

APPENDIX H – SURVEY

1 The Panel’s project contemplated gathering information from key audiences using a variety of means. Early in the project the Panel decided to seek information about a wide range of issues from a number of sources through a mail survey, “Request for Opinions on Issues of Audit Effectiveness Addressed to Thought Leaders and Key Stakeholders.” The survey was issued on September 1, 1999.

2 The survey was not intended to be an opinion poll. Rather, the Panel encouraged each respondent to give free-form responses to as many of the questions as possible from that person’s unique perspective. The Panel also informed all potential respondents that their responses would be held in confidence and would not be available for public inspection.

CONSTITUENCIES RESPONDING

3 The intent of the Panel was to seek the views of many constituencies. Toward that end, the Panel addressed the survey to a number of selected individuals and organizations. Among the constituencies surveyed were preparers and users of financial statements, auditors, regulators, academicians, lawyers and analysts. While the list of those initially selected was broad, the Panel did not limit responses to those on the list. Rather the views of everyone interested in the Panel’s project were welcomed. The survey questionnaire was included on the websites of the AICPA and the SEC for anyone to obtain and answer.

4 An analysis of the constituencies included in the Panel’s original mailing and the constituencies responding follows:

<u>Constituency</u>	<u>Original Mailing*</u>	<u>Responses*</u>
Accounting firm personnel	46	15
CPA organizations or personnel	157	18
Legal firm personnel	36	2
Governmental organizations	80	9
Management organizations	16	4
Corporate management	15	7
Investment management or analysts	88	7
Public interest organizations	56	9
Academia	<u>43</u>	<u>19</u>
Totals	<u>537</u>	<u>90</u>

* Some individuals or organizations could fit into more than one category.

SURVEY QUESTIONNAIRE

5 The survey was designed to provoke thought by setting forth points of view in a number of areas, with related questions for respondents to address as they saw fit. The areas explored in the survey were:

1. The Business Environment
2. Responsibilities for Detecting Financial Statement Fraud
3. The Audit Risk Model
4. Breadth of Auditors' Involvement
5. Audit Committees and Auditors' Communications
6. The Auditing Profession
7. The Business of Auditing
 - i) The effects of competition
 - ii) Scope of services offered by audit firms
 - iii) Organizational structures
 - iv) Litigation
8. Regulation and Self-Regulation
 - i) Roles and responsibilities
 - ii) Auditing standards
 - iii) The AICPA and audit firms
9. Costs, Benefits and Other Issues

A copy of the survey questionnaire is included at the end of this appendix.

ANALYSIS OF SURVEY RESPONSES

6 The Panel reviewed all of the survey responses. The details of each response were related to the applicable question or questions in the survey. Matters appearing to be of common interest and common themes were identified and discussed. In general, the Panel addressed:

- Key substantive observations made in response to each of the survey's questions
- Specific recommendations for Panel action or non-action
- Comments about the Panel's project, process and scope
- Specific ideas for enhancing audit effectiveness, including incentives and disincentives
- Other ideas for enhancing investor protection, not necessarily directly involving auditing or auditors
- Cost-benefit considerations and recommendations

7 The information that the Panel received from the survey was valuable in its deliberations and in formulating many of its recommendations. The Panel expresses its appreciation to all respondents for their efforts and the quality of their responses.

COPY OF THE QUESTIONNAIRE

8 A copy of the survey questionnaire is reproduced below.

C. The Questionnaire

Each section of the questionnaire begins with an introductory paragraph, setting out some points of view that you may or may not agree with, and that are not necessarily representative of the views of the Panel. Please feel free to consider these points of view in forming your responses to the questions that follow, or set them aside, as you see fit. They are merely meant to provoke thought.

1. The Business Environment

Auditors operate in an environment of increasing complexity, accelerating change and intense business competition. There is significant merger and acquisition activity, newer and more complex financial transactions and instruments to hedge or mitigate risks, and more intangible or “soft” assets on corporate balance sheets than ever before. Businesses often change strategic directions giving rise to restructuring activities with corresponding reserves set aside to cover the anticipated costs of those activities. Accounting standards address many of these areas, but they often are subject to varying interpretation. In preparing financial reports, management must rely far more on making informed judgments and estimates about the effects of future events and transactions.

Core Questions

- Are auditors devoting sufficient attention to the areas where management discretion and judgment are required in financial reporting? If not, please explain why you believe this.
- To what extent do analysts’ earnings estimates influence management’s judgments in preparing financial statements, and what are the effects on the auditor? If you see any effects, please elaborate on their importance.
- Do accounting standards issued in recent years help or hinder auditors in meeting the needs of users of financial statements? If they hinder auditors, how do they do so and what should be done?

Extended Question

- Analysts' earnings per share estimates establish expectations (sometimes to the penny) in the marketplace for companies to achieve. Can audits ever be expected to be this exact? If not, what should be done, if anything, to deal with this situation?

2. Responsibilities for Detecting Financial Statement Fraud

Under current auditing standards, auditors have the responsibility to assess fraud risks and obtain reasonable assurance that the financial statements are free of material misstatement, whether caused by error or fraud. This is not the same as saying that audited financial statements are a “guarantee” that fraud has not taken place. Investors clearly place some responsibility for the detection of fraud in the hands of auditors, but the extent of these responsibilities often is unclear to many of those involved in the financial reporting process.

Core Questions

- Are auditors' responsibilities with respect to the detection of deliberate misstatements of earnings appropriate? Please explain your view.
- What are users' views of those responsibilities and are they realistic? Please feel free to elaborate on differing views of various types of users, such as individual investors and institutional investors.
- What, if anything, should be done to change these views, or to change auditors' responsibilities for detecting fraud?

3. The Audit Risk Model

Audits are conducted using an “Audit Risk Model” that requires auditors to use their judgment in assessing risks and then in deciding what procedures to apply. The model allows auditors to take the client's business, financial and other circumstances into account in selecting their audit approach. This model can be applied differently by different audit firms, so long as they comply with “generally accepted auditing standards.”

Core Questions

- Is this model, where auditors are encouraged to use their judgment in selecting their audit approach based on the individual company's nature and circumstances, appropriate? Please elaborate on your point of view.
- What are the best safeguards to make sure that auditors exercise this judgment in ways that protect shareholders and other investors?

Extended Questions

- Does this model allow too much chance that errors in auditors' judgments will result in problems for investors?
- Does the model require auditors to explore in sufficient detail the accounting policies and procedures that individual companies use?
- Does the model meet the expectations of the investment community in constraining inappropriate management behavior, especially in judgmental areas?
- Is this model equally appropriate in all industries, or are there some where a different approach might be needed?
- Are auditors sufficiently equipped to deal with the growing role of information technology? What incremental skills are needed?
- Do auditors exert the right balance between efficiency and timeliness on the one hand and thoroughness on the other? Do you have any observations about the level of experience of auditors assigned to engagements, how they are supervised and their work reviewed, or the nature and extent of the audit documentation that they retain in their working papers?

4. Breadth of Auditors' Involvement

Some argue that, in light of increased business complexity, technology, new financial instruments, and other developments, auditors do not pay enough attention to business systems, management processes, unique industry factors and operational matters. According to these observers, auditors place too much emphasis on historical financial information and not enough on the current and future risks of managing the business and on the entity's communications with investors. Others believe that it would be impractical or inappropriate for auditors to focus more attention on these matters.

Core Question

- Do you believe auditors should be more involved in and familiar with their clients' business and operational matters and ongoing communications with the investment community? Please explain why you feel the way that you do.

Extended Questions

- Should auditors be more or less involved with:
 - internal controls

- interim financial statements
- forecasts
- management's discussion and analysis
- non-financial data
- Should auditors be required to report on such matters? If so, which matters and why?
- Would greater involvement in these areas improve the value of the independent audit?
- Would the costs of greater involvement outweigh the benefits?

5. Audit Committees and Auditors' Communications

A significant part of the debate about audit effectiveness has focused on the current and future roles of audit committees, including their roles in enhancing communications among themselves, the board, management, shareholders, and the auditors. Some believe that a stronger role for audit committees may be a necessary and helpful way of improving the effectiveness of audits. (The Panel does not intend to duplicate the work of the Blue Ribbon Committee on the Effectiveness of Audit Committees.)

Core Questions

- Do you believe auditors currently communicate effectively with:
 - management
 - audit committees
 - boards of directors
 - stockholders (feel free to elaborate on institutional versus individual investors)

Extended Questions

- Do you have any suggestions for improving the effectiveness of auditors' communications?
- Should auditors do more to assist audit or other committees of a board of directors?
- Are audit committees effective in promoting quality audits? How can audit committees be more effective in that regard? Do audit committees do enough to seek out auditors' opinions and input?

6. The Auditing Profession

Some have sensed that it is becoming more difficult to attract and retain young people in auditing as a career. Others believe that this has long been a challenge and that things are not so different today.

Core Questions

- Do you believe that the quality of new recruits into auditing has been declining in recent years, and if so, is this having an effect on the quality of audits?
- Are the opportunities and rewards in the auditing profession sufficient to attract and retain high quality entrants? (Please separate the question of attracting versus retaining as you see fit.) If not, what more should be done to attract and retain more high quality individuals over the long term?
- What are your views on audit personnel taking jobs with clients?

7. The Business of Auditing

i) The effects of competition

Audit firms operate in a highly competitive environment, and there is a debate about the effects of that competition on the quality of audits. While the largest five firms audit the preponderance of publicly held companies, changes in audit firms by publicly held companies are relatively infrequent. Some believe that competition improves the quality of audits while others argue that emphasis on competition weakens their quality.

Core Questions

- What are your views about the effects of competition and pricing on the quality of audits?
- How do you see time and budget pressures affecting the quality of audits?

ii) Scope of services offered by audit firms

Some believe that audit firms are placing less emphasis on audit work and more emphasis on other services they provide, thus weakening the quality of audits. Others assert that

non-audit work either has no effect, or actually helps audit firms perform better audits by keeping their skills and understanding of business more up to date.

Core Questions

- What are your impressions of the importance (stature, compensation, advancement, investments, etc.) audit firms place on audit work relative to the other services they offer, and how, if at all, does this affect the quality of audits?
- Do you believe non-audit services offered to audit clients affect the independence or perceived independence of auditors? If so, how do they do so and what should be done about this?
- Do firms properly balance the importance of high quality, independent audits with
 - The goal of practice growth and firm success?
 - The goal of client retention?
 - The goal of enhancing relationships with clients?
- Do firms place sufficient importance on professional qualifications, accounting and auditing training, specialized skills, experience and integrity of auditors?

iii) Organizational structures

Over the past decade, audit firms have diversified into a variety of services either by internal expansion or by acquisition. Furthermore, some non-audit organizations have acquired audit firms or parts of them.

Core Questions

- What are the effects of the following on the quality of audits:
 - non-audit organizations acquiring audit firms or parts of them?
 - audit firms broadening their range of non-audit services through acquisition or by internal expansion?
- Are current organizational structures appropriate to promote quality audits?

iv) Litigation

Some believe that litigation or the threat of litigation has a salutary effect on the quality of audits. Others assert that litigation has unreasonably driven up costs for audit firms, and combined with downward pressures on prices, may have weakened audit quality.

Core Questions

- What are your thoughts on the effects of litigation on the quality of audits?
- Will recent changes in federal or state laws affect the quality of audits? In what way?
- Are more changes to securities or other laws needed? If so, what changes?

8. Regulation and Self-Regulation

i) Roles and responsibilities

Currently, there is a wide array of practices in place to enhance audit quality, including oversight by regulatory bodies, self-regulation by professional associations, and policies and practices within each audit firm.

Core Questions

- Do you think that there is the right balance between regulation and self-regulation, insofar as enhancing audit quality is concerned?
- What changes, if any, would you suggest in the approaches taken by regulatory bodies, self-regulatory bodies, and individual firms to enhance audit quality?

ii) Auditing standards

Auditing standards are established by the Auditing Standards Board of the AICPA, a 15-member board comprising representatives from each of the five largest audit firms, eight other audit firms, a member of the academic community and a member from government. The SEC oversees the activities of the ASB.

Core Question

- Do “generally accepted auditing standards” and the way they are formulated meet the needs of the investment community? If not, what changes would be useful?

iii) The AICPA and audit firms

The AICPA exists to serve the accounting profession’s interests in a variety of ways, including speaking on behalf of the profession on topical issues. Audit firms, of course, speak on their own behalf and promote their own individual capabilities.

Core Question

- What would you like to see the AICPA and individual firms do to enhance the public’s trust and confidence in the auditing profession?

9. Costs, Benefits and Other Issues

Actions to improve the effectiveness of audits in protecting investors’ interests need to be justified in terms of their costs versus the benefits to be derived from them.

Core Question

- What recommendations would you like to see the Panel make, and how do you assess their costs and benefits?

The foregoing questions are intended to cover key issues relating to audit effectiveness. The Panel invites respondents to provide comments on issues that may not be addressed or adequately covered by this questionnaire. You may draw on personal experiences or observations, as you deem appropriate.
