



MEMORANDUM

Reference : AQI 2023
To : Industry for feedback
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AUDIT QUALITY INDICATORS

1. PURPOSE

The purpose of this memorandum is to provide an outline of the research and development phase conducted in relation to the proposed Audit Quality Indicators (AQIs). It is envisioned that the Council for Medical Schemes (CMS) will replace its current auditor accreditation and approval processes and systems to one based on the evaluation of the assessments of AQIs by schemes and their audit committees in the selection of their auditors. The CMS will welcome feedback from schemes, their audit committees, and auditors on the proposed AQIs.

The AQIs proposed in this phase is based on research of what other regulators internationally, as well as the IRBA locally, considered to be appropriate, as well as taking into consideration CMS' own experience specific to the medical scheme industry.

Not all AQIs listed by other regulators and countries were included in our proposal, as this may have resulted in an onerous list of general, non-measurable, irrelevant, or non-material AQIs being included. Only AQIs which are relevant to medical scheme audit committee decision-making processes, were included.

2. BACKGROUND

Section 36(2) requires the Registrar to approve the appointment of the auditor by a medical scheme on an annual basis: “The appointment of an auditor shall not take effect unless it has been approved by the Registrar, subject to such conditions as he or she may deem fit.”

There have been recent developments in the auditing profession, both globally and locally, whereby the various auditing regulators seek to shift more responsibility around the selection and evaluation of auditors and audit quality to the audit committees of entities. The proposed mechanism to achieve this is using Audit Quality Indicators, or AQIs as abbreviated.

Audit Quality Indicators (AQIs) refer to a portfolio of quantitative measures provided by an audit firm to an audit committee of their client, or future client, for use in transparency reports and for regulatory purposes. These measures could be used to enhance dialogue about, and an understanding of, auditors and their audits as well as ways to evaluate their audit quality. That way, users can be better informed about key matters that may contribute to the quality of an audit (both at audit firm level and audit engagement level). This could benefit audit committees in discharging their oversight responsibilities regarding the external audit process, including the appointment or reappointment of the external auditor.

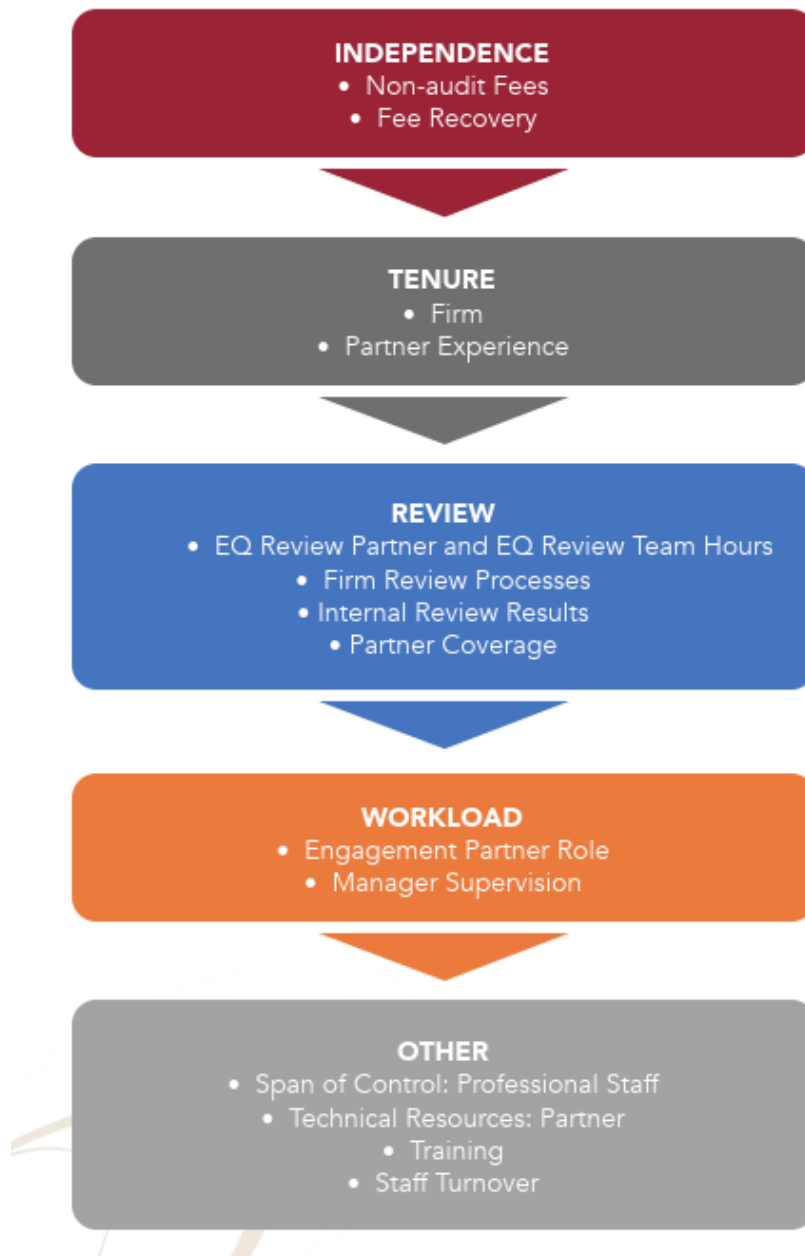
The Independent Regulatory Board for Auditors (IRBA) has published three reports on AQIs, covering the calendar years 2018, 2019 and 2021. The report compared the AQIs of selected audit firms (on an anonymous basis).

IRBA has consulted extensively with various stakeholders while researching global developments on AQIs. As such, the selected AQIs were developed based on those raised most frequently by the stakeholders consulted. Firms use AQIs to help benchmark and manage audit quality internally, while audit committees and others use them when overseeing and assessing the quality of external auditors. The IRBA, on the other hand, relies on AQIs as a source of information for business intelligence gathering and risk-based selections, as part of its inspection process, and to monitor the overall trend of relevant measures impacting audit quality in the profession.

The following diagram illustrates the thematic areas covered by the IRBA report:

*Extract from IRBA AQI Report 2021

OVERVIEW OF AQI CATEGORIES



IRBA engaged CMS in 2021 as part of a survey for our input on AQIs that would be relevant to the medical schemes' environment. We agreed with those areas highlighted in the diagram above. CMS also identified the following additional AQIs that might be relevant in the medical schemes industry (it is in essence an elaboration of the above indicators tailored for medical schemes experience):

- Tenure firm (years) in specific industry (industry knowledge)
- Tenure: partner experience (years) in specific industry (industry knowledge)
- Tenure: EQ* review partner experience (years) in specific industry (industry knowledge)
- Tenure: experts used such as actuaries (years) in specific industry (industry knowledge)
- Tenure: firm (years) – specific entity (client knowledge and rotation)
- Tenure: partner experience (years) – specific entity (client knowledge and rotation)
- Tenure: audit manager experience (years) – specific entity (client knowledge)
- Workload: Engagement partner - nr of entities in specific industry with the same year-end (resource planning)
- Workload: Manager - nr of entities in specific industry with the same year-end (resource planning)
- Provision of an audit plan when the audit partner is responsible for several audits occurring simultaneously (resource planning)
- Technical Resources: availability of CAATS and experts such as actuaries
- Training (hours per person) – IFRS expert in specific industry matter
- IRBA inspection results (firm and engagement partner)
- RI reports issued in respect of specific entity (legislated requirement)
- Reason for termination of appointment (legislated requirement)

*EQ refers to *Engagement Quality*

The benefit of utilising AQI's are as follows:

- These indicators facilitate efficient and effective dialogue between management, audit committees and auditors, leading to improved oversight and project management of the audit.
- AQIs can help create a mutual understanding of the roles and responsibilities of each of the parties related to audit quality.
- They focus discussions on those areas, and factors, of the audit that impact audit quality the most.
- AQIs offer improved knowledge of the audit process as well as a more efficient measurement and an evaluation of audit quality, with a proactive focus on potential weaknesses.
- AQIs can help audit committees to ask the appropriate questions regarding potential weaknesses in the audit quality value chain, and requesting remedial adjustments to be made, e.g., to audit resourcing.

3. SOURCES

CMS considered AQIs developed by international regulators (and IRBA locally) as part of our research on AQIs. CMS' own experience specific to the medical scheme industry was also considered. Accountancy Europe produced a concise summary of AQIs used / proposed by various international regulators.

Kindly refer to the link below for a summary of AQI's from various international regulators in the Accountancy Europe document:

[Accountancy Europe – Audit Quality Indicators – A Global Overview of Initiatives.](#)

Of particular interest, were the results of the following regulators (please click on the links for the detailed documents):

- Canada - Canadian Public Accountability Board ([CPAB](#))
- Germany – Institute of Public Auditors ([IDW](#))
- UK – Public Company Accounting Oversight Board ([PCAOB](#))
- South Africa – Independent Regulatory Board for Auditors ([IRBA](#))

4. RESEARCH RESULTS

Extracts from the Accountancy Europe document is summarised below:

INSTITUTE OF PUBLIC AUDITORS (IDW), GERMANY

In its [position paper](#) (December 2021), the IDW explains what constitutes audit quality from the profession's point of view, and how it can be measured and evaluated. The position paper shows which criteria can be relevant when selecting AQIs to assess the audit quality. In addition, it presents various aspects to be considered when interpreting AQIs.

Finally, it proposes a set of AQIs under the components listed below. The indicators are classified as either firm-related or engagement-related for each component.

Component	AQIs
Quality culture	<ul style="list-style-type: none"> ▪ governance ▪ leadership ▪ professional scepticism & independence
Workforce quality	<ul style="list-style-type: none"> ▪ expertise ▪ industry understanding & experience
Process quality	<ul style="list-style-type: none"> ▪ availability of human and technical resources ▪ involvement ▪ IT systems & audit tools ▪ fit of the audit process ▪ quality management process
Communications	<ul style="list-style-type: none"> ▪ communication with the supervisory body ▪ communication with the management
Cross-divisional AQIs	

CANADIAN PUBLIC ACCOUNTABILITY BOARD (CPAB), CANADA

In 2016, the CPAB launched an exploratory AQI pilot project to get feedback on AQIs' usefulness and support broader national and international discussions. The results of the initiative were summarised in [the final report](#) published in 2018. The report provides the following set of AQIs as an example:

Type	AQIs
Engagement team indicators	<ul style="list-style-type: none"> ▪ experience of engagement team* ▪ training and professional development ▪ turnover of the engagement team ▪ partner/manager involvement ▪ partner workload
Audit execution indicators	<ul style="list-style-type: none"> ▪ audit hours by areas of significant risk* ▪ timing of audit execution* ▪ audit progress milestones ▪ technology in the audit ▪ specialist engagement* ▪ service delivery centres
Management indicators	<ul style="list-style-type: none"> ▪ management deliverables* ▪ remediation of control deficiencies ▪ reliance on controls
Firm-level indicators	<ul style="list-style-type: none"> ▪ results of inspections ▪ independence ▪ reputation ▪ tone at the top
Client service indicators	<ul style="list-style-type: none"> ▪ communication with the audit committee ▪ sharing of insights

INDEPENDENT REGULATORY BOARD FOR AUDITORS (IRBA), SOUTH AFRICA

The IRBA published a [survey report](#) in 2021 on AQIs. Firms auditing listed companies were requested to submit AQI-related information and the report describes the results of the information submitted, under the five broad thematic categories:

Category	AQIs
Independence	<ul style="list-style-type: none"> ▪ non-audit fees (%) - as a percentage of the total audit fees billed to audit clients ▪ fee recovery (%) - audit fees billed as a percentage of the total audit fees internally charged
Tenure	<ul style="list-style-type: none"> ▪ firm (years) - average number of completed years as the audit firm for the audit client ▪ partner experience (years) - average tenure as an engagement partner
Internal firm quality review processes	<ul style="list-style-type: none"> ▪ engagement quality review partner hours and engagement quality review team hours (%) ▪ firm review processes ▪ internal review results (%) ▪ partner coverage (%)
Workload of partners and audit managers	<ul style="list-style-type: none"> ▪ engagement partner role (%) ▪ manager supervision (%)
Other	<ul style="list-style-type: none"> ▪ span of control: professional staff (ratio) ▪ technical resources: partner (ratio) ▪ training (hours per person) ▪ staff turnover (%)

An extract from the PCAOB document follows below:



PCAOB Release No. 2015-005
 July 1, 2015
 Page 13

The 28 potential indicators are:²⁰

AUDIT PROFESSIONALS	Availability	1. Staffing Leverage 2. Partner Workload 3. Manager and Staff Workload 4. Technical Accounting and Auditing Resources 5. Persons with Specialized Skill and Knowledge
	Competence	6. Experience of Audit Personnel 7. Industry Expertise of Audit Personnel 8. Turnover of Audit Personnel 9. Amount of Audit Work Centralized at Service Centers 10. Training Hours per Audit Professional
	Focus	11. Audit Hours and Risk Areas 12. Allocation of Audit Hours to Phases of the Audit
AUDIT PROCESS	Tone at the Top and Leadership	13. Results of Independent Survey of Firm Personnel
	Incentives	14. Quality Ratings and Compensation 15. Audit Fees, Effort, and Client Risk
	Independence	16. Compliance with Independence Requirements
	Infrastructure	17. Investment in Infrastructure Supporting Quality Auditing
	Monitoring and Remediation	18. Audit Firms' Internal Quality Review Results 19. PCAOB Inspection Results 20. Technical Competency Testing
AUDIT RESULTS	Financial Statements	21. Frequency and Impact of Financial Statement Restatements for Errors 22. Fraud and other Financial Reporting Misconduct 23. Inferring Audit Quality from Measures of Financial Reporting Quality
	Internal Control	24. Timely Reporting of Internal Control Weaknesses
	Going Concern	25. Timely Reporting of Going Concern Issues
	Communications between Auditors and Audit Committee	26. Results of Independent Surveys of Audit Committee Members
	Enforcement and Litigation	27. Trends in PCAOB and SEC Enforcement Proceedings 28. Trends in Private Litigation

5. SELECTED AQI's

The CMS is proposing the following list of 25 AQIs across key areas for consideration by the medical schemes industry:

A) Firm: Independence		Sources and Comment
The firm is independent with no conflicts of interest.		IRBA, PCAOB
i.	Mature client acceptance and continuation processes	General
ii.	Audit fee in relation to total firm fees (%)	IRBA
iii.	Non-audit fees (%)	IRBA
iv.	Audit tenure: firm (years)	IRBA
B) Firm: Audit quality and technical competence		Sources and Comment
i.	Prior experience in auditing medical schemes	PCAOB, IRBA, GERMANY
ii.	Internal quality reviews	IRBA, GERMANY, PCAOB
iii.	Technical accounting department and use of other experts	GERMANY, CANADA, PCAOB
iv.	IT audit capability	GERMANY, CANADA, PCAOB
v.	Regular training	GERMANY, CANADA, IRBA, PCAOB
C) Firm: External reviews by Regulators (IRBA and CMS)		Sources and Comment
The IRBA has performed a recent firm wide review, and the auditor has provided this to the audit committee for assessment		CANADA
i.	Firm's leadership and ethics	CMS
ii.	Audit quality and engagement performance	CMS
iii.	Monitoring and review processes	CMS
iv.	Referred to Investigation Department	CMS
v.	CMS findings	CMS
D) Engagement partner and audit team: Independence		Sources and Comment
The engagement partner and engagement team are independent of the Medical Scheme.		IRBA, PCAOB, CANADA
i.	Audit tenure: engagement partner (years)	IRBA
E) Engagement partner and audit team: Audit quality and technical competence		Sources and Comment
i.	Prior experience in auditing medical schemes.	PCAOB, CANADA GERMANY
ii.	Knowledge of relevant legislation and industry guidelines	PCAOB, CANADA GERMANY
iii.	Adequate resource allocation	GERMANY, CANADA, PCAOB
iv.	Engagement partner workload	IRBA, PCAOB, CANADA
v.	Management supervision workload (%)	IRBA, CANADA
vi.	Retraction of audit opinion	CMS

F) Engagement partner and audit team: External reviews by Regulators (IRBA and CMS)		Sources and Comment
The IRBA has performed a recent review on the engagement partner, and the auditor has provided this to the audit committee for assessment		CANADA
i.	Referral to Investigation Department	CMS
ii.	IRBA findings and offences	CMS
iii.	Results of individual IRBA reviews and inspections	CMS
iv.	CMS findings	CMS

6. AQI OBSERVATIONS

A) Firm: Independence

The firm is independent from the Medical Scheme with no conflicts of interest.

i. Mature client acceptance and continuation processes

Description / purpose

Firm has a mature client acceptance and continuation processes which assess independence prior to engagement acceptance.

How to interpret the AQI

This is a measure that may indicate threats to independence. It is an indicator that measures whether the audit firm has consistent and thorough processes and frameworks in place to identify, assess and respond to independence threats prior to accepting audit clients.

ii. Audit fee in relation to total firm fees (%)

Description / purpose

Audit fees billed (rands invoiced) to the audit client as a percentage of the total audit fees billed by the firm (rands invoiced) to all their audit clients for completed engagements.

How to interpret the AQI

This is a measure that may indicate threats to independence. It is an indicator that measures the extent to which the firm is dependent on a particular client for audit fees.

iii. Non-audit fees (%)

Description / purpose

Non-audit fees billed (rands invoiced) to the audit client as a percentage of the total audit fees billed (rands invoiced) to the audit client for completed engagements.

How to interpret the AQI

This is a measure that may indicate threats to independence. It is an indicator that measures the extent to which the firm is dependent on a particular client for audit versus non-audit fees.

iv. Audit tenure: firm (years)

Description / purpose

The audit tenure (i.e., number of years) the firm had been responsible for the audit engagement.

Mandatory Audit Firm Rotation (MAFR) is required for auditors of all public interest entities (PIE), as defined in Sections 290.25 to 290.26 of the amended IRBA Code of Professional Conduct for Registered Auditors with effect 1 April 2023.

How to interpret the AQI

This is a measure that may indicate a familiarity risk. The longer the tenure, the greater the familiarity threat to independence. Alternatively, the shorter the tenure, the greater the risk of lack of experience and knowledge of the business of the medical scheme.

Familiarity threat – the threat that due to a long or close relationship with a client, a registered auditor will be too sympathetic to that client's interests or too accepting of their work.

B) Firm: Audit quality and technical competence

i. Prior experience in auditing medical schemes

Description / purpose

The firm has prior experience in auditing medical schemes. Consider the number of years' experience by active engagement partners, and the number of medical schemes audited.

If no prior experience, has the firm considered proposing a joint audit arrangement with a firm that has medical scheme experience.

How to interpret the AQI

This is a measure that indicates industry-specific experience. Audit committees can assess whether the firm has extensive knowledge of the industry and adequate experience in the audit of medical schemes.

ii. Internal quality reviews

Description / purpose

The firm has a robust process for conducting internal quality reviews and acts upon recommendations for improvement.

Consider the following:

- the number of satisfactory reviews as a percentage of total reviews;
- The number of partners reviewed as a percentage of the total number of partners that signed off engagements; and
- The number of engagements selected as a percentage of total number of engagements signed off.

How to interpret the AQI

This is a measure that may indicate that the firm takes a proactive approach to, and give priority to, audit quality. Compared to external regulatory inspections, internal quality reviews should be more frequent and of higher coverage. This can be assessed by the frequency that audit partners are selected for review and by monitoring the results of the reviews over time.

iii. Technical accounting department and use of other experts

Description / purpose

The firm has a dedicated technical department to assist with complex accounting issues. Are these experts familiar with medical scheme / insurance industry pertinent issues? If no internal dedicated department exists, has the firm any agreement with external technical experts?

The firm has access to other experts such as actuaries.

How to interpret the AQI

This is a measure that may provide insight into the technical capabilities of the firm. The medical scheme industry is considered to be a complex environment, and as such expert advice might be required to evaluate management judgements and estimations.

iv. IT audit capability

Description / purpose

The firm has the required Information Technology (IT) audit capability with regards to assessing IT General Controls, IT controls and performing Computer Assisted Audit Techniques.

How to interpret the AQI

Many core processes of medical schemes require the use of automation, data analytics, IT controls and the integration of various internal and external IT systems. This measure provide insight into not only the technical capabilities of the audit firm, but also how it relates to audit efficiency.

v. Regular training

Description / purpose

The firm's staff attend regular training with regards to IFRS and audit methodology.

How to interpret the AQI

This is a measure that may provide insight into the overall professionalism, technical competency and audit quality delivered by the firm.

C) Firm: External reviews by Regulators (IRBA and CMS)

The IRBA has performed a recent firm wide review, and the auditor has provided this to the audit committee for assessment.

i. Firm's leadership and ethics

Description / purpose

The IRBA noted findings on the firm's leadership and ethics. Consider the audit firms response in their remedial action plans, where necessary.

How to interpret the AQI

This is a measure that provides insight into the overall level of professionalism and ethical standards applied by the firm.

ii. Audit quality and engagement performance

Description / purpose

The IRBA noted findings on the firm's audit quality and engagement performance. Consider the audit firms response in their remedial action plans, where necessary.

How to interpret the AQI

This is a measure that may provide insight into the overall audit quality delivered by engagement teams, as assessed through the eyes of an independent regulator.

iii. Monitoring and review processes

Description / purpose

The IRBA noted findings on the firm's monitoring and review processes. Consider the audit firms response in their remedial action plans, where necessary.

How to interpret the AQI

This is a measure that may provide insight into the ability of the audit firm in identifying and improving upon areas of weakness in audit quality.

iv. Referral to Investigation Department

Description / purpose

The IRBA has referred the firm to its Investigation Department.

How to interpret the AQI

This is a measure that may provide insight into the overall attitude of the firm's leadership and how it translates to audit quality.

v. CMS findings

Description / purpose

Was the audit firm rejected or sanctions imposed on it by the CMS in the past?

How to interpret the AQI

This is a measure that may provide insight into the firm's technical capabilities and audit quality delivered as assessed by an independent regulator operating in the medical scheme industry's specialised environment.

D) Engagement partner and audit team: Independence

The engagement partner and engagement team are independent of the medical scheme.

i. Audit tenure: engagement partner (years)

Description / purpose

The audit tenure (i.e., number of years) the engagement partner had been responsible for the audit engagement.

How to interpret the AQI

This is a measure that may indicate a familiarity risk. The longer the tenure, the greater the familiarity threat to independence. Alternatively, the shorter the tenure, the greater the risk of lack of experience and knowledge of the business of the medical scheme.

Familiarity threat – the threat that due to a long or close relationship with a client, a registered auditor will be too sympathetic to that client's interests or too accepting of their work.

E) Engagement partner and audit team: Audit quality and technical competence

i. Prior experience in auditing medical schemes

Description / purpose

The engagement partner has prior experience in auditing medical schemes. Consider the number of years' experience, and the number of medical schemes audited.

If no prior experience, the engagement partner allowed for oversight and guidance using an engagement quality review partner with medical scheme experience.

How to interpret the AQI

This is a measure that indicates industry-specific experience. Audit committees can assess whether the individual auditor has extensive knowledge of the industry and adequate experience in the audit of medical schemes.

ii. Knowledge of relevant legislation and industry guidelines

Description / purpose

The engagement partner and engagement team are familiar with relevant legislation applicable to the medical scheme industry i.e., the MS Act, NCA, CPA, POPIA, TPCA, FAIS Act, FIC Act.

The engagement partner and engagement team are familiar with the SAICA Medical Scheme Accounting Guide, and IRBA Medical Scheme Auditing Guide.

How to interpret the AQI

This is a measure that may provide insight into the technical competence of the engagement partner and engagement team. The medical scheme industry is a highly complex environment and has specific accounting and auditing requirements that needs be adhered to.

iii. Adequate resource allocation

Description / purpose

The firm has assigned adequate staff and engagement partner hours to the planning, execution, and completion phases of the audit.

How to interpret the AQI

This is a measure that may indicate that the audit team has assigned adequate resources to successfully deliver a quality audit within specified timeframes with adequate level of review at all stages. The hours assigned by the audit team should be aligned with expected volume, complexity and reporting timelines required.

iv. Engagement partner workload

Description / purpose

The engagement partner has adequate workload capacity and assigned sufficient hours to the engagement:

- Total partner hours assigned
- Number of concurrent engagements within same timeframe

Adequate engagement partner review time (% of total hours) has been assigned to the engagement at all stages of the audit:

- Planning
- Execution
- Completion

How to interpret the AQI

Higher hours indicate a greater involvement of the engagement partner and may be indicative of a higher quality audit file, or an audit with more areas of significant judgement. Alternatively, higher hours may indicate an understaffed or inexperienced engagement team, or other execution issues.

v. Management supervision workload (%)

Description / purpose

Total audit manager hours as a percentage of total audit hours.

How to interpret the AQI

Higher ratios indicate a greater involvement of the audit manager/s; and there may be many reasons for such involvement. Alternatively, high ratios may indicate a lack of review and involvement by the engagement partner and/or an understaffed engagement team.

vi. Retraction of audit opinion

Description / purpose

Has the engagement partner ever had to retract an audit opinion?

How to interpret the AQI

This is a measure that may provide insight into the due care and professionalism applied by the engagement partner.

F) Engagement partner and audit team: External reviews by Regulators (IRBA and CMS)

The IRBA has performed a recent review on the engagement partner, and the auditor has provided this to the audit committee for assessment.

i. Referral to Investigation Department

Description / purpose

Has the engagement partner been referred to IRBA's investigation department in the past?

How to interpret the AQI

This is a measure that may provide insight into the overall attitude of the engagement partner with regards to leadership, professionalism, and ethics. It also provides insight into the overall audit quality delivered by the engagement partner, as assessed through the eyes of an independent regulator.

ii. IRBA findings and offences

Description / purpose

Has the engagement partner been found guilty of an offence by the IRBA?

How to interpret the AQI

This is a measure that may provide insight into the overall attitude of the engagement partner with regards to leadership, professionalism, and ethics. It also provides insight into the overall audit quality delivered by the engagement partner. Audit committees should evaluate the nature and materiality of the offence.

iii. Results of individual IRBA reviews and inspections

Description / purpose

Has the engagement partner provided the results of their individual IRBA reviews and inspections and provided remedial action plans where necessary?

How to interpret the AQI

This is a measure that may provide insight into the overall attitude of the engagement partner with regards to leadership, professionalism, and ethics. It also provides insight into the overall audit quality delivered by the engagement partner. Audit committees should evaluate the nature and materiality of the findings and relevant remedial action plans.

iv. CMS findings

Description / purpose

Has the engagement partner's authorisation / approval been rejected by the CMS in the past?

How to interpret the AQI

This is a measure that may provide insight into the engagement partner's technical capabilities and audit quality delivered as assessed by an independent regulator operating in the medical scheme industry's specialised environment.

7. CONCLUSION

The CMS is of the opinion that the above AQI's can be considered easily measurable, information easily obtainable and evaluated, and are key areas for consideration by an audit committee of a medical scheme in appointing an auditor as it addresses independence, technical skill, experience, resourcing, and quality.

It is proposed that the above AQI's be approved as a conceptual framework for engagement with various stakeholders.

The industry (specifically medical schemes and their audit committees, and auditors) and IRBA are invited to provide further comment on the above.

Kindly provide feedback to Sameer Rajab via email (s.rajab@medicalschemes.co.za) by no later than 23 March 2023.