

ADGM Registration Authority

Audit Monitoring Report 2023

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1.0 Foreword from the CEO



Hamad Sayah Al Mazrouei
Chief Executive Officer,
ADGM Registration Authority



High-quality audit has been and will remain a key regulatory objective for the ADGM Registration Authority (RA).

At ADGM we recognise the importance of meaningful, reliable and timely corporate reporting for the efficient functioning of capital markets, investor protection, and for safeguarding the public interest. When corporate reporting includes accurate information about a company's affairs, performance and prospects, it helps to grow economic activity and create a more resilient economy.

The calendar year 2023 was a pivotal one for ADGM wherein the RA commenced its programme of risk-based audit onsite inspections using our in-house developed inspection methodology. These inspections were led by RA staff and were conducted at the offices of ADGM audit firms where inspection staff also reviewed the underlying audit work performed.

In 2023, the RA inspected six ADGM audit firms and unfortunately, the conclusions from four inspections revealed some disappointing findings. The findings indicate that some audit firms in ADGM have a significant amount of work to do to lift the standard of audit work they carry out.

Looking ahead, the RA will continue to build on its inspection programme and increase coverage over both - the number of audit principals and the number of audit files reviewed in the coming years. The RA is also committed to working with audit firms, regulators and authorities both in the UAE and internationally to improve audit quality and therefore strengthen corporate reporting.

In this report, you will read about the key findings we identified at our inspections and see our areas of focus for the remainder of the calendar year 2024.

I encourage audit committees, audit partners, audit engagement teams, investors, and other stakeholders who are interested in corporate reporting and financial audits to read this report.





2.0 Introduction and Overview

The RA is the commercial regulator for the jurisdiction of the ADGM which includes both Al Maryah and Al Reem Islands in the Emirate of Abu Dhabi. As part of its mandate, the RA is the competent authority responsible for registering, supervising, monitoring, and where necessary it has powers to sanction both audit firms and audit principals operating in ADGM.

At the time of publishing this report, there are more than 7,500 ADGM licensed persons. Not all entities are required to prepare and lodge annual audited accounts with the ADGM Registrar. However, those who are required to or voluntarily decide to have a statutory audit of their financial statements must use an ADGM Registered Auditor.

Generally, all ADGM Financial Institutions, private companies, limited liability partnerships and Distributed Ledger Technology (DLT) Foundations are required to have a statutory audit carried out. Audit exemptions are available for certain entities but where an audit exemption is availed, the reporting entity must ensure that all conditions attached to the exemption are followed.

The ADGM Companies Regulations (Auditors) Rules 2023 (Auditors' Framework) is part of the legal framework that governs auditors in ADGM. The enhanced ADGM Auditors' Framework came into effect on 1 December 2021 following approval by the ADGM Board of Directors. A key requirement under the Auditors' Framework is the requirement for ADGM auditors to hold the appropriate Additional Permit if they wish to audit ADGM public companies and/or Financial Institutions (regulated by the ADGM Financial Services Regulatory Authority).



ADGM's firm population includes more than 200 Financial Institutions and 21 public companies. As of 31 December 2023, there were 23 Registered Auditors (firms) and 95 Registered Audit Principals (individuals) in ADGM. Only these firms and individuals were eligible to carry out statutory financial audits of ADGM entities in 2023.

The purpose of this report is to highlight the results of the RA's audit monitoring activities in 2023 and list the areas of focus for the remainder of the calendar year 2024. This report will be of particular interest to audit firms, audit engagement teams, audit committees, investors and other stakeholders interested in financial reporting and audits.



3.0 Summary and statistics at a glance

In 2023, the RA inspected six firms covering nine audit principals through file reviews of 12 audit files, including audit reviews of two public interest entities.

The RA's inspections show that 67% of firms inspected required significant improvements in the quality of audit work they carry out. 11 out of the 12 audit files reviewed had at least one finding, with eight files being graded as requiring improvement, and in some cases significant improvement. In most cases, the findings are the result of insufficient audit evidence, significant gaps in documentation and/or poor

planning and risk assessment that led to the design of weak audit tests at the execution stage of the audit process. As part of its root-cause analysis, the RA considers stronger engagement partner involvement in the audit process coupled with the use of appropriate and current audit methodologies that factor in ADGM requirements would have helped prevent a number of the findings raised.

2023 Key audit inspection findings

No.	Finding area	Issue
1.	Audit methodologies	Limited or no use of an appropriate audit methodology and/or financial statement disclosure checklist that factors in ADGM requirements.
2.	Planning procedures	Gaps in planning procedures, understanding of the entity and its environment and risk assessment.
3.	Revenue	Insufficient audit evidence on key audit assertions which in some cases is partly due to the design of weak audit tests and inadequate audit planning procedures.
4.	Group audits	Inadequate group audit work by group auditor, including areas concerning scoping and materiality, understanding the component auditor(s), and communication with the component auditors.
5.	Journals testing	Limited to no work on journals testing, particularly on files where the audit team highlighted the significant risk of management override of controls.
6.	Going concern and subsequent events	Inadequate audit work to support the assumption that the entity is a going concern and/or to confirm post-period end events requiring disclosure or adjustment have been identified in the financial statements.
7.	Quality control	Limited involvement of the ADGM Registered Audit Principal in the audit process from planning to completion or the engagement partner is not the same as the individual issuing and signing the audit report.



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2024 Areas of focus

No.	Area of focus
1.	Engagement acceptance – including assessing how the firm gained comfort accepting/ continuing with the audit engagement.
2.	Quality control – emphasis on the role and involvement of the engagement partner in the audit process.
3.	Revenue – particularly assessing if the audit evidence obtained is sufficient and appropriate.
4.	Completion and reporting – overall approach to this stage of the audit process, particularly the audit team’s work on going concern, subsequent events and communication with those charged with governance.
5.	Group audits – assessing how the audit team understood and fulfilled the requirements of group auditors, including communication with component auditors.
Whole firm areas	
6.	Professional indemnity insurance (PII) – assessing the adequacy and appropriateness of the audit firm’s PII arrangements.
7.	System of quality management – assessing the firm’s implementation of quality management standards.

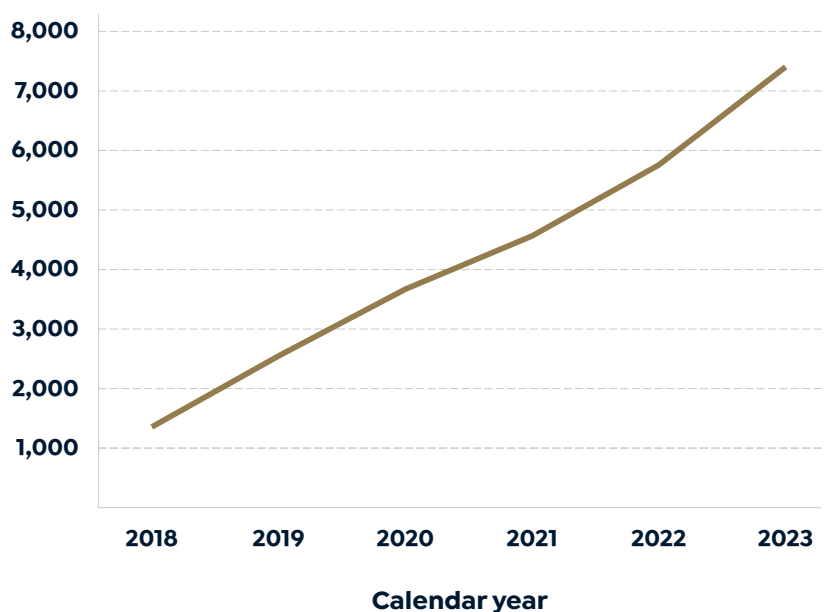
Statistics at a glance (2023)*

<p>c.7,200 ADGM Licensed Persons (vs c.5,800 at end of 2022)</p>	<p>20 ADGM Public Companies (vs 14 in 2022)</p>	<p>23 ADGM Registered Auditors (vs 20 at end of 2022)</p>	<p>90 ADGM Registered Audit Principals (vs 47 at end of 2022)</p>
<p>12 Audit file reviews</p>	<p>11 Number of files with at least one finding</p>	<p>6 Audit Firms inspected</p>	<p>9 Audit Principals reviewed</p>
<p>2 Audit file reviews of public interest entities</p>	<p>8 Number of files requiring improvement</p>	<p>4 Firms received a 'significant improvement' required rating</p>	<p>2 Number of firms sanctioned</p>

**ADGM's Firm
Population Growth****

2018 to 2023

ADGM Licensed Persons



* Comparatives only provided where relevant

** These figures do not include legal persons on Al Reem Island.



4.0 2023: Audit inspection findings

In this section, we cover the key findings that the RA considers were the key reasons behind the grading of the audit file reviewed and therefore the overall grade of the inspection.

All audit engagements selected for review in 2023 were selected using the RA's risk-based approach to file selection. As the RA's audit oversight function evolves and builds further capacity, file selection in future years will see audits being selected at random as well.

The RA's risk-based approach to file selection considers a number

of factors that include the standing data the RA holds about the audit firm, principal(s), the underlying entity, assessing the public profile of the entity, the sector the entity operates in, the size and nature of the entity, as well as the underlying entity's significance to the economy and financial system of Abu Dhabi, the UAE and globally.



Finding area 1 - Audit methodologies

Four of the six firms we inspected were using incomplete or did not use an appropriate audit methodology at all. This meant audit engagement teams had limited or no work programmes to help direct their work at all stages of the audit process and in particular for significant risk areas, such as revenue recognition. Audit methodologies that are regularly updated to incorporate changes to International Standards on Auditing (ISAs) are key for a high-quality audit. Audit work programmes are vital to ensure sufficient work is being undertaken that is appropriate for the audit assertions being tested.

Similarly, most firms we inspected did not use a financial statement disclosure checklist or they used one that did not specifically and adequately include all the accounts requirements in ADGM's Companies Regulations 2020 (CR 2020). This is particularly relevant because CR 2020, ADGM's company law, has some disclosure requirements for accounts that go over and above those in the International Financial Reporting Standards (IFRS), such as disclosing information about employee numbers and costs.

Finding area 2 - Planning procedures

Despite the planning stage being a key area of the audit process, our file reviews showed several instances where engagement teams did not perform sufficient audit work in this area. This included communication with those charged with governance (ISA 260), assessing the nature of the related parties (ISA 550), understanding applicable laws and regulations (ISA 250), performing analytical procedures (ISA 315 and ISA 330), assessing significant accounting estimates (ISA 540) and documenting a thorough planning risk assessment that included the risk of fraud (ISA 240).

Further, where certain risks were identified or commented on, the audit files did not show how the audit team linked the planning risk assessment to their audit response or the underlying audit work carried out as part of their fieldwork and completion procedures. Additionally, the RA found in one instance, despite a significant limitation of scope on several significant risk areas, the audit engagement team continued with the audit engagement and failed to document and show what attempts it made to remove any or all the limitations or document why it could continue with the engagement. The firm relied entirely on issuing a modified audit opinion year after year.

Finding area 3 - Revenue

In several instances, we found insufficient audit evidence (ISA 500) on the relevant audit assertions for revenue. In most cases, the gaps in audit evidence were due to poor planning procedures and risk assessment, lack of an understanding of the entity and its environment, and insufficient audit work on assessing the design and implementation of key controls linked to the revenue cycle that led to poor designing of audit tests at the execution stage.

In one instance, we were pleased to see the engagement team highlight completeness and cut-off of revenue as a significant risk based on its understanding of the underlying entity, however, the direction of the audit test at the fieldwork stage did not provide adequate comfort over cut-off or completeness of revenue.

Finding area 4 - Group audits

The inspections show group audits are an area of real challenge for a number of audit firms inspected. The RA identified several findings in relation to group audits, particularly around the requirements of ISA 600.

A number of the audit engagements reviewed by the RA were those where the ADGM auditor acted as group auditor and issued an audit report on the consolidated financial statements of the ADGM entity.

In three audit engagements reviewed, the group auditor failed to perform adequate audit work as required by the ISAs. The findings related to insufficient work on group scoping and materiality, communication and group audit instructions with component auditors, auditing the consolidation, reviewing the work of the component auditor, inconsistent accounting policies or adequate professional challenge on the accounting treatment adopted, and gaps in documentation particularly around significant risk areas.

In one instance, the audit firm accepted the group audit engagement after all significant components had been through a statutory audit within their own jurisdiction. The group auditor simply relied on the component audit reports as audit evidence and as a satisfactory basis for issuing a group audit report.

Effective communication between group and component auditors coupled with robust planning and adequate documentation are critical for carrying out a high-quality group audit. Group audits vary drastically, from large and complex groups involving significant components in multiple jurisdictions to simple groups where most of the work can or is performed by a single audit engagement team in one location. The underlying requirements however are broadly the same and it is vital that audit engagement teams fully understand the group and tailor their approach accordingly.

Finding area 5 - Journals testing

Journals are a key part of the financial reporting process. Journals are used by the finance teams of entities to put through key adjustments that directly impact the final look of the financial statements.

ISA 240 is clear and has made journals testing mandatory irrespective of the risks of management override of controls. Despite this, on a number of audit file reviews, the RA found insufficient audit work in this area including showing what journals the audit teams selected made at the end of a reporting period, documenting their consideration of the need to test journal entries throughout the reporting period, and the inquiries made about inappropriate or unusual activity relating to the processing of journal entries. Where engagement teams did consider journals testing, the RA found insufficient audit evidence and weak documentation to show how the journals are backed by detailed calculations and documentary evidence.



The inspections show group audits are an area of real challenge for a number of audit firms inspected.





Finding area 6 – Going concern and subsequent events

As part of the audit engagement team’s completion and reporting procedures, on several instances, the RA noted inadequate work on the areas of going concern (ISA 570) and subsequent events (ISA 560).

Under the going concern basis of accounting, the accounts are prepared on the assumption that the entity is a going concern and will continue trading and operating for the foreseeable future. The auditor’s responsibilities include obtaining sufficient appropriate audit evidence to conclude on the appropriateness of management’s use of the going concern basis of accounting in the preparation of the financial statements.

In several instances, the audit work on going concern observed did not adequately show how the audit team evaluated and concluded on management’s assessment of the entity’s ability to continue as a going concern. In a few instances, there were clear indicators of events or conditions that suggested significant doubt on the ability of the entity to continue as a going concern, however, the audit file did not demonstrate what procedures or evidence the auditor performed and gathered to support the audit opinion issued. This included weaknesses such as not obtaining and challenging the forecast or budget for twelve months from the date of the period end, and lack of a letter of support or assessment of the financial health of the person (legal or natural) before placing reliance on confirmations of support.

Finding area 7 – Quality control

In most audits reviewed, the RA is particularly concerned with the level of involvement of the engagement partner in the audit process (or lack thereof). The ISAs are clear when it comes to what is required from the engagement partner; which includes direction, supervision and performance of the engagement as well as responsibility for reviews of the underlying audit work.

In five of the six audit firms we inspected, we found instances of non-compliance with ISA 220 (Quality Control) that related to insufficient involvement of the engagement partner in the audit process. In some instances, the ADGM Registered Audit Principal effectively simply signed the audit report without evidencing their review and involvement on the audit file.

Firms should pay attention to this area particularly given the relatively new quality management standards for audit (effective December 2022) that introduce a new requirement for firms to proactively identify and respond to risks of quality.

The RA is clear that under no circumstances would it expect that there should be any reason why the signing partner issuing the audit report will be separate from the engagement partner as defined in the ISAs. Firms need to ensure that the person taking responsibility for the audit meets all the criteria set out in ISA 220 and has authority from the RA to sign the audit report.



5.0 2024: Areas of focus

The RA will increase the number of inspections it carries out in 2024 and at the same time will increase its coverage of audit principals reviewed at each firm it inspects.

Stakeholder protection, including investors, as well as improving and helping to create a level playing field in ADGM will be at the heart of these efforts. With that in mind, the RA will be focused on the following areas in its audit supervisory activities for 2024:

a) Engagement acceptance and non-audit services

Careful consideration is required at the audit engagement acceptance and/or continuance stage for a high-quality audit, with particular reference to the requirements of ISA 210. The RA will assess the firm's procedures, thought process and rationale as part of its risk assessment to determine how the firm gained comfort accepting and/or continuing with the engagement. This will include the firm's client due diligence procedures.



Stakeholder protection, including investors, as well as improving and helping to create a level playing field in ADGM will be at the heart of the RA's audit supervisory efforts.



b) Engagement partner role and quality control

The RA will assess how the requirements of ISA 220 are met on each audit, with particular emphasis on the role of the engagement partner. Audit is a regulated activity in ADGM and the RA expects that only those individuals eligible to fulfil the role of an engagement partner are leading audits and issuing audit reports on behalf of the audit firm.

c) Revenue including long-term contracts

Revenue is often a key area of financial statements. The RA will continue to review the audit work performed in this area. The RA expects engagement teams to ensure the audit file clearly documents the team's planning risk assessment and understanding of the entity with linkage to the audit work carried out at the execution stage of the audit process.

d) Going concern and subsequent events

The RA will be assessing the auditor's evaluation of the fundamental assumption that an entity will continue to operate in the foreseeable future – a key concern for investors, management and auditors alike. The RA expects to see clear documentation on audit files to show how the audit team were comfortable with the financial viability of the entity and its ability to be resilient against current and future stresses.

Similarly, the RA will also be assessing the audit work on subsequent events that impact the financial statements in line with International Accounting Standards (IAS). IAS are clear and prescribe when an entity should adjust its financial statements for events after the reporting period and the disclosures that an entity should give about the date when the financial statements were authorised and about events after the reporting period.

e) Group audits

This is an area of challenge for several audit firms. The RA's audit file reviews will be assessing the audit work on various areas of group audits, including but not limited to scoping and materiality, communication with component auditors, logistics on group audits, audit of the consolidation, review of the component auditor's work and the arrangements around regulator access to working papers of the component auditor in accordance with Rule 23 of the ADGM Companies Regulations (Auditors) Rules 2023.



At a firm-wide level, the RA will pay particular attention to the whole firm procedures including:

f) Professional indemnity insurance arrangements

Assessing the adequacy and appropriateness of the firm's professional indemnity insurance (PII) arrangements with reference to its size, nature, and activities. It is the RA that assesses the firm's PII arrangements. The RA expects firms to cooperate fully with the RA and not conceal any information from it in accordance with Rule 27 of the Auditors' Framework.

g) System of quality management

The scope of the RA's audit inspections will continue to include an assessment of the firm's implementation of the International Standard on Quality Management (ISQM) 1.



6.0 Conclusion

The value of auditors and the role of auditors should not be underestimated. The financial statements published by directors of companies are independently audited in order for them to be considered credible.

Auditors are in a unique position and have access to information not many other professional services firms and advisors have. When an audit is of high-quality and carried out in accordance with the ISAs, it provides significant comfort to the users of the financial statements and helps stakeholders, particularly investors, make informed decisions.

The RA recognises the important role of auditors and considers itself to be an improvement regulator that supervises in a manner that is risk-based and proportionate to the circumstances.

Audit firms have numerous challenges to face in 2024, including, increasing regulation, new accounting and auditing standards, the impact of

climate change, the adoption of artificial intelligence, and decreasing rates of newcomers in the profession coupled with recruitment and retention challenges. It is imperative that auditors face these challenges head-on, and that all stakeholders work together to support high-quality audit, e.g. auditors, regulators, professional accountancy bodies and underlying entities.

The RA urges audit firms and audit engagement teams to take note of the revised ISA 315 standard and ensure they are following the 'stand-back' procedures. Engagement partners in particular should make sure that someone is standing back, that audit teams are sufficiently resourced, and that their involvement in the audit process is timely and adequate.



7.0 Additional resources

The RA regularly publishes new resources and updates existing resources on the ADGM website.

Some key resources include the following:

1. RA Auditors

a. Public Register

ADGM licensed persons must use an ADGM registered auditor for a statutory audit of their annual accounts. The list of ADGM Registered Auditors (firms) and Registered Audit Principals (individuals), can be accessed here:

<https://www.adgm.com/operating-in-adgm/auditors/find-an-auditor>

b. New auditors

Auditor applicants wishing to establish themselves in ADGM can find out more about the process and view the frequently asked questions sections here:

<https://www.adgm.com/operating-in-adgm/auditors/new-auditors>

2. RA Annual Accounts Guidance

For guidance about the accounts' obligations for ADGM companies, please access the Annual Accounts Guidance here:

<https://www.adgm.com/documents/legal-framework/guidance-and-policy/ra/guidance-for-registered-entities/ra-annual-accounts-guidance-v10-09092022.pdf>

3. RA Decision Procedures, Disqualification and Enforcement Manual

For more information on the RA's approach to enforcement, please refer to the RA Decision Procedures, Disqualification and Enforcement Manual, available here:

<https://www.adgm.com/legal-framework/guidance-and-policy-statements>

4. RA Regulatory Alerts

The RA publishes regulatory alerts about potential misconduct such as fraud or unlicensed activities to inform the public (including investors) so that they take any required action to protect themselves from harm. Regulatory alerts can be accessed here:

<https://www.adgm.com/operating-in-adgm/monitoring-and-enforcement/regulatory-alerts>

5. RA Regulatory Actions

The RA publishes its regulatory actions on the RA Regulatory Actions page, examples of such enforcement actions include imposition of financial penalties, cancellation of licence, imposition of conditions/restrictions on licence, censures, enforceable undertakings, settlement agreements, etc. The Regulatory Actions page can be accessed here:

<https://www.adgm.com/operating-in-adgm/monitoring-and-enforcement/regulatory-actions>

6. Register of Disqualified Directors

The RA publishes details of directors disqualified from being a director of any ADGM company or prohibited from being concerned or taking part in the promotion, formation or management of any ADGM company for a period of time. The register may be accessed here:

<https://www.adgm.com/operating-in-adgm/monitoring-and-enforcement/register-of-disqualified-directors>



7. Public Notices

The RA announces important notifications primarily in relation to voluntary and involuntary strike offs. Public Notices also include liquidations, receiverships, restorations and registered documents where applicable or required to be published by the Companies Regulations 2020.

<https://www.adgm.com/registration-authority/public-notices>

8. Complaints

The RA manages and assesses complaints concerning potential contraventions of the ADGM's commercial legislation or activities that may cause damage to the reputation of ADGM. Information on how to submit a complaint to the RA can be accessed here:

<https://www.adgm.com/registration-authority/complaints>

Disclaimer

This report provides information on the Registration Authority's audit monitoring activities. This report is only a guide and should be read together with ADGM's commercial legislation, including relevant regulations and enabling rules (which may change over time without notification). Further advice from a specialist professional may be required.

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