of background

- Audit is self-regulated and the quality reviews are delegated to the Accredited Professional Organization.
- However, because of the reasons listed on the previous slide, we as an Accredited Professional Organization do not have the power to regulate the whole market, because of the deferral of the enforcement of the law.
- In addition, we do not have the precise information about the market, we do not now how many audit firms are beyond the register, or how many companies are audited by them.
- The government of Georgia has also drafted an order, which determines the auditors who are given the right to perform statutory audits.
- The above mentioned is also opposing the law, as the law states that the audit firms which have the right to perform statutory audits are determined by the results of the audit quality review.
- Things are made even harder by the fact that the some firms are added to the order in a mysterious way – no information exists what has to be done to be included in the order.
- Not all firms in the government order are members of the Accredited Professional Organization, therefore, they are not part of the register of auditors.
- Because of these reasons, the information that will be provided is solely the information that concerns the audit firms that are members of GFPAA – the Accredited Professional Organization.

Background information – state of audit market

Number of auditors: 6 individual auditors (sole practitioners)

Number of audit firms: 72 audit firms

Number of entities, subject to statutory audit: Precise number is not known.

Which entities are subject to statutory audit according to the local legislation?

Entities under the supervision of the National Bank of Georgia and other entities, specifically determined by the Law. The entities are generally banks, insurance undertakings and brokerage firms.

Legal framework

- *Auditing Law adopted on 29 June 2012*
- *ISA adopted on 29 June, 2012*
- *No other relevant laws except the Accounting and Audit Law.*
- *Statutory Audit Directive was not consulted during the development of the current Law.*

Public Oversight Authority (1)

Audit regulation is delegated to the Accredited Professional Organization, a member of IFAC, which currently is Georgian Federation of Professional Accountants and Auditors (GFPAA). It is an independent regulator.

Ideally, the body should be responsible for the regulation of all the auditors, but because of the confusion caused by the current law (described in the Description of Background), not all auditors are required to be members of this organization.

The budget of this body is financed by the membership fees of the Audit Firms.

No other relevant bodies exist which would regulate audit practice.

Public Oversight Authority (2)

The objective of the Accredited Professional Organization is to regulate the audit profession in a manner to ensure that the audit reports issued in Georgia are in accordance with applicable standards and are of high quality. To do this, GFPAA plans to carry out quality reviews of its members.

Its duties are to perform quality control checks at least once in every three years and to maintain the register of statutory and non-statutory audit firms.

Oversight body is being governed by the supervisory board which is being elected periodically by its members. The organization has different membership types which currently are individual auditors (sole practitioners), audit firms and associated persons as its members.

GFPAA has the power of including or excluding an audit firm from the register of auditors. If the audit firm fails to pass the audit quality review GFPAA will exclude it from the audit register effectively denying the firm the right to perform audit of financial statements for the predetermined amount of time. (This power is also compromised by the deferral of the enforcement of the law, as none of the companies is looking at the register nowadays).

Public Oversight Authority (3)

GFPAA has developed a statute regarding the quality reviews, which are about to start in 2014 (we did not have systematic quality reviews before). The statute intends to assess the degree of compliance of each audit firm with ISAs. This will be achieved by assessing the firm's methodology, whether it complies with ISAs and whether the firm applies the methodology on different engagements.

In the event of non-compliance of the firm's methodology with ISAs or its non-consistent application GFPAA can exclude the firm from the register of auditors, or exclude the firm from the register of statutory auditors, leaving the firm the right to perform non-statutory audits only. GFPAA can also act against a single partner who is continuously inconsistent with the methodology of his/her firm and deny him/her to sign audit reports for a predetermined period of time.

GFPAA is a professional organization where all the people in the profession can become its members and gain a vote on its elections of the supervisory board. Members can also nominate their candidates to be included in the board. GFPAA reports to the public with its general report once every year.

Quality Assurance System (1)

- GFPAA has long aimed for the audit quality reviews to be conducted within the audit firms. GFPAA plans to perform first systematic reviews at the end of 2014. The Quality Review will include review of the firm's quality control system and the review of its practical implementation.
- In accordance with the current law, Accredited Professional Organization is responsible to conduct audit quality reviews and, based on the results, issue one of the four QR category reports. The first two will give the firm the right to be able to perform both statutory and non-statutory audits, while the third category gives the firm right to perform non-statutory audit only and the fourth category will deny the firm to perform audit for a predetermined amount of time.
- Quality Reviews will take place with the help of Certified Quality Controllers (This way of control is defined by the law). The certification of quality controllers took place just recently. Currently, GFPAA has three certified quality controllers, each having at least 6 years of experience in the audit field. However, they are not professional quality controllers, they are practicing auditors (Managers and above).
- GFPAA selects auditors which will undergo quality control review in a calendar year based on a **random selection** from the members of the professional organization. (i.e. firms that can be found in the register).

Quality Assurance System (2)

- *The reviews will take place either at the client's site or remotely, however it's intended to be a combination of both in most cases.*
- *Review of activities of sole practitioners has not yet been designed, but the review of the audit firms could last as long as five calendar days. However, this is the maximal amount of days. The best estimation of the average fieldwork days would be two days on any audit firm. This, however, will be followed by documentation of findings and issuance of the QR report which will take some time.*
- *The primary aim of GFPAA's quality control is to assess that the methodology of the audit firm complies with ISAs and that the methodology is being applied consistently on all audit engagements. Focus will be split on both, on a review of internal quality systems as well as engagement reviews. Because of the situation on the market, however, we estimate that most time will be taken on the assessment of the firm's quality control system rather than individual audit engagements.*

Quality Assurance System (3)

- *As for the selection of engagements to be reviewed, GFPAA plans to let quality controllers select one engagement per partner in an audit firm, with statutory audits being preferable. Complexity of projects will be taken in account when selecting the engagement.*
- *We lack the resources required for the quality reviews. Because we did not have non-practitioner auditors with sufficient competence (which were preferable to the practitioners) we certified currently practicing auditors. Current amount of quality reviewers is only three, which may not be enough to carry out the activity.*
- *According to the statute, the QR results will be made available to the public by the professional organization electronically (via its website, it is planned to be integrated within the register of auditors).*
- *Because we have not yet performed the quality control reviews we can not talk about major non-compliances by the auditors, however, many firms will have major drawbacks with their methodologies as they are not being in compliance with ISAs. Many firms do not have methodology at all and this will be a major problem.*

The relationship between POA and other financial sector regulators

- *There is a very weak link between GFPAA and other financial sector regulators, if any. The regulator in the financial sector is the National Bank of Georgia, which regulates banks and insurance undertakings. Because these entities are required to perform statutory audit, the professional organization maintains a register of statutory auditors. However, we are not sure whether all statutory audits are performed by the firms that have the right, because the Law is not effectively enforced.*
- *Other firms exist, which perform audits but are not members of the professional organization. Hence, they can not be found in the register, because the professional organization maintains the register of its members only (required by the law).*

Conclusions

There are several challenges in the country regarding the accounting and audit profession:

- Micro-enterprises are not required to maintain accounting records at all by the current law. This creates a gap between the current legislation and the Euro directive.*
- There is a very large gap between the tax accounting and financial accounting, which creates confusion.*
- IFRS for SMEs is defined to be usable by the law, however, European directive does not mention IFRS for SMEs, however it mentions IFRS.*
- There is no regulatory body, which would be independent from the profession and perform quality control reviews, maintain the register of auditors. GFPAA stresses the importance of existence of such a body, as GFPAA is not completely independent in this respect.*
- No requirement at all to publish financial information of any firm. Because of this, firms that conduct audits, even non-statutory audits, do not make their information available, rather, they are used only internally. We suggest there should be a mechanism, which would stress the importance of publishing financial information and regulate the activity.*