
STANDARDS AND EMERGING ISSUES ADVISORY GROUP MEETING

DISCUSSION – FIRM AND ENGAGEMENT PERFORMANCE METRICS

NOVEMBER 2, 2022

INTRODUCTION

At the June 2022 Standards and Emerging Issues Advisory Group (“SEIAG”)¹ and Investor Advisory Group (IAG)² meetings several members indicated there was continued interest by our stakeholders in the topic of firm and engagement performance metrics, also referred to as audit quality indicators (“AQI’s”). In addition, some commenters to the Board’s Draft Strategic Plan 2022-2026 encouraged the Board to continue to consider this topic.³ In October 2022 the PCAOB updated its standard-setting agenda to include a research project on “Firm and Engagement Performance Metrics” to assess whether there is a need for guidance, changes to PCAOB standards, or other regulatory actions in light of the increased disclosure and demand for firm and engagement metrics.⁴ At the November 2022 SEIAG meeting, members will discuss firm and engagement performance metrics. This paper provides background information, outlines key areas related to the topic, and includes discussion questions. We would like to obtain SEIAG members’ feedback about how some of these metrics that are currently publicly available are being used, among other things, in order to inform our future actions. The IAG also discussed this topic at the October 2022 meeting.⁵

¹ See <https://pcaobus.org/news-events/events/event-details/pcaob-standards-and-emerging-issues-advisory-group-meeting>.

² See <https://pcaobus.org/news-events/events/event-details/pcaob-investor-advisory-group-meeting-2022>.

³ See *Draft 2022-2026 PCAOB Strategic Plan*, PCAOB Release No. 2022-003 (August 16, 2022). The comment letters received in response are available on our website at <https://pcaobus.org/about/strategic-plan-budget/comments-on-pcaob-draft-strategic-plan-2022-2026>.

⁴ See <https://pcaobus.org/oversight/standards/standard-setting-research-projects/firm-and-engagement-performance-metrics>.

⁵ See October 2022 IAG meeting at <https://pcaobus.org/news-events/events/event-details/pcaob-investor-advisory-group-meeting>.

This document was developed by the staff of the Office of the Chief Auditor as of November 2, 2022 to foster discussion among the members of the Standards and Emerging Issues Advisory Group. It is not a statement of the Board; nor does it necessarily reflect the views of the Board, any individual Board member, or PCAOB staff.

BACKGROUND

On October 6, 2008, the U.S. Department of Treasury's Advisory Committee on the Auditing Profession ("ACAP") published a report detailing recommendations that would enhance the sustainability of a strong and vibrant public company auditing profession.⁶ These recommendations were separated into three categories; Human Capital, Firm Structure and Finances, and Concentration and Competition. Certain of these recommendations were directed at the PCAOB, while other recommendations suggested actions by other organizations in addition to the PCAOB, including the SEC, AICPA, and NASBA.

One recommendation proposed by ACAP related to developing key indicators of audit quality. This recommendation urged the PCAOB to determine the feasibility of developing key indicators of audit quality and effectiveness and requiring auditing firms to publicly disclose these indicators and, assuming development and disclosure of indicators of audit quality are feasible, require the PCAOB to monitor these indicators.

ACTIVITIES TO DATE

October 2013 IAG Meeting

At the October 2013 IAG Meeting,⁷ an IAG working group made recommendations for audit firms to be required to provide the PCAOB with data compiled at both the engagement level and the firm level, including:

- Identification of key risk areas and hours spent by the engagement partner in addressing them.
- Hours spent by audit partners and staff in firms that are not subject to an inspection by the PCAOB, as well as the percentage of the balance sheet, income statement and cash flows audited by the non-inspected firm.
- Percentage of audit hours outsourced to either another firm or an affiliate in a foreign country.

⁶ See ACAP's Fact Sheet: Final Report of the Advisory Committee on the Auditing Profession available at <https://home.treasury.gov/news/press-releases/hp1158#:~:text=The%20U.S.%20Treasury%20Department%20%27s%20Advisory%20Committee%20on,into%20three%20sections%20by%20principal%20areas%20of%20focus>.

⁷ See https://pcaobus.org/news-events/events/event-details/pcaob-investor-advisory-group-meeting_758.

- The name of the lead engagement partner, in order to assess whether he or she has participated in other audits whose credibility has been questioned.

PCAOB Concept Release on Audit Quality Indicators

The PCAOB's 2015 Concept Release on Audit Quality Indicators⁸ proposed and sought comment on 28 potential indicators. The indicators fall into three groups:

- Audit professionals – Measures dealing with the availability, competence, and focus of those performing the audit.
- Audit process – Measures about an audit firm's tone at the top and leadership, incentives, independence, attention to infrastructure, and record of monitoring and remediation.
- Audit results – Financial statements, internal control, going concern, communications between auditors and audit committees, and enforcement and litigation.

The Concept Release discussed (i) the nature of the potential indicators, (ii) the usefulness of the indicators, (iii) suggestions for other indicators, (iv) potential users of the indicators, and (v) approach to implementation over time of an AQI project. The PCAOB received 50 comment letters in response to the Concept Release.⁹ Most commenters expressed support for the general idea that AQIs could provide some usefulness in advancing audit quality. However, the views varied widely. Letters from the audit professional suggested that there was no standard group of AQIs that could advance a person's understanding of audit quality. These commenters suggested that variations in auditor and issuer made it impossible to identify a single group of meaningful indicators. Investors indicated that indicators should be made public and could be used to stimulate competition based on quality among audit firms, remedy the deficiency of information about audits, and give shareholders meaningful information to help them in voting on auditor selection.¹⁰

October 2017 IAG Meeting

At the October 2017 IAG meeting, an IAG working group discussed the following topics:¹¹

⁸ See *Concept Release on Audit Quality Indicators* ("Concept Release") https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/rulemaking/docket_041/release_2015_005.pdf?sfvrsn=de838d9f_0.

⁹ See <https://pcaobus.org/about/rules-rulemaking/rulemaking-dockets/docket-041-concept-release-on-audit-quality-indicators/comment-letters>.

¹⁰ See November 2015 SAG Briefing Paper, https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/news/events/documents/11-12-2015-sag-meeting/sag-aqi-memo.pdf?sfvrsn=2e46f557_0.

¹¹ See https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/news/events/documents/10242017-iag-meeting/wg-slides-aqi.pdf?sfvrsn=669ae438_0.

- Why Audit Quality and AQIs Matter to Investors
- PCAOB Authority and Efforts to Date to Enact AQIs
- Audit Quality Initiatives in Other Jurisdictions

The 2017 working group endorsed the 2013 AQI working group recommendations and added a few other indicators to consider, refer to **Attachment A**.

PCAOB Initiatives to Provide Firm and Engagement Level Information Publicly

- Auditor’s Report¹²
 - Critical Audit Matters – those matters that involved especially challenging, subjective, or complex auditor judgement
 - Auditor Tenure – how long the auditor has been serving as the company’s auditor
- Information available through Form AP¹³
 - Disclosure of the name of the engagement partner
 - Identify a change in engagement partner
 - Other public engagements for which an engagement partner is responsible
 - Percentage of the audit performed by other firms
 - Names of other firms involved in the audit (over a certain percentage)
- Form 2
 - Percentage of fees billed to issuer audit clients in relation to total fees billed to all clients

¹² See AS 3101, *The Auditor’s Report on an Audit of Financial Statements*.

¹³ See PCAOB Rule 3211, *Auditor Reporting of Certain Audit Participants*. The entire Form AP dataset (updated daily) and data dictionary are available to download in CSV format under the section, “Download the entire data set,” at <https://pcaobus.org/resources/auditorsearch>.

- Form 3
 - Certain legal proceedings, including, SEC and other regulatory enforcement actions¹⁴

PCAOB Initiatives by the Office of Economic and Risk Analysis

The Office of Economic and Risk Analysis (“OERA”) has reviewed the extant literature and engaged academic fellows in reviewing potential performance metrics of audit quality.¹⁵ It has been noted that a significant limitation in establishing a relationship between potential audit quality performance metrics and audit quality is the fact that audit quality is itself immeasurable, and there are no set criteria for what defines quality in an audit.¹⁶ The majority of the academic literature uses publicly available measures of audit failure to proxy for audit quality (or the lack thereof), such as the occurrence of a restatement, the release of a PCAOB inspection finding, or internal assessments of audit quality performed by auditors. Some studies even use discretionary accruals¹⁷ or audit fees in absence of any alternative measures.¹⁸ Furthermore, it is not clear whether the relationship observed in these studies is due to improved (reduced) audit quality as it relates to the performance metric or due to underlying financial reporting quality, because the proxies used could indicate either or both.¹⁹

A few studies have made use of proprietary PCAOB data (i.e., Part I findings matched to issuer engagements) and have found evidence of relationships between certain audit inputs (e.g., who performs the audit, engagement team-member turnover, and early engagement partner rotations) and Part I findings²⁰ – indicating there are some identifiable instances in which an audit input could relate to audit quality. However, in the overall academic literature the relationships identified between audit metrics

¹⁴ This information is publicly available on Form 3, *Special Reporting Form*, unless a firm has requested confidential treatment of the information. The PCAOB posts all publicly available Board opinions, orders, termination of bars, and other Board enforcement actions. By law, the PCAOB is not permitted to publish pending PCAOB enforcement actions per Section 105(b)(5)(A) of Sarbanes-Oxley, 15 U.S.C. § 7215(b)(5)(A).

¹⁵ Publications and working papers developed by PCAOB fellows are available at:
<https://pcaobus.org/resources/information-for-academics/publications-and-workingpapers>

¹⁶ [Knechel et al. \(2013\)](#).

¹⁷ Discretionary accruals (*a.k.a.* abnormal accruals) which may arise from earnings management, and other measures of earnings quality, are sometimes used within the academic literature as proxies for audit quality, yet they may not relate to audit quality or are poor proxies for it. See, e.g., [Francis \(2011\)](#) and [DeFond and Zhang \(2014\)](#) for a discussion of these issues.

¹⁸ See, e.g., [Francis \(2011\)](#), [Knechel et al. \(2013\)](#), [Bell, Causholli, and Knechel \(2015\)](#), [Aobdia \(2019\)](#), and [Chen and Choudhary \(2020\)](#). For a brief review of proposed audit quality indicators up to 2010, see, e.g., [Bedard, Johnstone, and Smith \(2010\)](#), for a lengthier review of archival research including as it relates to audit quality indicators, proxies, and audit quality frameworks see, e.g., [DeFond and Zhang \(2014\)](#). A few studies have sought to query auditors and investors on their views on audit quality indicators based on the [2015 Concept Release](#) and across levels of seniority in the audit profession (see, e.g., [Christensen et al. \(2016\)](#), and [Brown, Gissel, and Neely \(2016\)](#)).

¹⁹ [DeFond and Zhang \(2014\)](#).

²⁰ See [Gipper, Hail, and Leuz \(2021\)](#), [Gipper, Hail, and Leuz \(2022\)](#), and [Aobdia, Choudhary, and Newberger \(2022\)](#).

and audit quality are often mixed and varies depending on the proxy used for audit quality,²¹ leaving open questions as to whether the relationships identified are robust.

Additionally, OERA has internally reviewed and evaluated potential economic impacts of requiring disclosures of firm and engagement performance metrics. Staff explored whether hypothetically requiring disclosure of such performance metrics would improve the selection of high-quality auditors and possibly increase the information available to investors regarding the audit process. The staff also heuristically evaluated potential drawbacks of required disclosures of those performance metrics, including impacts on smaller audit firms, the potential for performance metric manipulation, and impacts on inspections.

Current Firm Reporting

Since the Concept Release, some audit firms are publicly reporting various firm level information addressed in the Concept Release through their Audit Quality Reports, Transparency Reports, or other published reports.²² Using the 28 indicators identified in the Concept Release, staff reviewed the most recent firm reports available to identify which indicators firms are currently reporting. In addition, for each firm level metric currently being reported, staff included examples of how firms calculated the metric as well as the total number of firms reporting the specific firm-level metric.

Firm Level Metric	Firm Level Description from Concept Release	Example Firm Calculations	Number of Firms Reporting
Staffing Leverage	Measures the time of experienced senior personnel relative to the volume of audit work they oversee.	Leverage ratio of partners and managing directors to audit personnel Leverage ratio of managers and senior managers to senior and staff Leverage ratio of supervisor hours	7
Partner Workload	Generates data about the level of work for which the audit engagement partner is	Average annual hours worked in excess of 40 hours per week for partners	3

²¹ [Aobdia \(2019\)](#).

²² Various reports issued by nine firms were reviewed to identify firm level metrics disclosed in public reports. These firms are BDO USA, LLP, CohnReznick LLP, Crowe LLP, Deloitte & Touche LLP, Ernst & Young LLP, Grant Thornton LLP, KPMG LLP, PricewaterhouseCoopers LLP, and RSM US LLP.

Firm Level Metric	Firm Level Description from Concept Release	Example Firm Calculations	Number of Firms Reporting
	responsible and the number of claims on his or her attention.	Number of issuer audit engagements that audit partners lead	
Manager and Staff Workload	Information about the workload of audit managers and audit staff.	Average annual hours worked in excess of 40 hours per week by level Annual utilization rate	4
Technical Accounting and Auditing Resources	Measures the level of a firm’s central personnel (or other resources engaged by the firm) available to provide engagement teams with advice on complex, unusual, or unfamiliar issues and the extent to which they are used in a particular engagement.	Partners and managing directors serving in technical professional practice roles to all partners and managing directors Total number of professionals serving in a technical role Total hours contributed by professional practice	9
Persons with Specialized Skill and Knowledge	Measures the use in an audit engagement of persons with “specialized skill and knowledge,” other than accounting and auditing personnel counted as technical accounting and auditing resources. These individuals may be firm personnel or they may be retained by the firm.	Percentage of audit hours provided by specialists	5

Firm Level Metric	Firm Level Description from Concept Release	Example Firm Calculations	Number of Firms Reporting
Experience of Audit Personnel	Measures the weighted average experience of firm's personnel generally.	Partner [managing directors] average years of experience within the firm Average tenure at firm by level	6
Turnover of Audit Personnel	Measures turnover, that is, movement to other firms, at the firm level.	Average annual voluntary turnover rate by staff level Average annual retention rate by staff level	8
Amount of Audit Work Centralized at Service Centers	Measures the degree to which audit work is centralized by the audit firm at service centers.	Percentage of audit hours performed by shared service center professionals	5
Training Hours per Audit Professional	Focuses on the hours of relevant training that staff and partners of the firm receive.	Average training hours completed by level Firm's policy on minimum training hours Total learning credits completed	9
Allocation of Audit Hours to Phases of the Audit	Measures the effort and staffing the audit devotes to audit planning, interim field work, and audit completion.	Percentage of audit work performed three months before the company's year-end Percentage of audit work performed before the company's year-end	1

Firm Level Metric	Firm Level Description from Concept Release	Example Firm Calculations	Number of Firms Reporting
Results of Independent Survey of Firm Personnel	Measures an audit firm's "tone at the top" through use of a survey tool.	<p>Percentage of Assurance professionals who reported receiving consistent messages about the importance of audit quality from firm leadership</p> <p>Percentage of Assurance professionals who reported understanding the firm's audit quality objectives</p>	3
Compliance with Independence Requirements	Measures several elements of a firm's independence training and monitoring program and the importance it assigns to that program.	<p>Number of professionals who maintain independence policies, processes, and controls</p> <p>Number of independence-related consultations</p> <p>Number or percentage of partners and other professionals tested for their compliance with the firm's independence policies</p>	4
Investment in Infrastructure Supporting Quality Auditing	Measures the amounts audit firms invest, in people, processes, and technology, to support the base on which quality auditing depends.	<p>Dollar amount invested in a learning and development center</p> <p>Dollar amount invested in delivery of new audit processes</p>	2
Audit Firms' Internal Quality Review Results	Contains information about the internal quality reviews conducted by each audit firm.	Number of engagements subject to internal inspection or pre-issuance reviews	6

Firm Level Metric	Firm Level Description from Concept Release	Example Firm Calculations	Number of Firms Reporting
		Percentage of compliance rate for engagements that were internally inspected	
PCAOB Inspection Results	Contains information about PCAOB inspection results relating to the audit firm involved.	Number of audits inspected and number of audits included in Part I.A	6
Frequency and Impact of Financial Statement Restatements for Errors	Measures the restatements for error of financial statements whose audit the audit firm has performed.	Percentage and number of issuer audit client financial statements that were (or were not) restated Percentage and number of reports on an issuer’s internal control over financial reporting that were (or were not) reissued or withdrawn	6

Information Regarding Audit Firms

Some PCAOB registered firms provide firm level performance metrics as noted above. There are approximately 690 firms that currently audit issuers. Some information regarding those firms, include:²³

- Approximately 99% of the S&P 500 issuers (representing market capitalization of approximately \$35,101 billion) are audited by the U.S. global network firms.²⁴
- Approximately 52% of issuers (representing market capitalization of approximately \$43,099 billion) are audited by the U.S. global network firms.

²³ Based on information as of August 31, 2022.

²⁴ See <https://pcaobus.org/oversight/registration/global-network-firms>.

- Approximately 15% of issuers (representing market capitalization of approximately \$403 billion) are audited by firms that were annually inspected firms in 2021, excluding U.S global network firms.
- Approximately 33% of issuers are audited by the remaining registered firms.

Activities by Other Regulators and Professional Organizations

Organizations, including regulators, oversight bodies, professional bodies, and independent forums around the world are continuing to conduct activities related to initiatives to improve audit quality. In May 2022 Accountancy Europe performed a review of recent initiatives in Europe and beyond and published a fact sheet describing its findings, refer to **Attachment B**.²⁵ Three initiatives of other regulators to highlight are:

- The Portuguese Securities Market Commission (CMVM), Portugal – The CMVM identified a set of 8 indicators that it requires firms to report under a transitional implementation process whereby the six largest firms auditing PIEs were required to report their indicators and metrics at the firm and engagement levels for 25 group audit engagements beginning in 2019. Beginning in 2020, five more firms were required to report their metrics for five group audit engagements each.
- Independent Regulatory Board for Auditors (IRBA), South Africa – IRBA requested firms auditing listed companies to submit AQI-related information to the IRBA, and IRBA published a survey report in 2021 that describes the results of the information submitted under the five broad thematic categories: independence, tenure, internal firm quality review processes, workload of partners and audit managers, and other. The report presents comparisons across audit firms on an anonymous basis and illustrates some of the challenges associated with comparing certain indicators across firms, in particular, without the benefit of qualitative context.
- The Financial Reporting Council (FRC) issued a consultation on June 22, 2022, on publishing audit quality indicators for the largest UK audit firms.²⁶ The proposal includes 11 proposed AQIs and covers a range of topics including firm culture, audit quality inspection results, staff workloads and the level of partners’ involvement in individual audits. The deadline for

²⁵ See Accountancy Europe May 2022 publication, *Factsheet, Audit Quality Indicators, A Global Overview of Initiatives* <https://www.accountancyeurope.eu/wp-content/uploads/220401-Factsheet-Audit-Quality-Indicators.pdf>.

²⁶ See FRC Consultation Document: *Firm-level Audit Quality Indicators*, https://www.frc.org.uk/getattachment/a2080b36-f3f6-4fa3-85b1-beeba16ef0d7/FRC-Consultation-Document-Firm-level-Audit-Quality-Indicators_2022.pdf.

responses to the consultation was August 18, 2022. The FRC indicated that it plans to produce a feedback statement and a final version of the proposals in late 2022.

QUESTIONS:

1. How are you currently using the information that is publicly available either from the PCAOB or the firms?
2. What are your views related to the comparability across firms of these performance metrics?
3. Besides the metrics already published by the PCAOB and provided by the firms, what other performance metrics would be useful?
4. How do/will users use firm level or engagement level performance metrics, in their decision making?
5. How would you expect this information to be reported, through Form AP, the firm's audit quality reports, published by the firm on their website?
6. Which firms should be required to provide this information?
 - a. All firms
 - b. Firms that audit over 100 issuers (firms annually inspected by the PCAOB)
 - c. Firms that audit a specific number of issuers or broker dealers
7. Are there unintended consequences to requiring firm reporting of performance metrics?

* * *

The PCAOB is a nonprofit corporation established by Congress to oversee the audits of public companies in order to protect investors and the public interest by promoting informative, accurate, and independent audit reports. The PCAOB also oversees the audits of brokers and dealers, including compliance reports filed pursuant to federal securities laws, to promote investor protection.

Attachment A – Previous IAG Recommendations Matrix

SEIAG Meeting November 2, 2022

1 | Page

At the October 2013 meeting¹ of the Investor Advisory Group, a working group of the IAG (IAG Working Group on Audit Quality Initiatives) made recommendations for firms to provide the PCAOB with data compiled at both the engagement level and the firm level. These recommendations were subsequently endorsed by the 2017 IAG Working Group on Audit Quality Initiatives. In the table below, the staff of the Office of the Chief Auditor indicates where this information may be available publicly.

Note: This document was developed by the staff of the Office of the Chief Auditor as of November 2, 2022 to foster discussion among the members of the current Standards and Emerging Issues Advisory Group. It is not a statement of the Board; nor does it necessarily reflect the views of the Board, any individual Board member, or PCAOB staff.

* These items were only recommended by the 2017 IAG Working Group on Audit Quality Initiatives.²

** There items were included in the PCAOB’s 2015 Concept Release on Audit Quality Indicators.

IAG Recommendation	Provided to the Audit Committee	Published by PCAOB	Published by the Firm in its Audit Quality Report	Published by Others	Not provided
ENGAGEMENT LEVEL AQI					
Ratio of partner and manager hours to the hours charged by the rest of the engagement team.**					X
Identification of key risk areas and hours spent by the engagement partner in addressing them.**	X – Key risk areas only, AS 1301				
Whether the audit had been inspected by the PCAOB in the most recent year. If so, whether any deficiencies in the audit were noted and a description of the types of deficiencies.**					X
Hours spent by audit partners and staff in firms that are not subject to an inspection by the PCAOB, as well as the percentage of the balance sheet, income statement and cash flows audited by the non-inspected firm.		X – Form AP			

¹ See https://pcaobus.org/news-events/events/event-details/pcaob-investor-advisory-group-meeting_758.

² See https://pcaobus.org/news-events/events/event-details/pcaob-investor-advisory-group-meeting_1085.

Attachment A – Previous IAG Recommendations Matrix
SEIAG Meeting November 2, 2022

2 | Page

IAG Recommendation	Provided to the Audit Committee	Published by PCAOB	Published by the Firm in its Audit Quality Report	Published by Others	Not provided
Percentage of audit hours outsourced to either another firm or an affiliate in a foreign country.		X – Form AP			
Whether there was any consultation with the national technical office, and if so, on what issue(s).	X – AS 1301				
The name of the lead engagement partner, in order to assess whether he or she has participated in other audits whose credibility has been questioned.	X	X – Form AP			
AUDIT FIRM LEVEL AQI					
Policy on measurement and management of audit quality indicators which should be made public.					X
Compensation Policy for (1) executive partners, (2) audit partners and (3) audit staff and whether (and if so, how) compensation levels are linked to audit quality, including specific triggers measured and used in linking audit quality to compensation.			X – Audit partner compensation policy that links to audit quality	X – Required for partners under the European Union Audit Directive, Article 13	
Average billing/hours responsibility of audit partners. Also average chargeable hours of (1) partners, (2) managers and (3) audit staff.**			X – Only average audit utilization percentage		
Number of audit engagements for which an independence review occurred and, of those, the number and aggregate estimated fees of non-audit engagements which the firm declined to accept.					X
Identification of affiliates not subject to an inspection by the PCAOB.		X – Only those PCAOB not permitted to inspect			
Identification of affiliates who do not provide audit documentation to the U.S. affiliate in compliance with SOX					X
Number of restatements, by major industry groups.			X – Total number of restatements (and percentage of total number of	X – Audit Analytics	

Attachment A – Previous IAG Recommendations Matrix
 SEIAG Meeting November 2, 2022
 3 | Page

IAG Recommendation	Provided to the Audit Committee	Published by PCAOB	Published by the Firm in its Audit Quality Report	Published by Others	Not provided
			restatements of issuer engagements).		
Number of material weaknesses reported, by major industry group.				X – Audit Analytics	
Billable fees or hours by major industry groups.					X
Portion of audits assessed as being “high risk” audits.					X
Percentage of revenues spent on audit staff.**					X
Dollar investment in audit tools and audit technology.**			X – Some firms publish this information in other locations.		
Number of pending SEC and PCAOB enforcement actions.**				X – Pending SEC orders	X – Pending PCAOB orders
Average salary for new hires on the audit staff.					X
The number of first year audit engagements where the prior auditor resigned, or there was a disagreement reported with the prior auditor.				X – SEC	
ENGAGEMENT AND FIRM LEVEL AQI					
Average hours of professional education for (a) partners, (b) managers, and (c) staff assigned to audit.**			X		
Turnover in staffing at (a) partner, (b) manager, and (c) staff levels**			X		
Average years of experience of audit partner and personnel staff assigned: (a) experience on specific engagement; (b) experience in the industry; and (c) overall audit experience.**		X – Partner (a) only	X – (c) only		
Any violation of the PCAOB auditor independence rules.**	X – Rule 3526	X – Part I.B Independence findings only			X – Part II Independence findings
Transparency of inspection grades and results*					X

Attachment A – Previous IAG Recommendations Matrix
 SEIAG Meeting November 2, 2022

IAG Recommendation	Provided to the Audit Committee	Published by PCAOB	Published by the Firm in its Audit Quality Report	Published by Others	Not provided
Trends in both private and regulatory legal actions*,**		X – Form 3 for regulatory legal actions			X – Private legal actions
Timely reporting of going concern reports*					X



**ACCOUNTANCY
EUROPE.**

AUDIT QUALITY INDICATORS

A global overview of initiatives

Factsheet

FACTS.

**AUDIT & ASSURANCE
MAY 2022**

HIGHLIGHTS

This paper presents an overview of selected recent initiatives on audit quality indicators (AQIs) in Europe and beyond. These have been initiated by different types of organisations, including regulators, oversight bodies, professional bodies, and independent forums. There exist also differences in terms of their intended users and transparency.

The publication aims to advance the European and global discussions on how to define, measure and improve audit quality. Accountancy Europe is actively working on this topic and will continue to contribute to the debate with evidence-based facts and constructive recommendations.

TABLE OF CONTENTS

Introduction	2
Background	2
Objective.....	2
New global framework for quality management	2
Overview of audit quality indicators initiatives	4
Initiatives in EU Member States	6
Institute of Public Auditors (IDW), Germany	6
Quartermasters, Netherlands	7
The Portuguese Securities Market Commission (CMVM), Portugal	8
Initiatives in other European jurisdictions.....	9
Federal Audit Oversight Authority (FAOA), Switzerland	9
Financial Reporting Council (FRC) – UK.....	10
Initiatives in other jurisdictions	11
Canadian Public Accountability Board (CPAB), Canada	11
The Institute of Chartered Accountants (ICAI), India.....	12
Accounting and Corporate Regulatory Authority (ACRA), Singapore.....	13
Independent Regulatory Board for Auditors (IRBA), South Africa	14
Center for Audit Quality (CAQ), US	15
About Accountancy Europe	1

INTRODUCTION

BACKGROUND

The European Commission launched an initiative to improve the quality of corporate reporting and its enforcement. The EC [consultation](#) included questions related to quality indicators for audit and its supervision. Accountancy Europe is willing to contribute to this topic by providing evidence-based facts and constructive recommendations.

This is also topical in other jurisdictions, for example:

- the Global Audit Quality Working Group of the International Forum of Independent Audit Regulators (IFIAR) has been working on an appropriate list of audit quality indicators (AQIs)
- the Public Company Accounting Oversight Board (PCAOB-US) identifies an objective to determine, develop, and communicate AQIs in its [Strategic Plan 2020-24](#),
- the Financial Reporting Council (FRC-Australia) plans to work with the accounting/audit firms and professional bodies on how to define and report on AQIs in its [Audit Quality Action Plan](#)

OBJECTIVE

Accountancy Europe issued [an information paper](#) in 2016 to provide an overview of AQIs by different organisations worldwide. Since then, there has been considerable change in the business environment, including operational models in companies, audit firms and regulators. Several new initiatives have emerged proposing or mandating various sets of AQIs. This publication presents an overview of these initiatives to provide a basis for informed discussions.

NEW GLOBAL FRAMEWORK FOR QUALITY MANAGEMENT

The International Auditing and Assurance Standards Board (IAASB) issued three new standards on audit quality which will come into effect by the end of 2022:

- *International Standard on Quality Management 1 (ISQM 1)* requires audit firms to adopt a risk-based and integrated quality management approach at firm-level
- *ISQM 2* addresses the appointment and eligibility of the engagement quality reviewer as well as their responsibilities relating to the performance of an engagement quality review
- *International Standard on Auditing (ISA) 220* focuses on quality management at the engagement level and requires the audit engagement partner to take responsibility for the achievement of quality

ISQM 1 requires a proactive and tailored approach to quality management. It focuses on achieving quality objectives through identifying risks to those objectives and responding to the risks. According to the ISQM 1, a system of quality management addresses the following eight components:

- the firm's risk assessment process
- governance and leadership
- relevant ethical requirements
- acceptance and continuance of client relationships and specific engagements
- engagement performance
- resources
- information and communication
- the monitoring and remediation process

The firm's risk assessment process and monitoring and remediation process set out specific procedures that the audit firm is required to follow. The remaining components comprise specific quality objectives the audit firm is required to establish.

Audit firms' key performance indicators and AQIs determined by different organisations usually fall into one or more of these components.

OVERVIEW OF AUDIT QUALITY INDICATORS INITIATIVES

The table below presents an overview of various AQI initiatives, followed by more details. A brief analysis of these initiatives allows the following observations:

- **Owner:** The initiatives are mostly launched by audit oversight bodies and professional organisations. Firms use their own metrics to monitor audit quality, and these are structured in different ways.
- **User and transparency:** Audit committees, oversight bodies and audit firms are considered the primary users. AQIs are often reported exclusively to specific users and not made public.
- **Nature and selection:** AQIs are not limited to quantitative elements and are presented in a wider context. There are several factors to be considered when selecting, evaluating, and reporting AQIs (e.g. cost-benefit of tracking indicators and results of external reviews). A combination of metrics is recommended for a profound insight into audit quality.

Owner	Background of the owner	Intended user	Transparency (public or private)	Short overview
IDW – Germany	Professional organisation	Audit committees, oversight body and public	Mainly for reporting to audit committees and oversight body	32 AQIs under four components below and one cross-divisional AQI: Quality culture Workforce quality Process quality Communication
Quartermasters – Netherlands	Independent group of experts assigned by the Minister of Finance	All stakeholders, including public	Subject to adoption by the Ministry of Finance, firms will be obliged to report	11 indicators under three categories: Audit quality Quality control system Context
CMVM – Portugal	Audit oversight body	Oversight body	For the first two years, exclusive reporting to the CMVM	Eight indicators, four of which are at firm-level, one at engagement level and three for both firm and engagement levels
FAOA – Switzerland	Audit oversight body	Oversight body	FAOA presents a summary, including trends, in its annual reports	Nine indicators and three of these are to be reported separately for the Swiss Market Index (SMI) and non-SMI companies
FRC – UK	Audit oversight body	All stakeholders, including public	FRC will consult on AQIs to be included in audit firms' transparency reports	FRC identified 52 AQIs that are monitored by the six largest audit firms in the UK, and these can be grouped into six broad categories
CPAB – Canada	Professional organisation	Audit committees and audit firms	This was a pilot project without any specific requirements, and most participants tracked AQIs	An exemplary list of 20 AQIs is presented along with their definitions and types

Owner	Background of the owner	Intended user	Transparency (public or private)	Short overview
			in a standalone report, typically produced by the auditor for audit committee	
ICAI – India	Professional organisation	Oversight body and audit firms (for self-evaluation)	No public reporting envisaged	The model suggests scoring criteria for competency bases under three categories: Operations management – Human resource management Strategic/functional management
ACRA – Singapore	Audit oversight body	Audit committees and audit firms	Audit firms are encouraged to share the AQI data privately with audit committees	The Framework comprises seven AQIs, which are to be disclosed at engagement and/or firm-level
IRBA – South Africa	Audit oversight body	Audit committees, audit firms and oversight body	IRBA issued a survey report based on AQI-related information provided by the firms auditing listed companies	The AQIs cover the following thematic areas: independence tenure internal firm quality review processes workload of partners and audit managers span of control technical resources training staff turnover
CAQ – US	Autonomous public policy organization	Audit firms	Firms are encouraged to consider public disclosure	The Framework includes a non-exhaustive list of firm-level AQIs for the six elements of audit quality: leadership, culture, and firm governance ethics and independence acceptance and continuance of clients and engagements engagement team management audit engagement performance monitoring

INITIATIVES IN EU MEMBER STATES

INSTITUTE OF PUBLIC AUDITORS (IDW), GERMANY

In its [position paper](#) (December 2021), the IDW explains what constitutes audit quality from the profession's point of view, and how it can be measured and evaluated. The position paper shows which criteria can be relevant when selecting AQIs to assess the audit quality. In addition, it presents various aspects to be considered when interpreting AQIs.

Finally, it proposes a set of AQIs under the components listed below. The indicators are classified as either firm-related or engagement-related for each component.

Component	AQIs
Quality culture	<ul style="list-style-type: none"> ▪ governance ▪ leadership ▪ professional scepticism & independence
Workforce quality	<ul style="list-style-type: none"> ▪ expertise ▪ industry understanding & experience
Process quality	<ul style="list-style-type: none"> ▪ availability of human and technical resources ▪ involvement ▪ IT systems & audit tools ▪ fit of the audit process ▪ quality management process
Communications	<ul style="list-style-type: none"> ▪ communication with the supervisory body ▪ communication with the management
Cross-divisional AQIs	

Acknowledging the lack of a globally accepted definition for audit quality, the position paper notes that AQIs cannot be limited to quantitative dimensions but should also address qualitative factors.

QUARTERMASTERS, NETHERLANDS

In the Netherlands, the quartermasters, appointed to ensure the audit reform delivery, [proposed](#) (February 2022) 11 quality indicators that were developed upon a public consultation:

Category	AQIs
Audit quality	<ul style="list-style-type: none"> ▪ involvement of external auditor ▪ weaknesses in audits and financial statements ▪ contemporary topics: fraud and continuity
Workforce quality	<ul style="list-style-type: none"> ▪ quality-enhancing measures ▪ quality control systems
Context	<ul style="list-style-type: none"> ▪ culture ▪ audit team turnover ▪ investments in innovative technology ▪ budget overrun ▪ training hours for environmental, social and governance (ESG) matters ▪ client satisfaction

In their proposal, the quartermasters suggest that there is not a single indicator or definition that can provide a profound insight into the audit quality. Hence, consideration should be given to other factors such as the administrative burden, comprehensiveness and comparability regarding each indicator. Once the Dutch Ministry of Finance adopts the proposal, audit firms with a license to perform statutory audits will be obliged to publicly report on these AQIs as from 2023.

The Royal Netherlands Institute of Chartered Accountants (NBA) is going to collect relevant data from the audit firms, and the disclosure will be made through a public dashboard. A specific committee will be formed to monitor the deployment and the update of AQIs, where necessary. The Dutch Authority for the Financial Markets (AFM) will be overseeing the entire process.

THE PORTUGUESE SECURITIES MARKET COMMISSION (CMVM), PORTUGAL

In 2021, the CMVM updated its [AQI model](#) that includes a set of indicators that, together with a quality assessment, may allow to assess the audit quality. The update consisted mainly of fine-tunings to the indicator “hours per audit phase” and some clarification of concepts in relation to the indicators “quality control results”, “experience”, “responsibilities under management” and “team setup”.

The CMVM suggests a transitional implementation whereby the six largest firms auditing PIEs (Group A) were required to report their AQIs (indicators and metrics at firm and engagement level) for 25 group audit engagements starting from 2019. As from 2020, five more firms (Group B) are required to report their AQIs for five group audit engagements each.

The firms’ reporting for both 2019 and 2020 financial statements audits were to be submitted exclusively to the CMVM. The indicators identified by the CMVM are as below:

- team setup
- responsibilities under management
- experience
- training
- staff turnover
- hours per audit phase
- quality control results
- quality control functions

INITIATIVES IN OTHER EUROPEAN JURISDICTIONS

FEDERAL AUDIT OVERSIGHT AUTHORITY (FAOA), SWITZERLAND

The FAOA collects nine audit quality indicators (AQIs) from the five largest audit firms. It uses these primarily to analyse trends, and for its risk assessment and inspection planning. The FAOA provides an overview of the last four years, including the minimum and maximum amounts observed for each AQI, in [its 2021 annual report](#). The indicators are as below:

- annual revenue per audit partner
- non-audit fees to audit fees ratio*
- number of staff per partner
- training hours
- staff turnover in %
- average number of engagement quality control review hours*
- average number of auditor-in-charge hours*
- number of foreign shared service centre hours as a percentage of overall hours at public companies
- number of consultations per public company audit

* to be reported separately for Swiss Market Index (SMI) and non-SMI companies

The FAOA notes that the five largest audit firms in Switzerland use their own AQIs and these are structured in different ways.

FINANCIAL REPORTING COUNCIL (FRC) – UK

[FRC Thematic Review](#) from May 2020 defines AQIs as quantitative and qualitative measures of external audit quality, including both inputs and outputs. The review benchmarks the AQIs monitored by the largest six audit firms in the UK. The AQIs used by the firms are classified as ‘leading’ (before the audit commences), ‘in-flight’ (during the audit) and ‘historical’ (after the audits have happened).

There are nine key messages drawn from this review which concludes that the most common AQIs can be grouped into the categories below:

- people (13 AQIs)
- other inputs (6 AQIs)
- project management (5 AQIs)
- other processes (11 AQIs)
- management initiatives (6 AQIs)
- outcomes (11 AQIs)

There is a variety with regards to selecting AQIs and only three of the 52 indicators were monitored by all of the audit firms within the scope of the review.

According to the FRC, audit committees should use AQIs when appointing their auditor, and to assess quality on an ongoing basis, by benchmarking against other firms. In addition, management and leadership within audit firms should use AQIs to encourage a culture focused on quality. The review suggests that FRC would consult publicly on a core set of AQIs that firms would be required to present in their transparency reports.

In its [3-year plan for 2022-25](#), the FRC commits to continue its work on audit culture and audit quality indicators, describing these as the essential components of understanding how audit quality is improving over time.

INITIATIVES IN OTHER JURISDICTIONS

CANADIAN PUBLIC ACCOUNTABILITY BOARD (CPAB), CANADA

In 2016, the CPAB launched an exploratory AQI pilot project to get feedback on AQIs' usefulness and support broader national and international discussions. The results of the initiative were summarised in [the final report](#) published in 2018. The report provides the following set of AQIs as an example:

Type	AQIs
Engagement team indicators	<ul style="list-style-type: none"> ▪ experience of engagement team* ▪ training and professional development ▪ turnover of the engagement team ▪ partner/manager involvement ▪ partner workload
Audit execution indicators	<ul style="list-style-type: none"> ▪ audit hours by areas of significant risk* ▪ timing of audit execution* ▪ audit progress milestones ▪ technology in the audit ▪ specialist engagement* ▪ service delivery centres
Management indicators	<ul style="list-style-type: none"> ▪ management deliverables* ▪ remediation of control deficiencies ▪ reliance on controls
Firm-level indicators	<ul style="list-style-type: none"> ▪ results of inspections ▪ independence ▪ reputation ▪ tone at the top
Client service indicators	<ul style="list-style-type: none"> ▪ communication with the audit committee ▪ sharing of insights

* AQIs selected by more than 75% of participants in the pilot project

The CPAB notes that there are no silver bullet AQIs and there is a range of perspectives depending on the individual audit committees' unique needs and circumstances.

The report lists the benefits and challenges identified while using AQIs. It also explains the factors to consider when selecting, evaluating and reporting them.

THE INSTITUTE OF CHARTERED ACCOUNTANTS (ICAI), INDIA

The ICAI-India proposed an [Audit Quality Maturity Model](#) (AQMM) as a capacity-building measure in 2021. The initiative's primary objective is to provide an opportunity for audit firms to self-evaluate their maturity level in terms of audit quality. It would be voluntary initially and after the first year of implementation, the ICAI will review the date from which it would become mandatory.

Firms auditing listed entities, banks and insurance companies are in the scope of the model. ICAI suggests that the maturity level should not be publicised or mentioned by audit firms in the public domain. The model includes scoring criteria for the following competency bases:

Competency basis	AQIs
Practice management – operation	<ul style="list-style-type: none"> ▪ practice areas of the firm ▪ workflow - practice manuals ▪ quality review manuals or audit tool ▪ service delivery - effort monitoring ▪ quality control for engagements ▪ benchmarking of service delivery ▪ client sensitisation ▪ technology adoption ▪ revenue, budgeting & pricing
Human resource management	<ul style="list-style-type: none"> ▪ resource planning & monitoring as per the firm's policy ▪ employee training & development ▪ resources turnover & compensation management ▪ qualification skill set of employees and use of experts ▪ performance evaluation measures carried out by the firm (KPIs)
Practice management - strategic/functional	<ul style="list-style-type: none"> ▪ practice management ▪ infrastructure – physical & others ▪ practice credentials

The outcome of the self-evaluation would be a score between 0 and 600, indicating the maturity level of the audit firm in terms of audit quality.

ACCOUNTING AND CORPORATE REGULATORY AUTHORITY (ACRA), SINGAPORE

In 2015, the ACRA introduced an Audit Quality Indicators Disclosure Framework to enhance discussions between audit committees and audit firms on elements that contribute to or are indicative of audit quality. In 2020, ACRA updated the framework which is available for voluntary adoption by audit firms.

The [revised Framework](#) comprises seven AQIs, which are to be disclosed at engagement and/or firm-level as follows:

- audit hours: time spent by audit team members during each audit phase
- experience: years of audit experience and industry specialisation
- training: average training hours and industry-specific training
- inspection: results of external and internal inspections
- quality control: headcount in quality control functions
- staff oversight: staff per partner/manager ratios
- attrition rate: degree of personnel losses

Under the Framework, audit firms are encouraged to share the AQI data privately with audit committees after each annual audit is completed and when the audit committee considers a change in auditor.

The ACRA has also issued [guidance for audit committees](#) to explain the AQIs and how audit committees should interpret them. The ACRA will be performing sample checks to ensure that the AQI data provided by audit firms are prepared in accordance with the framework.

INDEPENDENT REGULATORY BOARD FOR AUDITORS (IRBA), SOUTH AFRICA

The IRBA published a [survey report](#) in 2021 on AQIs. Firms auditing listed companies were requested to submit AQI-related information and the report describes the results of the information submitted, under the five broad thematic categories:

Category	AQIs
Independence	<ul style="list-style-type: none"> ▪ non-audit fees (%) - as a percentage of the total audit fees billed to audit clients ▪ fee recovery (%) - audit fees billed as a percentage of the total audit fees internally charged
Tenure	<ul style="list-style-type: none"> ▪ firm (years) - average number of completed years as the audit firm for the audit client ▪ partner experience (years) - average tenure as an engagement partner
Internal firm quality review processes	<ul style="list-style-type: none"> ▪ engagement quality review partner hours and engagement quality review team hours (%) ▪ firm review processes ▪ internal review results (%) ▪ partner coverage (%)
Workload of partners and audit managers	<ul style="list-style-type: none"> ▪ engagement partner role (%) ▪ manager supervision (%)
Other	<ul style="list-style-type: none"> ▪ span of control: professional staff (ratio) ▪ technical resources: partner (ratio) ▪ training (hours per person) ▪ staff turnover (%)

The report argues that high or low ratios may mean different things to different users, and they may be interpreted differently when correlated with other statistics. Thus, the context of the AQIs should always be carefully considered.

The report presents comparisons across audit firms on an anonymous basis. The IRBA relies on AQIs as an information source for business intelligence gathering and risk-based selections, as part of its inspections process. They also help the IRBA monitor overall trends related to audit quality.

CENTER FOR AUDIT QUALITY (CAQ), US

The CAQ's [Audit Quality Disclosure Framework](#) was developed in consultation with a range of CAQ member firms. It aims to aid audit firms as they develop (or consider developing) their transparency or audit quality reports. The Framework, which adheres to three key principles:

- is voluntary and illustrative
- is flexible, giving firms the ability to tailor the information that is most relevant
- relates to disclosure of a system of quality control at a firm level, rather than at the engagement level

Based on these overarching principles, the Framework provides points of focus and certain examples of firm-level AQIs for the six elements of audit quality listed below:

- leadership, culture, and firm governance
- ethics and independence
- acceptance and continuance of clients and engagements
- engagement team management
- audit engagement performance
- monitoring

The CAQ notes that stakeholders may have different views on how to measure and communicate information about audit quality. Accordingly, no single metric or set of metrics should be viewed as the sole determinant of audit quality. However, a combination of metrics, if taken as a whole and supplemented with robust discussion, may provide useful information and additional transparency into a firm's quality management systems.



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