



IAASB CONSULTATION PAPER: A Framework for Audit Quality

RESPONSE FROM ICAS TO THE IAASB

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Background

1. ICAS welcomes the opportunity to comment on the IAASB's Consultation Paper: *A Framework for Audit Quality*. Our CA qualification is internationally recognised and respected. We are a professional body for over 19,000 members who work in the UK and in more than 100 countries around the world. Our members represent different sizes of accountancy practice, financial services, industry, the investment community and the public sector. Almost two thirds of our working membership work in business, many leading some of the UK's and the world's great companies.
2. Our Charter requires its committees to act primarily in the public interest, and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members' views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

Key Points

We welcome the initiative taken by the IAASB to issue the Framework and see it as a useful reference tool and source of guidance for auditors and other stakeholders.

We do, however, have concerns over the lack of emphasis given to smaller entities and would have preferred some guidelines on how proportional application of the Framework might be applied to these entities.

We believe that the issue of audit quality is of key importance, demonstrated by our collaboration with the Financial Reporting Council (FRC) in the UK on two research projects commissioned to investigate the competencies and professional skills of auditors. These projects will consider the mix of attributes, competencies, professional skills and qualities that need to be combined in an audit team in order for it to perform a high quality public interest audit in a modern, complex global business environment. The findings from these projects are expected to be published in 2014. We will of course forward copies of the released reports to you when they have been published.

Our responses to the specific consultation questions:

Question 1

Does the Framework cover all of the areas of audit quality that you would expect? If not, what else should be included?

Response 1

We would have preferred a greater emphasis on considerations specific to smaller entities within the paper, along with guidelines on how proportional compliance with the Framework might be applied to SMPs and SMEs. At present, the reference to such entities is only contained in the final pages of the Framework.

Question 2

Does the Framework reflect the appropriate balance in the responsibility for audit quality between the auditor (engagement team and firm), the entity (management and those charged with governance), and other stakeholders? If not, which areas of the Framework should be revised and how?

Response 2

We welcome the inclusion of the regulators as part of the audit quality process and references to the other parties involved in the audit process in recognition that audit quality is dependent on the involvement of all stakeholders.

However, the Framework should include some stipulations against placing too much emphasis on information obtained from management when obtaining reliable audit evidence. It should be stressed within the Framework that independent information is normally more reliable and therefore the requirement to corroborate information obtained directly from management should be embedded within the Framework.

Question 3

How do you intend to use the Framework? Are there changes that need to be made to the form or content of the Framework to maximize its value to you?

Response 3

We acknowledge the usefulness of the Framework and envisage that it will form a helpful reference tool and source of guidance for auditors, investors, those charged with governance and other stakeholders.

We have observed the numerous references throughout the framework to the need for auditors to exercise professional judgement during an audit engagement. Guidance on the application of professional judgement is available in the ICAS publication: *A professional judgement framework for financial reporting*. We would supplement the proposed Audit Quality Framework with this publication to provide assistance and guidance to auditors on how professional judgement might be applied for a particular transaction or group of transactions. The publication can be viewed at: <http://icas.org.uk/pjf/>

Question 4

What are your views on the suggested Areas to Explore? Which, if any, should be given priority and by whom? Are there additional Areas to Explore?

Response 4

Within the areas to explore, we have made the following comments:

1. Establishing global guidance against which audit firms can assess their governance arrangements (refer to page 25)

We would agree that there should be governance arrangements in place for the largest audit firms auditing companies trading on regulated audit markets. Any global guidance should be flexible enough to allow national requirements to be recognised.

We agree that there is a need for firms that do not audit companies that trade on regulated markets to have governance requirements in place, but believe that these requirements should be proportionate to the size of the firm and the client base. We would also argue that the “tone at the top” requirements are adequately covered for such firms by the requirements in ISQC1.

2. Establishing a common understanding of capabilities, and how they are demonstrated and assessed, as they relate to audit quality for use by audit firms when recruiting, evaluating, promoting, and remunerating partners and staff (refer to page 26).

This is an area that we believe should be given priority. ICAS and the FRC have recently commissioned two joint research projects investigating the competencies and professional skills of auditors. These projects will consider the extent of auditors’ responsibilities today and how this might change in the future. The aim of the projects is a contribution to restore market confidence through improving audit quality and re-building trust in the audit profession.

The projects intend to investigate the mix of attributes, competencies, professional skills and qualities that need to be combined in an audit team in order for it to perform a high quality public interest audit in a modern and complex global business environment.

The projects will also consider whether a reassessment of the staffing model is required for the audit of complex businesses to incorporate, for example, individuals with relevant business or technical experience within the audit team, and associated training implications.

The projects will identify and compare the essential audit skills and competencies within audit teams in the UK and those in Europe, South Africa and Australia. The findings are expected to be published in 2014. We will of course forward copies of the released reports to you when they have been published.

3. Improving information sharing between audit firms when one firm decides to resign from, or is not reappointed to, an audit engagement (refer to page 29).

There are currently ethical and statutory requirements within the UK for information sharing between audit firms but whether these could be applied on a global basis will depend upon the current ethical and legislative arrangements within each jurisdiction.

4. Considering whether audit inspection activities can do more to improve audit quality and to make audit quality more transparent to users (refer to page 42).

The comment in the consultation paper refers to the fact that audit inspection is a relatively new activity in many territories and that practices are evolving. This is not the case in the UK where audit inspection is a mature regime which has been operating for, and has evolved significantly, over 23 years.

In the UK, the audit inspection process looks at audit quality and our work is subject to oversight and supervision (via annual inspection visits) by the FRC, itself responsible for monitoring the largest of the firms auditing clients trading on regulated markets.

Each body reports to its monitored populations on the key findings for the year, and all UK recognised supervisory bodies, of which ICAS is one, are required to report their findings annually to the FRC which publishes an annual public report on all UK monitoring activities.

In addition to ICAS promoting audit quality on a firm by firm basis through the inspection, committee and follow up process, the FRC has also been active in requiring each audit recognised supervisory body to promote audit quality through various initiatives (and indeed has been inspecting our initiative programme each year to ensure it is appropriate). ICAS has been active in the last number of years in various audit quality initiatives which include education and support to our audit firms. This includes the provision of training and publications by the ICAS monitoring function.

Whilst we recognise that there may be benefit in national initiatives or international information sharing, we would strongly argue against any moves towards international harmonisation or the development of international requirements which could potentially hamper more established regimes from innovating and developing further.

5. Exploring whether there would be value in national authorities responsible for determining sanctions on auditors exchanging information with a view to evaluating the relative effectiveness of their different arrangements (refer to page 42).

Arrangements for taking disciplinary actions on auditors have evolved in a national context and are likely to be closely linked with the underlying national legal framework. That said, the sharing of information on matters such as the criteria that define an audit failure, the thresholds for sanctions, and available sanctions may assist to improve these arrangements.

6. Considering “root causes” and best practices by regulators, audit firms, and the wider audit profession in order to learn from past audit deficiencies and to identify and address systemic issues (refer to page 42).

Investigations into possible audit failures are likely to identify areas of audit weakness. To the extent that such weaknesses could be systemic it is important that action is taken to eliminate them as soon as practicable. Formal analysis of the ‘root causes’ of audit failings may assist action being taken to stop them recurring.

Audit firms and professional accountancy organisations would also benefit from self-examinations and internal inspections and investigations that lead to improving audit methodologies and approaches.

Again, whilst we appreciate that international information sharing would be of benefit we would argue against international 'harmonisation' or requirements.

7. Increasing the informational value of auditor's reports and improving perceptions of the value of the audit (refer to page 44).

Recent proposals by the IAASB, the FRC in the UK and within Europe to improve the auditor's report have been seen as a welcome move to increasing the informational value of the auditor's report and enhancing the perceived value of the audit process. The recent IAASB proposal recommends that the auditor's report includes commentary and reference to the key audit areas and assumptions considered during the audit process; references to the significant risks that the entity faces and an explanation of the application and calculation of materiality levels. It is hoped that this additional information will provide users and readers with a greater insight into the work undertaken by the auditor and the audit process itself thus increasing the perceived value of the audit. We look forward to contributing to the developments in this area.

8. Achieving improved two-way communication between auditors and financial and prudential regulators, particularly in the financial services sector (refer to page 50).

We welcome the suggestion for improved two-way communication between auditors and financial and prudential regulators, and believe that having access to such additional information relating to the audit process, as referred to above, might facilitate such communication. We would also suggest that the definition of regulator is extended to include other regulatory bodies, for example, charity regulators, housing association regulators and the pensions' regulator.

9. Striving for greater international harmonization in the role of audit committees with regard to the evaluation of the quality of the external audit (refer to page 56).

And

10. Encouraging audit committees to provide more information to users of the financial statements on the work they have undertaken, the main issues they have addressed, and the reasons for their conclusions (refer to page 57).

A useful contribution when considering the role of the Audit Committee in the evaluation of the quality of the audit is the recently updated UK Corporate Governance Code. Whether this could be applied on a global basis will depend upon the current ethical and legislative arrangements within each jurisdiction.

The Code seeks to strengthen the role of the Audit Committee in the external audit evaluation and financial reporting process and their responsibility for monitoring the integrity of the financial statements.

Under the Code, the Audit Committee will also ensure the independence, objectivity and effectiveness of the audit process in accordance with the relevant regulatory environment and advise the board on whether the annual report and accounts is fair, balanced and understandable.

This guidance within the Code might provide a useful reference point when considering the role of the Audit Committee in other jurisdictions.