The Importance of Audit Quality

Investor confidence is fundamental to the efficient operation of the world’s financial markets and contributes to economic growth and stability worldwide. Investors need to know that the financial information on which they base capital allocation decisions is credible and reliable. Audits, and audit opinions on financial reports, are crucial to achieving this. Independent auditors play a vital role in enhancing the reliability of financial information produced by companies, not-for-profits, government agencies, and other entities by providing assurance on the reliability of the financial statements.

While the primary responsibility for the quality of financial statements is with the management of the company producing those statements, external auditors provide independent assurance about that quality.

The Value of International Standards

The rapid growth of global markets has put renewed emphasis on the development of and need for international standards on auditing. As the world continues to become smaller and international investment more and more frequent, the use of a common set of international standards presents clear benefits to investors, regulators and audit firms.

- **For Investors**
  Few major investors confine their activities within the borders of their own countries. As they seek to evaluate investment opportunities and monitor the performance of a global portfolio, investors will benefit from having access to financial information that has been prepared in accordance with international standards. They will have a better understanding of and more confidence in the financial information of the companies in which they have invested if the financial information they are reviewing is prepared and audited using common international standards.

- **For Regulators**
  For international regulators, the advantages are similar to those for investors — it is easier to accept that foreign issuers are meeting the necessary standards if those standards are being used for domestic purposes as well as for international ones. In addition, a regulator enforcing international standards at home may find it easier to persuade a foreign regulator to rely on the home regulator’s work.

- **For Audit Firms**
  For the international auditing firms, the advantages are efficiency associated with applying a common audit approach and knowing that it complies with relevant standards. There are benefits to other audit firms as well. For example, if auditors have clients with overseas subsidiaries, the process of instructing overseas auditors and relying on their work will be facilitated if the usual standards, which are applied locally, are the same as those of the parent auditor. Similar advantages will be clear where the auditor is dealing with a subsidiary of a group audited by another overseas firm.
The Criteria for High-Quality Standards

Quality is the most fundamental characteristic of international auditing standards. What does quality mean and how can it be achieved? Quality standards should be understandable and based on clear principles. They should be capable of consistent interpretation. They should be capable of unambiguous translation, should be enforceable, and should be designed to achieve a high quality audit. Most importantly, they need to be established by an international body that follows a rigorous due process with significant public interest input. The International Auditing and Assurance Standards Board is such a body.

International Auditing and Assurance Standards Board

The International Auditing and Assurance Standards Board (IAASB) is a standard-setting body designated by, and operating under the auspices of, the International Federation of Accountants (IFAC) and subject to the oversight of the international Public Interest Oversight Board (PIOB) for accountancy. The IAASB issues high-quality international standards on auditing and assurance, quality control and related services, and facilitates convergence of national and international standards.

- **Composition**
  The IAASB consists of a full-time chairman and 17 volunteer members from around the world comprising accountants in public practice with significant experience in the field of auditing and other assurance services, as well as individuals who are public members.

  Members of the IAASB are nominated by IFAC member bodies, the Transnational Auditors Committee (TAC) (which acts as the executive committee of the Forum of Firms) and, for public members, through nominations from member bodies, the TAC, other organizations, and the general public. The PIOB approves the nominations to the IAASB. Biographies of IAASB members are available on IFAC’s website (www.ifac.org/iaasb). Official observers with the right to speak at IAASB meetings are the Chair of the IAASB Consultative Advisory Group and representatives of the European Commission, the Japanese Financial Services Agency, and the US Public Company Accounting Oversight Board.

- **IAASB Meetings: Open and Transparent**
  The IAASB meets four to five times a year at different locations around the world. Its meetings are open to the public. Individuals may register to attend these meetings through the IFAC website. Agendas, background papers and project histories may be downloaded from here as well. The highlights of each meeting are also posted on the IAASB section of the IFAC website. In addition, individuals can view project histories and may download audio recordings of the IAASB meeting proceedings. They can also download IAASB exposure drafts and view all comments made on those drafts by regulators, investors, firms, standard setters and others.

International Auditing and Assurance Standards Board

Professional Composition

![Diagram showing professional composition of the IAASB members]
International Standards on Auditing
The IAASB's pronouncements govern audit, assurance and related services engagements that are conducted in accordance with international standards. International Standards on Auditing (ISAs) are to be applied in the audit of historical financial information. Through an extensive consultative process, the IAASB strives to ensure that these standards are responsive to the public interest, reflective of business reality, and capable of application by auditors worldwide. Recognizing that the auditor’s ability to carry out his or her responsibilities effectively is empowered by the public trust, the IAASB works to help auditors to retain that trust by continually reviewing and updating its standards in the light of changes and developments in the worldwide business and regulatory environments.

The IAASB works on the basis that if the public is to have confidence in audited financial statements, they must have confidence in the standards that govern auditors' work.

• Rigorous Due Process
  The IAASB follows a rigorous due process in the development of its standards and guidance, which includes substantial public interest input. The IAASB identifies new projects based on a review of national and international developments and on comments and suggestions from those who are interested in the development of its international pronouncements. In addition, when it is determined that a wide range of views is needed on a particular topic, the IAASB may hold a public forum or roundtable on the topic.

  Generally, the due process is comprised of the following steps:

  Research and consultation — A project task force is established with the responsibility to develop a draft standard. The task force develops its positions based on appropriate research and consultation. The task force may include non-IAASB members who have an interest or expertise in the subject.

  Transparent debate — A proposed standard is presented as an agenda paper for discussion and debate at an IAASB meeting, which is open to the public.

  Exposure for public comment — Exposure drafts are placed on the IAASB’s website and are widely distributed for public comment. The exposure period is ordinarily no shorter than 120 days.

  Consideration of comments received on exposure — The comments and suggestions received as a result of exposure are considered at an IAASB meeting, which is open to the public, and the exposure draft is revised as appropriate. If the changes made after exposure are viewed by the IAASB to be substantive so as to required re-exposure, the revised document will be reissued for further comment.

  Affirmative approval — Approval of exposure drafts, re-exposure drafts, international standards and practice statements is made by the affirmative vote of at least two-thirds of the members of the IAASB.

The Public Interest Oversight Board has approved this due process.
• **Outreach to Stakeholders**
  The IAASB makes it a priority to reach out to its stakeholders on an ongoing basis. Such outreach is critical to understanding the needs of those who use its standards and to understanding the expectations of the public.

  The IAASB receives advice on its work program and on technical matters from its independently chaired Consultative Advisory Group, which is comprised of representatives of business, investors, and other users of its standards. The IAASB seeks input on matters of importance to small- and medium-sized accounting practices and enterprises through dialogue with IFAC’s Small and Medium Practices Committee. The IAASB also works with national auditing standard setters from around the world on convergence, collaboration on projects and sharing of resources. In addition, when it is determined that a wide range of views is needed on a particular topic, the IAASB may hold a public forum or roundtable on the topic.

• **Current Developments**
  The IAASB has undertaken an ambitious program to make its standards more understandable and capable of being translated, and to facilitate international convergence. It has developed a new drafting style that makes the standards more readable and that clarifies the obligations imposed on professional accountants by the requirements of the standards. It is anticipated that this IAASB “Clarity Project” will facilitate the use of future ISAs and thus further contribute to enhancing audit quality worldwide.

**Growing Acceptance of ISAs**

There is a growing acceptance of ISAs, particularly adoption and use of the standards by:

– The Financial Stability Forum, which includes International Standards on Auditing in its *12 Key Standards for Sound Financial Systems*;
– Large international accounting firms that are members of the Forum of Firms;
– Regulatory bodies accepting financial statements audited using the ISAs for regulatory filings in their countries, or requiring the use of ISAs by including them in company law; and
– National accountancy bodies that have used ISAs as the basis for their national auditing standards.

Over 100 countries are using or are in the process of adopting or incorporating ISAs into their national auditing standards or using them as a basis for preparing national auditing standards.

In addition, the European Commission has specified in its Eighth Company Law Directive that international standards on auditing will be used for all audits in all Member States and has indicated that it is considering the endorsement of ISAs as those international standards.

**International Standard Setting: A Look Ahead**

As it looks ahead, the challenges for IAASB are to:

– Review its audit standards on a regular basis to reassess whether they continue to meet the needs of investors and others in society and to provide a level of assurance that they expect;
– Address specific assurance subject matters taking account of developments in, and international views on, assurance work by auditors in areas such as sustainability reporting and internal control reporting; and
– Establish a process for responding to requests for interpretations and guidance on emerging issues.

The IAASB will continue to be responsive to the needs of the investing community and will continue to earn the trust of regulators, investors, auditors and others in providing the high-quality standards that the world demands.