

ANNUAL REPORT

First (extended) financial year from 20 October 2015 to 31 December 2016 inclusive

FOUNDATION FOR
AUDITING
RESEARCH



a unique collaboration
between science
and practice

FOUNDATION FOR
AUDITING
RESEARCH

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2015

Autumn 2015

2016

The FAR is established. The foundation adopts its first research agenda.

Foreword

We are happy to present the first annual report of Stichting Foundation for Auditing Research. We are proud to show in this annual report that the foundations have been laid for opening the audit “black box” – and thereby for innovative research through cooperation between academics and audit practitioners. The annual report makes it clear that good work takes time, but also that the audit profession takes academic research into audit quality seriously and attaches great value to such research. The profession itself is also looking for answers to important questions in this field.

The Foundation for Auditing Research (FAR) was established in Amsterdam on 20 October 2015. The new foundation aims at the sustainable improvement of audit quality. In this, the focus is on academic research into audit quality drivers. The formation of the FAR is in line with recommendation 5.10 of the improvement plan entitled (‘In the public interest’), which was presented by the audit profession in September 2014.

The new foundation focuses on the audit function at audit firms, businesses and government bodies. The nine largest audit firms in the Netherlands (Deloitte, EY, KPMG and PwC, plus Baker Tilly Berk, BDO, Grant Thornton, Mazars and Accon AVM) together finance the foundation’s activities by making an annual contribution totalling €1.5 million. This arrangement initially applies for a period of five years, subject to a positive interim evaluation of the FAR’s activities. Another important point is that the firms involved make relevant data available to the FAR researchers via a secure environment.

The FAR has achieved much in the short time since its formation:

- **Autumn 2015**
The FAR is established. The foundation adopts its first research agenda.
- **Spring 2016**
The FAR selects the first six research projects and organises the first International FAR Conference.
- **Autumn 2016**
The FAR obtains legal clearance and launches a data gathering pilot. In addition, the first FAR Masterclass is held and the research agenda is extended.
- **Spring 2017**
Researchers and audit firms meet each other during the Data Summits, and full data gathering can commence. On 7 and 8 June, the second International FAR Conference is held. New projects are initiated as well, such as Joint Working Groups and Case Studies.

Thanks to the enormous efforts made by the affiliated audit firms in unlocking data, we have taken significant steps towards actual data exchanges between practitioners and academics. These exchanges not only involve data contained in the firms’ files and information systems, but also participation in surveys, experiments and interviews. At the same time, the research teams have had to exercise considerable patience, but we expect that they can soon begin to actually gathering data. This shows that the audit profession is serious in trying to obtain academic insights that will help strengthen the audit profession sustainably.

Spring 2016

The FAR selects the first six research projects and organises the first International FAR Conference.

Autumn 2016

The FAR obtains legal clearance and launches a data gathering pilot. In addition, the first FAR Masterclass is held and the research agenda is extended.

2017

Spring 2017

Researchers and audit firms meet each other during the Data Summits, and full data gathering can commence. On 7 and 8 June, the second International FAR Conference is held. New projects are initiated as well, such as Joint Working Groups and Case Studies.

Autumn 2017

There is still much to be done, but the foundations have been laid – also with regard to the provision of confidential data. Although the first projects have commenced, most of the research teams can only start to work properly once the data has been made available. It is expected that thereafter the first new research results can be announced six months later – that is, by the spring of 2018 at the earliest. This requires patience, but good work just takes time.

We have all the confidence that, thanks to all participants, various publications will be produced in the coming years that will have a significant impact on science and practice.

On behalf of the board of Stichting Foundation for Auditing Research

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The executive board

Olof Bik

managing director and academic board member

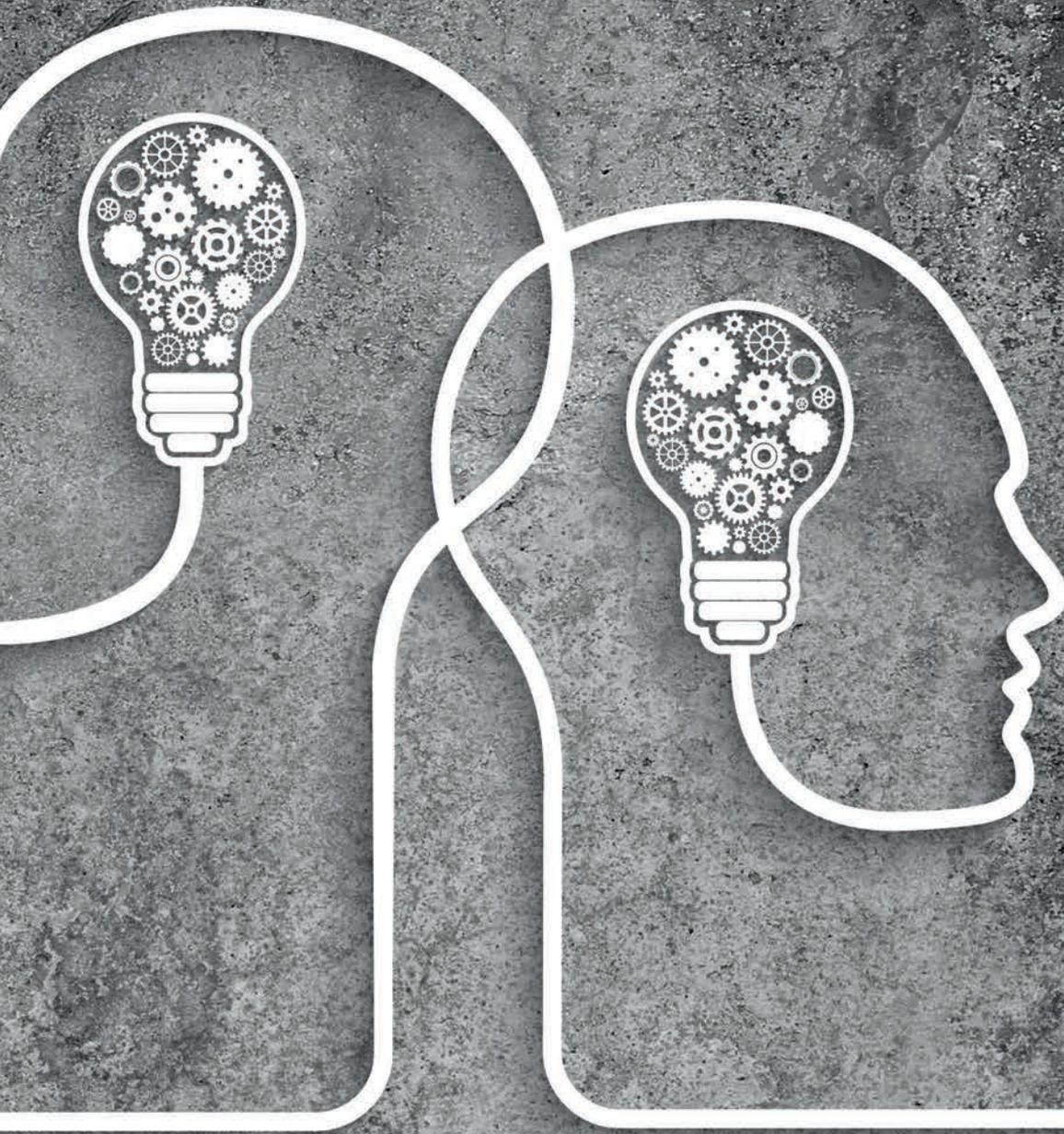
Jan Bouwens

managing director and academic board member

Henriëtte Prast

chair of the board





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BOARD REPORT

About Stichting Foundation for Auditing Research

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The Foundation for Auditing Research (FAR) aims at the sustainable improvement of audit quality. In this, the focus is on relevant and rigorous academic research into audit quality drivers. The FAR provides a unique environment for cooperation between science and practice, reinforces the learning curve of the audit profession and its stakeholders, feeds audit education and offers ongoing support to the research community in the area of auditing, both within the Netherlands and at international level. The activities to be carried out by the FAR consist of three elements: unlocking data, initiating and executing (or arranging the execution of) research projects, and finally communicating extensively about the knowledge expansion. The FAR was formed in October 2015 as part of the improvement plan of the audit sector entitled ('In the public interest').

Accountantsfonds

The FAR focuses on the audit function at large and smaller audit firms, businesses and government bodies. The eight largest audit firms in the Netherlands (Deloitte, EY, KPMG, PwC and Baker Tilly Berk, BDO, Grant Thornton and Mazars) took the initiative to provide financial support to the foundation and make data available for research over an initial period of five years (with an interim evaluation being held at the end of 2017). There is no such cooperation in this industry anywhere else in the world. Accon AVM became a FAR affiliate on 1 January 2017, which confirms that the FAR is also there for firms working in the SME sector. On 8 April 2016, the FAR announced a donorship agreement with the foundation Stichting Accountantsfonds. The primary object of this foundation is to subsidise the development of research and education programs.

Cooperation with audit firms and Stichting

Research Agenda: Drivers of Audit Quality

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In determining the research agenda, the FAR takes the perspective of the profession at large and its stakeholders. In December 2015, the FAR adopted its research agenda for the coming years. In the first year, this agenda involved the following two approaches in particular: on the one hand, to unlock academic knowledge in order to apply it in practice and, on the other, to define, invite and evaluate research proposals speaking to promising new research directions. In this, the focus is on strengthening the core aspects of audit quality in areas such as audit inputs, the audit process, the auditor's intention and behavior, audit outcomes, and the organisation, management and culture of audit firms.

The FAR aims to identify the drivers and root causes of audit quality and thus improve the audit practice. In doing so, the FAR gives consideration to:

- the underlying drivers of auditor judgment and decision-making, such as organisational circumstances that may stimulate auditors or, conversely, prevent them from working in the manner expected of them;
- the underlying causes of good and poor audit quality (rather than the symptoms of those causes); *and*
- the effectiveness of potential interventions (organisational changes and levers of control) that have been implemented to enhance audit quality, including the monitoring of these interventions.

Research Program 2016: first six research projects

Based on the research agenda, the FAR deliberately defined its first Call for Projects (2016) in open and broad terms. In this way, the FAR wants to give academics the opportunity to put forward research proposals and ideas that will help obtain insight into the drivers of good audit quality.

This call resulted in the submission of 16 research proposals by researchers in the Netherlands and abroad, all of which were carefully and thoroughly reviewed. After a first review round, nine research teams were given the opportunity to revise their research proposals, partly on the basis of the review report. Of those nine proposals, six were eventually selected in a second round for a grant from the FAR. This grant is a combination of financial resources and access to data.

The selection criteria involved aspects such as relevance, academic rigor, quality and publication status of the research team. The review process also considered the feasibility – including in terms of data gathering – of the research proposals, and the involvement of Dutch researchers, junior researchers and PhD candidates. Another important aspect in the FAR's view is the application of a multi-disciplinary research approach, enabling the audit industry to learn from academic insights gained in other disciplines (such as management, leadership, organisation, psychology, sociology, behavioral research, etc.). After all, one of the FAR's objects is the sustainable reinforcement of the auditing research community.

The six research projects selected in 2016 are the following:

- The loss of talent – A threat for audit quality
- Why some auditors thrive while others struggle – The effect of multiple team membership on audit quality
- Moving audit teams forward – Designing firm environments for sustainable learning from errors
- The auditor's evaluation of misstatements – Exploration, drivers, and consequences
- Professional skepticism profiles, effects on audit processes and outcomes, and the moderating role of audit firm culture
- Coordination and communication challenges in global group audits – Evidence from component audit leaders

These projects involve academics from Maastricht University, the University of Groningen, the Free University of Amsterdam, the University of Antwerp, Harvard Business School, the University of New South Wales, the University of Wisconsin and Villanova University. The research projects have a total duration of one to four years.

The following schedule contains a brief description of each research project.

TITLE

The loss of talent - A threat for audit quality

TIMELINE

09/16 – 12/18

WHAT?

The research team wants to investigate what defines audit talent, what factors affect the career advancement or potential loss of talent over several years and the impact of this on audit quality. This should enable audit firms to hold on to the talent for longer, and thus 'recover' their investment in training and development in the form of audit quality. The focus is on the effectiveness and possible improvement of the audit firms' Performance Management Systems, a management instrument used by firms in specific situations.

WHY?

Audit firms invest a lot in young talent and audit practitioners: they develop their human capital with the aim to realise audit quality, but see too much talent leave (prematurely) over the years. This loss of talent is a high cost item for these firms, who after all must be able to rely on their knowledge workers, and for the profession. It seems that most talent is lost just after the firms have assumed the greater part of the training costs. This results not only in a threat to audit quality, but also in high replacement costs. The importance which 'generation Y' attaches to a healthy work-life balance is one of the factors examined in this project.

WHO?

Prof. dr. F. (Frank) Moers
Professor of Management Accounting and Control, Maastricht University, School of Business and Economics
dr. I. (Isabella) Grabner
Associate Professor of Accounting, Maastricht University, School of Business and Economics
J. (Judith) Künneke MSc
PhD Candidate in Accounting, Maastricht University, School of Business and Economics

TITLE

Why some auditors thrive while others struggle – The effects of multiple team membership on audit quality

TIMELINE

09/16 – 12/20

WHAT?

The research team wants to identify the conditions under which audit firms can make the most effective use of multiple team memberships (in keeping with the firm's business model) and under which team members are in the best position to fulfil the requirements of fluid team membership. The objectives are: high audit quality, motivated staff and an appropriate team culture. In other words: to increase the advantages of working with fluid teams and to mitigate the adverse effects on staff of multiple team memberships.

WHY?

The purpose of this project is to discover why some staff members thrive while others struggle in the given business model (i.e. fluid teams and multiple team membership). Are there any factors that were not considered earlier? Can audit firms learn how to make better use of their human capital, in the context of the audit team and the firm? One objective is therefore to create appropriate organisational conditions for this team model. Another objective is to teach young talent and team leaders how to deal with possible negative effects and how to make the most of possible advantages (for example through training-on-the-job).

WHO?

dr. R.B.H. (Reggy) Hooghiemstra
Associate Professor, Department of Accounting and Department of Auditing, University of Groningen
Prof. dr. F.A. (Floor) Rink
Full Professor, Department of Human Resource Management and Organizational Behavior, University of Groningen
dr. D.B. (Dennis) Veltrop
Assistant Professor, University of Groningen; Economist, De Nederlandsche Bank

TITLE

Moving audit teams forward – Designing firm environments for sustainable learning from errors

TIMELINE

09/16 – 12/18

WHAT?

This research project focuses on the right circumstances / conditions under which audit firms can improve the extent to which firms / audit teams learn from errors. In other words: how can an organisational context / organisational climate be created in which audit teams can effectively learn from errors? And how can the interaction between the individual auditor's characteristics and the firm's organisational environment be improved with the aim to reinforce the quality of the audit opinion?

WHY?

Recent research by the research team has shown that audit firms may significantly improve their performance if auditors can actively learn from auditing errors. Because audits are sometimes the result of complex social interplay within an audit team, the audit quality, as well as the auditor's individual development, will eventually be the result of teamwork and interaction.

WHO?

Prof. dr. W.H. (Wim) Gijselaers

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Prof. dr. R.H.G. (Roger)

Meuwissen RA

Professor of Control and Auditing, Maastricht University, School of Business and Economics

dr. P. (Piet) van den Bossche

Associate Professor Learning in Organisations, Faculty of Social Sciences, University of Antwerp; Associate Professor, Department of Educational Research and Development, Maastricht University, School of Business and Economics

dr. T. (Therese) Grohnert

Postdoctoral Researcher and Lecturer, Maastricht University, School of Business and Economics

Prof. A.C. (Amy) Edmondson

Novartis Professor of Leadership and Management, Harvard Business School

TITLE

The auditor's evaluation of misstatements – Exploration, drivers, and consequences

TIMELINE

09/16 – 12/20

WHAT?

The research team wants to enhance understanding of and make potential recommendations for the process and consequences of evaluating, discussing and handling (material) misstatements in the financial statements: when and why does the auditor disregard a misstatement, and when does he request adjustment? The focus is on the effects on the 'negotiation process' (rather than on the actual evaluation of the misstatements). What is the type, nature, direction, size and degree of repetition of misstatements found and adjusted? To what extent are such adjustments effective in improving the actual quality of financial reporting (in other words, the value of the audit)?

WHY?

During the audit process auditors discover misstatements, whereupon the auditor decides in a (social) negotiation process with the management whether or not an adjustment is required. Because this decision directly affects the quality of the financial reporting, it is important for audit firms to know how the effectiveness of the 'negotiation process' about audit findings can be positively influenced.

WHO?

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Prof. R. (Roger) Simnett
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Prof. G.V. (Gopal) Krishnan
Tenured Full Professor, Department of Accounting and Taxation, Kogod School of Business, American University, Washington, DC

Prof. T.L. (Teri) Yohn
Professor, Department of Accounting, Kelley School of Business, Indiana University, Bloomington

TITLE

Professional skepticism profiles, effects on audit processes and outcomes, and the moderating role of audit firm culture

TIMELINE

10/16 – 01/20

WHAT?

This research project focuses on the potential improvement of the professional skepticism of the auditor and the audit firm in the interaction between the auditor's innate (professional) skepticism (personal trait), the culture at the audit firm and the audit quality, by addressing three questions. How naturally skeptical are auditors at different career and experience levels? How does this degree of professional skepticism affect the audit process applied by auditors and the audit quality eventually realised? And how does the culture at the audit firm and within the team affect professional skepticism in the audit?

WHY?

This research will provide insight into what more skeptical auditors naturally do differently during the audit process and show whether or not this results in higher audit quality levels (nature, timing and extent of audit procedures). Thus, it will enable audit firms to reinforce their corporate culture in stimulating professional skepticism. More specifically, it will show audit firms how they can create a fruitful environment in which naturally less skeptical auditors can nevertheless conduct a skeptical audit.

WHO?

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Prof. dr. A. (Ann) Vanstraelen
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Prof. K.M. (Karla) Johnstone
EY Chaired Professor of Accounting, University of Wisconsin, Madison

S. (Sanne) Janssen
Candidate Joint PhD, University of Antwerp and Maastricht University, School of Business and Economics, Master of Applied Economic Sciences

TITLE

Coordination and communication challenges in global group audits – Evidence from component audit leaders

TIMELINE

09/16 – 04/18

WHAT?

The aim of this research project is to identify barriers and best practices hampering or fostering high audit quality in global group audits from the perspective of the auditor of a component (operating company or part of the group). What is the effect of specific features of an audit engagement on the extent of the coordination and communication challenges for component auditors? What coordination and communication strategies may help reduce these challenges?

WHY?

The group auditor bears ultimate responsibility for the entire audit of the consolidated financial statements, irrespective of the degree to which component auditors are deployed during the global group audit. Nevertheless, the group auditor must ensure that the component audits are performed effectively and efficiently, despite having no direct control over these audits because the auditors are not working as a team at one physical location, as they usually do. He therefore faces a variety of coordination and communication challenges. The recommendations resulting from this research will enable him to tackle these challenges successfully.

WHO?

Prof. dr. A. (Anna) Gold
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PhD, CPA, Assistant Professor, Villanova University, Villanova, PA

A.J. (Andrew) Trotman
PhD, Assistant Professor, Northeastern University, Boston

Extended research agenda 2017

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At the end of 2016, the FAR decided to extend and streamline its research program. The latter means that the research subjects and questions were formulated in more specific terms, based on a survey among the affiliated firms and a number of major stakeholders (including a number of professional publications) of the main research subjects facing audit practitioners. This resulted in a few dozen possible subjects, from which the ten principal themes were selected for the 2017 research program.

Extending the research program meant that the FAR defined three new research programs in addition to the empirical research projects that were also selected in 2016: literature synthesis, design-oriented 'Joint Working Group' research projects and case studies into 'near misses' and quality measures in the profession. All this can be summarised as follows:

DESCRIPTION

RESEARCH SYNTHESIS

EMPIRICAL RESEARCH

FIRM DATA NEEDED

PROJECT TIMELINE

OUTPUTS

Research Program A Research Syntheses	Research Program B Empirical Research	Research Program C Joint Working Group Design Oriented Projects	Research Program D Case Studies
<p>To unlock what we already know about specific practical questions and potential interventions that can be suggested to strengthen audit quality (where possible in joint academic-practitioner teams). Should also inform knowledge gaps and future FAR research projects.</p>	<p>Archival, survey, experimental, interviews (and other qualitative) research by independent research groups. Longitudinal and cross-sectional research could be of specific relevance to study the effectiveness of interventions taken in the firms and the profession.</p>	<p>Projects directed by the FAR Board / MDs for the more pervasive, all-encompassing practical questions and dilemma's, geared towards professional interventions and improvements.</p> <p>In a Joint Working Group structure, meeting 3 to 5 times over a period of several years, comprising proactive participation of top practitioners and selected top researchers on the topic jointly.</p>	<p>Case Studies directed by the FAR MDs on:</p> <ul style="list-style-type: none"> the objectives and rationale behind firms' policy decisions in relation to audit quality enhancements; the root causes of restatements in financial statements after the audit opinion has been issued; <i>and</i> the root causes of (near) audit quality failures.
Yes	Yes	Yes	Yes
No	Yes	Yes	Yes
No	Yes	Yes	Yes (detailed case information)
6 to 12 months	1 to 4 years	1 to 3 years (depending on depth and breadth of the project)	6 to 12 months
<p>FAR Practice Notes and FAR Masterclasses. The potential to be published in, e.g. Journal of Accounting Literature or a JAE research synthesis call.</p>	<p>Intermediate deliverables: FAR Practice Notes, FAR Masterclass and FAR Conference presentations. Additional ultimate deliverables: FAR Research Paper and A-journal academic publication(s).</p>	<p>Intermediate deliverables: FAR Round Table meetings, FAR Practice Notes, FAR Masterclasses and FAR Conference presentations. Additional ultimate deliverables: FAR Research Paper and (if project allows) A-journal academic publication(s).</p>	<p>FAR Case Studies and FAR Masterclasses. The potential to be published in scholarly, educational journals.</p>

Call for Research Projects 2017

On 23 December 2016, the FAR invited researchers to submit research proposals within two Research Programs by 17 March 2017 at the latest. The purpose of Research Program A (Research Syntheses) is to unlock the information already available in the academic world (both within and outside the auditing discipline) about a specific question and about potential interventions that may be proposed with a view to improving audit quality. Research Program B (Empirical Research) involves the execution of empirical research projects. Researchers are requested to submit research proposals focusing on audit quality determinants.

FAR Projects: Joint Working Groups and Case Studies

In addition to Research Programs A and B, the FAR has initiated two other research programs. These programs are managed directly by the FAR managing directors and the FAR board. Research Program C will see the launch of two 'Joint Working Group Design-Oriented Projects' in 2017. In these projects, top practitioners and academics will collaborate on practical issues and dilemmas experienced to be all-encompassing. This involves the following two projects:

1. Root cause analysis methods in auditing: What are effective ways to conduct (continuous) Root Cause Analyses within audit firms?
2. The (future) auditing (partner) business model: How to balance audit firm management within the boundaries of the audit profession's value(s) (multi-stakeholder perspective on audit value and quality), audit firms' economic viability (business model, operational excellence and production function), and people (talent development)?

Research Program D involves case studies. The first case study pilot will deal with 'near misses': audits that nearly went wrong. How do the parties involved respond to these near misses, and what measures are taken to prevent audit quality failure in the future? With the cooperation of one of the affiliated audit firms, a complex 'near miss' audit case will be selected that will be studied in depth, the envisaged outcome being an academic case study that can be used in audit training. By now a case has been selected.

In the Call for Research Projects 2017, the international academic community was invited to submit research proposals for the following Program A and Program B projects:

PROJECT NAME

MAIN TOPIC

1. Going concern opinions (Program A project)	What are the main determinants, considerations and hurdles for auditors to move on to a going concern opinion?
2. Auditing standards' function, setting, interpretation and application (Program B project)	Do different stakeholders (e.g. audit firms and audit regulators) interpret and apply the audit standards differently in terms of nature, timing and extent of audit procedures (to be) performed?
3. Different audits for different purposes: auditing in the Owner-Managed-Business [OMB] environment (Program B project)	Does the OMB environment call for different audits and auditing standards?
4. The auditee's internal controls and financial reporting quality (Program B project)	What is the mutual impact of the audit and the auditee's internal controls and financial reporting quality?
5. Fraud detection by the auditor (Program B project)	What are the determinants of a fraud (not) being detected and reported by the auditor? What can be improved?

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The review process is still in progress, but we are happy to report that the FAR has received 12 high-quality research proposals.

Data Provision by the Affiliated Audit Firms

Just before Christmas 2016, legal clearance was obtained from all the affiliated audit firms. Coordinating this process required much time and effort from all the parties involved: the audit firms, the research teams and the FAR. Our first step was to make arrangements with one of the firms, of which 80-90% could apply to the other firms as well and subsequently be customised for each of them. When the FAR received actual legal clearance to access the audit firms at the end of 2016, a milestone had been reached.

Security measures

A number of security measures were agreed in order to create a data set which can no longer be traced back to a particular firm, specific client file, individual auditor or staff member. Identifiability is irrelevant to researchers anyway - they look for patterns based on large numbers and do not concern themselves with individual cases. The security measures involved here include the following:

- Audit firms do most of the anonymisation. The use of an encryption application prevents data from being directly traceable.
- By applying strict data-management procedures, such as transformation and calculation of derivative research

- variables, the FAR also eliminates indirect traceability.
- Remote access to the academics. This means that researchers often do not physically receive the data, but can only analyse the data in a secure FAR environment to which they can log in (and from which no data can be copied or exported). This has far-reaching, limiting consequences for the researchers, but these are accepted for the sake of being able to conduct the badly needed research.
- NDAs as a 'base line' with each academic involved.
- Confidentiality check by FAR of each draft publication prior to disclosure. In doing so, the FAR makes sure that the publication does not contain any identifiable data, but obviously has no substantive influence on the results of the research.

CentERdata, a specialised scientific data management bureau, supports the FAR in this process. Its activities include gathering and managing data and making this data available to research teams, all in a reliable and confidential manner.

“We are growing ever closer”

Data Gathering and Sampling Strategy: numbers, definitions, measuring differences

During the period January-March 2017, the FAR determined the data gathering and sampling strategy for the current research projects. All participants realise that this involves a very large number of cases (for example, 500 audit files per year, distributed proportionally among the nine firms) and a multitude of variables / information points that are required. An important finding regarding the former is that, due to confidentiality regulations, much data is kept under digital lock and key and is not easy to unlock. An important finding regarding the latter is that requested information points must be unequivocally defined, but even if they are, there will still be significant measuring differences between the firms that must be resolved by the researchers. In addition, this often involves data that is to be gathered from various systems (which must be linked) or that is still to be obtained from the audit teams by means of a supplementary request for information.

Data Summits: direct contact between audit firm and researcher

In April 2017 audit firms and academics sat around the table for the first time, hunched over the research projects, during the events known as Data Summits. As well as being mutually stimulating and informative, these events strengthened mutual understanding. Direct contact with the researchers created enthusiasm among the audit firms about the relevance of the research question. Firms subsequently invited those researchers to their offices in order to experience the practical side of things.

Exploration of alternative routes

The latter also forms the basis for current explorations: alternative routes, such as the research team holding discussions with each firm individually in order to gather data. This is because combining the data requests from so many research projects (each with its own specific data requests and selection criteria) into one large data request proves to be difficult. FAR provides the audit firms with intensive support, also by lending a hand in actually unlocking data. Even though we are well under way, once an actual data exchange has been established we will have achieved something unique. This therefore has our highest priority in 2017.

Knowledge Dissemination

(Conference, Masterclass, Papers)

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As well as stimulating research aimed at gaining new insights, the FAR also focuses on unlocking existing knowledge. Examples of this are the first International FAR Conference and the FAR Masterclass.

International Conference

'What do we know about audit quality?'

On 9 and 10 May 2016, the FAR held its first conference at Nyenrode Business Universiteit. During this conference, participants from science and practice shared their views on the question: what makes an audit a good audit? This event resulted in the development of a special edition of the journal *Maandblad voor Accountancy en Bedrijfseconomie* (MAB), entitled 'What do we know about audit quality?'

The FAR must close the gap between academic research and audit practice. This was one of the most important findings during the conference. 'The FAR is born: a love child of the academic world and the audit practice', said Henriëtte Prast, the freshly appointed chair of the new research institute, in her opening speech.

Using a broad research agenda, the FAR made a first request for research proposals to the international academic world. This has already elicited a range of proposals. When the next request is formulated, practice will receive even more explicit attention. 'Our main selection criteria are: does it add anything to what we know already, and will it help us to improve the audit practice?', said Prast. During the conference, several speakers emphasised the importance of gathering more data from professional practice. By now the eight largest

audit firms in the Netherlands have undertaken to make data available, but the FAR is open to other auditors, such as public-sector auditors or internal audit departments.

Matters discussed in more detail included methods for establishing the influence of corporate culture on audit quality, research into audit technology, efficiency and audit costs, and the effect of supervision on audit quality.

The speakers were Michael de Ridder (FAR board, PwC), Jere Francis (University of Missouri-Columbia), Liesbeth Bruynseels (University of Leuven), Marleen Willekens (University of Leuven), Christine Nolder (University of Suffolk), Ruud de Hollander (AFM), Marco van der Vegte (FAR board, Deloitte), Jan Nooitgedagt (chair of various audit committees), Egbert Eeftink (FAR board, KPMG), Suraj Srinivasan (Harvard Business School), Jeroen van Raak (Utrecht University), Robert Knechel (University of Florida), Joost van Buuren (Nyenrode Business Universiteit) and Willem Buijink (FAR board and Tilburg University).

'For me, this Masterclass confirms the importance of continued dialogue between practice and science: sharing knowledge and assessing what practitioners consider useful.' – participant in the Masterclass, working for a Big 4 audit firm.

Masterclass 'Designing audit firm environments for sustainable learning from errors'

The theme of the first FAR Masterclass on 22 November 2016 was: how do auditors as a professional group deal with making errors? Is there room to learn from errors? Professor Wim Gijssels, Professor Roger Meuwissen and PhD student Therese Grohnert (all from Maastricht University) led this Masterclass, in which science and practice learned from each other by sharing their knowledge and experiences.

May auditors learn from their errors?

The traditional picture in the audit industry is that a client makes errors, which are subsequently detected by the auditor. However, the errors addressed on this occasion were not the client's errors, but the errors made by auditors themselves. How does the professional group deal with errors? Is there room to learn? This interactive Masterclass was a textbook example of what cross-pollination between science and practice should look like: full of enthusiasm, energy and discussions which together result in new insights.

The principal four takeaways are:

- A safe learning environment is a condition for delivering greater audit quality.
- The judgment quality depends on whether individuals may learn from their errors and, in that context, have learned to reflect.
- Experience and self-confidence are no reliable predictors of a correct judgment and fewer errors.
- An individual's conduct contributes to a safe learning environment.

Stimulating a safe learning environment

What can an individual do to create a safe learning environment? Confidence is number one. Do not slate a person if they admit that they made an error. Regularly ask the question 'what does everyone else think?'. Try not to say 'that's not important' too often when young people raise a point. In this way, you encourage junior staff to share their observations. Give people the space to develop and facilitate discussion.

You must also set a good example: admit it if you have made an error. And be aware as an experienced auditor of the effect that your presence has on others. The latter is one of the points which the speakers will examine in more detail as part of the FAR-initiated research project 'Moving audit teams forward - Designing firm environments for sustainable learning from errors'. This project will focus specifically on the effect of the changing and hierarchical composition of audit teams and society's expectation that auditors should not be allowed to make errors.

For more information, please visit the FAR's website:
www.foundationforauditingresearch.org

Organisation

The FAR was formed on 20 October 2015 and consists of a governing board, an executive board and an office organisation with a number of part-time employees.

Henriëtte Prast appointed chair of the board

On 8 April 2016, Prof. dr. H.M. (Henriëtte) Prast was appointed as FAR chair. She is a member of the Upper House of Parliament and Professor of Finance at the Tilburg School of Economics and Management, a part of Tilburg University. Henriëtte Prast succeeded drs. P.J.A.M. (Pieter) Jongstra RA who, as the chair of the Royal Netherlands Institute of Chartered Accountants (NBA), had also been the acting chair of the FAR since its formation.

Board composition

In addition to the independent chair, the FAR board has four independent members from the academic world and five members from affiliated audit firms. Together with Prof. dr. Jan Bouwens (University of Amsterdam) and dr. Olof Bik RA (Nyenrode Business Universiteit), both FAR managing directors, the chair also forms the executive board of the foundation. Where applicable, the chair has the casting vote within the board.

The board consists of the following persons:

- **dr. O.P.G. Bik RA**, managing director and academic board member
- **Prof. dr. J.F.M.G. Bouwens**, managing director and academic board member
- **Prof. dr. W.F.J. Buijink**, academic board member
- **Prof. drs. E. Eeftink RA**, board member representing KPMG Accountants
- **drs. P.A.J. Hopstaken RA**, board member representing Mazars Accountants, as well as Baker Tilly Berk, BDO and Grant Thornton
- **drs. J.F.M. Kamphuis RA**, board member representing EY Accountants
- **Prof. dr. W.R. Knechel**, academic board member
- **Prof. dr. H.M. Prast**, chair of the board
- **drs. M. de Ridder RA**, board member representing PwC Accountants, as well as treasurer of the board
- **M.J. van der Vegte RA**, board member representing Deloitte Accountants

Board meetings and other consultations and gatherings

During the first (extended) financial year, six board meetings were held. The first three were presided over by acting chair Pieter Jongstra, the others by Henriëtte Prast. There were four financial consultation meetings with the treasurer. The FAR consulted periodically with Stichting Accountantsfonds about the research agenda and wider professional developments. In addition, discussions were held with various stakeholders about the FAR's objectives and research agenda, including the NBA, MCA, AFM, IAASB, IIA and NBA Young Profs. The FAR was represented at a number of academic conferences.

Other audit firms and departments may also participate in the foundation, by paying an annual contribution of €50,000 or more and providing access to their data. Any other parties who wish to contribute, by providing data or financial resources, will be welcome as sponsors.

Working organisation

The FAR is based at Antonio Vivaldistraat 2-8 in Amsterdam. In compliance with arm's length financial arrangements, laid down in a Service Level Agreement, the foundation uses the facilities of the Royal Netherlands Institute of Chartered Accountants. These include the secretariat, management support, financial administration department and meeting facilities.

In addition, the office organisation comprises a limited number of part-timers who work for the FAR on a freelance basis in the areas of program management, data gathering, unlocking of knowledge and communication.

Financial Results

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The FAR's financial income primarily consists of contributions committed by the affiliated audit firms on the basis of undertaken research projects and approved office costs. These made up € 1.5 million of the income recognised in the first financial year. In addition, we are very grateful to Stichting Accountantsfonds for its donation of € 100,000.

The maximum research grants available were spent largely on the selected research projects. The total amount of multi-year grants for these committed research projects is € 1,038,000, which includes the costs directly relating to the execution of the research projects. These are recognised as an expense in the statement of income and expenses and as a liability in the balance sheet, because unconditional commitments for this amount were made to research teams. In addition, an amount of € 102,000 is recognised as project-related research costs, which concerns the costs of the research agenda and the selection of research projects in particular.

The office costs, including board costs and costs of conferences and suchlike, amounted to € 231,000 in this (extended) financial year. This leaves a positive balance of € 229,000 at the end of the financial year, which is € 182,000 more than originally budgeted. To ensure that the FAR will be able to meet its general obligations also in the future, the board considered it desirable to designate this balance as a continuity reserve. The continuity reserve now created, equalling 0.9 times the organisational costs, is considered adequate.

Funding through invoicing will only take place if there is a liquidity requirement as the research projects progress, or in order to cover the approved and budgeted office costs. This means that the FAR has no unused financial resources.

The FAR has an external auditor, RSM Netherlands Accountants N.V., who audits the financial statements. These 2016 financial statements were discussed with the auditor on 17 May and 23 June 2017.



Outlook for 2017

Now that the foundations for the FAR have been laid, we look forward to going at full steam in the coming financial year. Our particular aim for this year is to implement the data gathering process, which is crucial in order to realise the research agenda.

At the end of 2016, we reached agreement with the participating audit firms about the manner in which the information for the research projects will be exchanged and about the control measures required in this context. A Data Summit was held in April 2017, at which representatives of the audit firms involved in the FAR and the FAR research teams had the opportunity to discuss their expectations and possibilities. This more direct liaising and cooperation between the research teams and the participating firms is expected to be continued in the data gathering strategy. The FAR expects that the first actual data provision by the affiliated firms to the research teams can be realised shortly after the summer of 2017. Thereafter, the research teams will be able to start the empirical part of their research projects, the first results of which may be published in working papers early in 2018.

Second International Conference

Meanwhile, we are continuing to initiate new research and unlock existing research. An example of this is the second FAR International Conference, which was held on 7 and 8 June 2017.

Second FAR conference: the ball is now in the audit profession's court

A Minister of Finance who lays down challenges, an ambitious regulator, a wide and engaged audience and a substantive debate on intriguing statements: the second FAR Conference brought the organisation and participants everything they had hoped for – and more. Most of all, the conference, featuring a range of renowned international speakers, was a unique meeting between academics and audit practitioners.

The questions central to the conference were: is the gap between theory and practice too wide, what is the definition of audit quality, how do we measure such quality, how can the industry regain trust and what personal qualities of the auditor play a part (or perhaps: a much more important part than we tend to think) in an audit?

The profession's importance for society was reflected in the make-up of the audience during the conference. Compared to the previous year, a greater number of practitioners made their way to Breukelen: 45 percent of the visitors were practitioners (or both practitioners and academics), against 37 percent in 2016. Academics made up 44 percent of the audience, against 57 percent last year. The FAR is happy with these numbers. 'We want to close the gap between the academic world and practice', said chair Henriëtte Prast in her opening speech. 'If you are ensconced in an academic ivory tower, you are unaware that people in other areas or other industries do not always understand your language.'

‘I also attended last year’s FAR conference’, says a participant in the 2017 FAR Conference who is also a researcher and a practitioner. ‘What I really like is the fact that both practice and theory are addressed here.’

The first keynote speaker at the conference, Mark DeFond from the University of Southern California, started his address (entitled ‘Controversies of Audit Quality’) by provocatively taking a step backwards. His question, taken from a research paper, was ‘Should we research audit quality at all?’ DeFond made his own position clear from the start: he does not agree, but believes nevertheless that the question must be taken seriously.

The second day of the conference was characterised by contributions from two prominent speakers: Finance Minister Jeroen Dijsselbloem and AFM board member Gerben Everts. In order to regain society’s trust, the audit industry must itself take the initiative, also towards the authorities. This was the core message of Jeroen Dijsselbloem’s address. ‘Show that it is the practitioners, rather than politicians, who take the first step’, said Dijsselbloem, who referred to regaining trust as an ‘uphill battle’.

Just like Dijsselbloem, AFM board member Gerben Everts also encouraged the audit industry to develop initiatives, especially in the area of innovation. Robert Knechel, in the audience, pointed out that the industry must innovate, but that tolerance of failure is the other side of the coin. Everts agreed, and therefore wants to offer companies a ‘safe haven’ when it comes to innovation. If audit firms see possibilities for providing assurance in a model different from the current one, the AFM will be prepared to grant ‘waivers’ of the applicable rules. ‘In that case, we want to offer flexibility’, said Everts.

During the conference, four FAR research projects were presented by Frank Moers (‘The Loss of Talent’), Kris Hardies (‘Professional Skepticism’), Reggy Hooghiemstra (‘Multiple Team Membership Effects’) and Denise Hanes Downey (‘Group Audits’).

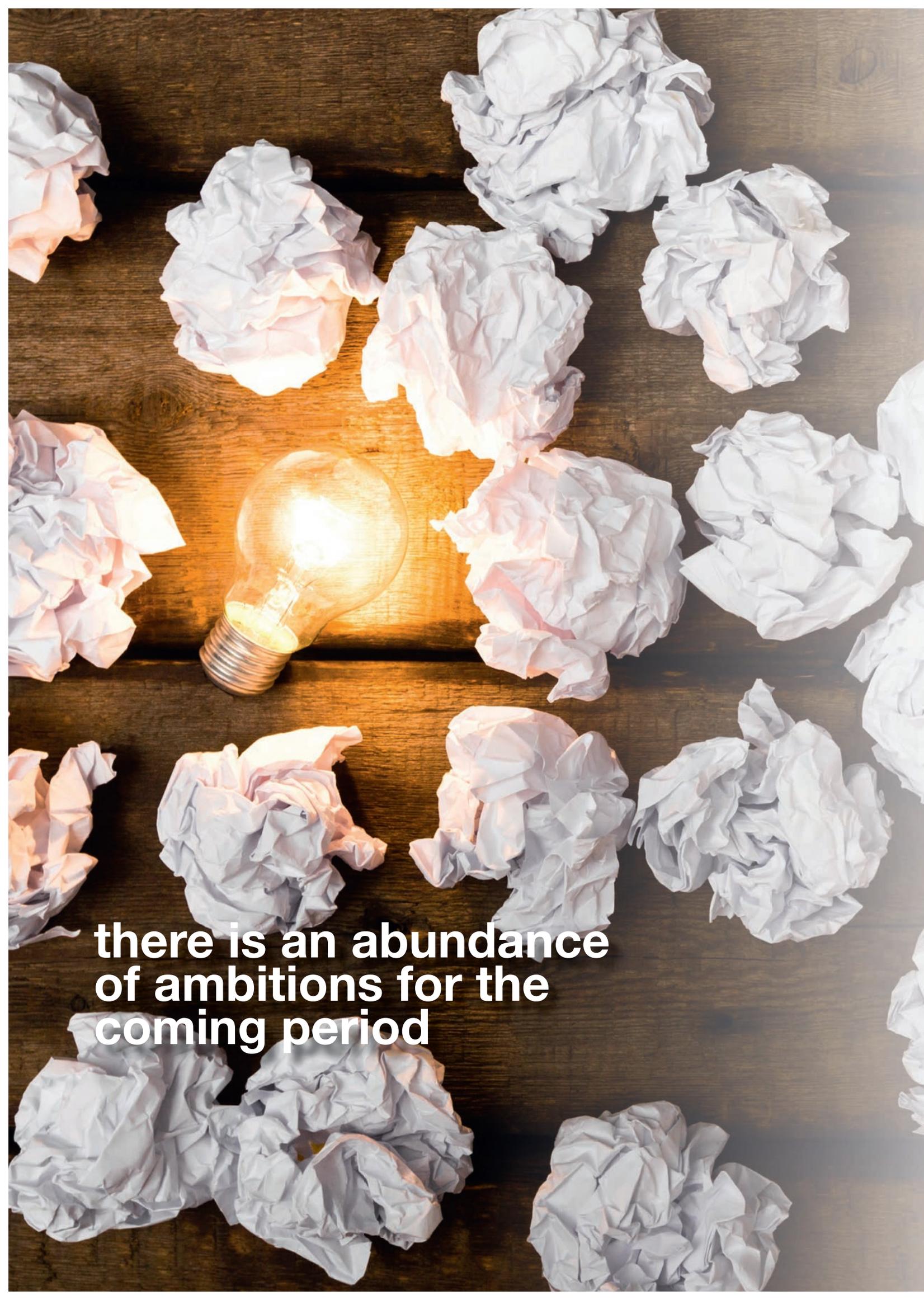
Research

By July 2017, we hope to have completed the next selection of empirical research projects, based on the ‘Call for Research Projects 2017’.

Another key concern in the coming period is to set up the Joint Working Groups around the future firm-and-partnership business model and the root-cause analysis methods. We expect that the first summit on both themes can be held in the autumn of 2017. In preparation for these summits, an initial exploratory investigation will be conducted on the basis of literature, documents and interviews with practitioners. In addition, we hope to launch the first Case Study pilot in the coming year.

Masterclasses

A number of Masterclasses have been scheduled for the autumn of 2017, including one on 15 November 2017 about the identification and discussion of audit findings by Prof. dr. Ann Vanstraelen from Maastricht University. In addition, the first ‘in-house’ Masterclass will be organised in the autumn in order to find out whether such closed meetings with a specific purpose within a particular organisation will help achieve the FAR’s object.



**there is an abundance
of ambitions for the
coming period**

Financial outlook

To help us flesh out our research agenda, unlocking of knowledge and contribution to the development of the profession, the FAR will also in the coming year rely on the financial contributions committed by the affiliated audit firms and donor(s). These contributions total a maximum of € 1.6 million for 2017 as well. Taking account of the project-related research costs (budgeted at € 100,000) and the general office costs (budgeted at € 250,000), the maximum research budget for the coming year amounts to € 1,250,000. It appears that financial resources do not always have the highest priority for the research teams – their principal concern is access to data. While the FAR expressly wants to invest in building up the research community in the auditing discipline – which entails funding PhD students, for example – this does not mean that large financial contributions will be requested all the time, and it is therefore not certain that the entire budget will be required to fund the projects we want to conduct. At the same time, the research program has been extended by elements such as Joint Working Group and Case Study projects. In addition, the unlocking of data by the audit firms requires considerable efforts and investments from those firms. Where possible, the FAR will support them in this.

When the FAR was formed, preference was given to a transitional model based on a coordinating office organisation. The aim is still to keep the fixed organisation to a minimum by cooperating as much as possible with the affiliated research groups and audit firms. We pursue a cost ratio not exceeding approximately 15 percent of the current basis of financial contributions. In view of the FAR's ambitions and the growth of its activities, however, consideration will also be given in the coming period to further professionalisation of the working organisation.

Accordingly, there is an abundance of ambitions for the coming period. We are excited about the foundations that have been laid, and have every confidence that further major steps can be taken in the coming period towards academic research into the audit quality drivers and thereby the unlocking of the audit 'black box'.

Amsterdam, 23 June 2017

On behalf of the executive board of Stichting Foundation for Auditing Research

sgd **dr O.P.G. Bik RA** – managing director and academic board member

sgd **Prof. dr. J.F.M.G. Bouwens** – managing director and academic board member

sgd **Prof. dr. H.M. Prast** – chair of the board

Auditors open their 'black box'

Secret data now finally accessible to FAR researchers

Bas Knoop and Jeroen Piersma

It is their 'love child'. For 15 years Jan Bouwens, professor in Amsterdam, and Olof Bik, researcher at Nyenrode, lobbied for an organisation that conducts academic research into pressing audit questions. By now the wait is over. In the autumn of 2015 the Foundation for Auditing Research (FAR for short) was born, and now, 18 months down the line, the first research teams are ready to start.

Olof Bik: 'The creation of the FAR shows that audit firms are looking for genuine answers to the big questions.'

The FAR has not come a moment too soon. Although the turmoil which the profession experienced in recent years has eased off, an accounting scandal may be just around the corner. The circus of critical media reports and indignant MPs, as well as an industry trying to pull itself out of the mire by its own hair, may kick off again at any time. As it did in 2014, when the scandals at KPMG prompted a major 53-point reform plan. One of those points was the formation of the FAR.

The problem is that most of those points of reform are based on experience, intuition, vision and gut feeling, but not on scientifically informed knowledge of how

the audit profession works and what drives the quality of auditors' work. And this applies not only to the 53 points, but also to all other measures poured out over the industry in recent years, such as a licensing requirement, a regulator, mandatory audit firm rotation and separation of consultancy and audit.

Bouwens: 'We have too little knowledge of the drivers of audit quality. Indeed, we do not even agree what quality actually is.' The problem is that academic researchers have always looked at the profession from the outside. They never had access to the essential data, such as the audit files. 'The firms were always as closed as an oyster', says Bouwens.

This is where the FAR is to make a difference. The nine largest audit firms in the Netherlands have agreed that research teams will gain access to their data. Each year, around five hundred audit files will become available for academic research. In anonymous form, so they cannot be traced back to the individual firm, the auditor or the client.

Nearly all formal hurdles have been cleared and research work can start; the first results will become available in 2018

Intuition

Supporters of audit profession reform do not normally base their plans on science, says Jan Bouwens. A well-known example is mandatory audit firm rotation. It appears that such measures tend to reduce rather than enhance audit quality.

Heavyweight committees are also more likely to proceed from intuition, vision and assumptions. The Monitoring Committee Accountancy found that further reforms are required because of 'wicked problems', such as the audit firms' partner and earnings model. 'On what did they base that conclusion?', wonders Bouwens. 'It is far from certain that audit quality will increase if the earnings model is changed.' Quality-based remuneration is another sore point. 'You should not reward quality, but punish a lack of it. And first we must still define the meaning of quality, before we know what we are going to reward or punish.'

Audit firms have a duty of confidentiality in respect of the information provided to them by their clients, which is why they have always been so reluctant to make disclosures. Not surprisingly, therefore, a lot of water had to pass under the bridge before the firms were prepared to make the data available. Bik: 'This is what kept us busy for most of 2016. Just before Christmas of last year, we concluded a hefty agreement with them on this point.'

In his opinion, the audit firms capitulated in part because of the social pressure on the profession. But they also wanted it themselves. 'They have become convinced that it is important to know how the audit black box works. They were confronted with incidents which they could not properly explain. The industry is seriously looking for answers.'

According to Bik and Bouwens, the FAR occupies a unique position. Nowhere else in the world do researchers have comparable access to the large firms' data. This is why the FAR teams also include researchers from universities such as Harvard. Bouwens: 'They are unable to obtain this data in the US.'

The FAR is funded by the profession and representatives of the large firms have taken place on the board.

What about the independence of the research? 'Our independence is safeguarded by the governance structure. The independent board members hold the majority of the votes', says Bik. But this is a formal position which Bik and Bouwens are reluctant to adopt. What matters is

cooperation. 'The board position for the audit firms is also intended to guarantee access to the internal data.'

Now that nearly all formal hurdles have been cleared, the research work can start. We may expect the first results in 2018. The teams are advancing on four fronts: literature synthesis, empirical research, project research into major issues such as the relationship between the firms' earnings models and quality, and case studies into audit quality failures.

The research results may play a useful role. Follow-up must still be given to a report from the Monitoring Committee Accountancy, which concluded in November of last year that the 53 points did not put the profession in the clear yet. Furthermore, the AFM will publish another – undoubtedly critical – report in June about quality at the Big Four.

'We do not pretend that we know it all or that we should be the ones to determine policy', says Bouwens. 'But our aim is that policymakers consult us before introducing more changes to the industry. We hope that they will start with the FAR.'

This is a translation made by FAR of a Dutch article. Source: Het Financieele Dagblad, 9 June 2017, page 5.



Accountants openen hun 'black box'

Geheime gegevens zijn nu eindelijk toegankelijk voor onderzoekers FAR

Bas Knoep en Jeroen Piensa
intuïtie

Het is hun 'lovebaby'. Vijftien jaar lang hebben de Amerikaanse hoofdleraar Jan Bouwens en Nyntrode-onderzoeker Olof Bik eindelijk voor een organisatie die wetenschappelijk onderzoek doet naar de vraagstukken rond accountancy. Inmiddels is het zover: in het najaar van 2017 zal de Foundation for Audit Research, kortweg FAR, geboren, en nu, in de eerste maanden van 2018, zal de eerste onderzoeksrapporten op het punt om aan de slag te gaan.

Olof Bik: 'Dat de FAR er is gekomen, toont aan dat de accountantskantoren op zoek zijn naar de echte antwoorden op de grote vragen. De FAR heeft geen moment te vroeg de truilentorie waarin de sector jarenlang verkeerde is weliswaar wel afgevoerd, maar een boekhoudaffaire zit in een klein hoekje. Het creëren van kritische mediabehoeftigheid, verontwaardigde kantoffelen en een veld van de jacht aan de eigen haren uit het moeras probeert te trekken, kan zwaai van start gaan. Net als in 2014, toen de affaire bij AFM's afdeling kwam voor een groot hervormingsplan van 53 punten. Een daarvan was de oprichting van de FAR. Het probleem is dat de meeste van die hervormingspunten zijn gebaseerd op ervaring, intuïtie, visie en halvegeloof, maar niet op wetenschappelijk gefundeerde kennis over de werking van de accountancy en wat de kwaliteit van het werk van accountants bepaalt. En dat geldt niet alleen voor de 53 punten, maar ook voor alle andere maatregelen die de afgelopen jaren over de sector zijn uitgegaan, zoals de vergoedingsschijf, een toezichtbodem, verplichte roulatie van accountantskantoren en schending van advies en controle.

Bouwens: 'We hebben te weinig kennis over de factoren die de kwaliteit van het accountantswerk bepalen. Sterker nog, we zijn het er niet over eens over de kwaliteit eigenlijk.' Het probleem is altijd van buitenaf naar de sector hebben gelopen. 'De eerste belangrijke gouverneurs, zoals de controlebodeurs, kregen zij nooit onderzoek. De kantoren waren er altijd zo gelukkig als een oester', zegt Bouwens.

Maar moet de FAR het verschil maken? De negen grootste accountantskantoren van Nederland hebben afgesproken dat onderzoekers toegang krijgen tot hun data. Jaarlijks komen er vijfduizend controlerende agents beschikbaar voor wetenschappelijk onderzoek. Geanonimiseerd en dus niet herleidbaar tot het individuele kantoor, de accountant en de klant.

Accountantskantoren zijn gebonden aan geheimhoudingsplicht over de informatie die hun klanten hen verstrekken, daarom waren ze altijd zo terughoudend om openheid van zaken te geven. Vandaar dat ook de oprichting van de FAR nog flink wat water door de rijen moest voordat de kantoren over waren dat zij de data beschikbaar stellen. Daar zijn we eigenlijk het grootste deel van 2016 mee bezig geweest. Vlak voor de kerst vorig jaar hebben wij daar een dik contract met hen over gesloten.'

De kantoren zijn volgens hem mede overtuigd gegaan door de maatschappelijke druk op de sector. Maar het blijft ook uit kracht. 'Zij zijn ervan overtuigd gemaakt dat het belangrijk is om te weten hoe de black box van de accountancy controle werkt. Zij hadden te maken met incidenten die ze niet goed konden verklaren. De sector is serieus op zoek naar antwoorden.'

Volgens Bik en Bouwens heeft de FAR een unieke positie. Niemand heeft eerder hebben onderzoekers een vergelijkbare toegang tot de data van de grote kantoren. Vandaar dat ook onderzoekers van bijvoorbeeld Harvard plaats nemen in de FAR teams. Bouwens: 'Deze data kunnen ze altijd in de VS niet krijgen.'

De FAR wordt gefinancierd door de sector en vertegenwoordigers van de grote kantoren hebben een plaats in het bestuur. Hoe zit het met de onafhankelijkheid van het onderzoek? 'Onze onafhankelijkheid is gewaarborgd in de bestuursstructuur. De onafhankelijke bestuursleden hebben de meerderheid van de stemmen', zegt Bik. Maar dat is een formele positie die Bik en Bouwens niet graag inzetten. Het gaat om samenwerking. 'De plek in het bestuur voor de kantoren is ook bedoeld om de toegang tot de interne gegevens te garanderen.'

Nu de formele hordes vrijwel genomen zijn, kan het onderzoek van start. De eerste resultaten kunnen we in 2018 tegenmoeten zien. De teams zullen over vier fronten op terreinen uitbreiden, empirisch onderzoek, projectonderzoek naar grote vragen zoals de relatie tussen het verdienmodel van de kantoren en de kwaliteit, en onderzoek naar casussen waar iets mis is gegaan.

De onderzoeksresultaten kunnen een nuttige rol spelen. Er is nog een rapport van de Monitoring Commissie Accountancy die vorig jaar werd uitgebracht. Concludeerde dat de sector er nog niet was met de 53 punten. Bovendien komt de AFM eind juni weer met een, ongeveer gelijksoortig, rapport over de kwaliteit bij de Big Four.

'We hebben zeker niet de illusie dat wij het beleid zouden moeten bepalen', zegt Bouwens. 'Maar we streven ernaar dat beleidmakers ons raadplegen als zij nieuwe veranderingen in de sector willen doorvoeren. We hopen dat zij bij de FAR beginnen.'

Hoofdlezer Jan Bouwens (l) en onderzoeker Olof Bik.

FOTO: PETER STRELSMA VOOR HET FD

intuïtie

Voorstanders van hervorming van de accountantssector moeten niet op wetenschappelijk gefundeerde kennis over de werking van de accountancy en wat de kwaliteit van het werk van accountants bepaalt. En dat geldt niet alleen voor de 53 punten, maar ook voor alle andere maatregelen die de afgelopen jaren over de sector zijn uitgegaan, zoals de vergoedingsschijf, een toezichtbodem, verplichte roulatie van accountantskantoren en schending van advies en controle.

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De formele hordes zijn vrijwel genomen en het onderzoek kan van start; de eerste resultaten zullen in 2018 te zien zijn

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FINANCIAL STATEMENTS

First (extended) financial year from 20 October 2015 to 31 December 2016 inclusive

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1. BALANCE SHEET AT THE END OF THE FINANCIAL YEAR

(after appropriation of the balance of income and expenses)

31-12-2016

x € 1,000

Ref.

ASSETS

Receivables	1	€	1,000
Cash	2	€	372

TOTAL ASSETS

€ 1,372

LIABILITIES

Equity	3	€	229
Research commitments	4	€	1,038
Current liabilities	4	€	105

TOTAL LIABILITIES

€ 1,372

2. STATEMENT OF INCOME AND EXPENSES¹

		Actual 2016	Budget 2016
		<i>x € 1,000</i>	<i>x € 1,000</i>
	Ref.		
INCOME	5		
Financial contributions 'Big 4'		€ 1,200	€ 1,200
Financial contributions 'Middle 4'		€ 300	€ 300
Donation Stichting Accountantsfonds		€ 100	€ 100
TOTAL INCOME		€ 1,600	€ 1,600
EXPENSES	6		
Research-related costs		€ 102	€ 107
Costs of research projects		€ 1,038	€ 1,131
<i>Total project costs</i>	<i>6a</i>	<i>€ 1,140</i>	<i>€ 1,238</i>
Formation costs		€ 7	€ -
Office costs		€ 34	€ 52
Board costs		€ 107	€ 145
Overhead		€ 60	€ 57
<i>Total office costs and overhead</i>	<i>6b</i>	<i>€ 208</i>	<i>€ 254</i>
International conferences		€ 3	€ 11
National conferences		€ 20	€ 50
<i>Total conferences</i>	<i>6c</i>	<i>€ 23</i>	<i>€ 61</i>
TOTAL EXPENSES		€ 1,371	€ 1,553
BALANCE		€ 229	€ 47

¹ The figures relate to the first (extended) financial year from 20 October 2015 to 31 December 2016 inclusive.

Actual 2016	Budget 2016
<i>x € 1,000</i>	<i>x € 1,000</i>

**Appropriation of the balance of income
and expenses:**

Addition to continuity reserve	€ 229	€ -
	€ 229	€ -

3. ACCOUNTING PRINCIPLES

3.1. Objectives and activities

Stichting Foundation for Auditing Research [hereafter: the FAR] has its registered office at Antonio Vivaldistraat 2-8 in Amsterdam. Its objectives are to make a structural contribution to the learning curve and to the sustainable development in general of audit firms, the audit profession and audit training and research in the Netherlands, among other things in order to:

- bring about a sustainable improvement of the audit practice (including the applicable or associated laws and regulations);
- feed audit training programs; *and*
- at the same time reinforce academic auditing research.

In order to achieve its objectives, the FAR initiates (often multi-year) research projects on the basis of a research agenda. These projects are awarded through procedures such as Calls for Research Projects, which are open to universities and research teams at both national and international level. By means of these research projects, the FAR also aims to stimulate auditing research (in the Netherlands) and to disseminate the knowledge thus obtained via research articles, education and contributions to the professional debate (for example, by organising conferences and masterclasses and by publishing professional articles). Furthermore, the FAR focuses on unlocking existing scientific insights for audit practitioners.

To this end, the FAR obtains financial contributions from the affiliated audit firms and donors, initially for a period of five years (with an interim evaluation being held at the end of 2017). In addition, affiliated audit firms have undertaken to provide access to data.

3.2. Principles of valuation of assets and liabilities

3.2.1. General

The financial statements have been prepared in accordance with the 'Guideline for Non-Profit Organisations' [DAS 640], as published under the responsibility of the Dutch Accounting Standards Board. The accounting principles proceed from measurement at nominal value, unless a different principle is stated. The reporting period comprises an extended financial year from 20 October 2015 (the formation date) to 31 December 2016 inclusive. The financial statements have been prepared in euros. Reference numbers refer to the explanatory notes.

3.2.2. Receivables

Receivables are valued on initial recognition at the fair value of the counter-performance, including any material transaction costs. After initial recognition, receivables are valued at amortised cost. Bad debt provisions are offset against the book value of the receivable.

3.2.3. *Cash*

Cash consists of bank balances with a term to maturity of less than 12 months.

3.2.4. *Liabilities*

Current liabilities are accounted for at fair value on initial recognition. After initial recognition, current liabilities are valued at amortised cost. This is usually the nominal value.

The current liabilities have a remaining term to maturity of less than one year.

3.3. **Principles for the determination of the result**

3.3.1. *Income*

The FAR's income consists primarily of contributions committed by the affiliated audit firms. The level of the contribution is determined on the basis of undertaken research projects and approved office costs. These contributions are shown in the statement of income and expenses in the year in which the subsidised expenses or office costs are recognised.

3.3.2. *Expenses*

The total grants for committed research projects, even if they cover multiple years, are recognised as an expense in the statement of income and expenses and as a liability in the balance sheet insofar as unconditional commitments have been made to research teams by the balance sheet date (other than the condition that the research must be conducted in conformity with the research proposal). The FAR simultaneously recognises the estimated expected costs (other than the commitments to research teams) directly associated with the execution of the research projects to which those commitments relate.

The other costs (office costs) are recognised in the period to which they relate.

The FAR is not recognized as an enterprise for VAT purposes and is therefore not liable to pay VAT, or able to reclaim VAT paid.

4. NOTES TO THE BALANCE SHEET

1. Receivables

		31-12-2016
		<i>x € 1,000</i>
	Ref.	
Accounts receivable	(a)	€ -
<i>Accrued income:</i>	(b)	
Still to invoice to 'Big 4' firms		€ 800
Still to invoice to 'Middle 4' firms		€ 200
		€ 1,000

a. Accounts receivable

There is no accounts receivable balance as at the balance sheet date. For this reason, no bad debt provision has been included.

b. Accrued income

In particular, the accrued income relates to the financial contributions still to be invoiced to the affiliated audit firms in respect of the research projects committed in 2016. These contributions are payable by the firms during the term of the projects and in line with their progress.

The non-current part of the accrued income amounts to € 638,000 (detailed under 6a).

2. Cash

	31-12-2016
	<i>x € 1,000</i>
Current account with ABN Amro	€ 372
	€ 372

The cash is at the FAR's disposal.

3. Equity

		Balance on 31-12-2016	Movements 2015 / 2016	Balance on 20-10-2015
		<i>x € 1,000</i>	<i>x € 1,000</i>	<i>x € 1,000</i>
	Ref.			
Continuity reserve	(a)	€ 229	€ 229	€ -
		€ 229	€ 229	€ -

a. Continuity reserve

To ensure that the FAR will be able to meet its obligations also in the future, the board has created a continuity reserve.

In determining the level of the continuity reserve, the FAR follows the guidelines of the Fundraising Institutions Association (*Vereniging voor Fondsenwervende Instellingen*, VFI). The guidelines permit a maximum reserve of 1.5 times the annual organisational costs (including costs of staff, accommodation, administration and board). The estimated organisational costs are approximately € 250,000. The continuity reserve now created, equalling 0.9 times the organisational costs, is considered adequate.

4. Research commitments and current liabilities

		31-12-2016	
		<i>x € 1,000</i>	
	Ref.		
Research commitments	(a)	€	1,038
Accounts payable		€	69
Other accrued costs		€	36
		€	1,143

a. Research commitments

The accrued project costs concern the financial grants relating to the research projects committed in 2016 and the expected research and project costs directly associated with these projects. These can be detailed as follows:

	2016-2017		2018		2019		2020		Total	
<i>Amounts x € 1,000</i>										
Committed research grants	€	296	€	289	€	100	€	80	€	765
Data gathering costs	€	87	€	73	€	44	€	14	€	218
Other project costs	€	17	€	20	€	10	€	8	€	55
Total	€	400	€	382	€	154	€	102	€	1,038

The non-current part of this liability amounts to € 638,000.

b. Identified contingencies and other commitments

The affiliated audit firms and the donor have committed themselves for an initial period of five years, with an interim evaluation being held at the end of 2017. In this context, the audit firms have legally undertaken to pay the committed research contribution relating to the already approved multi-year research projects for their entire duration.

5. NOTES TO THE STATEMENT OF INCOME AND EXPENSES

5. Income

Effective from the FAR's formation, the affiliated audit firms have committed themselves to pay an annual financial contribution not exceeding € 1,500,000 for an initial period of five years (with an interim evaluation being held at the end of 2017). Thus, the FAR's funding primarily consists of funds that are committed by and received from the audit firms on the basis of the committed research projects and approved budget. In this context, the audit firms undertake at the time of the commitment to pay contributions to cover the approved multi-year research projects for their entire duration, so as to enable research teams to complete the research for which they obtained the FAR's approval. The affiliated audit firms are invoiced for committed contributions as the research projects progress, that is, at the moment when the project costs have been incurred, taking account of the cash position required to cover the general office costs.

In addition, Stichting Accountantsfonds and the FAR entered into a donorship agreement effective from 1 January 2016. Under this agreement, Stichting Accountantsfonds makes an annual contribution of € 100,000. In principle, this commitment and donation apply for a period of five years.

6. Expenses

a. Project costs

	2016
	<i>x € 1,000</i>
<i>Research-related costs:</i>	
Research Agenda and Call for Research Projects	€ 15
First review and long list	€ 44
Second review and shortlist proposal	€ 11
Data management	€ 18
Final selection and communication	€ 8
General research project assistance	€ 6
	<hr style="width: 100%; border: 0.5px solid black;"/>
	€ 102
 <i>Costs of research projects:</i>	
Endowments to research teams	€ 765
Project-specific data management	€ 36
Data gathering and management	€ 182

Project management and monitoring	€	25
Project reports and communication	€	30
	€	1,038
Total project costs	€	1,140

The costs of the research projects, and the associated liabilities, can be detailed as follows over time:

	2016-2017	2018	2019	2020	Total
<i>Amounts x € 1,000</i>					
Committed research grants	€ 296	€ 289	€ 100	€ 80	€ 765
Data gathering costs	€ 87	€ 73	€ 44	€ 14	€ 218
Other project costs	€ 17	€ 20	€ 10	€ 8	€ 55
Total	€ 400	€ 382	€ 154	€ 102	€ 1,038

b. Office costs and overhead

	Ref.	2016
		<i>x € 1,000</i>
Formation costs		€ 7
Secretariat and administration		€ 34
Consultancy fees		€ 9
General data gathering costs		€ 28
Board costs	(l)	€ 107
Communication		€ 23
Total office costs and overhead		€ 208

The FAR does not employ any staff.

I. Board costs

The board costs comprise the fees paid to the chair of the board, to the institutions providing the other two members of the executive board (also academic board members) and to the (other) academic board members. In addition, board members are reimbursed for expenses incurred, including expenses for travel and stay. The total fee amount adopted and paid out by the FAR's full board in respect of this financial year is € 154,000 (excluding VAT). Of this amount, € 73,000 is recognised under research-related costs.

c. Conferences

		<u>2016</u>
		<i>x € 1,000</i>
	Ref.	
International	(I)	€ 3
National	(II)	€ 20
Total costs of conferences		<u>€ 23</u>

I. International

These are the costs relating to participation in various scientific conferences in other countries.

II. National

The FAR organised two public events in 2016, being the 2016 International Conference (on 9 and 10 May) and the first FAR Masterclass (on 22 November).

7. Analysis of actual 2016 figures against budgeted figures

Considering that the FAR selects research projects based on relevance for its research agenda and research quality, while access to data is at least equally important for academic research, the FAR was unable to utilise its maximum estimated research budget of € 1,131,000 in full. During this financial year, the FAR committed € 1,038,000 in research grants for six research projects. Because the FAR was in its start-up phase, preference was given to a transitional model. In this financial year, this meant among other things that the total office costs and overhead were € 46,000 lower than

originally budgeted. This is due in part to lower board costs, because the chair of the FAR's board was appointed with effect from 8 April 2016, and in part to lower office costs in relation to management support. In addition, the costs of conferences were € 38,000 lower than budgeted because the conferences, masterclasses and suchlike organised by the FAR were being started up, and because the number of international conferences on auditing research attended was still limited. Taking account of the creation of the continuity reserve, the committed contributions were realised in full, resulting in total income of € 1.6 million.

8. Events after the balance sheet date

There are no events after the balance sheet date.

9. Proposed recognition of balance of income and expenses for the first (extended) financial year

The FAR's board has approved that the balance of income and expenses for 2016, in the amount of € 229,000, will be added in full to the continuity reserve. This has been recognised in the financial statements.

The financial statements were adopted by the FAR's executive board in Amsterdam on 23 June 2017:

sgd dr. O.P.G. Bik RA
*Managing director and
academic board member*

sgd Prof. dr. J.F.M.G. Bouwens
*Managing director and
academic board member*

sgd Prof. dr. H.M. Prast
Chair of the board

The financial statements were also approved by the other members of the FAR's governing board at the board meeting held in Amsterdam on 7 July 2017:

sgd Prof. dr. W.F.J. Buijink
Academic board member

sgd Prof. drs. E. Eeftink RA
Board member representing KPMG

sgd drs. J.F.M. Kamphuis RA
Board member representing EY

sgd drs. P.A.J. Hopstaken RA
*Board member representing Mazars, BDO,
Baker Tilly Berk and Grant Thornton*

sgd Prof. dr. W.R. Knechel
Academic board member

sgd drs. M. de Ridder RA
Board member representing PwC

sgd M.J. van der Vegte RA
Board member representing Deloitte

OTHER INFORMATION

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INDEPENDENT AUDITOR'S REPORT

To: the Board of Stichting Foundation for Auditing Research

A. Report on the audit of the financial statements included in the annual report for the extended financial year from 20 October 2015 to 31 December 2016 inclusive

Our opinion

We have audited the financial statements for the extended financial year from 20 October 2015 to 31 December 2016 inclusive of Stichting Foundation for Auditing Research, based in Amsterdam.

In our opinion the accompanying financial statements give a true and fair view of the financial position of Stichting Foundation for Auditing Research as at 31 December 2016, and of its result for the period 20 October 2015 to 31 December 2016 inclusive in accordance with the Guideline for annual reporting 640 "Not-for-profit organisations" of the Dutch Accounting Standards Board.

The financial statements comprise:

1. the balance sheet as at 31 December 2016;
 2. the statement of income and expenses for the period 20 October 2015 to 31 December 2016 inclusive;
- and
3. the notes comprising a summary of the accounting policies and other explanatory information.

Basis for our opinion

We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. Our responsibilities under those standards are further described in the 'Our responsibilities for the audit of the financial statements' section of our report.

We are independent of Stichting Foundation for Auditing Research in accordance with the *Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten* (ViO, Code of Ethics for Professional Accountants, a regulation with respect to independence) and other relevant independence regulations in the Netherlands. Furthermore we have complied with the *Verordening gedrags- en beroepsregels accountants* (VGBA, Dutch Code of Ethics).

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

B. Report on the other information included in the annual report

In addition to the financial statements and our auditor's report thereon, the annual report contains other information that consists of the board report.

Based on the following procedures performed, we conclude that the other information is consistent with the financial statements and does not contain material misstatements.

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We have read the other information. Based on our knowledge and understanding obtained through our audit of the financial statements or otherwise, we have considered whether the other information contains material misstatements.

By performing these procedures, we comply with the requirements of the Dutch Standard 720. The scope of the procedures performed is substantially less than the scope of those performed in our audit of the financial statements.

The board is responsible for the preparation of the other information, including the board report in accordance with the Guideline for annual reporting 640 "Not-for-profit organisations" of the Dutch Accounting Standards Board.

C. Description of responsibilities regarding the financial statements

Responsibilities of the executive board and members of the Board who are not members of the Executive board for the financial statements

The Executive Board is responsible for the preparation and fair presentation of the financial statements in accordance with the Guideline for annual reporting 640 "Not-for-profit organisations" of the Dutch Accounting Standards Board. Furthermore, the Executive Board is responsible for such internal control as the board determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

As part of the preparation of the financial statements, the Executive Board is responsible for assessing the foundation's ability to continue as a going concern. Based on the financial reporting frameworks mentioned, the Executive Board should prepare the financial statements using the going concern basis of accounting unless the board either intends to liquidate the foundation or to cease operations, or has no realistic alternative but to do so.

The Executive Board should disclose events and circumstances that may cast significant doubt on the foundation's ability to continue as a going concern in the financial statements.

Members of the Board who are not members of the Executive Board are responsible for monitoring the process of financial reporting of the foundation.

Our responsibilities for the audit of the financial statements

Our objective is to plan and perform the audit assignment in a manner that allows us to obtain sufficient and appropriate audit evidence for our opinion.

Our audit has been performed with a high, but not absolute, level of assurance, which means we may not detect all material errors and fraud during our audit.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

We have exercised professional judgement and have maintained professional skepticism throughout the audit, in accordance with Dutch Standards on Auditing, ethical requirements and independence requirements. Our audit included e.g.:

- Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the foundation's internal control;
- Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board;
- Concluding on the appropriateness of management's use of the going concern basis of accounting, and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the foundation's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause a foundation to cease to continue as a going concern;
- Evaluating the overall presentation, structure and content of the financial statements, including the disclosures; and
- Evaluating whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant findings in internal control that we identify during our audit.

Amsterdam, June 23, 2017

RSM Netherlands Accountants N.V.

was signed drs. W.J.O. Castricum RA

The Foundation

The Foundation for Auditing Research offers the unique opportunity to bring about cooperation between researchers and audit firms for exchange in the search for the drivers of audit quality and the root causes of audit quality failures.

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