Center for Audit Quality Update

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Thank you.

I will echo Bill in saying that I am very much looking forward to the insights that will be shared at this conference. I also want to congratulate Barry and Bill and the entire AICPA staff for the “Feed the Pig” financial literacy campaign, which recently won the Ad Council’s top creative award of the year. It is a fantastic campaign and it’s great to see it being recognized.

I’m pleased to have the chance to contribute to the discussion with an update on the Center for Audit Quality and our policy work.

To frame my policy discussion, let me begin at a more fundamental level and focus on the underlying strength of our profession. As we all know, a strong profession is critical to protecting investors.

A strong profession. It reminds me of an advertisement I saw recently for the Chevy Silverado pickup truck. You may have seen this one too—it’s been watched close to a million times on YouTube. Let’s watch a snippet.

- He’s strong  
- He’ll pick you up and won’t let you down  
- Rock solid inside out  
- Somebody you can trust  
- Steady as the sun  
- Ain’t nothing gonna knock him off the road he’s rollin’ on  

Now, this ad clearly pulls on a number of heartstrings. One is fatherhood, and, as the daughter of a steelworker, it sure reminded me of my dad.
The ad also speaks to pride in work and a job well done. As we all know, that is not something unique to steelworkers and farmers.

I think you can find a lot of that kind of pride right here among the men and women at this conference.

Because, as has been true since the industrial revolution, the accounting and auditing profession is strong, and we should be proud of that strength.

That strength is demonstrated by third-party research and metrics on investor confidence, as I’ll discuss now.

Simply put, public company auditing is in very good shape in the United States. An analysis of financial reporting trends released last March by Audit Analytics found that the total number of financial restatements has leveled off over the last few years.

The average number of issues per restatement has fallen to a 12-year low. The severity of restatements continues to decline, and restatements are being filed more quickly after a misstatement is disclosed.

I attribute these improvements to the combined efforts of auditors, issuers, audit committees, the PCAOB, the SEC, FASB, and others. We’re all in this together, and we all have the same goal—quality financial reporting, which of course is important for investor confidence.

The improvements that I’ve mentioned are reflected in robust investor confidence in public company auditors. As you all may recall, since 2007, the CAQ has commissioned an annual survey of investors on four key confidence measures pertaining to capital markets. We call this our Main Street Investor Survey, as it targets retail investors exclusively.

Since 2011, we’ve asked participants in this survey how much confidence they have in a number of different entities when it comes to effectiveness in looking out for investor interests.

As in past years, investors express the most confidence in independent auditors.

Just as the song in that Chevy ad says: “Somebody you can trust.”

This strength of trust, of course, doesn’t happen overnight or without commitment and focus. No, it is carefully built through high quality auditing practices and sustained efforts on the part of the profession to strengthen trust. This sustained commitment—the “continuous cycle of improvement”—is a critical component of the profession’s focus on enhancing audit quality. So let’s look further at how the public company auditing profession is strong—and getting stronger.

First, we’re communicating better than ever with investors. In a moment, I’ll discuss this further in the context of our collaborative efforts on transparency.

Next, the public company auditing profession shows its strength in its ability to attract and invest in talent. In fact, the accounting and auditing profession is a major job creator. I won’t repeat the statistics that Bill cited but we are seeing very positive trends. After all, the profession’s greatest asset is its people. And we know that firms and companies spend tremendous resources on continuing education. At all levels, training is a critical component of developing the skills of professionals conducting audits.

In addition to human resources, we are building our intellectual capital in our efforts to continuously improve. From the vantage point of the CAQ, I’ll mention but two.
One is our focus on better managing and anticipating risks. The CAQ and its member firms are undertaking an initiative to compile and analyze issues and trends identified from inspections and assessments of internal quality controls processes. The goal of this effort is to help summarize potential areas of risk and communicate this information to our member firms so they can address the risks in a proactive, accelerated manner.

This approach will not only be useful in identifying trends for firms being inspected annually—it will also help firms that are not subject to annual inspections become informed of the issues that are identified. We are looking to issue this alert in the next week or two, in time for the 2013 audit cycle.

Another example is the development of the Judgment Framework Resource. The aim of this resource is to provide auditors with a practical decision-making process—guidance for auditors in developing, substantiating, and documenting important judgments made during the course of an audit.

Throughout this year, the CAQ has led an effort involving extensive research and input from our members in the development of the Judgment Framework Resource. Publication of the tool is set for the first half of next year.

Here’s another way public company auditors show strength. We are working together more closely than ever with our partners in the fight against financial reporting fraud.

Three years ago, the key players in the financial reporting supply chain came together to form the Anti-Fraud Collaboration. The groups involved represent those with primary responsibility for deterring and detecting financial reporting fraud: Financial Executives International, The Institute of Internal Auditors, the National Association of Corporate Directors, and the CAQ.

Since forming, the Collaboration has developed a range of educational programs, videos, and case studies, all of which you can find at its website: AntiFraudCollaboration.org or at the CAQ’s website. All of these resources are publicly available and free of charge.

One teaching and training tool, the “Hollate Manufacturing,” case study was released last March. So far, over 140 individuals have been trained to teach this case study, created with the help of the Harvard Business School. We know that universities are using it in the classroom and firms are using it for training. In fact, the case was used in a recent competition of the best and brightest university students in the state of Georgia.

If you’re interested in using the case study for training or teaching, there is a companion teaching guide to assist in that effort. There also is a video giving practical tips on how to teach the case. And, a second case study in the works, set for release early next year.

These and our other anti-fraud efforts, complement the work being done by policymakers, such as the renewed focus on financial fraud at the SEC and the creation of its Financial Reporting and Audit Task Force. In addition, the PCAOB’s Standing Advisory Group has also recommended that the PCAOB create a Fraud Task Force.

Besides fighting fraud, we are showing strength in our work to enhance transparency.

In 2012, the CAQ joined with the Association of Audit Committee Members, Corporate Board Member, the Directors’ Roundtable, National Association of Corporate Directors, and Tapestry Networks and others. This Collaboration formed in recognition of the critically important role the audit committee has with respect to quality audits and quality financial reporting.
Last year, the Audit Committee Collaboration released an assessment tool to help audit committees evaluate the external auditor. More recently, the Collaboration issued a *Call to Action*, which encourages audit committees to increase the effectiveness of their disclosures ahead of the 2014 proxy season.

The *Call to Action* does not require audit committees to take on additional responsibilities, but simply provides insights to investors and others about the important work they are already doing. Ultimately, it is the quality of information made publicly available to investors that forms the foundation for confidence in the U.S. capital markets system and allows for the efficient and effective allocation of capital by investors.

The best practices highlighted in the *Call to Action* are not prescriptive, or part of any mandate. Rather they are intended to provide a clear path of action that other audit committees can follow to strengthen their own disclosures.

We hope the *Call to Action* will stimulate a broad conversation around the effectiveness and the important work of public company audit committees, especially in light of more comprehensive disclosure efforts recently announced by SEC Chairwoman Mary Jo White and Commissioner Gallagher.

The desire to strengthen transparency is also a driving force behind one of the most prominent policy challenges facing the public company auditing profession: identifying specific “audit quality indicators” (AQI).

This effort, of course, goes to the core of the Center for Audit Quality’s mission. It’s also a vital one for investors and for policymakers. The CAQ has been working in this area for some time. We have already provided perspectives to the PCAOB, which announced its plans to pursue a project to define key elements of audit quality last May.

We will offer more developed recommendations on this important work going forward. As a profession, we believe a communication of audit quality should do several things.

First, it should be the starting point for a meaningful dialogue with the audit committee on key metrics and which of them are most important to the audit committee.

Second, it should focus on engagement-level metrics with relevant firm or industry information, as needed to provide context.

Third, it should recognize the audit committee’s oversight role.

Fourth, it should incorporate compliance with input- and output-based regulations and professional standards, as well as consideration of the audit firm’s own system of quality control.

And finally, it should link the key elements of an audit quality framework based on the PCAOB’s quality-control standards and other professional standards. These standards include areas such as ethics and attitude; knowledge, experience, and time; process and execution; and reporting and communications.

Of course, the AQI issue comes with significant challenges. Certainly, one of them is that views on audit quality vary widely among stakeholders. Much depends on the degree to which stakeholders have direct involvement in public company audits—and the lens through which they assess auditor responsibility and performance. At the CAQ, we are working through these issues to achieve consensus with various stakeholders where possible.
That leads me to a yet another way the profession is continuing to get stronger: a new sense of urgency around creating consistent regulatory regimes that work for businesses and investors globally.

With the increasingly global nature of our economy and markets, the need for rules and regulations that work across borders is as pressing as ever, as U.S.-based companies operating in multiple markets internationally must contend with disparate, sometimes conflicting regulatory requirements.

A front and center issue with global implications is the effort by policymakers to update the auditor’s reporting model. Regulators worldwide continue their drive to ensure investors have helpful information on the roles, responsibilities, and oversight of financial reporting.

Here at home, the CAQ has worked closely with the public company auditing profession to evaluate the PCAOB’s rule proposal to update the auditor’s report. The CAQ will weigh in on the Board’s plan this week. We will also provide this input to the IAASB, which has also has issued a proposal to update the auditor’s report.

Time doesn’t permit me to discuss our policy position in detail here, but know the public company auditing profession continues to invest significant resources in evaluating and field testing these proposals. Our aim is to develop an approach that will continue to meet the evolving needs of investors and other stakeholders.

It’s time for me to yield the podium to our keynote speaker, David Walker, who I’m eager to hear from.

But to quickly recap: the public company auditing profession can take pride in our fundamental strength.

We are building on that strength in several ways, to the benefit of our markets, investors, and the economy. We at the CAQ and throughout the public company auditing profession are:

• Investing in the formation of talent for the profession of the future.
• Developing new resources to continuously improve.
• Working together more closely than ever to fight financial reporting fraud.
• Taking a range of steps to improve transparency today in a number of areas.
• And advocating for rules that work for businesses and investors in a global economy.

All these tasks require enormous effort. But our dedication is just as strong.

Or, to paraphrase the song we heard in the Chevy ad earlier, nothing will knock us off the road we’re rolling on.

Thank you.