

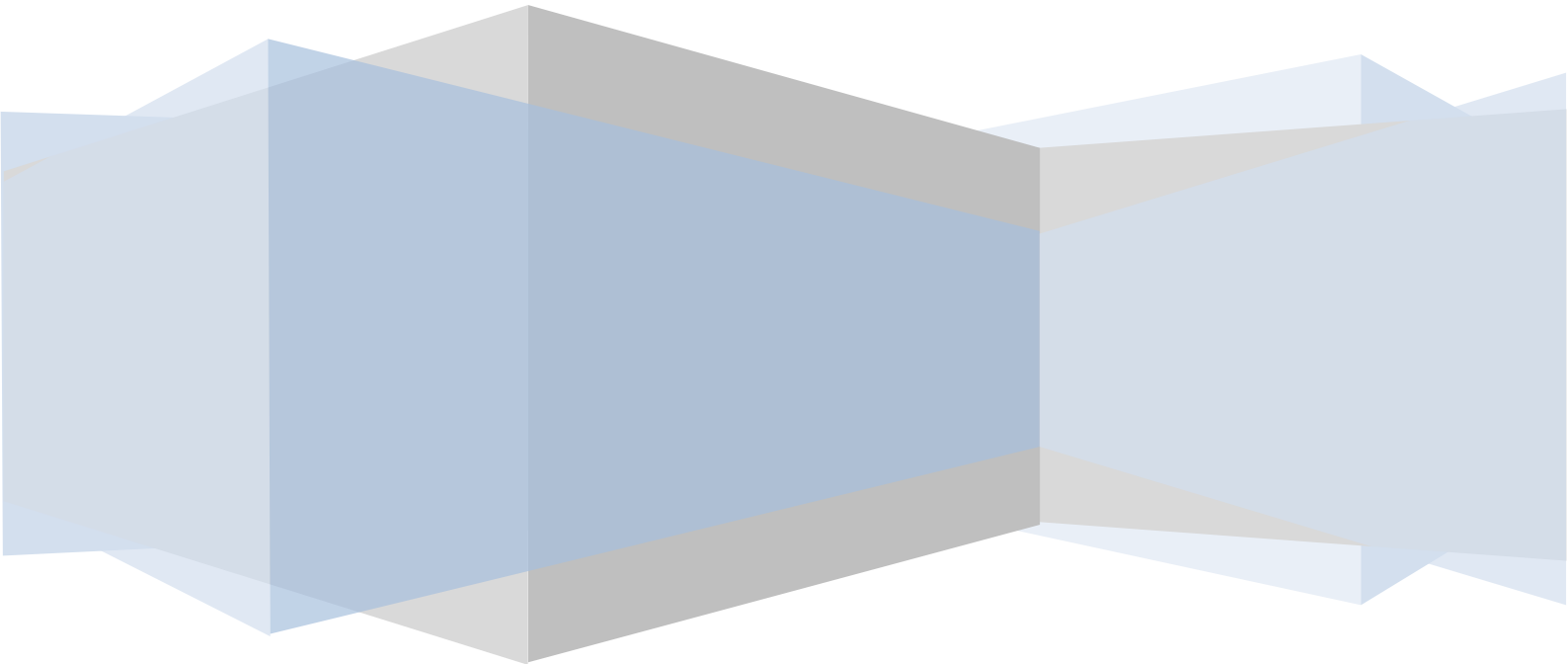


Capital Markets Board of Turkey

Audit Quality Assurance Annual Report 2013

February 2014

Department of Accounting Standards



Prepared By

CAPITAL MARKETS BOARD OF TURKEY

DEPARTMENT OF ACCOUNTING STANDARDS

This report is prepared only to inform public, so it cannot be published in any place including web sites or it cannot be copied in any form. It can only be quoted by showing resource.

Capital Markets Board of Turkey shall not accept any responsibility for losses resulted from using the information included in the Report.

Capital Markets Board of Turkey;

The Capital Markets Board of Turkey (the CMB/the Board) has been established for carrying out the tasks and exercising the authorities granted with the Capital Market Law (CML) and the related legislation, to maintain secure, transparent, efficient, fair, and competitive capital markets, and to protect rights and interests of investors. The CMB is a statutory public legal entity with administrative and financial autonomy, and exercises its authorities independently under its own responsibility.

The CMB is related with the Minister assigned by the Prime Minister.

The mission of the CMB is to regulate and supervise the capital markets for the secure, fair, transparent and efficient functioning of the capital markets within the framework of objectivity and accountability, conducting supervision and making clear and comprehensible approach that is in conformity with international norms and developments which meets varying market needs. The vision of the CMB is to be a leading dynamic and respected institution in national and international arena.

Regarding independent audit activities and audit firms in capital markets, the Board; has responsibility and authority to

- 1. specify the corporations and institutions subjected to the CML, whose financial reports are prepared according to Turkish Accounting Standards and the regulations of the CMB, which should be audited,*
- 2. regulate additional conditions for audit firms, to conduct audit in capital markets, which are authorized by Public Oversight Accounting and Auditing Standards Authority of Turkey and authorize these firms,*
- 3. engage in quality assurance reviews to the audit firms which are authorized to perform do auditing in capital markets,*
- 4. cooperate with other institutions.*

The Board conduct those responsibilities and authorities by the Department of Accounting.

TABLE OF CONTENTS

1. Introduction	5
2. Main Findings	7
2.1. Findings Regarding Full Quality Assurance Reviews	7
2.1.1. Establishment Requirements	7
2.1.2. Overall Audit Plan and Programme	7
2.1.3. Documentation of the Audit	7
2.1.4. Obtaining Appropriate and Sufficient Audit Evidence	8
2.1.5. Risk Assessments and Audit Materiality Level	9
2.1.6. Performing works to understand the industry, economic and legal environment of the company	9
2.1.7. Evaluation of the Internal Control System	9
2.1.8 Not utilizing auditor’s expert.....	9
2.1.9. Accounting Estimates	10
2.1.10. Checking the correctness of fair value calculations	10
2.1.11. Related Party Transactions.....	10
2.1.12. Audit Letter.....	11
2.1.13. Professional Training	11
2.1.14. Ethical Principles.....	11
2.1.15. Notification Obligation to the Board.....	11
2.1.16. The Other Issues.....	11
2.2. Thematic Quality Assurance Review	12
2.2.1. Establishment Requirements	12
2.2.2. Quality assurance systems	12
2.2.3. Overall audit plan and programme	12
2.2.4. The other issues	13
3. Overall Assessment and Result	13

1. Introduction

Auditing in capital markets are carried out by audit firms, authorized by Public Oversight Accounting and Auditing Standards Board of Turkey, which ensure additional conditions requested by the Board.

The CMB is authorized by the 62th and 128th articles of the CML and Communiqué Regarding Independent Audit Standards in Capital Markets, to conduct quality assurance reviews on independent audit firms, which are authorized to conduct audit in capital markets, according to the auditing standards and to the said regulations.

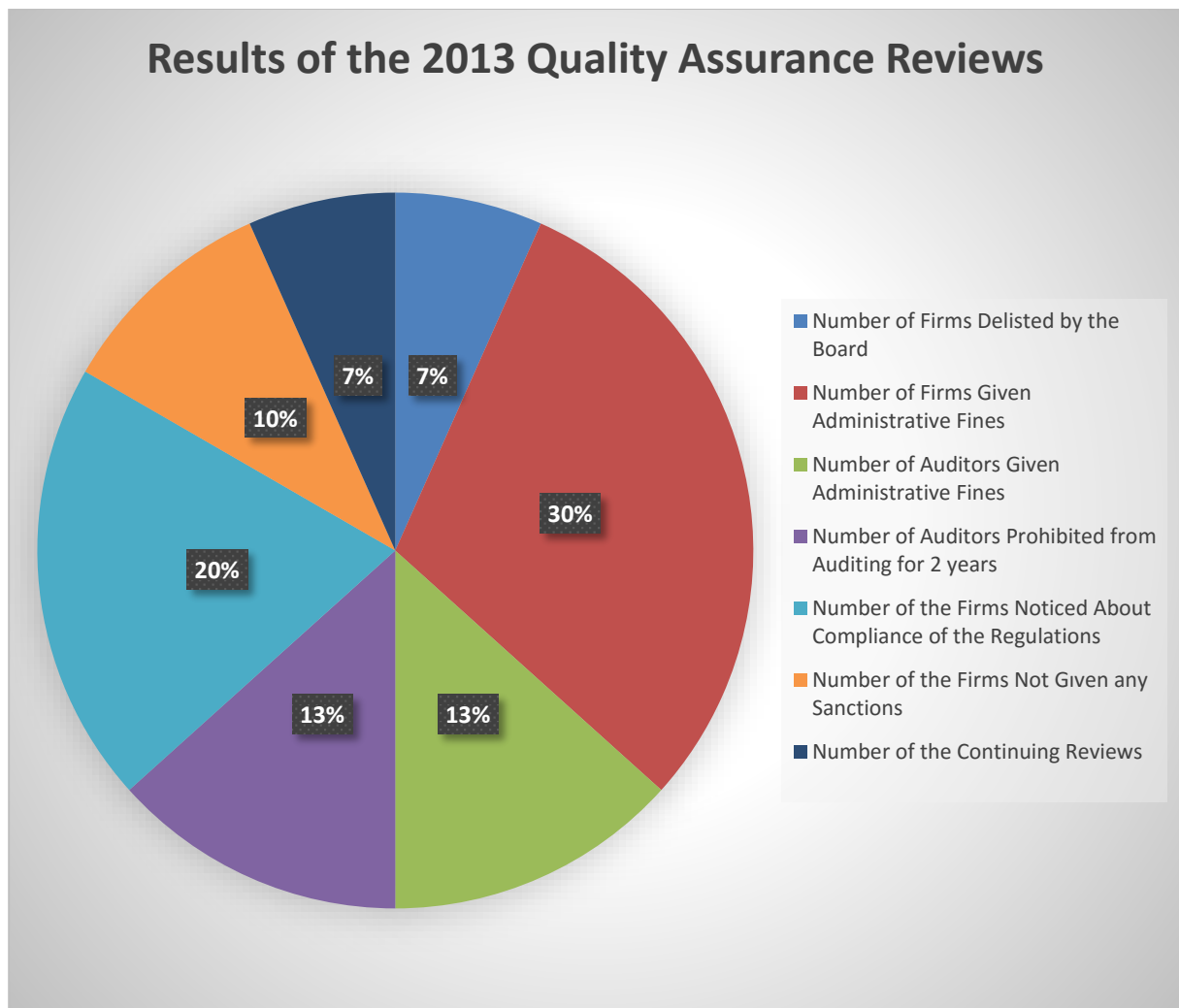
In addition, the project called the Remote Data Transfer System (UVAP), which was created to improve the efficiency of oversight of auditing activities, are used by audit firms to submit a variety of information that enables the CMB to monitor firms on timely basis. Thus, UVAP system also enables CMB to generate reports electronically.

A total of 22 quality assurance reviews are conducted on independent audit firms in 2013, by the CMB. 13 of these reviews were full and 9 of them were thematic¹. Also, there are two reviews proceeding. During the inspections the CMB reviewed 52 audit files. These reviews are implemented according to risk profiles of the audit firms, results of surveillance activities of the CMB and notifications about the firms.

The statistics related to quality assurance reviews implemented by the Board in this period is shown in the following table:

¹ Thematic quality assurance reviews; are the reviews whose content is limited by establishment requirements, overall plan and programme and quality assurance systems of the audit firms.

Table: Results of the 2013 Quality Assurance Reviews							
Number of Firms Delisted by the Board	Number of Firms Given Administrative Fines	Number of Auditors Given Administrative Fines	Number of Auditors Prohibited from Auditing for Two Years	Number of the Firms Noticed About Compliance of the Regulations	Number of the Firms Not Given any Sanctions	Number of the Continuing Reviews	The Number of the Total Quality Assurance Reviews
2	9	4	4	6	3	2	22



2. Main Findings

Overall results of the quality assurance reviews conducted by the Board in 2013 are summarized below:

2.1. Findings Regarding Full Quality Assurance Reviews

Overall results of the full quality assurance reviews conducted by the Board in 2013 are summarized below:

2.1.1. Establishment Requirements

It has been determined that 1 audit firm didn't provide the establishment requirements prescribed by the 3th article of the Second Section of "Communique About Auditing Standards in the Capital Markets" by not employing enough number of or sufficient and well-qualified auditors.

2.1.2. Overall Audit Plan and Programme

Within the audit firms reviewed, 6 of them were have deficiencies in their overall plan and programme. Main contradictions and deficiencies related to overall audit plan and programme are consolidated below:

- Not updating the existing audit plan and programmes,
- Not giving detailed information about the strategy which will be used in an audit plan,
- Not having audit programmes that contains all auditing standards,
- Not utilizing the audit plan and programmes during an audit,
- Not stating the specific circumstances of the client company in the audit programme,
- Insufficiency in the content of the audit plans.

2.1.3. Documentation of the Audit

Within the audit firms reviewed, 10 of them were have deficiencies in the documentation of the audits. Main contradictions and deficiencies related to documentation of the audit are consolidated below:

- Lack of enough information regarding; the content and time of the performed, auditing procedures, by whom these work and checks were performed and results of these procedures,
- Lack of evidence of audit in the working documents regarding that any account items of the financial statements was checked,
- Lack of documentation of works made by auditor to understand the accounting and internal control systems of the company,
- Lack of documentation of statements regarding auditing techniques used by the auditor,
- Lack of documentation of strategy of an audit,
- Lack of documentation relating to the structure of the audit techniques, content and timing in audit plan going to be used in audit work,
- Lack of documentation of the evaluations and works made in contemplation of professional skepticism related to fraudulent and unlawfulness actions determined during an audit,
- Lack of taken confirmation letter from the company administration concerning interception of fraudulent and unlawfulness actions in arranging financial statements,
- Lack of documentation of work related to quality control of audit,
- Lack of documentation of works made by partners concerning the acceptance of client, attendance of the relations with client and procedures which must be implemented in specific audits.
- Lack of documentation of analytical techniques which need to be performed during an audit,
- Lack of documentations of works regarding the going concern principle,
- Lack of content and quality of the working papers,
- Not combining working papers as an audit file in 60 days.

2.1.4. Obtaining Appropriate and Sufficient Audit Evidence

Within the audit firms reviewed, 8 of them were have deficiencies in obtaining sufficient, confidential and appropriate audit evidence that provides reasonable assurance. Main contradictions and deficiencies in obtaining appropriate and sufficient audit evidence are consolidated below:

- Auditor's absence at the cash count,
- Auditor's absence at the physical inventory count or not evaluating sufficiently the physical inventory,
- Not collecting sufficient and appropriate evidence related to the sales,
- Relying on documents obtaining from the company itself without taking sufficient confirmations about trade receivables and trade payables,
- Not checking the correctness of the rediscount calculations,
- Taking insufficient confirmation from the banks,
- Insufficient information and documentation for doubtful receivables,
- Not fulfilling the analytical procedures in evaluating the financial information,
- Not collecting sufficient evidence for the measurement of the fair value of tangible and intangible assets,

- Not checking the physical existence of tangible fixed assets,
- Not checking the correctness of the deferred tax calculations,
- Not arranging working papers for the consolidation of financial statements,
- Not obtaining the sufficient evidence in detecting fraudulent and unlawfulness actions during an audit.

2.1.5. Risk Assessments and Audit Materiality Level

Within the audit firms reviewed, in 8 of them, any practice could not be detected about defining the audit materiality level which determine the content and timing of the audit procedures that need to be applied during audit work and evaluating the risk of significant error relevant to the information, documentation and declaration presented by the company.

2.1.6. Performing works to understand the industry, economic and legal environment of the company

Within the audit firms reviewed, 6 of them were have deficiencies in conducting audit works to understand the industry, economic and legal environment of the company. Main contradictions and deficiencies in conducting works to understand the industry, economic and legal environment of the company are consolidated below:

- Evaluation related to the industry, economic and legal environment which the company operates,
- Analytical tests for understanding the industry risk of the company.

2.1.7. Evaluation of the Internal Control System

Within the audit firms reviewed, in 6 of them, any practice could not be detected in documentation of their audit works to evaluate the accounting and internal control system of the company audited.

2.1.8 Not utilizing auditor's expert

Within the audit firms reviewed, 4 of them didn't perform a work to understand expert's objectivity and competence, and/or didn't perform a work to evaluate the results of the expert's study, in using expert studies as an audit evidence.

2.1.9. Accounting Estimates

Within the audit firms reviewed, 6 of them were have deficiencies in defining accounting estimates in the audit works. Main contradictions and deficiencies in defining accounting estimates are consolidated below:

- Not sufficiently evaluating accounting estimates and assumptions related to the useful life of tangible assets and impairment loss of them,
- Not sufficiently evaluating accounting estimates and assumptions of deferred tax assets,
- Not giving sufficient explanation about audit techniques and methodology of estimation related to provision for severance pay,
- Not giving sufficient explanation about audit techniques and methodology of rediscount calculations,
- Not calculating rediscount rate according to the IFRS; on the contrary calculating it according to the tax regulations.

2.1.10. Checking the correctness of fair value calculations

Within the audit firms reviewed, in audit works which are performed by 6 of them, various errors were detected related to fair value estimations of the financial statements which need to be arranged in accordance with IFRS. By reason of detection of these errors, it was understood that the accuracy of the fair value estimations were not checked.

2.1.11. Related Party Transactions

Within the audit firms reviewed, 1 of them were have deficiencies and contradictions in related party transactions of the audits. Main contradictions and deficiencies in related party transactions are consolidated below:

- Not performing the required audit techniques to expose the extraordinary transactions or transactions with extraordinary prices,
- Not working sufficiently on trade receivables and debts from related parties.
- Not controlling the working papers of the previous accounting period,
- Not stating the expenses which are accounted as bad debts in accounting period in financial statements,
- Not obtaining sufficient audit evidence about related party transactions and taking into account the documents given from the company administration.

2.1.12. Audit Letter

Within the audit firms reviewed, 4 of them were have contradictions and deficiencies in arranging audit letters. Main contradictions and deficiencies in arranging audit letters are consolidated below:

- Arranging affirmative audit letter despite the fact that there were any restricting factors and/or requiring conditional factors during audit work,
- Arranging affirmative audit letter despite the fact that financial statements and their footnotes were contrary to the regulations of the Board related to the financial reporting standards.

2.1.13. Professional Training

Within the audit firms reviewed, in 2 of them, it was detected that professional training for auditors to enable improving themselves and gaining professional competence for auditing was not efficient together with lack of on-the-job training.

2.1.14. Ethical Principles

Within the audit firms reviewed, 5 of them were have deficiencies in violation of independence, prohibition of trade and activities that are not suitable for the occupation, and professional competence and diligence principles. Main contradictions and deficiencies in violation of independence, prohibition of trade and activities that are not suitable for the occupation and professional competence and diligence principles are consolidated below:

- During an audit procedure, not working sufficiently about implementing duties on supervision and coordination which should be performed by partners,
- Being a director in a commercial company,
- Providing consultancy service and training about accounting,
- The risk of determining audit fee according to the other services given by audit firm.

2.1.15. Notification Obligation to the Board

Within the audit firms reviewed, 2 of them did not send or sent with a delay any document and information, as a hard or soft copy, which have to be sent in accordance with the Board's regulation about notification liabilities of the audit firms.

2.1.16. The Other Issues

Within the audit firms reviewed, 7 of them have contradictions and deficiencies in other issues. Main contradictions and deficiencies in other issues are consolidated below:

- During an audit, not taking into account other regulations which the companies are subjected to,
- Not sufficiently evaluating the operations of the companies' internal inspection department,
- Inadequate analyze of the going concern principle,
- Inexistence of the minimum terms which are determined by CMB's regulations for audit engagements,
- Providing valuation services to the companies contrary to the Board's regulations.

2.2. Thematic Quality Assurance Review

Overall results of the thematic quality assurance reviews conducted by the Board in 2013 are summarized below:

2.2.1. Establishment Requirements

Within the audit firms reviewed, 3 of them were have deficiencies in providing establishment requirements prescribed by the 3th article of the Second Section of "Communique About Auditing Standards in the Capital Markets". Main contradictions and deficiencies related to establishment requirements are consolidated below:

- Not employing sufficient and well-qualified auditors,
- Not having quality assurance committee,
- Not having required minimum assurance coverage determined by the Board.

2.2.2. Quality assurance systems

Within the audit firms reviewed, 6 of them were have deficiencies in their quality assurance systems. Main contradictions and deficiencies related to quality assurance systems are consolidated below:

- Inexistence of guidelines about policies and procedures of the quality assurance systems and ethical principles for auditors.
- Inefficiency or insufficiency of the operation of the quality assurance systems.

2.2.3. Overall audit plan and programme

Within the audit firms reviewed, 5 of them were have deficiencies in their overall audit plan and programme. Main contradictions and deficiencies related to overall audit plan and programme are consolidated below:

- Not updating existing audit plan and programme,
- Inadequate content of the audit programmes.

- Not including the basic principles of IFRS such as valuation, classification and disclosure in the audit programme,
- Inappropriateness of the audit programme to the IFRS,
- Inexistence of guidelines about ethical principles for audit planning procedures,
- Not having subsidiary document for audit planning procedure,
- Not preparing the content of the audit programme which enables to use audit standards during an audit.

2.2.4. The other issues

Within the audit firms reviewed, 3 of them have contradictions and deficiency in other issues. Main contradictions and deficiencies in other issues are consolidated below:

- Not performing any audit work by the audit firm in last five years,
- Non-compliance of the regulations regarding drawing up and rescission procedures of the audit engagement.

3. Overall Assessment and Result

The consequences of 22 quality control reviews fulfilled by CMB in 2013 is summarized as follows:

1. An audit firm which cannot provide the establishment requirements can be delisted by the Board.
2. The planning of an audit work is a dynamic process which reduces the audit risk and effects the result of an audit work due to the fact that it can require to apply further audit techniques according to the specific conditions of the client company and also can require to apply different audit strategies. Seen as the methodology of audit firms, audit programmes are defined one of the mandatory establishment requirements. Therefore, audit programmes should be kept up to date.
3. The documentation of an audit work is very important because an audit work which is not documented is assumed as nonexistence of that audit work.
4. The collection of sufficient audit evidence together with preparing working papers for each section of an audit work, constitutes basis of an audit.
5. Insufficiency of audit planning, determining the level of materiality, understanding the operational area and relationships with legal environment, evaluation of material error risks and internal control systems makes the whole audit process questionable.
6. It is possible to use an expert study as an audit evidence, but the auditor should revise the objectivity and professional competence of the expert and also appropriateness of the assumptions and methodologies used in expert's study together with the correctness of the result of the expert's study.
7. Due to the fact that accounting estimates, fair value calculations, related party transactions and evaluation of going concern of the company significantly effects fair presentation, these issues are regulated in auditing standards as well as in financial reporting standards.

On the other hand, related party transactions have a significant importance in the Board's regulations, as they can cause illegal transfer pricing activities.

8. The audit firms and auditors have joint liability to the shareholders of the client company because of deficiencies and faults in the audit letters.
9. Auditors training so as to provide professional competence, establishment of corporate structure to adapt the ethical principles and control of the quality of an audit work are the major factors for obviating the deficiencies and insufficiencies in audit works and raising the quality of an audit.
10. The audit firms should fulfill their notification obligation on time and correctly.

The primary goal of the CMB in fulfilling these quality control reviews is to raise audit quality in terms of auditing standards and ethical principles. As a result of these reviews, it is mandatory to apply sanctions for audit firms and auditors, conducting audit contrary to the auditing standards and the Board's regulations. In this framework, delisting, administrative fine and notice are the sanctions applied to these audit firms and auditors by the CMB.

CAPITAL MARKETS BOARD OF
TURKEY
ESKİŐEHİR YOLU 8. KM
NO:156 06530
ANKARA-TURKEY
Tel : +90 (312) 292 90 90
Faks: + 90 (312) 292 90 00
<http://www.cmb.gov.tr/>