

# AUDIT QUALITY IMPROVEMENT AND PUBLIC SUPERVISORY SYSTEM CHANGES IN LITHUANIA: DEVELOPMENT, CURRENT SITUATION AND OUTLOOK

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## **Research objective:**

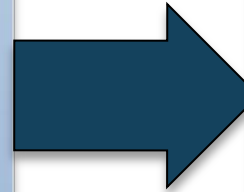
To analyse and describe the system of audit quality and oversight currently designed and implemented in Lithuania, and to identify potential areas of improvement.

## **Research tasks:**

- To identify the main stages of development of audit quality and oversight system;
- To determine the relationships between audit quality and oversight systems and the consistency of control system.

## Audit objectives

- To **determine** whether financial statements of audited entity **fairly present**, in all material respects, its financial position, financial performance and cash flows in accordance with the law, governing accounting and financial reporting, and to **identify** whether financial data in the annual report or annual activity report **correspond** to the data in the annual financial statements.



## Audit outcome

- **Independent auditor's report** on entity's financial statements.
- The audit report should give a certain **minimum level of assurance** concerning the reliability of financial information.

**1997–2000:** Beginning of audit quality assurance system, minimum procedure and documentation requirements; the audit quality assurance system is based on self-control.



**2000-2002:** The Ministry of Finances of the Republic of Lithuania was tasked with control of audit quality, however, this official function was not realised in practice.



**2002-2004:** The audit quality control was carried out by the LCA. The first audit methodology, as well as national standards on auditing and code of ethics for auditors were developed. There was no any systematic and regular oversight and control of auditors and audit firms' activities.



**2004-2008:** After extension of the rights of the Audit Quality Control Committee the audit oversight became independent; the planning element was adopted for the oversight of auditors and audit firms.



**2008–2016:** The audit quality assurance is being implemented by the AAA together with the LCA; the LCA establishes the Procedure for implementation of audit quality assurance and organises audit quality assurance reviews; the AAA ensures the quality of conducted audits by performing investigations.



**2016 - ...** Currently, legal documents concerning amendments to audit quality control and public oversight system are being drawn up in accordance with the Directive 2014/56/EU and Regulation (ES) No 537/2014.

LCA

Audit firms and  
auditors

LCA, AAA

**PREVENTIVE CONTROL**

**Oversight of auditors' qualification**

- Qualification examinations
- Post-qualification control

Audit regulation

- ISAs, Audit Law of the Republic of Lithuania
- Guide to Audit Quality Control
- Audit firm's quality control policies

**CURRENT CONTROL**

**Audit quality control review**

- Review of engagement auditor's working papers and procedures
- Review of non-engagement auditor's working papers and procedures

**FOLLOW-UP CONTROL**

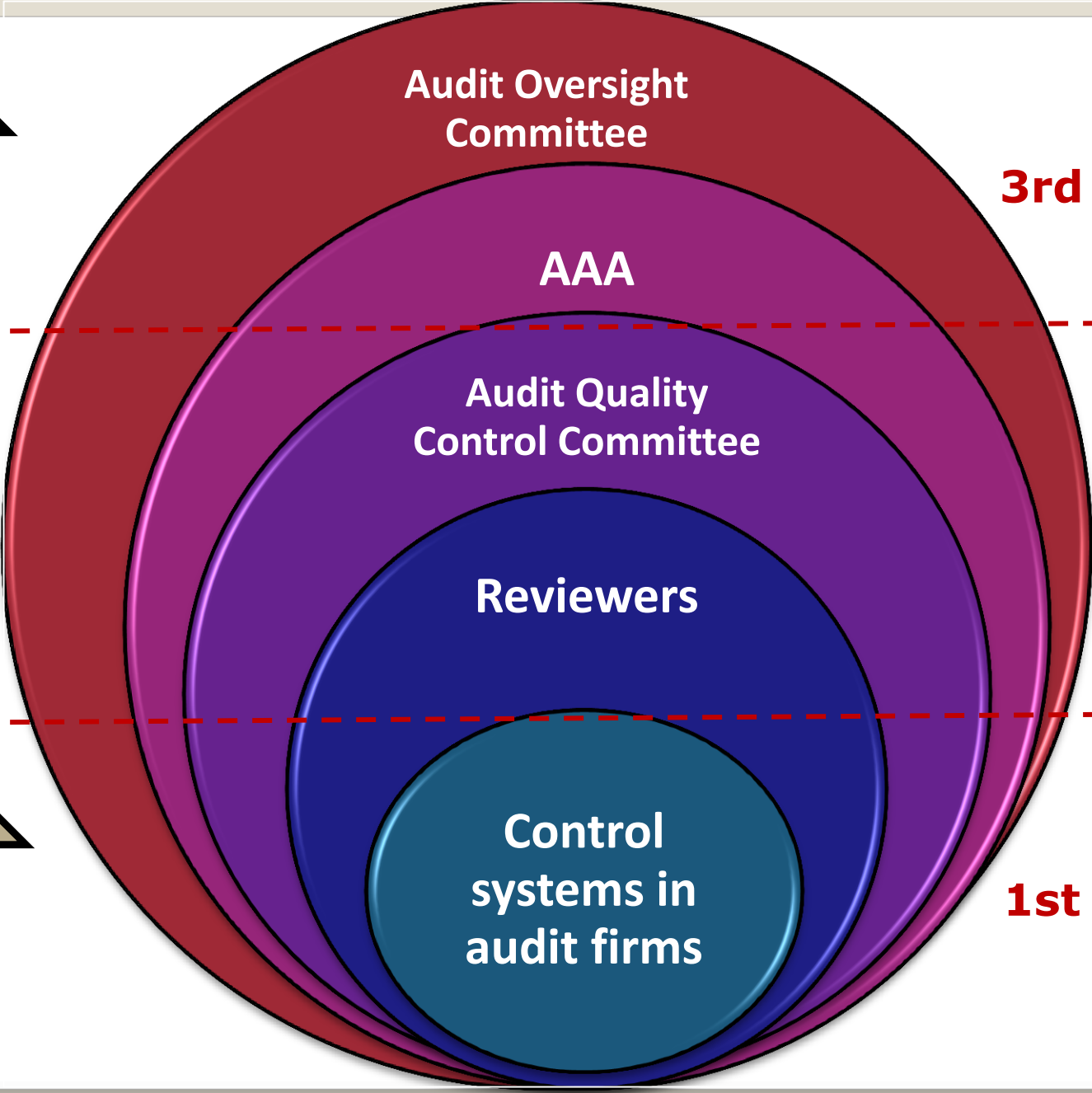
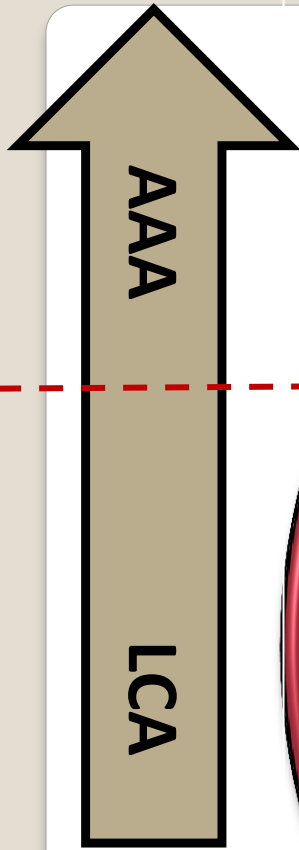
**Performed audit quality control (review) – reviewers and Audit Quality Control Committee**

- Review of working papers

**Public oversight (investigation of performed audit quality control) – AAA and Audit Oversight Committee**

- Review of working papers

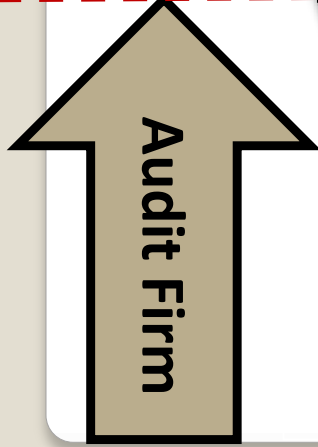
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**3rd level**

**2nd level**

**1st level**



# Independent audit.

## Assurance of audit quality

- ▲ **The AAA together with the LCA implements quality assurance of audits carried out by auditors and audit firms'.**
- ▲ The LCA carries out **quality reviews** of audits at least **each six years** to check all auditors and audit firms.
- ▲ The quality of audits performed by **audit firms registered in Member States** is reviewed in so far as they relate to the statutory audit established by the Law of the Republic of Lithuania.
- ▲ The quality reviews of audits performed by auditors and audit firms, **auditing public-interest entities**, shall be carried out at least on a three years basis.
- ▲ Audit quality reviews are performed by **reviewers**. Audit quality assurance shall be based on **independence**.
- ▲ The AAA carries out **investigation** of audits performed by auditors and audit firms.

## Independent audit. Public oversight

- ▲ The **AAA carries out public review** of audits performed by auditors and audit firms.
- ▲ AAA is a **public body** established in accordance with laws.
- ▲ AAA is **headed** by a Director. The director shall be non-practitioner with at least 3 years experience in the field of audit, accounting, law and/or finances.
- ▲ AAA has established the **Audit Oversight Committee**, a collegiate advisory body. This committee advises the director and structural unit, which carries out public oversight of audit, on issues concerning public oversight of audit.



## Why?

### The reasons behind regulatory changes

- ▲ The **role** of auditors and audit **quality deficiencies** during global financial crisis (lack of scepticism during audits; provision of non-audit services to audit clients)
- ▲ **Gap** between **expectations** of audit clients and users
- ▲ **Lack of communication** between auditors and regulators
- ▲ **Insufficiently coordinated** actions of regulators
- ▲ **Non-harmonised** regulatory framework
- ▲ **Insufficient independence** of audit oversight system

# Directive 2014/56/EU

Sets new and additional requirements for the oversight of audit quality assurance

Provides requirements for audit

Establishes the system informing about infringements of the Directive and the Regulation

Establishes enhanced regulation of audit report

Develops provisions for strengthening the role of an audit committee

Establishes requirements for audit firm's organisational structure

Elaborates professional ethics and independence requirements

Enhances regulation of sanctions

Lists measures to increase competition in the audit market

Expands the scope of the Audit directive

Requirements concerning regulation of audit of public interest entities and oversight were moved from the Directive to Regulation.

# Regulation (EU) No 537/2014

Sets requirements for audits of public interest entities and activities of audit firms

Sets requirement to submit additional report to the audit committee

Establishes enhanced regulation of audit report

Changes requirements for nomination of auditors and audit firms and their rotation

Sets limitations on fees for non-audit services and fees received from one public interest entities

Lists prohibited non-audit services

Lays down more enhanced requirements regarding PIEs engagement quality review

# Situation in Lithuania

- ▲ Currently, Lithuania preparing a **draft law** on amendment to the Law on Audit of the Republic of Lithuania. The most **discussions and disputes** relate to the issue of ensuring optimal and effective audit quality, and establishment and implementation of public oversight system of audit.
- ▲ **NOTE:** The text of new Directive does not include requirements for the **composition of the competent authority**. Therefore, the LCA believes that it may be appropriate to preserve the composition of the oversight system. It should reflect a wide range of stakeholders and not merely government officials, such as representatives of business, regulators and shareholders who are knowledgeable in the areas relevant to statutory audit.

# Proposal to use the option to delegate the oversight of audit quality

Oversight target:		Oversight target:
Audit firm carrying out the statutory audit of public-interest entity	Functions	Audit firm carrying out <b>the statutory audit of non-public interest entity</b>
Delegation possible	Approval and registration of auditors and audit firms carrying out statutory audit	Delegation possible
	Adoption of relevant standards, regulations	
	Ongoing training	
Delegation not possible	Quality assurance system	
Delegation is possible, but only to institution independent from audit profession	Investigations and disciplinary systems	

**Thank you for your attention**