



**金融監督管理委員會**  
**Financial Supervisory Commission**

2018 CPA Firm Inspection

# **General Inspection Report**

**Financial Supervisory Commission, Taiwan**

May 2019

*This is an English translation of the original Traditional Chinese text. In the event of any inconsistency between this translation and the original text, the latter shall prevail for all purposes.*

## **I. Introduction**

### **(I) The purpose and principle of CPA firm inspection**

Article 19 of the 'Certified Public Accountant (CPA) Act' provides as follows: "In order to safeguard the interests of the general public and promote the good of society, the competent authority may dispatch personnel to inspect the operations and operations-related financial status of a CPA firm that has been approved to provide attestation services to public companies. A CPA firm may not avoid, impede, or refuse to cooperate with such an inspection." The purpose of such inspections is to ensure high audit quality, enhance the internal quality control of CPA firms, and reduce the potential risks of audit failure. Through the inspection mechanism and promotion of high quality auditing, the FSC aims to increase public confidence in the audit opinions of accountants and financial reporting, and has no punitive intent. If an accountant is found to have made material error or committed negligence in attestation on financial reports, or seriously violated Article 61 of the CPA Act to the extent of damaging the accountant's reputation, the FSC will transfer the case to the CPA Discipline Committee for disciplinary actions.

### **(II) 2018 overall inspection findings**

The FSC inspection team has inspected 4 joint CPA firms during 2018 and focused on quality control systems of CPA firms and audit engagement reviews. The inspection results were as follows:

- i. Quality control systems: There were 45 quality control findings in 2018. This was a significant increase compared to 7 findings across 3 CPA firms inspected last year (2017). Most inspected targets in 2018 were mid-tier CPA firms while all were large-sized ones in 2017. The resources and employees of mid-tier firms were much less than their larger counterparts, hence there were more inspection findings.
- ii. Audit engagement reviews: There were 22 findings across 7 engagements reviewed in 2018, which increased 46% compared to last year (2017). The increase was due to difference in the number of engagement reviews (There were 6 samples in 2017), as well as the size difference of the inspected CPA firms. As a result of lack of resources and employees, mid-tier CPA firms were unable to implement internal

quality control as effectively as large CPA firms, hence there were more review findings.

**(III) Improvement in audit quality**

The FSC will propose a draft General Inspection Report within 1-2 months after the on-site inspection. The inspected firms are required to provide written opinions on inspection observations and findings within 30 days, submit improvement projects to FSC within 2 months and continue to track the improvement. If firms did not execute the improvement projects, or address findings within the prescribed period by the FSC, the FSC may rescind or repeal approval of the inspected CPA firm to conduct auditing and attesting businesses for public company financial reports under Article 10.1. (6) of the Regulations Governing Approval of Certified Public Accountants to Audit and Attest to the Financial Reports of Public Companies’.

**(IV) Communication between CPA and Managers and Audit Committee**

Managers and audit committee of public companies are responsible for the preparation and fair presentation of financial statements. To ensure the quality of financial statements, they can enhance communication with CPAs by including common findings in the Inspection Findings Survey Report issued by International Forum of Independent Audit Regulators (IFIAR) into communicative items.

**II. Domestic Accounting Profession Profile:**

- (I) As of the end of Dec. 2018, the number of CPAs and the distribution of the types of CPA firms and practicing CPAs were as follows:

Status of CPAs	Num.	%
Have applied to conduct auditing and attesting for public company financial reports	711	9.32
Have applied to the competent authority for practice registration	3,471	45.5
Hold CPA certificate but do not practice as a CPA	4,154	54.5
Hold CPA certificate	7,625	100

Single-person CPA firm		Joint CPA firm		Co-location CPA firm		Total
Num.	%	Num.	%	Num.	%	
1,543	77%	431	21%	35	2%	2,009

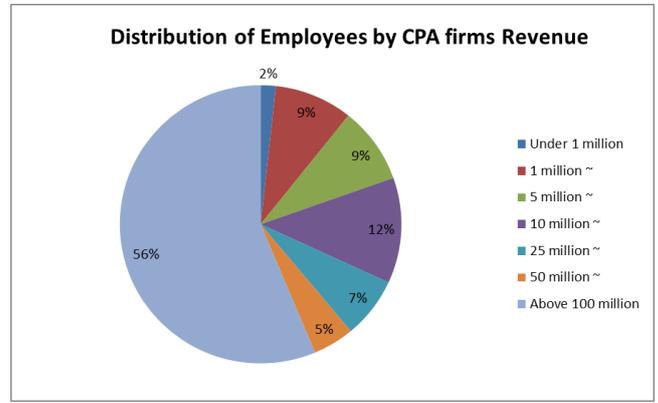
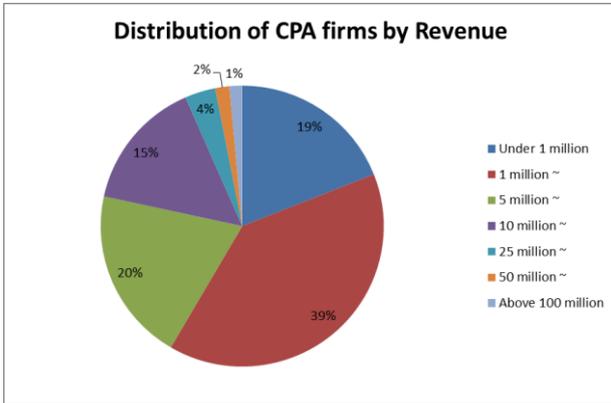
CPAs that have applied to the competent authority for practice registration	Big Four* CPA firms	Mid-tier CPA firms
Have applied to conduct auditing and attesting for public company financial reports	336	375
Have not applied to conduct auditing and attesting for public company financial reports	40	2,720

\* The Big Four CPA firms in Taiwan are Deloitte, PwC, KPMG and Ernst & Young.

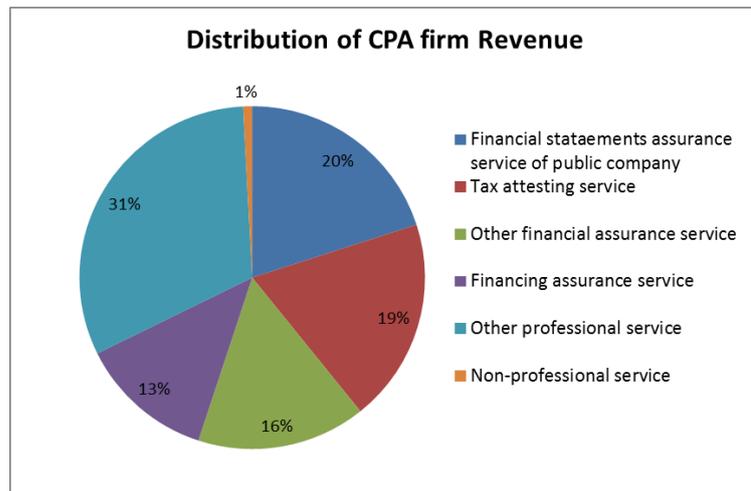
- (II) According to the latest Annual Survey of the Accounting Profession in Taiwan, the figures for the revenue of the 1,111 surveyed CPA firms and the number of employees at the end of 2018 were:

1. The scale of CPA firm revenue:

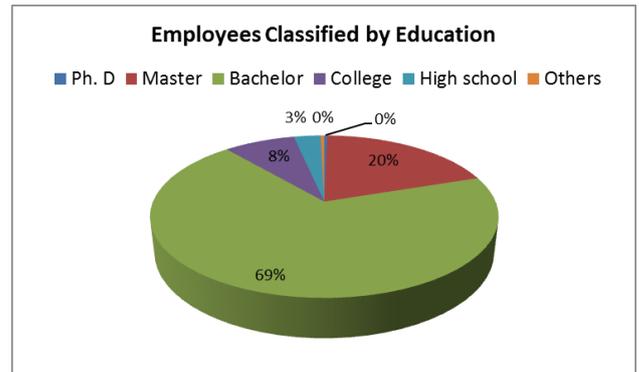
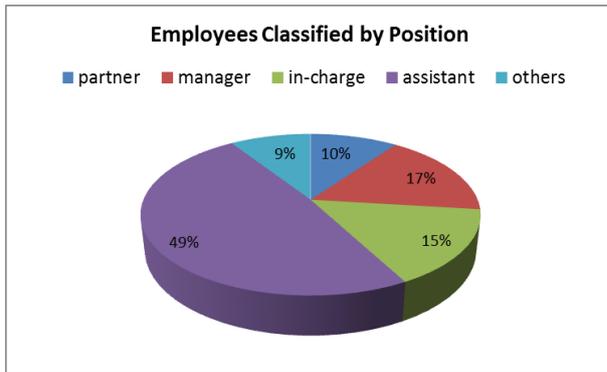
Revenue range (NTD)	Num. of CPA firms		Num. of employees		2016 Revenue	
	Firm Num.	%	Employee Num.	%	Revenue (thousand)	%
Total	1,111	100.0	21,344	100.0	30,178,598	100.0
Under 1 million	211	19.0	370	1.7	91,309	0.3
1 million ~	438	39.4	1,917	9.0	1,181,865	3.9
5 million ~	222	20.0	1,895	8.9	1,557,462	5.2
10 million ~	167	15.0	2,619	12.3	2,485,610	8.2
25 million ~	39	3.5	1,509	7.1	1,418,912	4.7
50 million ~	18	1.6	1,014	4.8	1,190,474	3.9
Above 100 million	16	1.4	12,020	56.3	22,252,966	73.7



2. The type of CPA firm revenue: According to the Annual Survey of the Accounting Profession, the major part of firm revenue in 2018 was from professional service revenue (99.2%), with non-professional service only 0.8%. Of professional service revenue, financial statement assurance service for public companies, the tax attesting service, other financial assurance service, financing assurance service and other professional services accounted for 20%, 19.2%, 15.8%, 12.7%, and 31.4%, respectively.



3. Composition of employees: There were 21,344 employees in the 1,111 CPA firms surveyed. The position categories were assistants, managers, in-charge, partners, and others (49%, 17%, 15%, 10% and 9%, respectively). In addition, classified by educational level, employees were mainly bachelor's, master's, and college level (69%, 20%, and 8%, respectively).



### III. Inspection Methodology:

#### (I) Inspection Principle, Focal Points, and Methodology

1. Inspection principle: The FSC carries out CPA firm inspection with a Risk-Based Approach in terms of inspected firm and audit engagement selection. The FSC also provides guidance and assistance for CPA firms to establish internal control quality system in line with regulations and Generally Accepted Auditing Standards (GAAS) and mandates the CPA firms to take improvement measures with the aim of improving audit quality.

2. Focal points of inspections:

##### (1) Quality control systems

Inspectors review firm policies, procedures, and audit engagements to assess whether the audit firm's quality control system is carried out in accordance with the requirements of the Taiwan Statement of Auditing Standards No. 46 Quality Control for Firms ("SAS No. 46" hereafter). The specific areas of the quality control system that inspection procedures address include the following:

- A. Leadership responsibility for quality control in the firm (Tone

at the top)

- B. Independence
- C. Client acceptance and continuance (risk management mechanism)
- D. Human resources (partner evaluation, compensation, admission, assignment of engagement team, and continuing professional training)
- E. Engagement performance (engagement quality control review, consultation, and disagreement)
- F. Monitoring (the firm's internal inspection program, communications, corrective actions, and follow-up of identified deficiencies)

(2) Audit engagements reviews

- A. Inspection focus and selection of audit engagements are planned annually with a risk-based approach.
- B. Audit engagements are selected by the FSC considering public interest, materiality and other risk factors, without influence from or limitation by the inspected firm.

3. Inspection Methodology

(1) Review of quality control systems

- A. Understand the CPA firm's quality control policies and procedures through interviews and related documents.
- B. Evaluate the design of the inspected CPA firm's internal quality control system.
- C. Conduct appropriate compliance tests to assess the effectiveness of the quality control system.

(2) Audit engagement reviews

- A. Interview the engagement partner and the engagement

team manager to understand risk assessment, audit focus, and audit method.

- B. Review the working papers to examine whether the audit conforms with the Regulations Governing Auditing and Attestation of Financial Statements by CPAs and the Taiwan SAS.
- C. Assess the effectiveness of the firm's quality control system through the findings of the individual audit engagement review.

**(II) Limitations of inspection results:**

- 1. Due to various factors (e.g. firm size, business model, nature of its clientele, and risk management strategies), different firms adopt different policies and procedures to comply with relevant laws and regulations and fulfill professional responsibilities.
- 2. This FSC general inspection report should not be regarded as an endorsement of a CPA's audit, nor should it be regarded as assurance that audited financial statements are free of any deficiencies, even if there was no deficiency noted in the inspection report.

**(III) Areas of future focus:**

- 1. **Continuing focus on audit quality:** Audit quality is the foundation for robust development of capital markets. When conducting the inspections, the FSC shall focus on improving and maintaining audit quality and the execution of relevant systems in CPA firms. The firms' system should include matters relating to promotion of high audit quality culture, assignment of responsibility and accountability of quality control between partners and staff, and independence of evaluation.
- 2. **Focusing on "Key Audit Area" and expanding number of audit engagement reviews:** To enhance the effectiveness of the inspection, the FSC plans to adjust the methodology of audit engagement reviews on the basis of a risk-based approach, including expanding samples and focusing on Key Audit Area in 2019. Key Audit Area is comprised of common inspection findings, audit areas ignored by CPAs recently

(e.g. : evaluation of impairment loss), as well as the evaluation, communication and audit of Key Audit Matters.

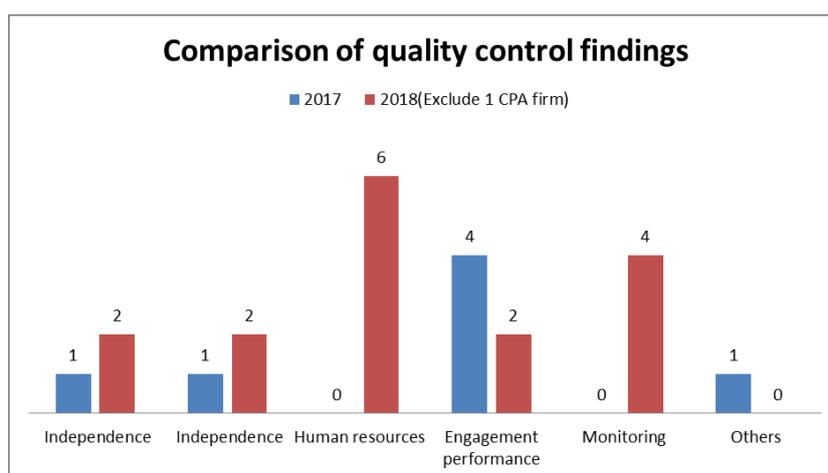
#### IV. Inspection Findings in 2018:

In 2018, the Financial Supervisory Commission (FSC) conducted on-site inspections of four joint CPA firms. The findings were:

##### (I) Quality control systems:

1. The inspectors found 45 quality control findings in 2018, which was a significant increase compared to 7 findings across 3 CPA firms inspected last year (2017). Most inspected targets in 2018 were mid-tier CPA firms while all were large-sized ones in 2017. The resources and employees of mid-tier firms were much less than their larger counterparts, hence there were more inspection findings. Furthermore, one mid-tier CPA firm inspected for the first time was found to have more deficiencies than its peers. In summary, after excluding the firm mentioned above, the findings were mainly related to Human Resources and Monitoring.

	2017	2018	2019
Number of inspection findings	7	16	9
Average findings per CPA firm	2.3	4	1.7



2. In review of the design and implementation of firm-wide audit quality control system, inspectors observed the following deficiencies that need to be addressed:

**(1) Leadership responsibility for quality control in the firm**

The manager did not take “understanding and compliance of audit quality control system and relevant procedures” into account when evaluating staff performance, which violated firm policy.

**(2) Ethical requirements**

- A. The firm only evaluated CPA independence, but left out other personnel subject to independent regulations in an engagement. In some cases, the CPA’s spouses held the shares of audit clients, which violated Article 16 of SAS No.46.
- B. The firm did not establish a control system pertaining to rotation of CPAs, as required under Article 20 of SAS No.46.
- C. The firm did not establish policy pertaining to rotation of audit quality reviewers and senior staff, as required under Article 20, 66-68 of SAS No.46.
- D. Staff interviewed were not familiar with the independence policy and procedures of the firm.
- E. The firm did not review the compliance of independence policy.

**(3) Client acceptance and continuance**

- A. The firm did not consult other partners for consent when deciding whether to accept an engagement with a new client.
- B. The firm did not establish client acceptance and continuance policy, as required under Article 21-25 and 72 of SAS No.46.
- C. The firm did not document evaluation procedures of client

acceptance and continuance, which violated Article 22 of SAS No.46.

- D. The firm had provided attestation service to a client before signing an engagement contract.

**(4) Human resources**

- A. The firm did not establish control measures to ensure that employees finished professional education and training, as required under Article 76 of SAS No.46.
- B. The firm did not establish promotion standards and disciplinary action to ensure employees complied with the firm's policy, as required under Article 74 and 77 of SAS No.46.
- C. The firm did not establish qualification evaluation procedures for promotion to partner, as required under Article 74 of SAS No.46.
- D. The firm did not update relevant procedures with changes of performance evaluation methodology for partners, which violated Article 57 of SAS No.46.
- E. The prescribed minimum education hours of CPAs conducting auditing and attesting for public company financial reports did not meet the requirement of Article 5 of Regulations Governing CPA Continuing Professional Education'.
- F. Other circumstances not in line with firm policies were:
  - i. The firm did not establish access and modification restrictions for firm policies and materials which were placed in the intranet folder.
  - ii. The firm did not establish a CPA workload system.
  - iii. The firm did not consider results of employee education and training in performance evaluation.

- iv. The procedures regarding promotion of newly promoted partners were not in line with firm policy.

**(5) Engagement performance**

- A. The firm's archive policy was not in line with Article 102 and 103 of SAS No.46. The policy stipulated that the filing of working papers could be finished in 60 days after the issuance of the certification of business/Income tax, on condition that it was issued simultaneously with the audit report and if a managing partner had approved it.
- B. The firm's policy stipulated that audit quality reviewer and the assistant reviewer could be the same person, which violated Article 97 of SAS No.46.
- C. The firm did not establish control system to prevent the working papers being tampered with without authorization or lost, as required under Article 105 of SAS No.46.
- D. There was no independence announcement and engagement record of the audit quality reviewer in an audit engagement, as required under Article 92 of SAS No.46.
- E. The reviewer did not sign the date on which audit quality review was completed, it was done by the audit team after reporting date was determined, which violated Article 93 of SAS No.46.
- F. The audit team did not utilize professional skepticism in determining the materiality of an engagement, as required under Article 4, 19 and 23 of SAS No.51.
- G. The firm did not specify the 6 types of financial reports of public companies that should be reviewed, which violated Article 32 of SAS No.46.
- H. The firm did not document evaluation procedures of audit quality reviewer's qualification and competency as well as stipulating the professional qualifications of the reviewer in different engagement situations, as required under Article

37 and 95 of SAS No.46.

- I. The firm did not establish relevant procedures pertaining to engagement implementation, as required under Article 37, 39, 44, 97, 105, 106 and 111 of SAS No.46.
- J. The firm did not document engagements being reviewed, attesting CPA, time, scope, results of the review, recommendations and continuous tracking of improvement, which violated Article 120 of SAS No.46.
- K. There were inconsistencies in borrowing and storage periods, file categories and file name stipulated in the firm's archive management regulations.
- L. Other situations not in line with the firm's archive management regulations were:
  - i. There was no lending record of working papers by external units in lending register book.
  - ii. The firm did not register borrowers, reasons and borrowing date of working papers in lending register book.

**(6) Monitoring**

- A. The firm did not review audit quality, and ensure the performance and operation of quality control system, as required under Article 46 and 112 of SAS No.46.
- B. The firm did not convene evaluation meetings as well as executing a motivation system.
- C. Monitoring personnel were not familiar with the procedures, and unable to determine the number of inspected engagements and firms. In addition, they did not sign the checklists to prove they had completed the required procedures.
- D. The audit quality reviewer was the same as the monitoring person, which violated Article 46 of SAS No.46 and the firm's

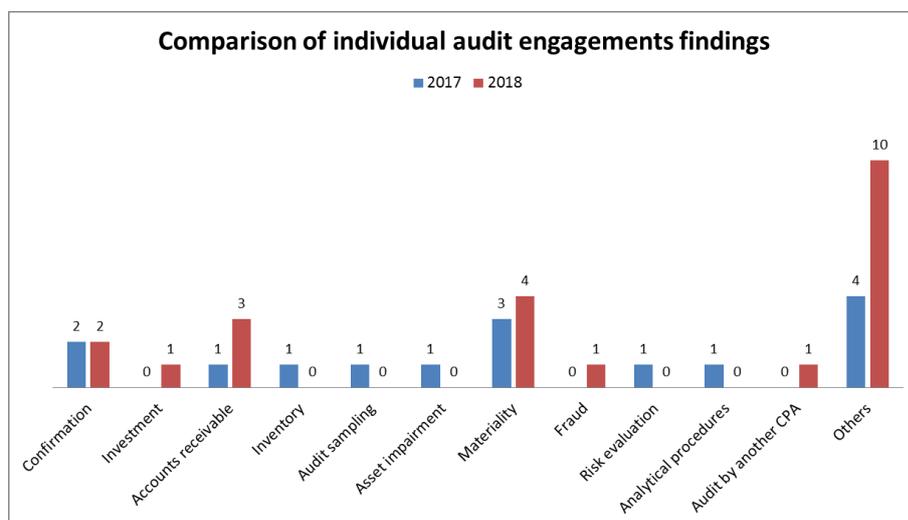
policy.

- E. The items listed on review checklist did not include effectiveness assessment of key elements, as required under Article 46 and 112 of SAS No.46.

**(II) Audit engagement reviews:**

There were 22 findings across 7 engagements reviewed in 2018, an increase of 46% compared to last year (2017). The findings were mainly about Accounts receivable and Materiality. The increase was due to the size difference of the inspected CPA firms. Mid-tier CPA firms were unable to implement internal quality control as effectively as large CPA firms due to lack of resources and employees. Comparing numbers of findings per engagement between 2017 and 2018, the increment reduced to 24%.

	2017	2018	Difference
Number of inspection findings	15	22	46%
Number of reviews of individual audit engagements	6	7	1
Average findings per engagement	2.5	3.1	24%



ings in 2018 review of individual audit engagements were:

**(1) Materiality**

- A. The firm did not document considerations and evaluations of the overall materiality threshold in working papers, which violated Article 13 of SAS No.51.
- B. The firm did not document considerations and evaluations of the “clearly trivial” threshold in working papers, as required under Article 14 of SAS No.52.
- C. During the audit process, the auditors did not re-examine the appropriateness of planning materiality, as well as evaluate the necessity to modify the overall materiality and the materiality of specific transactions, account balances or disclosure items, as required under Article 12 and 24 of SAS No.51.

**(2) Confirmation**

- A. The firm did not perform alternative audit procedures in terms of non-response of external confirmations of accounts receivable, as required under Article 30 and 32 of SAS No.38.
- B. The firm did not document sending processes (e. g., date and means of sending), as well as date, method, summary and tracking of response in the accounts receivable control list, as required under Article 29 of SAS No.38.

**(3) Accounts receivable**

- A. The firm did not understand the reasonableness of inconsistency between target customer and drawee of audited company and document the situation in working papers, as required under Article 20 of Regulations Governing Auditing and Attestation of Financial Statements by CPA.
- B. The firm did not involve inconsistency between target customer and drawee of an audited company in an internal control suggestion proposal.

- C. The firm did not document the reason for not implementing examination of accounts receivables in working papers, as required under Article 22 of Regulations Governing Auditing and Attestation of Financial Statements by CPA.
- (4) **Investment:** The firm did not document observation and examination of securities of the audited company's subsidiary, as required under Article 22 of Regulations Governing Auditing and Attestation of Financial Statements by CPA.
  - (5) **Fraud:** The audit team did not ask governance unit, internal auditors and other staff about potential fraud events and situations, as well as documenting the grounds and conclusion of evaluating identified fraud risks.
  - (6) **Audit by another CPA:** The firm did not verify whether the audited companies adopted a consistent accounting policy under similar transactions and circumstances, or adjusted its policy to address the difference, which violated Article 20 of Regulations Governing Auditing and Attestation of Financial Statements by CPA.
- (7) **Others**
    - A. The firm did not verify whether the loan procedures were in line with Regulations Governing Loaning of Funds and Making of Endorsements/Guarantees by Public Companies.
    - B. In the planning stage, the auditors had communicated with the governance unit about the audit areas of high concern, but did not document the reason why the communication items were not listed as key audit matters in working papers, as required under Article 17 of SAS No.58.
    - C. The firm did not confirm whether the private shareholders, land owners of construction projects and relevant companies of audited firm were related parties, as well as documenting the evaluation in working papers.
    - D. The firm did not sign the date on meeting minute as proof that audit projects were reviewed and approved by

engagement partners before executing audit work, which violated Article 29 of SAS No.47.

- E. There was no examination record of property, plant and equipment, which violated Article 20 of Regulations Governing Auditing and Attestation of Financial Statements by CPA.
- F. The firm did not sign the date on audit planning and completion memorandum as proof that audit projects were reviewed and approved by engagement partner before executing audit work, as required under Article 29 of SAS No.47.
- G. Major audit procedures written in working papers were only reviewed and approved by one engagement partner, which violated Article 24 of SAS No.45.

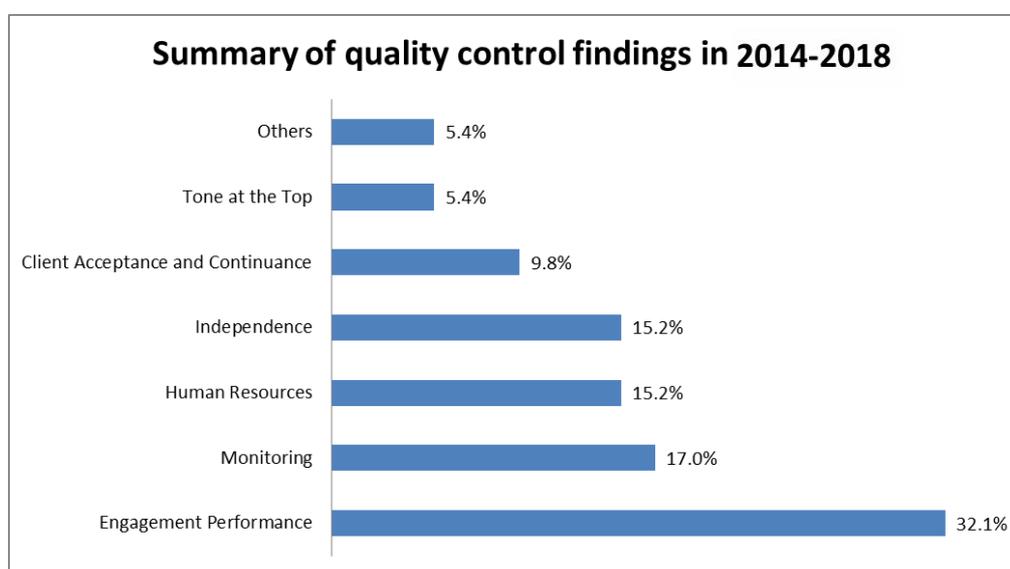
### **(III) Analysis of review findings in 2014-2018**

The FSC commenced CPA firm inspection activities in 2009. In 2011, the FSC entered into a Cooperative Arrangement with the Public Company Accounting Oversight Board (PCAOB) of the United States and has conducted joint inspection on local firms since then. The FSC has successfully performed the cycle of inspections on all big-four CPA firms three times and 22 medium/small CPA firms up to 2018. To assure audit firms' capability in auditing IFRSs financial reports, the FSC undertook the IFRSs thematic inspection of 54 medium/small CPA firms during 2011 and 2012. The analysis of inspection findings 2014-2018 was as below:

#### **1. Quality control systems**

Major findings from inspection of quality control systems in the five years 2014-2018 were related to Engagement performance, Monitoring, Human Resources and Independence. Please refer to previous inspection reports for details.

Items	Findings	Percentage
Engagement Performance	36	32.1%
Monitoring	19	17%
Human Resources	17	15.2%
Independence	17	15.2%
Client Acceptance and Continuance	11	9.8%
Tone at the Top	6	5.4%
Others	6	5.4%
Total	112	100%

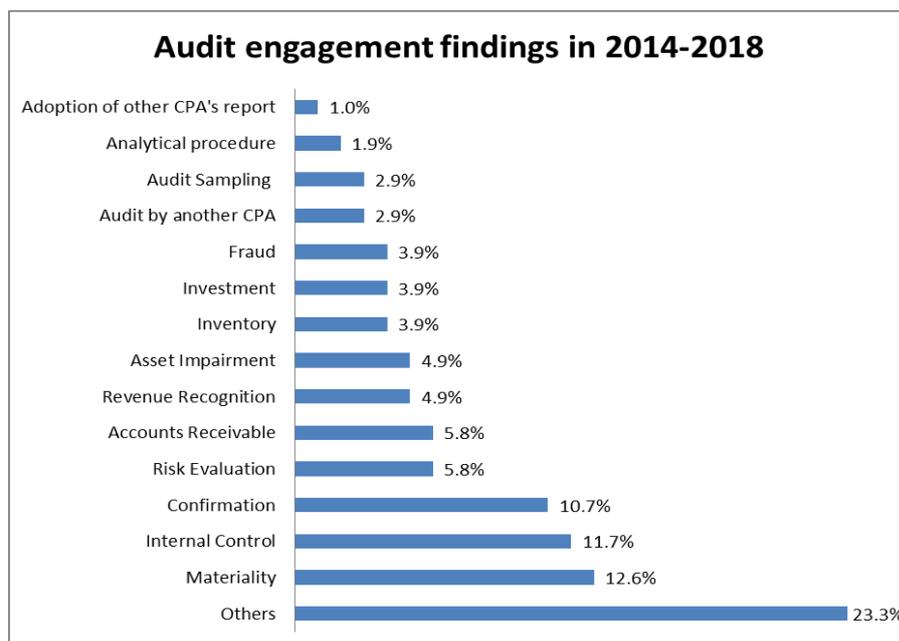


## 2. Audit engagements reviews

Major findings from audit engagement reviews were Materiality, Internal Control and Confirmations in the 5 years 2014-2018. Please refer to previous inspection reports for details.

Items	Findings	Percentage
Materiality	13	12.6%
Internal Control	12	11.7%
Confirmation	11	10.7%
Risk Evaluation	6	5.8%
Accounts Receivable	6	5.8%
Revenue Recognition	5	4.9%
Asset Impairment	5	4.9%
Inventory	4	3.9%
Investment	4	3.9%
Fraud	4	3.9%
Audit by another CPA	3	2.9%
Audit Sampling	3	2.9%
Analytical procedure	2	1.9%
Adoption of other CPA's report	1	1.0%
*Others	24	23.3%
<b>Total</b>	<b>103</b>	<b>100.0%</b>

\*Other findings include incomplete documentation of written working papers, lack of signature of audit staff (or reviewers) and date on working papers etc.



## **V. Conclusion**

Attestation service on financial reporting provided by CPAs reduces information asymmetry between public companies and outsiders, and is thus one of the most important external supervision mechanisms as well as the foundation of the well-functioned capital markets. Audit quality is highly relevant to the credibility of financial reports and social welfare, as a result, the FSC will continue to strengthen the supervision of CPA firms and assist them to improve audit quality. The yearly inspection of CPA firms is one of those important measures.

This inspection report summarizes the major findings from the FSC's inspection work in 2018. CPA firms should respond to findings, improve audit quality actively and establish internal control systems. The FSC suggests that CPA firms consult the practices adopted by foreign peers, including Root Cause Analysis (RCA), and set up a robust RCA Framework, which may help identify the causes of poor audit quality, trace current improvement circumstances and review the effectiveness of remedial measures to ensure high quality audits.

Finally, the FSC acknowledges that the maintenance and enhancement of audit quality is not only the responsibility of CPAs but management and audit committees. Management and audit committees should enhance their communication with CPAs and include findings mentioned in the inspection report as communication items in order to ensure audit work is conducted properly, improve audit quality and protect investors' interests.

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The Financial Supervisory Commission (FSC, Taiwan) was established on 1 July 2004 as the competent authority responsible for development, supervision, regulation, and examination of financial markets and financial service enterprises in Taiwan. The FSC seeks to ensure safe and sound financial institutions, maintain financial stability, and promote the development of our financial markets. Since its establishment, the main goals of the FSC have been to create a sound, fair, efficient, and internationalized environment for the financial industry, strengthen safeguards for consumers and investors and help the financial industry achieve sustainable development.