

# **The Second European Auditing Research Network Symposium**

## **EARNet provides forum for academics and practitioners**

The Second European Auditing Research Network (EARNet) Symposium was held on 31<sup>st</sup> October and 1<sup>st</sup> November 2003 in Manchester, England. The two-day program, organized by Professor Christopher Humphrey and Professor Stuart Turley from The Manchester School of Accounting and Finance, University of Manchester, included three plenary sessions, a panel discussion on the link between research and practice, and 24 research papers presented in 9 parallel sessions. The presentation of the Best Paper Award concluded the Symposium.

EARNet, founded in 2000, is intended to foster research and exchange ideas among auditing scholars and researchers on a European level. Its primary objective is to promote European auditing research. Also, EARNet aims to contribute to European policy making (secondary objective).

Correspondingly, the purpose of the Symposium was to provide a forum for academics, practitioners, policy makers and standard setters to discuss auditing research and current issues in the auditing environment. More information about EARNet and its Symposiums is available at <http://www.earnet.uni.essen.de>.

## **Current issues in auditing**

Clearly the current issues in the auditing environment include those that are related to the overall lack of confidence in financial reporting and auditing, and to the attempts to remedy this lack of confidence. Standard setters and regulators around the world are revising the rules and regulations and introducing new ones to restore this confidence.

Another important goal is the harmonization of standards in accounting and auditing. In Europe, the decision of the European Union to use international standards in accounting and auditing instead of national standards is a major step towards true global harmonization of standards. For example, by 2005 listed companies in the EU have to adopt the use of IFRSs (International Financial Reporting Standard) for their consolidated financial statements. In auditing, in May 2003 the European Commission issued a proposal that ISAs, (International Standards on Auditing) issued by IAASB (International Auditing and Assurance Standards Boards) should be adopted as the auditing standards in the EU though the process for EU recognition of ISAs and the timetable for their recognition have not yet been finalized.

## **A word from standard setters**

Consequently, it was very appropriate that two plenary addresses were given by Mr. Dietz Mertin, chair of IAASB and Mr. Richard Fleck, chair of the Auditing Practices

Board (APB) for the UK and Ireland, who were able to give perspectives on the development of standards from both the international and national point of view. In his presentation Mr. Mertin reported the current agenda and activities of IAASB. First, the recent development in the status of IAASB as a standard setting body was described. In essence, it seems that acceptance of IAASB has grown during the last few years globally. In addition to the recent proposal of the European Commission to adopt ISAs as auditing standards in EU, for example IOSCO (the International Organization of Securities Commissions) has created a program to review IAASB's process and standards in detail, INTOSAI (the International Organization of Supreme Audit Institutions) has expressed its interest in contributing new ISA's, and standard setting authorities in many countries have reportedly developed close cooperation with IAASB.

Mr. Mertin described the latest pronouncements and exposure drafts IAASB has announced and the work that is still in progress. The exposure drafts address topics such as auditors' responsibility for fraud detection, quality controls for audits, standards for audit risk, review of interim reports, and audit plans. New and revised ISAs in progress include the auditor's report on financial statements, group audits, accounting estimates, materiality, documentation, and modifications to the auditor's report. The latest pronouncements and exposure drafts as well as information about current projects are available on IAASB web page at the address <http://www.ifac.org/IAASB>.

Mr. Fleck commented on the challenge for a national standard setting body from a move to international standards and also discussed the significance of recent developments in ethical standards for auditors in the UK. According to APB's press releases (see [http://www.accountancyfoundation.com/auditing\\_practices\\_board/index.cfm](http://www.accountancyfoundation.com/auditing_practices_board/index.cfm)), it has issued for public comment five Exposure Drafts of proposed Ethical Standards (ESs) on the integrity, objectivity and independence of auditors in November 2003.

### **A need for knowledge facilitating policy-making motivates research**

Bearing in mind that EARNet aims to contribute to policy making in Europe, it is interesting to examine the research topics of the 24 research papers presented in the Symposium from that perspective. These papers were grouped into nine sessions covering issues such as auditor rotation, audit markets, quality control, auditing and governance, auditor reporting, and auditing contexts and perspectives. Overall, a review of the topics of the papers suggests that the need for up-to-date knowledge facilitating standard setting in auditing issues is a typical motivation for the papers presented in EARNet 2003.

### **Barriers in producing knowledge for policy-making**

There is however, a tension between the world of research and that of practice, and this tension can also be found in the area of auditing. In general, one major source of this tension is that researchers have very strong incentives to publish their work in academic journals, which is notoriously time-consuming while policy makers and practitioners seek timely information that will be useful to them. The main reason for the lengthy

publication processes is that academic journals are concerned about the rigor and technical perfection of the analysis that has produced the results. Secondly, and perhaps more importantly, journals are more interested in 'adding to the literature' than creating knowledge for solving practical problems in policy-making.

This tension and the barriers in producing up-to-date knowledge that is useful for policy-making purposes were addressed by Professor Peter Moizer from the University of Leeds in his plenary presentation *How published academic research can inform policy decisions: the case of mandatory rotation of audit appointments*. As regulators in many countries, for example in the UK, are currently making decisions whether or not to introduce the mandatory auditor rotation, the issue is very relevant and acute from standard setters perspective.

In his working paper, Professor Moizer presents an impressive state-of-the-art review on the topic that shows, in essence, that varying and constantly changing environments in different countries make it very challenging to produce knowledge that could be applied for other countries or settings other than those under examination. For the same reason, the life span of the applicability of results is often relatively short. However, at least in the particular case of auditor rotation, it seems that academics in auditing have been successful in producing research that can inform policy makers and standard setters. More specifically, taken together, it seems that on balance the research favors the arguments for mandatory rotation rather than the arguments against it.

### **The winners of Best Paper Award 2003**

Audit committees that give recommendations on the appointment and remuneration of auditors are often seen as another important safeguard against the threats for auditor independence. Although the mere existence of audit committees is not enough to protect against threats to auditor independence, (as we have learned from the US experience where there is a relatively long tradition in audit committees and perhaps the tightest requirements), it seems that standard setters in many countries perceive audit committees as being part of good corporate governance practice.

The paper probing into the formation of audit committees received the Best Paper Award at EARNet 2003. In their paper *Voluntary Audit Committee Formation and Practices among Belgian Listed Companies* Professor Marleen Willekens, Dr. Heidi Vander Bauwhede and Professor Ann Gaeremynck from the Catholic University of Leuven, Belgium, analyzed the factors related to voluntary audit committee formation among Belgium listed firms and evaluated the nature of existing audit committees against Belgian corporate government recommendations, the US requirements, and some best practice guidelines.

In short, their main findings are that the probability of having an audit committee increases with the number of independent directors on the board and having a Big Five auditor. Taken together, these findings suggest that the presence of good governance mechanisms creates a demand for even better governance. The comparison of existing

audit committee practices against the Belgian recommendation and US regulation reveals that while many listed companies do not have audit committees, those who have, perform quite well according to the Belgian recommendation, but not that well when compared against US requirements. For example, many audit committees do not have a financial expert or disclose the audit committee charter as required by the US rules.

### **Concluding remarks**

The Second EARNet Symposium provided the sixty-nine academics and practitioners from several European and other countries the two good days to meet colleagues in a friendly and sociable context, the unique opportunity for presenting research and learning what colleagues are doing. As the First EARNet Symposium, held in Wuppertal, Germany in 2001, also the Manchester meeting lived up to its goal as being an important forum for academics, practitioners, standard setters and policymakers to discuss current issues in auditing environment.

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