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OPENING A DISCUSSION: *THE FUTURE OF AUDIT AND ASSURANCE*

Dear Hilde:

The International Federation of Accountants (IFAC) values the opportunity to comment on the Federation of European Accountants (FEE) discussion document, *The Future of Audit and Assurance*. Through its current membership of 179 professional accountancy bodies in 130 countries and jurisdictions, IFAC represents approximately 2.5 million accountants in public practice, industry and commerce, government, and education.

General Comments

IFAC commends FEE on issuing this discussion document. It is important for the accountancy profession to periodically take stock of and reflect upon the future of the most critical aspects of its existence. Initiatives like this highlight the need for the profession to be proactive and forward-looking, or risk having its agenda set by others. Indeed, it is much easier for the profession to say to others that they “don’t understand”, that it is all “very complex”, and thus nothing really needs to change. However, as recent experience has shown, if the accountancy profession does not take responsibility for its own future, then others—many who have a less-informed understanding of the key issues—will see it as their place to impose upon the profession from outside.

IFAC would be pleased to discuss with FEE ways in which it might assist in progressing this discussion to an international level. That is, while IFAC’s response is provided within the environmental context in which this particular discussion is being undertaken—that is, Europe—many of the issues highlighted in the discussion paper do have broader, international relevance.

In responding to the following specific questions, IFAC notes that several appear to go beyond what might be considered the realm of audit and assurance. IFAC is encouraged to see the preliminary assumption on page 5 of the discussion document that notes that audit and assurance is only one part of a “*whole ecosystem of the financial and non-financial reporting supply chain within the broader corporate governance environment*”. This is a critical point to understand and demonstrates the difficult task that the profession and stakeholders confront in reviewing the future of audit and assurance in isolation.



Additionally, IFAC notes that there are several questions related to public sector financial reporting. IFAC believes it is important to debate the quality of public sector financial reporting; and that discussions about the future of audit and assurance should not be restricted just to the private sector.

Finally, IFAC has responded to several of the questions (e.g., Questions 13, 15, and 16) by presenting its views, but recognizes that in-depth consultation with a broad representative group to determine the future of audit and assurance services, what it is that the future of audit and assurance might look like, and clarifying the expectations of others, might ultimately lead to a different, or more refined, responses.

Specific Questions

Questions related to the objectives of opening this discussion

1. How can we respond to expectations in a constructive and realistic manner?

An open discussion and, a proverbial “clean slate”, might lead to proposals for alternatives to an audit, the need for wholesale changes in the scope of audits, and even a re-evaluation of some of the fundamental tenets of audit and assurance.

IFAC believes it is important for the profession—and its members—to be open and willing to accept the need to undertake a critical self-examination. Rather than being defensive, a broad range of options should be identified and considered in an open and constructive manner.

However, in recognition that audit and assurance is only one part of a complex financial reporting chain comprised of many components, relationships, and interactions, the profession will not be able to make changes and progress developments without the support and collaboration of others. In responding in a constructive and realistic manner, all key stakeholders—e.g., investors, analysts, other financial statement users, directors, corporates, regulators, standard setters—must be approached, consulted, and encouraged to actively contribute.

2. How should the profession engage with stakeholders?

The profession should be open and transparent in its engagement with stakeholders. It should aim to engage directly (e.g., one-on-one meetings, open debates, events, webinars, roundtables, etc.), as well as with the broader public through widely publicized discussion papers, consultations, and the like.

However, it will be important to aim for internationally consistent (where achievable)—ideally commonly agreed, if that is possible—expectations about what it is that is hoped to be achieved from this engagement.

Questions related to the section on the professional accountant’s focus in day-to-day activities

3. Do standards add the intended value or do they inhibit innovation? Are standards becoming too rules-based?

IFAC’s view is that it is unquestionable that high-quality, globally-accepted, standards add value to the process of high-quality financial reporting (and as appropriate, other professional services for which there are standards in place). The adoption and implementation of these standards across a range of jurisdictions promotes greater consistency and therefore comparability.



However, when considering whether standards add value or inhibit innovation, it is relevant to consider why standards are developed, how they are developed, and the environment within which they are being used. That is, standards that are “fit-for-purpose” and are responding to an identified need—a demand from stakeholders—will implicitly add value, and can be seen as innovative in terms of being new or revised.

Additionally, value is created by the manner in which standards are developed, the process that is followed, and the broad stakeholder engagement that is involved. Potentially, this means that innovation is promoted through the breadth of views presented and the matters considered. However, it is worth contemplating whether it is audit, as it is now described by auditing standards, that requires innovation; or whether it is what audit might be in the future that requires an innovative outlook. Differing perspectives may arise depending upon the views on whether standard setters should be innovators or the codifiers of practice. It might indeed become seen as a classic “chicken-and-egg” scenario. That is, how can practice evolve and innovate if the standards they use are too prescriptive?

In IFAC’s view, standards should be written and applied in a manner that permits—and requires—competent and professional auditors to exercise their professional judgment. The cultural environment and the pace of change within an environment can dictate the nature of the standards being used, and the type of standards—principles-based or rules-based—that are most effective. With this in mind, IFAC does not see that the issue is so much about the standards being “principles-based” or “rules-based”, but rather, about the manner in which the standards are adopted, implemented, interpreted, and enforced. While it is ideal that all jurisdictions adopt, implement, and interpret standards consistently, the reality is that this is very hard to achieve.

In considering the future of audit and assurance thinking needs to extend beyond the current confines of existing assurance services; for example, what an audit is, and how it is described and presented in auditing standards. That is, greater thought needs to be given to what it is that an audit should be, and the value that it currently provides. What is it aiming to achieve? What is it achieving? What should it aim to achieve? How can an audit create and enhance value?

4. Do standards make our profession stand out? Why or why not?

The global nature of the standard-setting process, the number of jurisdictions using the standards, and the shared private-sector/public-sector arrangements for setting standards, make the standards used by and set for the accountancy profession stand out from others.

It seems that there are very few examples of other professions or industries where there is the same degree of international acceptance and cooperation; including the high level of interaction that exists between the profession and the regulatory community.

However, it is not always clear that the public at large appreciates the stringent standards with which auditors must comply when completing an audit engagement; as well as the highly-evolved, robust processes in place for developing standards. Greater promotion of these points might conceivably make the profession stand out even further.



5. How can we further develop and demonstrate integrity and objectivity instead of only independence?

A critical examination and evaluation of the future of audit and assurance cannot be undertaken without questioning auditor independence. If a key construct in the future relates to the manner in which an audit (or whatever it might be known as in the future) adds “value” to financial and corporate reporting as part of a complex reporting chain, some argue that independence, as we currently understand it, could be too restrictive to enable an auditor to add greater value. Alternatively, others might argue that the greatest value that an audit provides to society, from a public interest perspective, stems from the auditor being totally independent of the entity being audited.

Principles of integrity and objectivity will continue to be paramount. However, it is not an easy matter to suggest how appropriate behavior, in line with these principles, can be promoted and instilled to the satisfaction of the “public perception”.

Education and a focus on value seem to be obvious suggestions, but are not particularly well-defined ones, and much more work would need to be undertaken on the subject. Discussions about “value” inevitably lead to debates around what values means, what it means to whom, and trade-offs between efficiency and effectiveness.

IFAC notes that questions about the appropriateness of behavior—acting with integrity and objectivity—should not just be restricted to auditors. In enhancing the quality of financial and corporate reporting, it is critical that all components of the reporting supply chain are held accountable for their roles and interactions, and behave in accordance with sound ethical principles.

6. At which level will you be affected by IT innovation in the coming years? If applicable, for which type of services?

IT innovation will impact IFAC across all of its constituent groupings and areas of responsibility and interest. Conceivably, IT innovation will impact the accountancy profession across all professional services that accountants provide.

As well as the impact on the operational (the way “we do things”) and day-to-day activities of the profession that will come with improvements and innovation in communications, there are several areas where inevitably, IT innovation would seem to have an impact. They include:

- the timeliness and accuracy of corporate reporting;
- the timeliness of auditing and the ability of an auditor to make “in-depth” enquiries with greater confidence;
- quality control and quality assurance of services such as audit engagements, as well as of members of professional accountancy organizations;
- cyber-security, confidentiality, data flows, and the privacy of data and information for all services;
- big data, and data analyses;
- anti-money laundering compliance and regulations; and



- the offshoring and outsourcing of professional services.
- 7. What are your views on the education and training of professional accountants and auditors? Is it fit for purpose? How can we ensure that it will be in the future? How can we develop education to improve the quality of services?**

IFAC believes that the education and training of professional accountants and auditors has typically been of a high standard, and have served the needs of the profession and society very well. There has traditionally been an appropriate combination of theoretical learning—largely in institutions of higher education and learning—and practical experience within the workplace.

However, the topic has long been debated. The need to ensure that professional accountants and auditors have the necessary technical expertise and competence to undertake their role is unquestioned. Unfortunately, however, there has not always been the same broad agreement on the need for relevant education and training in other important areas—e.g., “soft skills.”

It is important to consider that depending upon the types of services being provided, the education and training requirements of auditors and other professional accountants may vary greatly. The types of people being attracted to the profession might also change. It could be argued that more generally, professional accountants and auditors need to be educated on: behavioral matters that promote ethical behaviors (integrity, objectivity, and professional behavior); better communications, in particular listening, skills; better “people” skills, and enhanced critical thinking and reasoning, perhaps even being founded in some form of basic philosophy.

What is needed in the future depends on the types of services that will need to be provided. Without first having carefully examined what those services might be, it is not clear what education and training will be considered “fit-for-purpose”. However, one can envisage that in a rapidly changing business world where technological advances occur almost daily, the skills of the auditor would need to keep pace with the continually evolving environment. This includes the possibility that auditors will need to become more specialized and will be required to acquire and develop skills pertinent to specific industries, such as, for example, financial services or the energy industry.

In considering ways in which education can be developed to improve the quality of services, it is clear that the accountancy profession will need to maintain a close ongoing relationship with those providing education and training.

- 8. How can we ensure that we create a new type of auditor who can adapt and react to the current and future business challenges?**

As mentioned in the response to the previous question, predicting what type of auditor might be needed in the future is not a straightforward exercise. A critical re-evaluation of the service might lead to demonstrable changes. That is, the type of auditor that is needed in the future depends on the types of service that will need to be provided, and the environment—including whether it is the private sector or public sector—in which the auditor will be required to work.



Questions related to the section on the focus on the auditor’s communication

9. Do you see merit in further exploring the suggested changes in auditor reporting outlined above (i.e., page 9 of the discussion document)?

IFAC sees merit in further exploring the suggested changes outlined in the discussion document; but recognizes that there will be potentially a wide range of views across jurisdictions. IFAC reiterates that it is important to recognize that audit is only a part of the broader, more complex, financial reporting supply chain. Changes to auditor reporting—especially with respect to the frequency of reporting or the method of communication—cannot be done in isolation. These matters can only be considered in an effective manner with due consideration of what needs to be done to improve the reporting by the companies themselves.

Furthermore, there is a more fundamental issue to be considered when debating proposed changes to the auditor reporting arrangements and the reporting model. That is, whether changes to auditor reporting will answer the basic question about which many people appear to be concerned—what is it that an auditor is, or is not, supposed to do? A change in the reporting by auditors may not be as important as a change in the scope of an audit, or a fundamental re-think about what an audit should be, when critically examining the future of the service.

10. Are there any other areas in which the auditor’s involvement could add value?

In the current environment—where regulators are seemingly imposing more restrictive independence requirements, such as in relation to the provision of what may be considered “non-audit services”, especially for audits of public interest entities—it is not immediately obvious in what other areas the auditor’s involvement could add value.

If an audit service in the future was to be developed on a foundation of “objectivity” that was less restrictive than current independence rules, it is possible that: with the intimate knowledge of a company that an auditor gains and the risk assessment that an auditor undertakes; and with auditors’ technical expertise (and access to technical expertise); greater value might possibly be added in areas such as risk management and control, in communicating good practices, and in providing sound business advice.

Of course, some argue that broadening the scope of an audit could add value, including the provision of assurance on areas other than the financial statements; for example, integrated reporting. On whether value is created by an expanded auditor report, it is an open question as to whether more expansive auditor reporting will be seen as adding value for many stakeholders.

11. Do investors want different assurance to banks, to shareholders, to management?

It is assumed that this question refers to whether investors might desire to receive a different type of assurance service and/or a different level of assurance than might be desired by banks, shareholders, and/or management.

Based on that assumption, it is very likely that each of the stakeholders might have different expectations and requirements. This raises an interesting point to consider: Is it possible that assurance services of the future will be defined by the type of service that is provided, which may differ for different groups? Each group may engage with the assurance provider directly and pay for the service they desire.



While an examination of the future of audit and assurance might result in new and innovative services, based on the services that are currently available, it is conceivable that some groups may desire an audit, some might want a review, while others might want an agreed-upon procedures engagement. Furthermore, others still might be comfortable with the company's reporting and seek no additional professional service.

It is also possible that there may be more than one assurance provider per company, and that all assurance services might become voluntary and market/stakeholder demand driven. This, of course, would be a matter for each jurisdiction to determine.

12. Should the recipients of the audit report be more clearly defined?

Refer answer to Question 11 above.

Questions related to the focus on alternatives to better meet stakeholders' needs

13. According to your view, what range of services could be developed?

The range of services that might be developed will depend on the outcomes of a thorough self-examination and broad stakeholder consultation process. IFAC notes that currently there are a range of services that are available using international standards: for example, audits, reviews, other assurance engagements, agreed-upon procedures engagements, and compilations. IFAC also notes that other services have been developed in local jurisdictions, building on the international standards; such as an extended review engagement (in Denmark) and performance and compliance engagements (in Australia).

14. How can FEE be instrumental in further developments in this area?

The role that FEE might play is dependent on how further developments are identified, determined, and clarified. However, it seems that as the process evolves, FEE would have a role in facilitating further research, public discussions, debates, and consultations that in turn may assist in establishing its future role.

15. Is there a need to consider alternatives to statutory audit for SMEs?

IFAC believes that an examination of the future of audit and assurance, and the possibility for developing alternative services, should be broad and not specifically focus on the requirements for SMEs. That is, the process of examination and re-evaluation should consider the entire spectrum of entities and services; and should examine the fundamental pillars of audit arrangements, including regulation, that currently exists.

IFAC is firmly of the view that International Standards on Auditing™ (ISAs™) are designed for audits of entities of all sizes, and their design enables them to be applied in a manner proportionate to the size and complexity of an entity. However, it recognizes that there are some who raise the question of alternatives to statutory audit for SMEs as they hold the view that ISAs may not be appropriate for use for audits of SMEs. That is, they would challenge whether the current standards are sufficiently capable of application in a manner proportionate to the size and complexity of the entity; and suggest that a separate set of audit standards, or even alternatives to audit, should be considered that specifically cater to the needs of SMEs and their users. IFAC notes that there is work being done in several jurisdictions to examine the potential development of such alternatives.



In the spirit of innovation, IFAC does not discourage jurisdictions considering possible alternatives to audit—that is, other possible forms of assurance—but believes that any such alternatives should be clearly distinguished from an audit conducted in accordance with appropriate, high-quality auditing standards; ISAs.

16. How could the range of service offerings be adapted in order to meet current and future needs in the SME environment?

It is possible for local jurisdictions to consider developing other service offerings to meet the specific needs of their own environments, and to examine potential alternatives to a statutory audit. Importantly, however, IFAC is of the view that the development of such services should carefully consider, and to the extent possible draw upon and reflect, internationally accepted standards and principles. Also, as noted in the response to the last question, any such alternatives should be clearly distinguished from an audit conducted in accordance with appropriate, high-quality auditing standards; ISAs,

17. Is the profession too focused on financial information?

IFAC does not consider that the profession, as a whole, has been too focused on financial information. While the primary, traditional services provided by professional accountants—e.g., financial reporting, audit, taxation—have tended to focus on financial information, the profession has been heavily involved in many other initiatives that go well beyond financial information, most notably in relation to a range of management accounting, risk management, and internal control matters, and the development of integrated reporting.

18. Is there a market demand for assurance on narrative reporting in annual reports? Why (not)?

IFAC is of the view that the market demand for assurance varies by jurisdiction; and that specific research and empirical evidence is needed to determine these levels of market demand.

Furthermore, empirical evidence demonstrating the benefits and value of assurance would assist policy makers and others to consider how such market demand for assurance might be driven, especially in situations where market concerns and perceptions about information asymmetry are seen as being critical.

19. Will the market demand assurance on CSG, ESG and <IR> as this type of reporting becomes more widespread? Why (not)?

Refer response to question 18 above.

20. How can the profession help public sector entities achieve high-quality financial reporting?

IFAC supports the view that the quality and credibility of financial reporting is enhanced by audit.

More generally, IFAC believes that the profession can assist public sector entities to achieve high-quality financial reporting in a number of ways, by working more closely with governments, and :

- by speaking out on the topic and raising awareness of the importance of high-quality, accruals-based financial reporting by the public sector, with governments, credit providers, ratings agencies, and the public;
- through its continued support in setting high-quality internationally-accepted public sector financial reporting standards – i.e., International Public Sector Accounting Standards™;



- by developing the capacity of the profession to ensure that there are sufficient numbers of technically competent professionals to deliver high-quality financial reporting and auditing in the public sector; and
- by promoting the need for and establishing suitably focused education of relevant issues.

Question related to the conclusion

21. What additional points should be considered in this debate?

We offer no further comments about matters that should be considered in this debate.

Please do not hesitate to contact us should you wish to discuss how IFAC might be able to work with FEE to further discussion on the future of audit and assurance at an international level; as well as to clarify any of the matters raised in this letter.

Sincerely,

A handwritten signature in black ink, appearing to read 'Fayezul Choudhury', written over a light blue horizontal line.

Fayezul Choudhury
Chief Executive Officer