Institute of Chartered Accountants in England & Wales

THE CONTEMPORARY NATURE AND SIGNIFICANCE OF THE EXTERNAL AUDIT FUNCTION: AN EMPIRICAL SURVEY OF THE VIEWS OF ICAEW MEMBERS

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TABLE OF CONTENTS

LIST OF TABLES

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EXECUTIVE SUMMARY

BACKGROUND

Recent years have seen a wide range of initiatives, reviews, investigations and policy developments with respect to the external statutory financial audit – both in the UK and internationally. In all of this, there are often mixed messages as to the value of the external financial audit and the need for reform. Some reports will suggest that audit quality is high and that little needs fixing, while others will stress that the basic value of the audit is at risk, if not already declining. Some will position the external financial audit at the heart of the services offered by the profession, others will hardly give it a mention. Some 'vision statements' will stress the need to identify and secure new markets, others will emphasise the importance of dealing first with some fundamental problems associated with the external financial audit, such as the auditor's responsibilities to detect fraud and other illegal acts.

In terms of the desire for change, the external financial audit appears to be under continued pressure to serve broader, but potentially conflicting, sets of demands and interests groups. However, in contemplating attempts to promote change in the external financial audit function, it is noteworthy how often such a function seems to be pulled back to its historical roots. Often in the aftermath of a major corporate failure, concerns are expressed about the independence of auditors, the adequacy of auditor regulation and the extent to which monetary concerns and the desire for self-promotion dominate professional values and commitments to serving the public interest.

SURVEY DETAILS

In the light of continuing debates on the future of the external financial audit, we saw much value in surveying a sample of members of the Institute of Chartered Accountants in England & Wales (ICAEW) – especially given that the membership has been seen recently to hold varying opinions about the education and training of auditors, the status of the small company financial audit and the potential for alternatives such as the independent professional review. The survey was carried out in late 2000, following a series of interviews with 'leading opinion formulators' in the UK audit arena. The postal questionnaire was approved by the ICAEW's Centre for Business Performance and, in the case of audit partners, was distributed with a supporting letter from the ICAEW's Audit and Assurance Faculty.

In total, 202 usable responses were received, giving an overall usable response rate of 25% – a level of response that compared favourably with previous member surveys conducted by the Audit and Assurance Faculty. Respondents were of a senior nature in terms of audit experience. 90% of the responding auditors were partners in their respective firms while 65% of all respondents had been a qualified Chartered Accountant for over 15 years.

SURVEY SCOPE

The survey addressed five major themes: the contemporary status of, and future demand for, external financial auditing services; key auditor attributes and abilities; changes in external financial audit methods; the institutional framework governing the external financial audit function'; and ways of developing the external financial audit. The views obtained paint a complex picture of today's auditing environment –

confirming some existing standpoints but also contradicting others as to where auditing is succeeding or failing and where it needs to change. In particular, views of ICAEW members responding to the survey do differ quite considerably on some issues, depending on the context within which the members are working – whether as *Big 5 auditors, non-Big 5 auditors* or *'non-auditors'*.

MAIN SURVEY FINDINGS

Big 5 auditors are generally the most confident respondent group in believing that:

- the quality of auditing has improved over the last decade;
- auditing remains an attractive career for newly qualified accountants;
- today's external audit methods add more value to businesses being audited and are more effective at detecting material misstatements;
- the relationship between auditors and management is suitably balanced;
- the audit market will be strong in the future.

However, **Big 5 auditors** are the most convinced that:

- a major audit liability crisis exists;
- external audit fees do not adequately compensate audit firms for the risks involved and liability reform is needed across a range of dimensions;
- the reputation of the Big 5 firms exceeds that of the ICAEW;
- major reform is needed in the education and training of Chartered Accountants.

Non-auditors, those respondents working outside of audit firms:

- are the least satisfied in terms of the managerial contribution of today's audit approaches;
- do not regard 'added value business advisers' as a good description of external auditors;
- rate the organisational contribution of the external financial audit as less significant than a number of other audit forms, such as internal audit;
- are the least willing to accept calls for reductions in auditors' liability;
- see UK courts as being reasonably fair to auditors and see little reason for placing financial caps on auditors' liability;
- believe recent changes in external financial audit methods have been stimulated primarily by the desire to improve the profitability of audit assignments;
- feel that external audit fees adequately compensate auditors for the risks involved.

Non-Big 5 auditors are generally closer to **non-auditors** in their views than to Big 5 auditors. In particular, **both groups** feel that:

- the external financial audit is not highly valued by company management;
- internal audit plays a more significant corporate governance role than the external audit;
- the pressure for 'added value' audits is undermining traditional audit attributes.

Non-Big 5 auditors were distinctive in that they were the most supportive of the views that:

- the influence of company management on the external audit should be reduced;
- audit tendering processes are having a negative impact on audit quality;
- auditing standards have become too detailed;

- there should be different levels of attestation for the external audit of listed and non-listed companies.

The significance of the differences between respondent groups was further emphasised by a comparison of the views of Big 5 auditors and those of non-auditors audited by a Big 5 firm. The results showed a greater number of statistically significant differences between these two groups of respondents than between Big 5 auditors and all non-auditors.

INTERPRETING THE SURVEY FINDINGS

Overall, the results confirm that the views held by ICAEW members of the external financial audit are quite closely correlated with their working environment. This is a significant finding as it suggests that the so-called ‘audit expectations gap’ is more than a mere ‘education gap’. If qualified accountants, having gone through similar professional training, hold different views of the audit function, it does suggest that any audit expectations gap is being shaped by something more than differences in technical understanding. This viewpoint is reinforced by the way all respondent groups wanted to make some substantive changes to the role and scope of the audit (although, again, there were differences across the groups as to which changes were most desired). **All groups** wanted the different audit functions in organisations (such as internal, quality, health and safety, social and environmental audits) to become more integrated and felt that external auditors should be reporting on more than just the truth and fairness of a company’s accounts. Clear majorities of **each respondent group** wanted auditors to report on:

- the effectiveness of the organisation’s internal controls;
- the future viability of the organisation;
- organisational compliance with corporate ethical codes;
- any significant breaches of legislation (not just of company law).

There was also majority support in at least one respondent group for:

- external auditors to report on management integrity (supported by a majority of **non-Big 5 auditors** and **non-auditors**);
- external auditors to report on key operational business risks (supported by a majority of **Big 5 auditors** and **non-auditors**);
- more frequent external reporting as the electronic provision of financial information increases (supported by a majority of **Big 5 auditors**);
- auditors to become more active in detecting corporate corruption and money laundering activities (supported by a majority of **non-Big 5 auditors** and **non-auditors –** although there was a general acknowledgement across groups that external auditors have little chance of detecting senior management-led fraud);
- more informative external audit reports, in terms of disclosing where auditors have relied on senior management assurances, what material errors have been detected and what levels of materiality and audit risk have been applied by the auditor (all supported by a majority of **non-auditors**).

There was virtually unanimous support **across respondent groups** for auditors to be, and be seen to be, independent, and a general reluctance to reduce the regulatory involvement of the professional bodies. There was also a strong desire **across respondent groups** to preserve the requirement that there must be a majority of chartered accounting partners within audit firms. Interestingly, some traditional and, now, once again, topical reform options (such as placing restrictions on the provision of non-audit services and changing the auditor appointment process) were not strongly supported by **any respondent group** – although, in terms of statistical significance, **non-auditors** were the group with the highest level of minority support for such reforms. Given such responses, it was particularly interesting to see a clear level of support **across all groups** for another current avenue of reform – namely, strengthening the role, independence and public visibility of audit committees.

An intriguing aspect to the various calls for change is that they came on the back of some positive viewpoints about auditing. For instance, majorities in each **respondent group** felt that: the quality of auditing has improved over the last decade; the transparency of published company annual reports in the UK is generally high; audit committees have significantly improved standards of corporate governance; and that external opinion shopping by senior company management is very rare. Yet, change was still seen as necessary – although respondents acknowledged that it needed to be accompanied by some action on the part of users (not to expect too much of auditors), institutional investors (to become more active in processes of corporate governance) and corporate management (to give more attention to their responsibilities for preventing fraud and error).

SURVEY IMPLICATIONS

There are a number of broad implications of the survey. Overall, it highlights:

- the need for more debate and research on the external financial audit function;
- that there is still much to discuss about the scope, delivery, reporting and regulation of traditional external financial audits;
- that more needs to be known about the practical operation and impact of current audit methods;
- the need to review the degree of variation allowed in auditing mandates and the extent to which there can be different rules and regulations governing the audit of companies of different size (and the education and training of auditors on such audits);
- the scope for reviewing auditor responsibilities and exploring how developments in financial audit mandates can gain broad approval.

For those seeking a more socially relevant and intrusive external audit function, the results will be disappointing as there was little support for extending the auditors' remit to other 'stakeholder' groups and for auditors to report explicitly on the social and environmental impact of organisational activities.

Overall, the survey results emphasise the importance of consultation and interaction by professional bodies with their members. Leaving policy to be determined by Big 5 auditor representatives, for instance, would mean that some important issues are unlikely to get appropriate consideration. In the survey, Big 5 auditors were generally most content with the impact of recent developments in audit methods, less supportive of change in the role and obligations of the financial audit and the most supportive of reform in auditors' liability. The clear differences between ICAEW members working for Big 5 firms and those being audited by them suggest that there are some important contextual factors to explore in order to understand precisely how practical experience shapes what individual members regard as appropriate audit obligations and practices.

Ultimately, it is worth remembering that all respondents are members of the same professional body, with similar pre-qualification training and interests in ensuring its future well being. Their views may not sit comfortably with standpoints promoted by either leading professional representatives or their critics. However, they emphasise that there is still much to consider and debate with respect to the external financial audit. Most significantly, in light of recent corporate collapses and the desire for regulatory action in the financial audit arena, the survey results should provide a cautionary reminder to those in search of some quick-fix solutions. As seasoned accounting professionals have demonstrated here, change needs to go beyond matters of impression management or educational initiatives to a detailed examination of the role, scope, operation, achievements and possibilities of the external financial audit.

ABSTRACT

This paper presents the views of a sample of members of the Institute of Chartered Accountants in England & Wales (ICAEW) on a range of issues relating to the external financial audit. These include: its current role and status; auditor attributes and abilities; the nature/effectiveness of audit methods; auditor liability and regulatory regimes; and future developments in the provision of, and demand for, external financial auditing services. The responses obtained include both positive and critical views of the external financial audit function and identify a number of areas where significant change is supported. Most notably, a clear majority of respondents see scope for development in the reporting obligations of auditors. The results also reveal a number of significant differences in the views of this sample of ICAEW members, depending on the context in which they are working. Such differences, among accounting professionals provide a timely reminder that audit 'expectation gaps' are not just 'education gaps' but can relate to matters of audit performance. They also suggest that the most vocal claims for change in auditing circles are not necessarily those with the widest levels of support. As the Big 5 firms expand in a range of domestic and international markets and there are increasing international attempts to harmonise national auditing systems, this is a message with relevance well beyond the confines of England and Wales.

1. INTRODUCTION

Recent years have seen a wide range of initiatives, reviews, investigations and policy developments with respect to the external statutory financial audit – both in the UK and internationally. These have included general assessments of audit effectiveness (e.g. see Public Oversight Board, 2000), the added-value potential of auditing (see ICAEW, 1997), the promotion of assurance services (see AICPA, 1998; CICA, 1998, JASTF, 1997), the need for company law reform (see DTI, 2000a; 2000b; 2001) and the effectiveness of audit regulatory regimes (see DTI, 1998; Department of Enterprise, Trade and Employment, 2000; Dewing and Russell, 2001b). There has been much debate over basic concepts of auditing including the independence of auditors and the provision of management advisory services to audit clients (e.g., see Beattie *et al*., 1999; Firth, 1997; Canning and Gwilliam, 1999; Dewing and Russell, 2001a), the liability of auditors (e.g. see Cousins *et al*., 1999), the scope for change in audit reporting (e.g., see Hatherly *et al*., 1998), the nature of audit work and the effectiveness of new audit methodologies (see Beattie *et al*., 2001; Lemon *et al*., 2000) and the obligations of the auditor to prevent and detect fraud (e.g., see APB, 1998b), internal control effectiveness (APB, 1998a; 2001a; Turnbull Report, 1999), the effectiveness of audit committees (e.g. see NYSE/NASD, 1999; ICAEW, 2001) and the relationship between auditing and systems of corporate governance (e.g. see Hampel Report, 1998; APB, 1999, O'Sullivan, 2000; Short *et al*., 1999; CIMA, 1999; Demirag *et al*., 2000).

In all of this, there are often mixed messages as to the value of the external financial audit and the need for reform. Some reports will suggest that audit quality is high and that little needs fixing, while others will stress that the basic value of the audit is at risk, if not already declining. Some will position the external financial audit at the heart of the services offered by the profession, others will hardly give it a mention. Some 'vision statements' will stress the need to identify and secure new markets, others will emphasise the importance of dealing first with some fundamental problems associated with the external financial audit.[1]

An international review of a range of vision statements and professional policy documents reveals a number of different development paths for the external financial audit. At one level, the external financial audit is seen as a mature product, where the major opportunities for growth rest in diversification into other areas/styles of auditing and in satisfying a wider range of stakeholders (see ICAEW, 1997, p. 21). Another option is to deal with some of the longstanding problems which leave auditors struggling to meet user expectations, including: (1) responsibility for the detection of fraud and other illegal acts; (2) the treatment of financial distress and going concern issues; and (3) the treatment of risks, uncertainties and estimates

[1] For example, the CPA Vision Project (2011 and Beyond) in the USA, makes no specific reference to the external financial audit in its identification of 'core services', preferring a more generic description of 'assurance and information integrity' services. While the statutory financial audit can be fitted into this heading, its low status is indicated by the issues raised at the 177 Future Forums (attended by American CPAs, with the emergent issues being used to construct the final vision statement). These pinpointed the need for CPAs to 'become more market driven and not dependent on regulations to keep them in business'. The market was also seen 'to be demanding less audit and accounting and more value-adding consulting services' (http://www.cpavision.org/final_report/page08.htm).

(AICPA, 1998, p. 6). Addressing such ‘tough problems’ were seen as helping the audit to remain competitive, address the ‘audit expectations gap’ and provide a strong foundation on which to build new assurance services (also see JASTF, 1997). Additionally, there is seen to be much scope to make better use of the knowledge gained on audits, using more relationship-based services, tailored to bring additional value to ‘client’ company management (see ICAA, 1998). There is also scope for expanding the business reporting model to include more on-line reporting and continuous assurance systems to establish a more timely and comprehensive information base than that currently provided by annual audited financial statements (see AICPA, 1998, p. 3; CICA, 1998).

In terms of external financial audit methodologies, it is clear that the last few years have seen some significant development projects – most notably the promotion of business risk-based approaches to the external financial audit. The larger firms have been investing heavily in such developments (e.g. see Bell *et al*., 1997; Winograd *et al*., 2000; Lemon *et al*., 2000). Some smaller practitioners, working with the assistance of the major firms, have also latched on to such developments – seeking to promote a 'value-added' approach to the audit of small businesses. In the UK such moves have been supported by the ICAEW's Audit and Assurance Faculty. They are claimed to be ‘re-engineering’ an undervalued audit function and replacing transaction testing with more analytical procedures to facilitate the provision of commercial advice/business risk assessment (for example, see Stewart, 1998, 1999a; 1999b).

However, questions have been raised as to the practical extent of change and the level of improvement in audit effectiveness. Lemon *et al*.’s (2000) review, for example, listed a number of issues needing further investigation. These included the extent to which business risk approaches have been accepted and adopted in practice, the adequacy of the skills base of practising auditors to implement such methodology. They also considered possible conflicts between the traditional objectives of the financial statement audit and the broader objectives of the business risk audit and whether the latter audit approach is creating expectations that cannot be fulfilled and, in turn, potentially undermining success on more traditional performance dimensions. Hatherly (1999) questioned the extent to which the switch to business-risk methodologies is causing the external audit to lose its substantive core and the extent to which changes are being driven by supply-side factors rather than the demands of audit clients (also see Hatherly, 1998; Klarskov Jeppesen, 1998). Power (1998) saw the new ways of talking about auditing as enabling the statutory financial audit to be conceived as a by-product of client servicing.

In terms of the desire for change, the external financial audit has been under some pressure to serve broader, but potentially conflicting, set of demands and interests groups:

> ‘A quality audit is envisaged as one that meets the expectations of the client, other legitimate stakeholders, including the public, the business requirements of the (audit) firm, which nowadays has to include staff development, and complies with audit regulation and auditing standards, which continue to develop. Many see managing a successful practice to achieve all these ends, which might appear at times to be in conflict, as increasingly complex.’
>
> (ICAEW, 2000b, p. 1)

In considering the role of the statutory financial audit, the UK Company Law Review initially recommended that it should be ‘substantially extended and enhanced’ (DTI, 2000a, para. 5.139), especially in terms of auditors' liability to third parties. In light of responses received, however, it was decided not to pursue such a matter, with the development of negligence law being deemed to be ‘best left to the normal process of case law’ (DTI, 2001, para. 8.135). Matters of corporate social responsibility and sustainability, nevertheless, continue to interest senior representatives of the accounting profession (e.g. see Ward, 2001). The Company Law Review has also supported a new, mandatory Operating and Financial Review (OFR) that would incorporate, where deemed relevant by the company’s directors, information on a company's relationship with its employees and other interest groups and the impact of its actions on the community and environment. The extension of the auditor’s responsibilities caused by the requirement for the OFR to be subjected to an 'appropriate' level of auditor review (DTI, 2001, para. 3.42; paras. 8.58-8.63) was accompanied by a recommendation that auditors be given the right to limit their liability through a contract with the company, approved by the shareholders in general meeting (DTI, 2000b, paras. 5.156-5.164; DTI, 2001, paras. 8.143-8.144).

The spread of audit into different arenas has been something that has attracted considerable academic attention, most notably in Power's work on the audit explosion and his thesis on the audit society (see Power, 1994; 1997) and studies inspired by his work (e.g. Strathern, 2000; Bowerman *et al*., 2000). It is a point of some debate as to the degree to which the external financial audit has been the driving force behind such a growth in auditing activity (e.g., see Humphrey and Owen, 2000; Power, 2000). However, Power’s observation that such an expansion in audit activity has come at a time when the external financial audit has never been subject to such a degree of public criticism remains intriguing. For instance, Owen *et al*. (2000) and Swift *et al*. (2000), exploring developments in the respective fields of social and quality audit, have shown that such audit forms are increasingly struggling with what have been longstanding problematic issues in the financial auditing arena. Similarly, in a public sector context, it is possible to see audit increasingly getting caught in some familiar tensions between serving the public and/or the executive (management) and between being an external check on the credibility of information and control systems and encouraging entrepreneurial activity and risk-taking (see Bowerman *et al*., 2002; Funnell, 1998).

In contemplating attempts to promote change in the external financial audit function, it is noteworthy how often such a function seems to be pulled back to its historical roots – getting immersed in debates which bear great similarity to those that had taken place 10 or 20 years earlier (see Humphrey *et al*., 1992; 1993; Chandler and Edwards, 1996). Improved regulation and monitoring of auditors are regular requests in the wake of a major corporate collapse/financial scandal, often being formalised in terms of proposals for more formal systems of auditor rotation and the need to ban auditors from providing non-audit services to audit clients.

Some writers have used such recurring patterns to consider whether the ‘expectations gap’ is an inevitable feature of a self-regulated, professional function (see Sikka *et al.*, 1998). Others have heralded the gap as a resource rather than a problem for the auditing profession. It enables the profession to promise something better for the future and gives it the space to engineer shifts in auditing traditions and practices – currently by re-writing the concept of independence and seeking to position audit more centrally within the arena of management and business strategy (e.g. see Klarskov Jeppesen, 1998; Power, 1997; 1998).

The significance of independence traditions and their links with the public responsibilities of the audit profession has been brought into much sharper focus, internationally, over the last two years. Breaches in rules covering the ownership of shares in audit clients initiated a major investigation of the American accounting profession by the Securities and Exchange Commission (SEC). The previous chair of the SEC, Arthur Levitt, clearly placed independence and public responsibility at the heart of the profession’s *raison d’être*:

> ‘But more important than one organization or any one rule, it is the people of this profession who weave the fabric of trust and integrity...people who give life to the concepts and ideals of a profession that demands and expects so much from its members. One generation of accountants passes on the light of independence to the next. That light sustains the profession's life through a culture of integrity, a mission of objectivity and an ethic of responsibility. You have been handed a precious legacy. What you do with it will determine the future of this profession. It is a heavy burden but an awesome privilege.’
> (Arthur Levitt, then Chairman of the US Securities and Exchange Commission, speaking to the Fall Council of the AICPA, Las Vegas, October 24, 2000)

Such messages were reinforced by the final report of the Panel on Audit Effectiveness, set up by the Public Oversight Board following a request by the SEC (see Public Oversight Board, 2000). This stated that its in-depth reviews of audits had been favourable and did not support the view that financial audits were being conducted in an ineffective manner (p. ix). However, it went on to express a number of concerns with auditing standards – suspecting that audit firms may have reduced the scope of their audits and levels of testing and stressing that the profession needs to address vigorously the issue of fraudulent financial reporting (listing a number of ways by which the external audit could assume a more ‘forensic’ style in its fieldwork). The Panel stressed the need for audit firms to set a more consistent, supportive view of the value of the audit function:

> ‘The Panel calls on audit firms to reaffirm, within their organizations and to the outside world, the importance of their audit practices and to stimulate their auditors to proudly hold high the banner of objectivity, independence, professional skeptism and accountability to the public by performing quality audit work. Similarly, the panel calls on the AICPA to actively and publicly

> promote the importance of audits. The Panel recommends that audit firms ensure that the performance of high-quality audits is recognized as the highest priority in their professional development activities, performance evaluations, and promotion, retention and compensation decisions.' (p. xi)

The Panel went on to emphasise that, in the final analysis, the most important determinants of audit effectiveness are the personal attributes and skills of the individual auditor:

> 'The personal attributes of individuals provide structure and definition for their role in society and establish the foundations for what constitutes a true professional. For the individual auditor, these attributes are independence in fact and in appearance, adherence to strong ethical standards, a great sense of personal integrity and the will to act objectively even in the face of intense pressures. Most importantly, individual auditors, as members of a respected profession, should assign their highest priority to protecting the public interest.' (pp. xiii-xiv)

New disclosure rules regarding non-audit services provided by auditors were issued by the SEC in November 2000, but were seen by some to be a very watered down version of the reforms that had initially been on the SEC's public agenda. The dramatic collapse of Enron, the US energy company, has brought forth further calls for substantial reform, with Arthur Levitt, emerging from retirement to question, in the editorial section of the *New York Times* (17/1/2002), 'Who audits the auditors?' He has argued that Congress and Federal regulators should use the Enron scandal to demand changes, especially in terms of placing limits on the consulting work performed by accounting firms for their audit clients and the need for a more independent form of audit regulation. The current SEC Chairman, Harvey Pitt, has stated that he will be considering a range of regulatory reforms, including mandatory auditor rotation.

Questions have been raised as to the specific UK relevance of recent American developments and the danger of assuming that any proposed reforms of the rules governing the US accounting profession need to be applied on an international scale. Indeed, it has been suggested that the UK already has a sufficient degree of independent regulatory oversight and that there is much that the US could learn from the less-rule based traditions of regulation and practice in the UK. Interestingly, an argument that has been used in defence of current UK audit practice is that much good audit work cannot come to the surface – with client confidentiality requirements preventing auditors from drawing attention to cases where audits have led to major improvements in standards of client company management and performance (e.g. see *Accountancy Age*, 24/1/02, pp. 8-9). That said, there have been expressions of concern from senior regulators, such as Sir Howard Davies, the chairman of the Financial Services Authority, that the current regulatory set-up would still not prevent such corporate scandals, accounting abuses and apparent audit failures from occurring in the UK (see *The Guardian*, 2/2/2002, p. 28). Such an opinion has stimulated the Treasury Committee, a Select Committee of the House of Commons to examine, in the light of the Enron collapse, the arrangements for financial regulation of public limited companies in the UK (Treasury Committee, Press Notice 13, Session 2001-02, dated 5/2/02).[2]

It was the spirit of such (continuing) international agendas for change and debates on the future of the external financial audit that motivated us, in the latter part of the year 2000, to seek out the views of a sample of members of the Institute of Chartered Accountants in England & Wales (ICAEW). If the public needs to know more about the work and achievements of auditors and if reform needs to be based on something more than knee-jerk reactions to highly public financial scandals, there is potentially much to be gained from studying the views of those close to the audit function - whether they be audit providers, the purchasers of audit services or just those whose accounting work is subject to close audit scrutiny. The timeliness of such a survey was reinforced by the way a number of related initiatives have been suggestive of the ICAEW membership holding rather different opinions over the education and training of auditors, the status of the small company financial audit and the potential for alternatives such as the independent professional review (e.g. see Graham, 1999; Acher, 1999; APB, 2001b; Hatherly, 2002). Debates on the small company audit have tended to concentrate on fairly specific issues such as the level of the audit threshold. However, as some studies have indicated, even the issue of the small company audit exemption needs to address broader issues and uncertainties regarding the value of the external audit. As Acher (1999) concluded, there is a real need to assess the overall costs and benefits of the statutory financial audit and to set any exemption at the level where costs exceed benefits (p. 75).

Above all, the competing range of potential development paths for the external financial audit (for instance, is it set to be a reinvigorated, public spirited function, or one of diminishing public significance? Is it a function that has become more effective or one cut down to the bare bones through commercial pressures?) demands information that goes beyond the official, ‘marketing’, material put out by the large accounting firms and the relevant professional accounting bodies. Indeed, in the past, studies of audit expectations have tended to treat the views of the accounting profession in a rather uniform manner, comparing the overall views of auditors (as a group) with those of others, e.g. investors, bankers etc. This has encouraged the conclusion that the gap is more of an education rather than a performance gap. However, if ICAEW members, with similar professional training but now working in different parts of the accounting profession, are found to have quite different views of the external financial audit, it does suggest that ‘gaps’ in expectations go beyond matters of education.

In the following sections of the paper, brief details of the nature of the survey instrument and response rates are provided (section 2), together with an overview of the differing responses of members to the main issues addressed in the questionnaire (sections 3-8). The final section (9) of the paper assesses the overall significance of the differences observed and considers the audit policy and research implications of the survey.

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[2] For a brief review of parallel investigations by the Financial Services Authority (FSA) and the Review Board and recent responses by the Big 5 firms, see the *Financial Times*, 7/2/2002, p. 5 and Appointments Section, p. II).

2. SURVEY DETAILS

800 questionnaires were sent to a random sample of ICAEW members in autumn 2000. The questionnaire was designed to cover a broad range of issues relating to the external financial audit function. The questionnaire was constructed following a comprehensive literature review of professional and academic auditing and accounting journals/publications, together with a series of 60 interviews held with 'leading opinion formulators' in the UK audit arena. These included specialists in financial audit and also in a number of other audit functions, such as social, environmental, quality, internal and public sector audit, together with a number of regulators, civil servants, financial directors, academics and other users of audited financial statements. The questionnaire was thoroughly piloted (involving a number of practising auditors and accounting academics). It was also approved (same view as earlier comment) by the Centre for Business Performance of the ICAEW and, in the case of audit partners, the questionnaire was distributed with a supporting letter from the ICAEW's Audit and Assurance Faculty.

In total, 202 usable responses were received, giving an overall usable response rate of 25%.[3] This level of response compares favourably with previous member surveys conducted by the Audit and Assurance Faculty, which normally have generated response rates of around 10%.[4] In terms of the basic distribution of responses, 18% of respondents were female and 82% male. Respondents were of a senior nature in terms of audit experience. 90% of the responding auditors were partners in their respective firms while 65% of all respondents had been a qualified Chartered Accountant for over 15 years. 36% of respondents were members of the Audit and Assurance Faculty, while 63% were university graduates, of whom 17% had a degree in accounting or business studies.

In the analysis which follows, the responses are split into three different, but evenly distributed sets of respondents – namely, ICAEW members working in practice with one of the Big 5 firms, members in practice with a non-Big 5 firm[5] and ICAEW members not in practice (e.g. working in industry and hereafter referred to as 'non-auditors'). The basic split between auditors and non-auditors allowed the opportunity to explore differences in the views of those involved in the provision and purchase/consumption of external auditing services. The division between Big 5 and non-Big 5 auditors gave an opportunity to judge the extent to which views on auditing practice are related to the context/environment in which auditors are working.

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[3] Additional non-usable questionnaires were received from ICAEW members no longer in audit practice and unwilling to complete the questionnaire (giving a total response rate of 32%).

[4] The main exception to this figure was the Audit and Assurance Faculty's survey on the issue of audit exemption and the appropriate threshold level. Conducted in late 1999, this generated, according to the Audit Faculty's *True and Fair* bulletin a 'staggering' 25% response rate, 'some 2.5 times the normal rate for a postal survey' (*True and Fair*, December/January 1999/2000, p. 2).

[5] The breakdown of numbers gave 50 Big 5 auditors, 76 non-Big 5 auditors and 69 'non-auditors' (7 respondents did not indicate an audit firm category). Non-Big 5 auditors included 28 respondents who classified themselves as working for a 'Top 6-50' accounting firm and 48 respondents who stated that they worked for either 'a local firm or as a sole practitioner'. The respective views of the 'sub-groups' were analysed and found to produce very few statistically significant differences, making it acceptable to treat them as one group.

The views obtained paint a complex picture of the auditing arena – confirming some existing standpoints but also contradicting others as to where auditing is succeeding/failing and where it needs to change. In particular, views of ICAEW members do differ quite considerably on some issues, depending on the context within which the members are working. In general, Big 5 auditors have the most positive views of the audit function. Non-Big 5 auditors tend to be closer in their views to non-auditors than to those of Big 5 auditors. This relative similarity in the views of non-Big 5 auditors and non-auditors could have been due to the latter essentially being non-Big 5 clients. The analysis of the results, accordingly, sought to control for such a possibility by comparing the views of Big 5 auditors and those of non-auditors working in organisations audited by a Big 5 firm. The results, interestingly, showed more statistically significant differences between these two groups of respondents than between those reported here for Big 5 auditors and all non-auditors.

In the sections which follow, the differing views are analysed in terms of five major themes: the contemporary status of, and future demand for, external financial auditing services; key auditor attributes and abilities; changes in external financial audit methods; the institutional framework governing the external financial audit function; and ways of developing the external financial audit.

3. THE STATUS OF, AND FUTURE DEMAND FOR, THE EXTERNAL FINANCIAL AUDIT

The general picture of the external financial audit portrayed by respondents was quite diverse. There were some very positive views, particularly in terms of improvements in the overall standards of audit work, but also some clear question marks over the nature of the audit market and the perceived contribution of the external financial audit.

TABLE 1: THE CONTEMPORARY STATUS OF THE EXTERNAL STATUTORY AUDIT FUNCTION

Percentage of respondents agreeing or tending to agree with the following statements:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds.**	**Stat. Sig.**
Over the last decade the market for auditing services has become more competitive	93%	96%	96%	88%	NS
Over the last decade, external auditing has become a significantly less profitable activity	76%	77%	80%	72%	NS
The external audit is highly valued by most company management	36%	52%	32%	29%	NS
'Added value business advisers' is a good description of external auditors	37%	60%	40%	18%	0.00
Internal auditing plays a more significant corporate governance role than the external audit function	68%	50%	79%	79%	0.01
Users of audited accounts generally expect too much of external auditors	80%	90%	81%	72%	0.05
External auditors have little chance of detecting senior management-led material fraud	66%	60%	67%	70%	NS
The transparency of published company annual reports in the UK is generally high	61%	72%	56%	57%	NS
The quality of external auditing has improved over the last decade	68%	88%	64%	58%	0.00
Audit committees enhance the independence of the external auditor	80%	94%	77%	74%	NS
Audit committees have significantly improved standards of corporate governance	73%	84%	65%	72%	NS
External audit 'opinion shopping' by senior company management is a very rare activity	59%	63%	57%	60%	NS
The external auditor's review of a listed company's corporate governance procedures is a valuable addition to the annual report	66%	76%	61%	65%	NS
External auditing is an attractive career option for newly qualified chartered accountants	53%	70%	41%	54%	0.01
Putting external audits out to tender undermines audit quality	48%	38%	65%	36%	0.00
External audit fees adequately compensate audit firms for the risks involved	48%	26%	43%	70%	0.00

Starting with the latter issues, each group very much agreed that the market for external financial audits had become more competitive over the last decade (at least 88% support) and that such audits had become a significantly less profitable activity (at least 72% support). In terms of the contribution of the external financial audit, just 36% of respondents felt that it is highly valued by most company management.

Similarly, only 37% of respondents thought that the term ‘added value business adviser’ is a good description of the work of the external auditor.[6] Significantly, while the drive behind the promotion of ‘added value’ audits has been premised on the need to make the audit more valuable to corporate management (see ICAEW, 1997), only 18% of ‘non-auditors’ felt happy with the description of auditors as ‘added value business advisers’. 79% of ‘non-auditors’ were of the view that internal auditing plays a more significant corporate governance role than the external financial audit (a view shared by 79% of non-auditors and 50% of Big 5 auditors) – potentially reflecting the emphasis placed on internal audit in the Turnbull Report (1999). Over 70% of respondents felt that users of audited financial statements expect too much of auditors, with over 60% of each respondent group acknowledging that external financial auditors have little chance of detecting senior management-led material fraud.

Despite such views and concerns, there were also some very positive messages about the external financial audit. Majorities of each respondent group felt that: the transparency of published company annual reports in the UK is generally high; the quality of external financial audits has improved over the last decade; audit committees enhance the independence of the external financial auditor and have significantly improved standards of corporate governance; external audit ‘opinion’ shopping by senior company management is a very rare activity; and the external auditor’s review of a listed company’s corporate governance procedures is a valuable addition to the annual report. Generally, Big 5 respondents were the most positive about the quality of external financial audits and the attractiveness of auditing as a career for newly qualified accountants. Big 5 auditors were also less accepting of the view that audit quality is being undermined by audits being put out to tender (non-Big 5 auditors being the most critical of such a development). However, Big 5 auditors were also the group least supportive of the statement that external audit fees adequately compensate audit firms for the risks involved. Just 26% of them took such a view, compared to 70% of non-auditors, who clearly suggested that any reductions in auditing profit margins over the last decade had been reasonable.

In order to explore further the contribution of the external financial audit, ‘non-auditor’ respondents were asked to rank on a four point scale[7] the value of the role played by the external financial audit in comparison to a number of other organisational audit functions. They were also asked to indicate their likely demand for a range of audit and advisory services in the future.

[6] In both of these latter two cases, it was only Big 5 auditors who expressed majority support for such statements.
[7] The categories on the four point scale ranged from (1) ‘no value’ to (2) ‘limited value’, (3) ‘quite valuable’ and (4) ‘very valuable’.

TABLE 2A: THE ORGANISATIONAL CONTRIBUTION OF AUDIT

Percentage of non-auditors stating that the following audit functions played either a quite or very valuable role in their organisation:	**Non-Auds.**
Internal audit	58%
Health and safety audit	54%
Quality audit	48%
External financial audit	35%
Environmental audit	32%
Value for money audit	26%
Social audit	5%

In terms of rank order, the contribution of the statutory financial audit was placed fourth, behind internal, health and safety and quality audits. Each of these four audit functions received an average rating between 'limited value' and 'quite valuable'. Three other audit functions (social, environmental and value-for-money audits) were rated, on average, as providing between 'no' and 'limited' value – which sits uncomfortably with the recent drives by leaders in the ICAEW to promote the value of broader-based audit functions (e.g. see Ward, 2001). Interestingly, no audit function received an average rating in the 'quite' to 'very' valuable range.

On average, 67% of respondents from the three groups felt that revenues from non-statutory assurance services would soon dominate those from external financial auditing, while the same percentage supported the view that chartered accountant firms in the future would not face increased competition from alternative providers of external auditing services. This latter position was supported by the responses to another question directed only at 'non-auditors', asking who would be their organisation's most likely first choice provider for the future provision of non-statutory audit and assurance services. 46% stated that this would be their current external financial auditor. A further 25% indicated that they would use another accounting firm, with 14% stating that use would be made of their organisation's internal audit department. Only the remaining 15% indicated that they would use a non-accounting firm (e.g. management consultants or IT specialists).

TABLE 2B: FIRST CHOICE PROVIDERS FOR NON-STATUTORY AUDIT AND ASSURANCE SERVICES

Percentage of respondents who said that one of the following would be their organisation's usual first choice provider for any future non-statutory audit and assurance services:	**Non-Auds.**
Current external financial auditor	46%
Other accounting firm (Big 5)	21%
Other accounting firm (Non-Big 5)	4%
Internal audit department	14%
Management consultancy firm	11%
Information technology (IT) firm	2%
Other firm	2%

The situation for external audit firms, however, looks less optimistic when consideration is given to respondent's expectations of the likely levels of growth in the usage of external auditing and advisory functions – including the statutory financial audit, internal auditing services, e-commerce assurance services, social and environmental audits, quality audits, forensic audits, public sector audits, due diligence work and management consultancy.

TABLE 2C: THE FUTURE DEMAND FOR AUDITING SERVICES

Percentage of respondents expecting either some growth or major growth in the provision (or purchase) of the following services:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds.**	**Stat. Sig.**
Management consultancy	71%	83%	80%	60%	0.00
Due diligence work	69%	94%	63%	54%	0.00
E-commerce assurance services	64%	98%	42%	63%	0.00
'Outsourced' internal audit services	50%	96%	38%	24%	0.00
Forensic audits	49%	86%	42%	21%	0.00
Environmental audits	35%	59%	7%	48%	0.00
Statutory financial audit	34%	63%	28%	15%	0.00
Quality (ISO9001) audits	29%	40%	10%	44%	0.00
Social audits	22%	45%	6%	21%	0.00

Across all three groups of respondents, no activity was expected, on average, to experience major growth. Overall, the three top-ranked growth areas were management consultancy, due diligence work and e-commerce assurance services (with an average ranking between 'little' and 'some' growth). External financial audits were ranked seventh, with an average rating of 'little growth', similar to environmental audits and just ahead of quality, public sector and social audits. Of the three groups of respondents, Big 5 auditors were clearly the most positive in terms of future growth rates. Interestingly, in several cases, the growth rates anticipated by non-Big 5 auditors were lower than those indicated by 'non-auditors' (for example, quality, social and environmental audits and e-commerce assurance services). This suggests that either future business possibilities are being underestimated by these audit firms or that the possibilities are likely to by-pass them in favour of their Big 5 counterparts.

4. CHANGES IN KEY AUDITOR ATTRIBUTES/ABILITIES

All three groups of respondents were fairly evenly split on whether key attributes and abilities of auditors have changed significantly over the last 10 years (overall, 56% of respondents supported this statement). However, there was a clear statistical difference in their views as to whether the pressure for 'added value' external audits is undermining traditional audit attributes. Just 21% of Big 5 auditors agreed with such a statement, compared to 56% of non-Big 5 auditors and 62% of non-auditors. The concerns expressed by non-auditors is again interesting as it suggests that those for whom the audit has been primarily redesigned or repackaged (as a 'value-adding business function') are not that happy with the pattern of development.

TABLE 3A: CHANGES IN KEY AUDITOR ATTRIBUTES/ABILITIES

Percentage of respondents supporting the following statements:	Total Resp.	Big 5 Auds.	Non-Big 5 Auds.	Non-Auds.	Stat. Sig.
Key attributes/abilities of external financial auditors have changed significantly in the last 10 years.	56%	61%	60%	49%	NS
The pressure for 'added value' external audits is undermining traditional audit attributes.	48%	21%	56%	62%	0.00

TABLE 3B: RANKINGS OF KEY AUDITOR ATTRIBUTES AND ABILITIES

Number of 'top four' rankings given to each of the following attributes and abilities of external financial auditors:	1st Rank (no.)	2nd Rank (no.)	3rd Rank (no.)	4th Rank (no.)
Integrity	74	38	13	14
Objectivity	49	48	20	20
Business acumen	24	28	32	23
Generating income/new clients	13	9	4	15
Initiative	10	17	27	21
Scepticism	7	13	13	17
People management skills	4	12	31	31
Industry specific experience	3	7	18	15
Tenacity	2	8	14	14
Loyalty to the firm	1	2	1	5
Information technology skills	1	3	13	7
Sense of public responsibility	0	4	3	6

Respondents were also asked to rank what they regarded as the four most important attributes and abilities of external auditors (from a list of 12 and the option to provide alternative ones themselves). In terms of the top ranked attributes and abilities, those receiving the most first ranks, were 'integrity' (74), 'objectivity' (49), 'business acumen' (24), 'generating income/new clients' (13) and 'initiative' (10). If all four ranks are included, the top ranked attributes and abilities are 'integrity' (139), 'objectivity' (137), 'business acumen' (107), 'people management skills' (78) and 'initiative' (75)

The rankings of key auditor attributes and abilities provided by respondents, were the same, regardless of whether they felt these attributes/abilities had significantly changed over the last 10 years – suggesting that any change is rather more apparent than real. Across the three groups, there was little difference in their respective rankings. The top three ranked attributes/abilities for each group were integrity, objectivity and business acumen, although non-auditors placed statistically more emphasis on objectivity than integrity (when assessed using the Kruskal Wallis test for differences in mean ranks). In terms of other attributes/abilities, only two significant differences were observed (at the 5% level of statistical significance) – with non-auditors placing statistically more emphasis on scepticism and IT skills than the two auditor groups.

5. CHANGES IN EXTERNAL AUDIT METHODS

The overwhelming majority of respondents felt that major change had taken place in external audit over the last decade, with just 11% of respondents feeling that there had been either no or little change.

TABLE 4A: CHANGES IN EXTERNAL FINANCIAL AUDIT METHODS

Percentage of respondents who agreed or tended to agree that the following changes had taken place over the last decade in the external financial audit methods used by their firm or by their external auditor:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds**	**Stat. Sig.**
Greater emphasis is being placed on processes of business risk assessment	96%	100%	94%	95%	NS
Levels of detailed testing of transactions and balances have declined.	94%	96%	94%	92%	NS
More reliance is placed on analytical review procedures.	95%	96%	94%	95%	NS
Specialists are now essential on major external audit assignments.	71%	94%	55%	70%	0.00
Greater reliance is being placed on computer-assisted audit techniques.	70%	81%	50%	82%	0.00
Today's audit methods place a greater reliance on professional judgement.	69%	62%	67%	78%	NS
More use is being made of senior audit firm personnel.	61%	77%	70%	36%	0.00
Any new external audit methods have been rigorously tested prior to implementation.	61%	94%	56%	38%	0.00
The business management skills of today's audit teams have to mirror that of the company being audited.	59%	67%	46%	69%	0.02
Today's external audit methods are more effective at detecting material mis-statements.	55%	73%	46%	51%	0.01
Today's external audit methods add more value to the business being audited.	54%	85%	44%	40%	0.00

Across all three groups of respondents, over 90% of respondents were of the view that levels of detailed testing of transactions and balances have declined and that more emphasis is being placed on processes of business risk assessment and analytical review procedures. Such a finding lends support to the view that changing audit methods are not just the primary preserve of the larger audit firms. At least 50% of respondents in all three groups also felt that today's audit methods place greater reliance on computer-assisted audit techniques (CAATs) and also on professional judgement and that specialists are now essential on major external audit assignments.

Overall, Big 5 auditors generally were the group most accepting of the various claims in Table 4A regarding new financial audit methods, with non-Big 5 auditors expressing a significantly lower level of agreement regarding the use of CAATs, the need for specialists on audit assignments and the need for the business management skills of audit teams to mirror that of the company being audited.

Some statements also produced significant differences between Big 5 auditors and non-auditors. For instance, 85% of Big 5 auditors felt that today's external audit methods 'add more value to the business being audited', while 73% felt that they were 'more effective at detecting material misstatements'. Non-auditors, well placed to assess such additions in value and enhanced detection capacities, were far less confident (as also were respondents from non-Big 5 firms). Just 40% of non-auditors felt that more 'added-value' was being provided by today's audit methods, while a slightly higher proportion (51%) acknowledged an increased error detection capability. An important claim made by audit firms in supporting the new methodologies has been the ability to use more senior personnel on audit assignments (supported by over 70% of respondents from Big 5 and non Big 5 firms). However, according to non-auditors this was not something that was generally taking place, with just 36% of them lending to support such a claim. Non-auditors were also more sceptical with respect to the claimed operational benefits of the new methodologies, with only 38% of them feeling that new external financial audit methods have been rigorously tested prior to implementation. In comparison, 94% of Big 5 and, a significantly lower, 56% of non-Big 5 auditor respondents supported this statement.

Suspicions as to a lack of confidence/faith in the overall effectiveness of today's audit methods were reinforced by respondent's views regarding the motivations for changes in audit methods.

TABLE 4B: PRINCIPAL MOTIVATIONS FOR CHANGES IN EXTERNAL FINANCIAL AUDIT METHODS

Percentage of respondents who felt that the following factors had a MAJOR influence in stimulating changes in external financial audit methods:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds**	**Stat. Sig.**
To improve the profitability of audit work.	49%	44%	40%	63%	0.03
To improve the effectiveness of audit testing	38%	60%	40%	17%	0.00
To realise the benefits of developments in computer technology.	34%	44%	27%	32%	NS
To cope with the increasing complexity of contemporary organisations.	28%	42%	14%	32%	0.00
To meet better the demands of corporate management.	20%	42%	5%	19%	0.00
To give a more dynamic image to the audit function.	9%	6%	9%	10%	NS
To meet better the demands of users of corporate annual reports.	8%	19%	0%	7%	NS
To provide a more interesting working environment for audit staff.	5%	13%	3%	2%	NS

Over 70% of respondents felt that the top five motivations listed in Table 4B had had either 'some influence' or a 'major influence' on the pursuit of new auditing methods. However, again there were some significant differences in views across the three groups of respondents. Big 5 auditors, for example, saw the changes as having been primarily designed to improve the effectiveness of audit work (with 60% of them seeing this as a major influence), but also to improve the profitability of audit work (49% saw this as a major influence) and to realise the benefits of developments in computer technology (34% viewed this as a major influence). Non-auditors, however, appeared more cynical regarding the motives for change. For example, by far and away the single major influence for them was the desire to improve the profitability of audit work. 63% of non-auditors saw this as a major influence compared to just 17% of them who felt that improving the effectiveness of audit testing had been a major factor. There was also a significant difference in the respective influence attributed to the desire to meet better the demands of corporate management – 42% of Big 5 auditors saw this as a major influence, compared to only 5% of non-Big 5 auditors and 19% of non-auditors. Of even less influence was 'the desire to meet better the demands of users of corporate annual reports' – just 19% of Big 5 auditors saw this as a major influence, compared to no (0%) non-Big 5 auditors and just 7% of non-auditors.

Such results suggest that a significant proportion of responding ICAEW members regard recent changes in audit methods as having been driven more by (short-term) financial concerns than a long-term commitment to enhancing shareholder or 'stakeholder' value. Further, the views of respondents also question the effectiveness of the changes in terms of the claimed supply-side benefits of 're-inventing' the external financial audit function. The new methodologies have been promoted as helping to provide a more interesting and challenging working environment for audit staff. However, only 13% of Big 5 respondents believed that this had been a major influence on the change process (and just 3% of non-Big 5 auditors and 2% of non-auditors), while 10% or less of each group saw the need to give auditing a more dynamic image as having been a major influential factor.

6. AUDITORS AND AUDITOR LIABILITY

As noted earlier, a frequent focal point for ideas about enhancing the role and effectiveness of the external audit function has been the institutional framework governing the provision of such a service. A most vocal call for reform over the last few years has concerned auditor liability (e.g. see International Federation of Accountants, 1995; Ward, 1998; Moizer and Hansford-Smith, 1998) and significant majorities of respondents across all three groups acknowledged that "the threat of litigation continues to be a significant barrier to any extension in the role of the external financial audit".

TABLE 5: THE INSTITUTIONAL FRAMEWORK GOVERNING EXTERNAL AUDITING – (1) LIABILITY

Percentage of respondents agreeing or tending to agree with the following statements:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds**	**Stat. Sig.**
There is a major external audit liability crisis.	52%	60%	49%	49%	NS
UK courts usually give reasonable judgements in legal cases concerning the role of external auditors.	63%	48%	63%	77%	0.01
External auditors' current legal liability for negligent actions is fair.	44%	12%	48%	61%	0.00
The threat of litigation continues to be a significant barrier to any extension in the role of the external audit.	78%	92%	76%	68%	0.01
A system of 'proportionate liability' for external auditors should be enshrined in UK law.	74%	88%	75%	52%	0.01
Audit firms should be allowed to operate as limited liability partnerships.	73%	90%	75%	60%	0.00
A financial cap should be placed on external auditors' liability.	68%	88%	77%	42%	0.00
External audit partners should not continue to be jointly and severally liable.	65%	86%	71%	43%	0.00
The practical emphasis on most external financial audits is to detect material fraud.	22%	15%	21%	28%	NS
Auditors would accept greater responsibility for fraud detection if fees could be increased substantially.	61%	62%	67%	65%	NS

All three groups were clearly in favour of the recent legal change in the UK that allows audit firms to operate as limited liability partnerships. There was also a majority of each group in favour of a system of 'proportionate liability' for external financial auditors being enshrined in UK law. Additionally, while a few respondents in each group felt that the practical emphasis on most external financial audits is to detect material fraud, a clear majority in each group (over 60%) felt that auditors would accept greater responsibility for fraud detection if audit fees could be substantially increased. This view very much lends support to a line of argument put forward by the Auditing Practices Board (see APB, 1998b).

Significant differences in views also existed across the three groups and some of these were rather unexpected. Starting with the unexpected results, respondents were very evenly divided over whether there was a major external audit liability crisis. Despite all the claims that have been made in recent years by the Big 5 firms and professional accounting bodies, only 60% of Big 5 auditors and 49% of non-Big 5 auditors and non-auditors saw auditor liability as a major crisis issue. Furthermore, a clear majority of non-Big 5 auditors (63%) and non-auditors (77%), together with a substantial percentage of Big 5 auditors (48%), felt that UK courts usually give reasonable judgements in legal cases concerning the role of external auditors. 61% of non-auditors also took the view that the current legal liability position for negligent actions on the part of external auditors is fair. This was also supported by 48% of non-Big 5 auditors but clearly rejected by Big 5 auditors, with just 12% accepting the statement.

For the two remaining statements in Table 6, non-auditors took a different view to both Big 5 and non-Big 5 auditors. Both of the latter two groups were clearly in favour of a financial cap being placed on the liability of external financial auditors and for external financial audit partners no longer to be jointly and severally liable. In contrast, the majority of non-auditors did not support such developments.

Overall, the views expressed with regard to auditor's liability suggest that it is a problem area but not as significant as some of the professional accounting literature would suggest. Also, there is a fair degree of division among members of the ICAEW as to the best course of action, with some suggestion that liability reform may need to be matched by extensions in the scope of audit services, for instance in the area of fraud detection.

7. AUDITORS AND AUDITOR REGULATION

Respondents generally were supportive of a number of existing elements of the audit regulatory process.

TABLE 6: THE INSTITUTIONAL FRAMEWORK GOVERNING EXTERNAL AUDITING – (2) REGULATION

Percentage of respondents agreeing or tending to agree with the following statements:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds**	**Stat. Sig.**
Routine audit monitoring visits by the Joint Monitoring Unit (JMU) provide a worthwhile control over external audit firms' activities.	78%	75%	76%	83%	NS
It is adequate for the JMU to visit external auditors of listed companies every three years.	76%	83%	73%	73%	NS
Auditing regulatory bodies should be able to investigate immediately in major cases of suspected external audit failure	91%	79%	95%	95%	0.01
Major corporate collapses severely damage the reputation of the auditing profession	84%	80%	80%	91%	NS
The majority of partners in a firm of chartered accountants should continue to be professionally qualified accountants	91%	76%	96%	96%	0.00
Multi-disciplinary partnerships (i.e. of lawyers and accountants) should be allowed by law	83%	92%	72%	78%	0.01
External auditors must not only be independent but also be seen to be independent	97%	94%	97%	99%	NS
No-one working for a firm of chartered accountants should hold shares in the firm's audit clients	81%	80%	86%	75%	NS
Audit committees need to monitor the work of external auditors more actively	66%	66%	56%	75%	NS
Audit committees should have a clear majority of independent non-executive directors	92%	100%	84%	94%	0.01
Listed companies should publish the report of their audit committee	78%	72%	82%	79%	NS
Regulatory bodies (such as the Auditing Practices Board) should have a clear majority of members who are not auditors	38%	39%	31%	47%	0.03

TABLE 6: THE INSTITUTIONAL FRAMEWORK FOR GOVERNING EXTERNAL AUDITING – (2) REGULATION, *continued*

Percentage of respondents agreeing or tending to agree with the following statements:	Total Resp.	Big 5 Auds.	Non-Big 5 Auds.	Non-Auds	Stat. Sig.
External auditors should be appointed by a body independent of the company being audited	27%	22%	24%	34%	0.01
External audits should be provided through separate legal entities which only undertake such work	27%	10%	30%	38%	0.01
The external audit process needs to be less influenced by the demands and desires of company management	67%	48%	81%	65%	0.00
External auditors should be banned from providing consultancy services to audit clients	24%	4%	27%	36%	0.00
Statements of Auditing Standards (SASs) have become far too detailed	67%	48%	80%	66%	0.00
The external audit process would be assisted by having tighter accounting standards	36%	36%	39%	31%	NS
Different levels of attestation need to be established for the external audit of listed and non-listed companies	76%	53%	91%	70%	0.00
There are too many arbitrary ethical rules governing the behaviour of external auditors	54%	62%	47%	57%	NS
The external audit should cease to be a statutory requirement for all private companies	35%	22%	37%	42%	NS
Companies with a turnover below £4.8m should not statutorily be required to have an external audit	48%	78%	37%	46%	0.04
Detailed guidance on matters like independence is best provided by individual firms rather than by the professional bodies/regulators	24%	26%	28%	16%	NS
The reputation of the 'Big Five' firms exceeds that of the ICAEW	71%	94%	64%	63%	0.00
External audit clients dropped by one 'Big Five' firm will usually be picked up by another 'Big Five' firm	87%	81%	87%	93%	NS

For example, at least 73% of each group were supportive of the frequency and effectiveness of the routine audit monitoring visits by the Joint Monitoring Unit (JMU). At least 79% of respondents also felt that auditing regulatory bodies should be able to investigate immediately in major cases of suspected audit failure. This supports recent extensions in the rights of the body charged with the investigation of major audit failures[8] and also reflects the fact that at least 80% of respondents in each group saw major corporate collapses as severely damaging the reputation of the auditing profession.

Over 75% of respondents in each group were supportive of the view that the majority of partners in a firm of Chartered Accountants should continue to be professionally qualified accountants. The removal of this restriction was recently proposed by the Office of Fair Trading (see OFT, 2001) on the grounds that it is preventing the establishment of multi-disciplinary partnerships – 'one-stop' professional shops. However, with over 70% of each group of respondents also feeling that

[8] Formerly the Joint Disciplinary Scheme and now known as the Investigation and Discipline Board (see DTI, 1998; The Accountancy Foundation, 2001).

multidisciplinary partnerships (i.e. of lawyers and accountants) should be permitted in law, it would appear that such a restriction was not perceived to be a major hindrance to such developments (or that the notion of 'multidisciplinary partnerships' was being viewed in fairly conservative terms).

Respondents strongly emphasised the importance of maintaining auditor independence. For instance, at least 94% of respondents in each group felt that auditors should 'be and also be seen to be independent'. At least 75% were also of the view that 'no one working for a chartered accountancy firm should hold shares in the firm's audit clients' – reflecting the concerns raised in the USA by the Securities and Exchange Commission (SEC).[9]

There was quite significant support for the external audit process to be less influenced by the demands of company management. 81% of non-Big 5 auditors and 65% of non-auditors took such a view (together with 48% of Big 5 auditors). Audit committees were seen as an important vehicle here for maintaining auditor independence, with significant majorities of respondents in each group wanting committees: 'to monitor the work of external auditors more actively'; 'to have a clear majority of independent, non-executive directors'; and (for those in listed companies) to publish their report. However, aside from this, independence was not seen as something that could be improved by major structural reform. Only a minority of respondents in each group were in favour of: (1) auditors being appointed by a body formally independent of the company being audited; (2) external audits being provided through separate legal entities that only undertake such audit work; and (3) an outright ban on the provision of management consultancy services by external auditors to their audit clients. Further, although respondents generally wanted regulatory bodies to move quickly in suspected major cases of audit failure, only 38% of them wanted regulatory bodies to have a clear majority of members who are not auditors (despite the current requirements of the newly established regulatory regime in the UK – see The Accountancy Foundation, 2001).

Responses to other questions indicated that a good number of respondents were in favour of a rather more discretionary audit regulatory environment. Less than 40% of each group felt that the auditing process would be assisted by having tighter accounting standards, while majorities of Big 5 auditors and non-auditors felt that too many arbitrary ethical rules currently govern the behaviour of external auditors. However, few ICAEW members wanted to go so far as having detailed ethical guidance being set by individual firms and approved by the regulator – with none of the groups expressing more than 28% support for such a development.

Where differences were observed between the views of the three groups of respondents, they tended to relate to the degree of flexibility that can be applied to the remit or requirements for audit. For example, clear majorities of non-Big 5 auditors (80%) and non-auditors (66%) took the view that Statements of Auditing Standards had become far too detailed, although only 48% of Big 5 auditors took such a view. 91% of non-Big 5 auditors and 70% of non-auditors felt that different levels of audit attestation needed to be established for listed and non-listed companies, compared to 53% of Big 5 auditors. Probably reflecting their client base, Big 5 auditors were the

[9] For a brief review, see *Business Week*, 25 September, 2000, pp. 68-73.

most supportive of raising the 'turnover' exemption for small company audits to £4.8m – the maximum level currently allowed under EU company law directives (78% support compared to 37% of non-Big 5 auditors and 42% of non-auditors). No group, however, wanted the external audit to cease to be a statutory requirement for all private companies.

One of the more interesting findings in this section was that clear majorities of each respondent group (a virtually unanimous view in the case of Big 5 auditors) felt that the reputation of the 'Big Five' firms exceeds that of the ICAEW. Such a reputational difference must cast some doubt on the ICAEW's ability to regulate the Big 5 firms and could well be used as evidence to support those who have claimed that such 'global' firms have become too powerful to be adequately regulated by a national professional body. Such concerns were also reinforced by the way the vast majority of respondents (even Big 5 auditors) felt that external audit clients dropped by one 'Big Five' firm would usually be picked up by another 'Big Five' firm. Such action is somewhat contrary to the image that the Big 5 firms like to present in terms of being tough on risky clients.

8. DEVELOPING THE EXTERNAL FINANCIAL AUDIT

While respondents raised questions over the current status and legal framework governing the external financial audit, they also identified a number of ways in which such a function could develop. Some of the most striking responses related to desired extensions in the scope and form of audit reporting.

TABLE 7A: DEVELOPING THE EXTERNAL FINANCIAL AUDIT

Percentage of respondents agreeing or tending to agree that the external financial auditor of a limited company should be reporting externally (i.e. to shareholders) on the following aspects of the company:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds**	**Stat. Sig.**
Effectiveness of its internal controls	77%	62%	77%	88%	0.00
Social and environmental impact of its activities	29%	22%	25%	37%	NS
Its future viability	69%	60%	68%	78%	NS
Integrity of its management	57%	38%	62%	67%	0.02
Its operational efficiency	39%	20%	51%	42%	0.01
Any significant breaches of legislation	83%	78%	81%	90%	NS
Compliance with corporate ethical codes	73%	74%	73%	73%	NS
Key operational business risks	57%	56%	48%	68%	NS

Despite prior expressed worries over liability exposures, clear majorities of respondents in each group felt that the external financial auditor should be reporting publicly on a number of additional issues for the standard company. These included: any significant breaches in legislation (not just Companies Acts); the effectiveness of the audited organisation's internal controls; compliance with corporate ethical codes; and the organisation's future viability. There was also majority support in two of three groups for the auditor to report publicly on the integrity of management (not supported by a majority of Big 5 auditors); and key operational business risks (not supported by a majority of non-Big 5 auditors). The degree of positive support recorded here sits in some contrast to the concerns of professional bodies over the problematic nature of reporting publicly on some of these matters (e.g. see APB, 1998a; APB, 2001a).

The general willingness of respondents to expand the audit reporting function, however, did not extend to reporting on the social and environmental impact of the audited organisation's activities – with relatively small minorities of each group of respondents supporting such a responsibility. This was somewhat surprising given the considerable institutional pressure recently for development in this area (with the ICAEW having established a quite high profile Sustainability Advisory Group).[10] Such a result also sits somewhat uncomfortably with the support expressed for reporting on compliance with corporate ethical codes. However, with some audits already requiring assessments of compliance with corporate governance or quality assurance codes, it may be that assessments of ethical compliance are less onerous for auditors than having to judge directly the impact of an organisation's activities (for more discussion on the status of audit as a second order control, see Power, 1997; Owen *et al*., 2000). That said, a majority of non-Big 5 auditors were supportive of auditors reporting on the operational efficiency of the company being audited – although this was not supported by Big 5 auditors or non-auditors.

Respondents were also asked to respond to a number of specific statements on ways in which the audit function could develop.

TABLE 7B: DEVELOPING THE EXTERNAL FINANCIAL AUDIT

Percentage of respondents agreeing or tending to agree with the following statements:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds.**	**Stat. Sig.**
The audit report should detail where external auditors have relied on senior management assurances	70%	48%	73%	84%	0.00
External auditors these days rely too much on management assurances	37%	14%	47%	53%	0.00
External auditing is becoming like management consultancy	44%	32%	47%	51%	NS
External audit reports should disclose all detected material errors	42%	14%	47%	57%	0.00
External audit reports should give details of audit materiality levels	34%	20%	27%	54%	0.00
External audit reports should give details of audit risk levels	32%	10%	27%	52%	0.00
A 'free-form' external audit report tailored to meet the circumstances of each company would be beneficial	39%	33%	43%	39%	NS

[10] In a recent speech, Ward acknowledged that reporting on matters such as sustainability and corporate social responsibility is in its infancy, but stressed that independent verification of any such reporting is a critical way of giving confidence to investors:

> '(c)ompanies must now demonstrate that they fully participate in the drive towards ever greater transparency. Internationally recognised principles of governance and transparency, sustainability and corporate social responsibility are now very real drivers of corporate success' (Ward, 2001, p. 8).

TABLE 7B: DEVELOPING THE EXTERNAL FINANCIAL AUDIT, ***continued***

Percentage of respondents agreeing or tending to agree with the following statements:	**Total Resp.**	**Big 5 Auds.**	**Non-Big 5 Auds.**	**Non-Auds.**	**Stat. Sig.**
External audit reports will have to be provided more frequently as advances continue in the electronic reporting of corporate financial information	39%	67%	29%	28%	0.00
External auditors need to become more active in detecting corporate corruption and money laundering activities	55%	45%	55%	62%	NS
Interim financial statements published by listed companies should be externally audited	50%	46%	54%	48%	NS
Company management increasingly want auditors to provide risk management services	68%	84%	63%	60%	0.02
External auditors should be able to participate in management decision making processes	23%	16%	25%	26%	NS
External audits should publicly rate businesses in terms of their exposure to risk	32%	26%	32%	37%	NS
External auditors should have a statutory obligation to report to stakeholder groups other than the company's shareholders	25%	19%	31%	23%	NS
The different audit functions in organisations need to become more integrated	78%	77%	72%	85%	NS
Institutional investors must become more active in processes of corporate governance	70%	81%	89%	63%	NS
More emphasis needs to be placed on corporate management's responsibilities for preventing fraud and error	92%	98%	95%	84%	0.01
More damages claims against external auditors should be taken to court rather than being settled 'out of court'	36%	30%	41%	35%	0.01
Revenues from non-statutory assurance services will soon dominate those from the external auditing	67%	65%	65%	70%	NS
The portfolio of skills now demanded of external auditors necessitates major reform in the education and training of chartered accountants	53%	78%	36%	53%	NS
Allowing audit firms to advertise their services has downgraded their professional image	20%	6%	33%	14%	0.00
Chartered accounting firms will face increasing market competition from alternative providers of external audit services (e.g. banks)	35%	24%	43%	33%	NS

Most notably, the vast majority of survey respondents did not support statutory extensions in the auditors' responsibilities to report to stakeholder groups other than the company's shareholders. As with their views on social and environmental matters, this contrasts with recent urgings by the ICAEW for auditors to consider their responsibilities in broader terms:

> 'External audit is no longer simply the compliance function it once was. Shareholders have a right to expect auditors to perform their work with their

> interests in mind. But directors expect auditors to add value to the business, and other stakeholders including employees, regulators and government agencies take an increasing interest in all aspects of the auditors' work. The audit has never been more valuable to such a wide constituency.'
>
> (ICAEW, 2000a, p. 1)

There was also general agreement among respondents that auditing should not extend into other areas such as 'publicly rating businesses in terms of their exposure to risk and having auditors 'participating in management decision making processes'. Only Big 5 auditors felt that external audit reports would need to be provided more frequently (on an 'on-line' basis) in response to advances in electronic provision of information. Respondents were fairly evenly divided over whether interim financial statements published by listed companies should be externally audited. They were similarly divided over whether external auditors need 'to become more active in detecting corporate corruption and money laundering activities' (non-auditors being the most supportive overall), again despite some prior institutional initiatives in this area (e.g., see AICPA, 1998; APB, 1998b).

All three groups did not give majority support for a 'free-form' audit report (see Hatherly *et al*., 1998), tailored to meet the individual circumstances of each audited company. However, there were some clear divisions between respondent groups over the level of detail to be included in the financial audit report. The majority of non-auditors wanted the standard audit report to provide details on: (1) where external auditors have relied on senior management assurances; (2) all detected material errors (i.e. both adjusted and unadjusted errors identified during the audit process); (3) audit materiality levels; and (4) audit risk levels. There was no majority support among Big 5 auditors for any of these possible developments. Non-Big 5 auditors were very supportive of (1) and evenly divided over (2) but against (3) and (4). One possible explanation for such differences in views is that a majority of non-auditors felt that 'external auditors these days rely too much on management assurances' and that 'external auditing is becoming like management consultancy'. Such points were supported by a significant minority of non-Big 5 auditors but rejected by most Big 5 auditors.

The final issue examined through the questionnaire was the degree to which respondents saw the responsibility for change as resting with the audit profession. While respondents have, in varying degrees, recognised the need for change in the nature and scope of the external audit function, they also saw the need for action on the part of other parties. For instance, clear majorities of each group felt that 'institutional investors must become more active in processes of corporate governance' and 'that more emphasis should be placed on corporate management's responsibilities for preventing fraud and error'. Such viewpoints very much reflect the way in which auditing standards have developed in recent years in areas like fraud detection and audit reporting – with clear attempts to distinguish between the responsibilities of corporate management and external financial auditors (for example, see APB, 1995). Similarly, there was only limited support from respondents for external auditors proactively to seek to clarify their legal responsibilities by taking more damages claims against them to court (instead of being settled out-of-court). However, a clear majority of Big 5 respondents and a basic majority of non-auditors did feel that the portfolio of skills now demanded of external auditors necessitates major reform in the education and training of Chartered Accountants. The majority of non-Big 5 auditors did not support such a move, reflecting the recent division of views over the need for the ICAEW qualification to be less generalist in its nature.

9. ASSESSING THE IMPLICATIONS FOR EXTERNAL FINANCIAL AUDITING AND THE CASE FOR CHANGE

In the introduction to this paper, it was noted that the external financial audit is very much a subject of lively debate, with quite a wide range of perspectives as to the status of auditing and the need for action and change. It was also suggested that there was much to gain from seeking the views of the broader ICAEW membership on a wide range of issues relating to the role, scope, conduct, reporting and regulation of the external financial audit function. The views obtained do show that ICAEW members differ quite considerably on some issues, depending significantly on the context in which they are working – whether as Big 5 auditors, non-Big 5 auditors or ‘non-auditors’. The value of the survey rests in part on such differences but also in the way the views serve to challenge some existing standpoints on the nature of contemporary external financial auditing and the key ways in which auditing needs to change. In particular, it does much to suggest that the audit arena is a complex, multi-faceted world and one that does not lend itself readily to simplistic, one-dimensional recommendations for change

Of the three respondent groups, Big 5 auditors were generally more confident that: the quality of auditing has improved over the last decade; auditing remains an attractive career for newly qualified accountants; today’s external audit methods add more value to businesses being audited and are more effective at detecting material misstatements; and that the relationship between auditors and management is suitably balanced. They were the most positive about the strength of future audit markets. However, they were the most convinced that: a major audit liability crisis exists; external audit fees do not adequately compensate audit firms for the risks involved and that liability reform is needed across a range of dimensions. They also felt most strongly that the reputation of the Big 5 firms exceeds that of the ICAEW and that major reform is needed in the education and training of Chartered Accountants.

Non-auditors, those ICAEW members working outside of audit firms, were the least satisfied with the managerialist, ‘value-added emphasis of today’ audit methods. They do not regard ‘added value business advisers’ as a good description of external auditors, while the organisational contribution of the external financial audit is rated as less significant than a number of other audit forms. Recent changes in external financial audit methods were seen as having been stimulated primarily by the desire to improve the profitability of audit assignments, while external audit fees are seen as adequately compensating auditors for the risks involved. Non-auditors were also divided over the existence of a major audit liability crisis, but see UK courts as being reasonably fair to auditors and see little reason for placing financial caps on auditors’ liability.

Non-Big 5 auditors were generally closer in their views to non-auditors than Big 5 auditors. Both groups, for instance, felt that: the external financial audit is not highly valued by company management; internal audit plays a more significant corporate governance role than the external audit; and that the pressure for 'added value' audits is undermining traditional audit attributes. Where non-Big 5 auditors did differ concerned the need to reduce the influence of company management on the external audit, especially in terms of addressing the negative impact of audit tendering processes on audit quality. They were also the most supportive of the view that auditing standards have become too detailed and of the need to have different levels of attestation for the external audit of listed and non-listed companies.

Taken together, the results confirm that the views held by ICAEW members of the external financial audit are correlated with the context in which they work – just as Rosenberg *et al*. (1982) showed the views of accountants to be dependent on the local government department in which they worked. This is a significant finding in terms of the general audit expectations gap literature as it questions the extent to which such a gap can be referred to as an 'education gap'. If qualified accountants, having gone through similar professional training, hold different views of the audit function, it does suggest that any audit expectations gap is being shaped by something more than differences in technical understanding.

Such a conclusion, ironically, is reinforced by the changes that respondent groups wanted to make to the external financial audit. Many of these changes were about changing the performance dimensions associated with the audit (its role and scope) rather than changing the way in which existing responsibilities are communicated/justified to user groups. For instance, there was strong support across all groups for the different audit functions in organisations to become more integrated. Such a finding adds some professional support to the dysfunctional consequences attributed to the recent 'audit explosion' identified by academics such as Power (1994, 1997) and others (e.g., Strathern, 2000). Furthermore, there was a real acknowledgement that external auditors should be reporting on more than just the truth and fairness of a company's accounts. Clear majorities of each respondent group wanted auditors to report on the effectiveness of an organisation's internal controls, its future viability, compliance with corporate ethical codes and any significant breaches of legislation (not just of company law). There was also support among some groups for external audit reports on management integrity and key operational business risks and for more frequent reporting as the electronic provision of financial information increases. Some wanted auditors to become more active in detecting corporate corruption and money laundering activities, with the general acknowledgement that external auditors have little chance of detecting senior management-led fraud. There was also some feeling that the current standard audit reports could become more informative, in terms of disclosing where auditors have relied on senior management assurances and what material errors have been detected. Non-auditors were the most supportive of change in this area (with Big 5 auditors generally seeing little need for action), even extending their support to disclosure of materiality and audit risks levels.

In an era when attempts have been made to re-write auditing concepts and to relax some of the controls governing the structure and membership of audit firms, there was considerable support for some quite traditional views of auditor independence (e.g. that auditors must be, and be seen to be, independent). There was also some reluctance to reduce the regulatory involvement of the professional bodies and a desire to preserve the requirement that there must be a majority of chartered accounting partners within audit firms. Some ‘old hobby horses’ (such as restrictions on the provision on non-audit services) were not strongly supported but there was a clear support for strengthening the role of audit committees. Majorities in each group wanted audit committees to become more independent of external auditors and more active in their monitoring of audit work – making public their findings on listed company auditors.

An intriguing aspect to these various calls for change is that they came on the back of some positive viewpoints about auditing. For instance, respondents generally felt that: the quality of auditing has improved over the last decade; the transparency of published company annual reports in the UK is generally high; audit committees have significantly improved standards of corporate governance; and that external opinion shopping by senior company management is very rare. Yet, change was still seen as necessary – although respondents acknowledged that it needed to be accompanied by some action on the part of users (not to expect too much of auditors), institutional investors (to become more active in processes of corporate governance) and corporate management (to give more attention to their responsibilities for preventing fraud and error).

Furthermore, there were also some potential signs of complacency or over-optimism on the part of respondents about the current state of the external financial audit. Respondents did not think that chartered accountancy firms would face increasing market competition from alternative providers of external audit services. They also felt that non-statutory assurance services would soon dominate those from the external financial audit, while Big 5 auditors gave much higher estimates than non-Big 5 auditors and non-auditors as to the future growth in a range of audit services.

There are a number of broad implications of the survey. At one level, it reinforces the need for more debate and research on the external financial audit function, particularly given the diversity of views obtained from people with considerable experience of such a function. Despite the promotion of ‘modern-day’ assurance services, it shows that there is still much to discuss about the scope, delivery, reporting and regulation of traditional external financial audits. In particular, there is more to know about the practical operation and impact of current audit methods. This is especially so given the critical views of those respondents (i.e. ‘non-auditors’) for whom new (business risk-based) audit methods have been supposedly designed to please and the widely acknowledged reductions in audit testing that have taken place. Likewise, there is much scope for discussion regarding the degree of variation allowed in auditing mandates and the extent to which there can be different rules and regulations governing the audit of companies of different size (and the education and training of auditors on such audits). There is also a viable case for reviewing auditor liability, but from a perspective that explicitly considers whether too much is being made of this issue by some of the more vocal elements of the profession and explores how developments in financial audit mandates can gain broad approval.

Despite the audit reporting changes supported by respondents, a potential stumbling block for those seeking a more socially relevant and intrusive external audit function is evident in their views of the auditor’s responsibilities towards broader ‘stakeholder’ groups. There was very little support for extending the auditors’ remit in this area, either in terms of functional relationships or in reporting explicitly on the social and environmental impact of organisational activities. Admittedly, these are areas which the ICAEW hierarchy has been particularly keen to promote in recent years but its actions do not as yet seem to have had much impact on the views of the broader membership.

Overall, the survey results emphasise the importance of consultation and interaction by professional bodies with their members. Leaving institute policy to be determined by Big 5 auditor representatives, for instance, would mean that some important issues are unlikely to get appropriate consideration. In the survey, Big 5 auditors were generally most content with the impact of recent developments in audit methods, less supportive of change in the role and obligations of the financial audit and the most supportive of reform in auditors' liability. The clear differences between ICAEW members working for Big 5 firms and those being audited by them suggest that there are some important contextual factors to explore in order to understand precisely how practical experience shapes what individual members regard as appropriate audit obligations and practices.

Ultimately, it is worth remembering that calls for change have come from each respondent group and that all respondents are qualified Chartered Accountants – not ill-informed user groups. This latter claim has been a persistent problem for the expectations gap literature, with the significance of observed differences being dismissed by classifying them as misunderstandings – gaps which can be solved by better educating user groups rather than changing the way in which audits are performed. Alternatively, claims of an audit expectations gap have been countered by methodological criticisms suggesting that the gaps between the views of auditors and users primarily reflect a self-rating bias on the part of auditors. From this perspective, such gaps are an inevitable feature of a study where one participating group is evaluating its own performance. Finally, there have been suspicions that for many user groups, audit is very much a free good and that in responding to a questionnaire survey they can always ask for more from the auditor without worrying about the economics of such requests.

While these problems cannot be completely eliminated from a survey which includes one group no longer working as external auditors, the fact that all respondents are members of the same professional body, with presumably fairly similar pre-qualification training and interests in ensuring its future well-being, represent good reasons for taking their views as sensible, informed commentary. The opinions of respondents may not sit comfortably with standpoints promoted either by leading professional representatives or their critics. However, they emphasise that there is still much to consider and debate with respect to the external financial audit. Most significantly, in light of recent corporate collapses and the desire for regulatory action in the financial audit arena, the survey results should provide a cautionary reminder to those in search of some quick-fix solutions. As seasoned accounting professionals have demonstrated here, change needs to go beyond matters of impression management or educational initiatives to a detailed examination of the role, scope, operation, achievements and possibilities of the external financial audit.

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