Audit Quality Indicators

Greg Jonas (Director of the Office of Research and Analysis, PCAOB) moderated a panel focused on identifying quantitative factors to assess audit quality, referred to as audit quality indicators ("AQIs"). The other panelists were Cindy Fornelli (Executive Director, Center for Audit Quality), Doug Niven (Senior Executive Leader for Financial Reporting and Audit, ASIC) and Mark Roth (Vice President/Business Management, Canada Pension Plan Investment Board). Mr. Jonas outlined the PCAOB's current approach, which seeks to identify approximately 15 indicators that will be useful to all stakeholders in assessing audit quality.

Ms. Fornelli presented the CAQ's approach to identification and implementation of AQIs, which also proposes AQIs but focuses on their communication to the company's audit committee. Doug Niven's presentation focused on audit quality within audit firm transparency reports, and stressed the need for transparency in such reports that will allow the user to understand how the auditor arrived at its assessments. ASIC has issued such guidance and he indicated that IOSCO would be publishing a document elaborating on this approach. Mark Roth, representing the investor point of view, did not endorse any specific indicators. He emphasized the need for an empirical system to evaluate audit quality that is consistent across sectors and markets and that includes, among other factors, transparency. He was also of the opinion that AQIs should serve investors as well as audit committees.

Discussion following the presentation included efforts undertaken by other IFIAR Members to gauge audit quality. IFIAR Members discussed their hope that AQIs will become a positive factor in audit firms competing on the basis of audit quality. It was agreed that this is only possible if there are solid AQIs that provide consistent results and allow comparison among the firms and, in many cases, among engagements. In addition, the discussion noted that AQIs would need some contextual explanation to be of use to consumers (e.g., audit committees and investors). For example, the number of hours spent by a partner on an engagement could be an indicator of quality due to sophisticated and experienced attention to the audit, or it could be an indicator of problems encountered requiring intervention. Therefore, this indicator would need to be understood in context. The indicators are not benchmarks, and no single indicator is determinative; they are designed to operate as a "balanced scorecard" to provide broad information about audit quality. Finally, it was agreed that, while AQIs may contribute to better audit quality, they may still be only a small factor in an investor's investment decision.

In summarizing the breakout session, Mr. Jonas observed gathering momentum behind the efforts of audit regulators to refine and use AQIs, if not always in precisely the same ways. This is part of a broader effort to identify and analyze key aspects of audit quality, providing additional insight for audit committees, investors, and others and, ultimately, to encourage firms to compete on the basis of quality.