



THE PRACTITIONER'S VIEW

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MAKING THE NEW QC GRADE

The new quality control standards – is your practice prepared?

The following article was adapted from an article written by Al Budlong, FCA, Director of Professional Services for the Institute of Chartered Accountants of Alberta.

If you are practicing as a sole practitioner or in a small-to-medium sized firm and are not registered with the Canadian Public Accountability Board (CPAB), you need to mark December 1, 2005, prominently on your calendar. That's the deadline for two new quality control standards to be in place within your practice.

The first of these standards – General Standards of Quality Control for Firms Performing Assurance Engagements, CICA Handbook, Section GSF-QC - is the **firm standard** and addresses the public accounting firm's responsibility for establishing a system of quality control. The second – Quality Control Procedures for Assurance Engagements, CICA Handbook, Section 5030 – is the **engagement standard** and addresses the practitioner's responsibilities in the performance of an individual assurance engagement. The main emphasis of the new quality control standards is that documentation must be in place to clearly show adherence to the CICA Handbook provisions – documentation that must include completion of a Quality Control Manual (QCM) by December 1. The new quality control standards complement the rules of professional conduct related to independence recently implemented in Canada and internationally, without imposing additional requirements beyond those of the rules of professional conduct.

Sound complicated? To make it a lot easier, the CICA has published a sample Quality Assurance Manual (QAM) and ICANS is offering a one-day seminar to educate and assist firms in producing their individual QCM. The CICA manual is a comprehensive, practical tool intended to help a firm develop and implement a functioning quality control system. Such a system would ensure the firm and its personnel comply with professional standards as well as regulatory and legal requirements, while also ensuring reports issued by the firm are appropriate in the circumstances. Ongoing updates of the manual will keep firms current with new requirements, best practices, and cost-effective strategies for managing quality control policies and procedures.

The ICANS workshop is intended to guide practitioners through the process to comply with the aforementioned CICA Handbook sections. Utilizing the QAM throughout, the workshop is designed to be interactive and encourage participants to think about why quality control measures are needed in their firm and how they might be implemented. Participants are encouraged to work on developing their firm's QC manual during the day. **Since it is not an option, but a required feature of continuing as a public accounting firm to have a QC system in place and functional**, the workshop is an invaluable tool for firms to utilize in the coming months. Several workshops have been scheduled during the fall to make it possible for firms to get the information they need as conveniently and efficiently as possible.

Behind the effort is a clear commitment to the public to enhance the quality of assurance engagements. It's no secret that post-Enron, et al, confidence in auditors was shaken and questions raised about audit quality and reliance. That led, over the last two years, to the profession implementing key initiatives to improve audit quality, including the new independence rules and the establishment of the Canadian Public Accountability Board (CPAB). In August 2004, the Auditing and Assurance Standards Board (AASB) took additional action by issuing the two new quality control standards. As articulated by Moira Burke, FCA, Chair, AASB, "In doing so, the public accounting profession will be able to demonstrate that it is firmly committed to a uniformly high

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quality of work and that it has the processes in place to ensure that the public expectations of the profession are met.”

Why two separate standards? Essentially, because quality control needs to be dealt with at two levels – the firm level and the engagement level. The publication of a standard directed at a firms’ responsibility is a first for the AASB and it requires that a firm performing assurance engagements establish an effective system of quality control. The firm standard, which forms part of generally accepted standards of practice for the profession, has been published in the CICA Handbook but outside assurance standards.

Canada is not alone in focusing on quality control. Last year, the International Auditing and Assurance Standards Board (IAASB) published new international quality control standards with which the Canadian standards have been harmonized. The upshot is that Canada will be consistent in its QC standards with those of other countries, and particularly with those of the US.

When all is said and done, the intent of the two new quality control standards is to respond to demands from the public and regulators for high-quality audits and other assurance engagements. Without a doubt, in the aftermath of the extreme business failures of recent years, stakeholders expect the public accounting profession in Canada to clearly demonstrate that quality is a core element of assurance engagements. Taking a leadership role in implementing far-reaching quality control standards is a vigorous response to that expectation.

Make your calendar today....December 1 is just around the corner. Make sure you’re adequately prepared.

The Manual	The Workshop
<p>The CICA sample Quality Assurance Manual provides assistance to practitioners in developing and documenting the required QC policies and procedures for their firms by providing:</p> <ul style="list-style-type: none"> • Sample quality control policy manuals for <ul style="list-style-type: none"> • Sole practitioners WITH NO STAFF • Sole practitioners WITH STAFF • Small to medium-sized practice • Small to medium-sized practice with public company audits • MS Word templates of the sample policy manuals for developing a firm’s own quality control manual • Commentary and guidance on quality control objectives, risks and strategies, independence and ethics, and the roles and responsibilities of firm leaders • Sample Engagement Letters for an external monitor and file reviewer, as well as other sample letters, forms and worksheets • Practice Aids and Other Reference Materials 	<p>The ICANS Quality Assurance Workshop includes sessions on:</p> <ul style="list-style-type: none"> • Background, need and benefits of the new QC standards • Overview of the new QAM • Opportunity to discuss solutions to implementation issues among peers • Practical approaches for conducting file quality reviews and practice monitoring • How practice inspectors will address QC procedures • Forms and checklists to implement the policies and procedures <p>At the end of the workshop, practitioners should be able to:</p> <ul style="list-style-type: none"> • Understand the practice risks addressed in the new QC standards • Identify the key QC policies needed in your firm • Develop a firm’s QCM, using the samples contained in the QAM

Workshop registration details were sent to all practising offices recently and are also included in the ICANS PD brochure, to be issued in mid-August.

Prerequisite

Participants are required to purchase, review and bring their copy of the QAM to the course which will be used in the case studies and for developing their own quality control.

Be prepared to invest the time, money and effort prior to the seminar to obtain maximum value.

To order, go to www.knotia.ca/store/QAM02 or call the CICA order department at 1-800-268-3793.

The cost of the manual is \$175 (plus HST and shipping & handling), which includes a subscription to the first year’s update. **Bonus:** Ordering the QAM also entitles members to a 50% discount on new subscriptions to PEM.

If you have any questions regarding the QAM or workshops, please contact Wenda Bennett at wbennett@icans.ns.ca or (902) 425-3291.

PRACTICE MATTERS

The following articles appeared in the May 2005 issue of News 'N Views, a publication of the Institute of Chartered Accountants of British Columbia and is reprinted with the permission of ICABC.

TAKING CARE OF BUSINESS

New Clients

As you grow your practice and interview potential new clients, be sure to find out how they heard about your firm. Are they just shopping for lower fees, saw your name in an advertisement or the yellow pages, or were they referred to you by a friend or client? If it is a referral, contact the reference to check out the background of your potential new client, the nature of their business, and their reputation for business ethics. If not, perhaps a call to the local Better Business Bureau may give an indication as to the client's business practices. Another suggestion is to ask to see recent correspondence from the previous accountant to get a better sense of the issues that are important to the client. Experienced practitioners know that it's never a good idea to accept just any client who walks through the door and that a little checking up front could save a great deal of headache later.

Liability Insurance

An item related to growth is professional liability insurance. As your clientele grows and changes, so does your risk for liability. Accordingly, prudent practitioners no longer carry just the minimum professional liability insurance required by the Institute's bylaws. At the time they renew their policies, practitioners review their client lists to look at the risks associated with the engagements to consider ways to minimize those risks and adjust their coverage to match the potentials for claims.

Communication with predecessor

Rules of professional conduct require members to contact the predecessor accountant prior to accepting an engagement. If you do not receive a response after a reasonable period of time (up to 30 days), consider giving the predecessor a phone call to follow up. The delay could be because there is reason why you should not accept the engagement but they just don't know how to put it in writing. It's a good idea to find out why the previous professional relationship ended and how it may affect you.

Engagement letter

Practitioners know the importance of getting a detailed engagement letter signed before starting work but how many of you take the time to go over the letter with a new client before they sign it? When you do so, and document that in your notes, you eliminate the possibility of the client coming back claiming they didn't know what they were signing or understand the terms and conditions of the engagement.

A condition of the engagement letter that is gaining popularity with members is the one whereby the client agrees not to distribute any statements (draft or final) without the practitioner's permission in writing.

Fire and Burglary

In addition to installing an alarm system, members should consider reviewing their fire and burglary insurance coverage. A fire is unlikely in a high office tower, but if your office is in a mall (storefront or upstairs) or a small office building, the risk of a fire increases and you need to make sure you and your property are protected. Furthermore, business offices are often targets for computer theft. Besides the cost of buying new computers, the loss of confidential files is of an even greater concern. Be sure to backup your computers regularly and keep the backup files at an off-site location.

As an extra precaution, members should consider password protecting any files and data stored on hard drives. Should your computers ever be stolen, you reduce the risk of the thieves accessing confidential client information.

Client Records

Since most practitioners will take possession of client records, however temporarily, it is important to consider the possible loss of client records (and even your own files) due to loss by fire or theft. While most insurance underwriters will issue a rider to recover valuable papers, the best precaution is to complete the work as quickly as possible and return all original records to your client. An investment members may want to consider is to purchase a good quality document scanner and make electronic copies of important client documents, which are then easy to store and don't take up valuable space.

Many thanks to John Hutton, FCA, for sharing his thoughts with the PAS Department on these topics.

RISKS ASSOCIATED WITH A NOTICE TO READER

Most practitioners think that a Notice to Reader should protect them from any lawsuits since it clearly states that the financial statements have not been audited or reviewed. Surprisingly, that is not the case. According to AICA, 10% of all claims between 1999 and 2002 were from non-review engagements. Practitioners often get themselves into trouble by offering additional comments on the financial statements that they have just compiled. In some cases, that has been construed to provide assurance on the information subject to a Notice to Reader. Members should proceed cautiously when communicating with third parties about client financial information.

Members are encouraged to read the article "Notice to Reader, Limited Responsibility with Potentially High Risk" in Appendix A, which is from the January 2005 issue of *CARM*, reprinted here with permission from AICA Services.

REAL STORY OF A CA OFFICE FIRE

The following article, by Kouri Berezan Heinrichs Chartered Accountants, appeared in the August 2004 issue of Public Practice, a publication of the Institute of Chartered Accountants of Alberta and is reprinted with permission.

This article chronicles the events surrounding a CA firm's ordeal with a severe fire in their offices...hear first-hand their story, including how they dealt with the aftermath, as they share lessons learned and provide valuable advice for other firms.

July 21, 2003

"Hello, this is _____, your office is burning!"

"What!!"

"There is a fire in your building and your office is being consumed..."

As I drove to the office, my first thoughts were what will I do about the client records which had just been sorted over two desks in the staff area, not to mention the other client records? Then all we could do was watch for the next four hours. Eventually the fire was out. While watching, we telephoned the staff to advise them of the fire and that we would be in contact with them over the next few days.

July 23, 2003

It was two days later before we were allowed into the building to assess the damage. During those two days we:

- contacted and met with our insurance broker to review coverage and procedures
- arranged for our office telephone number to be transferred to a cell phone and later to a "command centre"
- arranged for the command centre which, in our case, was an unused boardroom at a nearby client's offices
- contacted Canada Post to hold mail
- contacted normal delivery services to deliver to the command centre
- started arranging temporary space

When we were finally allowed into the building we ensured that we entered with the adjuster. This proved valuable in our subsequent discussions with the insurance people.

In the short time we were allowed in the building we:

- removed all of our computers
- assessed the damage and took a number of pictures. In our case, a portion of the office was gutted, and we sustained water damage and heavy smoke and soot damage.
- took some files we thought were required immediately, but brought them back as the smoke smell was so repugnant it precluded working on the files.

Having removed all our computers, our IT people spent the next couple of days assessing the damage, extracting the information from the hard drives and ordering replacement systems—all were lost mainly due to water damage and soot.

July 24, 2003

The next day we were allowed to remove our property. The files and equipment were to be removed to a restoration warehouse for further assessment. Ultimately the files were ionized to dry and remove the smell and wiped to remove the soot. We supervised the removal of the files and materials from the offices and desks. We also further assessed our losses, particularly in regards to assets. **This was one area in which we wished we had had more control, as the insurance company arranged for the restoration service. While we had input with the service, it must be recognized that they were spending insurance dollars. Of all the areas of expenditure, this was the one over which we felt we had the least control.**

July 25, 2003

Over the next ten days we:

- met with the staff to advise them of status and future plans
- met with the landlord to ascertain his plans and expectations
- met with the insurance people to ascertain what we could proceed to do
- continued to seek a temporary office location, which proved to be more difficult than we originally thought
- began to order supplies, particularly stationery and other printed matter

August 13, 2003

On August 13, 2003, we moved into our temporary location. By this time we had replaced all of our computers. In the temporary space we installed wireless technology rather than spend money putting in wiring. We rented all desks, chairs and tables. Our filing system consisted of bankers' boxes. The biggest challenge in the temporary location proved to be obtaining postal service.

Having moved and resumed operating in the temporary location, we began concentrating on the reconstruction of our premises, which really was going to be a complete redesign of our old space as the entire interior of the building had to be gutted and rebuilt.

Through this process, we worked with the office designer, the landlord, and the insurance people. In replacing the furniture we became very confused as to the differences in the nature of the quotations and quality of the furniture. To assist us we hired a furniture consultant. This considerably eased the process and reduced the cost.

December 2003

During Christmas and New Years, we moved into our redesigned, rebuilt space. A month later all the "little" things were cured and we felt we were almost back to normal.

We maintained detailed records of time associated with the fire, getting back into a full operating mode, re-establishing our office (including the new plan design), overseeing the re-construction and ordering the furniture. We did this not so much for an insurance claim, but to ascertain how much time the fire cost us. Approximately 510 partner hours and 1,265 staff hours were spent as a result of the fire.

Our direct cost of the fire was \$406,000, which did not include leasehold improvements as we did not own them. Approximately \$300,000 of the total claim was associated with the replacement of computer hardware, desks, workstations, filing cabinets, and supplies. The balance was related to soft costs, moving files, cleaning files, temporary equipment, etc.

Overall, we were fortunate it was not worse. No one was injured...it was summer, our slower time...our backup procedures worked...we had excellent IT people who really put in the gigantic initial hours getting us back functioning...and we had extremely understanding clients. Would we do it again? Hopefully not.

However, there can be disasters other than a fire, such as a flood, theft, viruses, or worms. Do you know what you would do? We now do, because we're compiling a documented plan to follow in the event of a disaster - not a whole lot different than preparing a will.

Important Lessons

What other things did we learn from this experience?

- Insurance is a unique industry. While we had more than adequate coverage, we learned that coverage is divided into various pools—equipment, valuable papers, etc. Shortfalls in one area cannot be transferred to another area. One really needs to understand the nature of their insurance coverage and, in particular, co-insurance assessments which have nothing to do with the company with whom the insurance coverage is placed.
- Ensure that you have a plan with respect to your computer information to retrieve data in the event the equipment is damaged or lost—a back-up plan. Test the plan periodically to ensure it works.
- Keep client records to a minimum and consider a "safe place" for client records.
- Have a current staff list in a number of accessible places.
- Set-up a separate time code for time spent on the fire. We obviously maintained an impeccable file of actual expenses. This again proved invaluable in negotiating with the insurance people.

What would we do differently, and what changes have we made as a result of the fire?

- In retrospect we wish we had met with the staff a little sooner to advise them of what had occurred and our future plans. This would have quelled some of the false rumors. For the first few days we did not feel we

had any information to provide them. We now realize that any information was better than none, and we could have tried to answer some questions.

- We did not own our leasehold improvements. This reduced the amount of coverage we required, but proved to be a stumbling block for the insurance people as, if we were required to replace any of our leaseholds, our coverage was inadequate. Three legal opinions later the insurance company finally believed us.
- We're making a conscientious effort to reduce the amount of junk we collect. Old Income Tax Acts and much more than that, quite frankly, we didn't even realize we had.
- Personal mementos were lost. There was an additional discussion as to under whose policy they should be covered.
- As all insurance agents recommend, maintain an asset list and pictures of your office as a record of what you own. Ironically, we were in the process of doing this, but the list was lost in the fire.
- We are doing more to keep files current and go paperless. Our computer backup procedures were flawless—we lost nothing on computers or our server, except the one computer in the gutted office. While our paper loss was actually also minimal, we were lucky and are making more of an effort to ensure "paper" items are on the computer system.

CICA NEWS

Have you seen the latest newsletters?

FYI (June 2005)

This issue of the Accounting Standards Board (AcSB) newsletter summarizes the significant points from feedback received to date on the AcSB's draft strategic plan for the future of accounting standards in Canada. It also discusses the reason for recently archiving the CICA Handbooks and includes an accounting standards project schedule.

AASB Update (July 2005)

This edition of Auditing and Assurance Update summarizes significant matters considered by the Auditing and Assurance Standards Board (AASB) from January to March 2005, including audit risk, management representations, terms of engagement, audit evidence considerations when an entity uses a service organization and auditor's report on controls as a service organization – **new and significantly revised sections of the CICA Handbook**. It also addresses small practice issues, such as proposed revisions to the wording of the Notice to Reader communication.

To access all CICA newsletters, go to www.cica.ca and click on "News".

THE RIGHTS OF DIRECTORS AND SHAREHOLDERS

The following article appeared in the March 2003 issue of Horizons, a publication of the Institute of Chartered Accountants of Saskatchewan and is reprinted with permission.

What are the rights of directors and shareholders of a corporation to view and access the financial records prepared by a Chartered Accountant on behalf of the corporation?

This is a legal question. When the Professional Conduct Committee sought advice on this matter, it was advised as follows. It is established by The Business Corporations Act that a director acting in good faith is entitled to access financial records of the corporation from the CA without delay. The rights of the shareholder of a corporation to access financial records are considerably more restricted. Generally, a shareholder has no right to direct access to the financial records of a corporation.

The Institute's Professional Conduct Committee has recently reviewed complaints relating to this question. If you find yourself in a situation where you are being asked to provide financial records or financial statements to a director or shareholder of a corporation, please obtain legal advice from your lawyer before acting on the request.

PROFESSIONAL LIABILITY INSURANCE

And finally...don't forget to send in your annual declaration of insurance coverage. If you've misplaced the form sent to you in June, please contact Wenda Bennett.

SUGGESTIONS FOR THE NEXT ISSUE?

Contact **Wenda Bennett, CA** at the Institute wbennett@icans.ns.ca or (902) 425-3291.

**NOTICE TO READER
LIMITED RESPONSIBILITY WITH POTENTIALLY HIGH RISK**

Between 1999 and 2002, almost 10% of all claims were from non review engagements, with the majority of these claims arising from lenders who relied on financial statements with a Notice to Reader.

Surprising?

Notice to Reader financial statements are compiled from information supplied by management. The Notice to Reader explicitly states that the Chartered Accountant "has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of such information" and further cautions readers that the statements may not be appropriate for their purposes.

Whether it appears on each page or each page is conspicuously marked "Unaudited — see Notice to Reader", the Notice clearly informs readers of the nature of the work. But can you assume that investors and lenders are sophisticated users who understand the accountant's limited involvement in the preparation of the statements? If the statements are subsequently used to procure financing, these users *should* know that they were not prepared with them in mind. Indeed, these users should demand an audit or review for their purposes.

So Why Do These Claims Arise?

One would think the accountant is protected with the Notice to Reader disclaimer. Not necessarily.

A typical situation is one where a banker calls the accountant to discuss the information on the statements and he or she engages in a discussion. When the claim later ensues, the bank takes the position that since the accountant knew the banker should not be relying on the statements for a lending decision, the accountant should not have been willing to discuss them. In a sense, the banker views the conversation as a waiver on the notice. In these situations, the accountant may be found to have failed to warn the bank that it is using the statements for a purpose for which they were not prepared.

The observations of practice inspectors validate another trend that is giving rise to claims: practitioners are doing extra work in compilation engagements, thinking this might afford additional protection. However, be aware that the courts will consider *what you ought to have done* and *what you actually did*. If you did extra work beyond the scope of the engagement and failed to detect a problem, you cannot hide behind the Notice to Reader claiming that your further procedures were not warranted.

Notice to Reader: Loss Prevention

- If a bank or other user contacts you, do not engage in a discussion about the financial statements.
- Clearly warn the caller that the statements were not prepared for that purpose.

- Communicate the limitations of the Notice to Reader financial statements.
- If you are aware that the client plans to use the financial statements for financing purposes, encourage the client to have a review performed. Put this advice in writing. Clients appreciate that the compilation engagement is a low cost service; however, the work must be appropriate for the purposes. If the service is not appropriate for the intended use, do not provide it.
- As the new independence rules require that you assess independence *de facto*, this fact must be disclosed in the Notice to Reader communication where independence is impaired. Make sure you and your staff clearly understand the requirements of these new rules. Document the independence assessment for the engagement.

Litigation is an adversarial process. Even if the claim is eventually found in your favour, the time demands and stress of the claims process are enormous. Protect yourself. Take preventative steps.

For loss prevention tips and guidance on other areas of risk exposure, refer to the AICA Services' *Loss Control Manual* available at

<http://www.aica.ca/pdf/Loss%20Control%20Manual.pdf>

and the archived CARM newsletter issues at www.aica.ca/carm_newsletters.aspx.

YOUR PROFESSIONAL LIABILITY INSURANCE COMMITTEE

To contact your PLIC representative, mail, fax or e-mail c/o AICA Services Inc.

Chairman	David Atkins, FCA <i>Toronto, ON</i>	
Committee Members	Robin Elliott, FCA <i>Vancouver, BC</i>	Mark Gray, LLB, CA <i>Winnipeg, MB</i>
Nil Allaire, FCA <i>Sherbrooke, QC</i>	Phillip Gaunce, CA <i>Halifax, NS</i>	Douglas Mundell, CA <i>Lethbridge, AB</i>

For further information:

AICA Services Inc.
277 Wellington Street West
Toronto, Ontario
M5V3H2

Toll free numbers:
English: 1-800-267-4734
French: 1-800-268-2630

Fax: (416) 204-3418
email: services@aica.ca