



The Future of Audit

Perspectives on how the audit
could evolve

July 2019

About this paper

Through a programme of large events and small gatherings, in person and online, PwC has brought together a wide range of organisations and individuals who each have a stake in the effectiveness of the audit. In sharing their time and perspectives, those who participated in this initiative have helped inform our own thinking about the audit of the future. Our ambition is to share their views and opinions more widely through this paper and to contribute to the lively and ongoing debate.

This document is set out in two main parts. The first part, *Perspectives from stakeholders of the audit*, reflects the views expressed by stakeholders throughout our programme of engagement, which do not necessarily reflect PwC's views. The second part, *PwC's perspective*, provides our perspective on and response to what we heard.

This document is not intended to address the specific questions that have been asked about the structure of the industry and how it is regulated, both of which are the subject of public reviews and on which PwC's position has been captured in formal submissions.

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Foreword



The audit matters, and it needs to evolve. That's the message we've heard around the country over the past several months as we opened up a public discussion on the future of the audit. As a profession, we are at a watershed moment, and at PwC we recognise the need for change if we are to be sufficiently responsive to the evolving needs of stakeholders and re-establish trust in the quality of the audit.

It is clear from the challenge and scrutiny in the public arena that the audit has not kept pace with society's expectations; there have been well-documented cases in which audit quality has fallen short of the standards expected. Those of us in the audit profession must acknowledge that our critics have raised valid concerns. And at PwC we are committed to change so that our work as auditors remains relevant and valuable. We are working hard to ensure that the quality of our audits continues to improve, and have put in place a substantial programme of measures to support this.



We know there are no easy answers and that no single participant can resolve the challenge.

But improving the audit alone will not be enough—a more fundamental review of the entire corporate reporting system will be required to ensure that stakeholders can have confidence in the information they need for decision making.

That's why we engaged with hundreds of people who have a stake in the audit's future as an important part of that system. By sharing what we heard, alongside our assessment of where change could be most usefully made, we hope this paper will make a valuable and timely contribution to the ongoing debate about the future of the audit and the profession at large.

Ensuring that the audit is fit for the future matters: it plays a crucial role in underpinning confidence and trust in businesses and the capital markets. Auditing has made a significant contribution to the UK's economic health over many decades, and we want it to continue to contribute to driving growth, trade and prosperity for all stakeholders. At the same time, technology is changing business, and the audit is no exception.

We know there are no easy answers and that no single participant can resolve the challenge; it will require many different perspectives and a large number of organisations, institutions and individuals working together to create effective change. Our aim is to contribute to the debate, and to work constructively with others to develop a system that we can all be confident in and is trusted.

Kevin Ellis

Chairman and Senior Partner

Introduction



The UK has a reputation globally for having some of the highest standards for corporate reporting, auditing and governance. This is why I, and many colleagues in the profession, have been proud to spend our working lives in the sector. But it is clear that for the UK to remain a leader, the audit and the profession at large need to change.

Those of us working to deliver audits day-in-day-out naturally have ideas about how our profession could evolve. But there are a wide variety of other groups and organisations interested in the effectiveness of the audit. That's why we have been trying to broaden the range of voices around the table: listening to the different stakeholders who are engaged with corporate reporting and auditing.

Through a series of roundtables across the UK, PwC brought together a mix of investors, audit committee chairs, finance directors, journalists, politicians and academics. We also gathered a wider range of perspectives through speaking directly with senior figures from the business and investment communities, as well as undertaking a survey of UK businesses and investors. Our aim was to hear what they had to say, from their concerns about today's audit to their suggestions of what it could or should look like in the future.



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The audit and the profession
have evolved before, and they
need to do so again now.

The first part of this paper captures the big themes, questions and ideas we heard. As head of PwC's Audit practice, I attended each of the roundtables, and it was valuable to hear the ideas and insights first hand. In my view, the most striking theme to come out was the desire from stakeholders to have more insight and clarity into the risks a company faces. Although there was consensus that auditors could not be expected to prevent companies from failing, there was an urge for the reporting and auditing system to provide more information about a business' future prospects.

In the second part of this paper, we outline where we see opportunities for change. While there are many steps that the audit firms can take themselves, we as a profession must work collaboratively with all stakeholders to together create a system that we can all be confident in. Areas of potential reform include enhancing the reporting and auditing of a company's internal controls, providing more insight into the material uncertainties facing a company, and helping stakeholders better understand the risks of fraud.

The audit and the profession have evolved before, and they need to do so again now. Having spent my working life as an auditor, I want audit to remain relevant so that others are inspired to become auditors in the future. And while there will be challenges, we support the need for change and we hope this contribution can help move the debate forward for evolving the audit and rebuilding trust.

Hemione Hudson

Head of Audit

Convening a public debate on the future of audit

Through a programme of large events and small gatherings, in person and online, PwC opened up a discussion with a wide range of organisations and individuals who each have an interest in making the audit fit for the future. From business leaders to investors, members of audit committees to academics, we heard many different views and perspectives on how the audit could evolve.

There was real enthusiasm from attendees at our roundtable events and those who responded to the survey about opening up the discussion, and many shared valuable insights and perspectives. Our ambition is to share those views and

opinions more widely through this paper, and to contribute to the lively and ongoing debate about the future of the audit and the profession.

Roundtables across the country

Across the country, we held open and frank conversations with a range of voices across business, the public sector, academia and the investment community. To enable participants to speak as freely as possible, we have anonymised the discussions and their contributions.



150+
participants

Including:

Investors, audit committee members, CEOs, CFOs and academics



Survey of UK businesses and investors

To understand the breadth and depth of opinion across the UK's business and investor community—those most closely involved in delivering or using the audit—we launched a survey in Spring 2019. In total, we heard from 175 investors and 198 business leaders.



Conversations with business leaders and investors

At the end of 2018, our Chairman and Senior Partner Kevin Ellis wrote to the business and investment communities—more than 5,000 across the country—to ask for their views on how the audit could and should evolve. Following this, we met individually with senior business leaders, investors and others who are interested in the audit to capture their ideas. These in-depth discussions complemented what we heard in the roundtables and survey.

Open invitation to contribute online

Not everyone who has a view on the future of audit could attend one of our roundtable events, participate in our survey or meet with us individually. That's why we created an open online forum to ensure that as many people as possible could share their views with us.



Our framework for debate

Our framework for debate

How the audit could and should evolve for the future is a complex question, touching on many different issues. Given this complexity, we developed a framework structured around six big topics to open up and guide our many conversations.



Beyond historical information

Would the audit be more valuable if it provided more information about the risks a company faces?



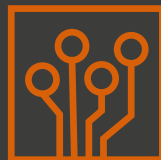
A different approach for big and small companies

Should all companies be subject to the same framework for an audit, regardless of their size and type?



Beyond shareholders

Should the audit evolve to serve a wider range of stakeholders?



Technology reshaping audit

How can new technologies make the audit more efficient and effective?



Beyond the financial statements

Could the audit cover the other types of information companies report?



Driving audit quality

How can the profession work to deliver consistently high quality audits?

Executive summary

Perspectives from stakeholders of the audit

PwC opened up a discussion on the future of audit through a series of roundtable events across the country, surveys of the UK's business and investment communities, and an open invitation to participate online. This captured the views of a wide range of organisations and hundreds of individuals, using a framework for debate structured around six big topics.

The first part of this paper summarises what we heard.



Beyond historical information

Would the audit be more valuable if it provided more information about the risks a company faces?

Stakeholders tell us they want:

- **A greater focus on the future**, including for the audit to provide assurance about a company's future prospects.
- **Clearer signalling of risk** in the annual report and, in turn, in the audit report.
- **A stronger going concern assessment**, which goes further and is reviewed more frequently by a company and its auditor.
- **A stronger viability statement** from a company that explicitly sets out its appetite for risk and for the statement to be within the scope of the audit.
- **Greater transparency through the auditor's report** by providing the auditor's view of a company's prospects and the risks it faces, and how well-equipped the company is at managing them.



An audit is by its nature a review of the past. But investors don't care about the past, they care about the future.

Asset manager, survey respondent



Beyond shareholders

Should the audit evolve to serve a wider range of stakeholders?

Stakeholders see a need for:

- **Simpler, more accessible corporate information** that is tailored to meet the interests of different stakeholders.
- **Seeking a better understanding of the needs of a wider stakeholder community** which could help ensure corporate reporting conveys the information stakeholders need to understand the business' performance and prospects.



Audit has societal purpose and is no longer just about shareholders, but broader stakeholders.

Academic, Edinburgh roundtable



Beyond the financial statements

Could the audit cover the other types of information companies report?

Among stakeholders there is:

- **A divergence in views about auditing non-financial information** given concerns that this information may not be sufficiently robust to be audited as compared with the core financial information.
- **An appetite for financial information reported outside the financial statements to be included in the audit**, particularly from investors who frequently use such information as a basis for their decisions.
- **A desire for the information that is audited to be customisable** so that the scope of the audit may be tailored to the needs of the company and its stakeholders.



Non-financial information is a very important part of the reporting cycle. But we wouldn't necessarily believe that extending the audit to cover that information is the most important next step.

CFO, London roundtable



A different approach for big and small companies

Should all companies be subject to the same framework for an audit, regardless of their size and type?

Stakeholders want the scope of the audit to be more flexible, and in particular to:

- **Recognise the needs of smaller businesses** because a single audit framework is considered too rigid to meet their stakeholders' requirements.
- **Look at whether to audit smaller privately-owned companies at all** given that their shareholders are often directors of the company and have access to all the information they need about the business.
- **Bring greater scrutiny for companies with the greatest societal footprints** because of the potential harm that could be caused by their collapse.

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The more we expand the audit, the less likely it is that one size will fit all.

Audit committee chair, London roundtable



Technology reshaping audit

How can new technologies make the audit more efficient and effective?

Among stakeholders there is:

- **Optimism about the potential impact of technology** to increase the efficiency and quality of audits.
- **Caution about the limits of technology** because it cannot provide auditors with everything they need to know about the company and its management.
- **A belief in the continuing value of human judgement** since, regardless of how big a role technology plays in the audit process, there will always be a role for the experience of human auditors.

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Technology clearly has a role to play—but you can't replace the human being walking around the finance department and standing tall with the CFO.

CFO, Manchester roundtable



Driving audit quality

How can the profession work to deliver consistently high quality audits?

Stakeholders have:

- **Differences in opinion about whether today's audit is 'broken'** with some, particularly investors, feeling it is not providing the assurance they need, but others thinking that 'broken' is too strong a term.
- **Questions about how to define quality**, with no consensus on a description of audit quality, but an agreement that the skills and experience of audit teams are critical.
- **A desire for a culture of challenge in audit teams** to ensure that auditors are consistently able to scrutinise companies effectively.
- **Demands for the audit to better communicate the risks of fraud**, with ideas ranging from more extensive measures to detect fraud to requiring companies to report on internal controls in respect of fraud.
- **A request to increase the responsibilities of company directors** so they are sufficiently accountable for the accuracy of the financial information published by the company.

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As investors, we are looking for judgement. We are looking for someone sceptical, willing to challenge—but we feel the 'beige-ness' has taken over.

Investor, London roundtable

Executive summary

PwC's perspective

The clear message we've heard around the country over the past several months is that the audit needs to evolve. Those who participated in our discussions on the future of the audit helped inform our own thinking of how this could happen.

The second part of this paper highlights our perspective on the key themes emerging from our discussions that we see as opportunities for change.

What we heard

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For the audit to move forward, the entire corporate reporting system needs to evolve

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The audit should provide more clarity and insight into the company's potential risks and future prospects

Opportunities for change





- **Strengthen the clarity and relevance of corporate reporting** to ensure the entire corporate reporting 'ecosystem' is as effective as possible.
- **Enhance the reporting and auditing of a company's internal controls** by requiring an attestation, from directors, of the design and effectiveness of a company's internal controls, and a corresponding attestation on internal control from the auditor for larger companies.
- **Develop better engagement between the audit profession, company management, shareholders and other stakeholders**, such as through a new **annual assurance meeting** or the introduction of an Assurance Map.



- **Create a single, coherent piece of company reporting that provides more insight into the future prospects of the company—including the scenarios in which the business model could fail**, giving stakeholders a clearer picture of the risks that could lead to failure so they can make informed decisions.
- **Provide more insight about the material uncertainties facing a company** by considering whether, market-wide, auditors should include a key audit matter on going concern in public interest audit reports.
- **Consider the need to provide assurance over other forms of risk** for which stakeholders may be seeking independent assurance, potentially as part of an Assurance Map exercise.

A new approach: Creating an Assurance Map

The statutory audit is just one way to provide assurance over the many financial risks facing a company. A way to make sure all sources of assurance over a company's principal risks, whether financial or not, are considered would be to make it an explicit responsibility for the audit committee to determine the level and type of assurance needed by their company's stakeholders and to present it to them and discuss it at the beginning of the reporting cycle. Creating this Assurance Map would prompt a constructive discussion at the top of the business about the needs of their stakeholders and make it possible to get assurance over the areas that are important to those stakeholders.

What we heard	Opportunities for change
<p>“</p> <p>There should be greater assurance beyond the financial statements</p>	 <ul style="list-style-type: none"> • Reporting and assurance need to expand to cover critical performance measures that stakeholders use in their decision making, such as non-GAAP financial performance measures.
<p>“</p> <p>The audit needs to recognise companies' different sizes and types</p>	 <ul style="list-style-type: none"> • Provide additional assurance over the companies that need it, without expanding the statutory audit for all and potentially overburdening smaller businesses.
<p>“</p> <p>Continued investment in technology will enable a better audit</p>	 <ul style="list-style-type: none"> • Continue to develop and roll out new technologies to improve the effectiveness of audits, focusing on using technology to improve quality, efficiency and auditor insight.
<p>“</p> <p>Auditors must deliver consistently high quality audits</p>	 <ul style="list-style-type: none"> • Increase investment in the training, technology and people required to conduct consistently high quality audits through a long-term commitment by audit firms. • Strengthen the culture of challenge in audit teams to ensure consistently effective scrutiny of companies. • Continue to reflect on how auditors can better tackle the risk of fraud, including considering use of fraud diagnostic surveys and involvement of forensic specialists at the planning stage.

Strengthening PwC's focus on audit quality

We are committed to continually improving and strengthening audit quality, and that is why we have introduced measures to ensure we deliver consistently high quality audits that meet the needs of investors, companies and society. Our plan has three areas of focus: (1) investing in training, people and technology, (2) further aligning the audit business behind audit quality and (3) reinforcing a focus on culture and quality control.





Stakeholder perspectives on

Beyond historical information

Would the audit be more valuable if it provided more information about the risks a company faces?

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The audit should start with the big picture—is the business viable?

CFO, Manchester roundtable

Recent high-profile corporate failures led to widespread questions about what more auditors could do to inform stakeholders so that they can assess potential problems. While a number of aspects of today's audit do consider the future, many asked if it could evolve to give more assurance about the future prospects of a business.

Today's statutory audit was originally designed to provide assurance over a company's financial position at a specific point in time and its financial performance, usually over the preceding 12 months, to the company's shareholders as a whole. However, a consistent concern in the audit debate is that financial statements and the audit process are too historically focused.

A greater focus on the future

Support for a greater emphasis on the future was reflected in our roundtable events. Our survey of businesses and investors also found substantial support for making the audit more focused on the future: more than two-thirds of both groups would like a company's long-term viability to be covered by the central scope of the audit.

In particular, many investors who attended our roundtables and responded to our survey felt that the audit would be more valuable for them if it provided assurance about a company's future prospects because it would give a better basis for their investment decisions. “An audit is by its nature a review of the past,” said one asset manager from our survey. “But investors don't care about the past, they care about the future.”

However, some investors disagreed, feeling that they already have all the information they need from today's audited financial statements to form a view about the future. At our roundtable in London, one suggested, “In all companies, failure signs are there and we shouldn't design a system that caters to people who don't read the accounts and aren't able to spot the signs.”

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It is incredibly difficult to take a view of the future, and investors should take that risk—with auditors focusing on historical information.

Investor, London roundtable

There also was concern that the further ahead the company looks, the harder it might become for them to provide sufficient enough evidence to support their assessment and for the auditor to rely on. “Let's not overburden auditors with doing much else before first we have got the historic financial statement audit nailed down,” argued an audit committee chair at the London roundtable. “If the historical information is wrong, then anything else looking forward is flawed.”

Investors and businesses are in favour of the audit scope considering key risks and uncertainties facing a company

72% Investment community
79% Business community

% of respondents answering that they strongly or tend to support including key risks and uncertainties in the central scope of the statutory audit

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It's important to start calibrating the degree of concern that auditors have—maybe through a traffic light system to show the level of risk or concern. However, the share price could collapse if this wasn't applied across all audits, and probably internationally as well.

Investor, London roundtable

Clearer signalling of risk

Most participants felt that warning signs about the risks faced by a company should be made more transparent and easier to interpret in the company's annual report and flagged by the auditor in the extended auditor's report.

Indeed, our survey showed that 72% of investors and 79% of businesses support including within the audit's scope an assessment of the key risks and uncertainties facing the company. And within the business community, this strength of feeling is strongest amongst company directors: nearly 90% of them would support including this within the scope of the audit, compared with 75% of company management. Even though some investors argued they were in fact already able to detect the warning signs in the audited financial information, they wondered whether these 'red flags' are visible enough for other stakeholders to spot.

A stronger going concern assessment

A majority of investors and businesses in our survey said they either read the auditor's going concern conclusions in detail, or at least scan them. However, there were consistent calls at our roundtables for auditors to 'do more' in their assessment of the directors' statement about whether a company is a going concern and can be expected to keep operating for at least the next 12 months.

Many people cited recent examples of corporate failure and questioned how a business could suddenly and unexpectedly collapse with little warning, especially since the auditors in those examples had concluded that the directors' going concern statement was appropriate.

However, a number of participants acknowledged that audits could not prevent companies from failing, and that some businesses will inevitably go out of business due to market forces or poor management. Despite this, there was general agreement that the audit could evolve to give a company's stakeholders more information about the risks it faces.

Some suggested that a company could review its going concern assessment more frequently, for example every six months or once a quarter—rather than once a year as currently. This could then be checked by the auditor.

Another idea put forward was to extend the period covered by the going concern assessment beyond the current minimum of 12 months. For the businesses and investors who support extending the going concern period, the consensus is that it should cover the next 2-3 years. However, our survey found clear overall majorities from both the investment and business communities in favour of maintaining the current time period.

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Going concern over-emphasises the next 12 months. Clearly that period is important, but there also needs to be a focus on how sustainable the business is in the longer term.

Investor, Manchester roundtable

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The audit profession needs to find a way to tell the ‘hidden story’. The vast majority of this goes on during the course of an audit and is not visible in the final reporting.

Company chairman and former PwC partner, Future of Audit online forum

A stronger viability statement

A viability statement outlines the directors’ view of the sustainability of the company’s business model and goes beyond the 12 months considered by the going concern statement. We heard from many investors that they felt this statement was of little value to them as it has become ‘vague’, with only ‘boilerplate’ language. Their view was that most companies do not devote sufficient effort to their viability statements, and that they tend to cover a three-year period, which is thought to be too short, especially for businesses in sectors with long-lived assets and liabilities.

To make the viability assessment more valuable, some participants suggested that directors should cover a longer period of time, cover the company’s appetite for risk more explicitly, and disclose the results of any stress testing that has been carried out on the future prospects of the business. There were calls for this more robust viability statement to fall under the scope of the audit. However, some business leaders questioned whether auditors currently have the right capabilities and experience to make an informed assessment of a company’s long-term viability.

Others were concerned that including the viability statement in the scope of the audit might lead to unintended consequences. In particular, there was a worry that putting the auditor’s views on a business’ future viability into the public domain might become a self-fulfilling prophecy by undermining the confidence of external stakeholders. In contrast, a number of participants believed that if this sort of approach became the established norm for all companies, then stakeholders would become used to this kind of discussion and expect that the market would adjust its reaction appropriately over time.

Greater transparency through the auditor’s report

The primary means of communication for auditors is through the long-form (extended) auditor’s report, which is required for all listed, and some unlisted, companies. When discussing how auditors can better communicate what they have done—and, even more importantly, what they found—participants suggested that it would be useful for the auditor to give a more detailed and comprehensive view on the company’s prospects and risks, and on how well-equipped the auditor thinks the company is at managing them.

Our survey showed that businesses and investors are overwhelmingly supportive of introducing graduated findings, as well as a better narrative and qualitative explanation of the auditor’s overall findings but wanted to retain the overall ‘pass or fail’ opinion for the company’s accounts. The additional colour and context that the narrative and qualitative explanation could provide was thought to be valuable particularly to investors, but would need to be accessible and easy to interpret to be relevant to a wider range of stakeholders.

Many investors and businesses surveyed told us they at least scan the audit opinion, and most look in detail at any qualifications or exceptions noted by the auditor. Furthermore, the survey also showed that 87% of investors and 97% of businesses at least scan the key audit matters section of the audit report, which describes the key risk areas in the audit.



Stakeholder perspectives on **Beyond shareholders**

Should the audit evolve to serve a wider range of stakeholders?

The statutory audit was designed so that a company's shareholders as a whole could have confidence in the financial statements of a company they have invested in. But if a company collapses, many other stakeholders can be hurt, financially or otherwise. That raised questions about whether, and how, the audit can evolve to provide assurance to a wider range of people.

From employees to customers, creditors to suppliers, many groups beyond shareholders may be interested in a company's financial position, performance and prospects.

Simpler, more accessible corporate information

The role of corporate reporting in better serving the needs of users of the information was a common thread throughout the discussions. It was felt that the main part of the responsibility resides firmly with the company and its directors to make the information it puts out as robust, useful and understandable as possible, with the auditor playing a role in ensuring they achieve that objective. Indeed, some felt that if the reported information itself was more readily understood (whether by shareholders or others) the audit too would become more useful.

Some participants suggested that corporate reporting could be improved by making it more simple, relevant and to the point. Some considered the accounting standards themselves to be the root cause of the challenge. "The auditor is being asked to audit against International Financial Reporting Standards (IFRS) fair value accounting that, from a business performance perspective, doesn't convey a lot about how a business is being managed," a CFO at our London roundtable argued.

But others felt that the need for corporate reporting to represent a complex world makes it difficult to see how corporate reporting can be simplified without removing some of its meaning. There were some who thought that the answer lay in greater levels of education for the users of financial statements. But others questioned why the communication of that information needs to be so complex in the first place.

We heard a similar message from PwC's recent 'Public Opinion Day', part of our Building Public Trust programme. When a panel of 22 members of the public was asked if they had requested or read a company's annual report in the last 12 months, only two had done so. We heard that these members of the public want to make more use of corporate reporting but find it difficult to do so. Across our Future of Audit roundtable events many suggested that a way forward could be for companies to tailor the information they report to the interests of the different stakeholders interested in the business.

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Stakeholders want comfort that someone has come into the company and said, 'your pension is safe' or 'your salary will be paid'.

**Audit committee chair,
London roundtable**

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The main problem is not the audit but the length and complexity of financial statements, which provide irrelevant and unintelligible details that obscure the underlying picture meant to be presented by the financial statements.

**Audit committee member,
survey respondent**

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Some annual reports are 400 pages long. Couldn't we have the same information in a simpler and more condensed format for different audiences?

**Member of the public,
PwC Public Opinion Day**

Investors and businesses are generally sceptical that today's audit meets the needs of a company's stakeholders such as employees, customers, suppliers and local communities

32% Investment community

52% Business community

% of respondents answering that the audit is somewhat or very effective at serving stakeholder needs

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At the end of the day businesses are owned by shareholders who've invested their money and should therefore be the primary focus.

**Audit committee chair,
Belfast roundtable**



Seeking a better understanding of the needs of a wider stakeholder community

One common discussion at our roundtable events and in our online forum centred on whether and how the audit, as well as corporate reporting, might find some way to respond to the needs of a broader range of stakeholders. Some of the businesses and investors responding to our survey said they are not convinced that today's audit meets the needs of a company's stakeholders such as employees, suppliers and others: less than a third of investors and just over half of businesses think it is doing so effectively.

Some participants—both businesses and investors—felt that the audit's current focus on the company's shareholders is appropriate given that they have provided financial capital to the company and consequently need to have an independent verification of how that capital is being used.



Stakeholder perspectives on Beyond the financial statements

Could the audit cover the other types of information companies report?

Today, the audit focuses on a company's financial statements. However, there were questions about whether assurance is needed over other information companies report about their performance and the risks facing the business.

There is growing interest in the range of metrics companies use to monitor their performance, health and resilience. These may be alternative financial performance measures (often called non-GAAP measures because they are not prepared under generally accepted accounting principles) or non-financial performance measures, such as levels of employee engagement, the strength of cyber security or environmental impact. Companies often disclose these financial and non-financial measures outside the audited financial statements. Although traditional users of the financial statements—especially shareholders—are increasingly using these types of information in their decision making, they're not included in the scope of the audit today.



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It would be really useful to develop tools to help auditors assess the culture of an enterprise, as often poor culture is a precursor to failure.

**Non-executive director,
Future of Audit online forum**

Investors and businesses have limited appetite for including corporate culture, ethics and behaviour within the scope of the audit

43% Investment community

35% Business community

% of respondents answering that they strongly or tend to support including corporate culture, ethics and behaviour within the central scope of the statutory audit

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We worry about mission creep for the audit. Non-financial information is a very important part of the reporting cycle. But we wouldn't necessarily believe that extending the audit to cover that information is the most important next step.

CFO, London roundtable

A divergence in views about auditing non-financial information

The predominant view expressed during our roundtables was that it would be valuable to have independent verification of the accuracy of information reported outside the financial statements. However, some participants had concerns about the practicality of including some of this information in the central scope of the audit, particularly if it relates to non-financial measures.

Although the businesses and investors in our survey had different priorities of what should be included in the scope of the statutory audit, there was support for expanding it to cover non-financial areas such as compliance with laws and regulations, operational key performance indicators (KPIs) and dividend policy, with investors generally feeling more strongly about including them. There was less enthusiasm for expanding the audit's scope to include sustainability KPIs.

Aside from the 'hard' financial metrics, some participants suggested that it would be useful if auditors could assess the 'softer areas', such as board effectiveness and company culture. A CFO at our roundtable in Edinburgh suggested that auditors could do this by drawing on the insights they gleaned during the audit process: "We have gone through an effectiveness review internally. This could become something that every company is required to do, with the auditors then giving an opinion on whether it is a fair assessment." However, extending the audit to cover corporate culture, ethics and behaviour had only limited support in our survey.

The concerns expressed about auditing non-financial information centred partly around whether the non-financial information reported by companies is ready for an audit. Participants questioned whether the underlying data would be robust enough to be audited, compared with the core financial information. Some also argued that today's auditors do not have the right skills and expertise to audit these types of metrics because their training and background has been focused on financial information. Some suggested that for some information, assurance could be provided more effectively by third party specialists rather than by the auditors of the financial statements.

Some businesses in particular were concerned that they risked being required to report, and have audited, information that was neither relevant nor appropriate for them or their stakeholders. Businesses also cited concerns about the additional cost involved.



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Given the prominence of non-GAAP measures and other figures in investor relations materials, this should be audited information.

Analyst, survey respondent

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You could have different scales of audit for different companies of different types, sizes and industries with different needs—such as a financial, operational, business, purpose or fraud audit. The different scales could come on a ‘shopping-list’ showing what you pay for.

Academic, Belfast roundtable

An appetite for financial information reported outside the financial statements to be included in the audit

While there was scepticism about how practical it would be to expand the audit to cover non-financial measures, there was more of an appetite for financial measures reported outside the financial statements to be included in the audit. Judging from what we heard, the pressure to include this kind of information in the audit is intensifying, especially amongst investors.

Our survey explored what additional areas businesses and investors would like to include within the audit. A large majority of investors supported expanding the audit to include financial information presented outside the annual report, followed by non-GAAP financial measures. The businesses surveyed were most keen to include non-GAAP financial measures as their top priority.

A desire for the information that is audited to be customisable

Some participants suggested that it would be valuable to have a customisable menu of additional options that would extend the scope of the statutory audit, and audit committees could select from that to tailor the audit to the needs of the company and its stakeholders. Participants suggested that, under such a system, if a company discloses information about an issue affecting the business, the audit could cover those deemed the highest priority and therefore reflect specific concerns its stakeholders might have, for example, about fraud, cyber risks or environmental impact.



Stakeholder perspectives on

A different approach for big and small companies

Should all companies be subject to the same framework for an audit, regardless of their size and type?

From large multinationals to small family-owned businesses, audits today follow a common framework. Some questioned whether this remains the right approach.

During our roundtables around the country, there was strong support amongst both investors and businesses—large and small, listed and family-owned—for making the scope of the audit flexible so it can be more closely tailored to the specific business being audited. A majority of businesses and investors in our survey also supported this.

There was a general sense that a ‘one-size-fits-all’ approach for the audit may not be appropriate in today’s world, given the very different types and sizes of business, and the differing needs of their shareholders and other stakeholders. The general view was that if the audit scope were to be expanded to include new types of information, or altered to appeal to a wider range of stakeholders, it would become even less appropriate to have a single, standard version in all circumstances.

Investors and businesses think the audit scope should be flexible

64% Investment community

82% Business community

% of respondents answering that the audit scope should be flexible so that it can be tailored to different entities



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The more we expand the audit, the less likely it is that one size will fit all.

**Audit committee chair,
London roundtable**

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I struggle with there being some kind of two-tier system. I am not entirely sure that they should be different based on size; it depends on the complexity and ownership structure.

Finance director, London roundtable

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Family businesses don't need an audit for the directors or shareholders. For us, the value is for people like the banks, credit insurance agencies, funders and regulators.

Finance director, Belfast roundtable

Recognise the needs of smaller businesses

At our roundtables, the loudest calls to tailor the audit came, perhaps unsurprisingly, from the smallest businesses. While there are differences between the audits of large and small companies today (such as the level of materiality applied), the same auditing framework is applied to all. This was felt to lead to audits being too rigid to meet the needs of the company, its shareholders and its other stakeholders.

The rise in regulatory obligations and other changes to auditing standards were also thought to have increased the complexity of the audit, meaning that the amount of work being done by the auditors, the level of documentation required and the final cost of the audit was felt to be out of proportion with the needs of smaller companies.

Look at whether to audit smaller privately-owned companies at all

Some smaller private businesses even questioned why they needed to be audited at all. The intention of the audit is to provide assurance to a company's shareholders (external providers of capital) about the information they receive from management, but for a small private business the shareholders are often directors of the company and have access to all the information they need about the business. This was thought to be even more true of family-owned businesses, where management and shareholders are often the same people.

However, there was consensus that for private companies an audit was useful for some external stakeholders. We heard from banks that lend money to privately-owned businesses who said that they use the audited accounts to guide their lending decisions, and—when they have chosen not to lend to a business—to help them explain why the request for funding has been turned down.

Bring greater scrutiny for companies with the greatest societal footprints

Some argued that there should not be a distinction between publicly-listed and private companies since the impact of some private businesses can be bigger than some listed companies, and so require a similarly high degree of scrutiny. If such private businesses run into financial difficulty, they argued, the impact on their employees, suppliers and other stakeholders could be substantial.



Stakeholder perspectives on Technology reshaping audit

How can new technologies make the audit more efficient and effective?

Rapid advancements in technology are transforming virtually all areas of business and the audit is no exception. As it becomes possible to capture and analyse ever greater amounts of data, questions were raised about how the audit could become more efficient and more valuable for those who rely on it and what role remains for human judgement.

Many audits today already make significant use of technology, including data analytics and automation. But we found there was a broad consensus amongst investors and business that they expect that as these technologies grow more sophisticated and become more widely implemented across the profession, they will dramatically transform how the audit is delivered.

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You need to automate the hell out of the ‘ticking and bashing’ parts of the audit, and instead have people doing audits who can really understand the business.

CFO, Manchester roundtable

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Technology means you can test almost everything. Today, the audit gets compressed by the regulatory burden of reporting within a tight time frame, and that harms quality. But technology lets you focus on transactions in real time and can help redefine overall quality.

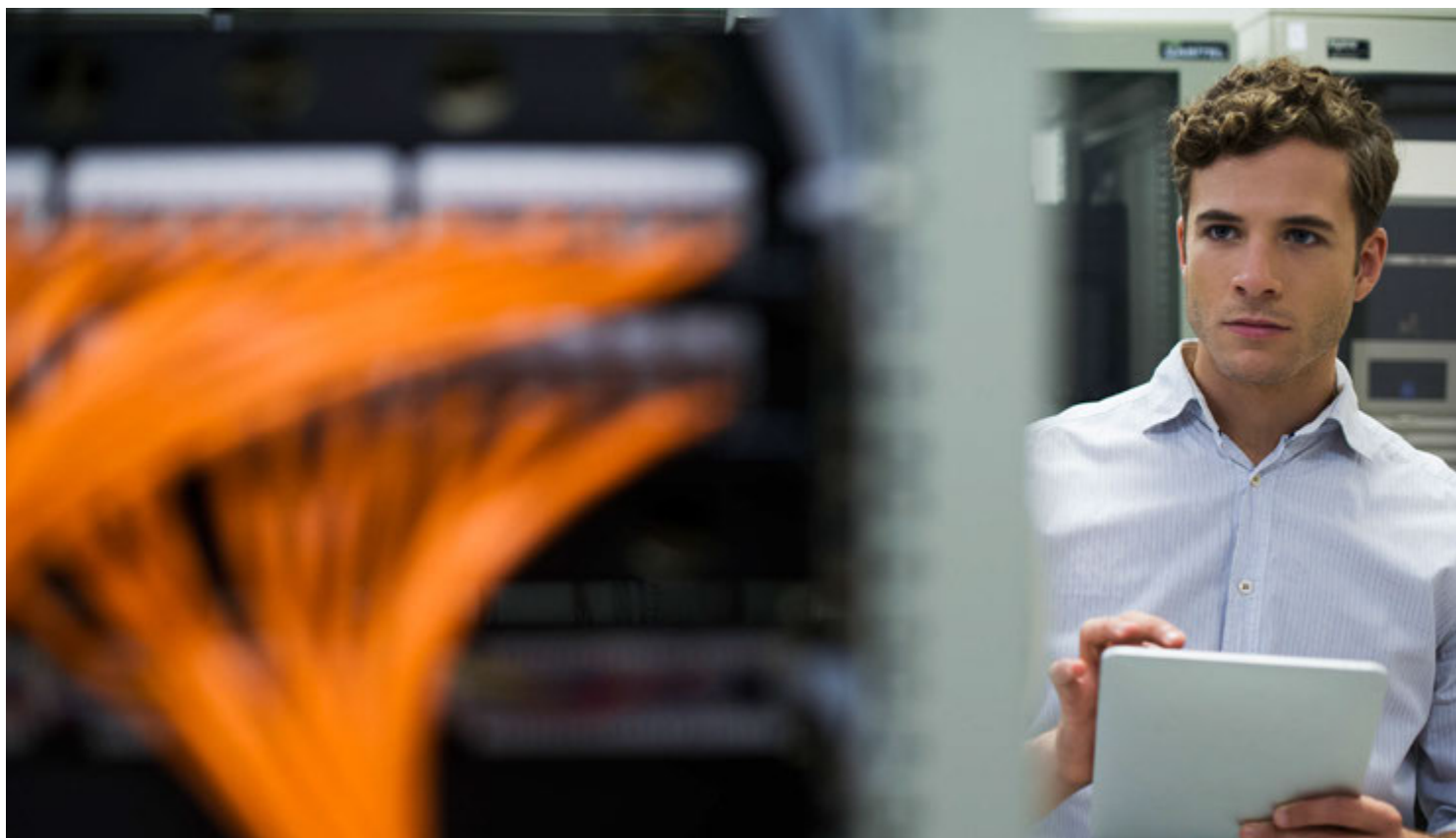
CFO, London roundtable

Optimism about the potential impact of technology

The general tone from our roundtables was optimistic about the ability of new technologies to improve many aspects of today’s audit.

Consensus was strongest around the possibility of increasing the efficiency of the audit. Our survey found that more than 80% of businesses, and more than three-quarters of investors, believe that technology will improve the efficiency with which audits are performed. Across the debates, the common theme was that such technologies will make it possible to free up auditors from repetitive and labour-intensive tasks, the so-called ‘ticking and bashing’, in an audit.

Some argued that if technology can make the audit substantially more efficient, then it would make it possible to expand the scope of the audit without having to dramatically increase the cost. Looking further ahead, some speculated that the audit process might even evolve from sampling parts of a company’s historical financial accounts to assessing all of a company’s information in ‘real-time’ so that auditors could provide assurance on more information, more often.



A majority of investors and businesses in our survey also believed that technology will improve the overall quality of audits. In particular, there was hope that the ability to crunch much larger amounts of data would enable auditors to better assess the key risk areas in a company's accounts, including being better able to spot potentially fraudulent activities.

Some participants suggested that if auditors were better able to combine this greatly increased amount of data about a company with the vast array of external data that is available today, then it could become possible to further corroborate what was learned during the audit, especially in areas like management's forward-looking assumptions.

Caution about the limits of technology

While the overall tone was positive, some expressed a note of caution about where they thought the limits of technology lay. Even if auditors were able to test substantially more data, some participants argued, this would not be able to tell the auditor everything they need to know about the nature of a company and its management. Indeed, our survey also found that businesses and investors are sceptical about the ability of technology to enable auditors to understand more about a business. As a participant in Belfast put it, "Technology can't tell you if the finance director is lying".

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Technology clearly has a role to play—but you can't replace the human being walking around the finance department and standing tall with the CFO.

CFO, London roundtable

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The auditor’s job will become more interesting—technology will take out all the drudge.

Investor, London roundtable

Many investors and businesses are sceptical that technology will help auditors better understand the business

36% Investment community

37% Business community

% of respondents answering that they think technology will help auditors better understand the business

A belief in the continuing value of human judgement

There was a strong consensus in our roundtables that regardless of how big a role technology plays in the audit process, there will always be a role for the experience and judgement of human auditors.

In particular, the view was that high audit quality would continue to depend on having auditors who understand the business, and who can apply judgement and professional scepticism when assessing a company’s accounts (or indeed issues beyond the accounts).

A critical component of this is being able to ‘stand tall’ against a company’s management when needed, challenging the assumptions or rationale behind a particular set of information. This was echoed in our survey, in which a majority of businesses and investors said that technology would better enable auditors to challenge the assumptions of management—a case for the continued role for human judgement.

But our survey respondents felt that by automating a large proportion of the routine audit work, the use of technology would make it harder for junior audit team members to acquire the core foundational skills they need, which would in turn create a problem for building up the pipeline of future senior auditors.





Stakeholder perspectives on Driving audit quality

How can the profession work to deliver consistently high quality audits?

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It's a complex problem and we won't solve it by focusing on the audit in isolation. There are many components including regulators, investors, audit committees and boards. Each part isn't functioning in the right way, which is leading to poor audit outcomes.

Business group, London roundtable

Many investors do not feel that today's audit effectively serves their needs

41% Investment community

68% Business community

% of respondents answering that the audit is somewhat or very effective at serving the needs of investors

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To prevent the kind of issues we've seen recently, an auditor has to be close to the board and its decisions, and has to understand the business model. That's not always the case.

Finance director,
Manchester roundtable

A key focus in the broader public debate has been on the quality of audits. The recent spate of high-profile corporate failures and auditor sanctions have shone a light on the need to deliver consistently high quality audits.

At our roundtables around the country, there was agreement that high audit quality is central to sustaining trust in the audit—and, in turn, that underpins confidence in the information companies disclose and in the capital markets more broadly. Therefore, maintaining and driving audit quality—and being seen to do so—was thought to be a priority for the auditing profession.

Differences in opinion about whether today's audit is 'broken'

The role that audit plays within our corporate governance framework was a common theme at our roundtables, and there was a significant split in opinion about whether the audit today was effectively 'broken', thus failing to provide the assurance it is designed to.

Less than half of the investors in our survey believe that the audit effectively serves their needs. Retail investors are particularly pessimistic. On the other hand, business respondents said they think the audit does meet investors' needs, a view held most strongly by company directors (76%).

Nearly 70% of investors said they do think the audit serves the needs of businesses, however. This was echoed by the 80% of business respondents who said they think the audit effectively serves their own needs, with company directors feeling this most strongly (96%).

Some participants said that labelling audit as 'broken' is too dramatic an assessment. "Broken is a strong word," we heard from a participant in London. "I would say, rather, that the audit system is vulnerable."

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A quality audit is in depth, thorough, with focus areas varying year-on-year, conducted by a talented and experienced audit team with a good understanding of the business dynamics and industry.

CFO, survey respondent

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In light of some of the recent scandals...auditors do need to be a little more like bloodhounds in uncovering serious director-led fraud, recognising that may mean both upskilling, allowing more time for audits and higher audit fees.

CFO, survey respondent

Questions about how to define quality

At our roundtables there was little consensus on how to define high audit quality, but one aspect came up repeatedly: the skills and experience of the people doing the audit. Many investors said in response to our survey that they find it hard to tell from the outside whether an audit is of high quality, and it is only when something goes wrong whether they can see that the audit was not good enough.

Our survey of investors and businesses asked respondents to describe in their own words a ‘high quality audit’. The answers were varied, with investors focusing on the quality of the financial statement output (e.g. ‘trustworthiness’, ‘accuracy’ and ‘reliability’) and businesses focusing on the audit process (e.g. ‘efficiency’, ‘value for money’, ‘uncovering something previously unknown’). But, as in the roundtable events, both groups highlighted the need for the auditor to be experienced and have a good understanding of the business being audited.

A number of common factors emerged for how the profession could ensure consistently higher audit quality in the future, such as:

- building skills and experience across the audit profession;
- ensuring that audit partners (not just junior auditors) are spending enough time on-site challenging management;
- ensuring that businesses have robust internal controls that enable stakeholders to have confidence in the reporting and audit processes;
- removing concerns about conflicts of interest; and
- bolstering a culture of challenge.

There was also support for auditors and audit committees engaging with investors and other interested parties more proactively.

Discussions about quality opened up the question of a refreshed definition of what the audit is designed to deliver (i.e. its purpose) and the standards to which it operates, both of which have a significant impact on how quality is understood.

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A high quality audit is one where auditors take steps and disclose what steps they took to look for fraud.

Analyst, survey respondent

Investors and businesses disagree on whether the audit's scope should include fraud detection (however material)

82% Investment community
53% Business community

% of respondents answering that they strongly or tend to support including fraud detection within the central scope of the statutory audit

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Responsibility rests with the directors and particularly the finance director for the accuracy and fair presentation of the financial statements. The first round of criticism should rest with the directors, especially if they have also been fraudulent in disclosures to the auditors.

Audit committee member, survey respondent

A desire for a culture of challenge in audit teams

A central feature of the discussions around quality was the necessity for auditors to be able to challenge a company's management. It was felt that to do so effectively required auditors to be sufficiently independent of the company's management, and concerns were raised that this was not always seen to be the case. That said, some participants acknowledged there is a balance to be had on this point, and that one way to get a good understanding of the business may come from the relationship the auditor has with key figures in the company.

Demands for the audit to better communicate the risks of fraud

Some participants at our roundtables said that their faith in audit quality had been dented by cases of auditors failing to spot fraud in a company's financial statements. And our survey revealed a clear demand from investors for greater detail about the risks of fraud, with a substantial majority of investors in favour of expanding the scope of the audit to include detecting fraud (regardless of the level of materiality). Some in the business community felt the same, with one CFO saying, "Whether practical or not, I think there will have to be some specific reassurance about fraud." However, many participants at the roundtables were keen to stress that they felt no proportionate system would ever be able to eliminate the risk of fraud, and that implementing such a system would be costly and potentially could cause more harm than good.

Some participants suggested that companies should be required to report on the strength of their internal controls with respect to fraud, with auditors in turn providing assurance over those controls. They said this would provide investors and other stakeholders with more information about the potential risks of fraud within the business. There was also widespread optimism amongst both businesses and investors that new technologies would enable auditors to better spot potentially fraudulent activities, such as by analysing larger amounts of data than is currently possible.

A request to increase the responsibilities of company directors

Participants across all the roundtables raised questions about whether company directors are sufficiently accountable for the accuracy of the financial information they publish. There was support for introducing a regime similar to that in the US in which, for public companies over a certain market capitalisation, management has a legal responsibility to assess and certify the effectiveness of financial controls over financial reporting, and the auditor then opines on the effectiveness of those controls.



PwC's perspective

Rising to the challenge: Key considerations for the audit profession

Across the country, we have heard a consistent call for the audit to change so that it is fit for the future.

It is clear from the public debate and from the views we actively sought on the future of audit that there is a lack of understanding and agreement about the scope and purpose of audit as it stands. Among the numerous views and ideas that emerged through our discussions, one of the most significant and important insights was the investment community's feedback on today's audit, with only 41% of those surveyed feeling that it meets their needs.

What is most concerning about this finding is that the audit is designed to give shareholders—those providing financial capital—comfort that the information they receive from the company can be relied upon for effective decision making.

In this section, we share our perspective on the key points we heard at our roundtables, in our online forum and in our surveys. We highlight the concerns that emerged and suggest ideas for addressing them.

What we heard



For the audit to move forward, the entire corporate reporting system needs to evolve

Across the country, the complexity of financial and corporate reporting was a common complaint. Many of those who came to our roundtable events argued that the volume and format of corporate reporting obscured more than it illuminated. There was therefore strong support for companies to provide more accessible information, even tailoring it to different groups of stakeholders.

There was also broad backing for strengthening the quality of reporting by including a company's internal controls within the scope of the audit. We heard support for directors and auditors attesting to the effectiveness of the company's internal controls, similar to the Sarbanes-Oxley regime in the US. We heard a consistent call for better engagement between the various groups and organisations involved in corporate reporting, in particular between investors and audit committees.



Opportunities for change

Strengthen the clarity and relevance of corporate reporting

Audit operates as part of an inter-connected corporate reporting 'ecosystem', which includes company directors, shareholders and regulators. The audit needs to change, but for this change to be as effective as possible the other roles in the ecosystem will need to evolve as well. Without this, there will be a significant lost opportunity.

At the core of this ecosystem is the clarity and relevance of corporate reporting. Over the years, corporate reporting in the UK has expanded in both volume and complexity, which has often compounded the difficulty for different stakeholders to find the information they need clearly and easily.

This is why we support the regulator being tasked with promoting brevity and comprehensibility in corporate reporting and with regularly assessing the extent to which the reporting framework is relevant to users' needs.

Separately, many of the potential changes that will enhance the audit rely, at least in part, on the reporting provided by others. For example, a company's directors would need to make a more detailed and granular disclosure of the potential risks to going concern in order for the auditor to provide a greater level of assurance.

Enhance the reporting and auditing of a company's internal controls

Creating a stronger framework of responsibility and reporting in respect of a company's internal controls would help improve the quality of reported information.

One way to do this would be to have a clear, public attestation from directors as to the design and operating effectiveness of the company's internal controls, which would be underpinned by:

- a clearly communicated expectation of the level of rigour and diligence to be applied in making that attestation; and
- an accountability mechanism with consequences for directors in the event of non-compliance.

This could be strengthened further by requiring the auditor to make a corresponding attestation on internal controls for larger companies of a greater public interest.



The introduction of reporting on internal controls could also provide an opportunity to explore the appetite for more frequent reporting throughout the year. New technologies could potentially allow ‘hands-free’ testing of the business controls, meaning it would be possible to imagine a future where some company reporting, and related assurance, could be provided continuously.

Develop better engagement between the audit profession, company management, shareholders and other stakeholders

Evolving the audit to meet the needs and expectations of stakeholders today and into the future will also need us to consider new ways of engaging between the audit profession, company management and directors, shareholders and other stakeholders.

A formal engagement mechanism could be a new ‘annual assurance meeting’, led by the audit committee, attended by the external auditor (and other assurance providers if relevant) who would be available to answer questions, and with all stakeholders invited. The audit committee chair could present both on the results of the audit (inviting the external auditor to comment), and on the planned assurance for the forthcoming audit cycle, prompting a constructive debate on both areas. Areas of particular importance, such as fraud risk and going concern, could be mandatory items on the agenda. This could be supported by the mechanism of developing an Assurance Map (see page 37).

To make any engagement effective it will be important to ensure that all parties work to understand one another’s perspectives and that the timing of the engagement is appropriate. Of course, some stakeholders do not consider engagement with auditors or companies on audit matters to be a priority. What is important is that those who do want to engage are able to do so.

What we heard



The audit should provide more clarity and insight into the company's potential risks and future prospects

At our roundtables across the country and in our survey of businesses and investors, there were consistent calls for the audit to be more focused on a company's future prospects, and the risks to achieving them. In particular, there was a desire for stakeholders to have a clear picture of the risks facing a company, including those that could lead to its failure.

While the responsibility for reporting this information resides with the company and its directors, there were calls for the auditor to make sure the information reported is as robust, useful and understandable as possible. And although some investors felt able to detect the early warning signs when a company is getting into difficulty, the consensus was that these are not always clear enough for the majority of stakeholders.



Opportunities for change

Create a single, coherent piece of company reporting that provides more insight into the future prospects of the company—including the scenarios in which the business model could fail

To enable stakeholders to have more insight into a company's future prospects, the responsibilities and reporting regimes for going concern and viability should be reformed to ensure that stakeholders have access to the right information.

The business model, principal risk, going concern and viability reporting regimes could be overhauled and replaced by a single, coherent piece of reporting focused on the directors' assessment of scenarios in which the business model could break, and how they plan to mitigate the risk of that happening. This reporting would focus on the next 12 months, as required by the Companies Act, with a more qualitative assessment of business model risks that could crystallise beyond that period, not confined to a prescribed 'viability period'. Auditors could still provide assurance on the detailed going concern analysis of the 12-month period reported by the company.

This would enable stakeholders to make more timely and informed decisions about their relationship with a company.

Companies will still fail, but unexpected failure will be less likely if stakeholders have a clearer picture of the risks that could lead to failure, and can make better decisions as a result.

Provide more insight about the material uncertainties facing a company

Auditors are required to highlight any material uncertainties about whether a company will remain a going concern, but the bar for this is high. In fact, such reporting can become a self-fulfilling prophecy because it signals the company is in difficulty, and other stakeholders then lose confidence in the business. This means that today, there is not a clear way for auditors to flag other potential issues that are not yet material.

Consideration should be given as to whether, market-wide, auditors should include a key audit matter (KAM) on going concern in public interest audit reports. This would provide helpful context about the auditor's views on the issues, and give the reader information that could help in their own assessment of the risks to the company's future prospects. Taking a consistent market-wide approach would reduce the risk of unintended consequences.

Consider the need to provide assurance over other forms of risk

There may be other important areas of risk about a company, such as the strength of their cyber security, that would not necessarily be covered by an enhanced going concern assessment, but over which stakeholders could want independent assurance. In such cases, company directors should consider the need for this type of additional assurance as part of an Assurance Map exercise (see page 37).



A new approach: Creating an Assurance Map

The statutory audit is just one source of assurance over the many different risks facing a company. Because the types of risks facing a business—as well as the level of assurance each company's stakeholders want about those risks—vary so widely, there is a need for a more flexible regime.

One way of obtaining assurance over those different risks would be to make it an explicit responsibility for the audit committee to determine the level and type of assurance needed by their company's stakeholders. Creating this Assurance Map would prompt a constructive discussion at the top of the business about the needs of their stakeholders. This would involve identifying:

- the principal risks faced by the company
- the controls in place to mitigate those risks
- the key performance indicators relevant to the company (which could be financial or non-financial)
- the information and results needed by users to assess risks, related controls and key performance indicators
- the assurance available, including who provides the assurance and how often.

The statutory audit would form one part of the Assurance Map, providing a level of assurance over a company's financial statements. It would then be possible for the audit committee to commission additional assurance, but not as part of the statutory audit, over the other areas that are important to stakeholders.

The various sources of assurance available to meet the needs of stakeholders could be made more visible by requiring a company to publish its Assurance Map at the beginning of the audit cycle. This would give an opportunity for stakeholders to comment on and, if necessary, challenge the areas for which they want more or less assurance. This means that the range and type of assurance over each company would be tailored depending on the needs of its stakeholders. And as stakeholders' expectations change over time, the assurance sought could be altered to best meet their needs. The approach would also ensure that there is clarity over the boundaries of the statutory audit and the external auditor's liability and duty of care in delivering that work.

What we heard

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There should be greater assurance beyond the financial statements

Today, the audit focuses on a company's historical financial position and performance. However, we heard a clear call from both businesses and investors to extend its scope to include other forms of information.

A majority of investors in our survey, along with a smaller majority of businesses, were in favour of expanding the audit to include additional areas, such as financial information presented outside the financial statements, including non-GAAP financial measures and operational KPIs.



Opportunities for change

Reporting and assurance need to expand to cover critical performance measures

Company stakeholders use information beyond the financial statements in their decision making. In fact, non-GAAP financial performance measures and non-financial performance measures are often key value drivers critical to assessing the performance and future prospects of a company. But these measures are not included in the scope of today's audit.

Often, non-GAAP financial performance measures have emerged because today's financial reporting framework has not adapted to the emergence of new value drivers and therefore GAAP performance information (i.e. that presented in accordance with generally accepted accounting principles, such as IFRS) gives an incomplete picture. Accounting standard setters should continue to allow the financial reporting framework to evolve to remain relevant. However, in the meantime, audit committees should be encouraged to consider commissioning assurance over critical non-GAAP financial performance measures. Although this would be outside the scope of the statutory audit, it may be that in many cases it is most appropriate for the external auditor to perform this work.

In implementing such a change, it would be important to consider the following:

- Defining what is meant by 'critical'. There is a danger that if only certain measures are assured, it could result in 'cherry picking' by the company. A potential solution would be to require those measures that are related to a principal risk and that are most difficult to reconcile to GAAP numbers to be subject to assurance.
- There is usually no recognised framework for calculating and disclosing non-GAAP financial performance measures, so a framework would need to be created to ensure consistency and act as a basis for assurance. For common non-GAAP financial performance measures, this could be developed by the regulator, building on existing principles for disclosure of such metrics as a starting point. Even in the absence of a recognised framework, it could still be possible to give some degree of additional assurance over the measures by using criteria set by the company and assessing the suitability and clarity of presentation of those criteria. This would, however, mean the company would need to make its basis of presentation disclosures much more robust.

In addition, given stakeholders' focus on a company's non-financial performance measures, the audit committee could consider the need for, and source of, assurance over these measures as part of the Assurance Map exercise (see page 37).

What we heard

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The audit needs to recognise companies' different sizes and types

There is strong appetite amongst investors and businesses—large and small, listed and family-owned—for making the scope of the audit flexible and tailored to the type of company being audited.

Small and medium-sized entities (SMEs) in particular support a scaled-back audit, arguing that applying a single common audit framework is too rigid for the needs of their stakeholders.

The amount of work done by the auditors, the level of documentation necessitated by increasing regulation and complexity and the related audit cost is seen to be out of proportion to their needs.

However, for some companies there was some consensus for greater levels of scrutiny and assurance, given the potential damage they could cause if they collapsed. This was thought to be especially relevant for those businesses with contracts to deliver public services funded by the taxpayer.



Opportunities for change

Provide additional assurance over the companies that need it, without expanding the statutory audit for all

At this stage, it is difficult to see how the audit could be scaled down for smaller companies. Nevertheless, given the strong calls from small and medium-sized businesses, it would be valuable to discuss further how the scope of the statutory audit could be tailored appropriately. For larger and more complex companies, the Assurance Map (see page 37) could be a useful mechanism to tailor the need for any additional assurance. This would offer a way of identifying areas for further assurance for companies where it is needed, without expanding the scope of the statutory audit and so potentially overburdening smaller businesses.

What we heard

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Continued investment in technology will enable a better audit

There was optimism from the investors and businesses we surveyed about the effect technology will have on the audit. As today's emerging applications, such as data analytics, automation and artificial intelligence, are more widely applied—and new ones developed—the expectation is that they will drive up both the efficiency and effectiveness of audits.



Opportunities for change

Continue to develop and roll out new technologies to improve the effectiveness of audits

So far across the profession, much of the investment in technology has been focused on developing tools to automate and enhance existing audit processes. This will continue to remain a core part of technology's role in the audit, but there is also the opportunity to enable the audit to evolve to provide assurance over new areas.

One example could be helping to provide assurance over non-financial information by using natural language processing to deal with large bodies of unstructured data.

Another area could be helping to identify fraud, using data analytics and machine learning. By 'training' the machine on large data sets where fraud had been committed it can learn which patterns to spot. But this won't be a silver bullet; the techniques used to commit fraud constantly evolve, so the response will have to change as well.

By operating with a clear set of programmable parameters and relying on logic, machines give much greater comfort when processing large amounts of data. But someone will always be needed to programme the machine, guide the artificial intelligence and offer experience as the basis from which machines can learn. That's why as a profession we need to think creatively about how we best develop the skills auditors will need for the future.

What we heard

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Auditors should deliver consistently high quality audits

There have been some recent well-documented cases in which audit quality has fallen short of requirements. We heard from many participants at our roundtable events that their faith in audit quality had been shaken.

Across the country, there was agreement that high audit quality was central to sustaining trust in the audit. And in turn, that trust underpins confidence in the information companies disclose and in the capital markets more broadly.



Opportunities for change

Increase investment in the training, technology and people required to conduct consistently high quality audits

Ensuring that every audit is of high quality requires the profession as a whole to strengthen and innovate its approach to delivering audits. This involves making a commitment to training and developing people, equipping them to do their jobs well by ensuring they have access to the technology and processes they need and creating the right culture, governance and oversight.

Continue to reflect on how auditors can better tackle the risk of fraud

In our experience, no proportionate system of internal control or audit can fully eliminate the risk of fraud, particularly when the financial impact is relatively low. However, consideration could be given to broader use of techniques such as fraud diagnostic surveys and involving forensic specialists at the planning stage.

As noted above, technology also has the potential to help the auditor identify fraudulent activities.

Strengthen the culture of challenge

Auditors' ability to challenge a company's management is an essential component of delivering a high-quality audit. At the heart of this is ensuring there is—and is seen to be—an appropriate degree of independence between the auditors and the management team.

But to challenge effectively, auditors also need to have a thorough understanding of the business and a working relationship with management. Ensuring every audit team has a culture of challenge and independence is critical for the whole profession.

Strengthening PwC's focus on audit quality

We are committed to continually improving and strengthening audit quality, and that is why we have introduced measures to ensure we deliver consistently high quality audits that meet the needs of investors, companies and society.

Our plan has three areas of focus:

1 Investing in training, people and technology

Investing an additional £30 million annually, targeted on training, people and technology initiatives

Doubling the face-to-face training programme for all our experienced auditors

Creating a new national 'digital audit team' focused on the development and roll-out of innovative technologies that will drive audit quality

Hiring over 500 additional experienced auditors across the UK

2 Further aligning the audit business behind audit quality

Creating a practice with a focus on external audit and strengthening its governance with our Independent Non-Executives

Undertaking a comprehensive review of the entities that we audit to ensure we achieve a return that allows continual investment in and focus on quality

3 Reinforcing a focus on culture and quality control

Increasing by two-thirds the number of specialists in our audit quality control team to enable them to conduct real-time reviews of ongoing audits

Commissioning an independent paper from Karthik Ramanna, Professor of Business & Public Policy at the University of Oxford's Blavatnik School of Government, on what a culture of challenge means for auditors in 2019. This will help inform our training and policies within the audit practice



Appendix: Survey results in detail

Survey methodology

PwC UK conducted an online survey between 4th and 25th April 2019, in which we received responses from 175 members of the investment community and 198 members of the business community. The respondents to the online survey were spread across a range of industries, roles and company sizes.

Notes:

- Not all figures add up to 100% as a result of rounding percentages and exclusion of 'neither/nor' and 'don't know' responses and unanswered questions.
- The rounded percentages for each response have been aggregated to reflect general support or opposition to a question. For example, 'tend to support' and 'strongly support' responses have been combined. Similarly, 'somewhat effectively' and 'very effectively' responses have been combined.

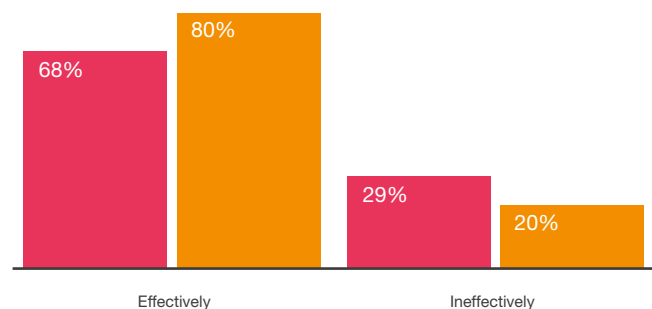
The online research was undertaken by PwC Research, the PwC Network's centre of excellence for primary research and evidence-based consulting services.

Key

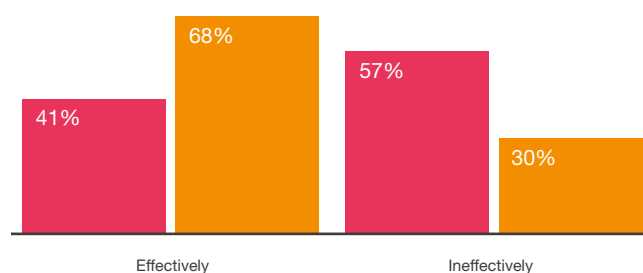
Investment community Business community

Q. In general, how effectively or ineffectively do you think today's statutory audit serves the needs of companies being audited, investors in audited companies and other stakeholders?

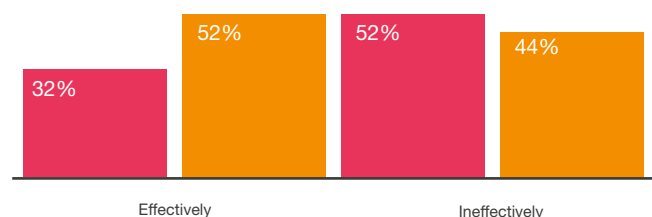
The company being audited



Investors in the audited company



Other stakeholders of the audited company

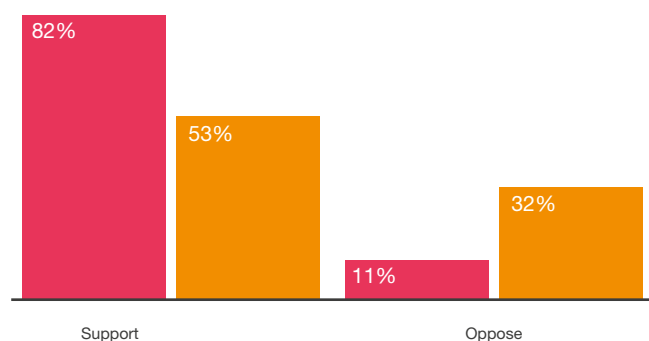


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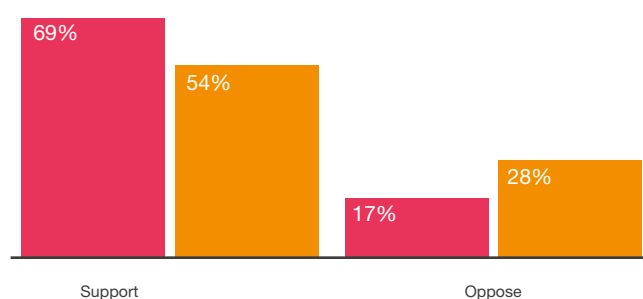
Investment community Business community

Q. For each area listed below, please say whether you support or oppose its inclusion in the central scope of the statutory audit.

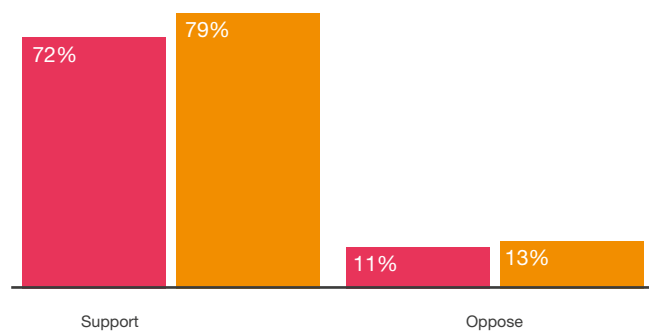
Any fraud (however material)



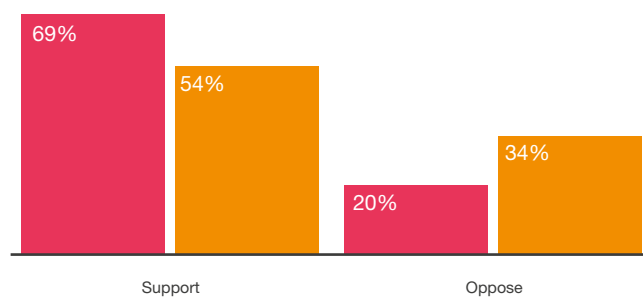
Financial information presented outside the annual report



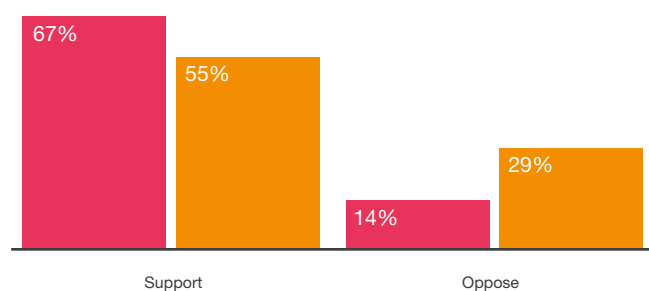
Key risks and uncertainties facing the company



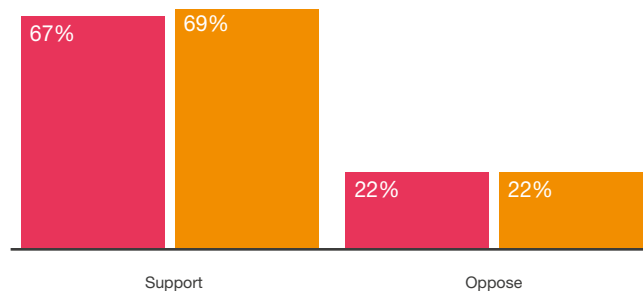
Compliance with all relevant laws and regulations



Operational KPIs



The long-term viability of the company

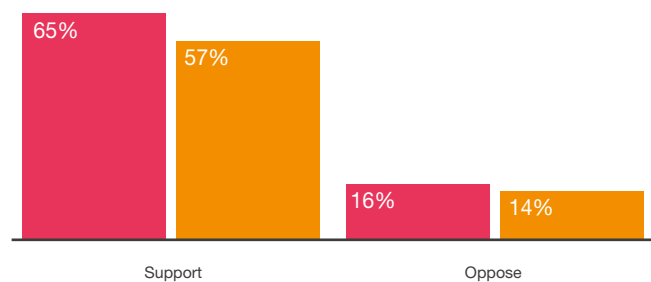


Key

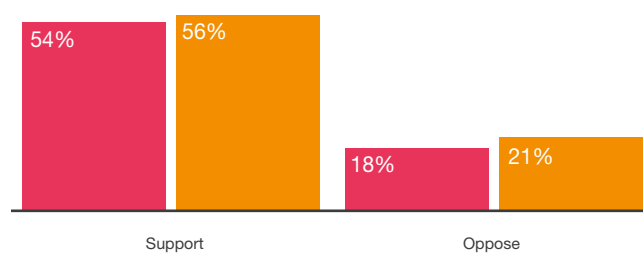
Investment community Business community

Q. For each area listed below, please say whether you support or oppose its inclusion in the central scope of the statutory audit.

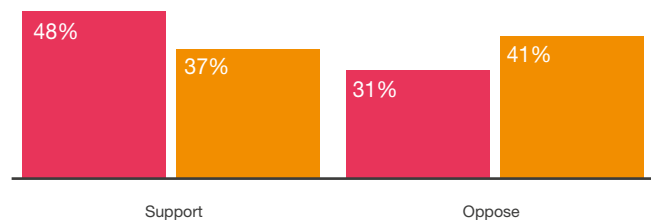
Non-GAAP financial measures



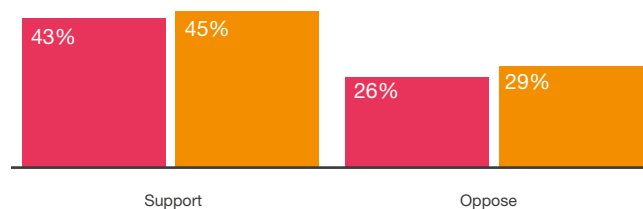
Dividend policy and distributions



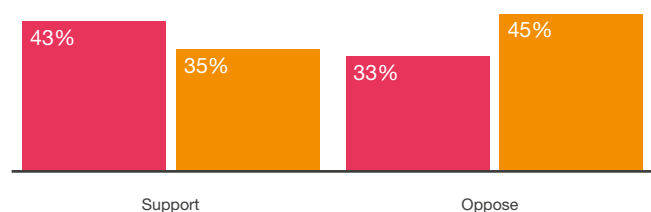
Forecasted performance metrics



Sustainability KPIs



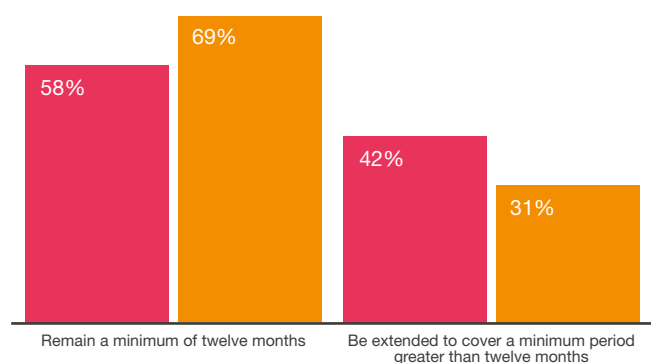
Corporate culture, ethics and behaviour



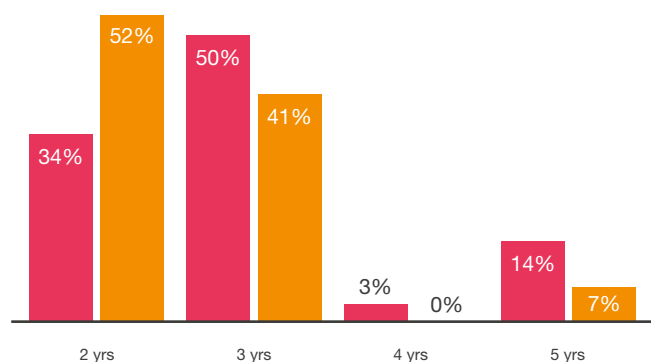
Key

Investment community Business community

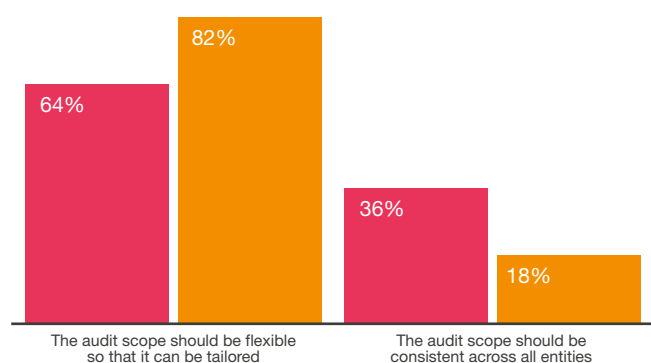
Q. Thinking about the time period covered by the going concern assessment, should it:



Q. If you think the period should be extended, what is the minimum time period you think the going concern assessment should cover?



Q. Thinking about the audit scope for companies of different sizes and types, which of the following statements comes closest to your view?

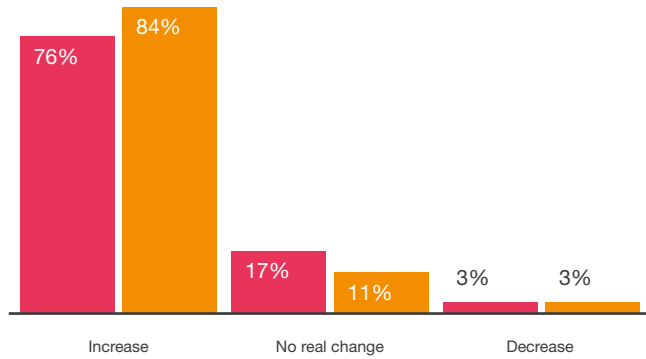


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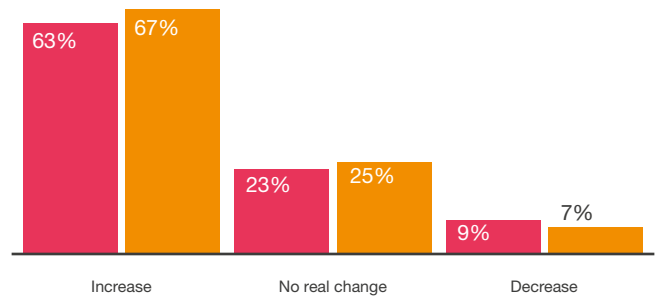
Investment community Business community

Q. Thinking about the use of technologies such as artificial intelligence, automation and data analytics in performing audits, do you expect greater use of these technologies to increase or decrease each of the following aspects of audit?

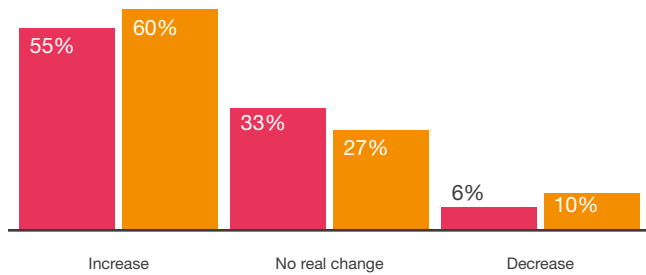
The efficiency with which audits are performed



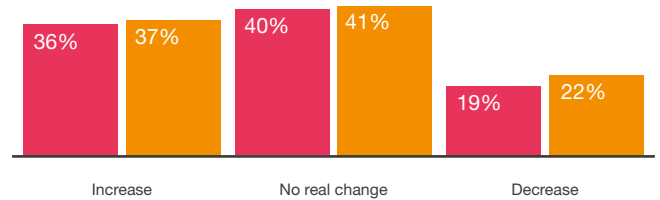
The ability of auditors to scrutinise and challenge the audited entity



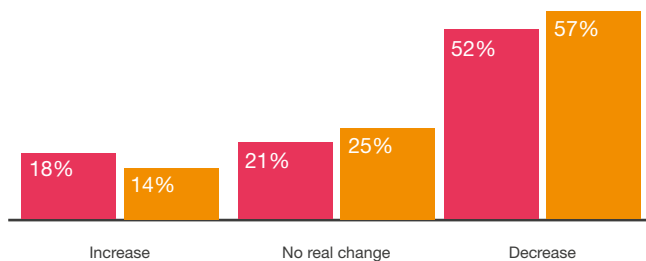
The overall quality of audits



The ability of an auditors to understand the details of a business and how it works



The opportunities for junior auditors to gain necessary experience through routine auditing tasks

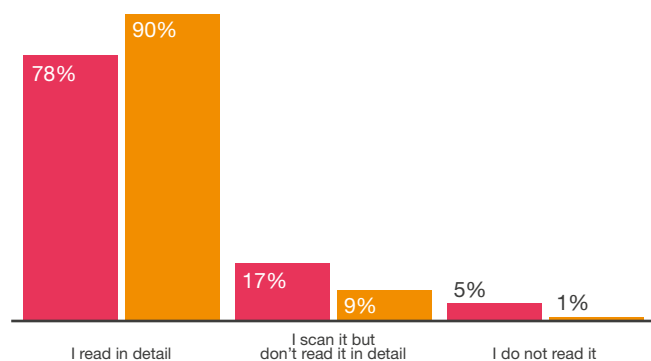


Key

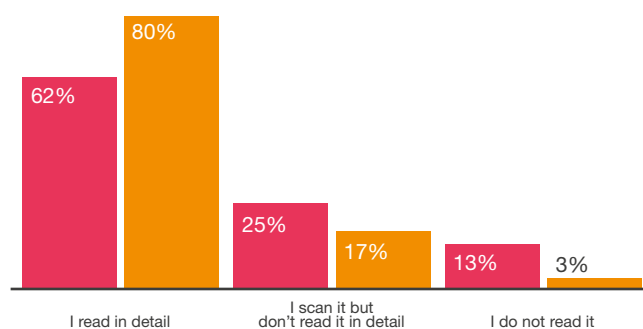
Investment community Business community

Q. Thinking about the audit reports for your company or the companies you invest in, to what extent, if at all, do you generally read the following sections?

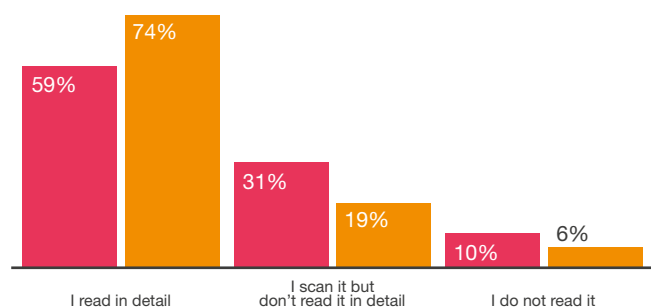
Any qualifications, exceptions or emphases noted by the auditor



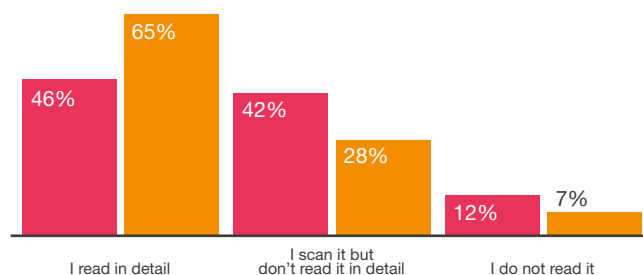
Key audit matters



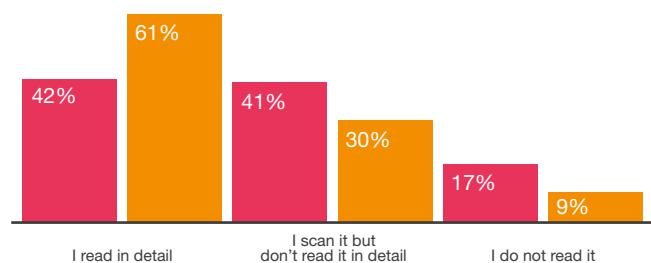
Conclusions relating to going concern



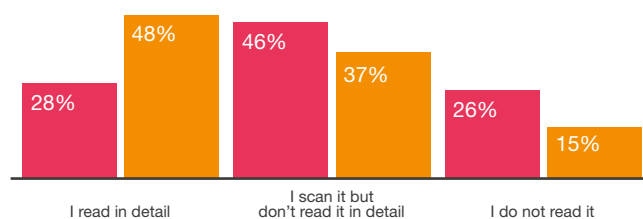
The audit opinion



Materiality



Scope

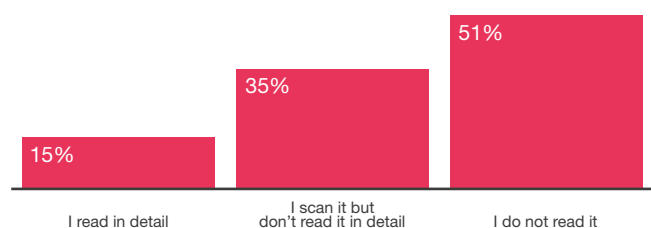


Key

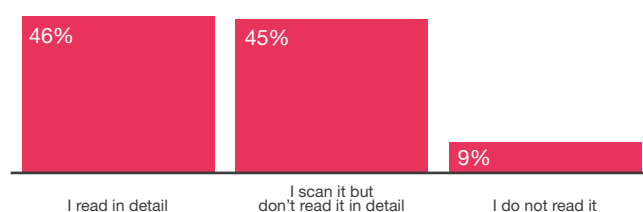
Investment community Business community

Q. Thinking about the audit reports for the companies you invest in, to what extent, if at all, do you generally read the following sections?

The name of the audit partner

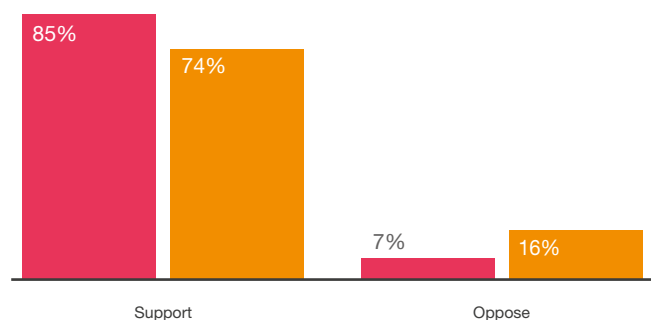


The name of the audit firm

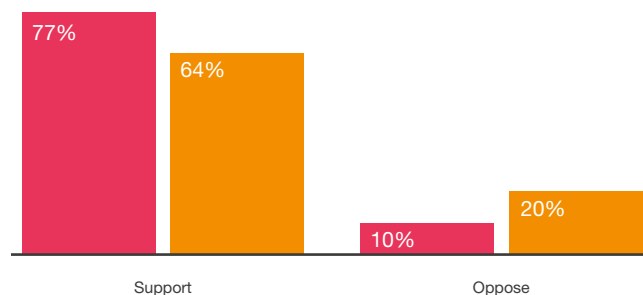


Q. Thinking about audits in the future, please say whether you support or oppose the inclusion of the following types of opinion in the audit report.

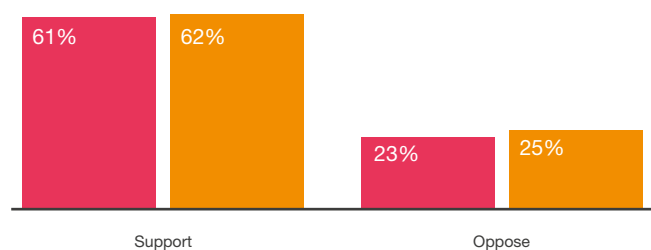
A narrative and qualitative explanation about the auditor's overall findings



Graduated findings



An overall binary pass or fail opinion on whether a company's accounts give a true and fair view



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