



Public Interest Oversight Board

2nd PIOB Public Interest Workshop: **PREPARING FOR THE NEXT GENERATION OF AUDITORS**



SUMMARY OF DISCUSSIONS

SESSION 1. TRENDS IN AUDIT

The “expectations gap” refers to the difference between the expectations of the general public on the audit and what the audit can actually deliver. Current trends affecting the audit may help narrow this gap in the future.

The development of IT systems (big data, data analytics) will increasingly reduce the routine aspects of the audit, enabling the auditor to focus more on issues that require professional judgement. The new auditor’s report, the introduction of the expected credit loss model (IFRS 9) and its impact on ISA 540 (Auditing accounting estimates, including Fair value accounting estimates and related disclosures), and the sustainability aspects of integrated reporting, all suggest a trend in which auditors may provide more assurance on forward-looking aspects affecting the financial statements.

Q1. *How are the challenges and opportunities above affecting the skills required from auditors and how will those skills be developed?*

Q2. *Is it important for financial stability that auditors give assurance on forward looking aspects of financial statements (e.g., going concern) that could help anticipate difficulties ahead?*

Q3. *Is positive assurance a tenable proposition given the increasing complexity of the audit, or is some form of negative assurance an alternative?*



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AUDITORS SKILLS

Participants agreed that auditor skills have evolved and further skills need to be developed. The current education model is outdated and no longer adequate. This applies both to the younger generations of auditors and current auditors. Emphasis was placed on developing data analytics skills, IT, valuation, risk assessment and auditor's critical thinking.

Skills need to specialize. Different skills are required in teams and not necessarily from each individual auditor. There should be different expertise within an audit team and there is a need to bring in outside experts into multidisciplinary teams. Also, there is a need for a different kind of audit partner, one who integrates, coordinates and communicates.

A point of general agreement was that auditors need to understand the client's business models to challenge management, their assumptions, changes in the business model, and to apply professional skepticism.

Technology may increase the expectations gap, on the expectation that audits could be performed on 100% of the data and would therefore be faultless. The credibility of data will become essential, as will the integrity of systems of internal control. Too much focus on developing data analytics skills over ethics and auditor behavior was highlighted as a risk. There is a need to educate users to avoid a new expectations gap.

FORWARD LOOKING ASPECTS OF FINANCIAL STATEMENTS

Forward looking information used in the determination of fair value, assessing the long-term viability of the business and the going concern status of an entity, are amongst the most important components of the financial statements. Audit already incorporates these forward looking aspects, but it was agreed that the audit could do more. Assurance on uncertainty is not possible, but assurance on the process of the audit of forward looking information can be better.

The need for assurance on forward looking aspects will grow, and with it one of the main elements in the expectations gap. Greater assurance on forward looking aspects would be beneficial for investors, and auditors would need additional legal protection.



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Despite efforts in communication, the expectations gap continues to grow. There was a general feeling that the expanded auditor's report would be a positive step. Financial education is important to help close the expectations gap: the reader of the financial statements needs to be educated to understand the context in which the entity is operating, the impact of the changing environment, the pace of change and how these changes impact the entity and its financial position.

Forward looking aspects do not only affect the auditor but the full financial reporting chain. Management has the primary responsibility to report on forward looking aspects of the company, and the auditor should provide assurance on managements' assumptions and assertions. The Audit Committee should also play its role. Management should be able to report about going concern and auditors should provide their independent judgement on this.

POSITIVE ASSURANCE

It is not in the Public interest to reduce the level of assurance.

There was agreement that anything less than a positive assurance will make auditing lose its value. How the auditor communicates positive assurance is very important given that this level of assurance is not a guarantee and should not be interpreted as such.

Big data and technological advances make positive assurance more probable, more tenable, and perhaps more defensible. However, professional judgement is still required and skills to use and mine the big data appropriately are essential. The auditor should understand and challenge the assumptions (professional skepticism) made by management.

The profession will need to deal with integrated reporting issues by providing different levels of assurance on different items.



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SESSION 2

2.A Auditor independence

In the current audit firms' business model, many firms report an increasing ratio of non-audit fees to audit fees, raising potential independence and audit quality concerns. Limiting the nature and relative amount of non-audit services provided to audit clients has been one approach to deal with independence concerns, as has the introduction of firm rotation in many jurisdictions.

Q4. *Does the current business model of audit firms affect the independence of auditors? If so, what are the effects on professional skepticism?*

Regulatory regimes dealing with non-audit services may vary across the world: from total prohibition of non-audit services to allowing to provide certain non-audit services to audit clients.

Participants felt that conflict of interests arise when audit firms provide non-audit services to audit clients. However, there were also views expressed against total separation and in support of multidisciplinary firms.

In addition to risks to the independence of the auditor, the risk of audit firms providing non-audit services is that audit quality and investment in audit quality may tend to diminish, given the lower profitability of audit in relation to other non-assurance services. On the other hand, views were expressed that audit-only firms will fail to acquire knowledge that may improve the ability of the firm to perform good quality audits, may face a loss of access to experts in areas related to the audit, and lose internal skill-development opportunities.

Audit firms need to be more transparent about their business model. There is a wide perception that the level of transparency of the firms is low. Better governance could be an important safeguard against the risks to independence of the current business model. Audit firms' "Transparency Reports" at the global level do not deal adequately with these issues. Better quality metrics and quality control measures would be welcomed. The question was asked whether the work of IFIAR could assist with this?

Some participants stated that audit firm rotation may have created competition on fees instead of competition on quality between firms. The Audit Committee should play its role in selecting the audit firm, yet many companies do not have audit committees.



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2.B Standard setting in the public interest

It is important that the public interest is taken into account in developing international standards. The PIOB has been given the task to monitor the respect of the public interest in the development of international standards on auditing, education and ethics. In fulfilling its tasks, the PIOB looks both at the substance of the standards and at the process for developing the standards (composition of the Boards, due process).

Q5. Do you believe that the standards developed by the IAASB, the IESBA and the IAESB take the public interest sufficiently into account? If not, what can or should be done to ensure that more attention is paid to public interest issues?

Q6. Do you believe that the PIOB is doing enough to ensure that the public interest is taken into account in the development of the standards? If not, what can or should be done to improve the present situation?

Q7. Do you believe that the present composition of the Boards is satisfactory from a public interest point of view? Should other stakeholders (e.g. investors) be included and how can this be done?

STANDARD SETTING BOARDS

Standard-setting in the public interest needs the right balance between due process, regulation, and oversight.

Participants highlighted that the three standard setting boards are different from each other, which makes it difficult to evaluate them together in the context of this question. Generally, the view was that the system is able to respond and reconcile different interests, notwithstanding the existing tensions.

There was a widely held view that SSBs take the public interest into account. The public interest is incorporated into the standard setting process –e.g.; selection of members; oversight of due process, role and make-up of the CAGs, range of people involved, efforts to consider all perspectives. Significant public interest input goes into the SSBs through Taskforces, the CAGs and the PIOB. The recent ITC is a good example of the openness of the IAASB.



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However, other views pointed out that comments from the PIOB and from regulators (supervisors) are not always taken into account. The large majority of the comment letters are coming from the profession or from audit firms, but listening to all stakeholders, including investors, is critical to respond to public interest concerns.

The public interest evolves continuously and so continuous review of the process is important.

There were suggestions that SSBs should act more strategically and devote more time to strategic standard setting and public interest matters instead of looking into details of the standard. Standards need to be timely and relevant, and that there is room for improvement.

CAGs have great potential to contribute but there are concerns about the effectiveness of SSBs in being able to deal with the wealth of CAG input, specially when the CAGs do not provide a consensus view.

There was some reservation about oversight – e.g., the absence of critical comments from PIOB Observer at IFAC Board meetings was cited as symptomatic of lack of robustness in oversight.

Concerns were expressed about the share of PIOB funding provided by IFAC. The PIOB budget was acknowledged to be the main challenge in the present system.

THE PIOB

The PIOB is seen to have a strong coordination role between the different constituents and to facilitate openness and good communication between stakeholders, which is key for the functioning of the standards setting system.

In general, the audience welcomed PIOB outreach efforts. Forums like the Public Interest Workshop are an effective mechanism for eliciting feedback and sharing points of view. There was encouragement to do more and to reach out for a broader audience.

In terms of PIOB input in the standard setting process, comments made by the PIOB are generally appreciated. Some participants suggested the PIOB should also participate (selectively) in Task Force meeting because that is the place where the scope and shape of the standard are discussed before full deliberation by the SSB itself. The PIOB should better monitor the public interest and the responsiveness to comments, specially from MG members.

There was a strong suggestion to improve PIOB communications in terms of describing what the PIOB does, how it approves Strategies and Work Programs, and standards, and how it takes part in the process. The PIOB Public Report could be improved. There was also a request to receiving PIOB comments during the meetings and not at the end of the process, and greater clarity on what the PIOB wants SSBs to evaluate in relation to public interest matters. The PIOB could also play a greater role in aligning the strategies of the SSBs.



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COMPOSITION OF THE BOARDS

Participants agreed that standard setting boards are made up of highly qualified members with a high level of knowledge of the audit profession. However, some suggestions were put forward to improve the current system.

The balance of members within the SSBs could be improved by bringing in past regulators, investors representatives or academics. There is under representation in the Boards from investors.

The different categories of membership may be misunderstood by the public. The current definitions should be clarified, specially that of Public Members. There is also a perception issue regarding IFAC financing volunteer public members, and in general, about dominance of the audit profession within the Boards.

There is under representation in the SSB from certain geographical regions. There is a perception of excessive influence of the Anglo-American perspective.

More outreach needs to be carried out in different countries.

The size of the SSBs could also be reviewed.