Audit Quality Indicators: In Search of the Right Measures

The Issue

Audit quality can be challenging to define, measure and quantify. This may be especially true for audit committees not involved in the daily audit process.

Around the world we are seeing the rise of audit quality projects, including Audit Quality Frameworks developed by the Financial Reporting Council (FRC) (UK) and the International Auditing and Assurance Standards Board (IAASB). The Public Company Accounting Oversight Board (PCAOB) and the Center for Audit Quality (CAQ) in the United States are also active in the area of audit quality indicators (AQIs). The CAQ released CAQ Approach to Audit Quality Indicators in April 2014 and has started pilot testing their proposed approach.

The PCAOB plans to issue a concept release in 2014 on this subject (additional details on the current project can be found here). The objective is to develop a portfolio of quantitative measures that provides insight into audit quality that an audit firm could share publicly or with audit committees and facilitates dialogue on the drivers of audit quality.

Why does this matter?

Combined, these initiatives will increase the conversation about audit quality matters and support key activities to enhance audit quality, including:

- Supporting audit committees in their oversight and evaluation of the auditor
- Audit committees annually assess the auditor. A number of audit committees in Canada have also completed or are planning to complete periodic comprehensive reviews. A series of audit quality indicators could further assist the audit committee in these reviews.

- Providing a way for audit firms to show their commitment to audit quality and facilitating competition among audit firms that is based on audit quality
- Competition for audit business is increasingly being evaluated primarily on price. We believe audit quality indicators would assist audit firms to quantify their commitment to and performance regarding audit quality. This could promote competition among auditors based on audit quality, allowing auditors to win, retain and be compensated for their work based on the quality of what they do, rather than purely on price.

Potential audit quality indicators

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<tr>
<th>Audit Firm Level AQIs</th>
<th>Engagement Level AQIs</th>
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<tbody>
<tr>
<td>Partner workload</td>
<td>Years of experience of partners and key audit team members</td>
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<tr>
<td>Partner to staff leverage</td>
<td>Years of industry experience of partners and staff</td>
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<tr>
<td>Training hours per professional (average)</td>
<td>Specialist hours (e.g. IT, valuations, tax) on the engagement</td>
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<tr>
<td>Technical resources per professional</td>
<td>Key engagement team workloads including hours of overtime during peak periods</td>
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What should be shared and with whom?

- **What information should be shared (audit firm level or at the engagement level)?**
  Consistent and sustainable audit quality depends on the contributions of professionals throughout an audit firm. A combination of firm-wide and engagement level measures could provide users with a balanced view of the factors impacting audit quality and places engagement level measures in context.

- **Should firm level audit quality indicators be shared publicly or just with the audit committee?**
  We believe there is a benefit to sharing firm level indicators publicly to improve the visibility of key measures and improve the dialogue on audit quality. To protect confidentiality of key information we understand it may be more appropriate to discuss engagement level information with the audit committee only.

**Did You Know?**

The Federal Audit Oversight Authority in Switzerland (FAOA) annually publishes a range of audit quality measures for the five largest state-regulated audit firms.

Did You Know?

PricewaterhouseCoopers in the United States publishes an annual audit quality report. The 2013 report included measures such as average annual hours worked over 40 hours and the ratio of technical support partners to total audit partners.

**Final Word**

CPAB encourages audit firms to increase the transparency of audit quality measures and recommends audit committees initiate this dialogue with their auditor.

We believe developing a portfolio of measures that an audit firm can share publicly and/or with audit committees is a good step toward increasing the dialogue on audit quality and can support audit committees in their oversight of the auditor. Additional information on audit quality indicators can improve the balance between quality versus price when audit committees select their auditor.

**Learn more**

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