

This series presents the PricewaterhouseCoopers Point of View on a range of auditing, accounting and regulatory issues affecting our clients and our profession. These positions represent the collective view of our network of firms.

## Setting standards for auditing

### What are the issues?

In recent years, auditing standard setting has undergone fundamental reform as part of the regulatory response to corporate reporting scandals. Standard setting was once one of the hallmarks of the accountancy profession's self-regulation. Two new standard setting models are emerging:

- Independent and proactive public interest oversight over existing structures (e.g., the Public Interest Oversight Body (PIOB) and the International Auditing and Assurance Standards Board (IAASB))
- New standard setting bodies that are independent of the profession (e.g., the US Public Company Accounting Oversight Board (US PCAOB))

Stakeholders will be looking for benchmarks to judge the success of the new standard setters.

### What is our response?

We believe the attributes of high quality standard setting are:

- 1 Stakeholder engagement.** Auditing standard setters frequently describe their primary objective as setting standards that are in the public interest. The "public interest" is difficult to define. However, processes that are designed to engage stakeholders – investors, preparers, auditors, monitoring bodies, regulators – and ensure that all views are heard and cost/benefit is weighed are important safeguards in achieving that aim. Without the engagement of all stakeholders, there is a risk of standard setters inadvertently creating expectation gaps by reacting to perceptions of, rather than knowledge of, stakeholders' collective needs.
- 2 Transparent process, including widespread consultation.** Transparency throughout the standard setting process engenders both confidence and participation. It helps to reassure participants that their voices have been heard and given due consideration, and also builds commitment by giving credibility to the validity of the final positions.
- 3 Appropriate expertise brought to bear.** The quality of the standards produced depends on having the right people and best minds at the table. Auditing standards are different from accounting standards – focussed more on behaviour and grounded in practice. They have their roots in the profession – originally being set by professional auditors for professional auditors with the aim of improving audit practice. Auditing standard setting that strays too far into theoretical or political domains risks losing effectiveness. The increased involvement of more non-practitioner stakeholders in auditing standard setting bodies is positive. But, it remains essential that the experience of those in practice be brought to bear throughout the process as well.

### 4 Commitment to principles-based standards.

Quality auditing depends on the application of sound professional judgement. Auditing standards should aim to guide the exercise of sound judgement, not supplant it with rules. Auditing standard setters need to guard against introducing greater prescription and reducing the scope for professional judgement. Doing so will inevitably drive behaviour towards a preoccupation with compliance with the rules rather than performing a quality audit. It will also hinder auditors' ability to adapt to changing circumstances and innovate, as well as impede global convergence. Importantly, principles-based standards also allow for scalability – able to be applied to audits of entities both small and large.

- 5 Facilitating convergence.** As capital markets and business increasingly globalise, the benefits of auditors using common high quality standards worldwide become self-evident. Stakeholders want to know that the quality of audits is the same regardless of where they are conducted. As with accounting standards, the path to convergence is likely to be staged. A strong international body is key. Equally, the path will be smoother if national standard setters actively contribute to the international standard setting process, avoid being insular, and are prepared to value the benefits of global consistency over local preferences.

### What does this mean?

We are committed to delivering quality audits that strengthen public confidence in financial reporting. Auditing standards – although admittedly only one of the supporting pillars – have a role to play in achieving that goal.

We believe that the attributes above are sound benchmarks to assess the effectiveness of auditing standard setting bodies and will encourage those with a stake in high quality auditing standards to use them when judging the success of the new bodies. In particular, PwC believes that:

- Principles-based auditing standards best drive high quality performance by auditors.
- Global convergence of auditing standards is both inevitable and desirable.
- Transparency, consultation and stakeholder engagement are vital if the standard setting process is to produce high quality auditing standards that meet the needs of the financial reporting supply chain.
- All stakeholders benefit from the profession's involvement directly in the standard setting process.

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