



Rebuilding trust in a profession under pressure

The role of accounting and assurance research

July 2019

Presented by

Professor Roger Simnett

UNSW Sydney and CEO & Chair of AUASB



UNSW
SYDNEY



Australian Government
Auditing and Assurance Standards Board

Structure for Session

1. A profession under pressure:
Environmental scan
2. Trust deficit and role of accountants
and auditors
3. Evidence informed standard-setting
and implications
4. My research and lessons learned



UNSW
SYDNEY



Australian Government
Auditing and Assurance Standards Board

1: The International Audit Environment

Ministers seek to reassure staff as Carillion collapse sparks anger

◆ Public contracts underwritten ◆ No relief in private sector deals ◆ Heated MPs' q

GILL PLIMMER, JIM PICKARD AND MARTIN ARNOLD

The government scrambled yesterday to contain the fallout from the collapse of Carillion, one of its biggest contractors, reassuring employees working on hospital, school and military contracts they would continue to be paid.

But there was no such relief for workers on Carillion's purely private sector contracts. David Lidington, the Cabinet Office secretary handling the company's liquidation, said private companies employing Carillion would have only 48 hours of government support.

The move would "give time for private sector counterparties to Carillion, to decide whether they want to accept termination of those contracts, or them



Can auditors save their integrity?

Jun 10 2018 10:15 Makhosandile Kwaza

of vital public services, collapsed into liquidation early yesterday in one of the most dramatic corporate failures of recent years. A last-ditch rescue attempt failed to raise £500m needed to keep the company operating as it staggered under the weight of £900m in debt and a £587m pension deficit.

Mr Lidington faced angry questions from MPs in the Commons about the impact of the collapse. Carillion's recent relaxation of bonus conditions for executives and why ministers had continued to award the company contracts despite three recent profit warnings.

He insisted that there had been no "bailout" for the company, which employs 19,000 workers in the UK. He said its shareholders and lenders would bear the "brunt of the losses".

However, the government is underwriting the cost of Carillion's public sector contracts to ensure the continuation of "vital" services, even if the company's assets do not cover those costs. The



Most public services were unaffected but work on some sites halted

The key contracts

process is being managed by PwC, the accountancy firm.

Most public services appeared largely unaffected as 90 per cent of Carillion's services are subcontracted to smaller suppliers. But work on some of Carillion's construction sites came to a halt as subcontractors were told to go home last night. They included workers on £71m student housing development Manchester as well as the £355m Royal Liverpool hospital.

There were concerns that Carillion owed hundreds of subcontractors a smaller businesses millions of pounds raising fears that they could go bust.

Banks are also facing heavy losses their £2bn exposure in the form of loans and drawn credit facilities. The big hits will be taken by Royal Bank of Scotland, Lloyds Banking Group, Barclays and Santander UK.

Around 5,900 of the 27,500 members of Carillion's 13 UK pension schemes have been transferred to the industry



Auditing The Auditors

Recent audit failures are bringing new scrutiny to the dominance and business practices of the Big Four accounting firms.

JULY 17, 2018 | Author: CRAIG MELLOW



KPMG audits show 'unacceptable deterioration': UK regulator

UK's Financial Reporting Council has said that KPMG, one of the 'Big Four' accounting firms, has

IRBA issues notice of transparency reporting for audit firms

The National Audit Environment

ASIC review uncovers more corporate accounting problems

PwC accused of inflating Vocation's revenue before its collapse

Poor work risks new Enron: Medcraft

Regulation ASIC chief says inspections have found appalling results.

Stressed Auditors
The quality of Australian corporate audits is appalling and getting worse, potentially leading to an Enron-style corporate collapse, according to corporate regulator Greg McDermott. As a result, government intervention in the audit market – assigning auditors to jobs and setting the fees they can

Double check
Key audit areas where the firm did not obtain reasonable assurance: the financial report was free of material misstatement (%)

Year ended	16 months to 30 June 2017	16 months to 30 June 2016
Largest four national firms	21%	18%
Other national network firms	20%	15%
Smaller firms	24%	42%

SOURCE: ASIC

audits was dangerous to the entire financial system, with creditors, investors and regulators all having to rely on information in financial statements. The audit business “should stand on its own and it should be high quality and be paid enough to attract high calibre people,” he said.

Big four hit back at regulator

The big four accounting firms have defended the quality of their audit work and highlighted their use of new technology in assessing financial statements. In response to criticism by corporate regulator Greg McDermott, the firms said they were focused on delivering high-quality audit services and that it was also the responsibility of the corporate regulator and companies to work with them to improve standards. “That’s how a relationship between audit

analytics tools, and digital platforms and will increasingly take in artificial intelligence,” Mr Yates said. He added that ASIC’s audit inspection program “continues to play an important role in identifying areas of good practice in our work and, crucially, areas where we can continue to improve further.” Mike Wright, of EY, said his firm was committed to delivering high quality audits, adding “the responsibility for financial statements rests with companies, regulators,”

Revealed: EY's multiple 'independent' roles at ANZ

✉ G+ f t in

RCR directors, auditors could face lawsuits after collapse

Jenny Wiggins
RCR Tomlinson’s board directors and auditors Deloitte may be sued by angry investors determined to recover losses following the Perth-based engineering group’s administration, which occurred less than three months after it raised \$100 million in equity. Lawyers told *The Australian Financial Review* they were considering suing RCR’s former board and auditors directly after the engineering group went into administration on Thursday.

RCR’s financial accounts were audited by its longstanding auditors Deloitte, which was paid \$738,165 in 2017-18. Deloitte, which has been RCR’s external auditor since 2010, was also named the “independent auditor” for the capital raising that was announced on August 28 – the same day as RCR released its annual financial report. Deloitte’s subsidiary, Deloitte Corporate Finance, was paid an additional \$125,000 to be RCR’s “investigating accountant” for the capital raising and

Deloitte said it attended RCR project review meetings and examined “a sample” of contracts to challenge the company’s forecast costs of completion. Deloitte did not raise specific questions about RCR cashflows but noted in the company’s 2017-18 annual report that there was “a material uncertainty” over its ability to continue as a “a going concern” if its capital raising was not successful or if the company could not retain the “ongoing support” of its banks. RCR collapsed after it ran out of cash

material uncertainty existed that may cast significant doubt on the group’s ability to continue as a going concern,” the spokesman said.

I’d expect ASIC to throw the book at them all.
Simon Mawhinney, MD of Allan Gray, which holds a 7.8 per cent stake in RCR

RCR’s board, which was chaired by Roderick Brown, had five directors when the company went into administration. Mr Brown did not respond to a request for comment. RCR was still teeing up new contracts during the capital raising. The company said on October 11 that it had signed an interim project alliance agreement with New Zealand’s City Rail Link, Auckland’s biggest transport project, to provide track and signalling services. City Rail Link chief executive Sean

PwC wants ASIC audit quality report to name individual firms

them all,” said Simon Mawhinney, managing director of Allan Gray, which holds a 7.8 per cent stake in RCR. ASIC declined to comment.

blowouts on its Hayman and Daydream solar projects in Queensland, as well as how the company recognised revenue from contracts and collected debts.

audited accounts prepared by Deloitte and lodged with the Australian Securities Exchange in August, the independent audit opinion indicated that a

take on dual roles at companies risk running into conflicts of interest because they may be unwilling to damage lucrative client relationships.

Auckland-based group believed the engineering group’s problems were confined to the one Queensland **Continued p16**

Audit environment

A profession under pressure

- General international view is of a profession under pressure
 - possible exception being the US:
why? SOX? Education? Competition?
- Professional firms audit revenue percentage now around 15-20%;
- Greater pressure, especially in UK, to create “audit-only firms” and “joint audits” to deal with independence and competition issues;
- Recruitment, margin erosion and regulatory review overload challenges increasing.



Audit environment

Increased regulator involvement



- Monitoring Group restructure of international standard-setting;



- Australia following closely the UK debate - impact of Haynes/Banking Royal Commission;



- High-profile activity in UK
 - 4 Commissions/parliamentary enquiries;



- Regulators are now more litigious
 - name & shame and “why not litigate? approach”

Audit environment

A profession under pressure

Audit quality and reporting quality debate should be **multidimensional**.

- Debate in press driven to date by “**inspection results**”. One element
- Audit firms becoming **more proactive** in debate
- Auditing and audit quality an issue **across all sectors**

Trust deficit

- Do we have the right products and right processes?

Structure for Session

1. A profession under pressure:
Environmental scan
2. **Trust deficit and role of accountants
and auditors**
3. Evidence informed standard-setting
and implications
4. My research and lessons learned



UNSW
SYDNEY



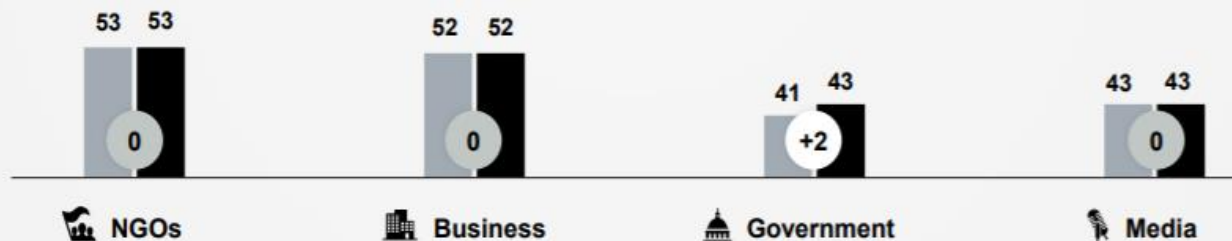
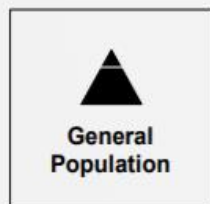
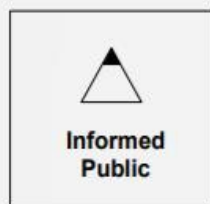
Australian Government
Auditing and Assurance Standards Board

The Trust Deficit Globally

No Global Recovery in Trust

Percent trust in each institution, and change from 2017 to 2018

■ 2017 ■ 2018
● 0 ● + Y-to-Y Change



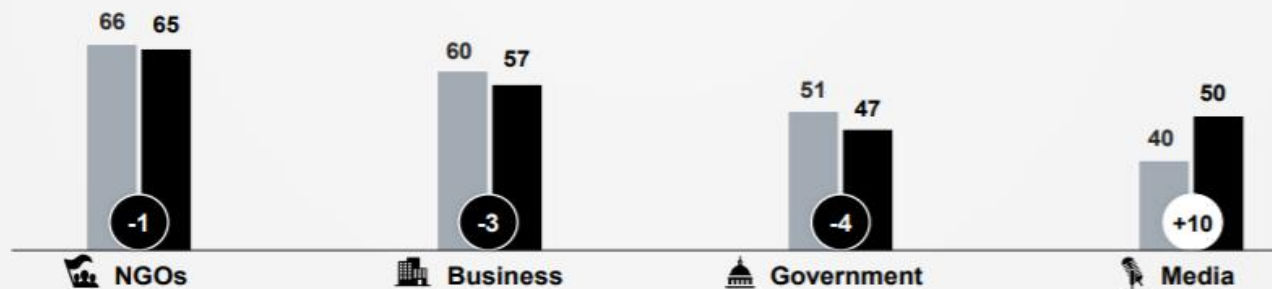
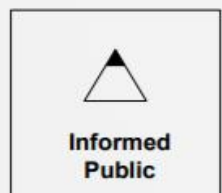
Source: 2018 Edelman Trust Barometer. TRU_INS. Below is a list of institutions. For each one, please indicate how much you trust that institution to do what is right using a nine-point scale, where one means that you "do not trust them at all" and nine means that you "trust them a great deal." (Top 4 Box, Trust) Informed Public and General Population, 28-country global total.

The Trust Deficit in Australia

Trust Declines Among General Population

Percent trust in each institution, and change from 2017 to 2018, in Australia

■ 2017 ■ 2018
- 0 + Y-to-Y Change



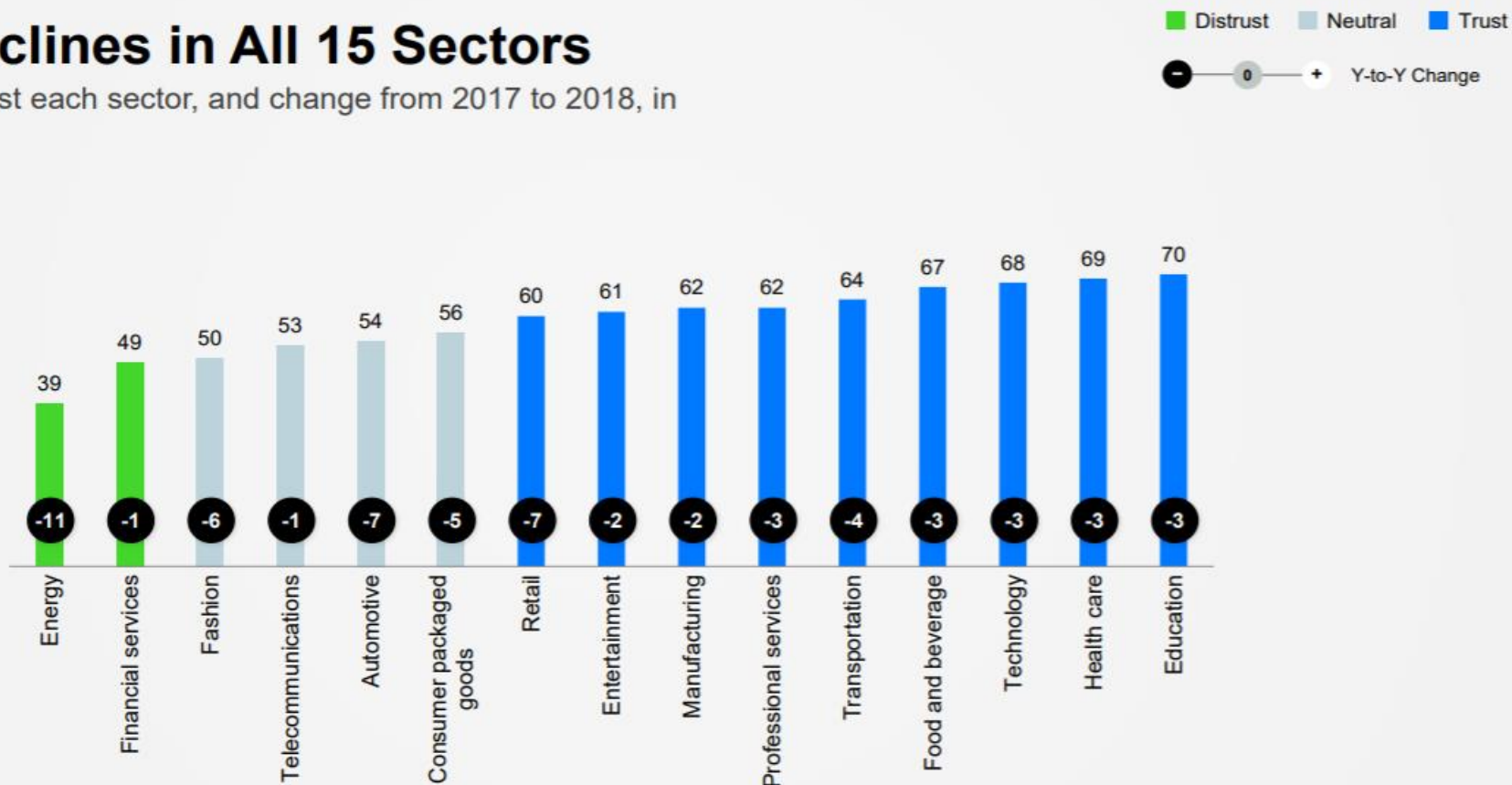
Source: 2018 Edelman Trust Barometer. TRU_INS. Below is a list of institutions. For each one, please indicate how much you trust that institution to do what is right using a nine-point scale, where one means that you "do not trust them at all" and nine means that you "trust them a great deal." (Top 4 Box, Trust) Informed Public and General Population, Australia.



The Trust Deficit in Australia

Trust Declines in All 15 Sectors

Percent who trust each sector, and change from 2017 to 2018, in Australia



Source: 2018 Edelman Trust Barometer. TRU_IND. Please indicate how much you trust businesses in each of the following industries to do what is right. Again, please use the same 9-point scale where one means that you "do not trust them at all" and nine means that you "trust them a great deal". (Top 4 Box, Trust), industries shown to half of the sample. General Population, Australia.



Responding to the Trust Deficit

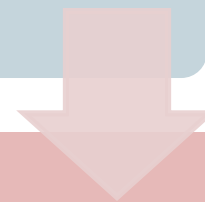
Stage 1: Performance

Organisations doing the right thing



Stage 2: Communication

Organisations communicating this doing
to stakeholders (Reporting including EER)

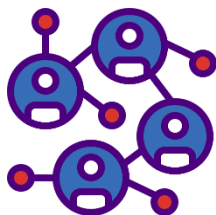


Stage 3: Credibility

Do we believe this communication?

Stage 1: Organisations doing the right thing

Trust Research



- Trust research at this individual and organisational level is spread over many disciplines.



- Accounting and Finance researchers can and do play a role, but not necessarily a natural advantage

Stage 2: Organisations communicating trust building activities to stakeholders (Reporting including EER)

Only way to rebuild trust is to communicate these activities.

Increased accountabilities

- Principal organisational communication device is traditionally the **annual report**
- Emphasis to-date has been within the **financial statement section** of the annual report, but increased accountabilities reflected in other information in annual report
- Other public reports such as **CSR, ESG, GhG and <IR>**

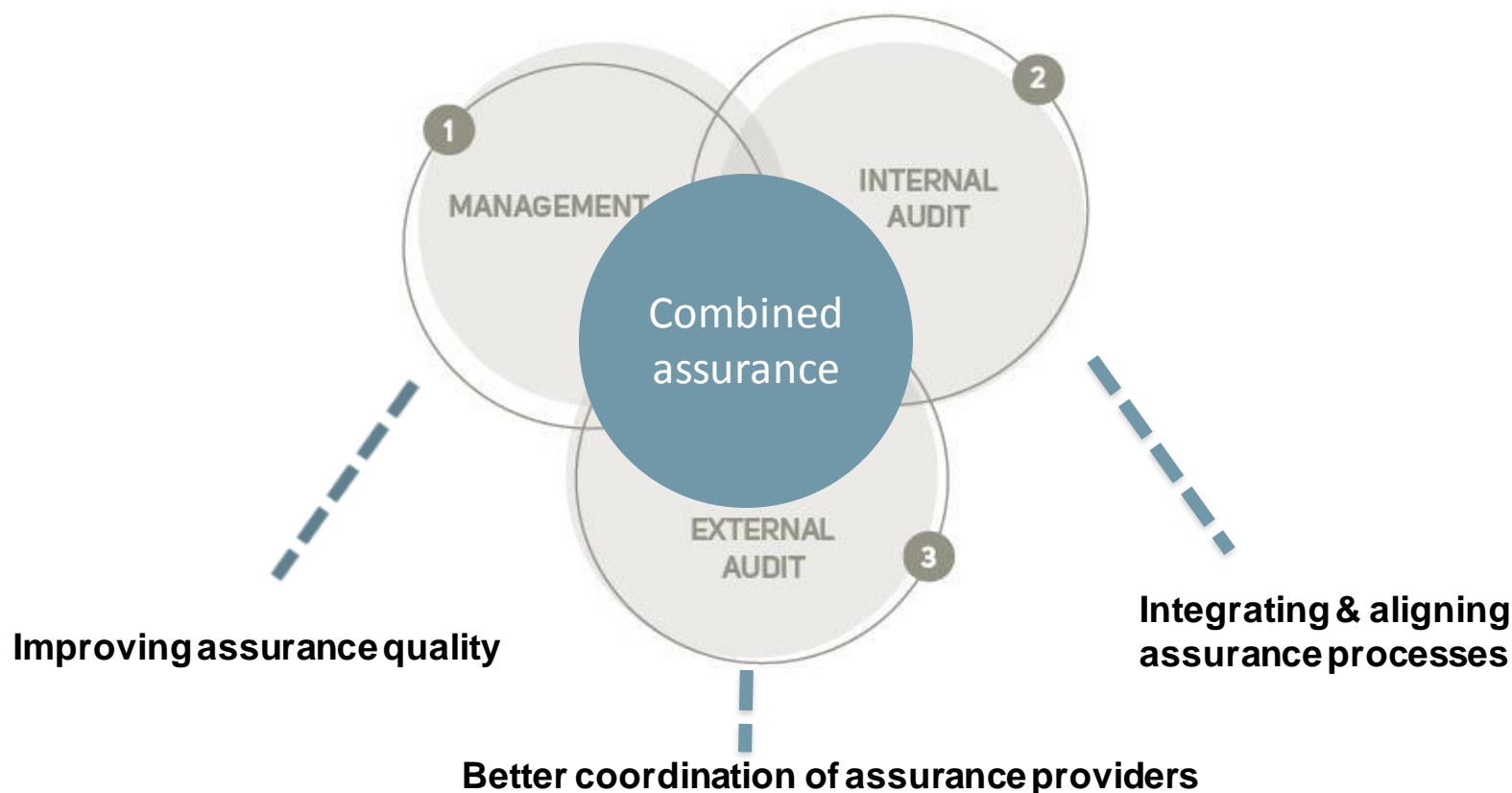
Stage 3: Do we believe the communication (credibility)

In annual report	Outside annual report
Revised auditing standards requires the auditor to “read and consider the other information”	About 60% of sustainability information assured, and about 60% assured by accounting profession

- Information benefits the **decision making of report users**
- Without credibility, corporate reports are potentially perceived as marketing documents and a part of greenwashing practice

Other credibility enhancing mechanisms: Combined assurance

South Africa market - King III Report recommends combined assurance



Structure for Session

1. A profession under pressure:
Environmental scan
2. Trust deficit and role of accountants
and auditors
3. **Evidence informed standard-setting
and implications**
4. My research and lessons learned



UNSW
SYDNEY



Australian Government
Auditing and Assurance Standards Board

Trends in policy making

- The use of evidence through economic analysis or appropriate theoretical lens in policy making is on the rise.
- Accounting and auditing are no exception.
- Using sound theory and robust empirical evidence should lead to better policies and regulations.
- Despite its obvious appeal and substantial promise, evidence-based policymaking is easier demanded than done.

The Opportunity for Academics

Need for evidence-informed standard-setting
and policy making



Academics in a unique position to play a leading role:

- Independent.
- Expert at devising appropriate research questions, research design and analysis.



All **other parties** have vested interest, or lack the expertise.

Impactful research in Australia



Australian Government
Australian Research Council

Engagement and Impact (EI) exercise

- Research receives substantial amounts of public funding

- Researcher have little formal evidence on their EI contributions.

- In December 2015, the Australian Government announced development of a national EI assessment

- How are universities translating academic research into economic, social and other benefits

Where are the research opportunities?



Australian Government

Auditing and Assurance Standards Board

1

AUASB and IAASB Evidence-Informed Standard-Setting Strategy (EISS)

2

Impact of research on our contemplations

3

Working with the AUASB

Regulators push for evidence Informed Standard-Setting Strategy



Australian Government

Auditing and Assurance Standards Board



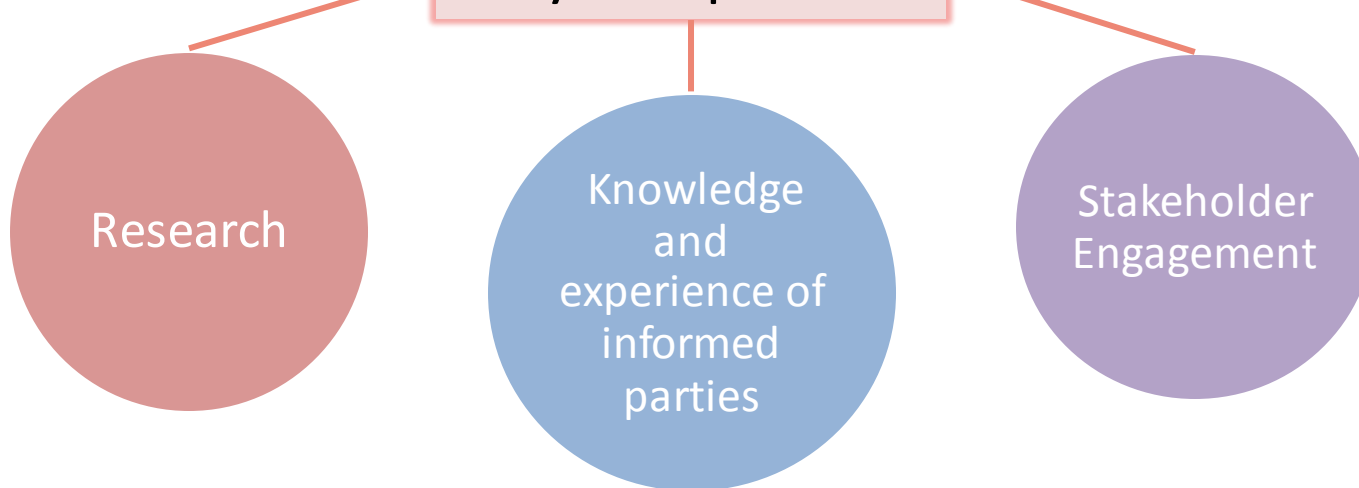
- Big push to ensure AUASB have evidence informed decision-making at Board level (basis for comment).
- Evidence informed standard setting strategy recently approved by AUASB
- IAASB is planning to have a defined research stage before project approval. Is a no-brainer.
- How does it effect academics? For each IAASB project, can we get an academic team together to synthesise the relevant research?

AUASB Evidence Informed Standard-Setting Strategy

Objectives

1. Ensures the AUASB has a robust and transparent evidence gathering process
2. Encourages formalising collaboration with academics

Key components



AUASB response to Trust Issues

Early this year ASIC reported 24% of key audit areas firms had not obtained "reasonable assurance" (down from 25% at last inspection)

The AUASB has been a key part of a profession-wide response to regulator concerns, supporting the local oversight body (FRC) through:

Broaden discussion

- Surveys of Audit Committee Chairs and Investor Groups on their perceptions of Audit Quality

Learn from results

- Separate dialogue with regulator and firms to identify common areas where additional guidance or revision is required

Knowledge sharing

- Improve transparency and knowledge sharing with local regulator on Audit Quality Inspection process and outcomes

Addressing Fundamental Elements of the Audit

High-Quality Audits
in a Changing Business Environment -
Influenced by Technology, Complexity,
and Demands for Continued Relevance

Quality
Control at the
Engagement
Level (ISA 220)

Risk
Identification
and
Assessment
(ISA 315)

Auditing
Accounting
Estimations,
Including Fair
Values (ISA
540)

Group Audits
(ISA 600)

Strengthening the Application of Professional Skepticism

Enhancing Firm's System of Quality Management (ISQM 1, ISQM 2)

Other AUASB Developments

- 1 Continuing activities to support Auditor Reporting Initiative
- 2 Additional focus on public sector auditing and assurance issues (e.g. Performance Engagement Standard, Compliance Engagement Standard)
- 3 Support opportunities to drive Extended External Reporting both locally and globally
- 4 Mapping of the challenges with the auditing standards associated with Data Analytics and the use of technology on audits
- 5 Evaluation of options to improve guidance for Small / Medium Practices/Entities
- 6 Other strategic projects supporting local implementation challenges – e.g. Reporting Frameworks; Charities/NFPs.

How well do we inform policy?

Review Of International Archival Audit Research



Article:

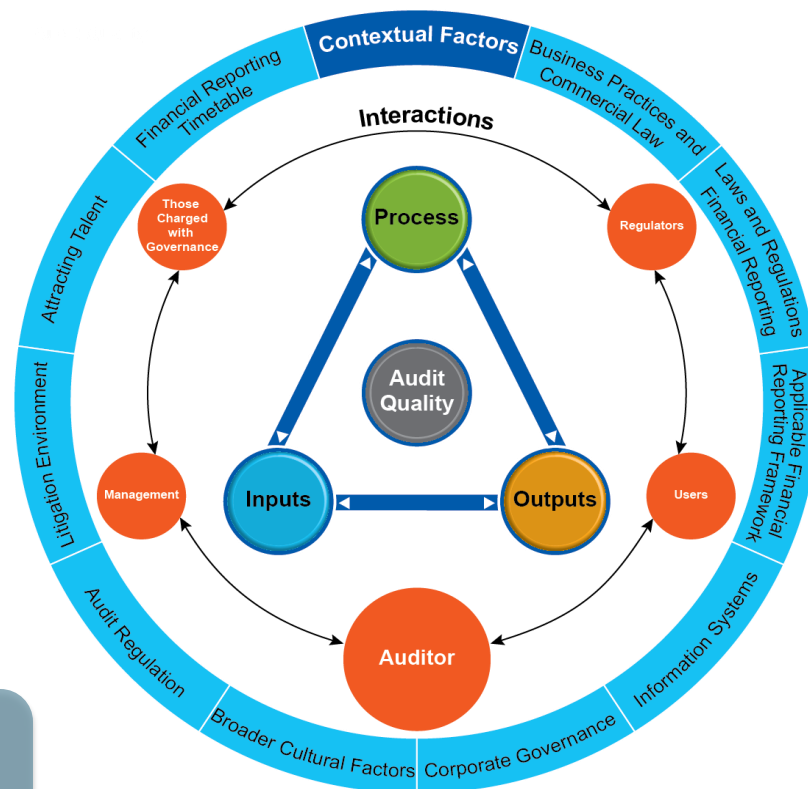
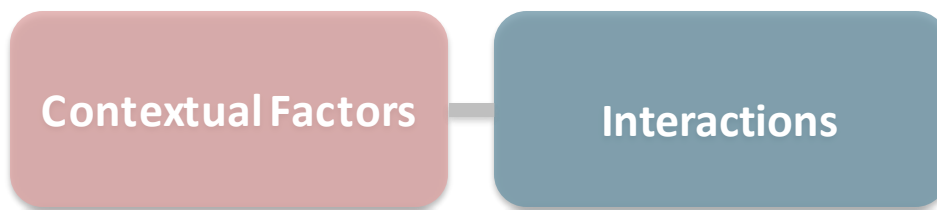
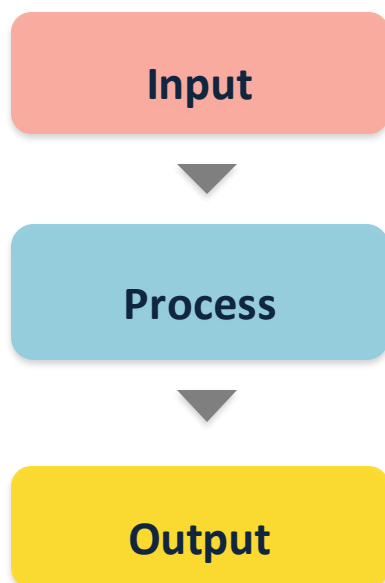
- Simnett, Carson & Vanstraelen (AJPT, 2016)

Sample

- 130 international archival auditing and assurance research articles published
 - from 1995-2014
 - in 8 leading accounting and auditing journals: *AOS, AJPT, CAR, JAE, JAPP, JAR, RAST, TAR.*

IAASB Framework for Audit Quality 2014

Key Elements



Some major findings

1

Very little international research is explicitly linked to standards or framework, or is aimed at informing standard-setters and regulators

2

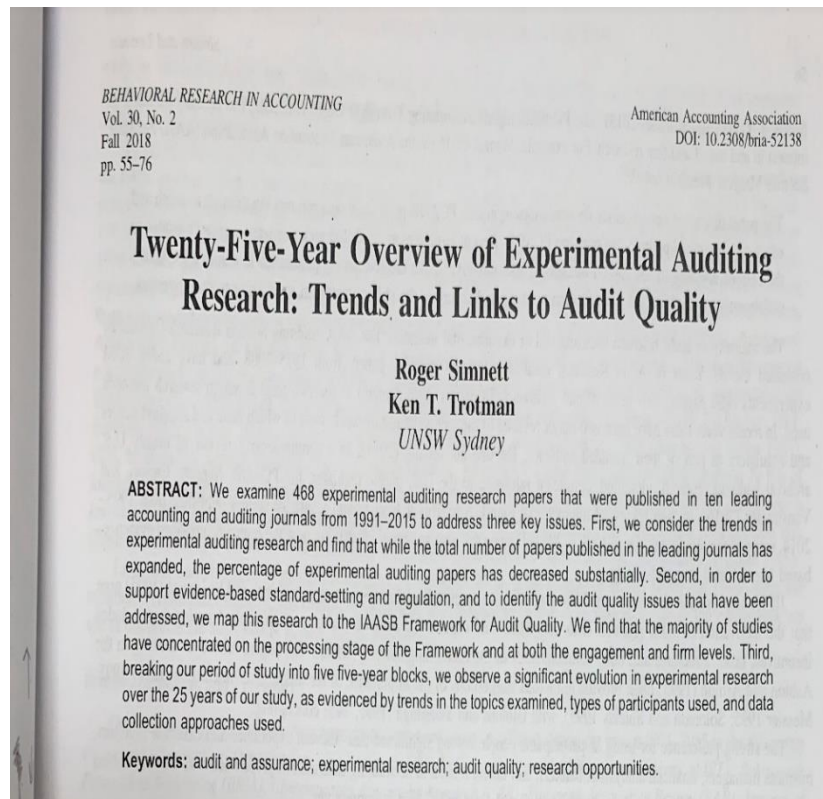
There is comparatively a small amount of international archival research compared with US-oriented research (at least published in leading journals).

3

Trend in archival is away from theory to interesting research question, and emphasising strength of causal relationship.

How well do we inform policy?

Review Of International Behavioral Audit Research



Article:

- Simnett & Trotman (BRIA, 2018)

Sample

- 468 international archival auditing and assurance research articles published
 - from 1991-2015
 - in 10 leading accounting and auditing journals: *AOS, AJPT, BRIA, CAR, EAR, JAE, JAPP, JAR, RAST, TAR.*

Some major findings

1

Much higher proportion of international research published and is explicitly linked to standards or framework, mainly at process stage.

2

There is a trend away from experienced auditors and controlled experiments to students and uncontrolled experiments.

3

Trend in behavioural is to theoretical contribution, incremental contribution, and multiple experiments.

EISS – Lessons from trends for auditing

Learnings for academics

- Complimentary research methods
- Very little international research publishes in leading journals; less cross-border research.
- Researchers have not clearly articulated why the research is of interest to the audit firms, standard-setters, and regulators. These are our natural domain of influence:
 - Very few studies refer to auditing standards and regulation.
 - Most of those that do refer to this work in motivation, not in method, results or conclusion.
 - Implications are very generic rather than specific.

Structure for Session

1. A profession under pressure:
Environmental scan
2. Trust deficit and role of accountant
and auditors
3. Evidence informed standard-setting
and implications
4. **My research and lessons learned**



UNSW
SYDNEY



Australian Government
Auditing and Assurance Standards Board

My current research agenda

1

Group audit research. Australian data informing ISA 600 and PCAOB

2

International data aimed at benefits and costs of inspections

3

Benefits of providing NAS, especially assurance of EER reports

4

Audit quality of Australian charities

5

Assuring <IR> and “other information”

Lessons learned from my experiences

Policy making research is difficult but beneficial

International policy related research is very difficult

Archival research with Australian/International data is difficult to publish in A* US journals. Behavioural research easier.

Trend in archival is away from theory to interesting research question, and emphasising strength of causal relationship. Trend in behavioral is to theoretical contribution, incremental contribution, and multiple experiments

The divide between practitioners and researchers in accounting is one of the largest of all the professions (social science much more removed compared with STEM)

There are few practitioners who understand our research, and the numbers have been getting fewer (is the trend reversing)?

Steps to support

1. Reconsider academic incentive systems

How do we
measure and
reward
impact?

Bias in publication
towards results,
even results which
are outliers

Recognise that
replication research
**builds a body of
knowledge:** incremental
contribution on every
study lessens
transparency.

2. Support for researchers

Regulators, standard-setters and key players in accounting and auditing can play a key role in helping **create a research infrastructure to inform policy making, and rewarding researchers for impact**

Accounting in 2036: A learned profession.

Barth M. 2019, *The Accounting Review*

“My vision is that by 2036 accounting is known as the learned profession that provides information for informed decision-making to support a prosperous society.

To achieve this vision, academics need to:

- 1) conduct fundamental and applied research;
- 2) communicate research insights outside of academia;
- 3) interact with practicing accountants and others who use accounting information, such as managers, capital providers, regulators, and government officials; and ensure that everyone understands that academic accountants are responsible for the “learned” part of accounting as a learned profession.”