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
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
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’ questions

KPMG audits show 'unacceptable deterioration': UK regulator

UK’s Financial Reporting Council has said that KPMG, one of the ‘Big Four’ accounting firms, has...
The National Audit Environment

ASIC review uncovers more corporate accounting problems

PwC accused of inflating Vocation's revenue before its collapse

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

RCR directors, auditors could face lawsuits after collapse

PwC wants ASIC audit quality report to name individual firms
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
  o 4 Commissions/parliamentary enquiries;

• Regulators are now more litigious
  o 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
No Global Recovery in Trust
Percent trust in each institution, and change from 2017 to 2018

Source: 2018 Edelman Trust Barometer. TRU JNS. 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

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)

<table>
<thead>
<tr>
<th>In annual report</th>
<th>Outside annual report</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revised auditing standards requires the auditor to “read and consider the other information”</td>
<td>About 60% of sustainability information assured, and about 60% assured by accounting profession</td>
</tr>
</tbody>
</table>

- 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

- Improving assurance quality
- Better coordination of assurance providers
- Integrating & aligning assurance 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
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**

- 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?

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

• 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?
Why take impactful Research?

Archival Research

Behavioural Research

EISS Implications

---

**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**

- Research
- Knowledge and experience of informed parties
- Stakeholder Engagement

---

AUASB Evidence Informed Standard-Setting Strategy

UNSW SYDNEY

Australian Government Auditing and Assurance Standards Board
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

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

Input

Process

Output

Contextual Factors

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

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

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
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.
“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.”