Audit Committees and Audit Quality:
Trends and Possible Areas for Further Consideration

1 Introduction

The audit committee plays an important role in oversight of audit quality and financial reporting. The audit committee may also oversee the risk management system of a company, including financial, operational and compliance risks. Concerns as to the impact of ineffective audit committees in the financial reporting failures at the turn of the 21st century have resulted in tighter regulatory and monitoring frameworks for audit committees across the globe. Even though the importance of audit committees is widely acknowledged, one study - by the University Utara Malaysia - has demonstrated that an independent audit committee is often not opted for voluntarily. Instead, the study noted a trend to have audit committees operate only in accordance with the minimum requirements as prescribed by local law.[1]

Direct supervision on audit committees by audit regulators is uncommon. Many IFIAR members do not have jurisdiction over audit committees or only in a monitoring capacity (EU). At the same time, audit regulators (whether they have jurisdiction or not) and audit committees share a central role in the support of audit quality and might help to improve audit quality by working together, *e.g.* by sharing information. This IFIAR paper provides information with the aim of developing a better understanding of how audit committees function under existing requirements. It also raises questions and identifies areas for further consideration that might provoke discussion among interested parties, such as investors, audit committee members, (audit) regulators and policymakers and also lead to improvement in individual jurisdictions, *e.g.* on whether audit regulators should share their inspection findings directly with audit committees. As such, the paper is intended to provide food for thought for those with jurisdiction over audit committees and all other interested stakeholders. This paper is not binding, nor an IFIAR position paper.

[1] Strengthening Corporate Governance Through An Audit Committee: An Empirical Study, article in Wulfenia 23(2):2-27, February 2016, https://www.researchgate.net/publication/293826024_STRENGTHENING_CORPORATE_GOVERNANCE_THROUGH_AN_AUDIT_COMMITTEE_AN_EMPIRICAL_STUDY

The purpose of this paper is to describe the state of play with respect to existing audit committee requirements around the world. In doing so, the paper draws heavily on a recent survey from the International Organization of Securities Commissions' ("IOSCO"). Secondly, the paper asks questions and identifies areas for further consideration by interested parties, both those IFIAR Members with jurisdiction over audit committees or in a monitoring capacity, as well as other interested stakeholders. For audit regulators that do not have jurisdiction over audit committees, the paper is for information purposes only.

The paper is structured as follows: Chapter 2 provides an executive summary. Chapter 3 elaborates on the results from the IOSCO Survey Report on Audit Committee Oversight of Auditors ("the 2016 Survey") on requirements related to audit committees. Chapter 3 also includes observations about the operation of audit committees in various jurisdictions around the world. Based on the information provided in the previous chapter, Chapter 4 raises various questions related to the oversight role of audit committees and their interaction with audit regulators, and also identifies areas for further consideration that might further enhance audit quality. Chapter 5 offers some brief concluding remarks.

Disclaimer

The content of this paper, including the questions raised and areas for consideration suggested in this paper, reflect the views expressed by some, but not necessarily all, of the Members of IFIAR. They are not intended to include, or reflect, any or all the views of individual Members. Nothing in this paper is binding on any Member nor gives rise to any legal rights or obligations. Members participate in IFIAR in accordance with their respective legal and policy frameworks, which are in no way affected by anything in this paper.

2 Executive Summary

Audit committees play an important role in audit quality oversight and in improving audit quality globally. A recent IOSCO survey of audit committee requirements around the world demonstrates that there is much common ground with respect to such requirements.

For example, in many jurisdictions:

- Audit committees (or some similar governance entity) are required within listed companies, and there are also requirements regarding the independence, special skills and expertise of audit committee members;
- The audit committee is responsible for or should at least play an active role in the selection of the external auditor, determination of the audit fees and the periodic assessment of auditor performance;
- The audit committee should set the policy for and monitor the provision of non-audit services by the auditor, including specific tax or advisory services to the audited entity; and
- Effective engagement and communication between the audit committee and the auditor is encouraged.

This paper also raises questions and identifies areas for further consideration that could enhance the role of audit committees in improving audit quality. For example, the following areas might benefit from further consideration, discussion and research by regulators, audit committees, shareholders and audit firms:

- The desirability of criteria that define and determine the independence, special skills and expertise of audit committees.
- To enable the audit committee to make more appropriate assessment of the auditor's performance, the utility of:

    - having a set of Audit Quality Indicators ("AQIs") which audit committees could use to engage auditors in audit quality matters;
    - asking audit firms and audit committees to consult with each other regarding the findings by the independent audit regulator of the reviews of the quality of statutory audits;
    - providing more detailed expectations for periodic assessments of auditor performance; and/or
    - asking audit committees to make use of other sources of information besides their own experiences and information from the company's management, which may not always be complete and objective.

- Engaging shareholders in auditor selection.
- Involving investors with audit committees as a way to incentivize audit firms to sharpen their focus on audit quality.
- How communications from audit regulators, the audit firms and shareholders to the audit committee can serve to improve audit quality.
- The use of a "comply or explain" procedure in carrying out various responsibilities of the audit committee, for example when an audit failure is exposed

The following chapter reviews the IOSCO Survey on requirements related to audit committees and provides a number of observations about the operation of audit committees in various jurisdictions around the world.

3 IOSCO's Survey provides a good starting point for understanding existing requirements for audit committees and identifying possible areas for further consideration

In 2016, the Audit Quality Task Force ("AQTF") of IOSCO's Board surveyed its ordinary members to gain a better understanding of the current requirements of its members related to the audit committee's oversight of the auditor and the audit process of publicly listed entities in IOSCO member jurisdictions ("the 2016 Survey").[2] These requirements include both existing legal and regulatory requirements, as well as soft law requirements, such as self-regulatory codes or best practices documents. In total, 47 IOSCO members took part in the survey.[3] The core areas covered by the 2016 Survey are the following: Audit Committee Requirements; Selection of the External Auditor and Fee Determination; Audit Committee's Role and requirements to Oversee the Audit and the Auditor; Periodic Assessment of auditor performance; Auditor's Communication with the Audit Committee; and Audit Committee Reporting to Shareholders.

A comparison of the 2016 Survey with IOSCO's previous survey of audit committee requirements in 2004 ("the 2004 Survey") illustrates that audit committees have been established in a growing number of jurisdictions. It indicates a promising progress which is welcomed by IFIAR. The information provided by the 2016 Survey have also helped in the identification of possible areas for further consideration related to audit committees.

3.1 Audit committees often require independence, special skills and expertise

Most of the responding jurisdictions in the 2016 Survey require an audit committee or a committee with similar functions. In all jurisdictions that have such a requirement, it is compulsory that at least one audit committee member is an independent non-executive director. Some require more than one, or all, audit committee members to be independent. The respondents reported various criteria which they apply to determine independence. Some take an objective approach (*e.g.* by considering share ownership percentage), while others take a more subjective approach (*e.g.* whether the audit committee member is independent of management and free from any business or other relationship that could interfere with the exercise of independent judgement or the ability to act in the best interest of a publicly listed entity). In addition, some jurisdictions limit the maximum total term for an audit committee member's (re-)appointment. These terms normally range from 6 to 12 years and may in some cases be aligned with other corporate governance requirements.

[2] http://www.iosco.org/library/pubdocs/pdf/IOSCOPD531.pdf
[3] Argentina, Australia, The Bahamas, Belgium, Brazil, Canada, Chile, China, Czech Republic, Denmark, Dominican Republic, El Salvador, France, Germany, Greece, Hong Kong, Hungary, India, Ireland, Israel, Jamaica, Japan, Lithuania, Luxembourg, Malawi, Malaysia, Mauritius, Mexico, The Netherlands, Oman, Pakistan, Poland, Portugal, Russia, Slovenia, Spain, Sri Lanka, Republic of Srpska, Sweden, Switzerland, Chinese Taipei, Thailand, Tunisia, Turkey, United Arab Emirates, United Kingdom, United States of America.

In the vast majority of the responding jurisdictions, one or more member(s) of the audit committee must possess special skills or experience. However, there is not a uniform approach as to whether the requirement is applicable to one member, several members, or all members of the audit committee. A limited number of jurisdictions apply incremental requirements only to the chair of the audit committee.

Independence
Ensuring the independence, objectivity and professional scepticism of the audit committee can be facilitated, for instance, by requiring the chair as well as the majority of the audit committee to be independent. Such a practice is in place in a number of jurisdictions.

Observed practice in many jurisdictions

Before a former audit practitioner can become an audit committee member, full departure and financial separation from the audit firm is required. Stock exchange listing rules require that the publicly listed entity itself establish clear hiring policies for employees or former employees of the independent auditor. It is also observed that further restrictions apply in the auditing and ethics standards.

Special skills and expertise
Specifying the required skills and expertise of audit committee members can contribute to the effectiveness of the audit committee. The increasing complexity of businesses, financial reporting, internal controls and the audit has an impact on both the scope and nature of the responsibilities of the audit committee. Therefore, it is important that the individual audit committee members possess appropriate expertise. Furthermore, the collective competence of an audit committee should be such that it is able to effectively carry out its responsibilities. Thus, it is important that the audit committee as a whole possesses the appropriate skills needed to carry out its work in a responsible manner.[4] Various stakeholders have emphasized the benefit of an audit committee composed of members with diverse experience and expertise and encourage a complement of financial and non-financial expertise to enhance the objectivity and scepticism of committee members.[5] In considering financial expertise, there should not be an undue emphasis on qualifications, but current and relevant experience should also be considered, for instance by having a background as a
Chief Financial Officer (CFO).

Chair
The importance of strong leadership qualities for the chair of the audit committee has been emphasized by various commentators.[6]

[4] Accountancy Europe recommendation for improvements of audit committees no. 4 http://www.accountancyeurope.eu/wp-content/uploads/Discussion_Paper_on_Audit_Committees_120615.pdf
[5] Global Observations on the Role of the Audit Committee, A summary of Roundtable Discussions http://thecaq.org/sites/default/files/globalobservationsontheroleoftheauditcommittee.pdf
[6] Global Observations on the Role of the Audit Committee, A summary of Roundtable Discussions http://thecaq.org/sites/default/files/globalobservationsontheroleoftheauditcommittee.pdf

3.2 The audit committee often plays an active role in the selection of the external auditor and in fee determination

The audit committee is involved in the initial selection and the subsequent re-appointment of the external auditor in the vast majority of responding jurisdictions in the 2016 Survey. They are either directly responsible or they are involved by means of making a recommendation to the board of directors (or equivalent body). For instance, the EU audit reform legislation requires that the audit committee be responsible for auditor selection procedure and also define the selection procedure.[7] On the other hand, the audit committee is often *not* involved in the determination of the audit fee According again to the 2016 Survey, in only some of the reporting jurisdictions is the audit committee required to make a recommendation or assessment of the audit fee for the consideration of the board of directors and in only a minority of the reporting jurisdictions is the audit committee directly responsible for the determination or approval of the audit fee, without further consideration by the board of directors.

Observed practice in many jurisdictions
The audit committee, in its capacity as a committee of the board of directors, is directly responsible for the selection and re-appointment of the auditor.

Quality First

It is a widely accepted view that it is not appropriate for the audited entity's management to appoint its own auditor. The selection of the auditor should be based more on the quality of the auditor than on fee considerations. In cases where the selection process is determined or significantly influenced by audit committees, this generally results in a more in-depth external audit (*e.g.* lower materiality threshold, greater degree of professional scepticism). It has also been suggested that auditors should not accept engagements where the audit committee is not leading the selection process.

In addition, it has also been suggested that, given the significance and complexity of the selection of an auditor, and recognizing that investors are the ultimate clients for a statutory audit, investors should be engaged in the selection process for the auditor. The audit committee could, for instance, include shareholder views and perceptions in risk indicator analyses. Moreover, by not including observations and perceptions from investors in the selection and evaluation of the auditor, investors may build in extra cost of capital for the audited entity.[8] A recent investor perception study carried out in Singapore also indicated that investors would like to engage with audit committees more and would like audit committees to explain to them the basis for selecting auditors.[9] This also comes from notes on good practice on audit tenders published recently by the Financial Reporting Council (FRC)[10].

[7] Directive 2014/56/EU − Article 39.6 (f), Regulation 537/2014 − Article 16
[8] Panel session with the Advisory Group to the IOSWG, IFIAR plenary meeting, 20 April 2016
[9] ACRA-SGX-SID Investor Perception Study https://www.acra.gov.sg/Into_the_Minds_of_Investors/
[10] Audit Tenders Notes on Best Practice, FRC, February 2017, https://www.frc.org.uk/Our-Work/Publications/Audit-Quality-Review/Audit-Tenders-notes-on-best-practice.pdf

Once the selection of the auditor is made, the determination of the audit fee can be the outcome of a careful consideration of different factors. Since investors pay the auditor's fee in their capacity as shareholders of the audited entity, this is often presented as the reason why the audit committee should actively engage with investors over the level of the fee. Ultimately, the fee should be dependent on the scope and quality of the audit and investors are not likely to accept a fee level that only delivers a low quality, high risk audit.

3.3 The role of the audit committee with respect to auditor independence and the provision of non-audit services by the auditor, including tax or advisory services, to the audited entity

In almost every reporting jurisdiction in the 2016 Survey, the audit committee is responsible for assessing and ensuring the independence of the auditor. In most cases, this assessment occurs only upon the appointment and re-appointment of the auditor. Many jurisdictions also noted that the applicable audit standards require the auditor to report to the audit committee whenever his or her independence is potentially impaired and to explain the safeguards in place to protect independence. In addition, in order to ensure auditor independence, the vast majority of the respondents prohibit the provision of certain non-audit services or, alternatively, require approval for certain non-audit services by the audit committee.

3.4 Periodic assessment of auditor performance is an important task of the audit committee in many jurisdictions

In approximately three quarters of the responding jurisdictions in the 2016 Survey, audit committees are responsible for periodically assessing auditor performance. In the majority of those jurisdictions, however, the specific factors to be considered are not set out in the relevant laws and regulations. Most audit committees choose to take into account the overall effectiveness of the audit process and their experience with the auditors by looking at quality and service.

Observed practice in many jurisdictions

Audit committees are required to establish and subsequently monitor a mechanism by which the audit committee can be alerted to complaints related to accounting, internal controls or auditing matters. Such a complaint monitoring mechanism (e.g. a whistle-blower hotline) can be used to monitor auditor performance, in addition to management's performance.

Assessing audit quality can be a challenge for the audit committee. For example, research by the Dutch Authority for the Financial Markets ("AFM") revealed that audit committees in the Netherlands tend to use their own experiences and information from the company's executive board for this purpose. They have limited access to or awareness of the findings of the internal quality reviews carried out by the audit firm on audit files or of the findings of reviews of the audit firm by the AFM or other supervisors.

On the other hand, drawing on evidence from own enquiries of the audit committee is also very valid. UK's FRC has developed a practice aid at the request of and with the input of audit committee members, which asked for guidance as to how to structure and obtain evidence to support their assessment of the external audit. The practice aid sets out how audit committees might obtain such evidence in the course of undertaking normal oversight of the financial reporting process; including drawing on the audit committee's observations of, and interactions with, the auditors and through interactions with management, company personnel and from external parties such as regulators.[11]

In recent times, greater emphasis has also been placed on measuring audit quality through the development of audit quality indicators ("AQIs") by some regulators, oversight bodies, professional bodies and audit firms[12]. Such indicators may help audit committees to make a more objective evaluation of the auditor's performance on audit quality, although it is recognised that selection of appropriate AQIs is key and that a range of more subjective factors will also be relevant.

Observed practice in the European Union

Jurisdictions that advocate transparency to all stakeholders require a Transparency Report. Recent European Audit Regulation contains specific requirements for the statutory audit of Public Interest Entities (PIE) and requires the auditor to prepare an additional report for the audit committee. In this additional report, the auditor explains the results of the statutory audit performed and includes information with respect to his communication with the audit committee, his findings in relation to (suspected or identified) non-compliance, to the extent these findings are considered to be relevant to the ability of the audit committee to perform its duties.

[11] Audit Quality Practice Aid for Audit Committees, FRC, May 2015, https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Audit-Quality-Practice-Aid-for-Audit-Committees.pdf
[12] Accountancy Europe's Overview of Audit Quality Indicators Initiative: http://www.accountancyeurope.eu/wp-content/uploads/1607_Update_of_Overview_of_AQIs.pdf

3.5 Effective communication between the auditor and the audit committee is widely required

In most of the responding jurisdictions in the 2016 Survey, the auditor is required to communicate with the audit committee. The level of detail and formalisation of requirements on communication varies widely across jurisdictions. Some respondents require an auditor to report on details and insights that are not provided in the ordinary audit report, such as the nature and extent of the auditors public reporting.

Observed practice in many jurisdictions

There are audit committee networks in which audit committees share (best) practices and Audit Committee Institutes that provide guidance and various resources in order to update and refresh the skills and knowledge of audit committees.

In addition, in some jurisdictions, which are nearly all European, the audit committee receives a report about the governance of the audit firm and elements of its system of quality control for financial statement audits.

The above suggests that the auditor's communication with the audit committee can be an important part of the audit process and that enhanced communication between the auditor and the audit committee can be beneficial to both parties in their respective duties. Moreover, communication between the auditor and the audit committee can facilitate the audit committee's periodic assessment of auditor performance because it reduces the information gap.

Observed practice in some jurisdictions

While not an explicit requirement for the audit committee to meet with the auditor without management present, a private meeting at yearly intervals is common practice.

To assist audit committees in communicating with auditors, some regulators provide practice aids or questions.[13] These offered a model and inspiration for annex 1 which provides various questions that audit committee members may want to ask their auditors.

[13] For instance a) the PCAOB Audit Committee Dialogue, May 2015, https://pcaobus.org/sites/digitalpublications/Pages/auditcommittees.aspx, and the b) FRC Audit Quality Practice aid for audit committee, May 2015, https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Audit-Quality-Practice-Aid-for-Audit-Committee-(1).pdf

Observed practice in a number of jurisdictions

Examples of guidance provided by some regulators on how audit committees might conduct their assessment of the effectiveness of the external audit include:

- *highlighting factors related to audit quality that audit committees could consider when making their assessment and steps they could take in doing so;*
- *describing possible inputs (sources of evidence) for the audit committee's assessment;*
- *discussing the key professional judgments the auditor makes during the audit and how audit committees might assess them; and / or*
- *describing three elements that audit committees can consider when evaluating the quality of their auditor: (i) Skills, Character and Knowledge; (ii) Mindset and Culture; and (iii) Quality Control.*

3.6 Communication from the audit committee to the shareholders

According to the 2016 Survey, half of the responding jurisdictions have established minimum requirements for audit committees to report to shareholders on the oversight of the auditor.

Shareholders have an (increasing) interest in understanding the role and performance of the auditor. By involving investors via the audit committees, the audit firms may feel an extra incentive to sharpen their focus on audit quality.

Observed practice

For those jurisdictions with audit committee reporting requirements to shareholders, many of the respondents noted that the requirements include the following disclosures:

1. *approach to appointing or re-appointing the auditor;*
2. *how the audit committee assessed threats to auditor independence;*
3. *work performed by the audit committee in overseeing the auditor; and*
4. *how the audit committee assessed the effectiveness of the audit process.*

4 Questions and Possible Areas for Further Consideration

The previous chapter discussed the results from the IOSCO Survey Report on Audit Committee Oversight of Auditors ("the 2016 Survey") on requirements related to audit committees, and also provided a number of observations about the operation of audit committees in various jurisdictions around the world. Based on the information in the previous chapter, this chapter poses various questions and identifies possible areas for further consideration about how to improve the oversight role of audit committees in order to further enhance audit quality globally. Many of the ideas presented below have previously been the subject of discussion in various jurisdictions around the world and will therefore benefit from additional discussion at the international level by interested parties, such as investors, audit committee members, (audit) regulators and policymakers as well as from academic research.

A. In order to enhance audit quality, to what extent should audit committee requirements address independence and special skills and expertise?

Independence

As can be noted from the results of the 2016 Survey, it is important for the audit committee to be independent. However, there are various criteria that may be applied in order to define and determine the independence of audit committee members. Would it be worthwhile to further explore which criteria should define and determine independence, and how could such criteria serve to enhance audit quality? Examples of such criteria that have been considered elsewhere but might benefit from additional discussion are:

- the maximum term that an audit committee member may serve in his or her role;
- the relationships and other functions the audit committee member is allowed to maintain while serving on the committee; and
- the maximum share ownership percentage the audit committee member may hold, either directly or indirectly through the entities the member represents or has links with.

Special skills and expertise

In the vast majority of the responding jurisdictions in the 2016 Survey, one or more member(s) of the audit committee must possess special skills or experience relevant to the company in question. The skills or expertise required for the individual member and the audit committee collectively vary across jurisdictions.To what extent might the following criteria serve to enhance audit quality?

- Required "competencies" for an audit committee member. Examples could be a university degree in economics or finance, a professional qualification from a relevant professional organisation or significant professional and practical experience in accounting/auditing.[14]
- Required qualifications, for instance a background in finance or qualifications in the field of IT.
- A validity period of such qualifications and a continuing education system to ensure that members stay up to date with the latest developments in their field.
- The composition of the audit committee and whether only non-executive directors should act as audit committee members. Such a requirement could include the exclusion of management including the CFO of the company from the audit committee.[15]

B. What factors should be taken into account in the periodic assessment of the auditor's performance?

In the majority of jurisdictions taking part in the 2016 Survey, the audit committee assesses the auditor's performance periodically. To what extent would it be beneficial for audit committees, in making their periodic assessment, to:

- have a framework of Audit Quality Indicators (AQI's) which audit committees can use in their discussion with auditors on audit quality. It is recognised that the selection of appropriate AQI's is key, however this discussion is still controversial and pending. Therefore, a range of more subjective factors may remain relevant;
- ask audit firms for their findings in the internal quality reviews. The audit committee could also request for the quality reviews of statutory audits by the independent audit regulator. These findings could be consequently discussed within the audit committee and be reflected on in future engagements and evaluations;
- provide a more detailed expectation for the periodic assessments of the auditor performance; and
- make use of sources of information that supplements to their own experiences and information provided by the company's executive board which potentially provides more objectivity.

The periodic assessment of the auditor by the audit committee provides an opportunity to review the quality of the audit being produced by the auditor. If such assessment only occurs on a periodic basis, the auditor could be expected to provide more attention to quality only at the time of the assessment. In between these periodic assessments, however, the auditor might feel less pressure from audit committees to provide high quality audits. This leads to the following questions:

[14] Accountancy Europe recommendation for improvements of audit committees no. 5 http://www.accountancyeurope.eu/wp-content/uploads/Discussion_Paper_on_Audit_Committees_120615.pdf
[15] Accountancy Europe recommendation for improvements of audit committees no. 2 http://www.accountancyeurope.eu/wp-content/uploads/Discussion_Paper_on_Audit_Committees_120615.pdf

- Would the auditor be more likely to deliver more consistently a high quality audit if audit committees were to demonstrate a more continuous interest in the quality of an audit and the outcome of a root cause analysis, for example, by putting, each audit on the agenda of the annual general meeting of the audited entity?
- What could be done to provide impetus to the audit committee to carefully monitor the audit and the auditor to ensure that deficiencies were prevented, or if not, at least exposed at an earlier stage?
- In the case of an audit failure without an appropriate remediation plan, what should be the response of the audit committee?
- Should it recommend not to reappoint the auditor or, as a last resort, propose to end the audit engagement with the auditor or the audit firm in question, or if it chooses not to do so, should it provide a reasonable explanation for retaining the auditor?
- In other words, should an internal procedure or a “comply or explain” practice be considered for the (dis)continuity of the auditor or audit firm by the audit committee in case of, for example, an audit failure or an ineffective root cause analysis?

C. How can communications with the audit committee serve to improve audit quality?

The 2016 Survey revealed that, in most responding jurisdictions, audit committees are responsible for periodically assessing the auditor’s performance without being subject to specific requirements regarding the factors that they need to consider in making this assessment. It may be of interest to further explore ways in which various communication channels could be beneficial to the audit committee’s efforts to oversee the quality of an audit.

Communication between the audit regulator and the audit committee

It is a practical reality that audit regulators cannot draw statistically significant conclusions on the full set of audits performed by a large global audit firm. Generally, a risk-based approach is applied. Inspections findings which point at inconsistent quality are representative for internal control weaknesses and lack of duty of care applied within an audit firm. Checks and balances being absent or dis-functioning, will have a potential negative impact on any engagement. It can therefore be considered valuable for all quality assessments by audit committees to discuss the findings of the independent audit regulator(s) and risk mitigating actions proposed/taken, even though an audit was not selected by the audit regulator. This leads to the following questions:

- Would it be beneficial if audit regulators were to share their inspection findings directly with audit committees? If yes;
- Would this provide audit committees with a useful source of objective information about the performance of the auditor and would the audit committee be better positioned to further improve its assessment function? If so;

- Should such information be disclosed for an individual audit, or at a higher level about the firm itself, and not related to any specific issuer audit?

Communication between the audit firm and the audit committee
If audit firms were to share their inspection results as well as information on their quality control function with the audit committee would this reduce the information gap and better position the audit committee to further improve its assessment function? Would the external auditor provide the audit committee with useful insights when they meet more frequently?

Communication between the shareholders and the audit committee
Would some form of communication from the audit committee to the shareholders regarding the audit and the auditor's performance be worthwhile? If so, should it be encouraged through a 'comply or explain' reporting approach?

Communication between the internal auditor and the audit committee
Would the audit committee benefit from receiving information about the activities of the internal auditor – mainly focusing on the effectiveness of the internal risk management and control systems – including the internal auditor's interactions with and views about the audit firm?

5 Conclusion

The intention of this paper has been to provide information about the current role played by, and existing requirements relating to, audit committees in various jurisdictions around the world in order to contribute to a better understanding of these matters by interested parties and to enhance awareness about the potential impact of audit committees on audit quality globally. The paper also raises questions and identifies areas for further consideration by investors, audit committee members, (audit) regulators and policymakers with respect to how the audit committee might play an even greater role in improving audit quality in the future than is currently the case. Further research, including from academia, is encouraged to provide insights about audit committee practices and their influence on audit quality.

Annex 1 – Possible Questions for Your Auditor (not limitative)

Materiality
Judgments about materiality are critical to the audit. The auditor has to determine an 'overall' level of materiality, this is essentially a judgment the auditor makes about the level of errors (misstatements) that would render the financial statements unacceptably incorrect. In planning the audit, materiality, taken together with the risk assessment, drives the extent and nature of the audit work. **Failure to make appropriate materiality judgments, or to update materiality during the audit, reduces audit quality by driving an inappropriate work effort, even if the auditor's risk assessment is valid.**
Examples of matters audit committees may consider when assessing the auditor's judgments about materiality: • What are the bases for the materiality levels set, and how appropriate are those benchmarks used by the auditor in determining materiality levels? How do these reflect the needs and expectations of users? • What is the overall performance materiality and what factors were taken into account in determining it? • How will materiality levels affect the scope and level of audit work? Is the auditor applying their informed judgment or adopting a limit in the audit firm's methodology with little or no judgment? What are the reasons for any change in materiality levels, and how does this affect the level of auditor's work? • What is the auditor's approach to qualitative aspects of materiality, for example, how does the auditor evaluate misstatements in narrative disclosures? • Have materiality levels been adjusted in the light of significant events arising near the year end and/or actual results that are very different from plan? • At what level are identified misstatements reported to the audit committee and why?

Nature and extent of audit work
The auditor has to make judgments about the nature and extent of audit work that needs to be performed, so that it is responsive to the risks identified, and takes account of the materiality levels set. **Designing an appropriate response to the risks identified requires the auditor to use their auditing skills to design tests of the financial reporting processes and controls and/or the reported financial information that will enable them to evaluate whether the identified risks have materialised.**
Examples of matters audit committees may consider when assessing the auditor's judgments about audit testing included: • Has the auditor been able to articulate their testing strategy in a manner that is understandable? • Are there specific areas of risk that are of greater concern to the audit committee, where they might want to probe the auditor's judgments more deeply? • To what extent does the auditor intend to rely on the effectiveness of internal controls? Is this consistent with the audit committee's understanding of the reliability of the company's relevant internal controls? • Can the auditor clearly explain their testing strategy in relation to fraud, revenue recognition, laws and regulation, and management override of controls?

Auditing estimates, including fair value measurements, and disclosures

Accounting estimates warrant significant audit attention because they involve subjective factors and judgments, which make them susceptible to management bias and material misstatement. For instance areas such as revenue, allowances for loan losses, inventory reserves, fair value measurements, and tax-related estimates.

Auditors also need to pay close attention to the identification and evaluation of indicators of asset impairments, particularly when economic conditions deteriorate. They need to pay close attention to the related controls.

Auditors have to make sure that they evaluate the available information that appeared to be contrary to the information management used to support its estimates, including, for example, cash flow forecasts used in the budgeting process that differ from those used to determine the fair value of intangible assets for purposes of assessing whether those intangible assets or goodwill is impaired.

Examples of matters audit committees may consider when assessing the auditing estimates, including fair value measurements, and disclosures:

- What does your auditor do to obtain a thorough understanding of the assumptions and methods the company used to develop critical estimates, including fair value measurements?
- What is your auditor's approach to auditing critical accounting estimates, such as allowances for loan losses, inventory reserves, and tax-related estimates?
- Will your engagement team use its firm's in-house valuation specialists? If so, how are the specialists integrated into the engagement team? How are specialists supervised, and how are significant issues they identify resolved? If the firm does not have in-house valuation specialists, does the firm engage external specialists to assist the auditor with their audit of complex estimates?

Referred work in cross-border audits

When auditing a multi-national company, the signing (or principal) auditor usually refers portions of the audit work (so-called "referred work") to other firms, which are usually affiliated firms that are located in the foreign countries where the company has operations. In such cases, the quality of the referred work can be critical to determining whether the financial statements are free of material misstatement and, if required, whether the company's internal control over financial reporting is effective.

Examples of matters audit committees may consider when assessing referred work in cross-border audits:

- How does the engagement partner assess the quality of the audit work performed in other jurisdictions?
- How does your auditor review the work? Does your auditor visit other countries to review the audit work done there? What steps does your auditor take to make sure that the work is performed by persons who understand the applicable audit and accounting standards and financial reporting requirements?
- As part of planning the audit, does your auditor consider performing additional steps if the referred work is in an area that has recently been the subject of a significant number of inspection findings on your auditor by your audit regulator?

Quality reviews by audit regulator and internal reviews
Examples of questions audit committees can ask their auditor: • Were the firms that participate in the group audit recently inspected by your audit regulator? If yes, what does the engagement partner know about the results? • To what extent are the audit quality issues identified by the audit regulator in their public reports related to the testing strategy and what remedial action has the auditor considered?

About IFIAR

Established in 2006, the International Forum of Independent Audit Regulators (IFIAR) comprises independent audit regulators from 52 jurisdictions representing Africa, North America, South America, Asia, Oceania, and Europe. The following organisations are observers of IFIAR meetings: Basel Committee of Banking Supervisors (BCBS) European Commission, Financial Stability Board (FSB), International Association of Insurance Supervisors (IAIS) International Organization of Securities Commission (IOSCO), Public Interest Oversight Board (PIOB) and the World Bank. Dedicated to serving the public interest and enhancing investor protection, IFIAR provides a platform for dialogue and information-sharing regarding audit quality matters and regulatory practices around the world, and promotes collaboration and consistency in regulatory activity. For more information about IFIAR, please visit www.ifiar.org.