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# 1

## **Opportunities for Assurance Services in the 21st Century: A Progress Report of the Special Committee on Assurance Services**

**Richard Lea**

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### **BACKGROUND AND FOCUS OF THE PAPER**

The Special Committee on Assurance Services (SCAS) was established in 1994 to develop new opportunities for the accounting profession to provide value-added assurance services. The Committee is composed of 14 members: six partners from the Big 6, one partner from a regional firm and two from local firms, a corporate financial executive, a representative from the GAO, two academics, and one communications consultant. In addition, SCAS has an Executive Director and other support staff provided by the AICPA. The Committee is scheduled to complete its deliberations and issue its final report at the end of 1996.

The stimuli leading to the formation of SCAS included the following:<sup>1</sup>

- Flat revenues earned for accounting and auditing services for the six years 1989 to 1994.
- Loss in market share of decision useful information covered by an audit.
- Ongoing concerns regarding the “tough problems” (for example, detection of fraud and illegal acts, financial distress and business failure, choice of generally accepted accounting principles).
- Dramatic developments in information technology that are leading to profound changes in how decision-makers deal with information (for example, format, content, timing, sources).
- Jenkins Committee findings and recommendations involving a new business reporting model and possible auditor involvement.<sup>2</sup>
- Increasingly contentious litigation problems.

The charge given to SCAS by the Board of Directors of the AICPA is to:

- Assess the current and future (i.e., 5-10 years out) needs of users of decision- making information and related needs for audit/assurance services.
- Examine the trends shaping the audit/assurance environment.
- Consider the definition of the audit/assurance function and the need for additional concepts.
- Identify opportunities for new or improved assurance services.
- Consider implications for potential changes in independence, professional skills, and professional education.

SCAS’s plan for addressing this charge involves three phases containing the following major tasks:

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<sup>1</sup> See: Elliott, R. K., 1994, Confronting the Future: Choices for the Attest Function, *Accounting Horizons* 8 (3): 106-124; Elliott, R. K., 1994, The Future of Audits, *The Journal of Accountancy* (September): 74-82.

<sup>2</sup> See: Special Committee on Financial Reporting, 1994, *Improving Business Reporting - A Customer Focus*, American Institute of Certified Public Accountants.

### **Phase I (completed):**

- Identification of customer needs (44 interviews were conducted by an outside consulting firm with senior management and boards of directors of corporations, institutional investors, banks, educational institutions, governmental agencies, etc.).
- Identification of current competencies (sources included human resource representatives of selected CPA firms as well as research by the AICPA and a recent New Zealand study).
- Identification of significant developments in the political, social, economic and technological environments (SCAS was assisted by experts in trend assessment, economic forecasting, and information technology).
- Establishment of a communication and change management function, which began the process of making contacts with all interested audiences, stakeholders, and constituencies (for example, CPA firms, regulatory agencies, financial executives, state CPA societies, etc.).

### **Phase II (in process):**

- Consideration of the future of the current audit. This involves a scenario building exercise that looks at various prototype audits such as: i) a large, publicly held, multinational, financially sophisticated client; ii) a small, privately held, domestic, financially less sophisticated client; and iii) a small governmental unit.
- Identification of additional assurance services representing “close-in” extensions of the current audit. This involves, among other things, a survey of firms to assess the types of “close-in” extensions presently being conducted in today’s market.
- Identification of new assurance services. This involves both the development of an institutional process for the ongoing identification and development of new assurance services and the development of illustrative business plans for introducing new assurance services.
- Identification of alternative approaches for dealing with legal liability issues.

### **Phase III (not yet started):**

- Identification of new competencies required for new types of assurance services that may be offered in the next ten years.
- Development of an appropriate conceptual framework for new assurance services. This task began in Phase I with the development of a working definition of “assurance services” - see further below.
- Testing of proposed assurance services with customer and business panels.
- Identification of barriers to the introduction of additional assurance services and ways to deal with them.

The remainder of this paper will focus on four areas of SCAS’s work: i) a proposed definition of assurance services; ii) an outline of a proposed scenario for the future of the current audit; iii) a brief overview of a proposed process for the ongoing identification and development of new assurance services; and iv) an example of an identified opportunity for extending assurance services to a new area. In reviewing the remainder of this paper, the reader should keep in mind that the next four sections represent “work in process.” All of these proposals are presently in the process of

development. Accordingly, SCAS is very eager to receive feedback from participants at this symposium as it completes Phase II and moves on to Phase III.<sup>3</sup>

## I - PROPOSED DEFINITION OF ASSURANCE SERVICES

The committee is proposing the following definition of assurance services:

**Assurance services are independent professional services that improve the quality of information, or its context, for decision-makers.**

Several aspects of this definition are worthy of comment. First, and most importantly, the definition adopts a *customer focus* by explicitly identifying the decision-maker as the intended beneficiary of assurance services. A customer focus is introduced for three reasons:

- 1- Over the past 15 years, virtually all industries have seen a dramatic shift in power from producers (suppliers, preparers) to customers (consumers, users). This shift is due to advances in technology, which have created the means for efficient and effective delivery of highly customized (demassified) products and services.
- 2- The explosive growth in networking of organizations and individuals is providing customers with increasingly rapid communications regarding customization possibilities. This connectivity fuels the power shift from producers to consumers.
- 3- Just as customers elsewhere have gained power, the customers for “decision-useful” information can be expected to do the same. Information technology is quickly providing opportunities for information users to receive the information they need any time, any place, and in any format.

In short, information is rapidly becoming a “buyers’ market,” and the proposed definition of assurance services explicitly recognizes this trend.

A second element of the proposed definition deals with the nature of the benefit that an assurance service provides to decision-makers, namely, *improvement in the quality of (decision-making) information, or its context*. Relevance and reliability are the two primary qualities that make information useful for decision making.<sup>4</sup> To date, the audit function has focused almost exclusively on enhancement of reliability for the benefit of users. In contrast, relevance enhancement has remained within the domain of the Financial Accounting Standards Board and its predecessor organizations (GASB is also charged with relevance enhancement).

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<sup>3</sup> Written comments may be sent to SCAS’s Executive Director, Don Pallais: 14 Dahlgren Road, Richmond VA 23233 (fax: 804/784-0885; e-mail: 75471.162@compuserve.com).

<sup>4</sup> See: Financial Accounting Standards Board, 1980, Statement of Financial Accounting Concepts No. 2: *Qualitative Characteristics of Accounting Information*.

SCAS predicts that assurance services will experience a dramatic shift in the next ten years in the relative emphasis given to reliability versus relevance. Relevance will become the primary benefit offered to users of assurance services. This shift in benefits to users is expected to occur for the following reasons:

1. Information systems are becoming increasingly reliable as designs exploit developments in software technology (object programming, extensive beta testing, code generators, etc.)
2. Information system reliability is further enhanced by the development of: i) electronic sensors and software agents that are capable of identifying unusual events or relationships; ii) fail-safe measures that exploit the rapid decrease in cost to performance ratios by building in massive redundancies.
3. The explosive growth in on-line information sources places a premium on the ability of decision makers to identify what is relevant. In short, on-line information has the capacity to: “drown them [decision makers] in data.... CPAs have a natural advantage in helping business decision makers navigate these seas of data and gather what will best support their decision needs.”<sup>5</sup>

### **A Closer Look at Relevance**

One way in which relevance is likely to be established will be through information technology. Users (individuals and groups) will explicitly state their information needs by their inquiries of preparer data bases and by their direct feedback addressed to preparers (and/or assurers). In short, the test for relevance under this scenario will become: ***If the user asks for the data, the data are relevant.***

A more penetrating analysis of relevance for a particular user will involve an exploration of various facets of the user’s decision modeling activities and the role of information in those activities. SCAS predicts that assurance regarding relevance will quickly move in this direction, in which case various modeling activities, such as those shown in Figure 1, will need to be explored.

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<sup>5</sup> Elliott, R. K. 1994, The Future of Audits, *Journal of Accountancy* (September), 78.

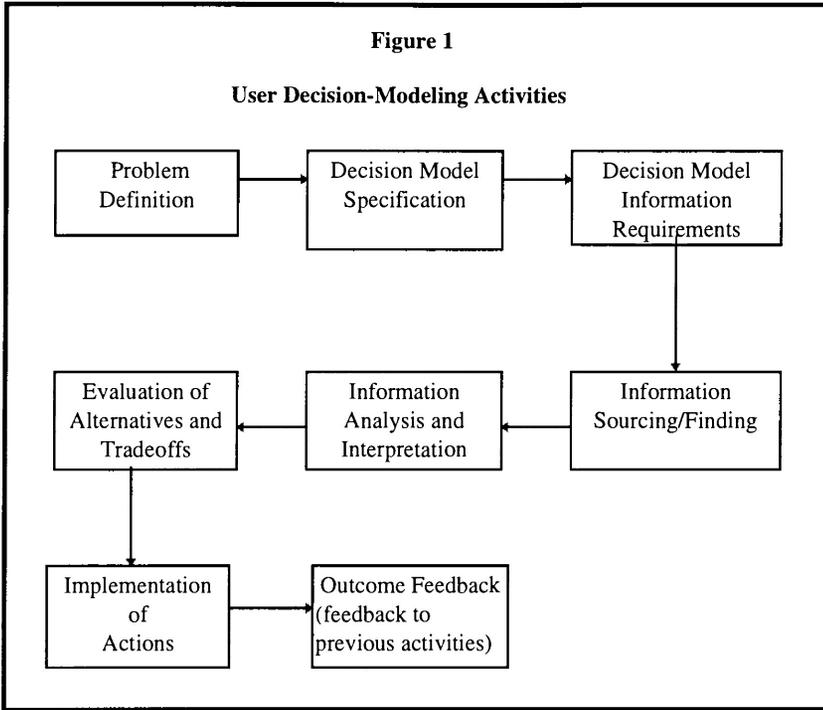


Table 1 presents a brief description of the types of assurance that might be provided to a particular user with respect to each of the decision-making activities identified in Figure 1. The table also identifies information technology developments that will have an impact on the various types of assurance.

Several points about the content of the Table 1 should be emphasized. First, many of the “assurances” identified in the middle column represent services that, in today’s market, would involve adding an assurance component to present consulting services. (See the Appendix for additional comments on the boundaries of assurance services vs. consulting services). In short, a very broad perspective is being taken regarding assurance services, namely, assurance services are any services that assist information users in improving the quality of their decision-making information, including their decision model.<sup>6</sup>

<sup>6</sup> When viewed broadly, “decision-making information” includes a user’s decision model, which is simply a set of information organized in a particular way for the purpose of making a decision. In this sense, issues regarding the quality of information extend naturally to the quality of decision models.

**Table 1**

**User Decision-Modeling Assurance**

<u><b>Decision Activity</b></u>	<u><b>Nature of Assurance Provided</b></u>	<u><b>Information Technology Considerations</b></u>
<b>Overview of assurers' involvement with specific users:</b>	Extensive involvement with specific users will become the norm.	Users will need much more assistance from assurers because of: -Vast amounts of available information -Increased electronic access -Rapid degradation in value -Widespread availability and use of computer decision models.
1 - Problem definition	-Problems will involve a broad range of economic and social issues faced by information users/decision makers; assurance may be given regarding the appropriateness of problem definition.	A broader range of issues may be identified and monitored through efficient and effective electronic sensors.
2 - Decision model specification	-Specific decision models tailored to specific user needs will become the norm; assurance may be given regarding the appropriateness of the model, given the problem definition.	Computer decision models used to model a broad range of economic and social decision problems will become widely available.

**Table 1 - Cont.**

**User Decision-Modeling Assurance**

<b><u>Decision Activity</u></b>	<b><u>Nature of Assurance Provided</u></b>	<b><u>Information Technology Considerations</u></b>
3 - Decision model information requirements	Information requirements will be identified in the context of the specific decision model that has been selected by the user. Assurance may be given regarding relevance of proposed information.	Complexity of computer decision models may require specialized skills in determining appropriate information required to run the models.
4 - Information sourcing/finding	-Users may need assistance in searching through vast quantities of information; assurance may be given regarding completeness of search.	Search processes will be influenced by: -Vast volume of available data -Increased electronic access -Development of efficient and effective software agents (perhaps controlled by assurers).
5 - Information analysis and interpretation	-Users will continue to seek assistance in analysis and interpretation from "information intermediaries," which may include assurers.	Even in contexts of formal computer decision models, users will need assistance in analysis/interpretation because: -Data may be in multimedia format, much of which will not fit neatly into formal decision models -Much data will not be "controlled" by standards enforced on preparers -Vast quantities of data will be available.

**Table 1 - Cont.**

**User Decision-Modeling Assurance**

<u><b>Decision Activity</b></u>	<u><b>Nature of Assurance Provided</b></u>	<u><b>Information Technology Considerations</b></u>
6 - Evaluation of alternatives and tradeoffs	- Users will continue to seek assistance in weighing alternatives and tradeoffs from “information intermediaries,” which may include assurers.	Computerized decision models may do much of this, but significant judgments may be still be left to the decision-maker.
7 - Implementation of actions	-Users may seek greater assistance in implementation, including assurance regarding appropriateness of implementation reporting activities.	Expertise will be needed in the design of electronic sensors to monitor implementation activities, which may be provided by assurers.
8 - Outcome feedback: -Feedback to preparers -Feedback to assurers	-Users will provide increasing feedback directly to preparers because of extensive user-preparer linkages and to assurers because of greater assurer involvement in user decision-making activities.	Emergence/proliferation of user “chat groups” will enhance communication links among users and between users, preparers, and assurers.

Second, other parties besides members of the profession are (or may become) involved in the delivery of assurance services identified Table 1. The profession will not have a monopoly on any of these services and must compete with others on the basis of perceived independence and competence. Third, many of the “assurances” involve issues for which standards are unlikely to provide detailed guidance; consequently, delivery of these types of assurances will involve high degrees of professional judgment. Fourth, even though many of the decision activities identified in Table 1 are assumed to take place within the context of a formal, well-defined computerized decision model ( a rapid increase in the availability of such models is expected ), considerable “expert judgment” outside of formal model boundaries will continue to be required.

**Independence and Professional Judgment**

Returning to the above proposed definition of assurance services, the third and final element of the definition that deserves comment involves the two adjectives in the phrase “*independent professional services*.” Both adjectives were briefly mentioned in the above discussion of relevance.

Historically, *independence* has been the foundation stone upon which the audit function has been erected: “Independence is the cornerstone of the accounting profession and one of its most precious

assets.”<sup>7</sup> SCAS believes that independence should remain a “bedrock” concept for all assurance services. In their roles as decision makers, information users must draw upon a wide range of information prepared by others, which immediately introduces the possibility that preparer and user interests are not congruent. Recognizing this possibility, users may want to seek the assistance of an assurer, who is recognized as independent of the preparer. Indeed, users will turn to assurers only if they believe that assurers have no stake in the outcome, other than to assist users in improving the quality of information (and decision models) entering into the user’s decision-making process.

SCAS’s purpose in including the second adjective, “*professional*,” is to underscore a major element involved in the delivery of virtually all assurance services, namely the high level of professional judgment involved. As indicated above, providing “assurance” involves numerous judgment calls for which standards are unlikely to provide detailed guidance. Even in those cases in which the user’s decision has been captured in a formal computerized decision model, considerable “expert judgment” is generally required outside of formal model boundaries. Hence, professional judgment is now, and will continue to be, an essential ingredient of assurance services.

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<sup>7</sup> Mednick, Robert, 1991, “Reinventing the Audit,” *Journal of Accountancy*, August, 75.

## II - A SCENARIO FOR THE FUTURE OF THE CURRENT AUDIT

SCAS is presently (Phase II) developing scenarios regarding the future of the current audit for various types of reporting entities. The scenarios reflect a SWOT (strengths, weaknesses, opportunities, threats) analysis of the current audit process. The intention of the scenario-building exercise is to develop a coherent picture of the future of the current audit that reflects expected developments in the audit environment identified in Phase I. These scenarios will then be the basis for making recommendations regarding changes in professional skills, education, etc..

To illustrate ideas, this section will present an outline of a proposed scenario (currently in development) involving a large, publicly-held, multinational, financially sophisticated company operating in the year 2006. SCAS also is in the process of developing other scenarios involving other types of entities.

### **Large, Publicly-held Company**

The large, publicly-held company scenario provides “views” of users, preparers and audits (and auditors) in the year 2006. Two basic assumptions underlie this scenario:

1. Historical financial information (GAAP) will continue to be reported. In addition, significant “enrichment” of the information set encompassed by GAAP will occur along the lines of the Jenkins Committee recommendations. The scenario presented below deals only with GAAP information. Extensions to this information set and the resulting impacts on the scenario are presently under consideration by SCAS.
2. The SEC will continue to require audits of public companies. SCAS is presently addressing the question of how this scenario would be altered if this assumption is dropped.

Given these basic assumptions, SCAS has developed “2006 views” of users, prepares, and audits (and auditors) which are presented in detail in Table 2 and briefly summarized below.

**Table 2**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

	Commentary on the Element
<p><u>View of Users (large creditors and individual and institutional investors):</u></p>	
<ul style="list-style-type: none"> <li>Users will want and need audits</li> </ul>	<p>User need is clearly established by work of Jenkins Committee and the SCAS customer needs interviews. Users recognize that auditor involvement enhances the integrity of financial information made available in capital markets. In short, users believe that audits fulfill a "watchdog" role.</p>
<ul style="list-style-type: none"> <li>Users will continue to look to audited financial statements as the key test of integrity of all published financial information</li> </ul>	<p>See previous comment. Although the annual period for audits will probably not change, the critical notion is that a "true-up" will occur regularly, which adds integrity to all financial information reported between successive "true-ups."</p>
<ul style="list-style-type: none"> <li>Users will continue to accept the "yes/no" audit report as a "seal of approval" regarding financial information</li> </ul>	<p>The messages contained in the auditor's report involving "reasonable assurance (confidence)" and "materiality (precision)" may undergo refinement. Users are believed to have more of a need for understanding the imprecision in information, perhaps through the communication of ranges (see below), than they have for understanding different levels of assurance. Reporting on "systems quality" may go beyond a "pass/fail" message and report on specific risk exposures - see further below under <u>Preparer</u>.</p>
<ul style="list-style-type: none"> <li>Power will shift from preparers to users, who will favor entities that provide more timely and complete disclosure</li> </ul>	<p>Connectivity provides for communication among users via chat groups, which will create the opportunity for users to speak with one voice. The recent Intel chip problem is indicative of how fast users can organize themselves on a public network to exert considerable power.</p>
<ul style="list-style-type: none"> <li>Users will become electronically "connected" with each other and with preparers and auditors</li> </ul>	<p>See the above comment on connectivity of users. Connectivity of users with preparers and auditors provides the necessary feedback loops for user views to become more clearly articulated.</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

<p><u>Elements of the 2006 Views View of Users (large creditors and individual and institutional investors) - cont.:</u></p>	<p><u>Commentary on the Element</u></p>
<ul style="list-style-type: none"> <li>• Connectivity will provide an ongoing "negotiation forum" for users vs. preparers. Points of negotiation will include:                             <ul style="list-style-type: none"> <li>• Levels of disaggregation</li> <li>• Treatment of soft information</li> <li>• Choice of multimedia formats</li> </ul> </li> </ul>	<p>See above comments on connectivity. The negotiation forum provides users with the essential feedback communication loop necessary to make their needs known regarding "precision" and also "level of assurance."</p>
<ul style="list-style-type: none"> <li>• Users will demand more:                             <ul style="list-style-type: none"> <li>• Disaggregation</li> <li>• Qualitative commentary (e.g., expanded MD&amp;A)</li> </ul> </li> </ul>	<p>These needs were clearly identified by the Jenkins Committee. Although users have expressed interest in auditors providing qualitative commentary (See Jenkins Committee report, Ch. 7), preparers will strongly resist this idea - see further below under <b>Preparers</b>.</p>
<ul style="list-style-type: none"> <li>• Users will expect timely, on-line financial information (GAAP) that provides "drill-down" options</li> </ul>	<p>Developments in information technology will sweep away barriers inhibiting timely reporting, and users quickly will become aware of these developments and make their demands known for timely information.</p>
<ul style="list-style-type: none"> <li>• Users will become adept at "mining" on-line information</li> </ul>	<p>Users may well need the help of "financial intermediaries" in attempting to search through the "sea of data" that will be available on public networks, but user capabilities will also dramatically increase here.</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

<u>Elements of the 2006 Views</u>	<u>Commentary on the Element</u>
<p><u>View of Users (large creditors and individual and institutional investors) - cont.:</u></p> <ul style="list-style-type: none"> <li>• Users will expect auditor involvement to lead to significant improvements in dealing with the <u>tough problems</u>:                             <ul style="list-style-type: none"> <li>• Detection of fraud and illegal acts</li> <li>• Early warning of financial distress</li> <li>• Early reporting on deviations from "expected"</li> <li>• Reporting on risks, uncertainties, estimates</li> <li>• Appropriateness of preparer's choice of GAAP</li> </ul> </li> <li>• Users will have the power to invoke "severe penalties" on entities that:                             <ul style="list-style-type: none"> <li>• Reveal prior misstatements</li> <li>• Report unpleasant surprises</li> <li>• Fail to report "negatives" on a timely basis</li> </ul> </li> </ul>	<p>Users will expect auditors to improve their detection capabilities. Users will also expect auditors, who they will view as working in the users' interests, to push for better disclosures in the listed areas.</p>
<ul style="list-style-type: none"> <li>• Users will have the power to invoke "severe penalties" on entities that:                             <ul style="list-style-type: none"> <li>• Reveal prior misstatements</li> <li>• Report unpleasant surprises</li> <li>• Fail to report "negatives" on a timely basis</li> </ul> </li> </ul>	<p>The Wall Street Journal regularly reports cases where "surprises" have led to dramatic declines in share prices. Connectivity will speed up user reaction and probably make it more severe, since users will be speaking with one voice. Users will demand that the reporting of "negatives" encompass lots of issues less extreme than potential business failure and also encompass a much longer time frame than the current one-year period associated with the "going concern" issue.</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

<p><b><u>View of Preparers (large, publicly-held, multinational, financially sophisticated):</u></b></p>	
<ul style="list-style-type: none"> <li>• Preparers will become increasingly responsive to users:             <ul style="list-style-type: none"> <li>• Power shift to users</li> <li>• Self interests of preparers will lead to adoption of a "customer focus"</li> </ul> </li> </ul>	<p>Users will seize power (see above), and preparers will give up power regarding disclosure in order to achieve lower costs of capital.</p>
<ul style="list-style-type: none"> <li>• Preparers will face increasingly complex GAAP reporting:             <ul style="list-style-type: none"> <li>• More countries</li> <li>• More currencies</li> <li>• More tax laws and regulations</li> <li>• More complex financial instruments</li> </ul> </li> </ul>	<p>The "multi" dimension will continue to make reporting increasingly complex. Opening markets in the former Soviet Union, Eastern Europe, and China are current examples.</p>
<ul style="list-style-type: none"> <li>• Preparers will seek timely auditor involvement on the complex, nonroutine transactions</li> </ul>	<p>Preparers will want to avoid being "burned" by financial reporting errors or reporting of unpleasant surprises. Developments in information technology enables preparers to seek timely, in-depth auditor involvement.</p>
<ul style="list-style-type: none"> <li>• Preparers will provide timely, on-line multimedia presentations of GAAP financial information (e.g., via WWW home pages)</li> </ul>	<p>Network presentations will become the most efficient and effective means for communicating financial information.</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

Elements of the 2006 Views	Commentary on the Element
<p><b>View of Preparers (large, publicly-held, multinational, financially sophisticated) - cont.:</b></p>	
<ul style="list-style-type: none"> <li>• Connectivity with users will provide preparers with feedback on user needs</li> </ul>	<p>See previous comments on connectivity and feedback communication loops between users, preparers, and auditors.</p>
<ul style="list-style-type: none"> <li>• Preparers will be pressured to disclose more and more "competitively sensitive" information</li> </ul>	<p>The tension between the user's right to know vs. the preparer's need for confidentiality of competitively sensitive information is not new and will continue. However, the power of the user is a new development, which will alter the balance towards greater disclosure. Also, as the pace of change quickens, the length of the period needed for protection of sensitive information is reduced (i.e., sensitive information becomes stale very quickly).</p>
<ul style="list-style-type: none"> <li>• Preparers will resist user demands for auditor qualitative commentary</li> </ul>	<p>Preparers will aggressively move to maintain control of the interface with users. Qualitative commentary will be seen as the preparer's legitimate domain. Also, auditor commentary will be seen as undermining the free flow of information in an audit. The audit process must allow for auditors to know more than they say; otherwise, the process would become adversarial. If auditors announce to preparers that they intend to add qualitative commentary, the preparer's likely response will be that they will provide the commentary and the auditors can review it for reasonableness. Hence, auditor commentary would become redundant.</p>
<ul style="list-style-type: none"> <li>• Preparer financial systems will move towards highly integrated data bases with powerful query capabilities</li> </ul>	<p>This movement is swiftly becoming a reality as systems, such as SAP, become implemented.</p>
<ul style="list-style-type: none"> <li>• Preparers will experiment with providing users with "defined views" of their data bases</li> </ul>	<p>In short, lots of different disclosure possibilities will be enabled by technology, ranging from providing defined views of data bases to highly structured, multimedia presentations developed by the preparer.</p>
<ul style="list-style-type: none"> <li>• Preparers will continue to increase their connectivity with other preparers (e.g., EDI linkages) in their value chain</li> </ul>	<p>This connectivity will continue to take place to improve the efficiency and effectiveness of preparer operating processes. As described further below under <b>Audits</b>, this connectivity will open up significant opportunities for new types of audit evidence involving triangulation (i.e., looking at the same transactions from different entity perspectives).</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

<u>Elements of the 2006 Views</u>	<u>Commentary on the Element</u>
<u>View of Preparers (large, publicly-held, multinational, financially sophisticated) - cont.:</u>	
<ul style="list-style-type: none"> <li>Systems reliability will increase with respect to routine transaction processing</li> </ul>	<p>Reliability enhancements will reflect improvements in software reliability (preventive controls), use of electronic sensors and software agents for monitoring and detection, and use of massive redundancy to insure fail-safe operation. Note that these reliability enhancement possibilities will also be available to the auditor in assessing system quality and searching for exceptions - see further below.</p>
<ul style="list-style-type: none"> <li>Systems will move from paper-based to an electronic-based environment</li> </ul>	<p>New types of risks will arise involving authentication, trustholding, and privacy.</p>
<ul style="list-style-type: none"> <li>BofD's and senior management will want assurance on the quality of their complex, integrated, multinational financial systems</li> </ul>	<p>The "multi" dimension of financial reporting systems will be of particular concern to BofDs and senior management because of the uneven skills/expertise resident in various domiciles.</p>
<b>View of Audits and Auditors:</b>	
<ul style="list-style-type: none"> <li>Audits will continue as a "core competence" service and will involve annual audit reports on yearly GAAP financial information</li> </ul>	<p>"Clean" audit reports across the range of publicly-held entities will continue to be the primary test of financial market integrity and the stamp of approval on all financial information that flows from public companies during the year.</p>
<ul style="list-style-type: none"> <li>MD&amp;A type information will increasingly become part of the audited financial statements</li> </ul>	<p>Auditor reviews of MD&amp;A will be the preparer's solution for dealing with user demands for auditor qualitative commentary. These reviews will be performed for the purpose of detecting misstatements, inconsistencies, and/or omissions in management's analytical commentary.</p>

Table 2 - Cont.

Large, Publicly-held Entities  
2006 Views of Users, Preparers, Auditors and Auditors

Elements of the 2006 Views View of Auditors and Auditors - cont.:	Commentary on the Element
<ul style="list-style-type: none"> <li>Auditors will be requested by preparers to give assurance in real time on significant, nonroutine transactions:                             <ul style="list-style-type: none"> <li>Continuous auditing will become the norm, leading to much faster issuance of the year-end audit report</li> </ul> </li> </ul>	<p>Continuous auditing of routine transactions will involve auditor monitoring of the preparer's <u>process</u>, using new techniques enabled by technology - see below. Continuous auditing of nonroutine transactions will involve auditor examination of <u>outputs</u> of the preparer's system. In short, the audit will become process oriented for the routine and output oriented for the nonroutine.</p>
<ul style="list-style-type: none"> <li>Worldwide audit networks will focus on timely responses to the "nonroutine," which will often involve multinational dimensions                             <ul style="list-style-type: none"> <li>Multi country, multi currency, etc.</li> </ul> </li> </ul>	<p>Timely responses worldwide is recognized as an extremely important "value-added" dimension of the audit process involving large companies.</p>
<ul style="list-style-type: none"> <li>As preparer systems become increasingly reliable in processing routine transactions, audit effort will shift away from getting the "bookkeeping correct":                             <ul style="list-style-type: none"> <li>Detailed substantive tests for accuracy will be drastically reduced</li> <li>Work on detailed "transaction error" controls will be rotated over several years</li> </ul> </li> </ul>	<p>Work on controls will shift focus to prevention controls for fraud and illegal acts.</p>
<ul style="list-style-type: none"> <li>Audit emphasis will focus on solving the <u>tough problems</u> (see above list under <u>Users</u>)</li> </ul>	<p>Users will expect increased detection capability with respect to fraud, illegal acts, and financial disruption. Current audit performance in these areas is below user expectations.</p>

Table 2 - Cont.

Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors

Elements of the 2006 Views View of Audits and Auditors - cont.:	Commentary on the Element
<ul style="list-style-type: none"> <li>• The <b>tough problems</b> will be attacked with new weapons enabled by technology:               <ul style="list-style-type: none"> <li>• Triangulation that exploits connectivity of preparers</li> <li>• Electronic sensors</li> <li>• Software agents</li> <li>• Computer modeling of industry/company relationships</li> </ul> </li> </ul>	<p>Many of the information technology innovations that preparers will use to strengthen the reliability of their systems may also be exploited by auditors in identifying unusual transactions or events. Also, EDI linkages among preparers provides auditors with the opportunity to look at specific transactions from different entity perspectives.</p>
<ul style="list-style-type: none"> <li>• The <b>tough problems</b> will also be attacked by “sharpening” existing weapons:               <ul style="list-style-type: none"> <li>• Better understanding of industries</li> <li>• Better understanding of business and key processes in the value chain</li> <li>• Better understanding of risks</li> </ul> </li> </ul>	<p>The “better understanding” will be reflected in new makeups of audit teams - see below.</p>
<ul style="list-style-type: none"> <li>• GAAS will continue to evolve towards a more flexible, output-oriented framework, which will accommodate a variety of audit process reengineering initiatives by individual firms</li> </ul>	<p>Firm by firm innovation regarding audit processes will not be constrained by GAAS.</p>

**Table 2 - Cont.**

**Large, Publicly-held Entities  
2006 Views of Users, Preparers, Audits and Auditors**

Elements of the 2006 Views View of Audits and Auditors - cont.:	Commentary on the Element
<ul style="list-style-type: none"> <li>• Auditor training will need to focus on:                             <ul style="list-style-type: none"> <li>• Better understanding of the "multi" issues</li> <li>• Better understanding of industries</li> <li>• Better understanding of business processes</li> <li>• Better understanding of information technology</li> </ul> </li> </ul>	<p>Although this list contains no surprises, the Committee feels strongly that the <u>tough problems</u> will only be solved by bringing new knowledge and skill sets to the audit team.</p>
<ul style="list-style-type: none"> <li>• Audit teams will need to dramatically expand their knowledge and skill sets:                             <ul style="list-style-type: none"> <li>• Fraud specialists</li> <li>• Legal, regulatory knowledge</li> <li>• Industry expertise</li> <li>• Business process expertise</li> <li>• Information technology skills</li> </ul> </li> </ul>	<p>See above comments on training .</p>

## Large, Publicly- held Company - 2006 Views

Based on the detailed analysis presented in Table 2, SCAS expects the following:

### Users will ...

- Continue to want and need audits
- Exert increasing power vis-à-vis preparers
- Demand real time access to financial information
- Increase their competence in information technology
- Have rising expectations regarding audits

### Preparers will ...

- Adopt a customer (user) focus
- Face increasing complexity
- Seek timely auditor involvement
- Develop highly reliable systems for the “routine”
- Experiment with a range of disclosure options enabled by information technology

### Audits will ...

- Continue as the primary “check and balance” on the integrity of financial reporting in public markets
- Provide preparers with timely assurance for the “non-routine”
- Redirect resources away from bookkeeping to the “tough problems”
- Attack the tough problems with new information technology weapons and sharpened existing weapons
- Be conducted by teams with more varied skill sets
- Remain the “bedrock” upon which other assurance services will be built.

## III - OVERVIEW OF A “NEW LINES” DEVELOPMENT PROCESS

SCAS and its various subcommittees are in the process of identifying new opportunities for the accounting profession involving extensions of existing assurance services and new assurance services. We hope that many of these identified opportunities will lead to the implementation of new services that will add value to users in their various decision-making activities. SCAS recognizes, however, that the real solution for the profession in the long run is not simply to identify a list of today’s opportunities. Such a list will inevitably have a very limited useful life. Instead a *process* is needed that will: i) continuously monitor long-term trends affecting assurance services; ii) assess new market needs; and iii) convert those needs into new assurance services.

SCAS believes that such a process should reside within the AICPA. The AICPA has considerable strengths that can be used to identify and validate new assurance service opportunities. The Institute has standard-setting power, and it can play an important role in positioning new assurance services as “CPA services” in the marketplace. The AICPA benefits from a diverse and involved membership that has daily contact with the marketplace. The Institute also has a large membership that buys CPA assurance services (CPAs in industry and government). Finally, as an organization that represents many financial executives in the aforementioned groups, the AICPA has access to governmental agencies, regulators, other associations of professionals, and a variety of resources that are not generally accessible to individual CPA firms.

SCAS recognizes, however, that the AICPA presently has certain inherent limitations that makes it less than an ideal organization for identifying new market opportunities and quickly developing responsive assurance services.. Table 3 identifies some of the limitations in the AICPA that must be set aside or changed in order to adopt a more aggressive role in service development activities.

<b>Table 3</b>	
<b>Limitations in Present AICPA Process</b>	
<b>AICPA Process</b>	<b>Desired Process</b>
· Generally reacts to practice problems	· Early identification of customer needs
· Consensus is good for standards development but not for innovation	· Early release of business development information without standards development or consensus
· Limited access to capital for product development	· Ability to bring necessary effort to bear to create new services
· New opportunities do not benefit all members equally	· Ability to target markets
· Slow, open process avails information to competitors	· Timely development of standards, training, and practice guides
· Multiple review and approval processes limit innovation and delay product introduction	· Partnering with CPA and non-CPA enterprises for service development and delivery

Associations like the AICPA, by their nature, are intended to be inclusive, consensus-driven organizations. The professional staff, especially those responsible for standards setting operations, are encouraged to seek consensus from the membership and prevent unauthorized members from making statements or pronouncements that appear to be linked to the AICPA. The association staff must please all of the members, control the members, and protect the association infrastructure from criticism. This is not a particularly nurturing environment for fast-track development of new services that might, for example, benefit some firms more than others.

The AICPA also has very limited capital with which to develop new service opportunities. It is also not likely to be the principal beneficiary of revenues from new service opportunities. Individual firms that develop markets for the new services will be the primary beneficiaries and so will be willing to invest talent and capital to develop and bring them to market.

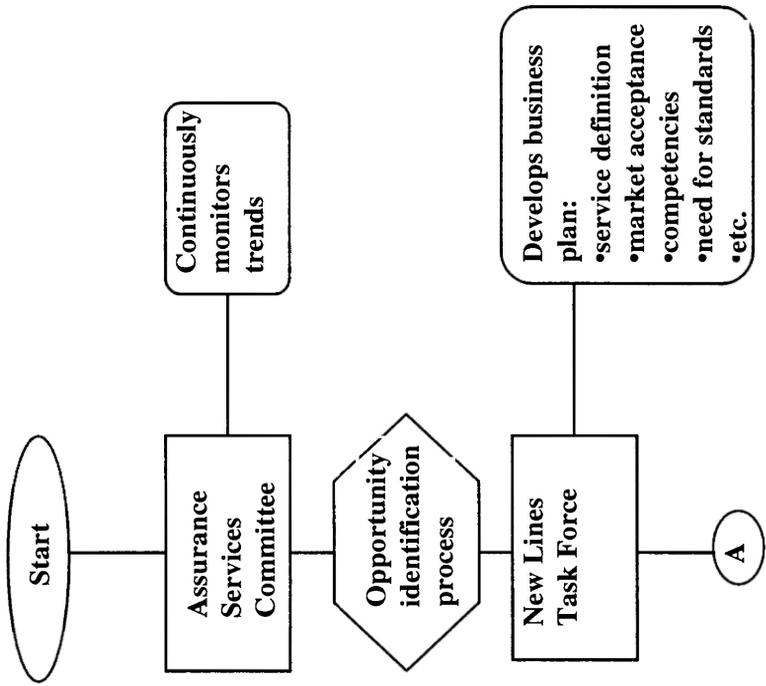
Some prospective new assurance lines can only be developed by the largest CPA firms. Others offer opportunities to small and medium-sized firms. There may also be new assurances services that benefit the entire spectrum of AICPA members in practice. While it might be in the profession’s interest for all such opportunities to be developed under the AICPA’s umbrella, it probably will not happen if they are subjected to a multi-level review and approval process.

In sum, if the AICPA is to be successful in pursuing assurance services development on behalf of its membership, then it must introduce some changes in its own organization and approaches.

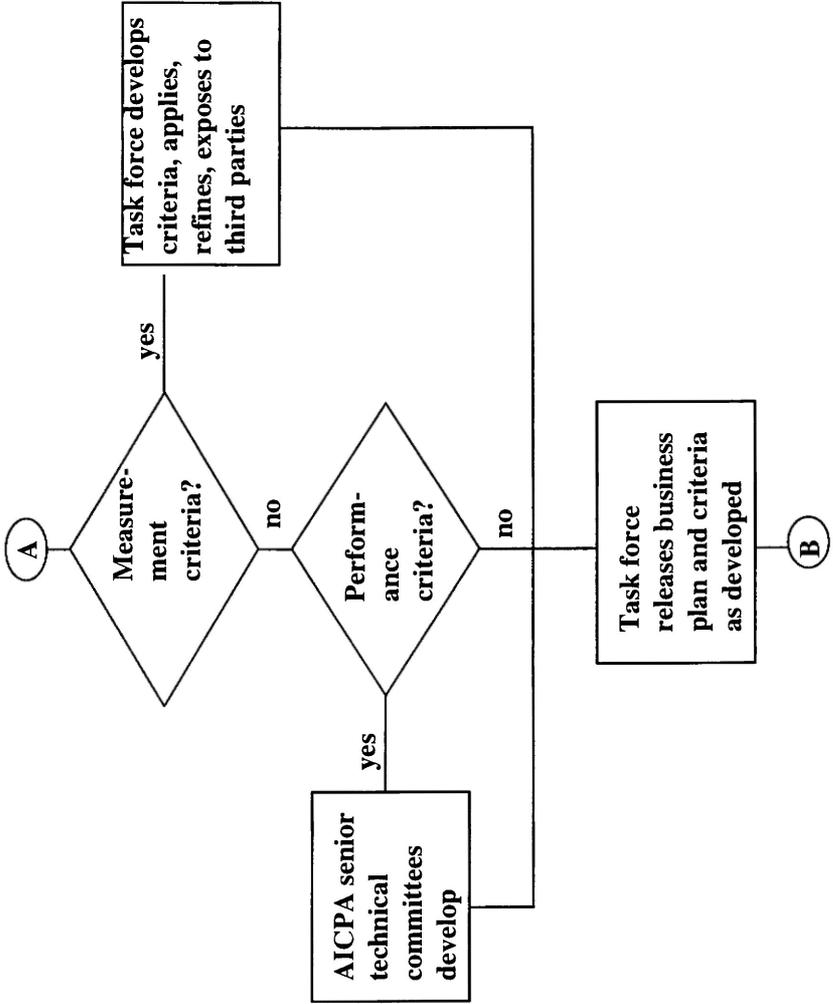
**SCAS Proposal for a New Lines Development Process**

SCAS believes that the AICPA should appoint a standing committee - the Assurance Services Development Committee (see Figure 2) - comprised of a mix of market-oriented senior partners of local, regional, and national firms that are actively involved in providing assurance

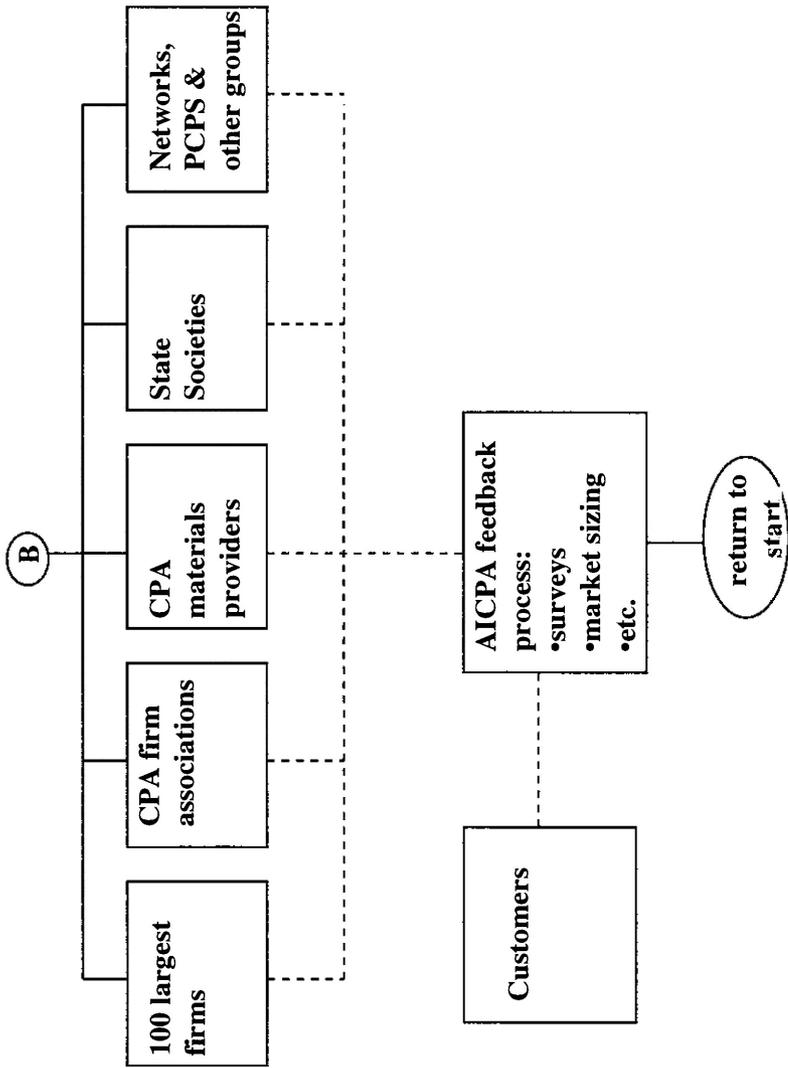
**Figure 2**  
**New Lines Development Process**



# New Lines Development Process- Cont.



# New Lines Development Process - Cont.



services. In addition, the Committee should include others within the profession who are known for their vision and future orientation. The Committee's charge would be to continuously collect and sift through information from a variety of sources to identify new or growing needs for assurance services.

As it seeks to monitor trends, the Committee would monitor the activities of the AICPA Washington office, the Strategic Planning Committee, Private Companies Practice Section (PCPS), senior technical committees, the Management of an Accounting Practice Committee (MAP), industry committees, the Accountants Forum, professional associations, such as those serving internal auditors and chief financial officers, and trends monitoring services. The Committee might also monitor developments in technology, government regulation, demographics, world trade, public policy, and a variety of other factors that could have long-term effects on assurance needs. The Committee would sift through massive and seemingly disconnected information in attempts to find meaningful and significant trends that show promise of giving rise to assurance needs. The Committee would make a preliminary assessment of which possibilities show the greatest potential for near-term development. Considerations would include market size, market attractiveness, the CPA's competitive advantages, the need for AICPA developed standards, and a variety of other issues.

For service areas that show great promise, the AICPA would create task forces to develop those services. A particular task force would bring together firms or individual CPAs who want to develop the identified service for their own practices. The task force might also create strategic alliances with industry or other specialized groups to create standards or market access.

Each task force would be charged with the development of a *business plan* for refining the identified service opportunity into a delivery mode. A business plan would address the various items listed in Figure 2 (see the **Health Care** example, below).

Members of a task force would be entitled to use the information developed by the task force in formulating new service strategies for their own practice units. Task forces would be obligated to develop business plans to a sufficient level where they can be shared with other practitioners who may wish to implement the new assurance services. If members of a task force decide to pilot the proposed new service in their own firms, they would be obligated to share the results of their efforts with the task force and other interested practitioners.

While individual CPAs or firms could develop new services on their own, task forces have the following advantages:

- Costs of development can be shared
- The Institute provides a forum for standards development
- A coordinated effort can help create a market through development of a critical mass of service providers
- The new service can be institutionalized under the CPA brand name.

If standards are required, a task force would communicate with and cooperate with appropriate senior technical committees or other working task forces to assist in their formulation. Also, a task force would develop the procedures and any reporting guidance in sufficient detail for practitioners to be able to understand and implement the services on their own. In addition, the AICPA would offer education, practice guides, and practice aids as appropriate.

Distribution to small firms would be accomplished through a variety of already established channels. Many smaller firms and sole practitioners might have limited ability to acquire the

competencies necessary to provide the new services. The AICPA would encourage development of appropriate training materials and practice aids through CPA associations (such as TAG, AAFI, and CPA Associates), state societies, CPA-oriented publishing houses, and franchisers. Wherever appropriate, the AICPA would follow along with standards and practice guides to assist practitioners and institutionalize the service as a “CPA service.”

As with the development of any new products or services in any industry, it is probable that many proposed assurance services will fail. We hope that some will soar. The AICPA should establish measurement systems to assess how broadly new service opportunities are disseminated through its membership and the size of markets developed through the new assurance services model. The Institute may also wish to monitor public acceptance of new assurance services developed through this process. This will provide further information as to how market permission is obtained for new services.

#### **IV - AN EXAMPLE OF AN OPPORTUNITY FOR EXTENDING ASSURANCE SERVICES**

As a result of the research performed in phase I, particularly the 44 customer needs interviews that covered a broad spectrum of decision makers, SCAS has been able to identify a long list of potential unmet needs for assurance services. Some of the most promising possibilities are listed in Table 4. In addition, selected possibilities are briefly analyzed in Table 5.

If the “New Lines Development Process” was presently in place (see Figure 2, above), each of the opportunities described in Tables 4 and 5 (and possibly others identified by SCAS) would immediately be passed off to various New Lines Task Forces that would begin the development of appropriate business plans. To assist such future task forces in getting started, SCAS is in the process of developing a series of “first-cut” business plans for several of the opportunities identified in Tables 4 and 5. An example of one of those proposed “first cut” business plans (work in process) is described in the following paragraphs.

**Table 4**  
**Promising Customer Needs**

<b><u>The Information/Assurance Need</u></b>	<b><u>Potential Customers</u></b>
<ul style="list-style-type: none"> <li>• Better information about business risk</li> </ul>	<ul style="list-style-type: none"> <li>• Boards of directors</li> <li>• Senior management</li> </ul>
<ul style="list-style-type: none"> <li>• Information about product quality</li> </ul>	<ul style="list-style-type: none"> <li>• Individuals</li> </ul>
<ul style="list-style-type: none"> <li>• Nonfinancial measures of performance</li> </ul>	<ul style="list-style-type: none"> <li>• Senior management</li> <li>• Individuals</li> </ul>
<ul style="list-style-type: none"> <li>• Quality of information reported to the board</li> </ul>	<ul style="list-style-type: none"> <li>• Board of directors</li> <li>• Institutional investors</li> </ul>
<ul style="list-style-type: none"> <li>• Quality of processes and controls</li> </ul>	<ul style="list-style-type: none"> <li>• Board of directors</li> <li>• Senior management</li> <li>• Investors</li> </ul>
<ul style="list-style-type: none"> <li>• Information about strategic plan execution</li> </ul>	<ul style="list-style-type: none"> <li>• Board of directors</li> <li>• Institutional investors</li> </ul>
<ul style="list-style-type: none"> <li>• Information about government performance</li> </ul>	<ul style="list-style-type: none"> <li>• Public (individuals and groups)</li> </ul>

Table 5

Identified Customer Needs  
Triangulation of Findings of Phase I

Need ID	The Customer's Need			Substantiation of Customer's Need		
	Statement of primary customer's decision problem	Desired information set	Customer needs interviews	External factors analysis	Info. tech. analysis	
#1	<p><b>Customer**</b></p> <p><b>Primary:</b> -Boards of Directors of publicly held co's</p> <p><b>Secondary:</b> -Senior mgmt. (P) -Institutional investors</p>	<p><b>Statement of primary customer's decision problem</b></p> <p>Corporate governance - Is top mgmt. effectively managing the co's portfolio of risks? Ultimately, the board's decision is whether to keep the current state of officers.</p>	<p><b>Desired information set</b></p> <p>Information about various risks, the controls in place to address those risks, and the effectiveness of those controls</p>	<p><b>Customer needs interviews</b></p> <p>-Various board members -Former FASB member -K-Mart -3M Corp -Conference Board -Calpers</p>	<p><b>External factors analysis</b></p> <p>-Increasing public demands for accountability -Increased concentration of capital in institutional investors who will hold boards accountable -Increasing pace of change in global economy leads to rapid changes in risk profiles and need for continuous monitoring</p>	<p><b>Info. tech. analysis</b></p> <p>--Rapid development and deployment of computerized risk assessment models</p>
#2	<p><b>Primary:</b> -Individual consumers of health care services</p> <p><b>Secondary:</b> -corp's and unions representing consumers -service providers (P) -third party payors (insurers, gov't)</p>	<p><b>Quality of health care</b> - What is the relative quality of care being provided by various (competing) service providers? Ultimately, the consumer's decision involves the selection of a particular service provider.</p>	<p>Comparative provider information about various medical conditions and a provider's success in dealing with those conditions in terms of improving patients' quality of life</p>	<p>-GAO -OMB -Personal life needs identified by various interviewees</p>	<p>-Increasing public demands for accountability -Aging of the U.S. population -Cost capitation in health-maintenance organizations</p>	<p>- Shift in power from producers to consumers who now have easy access to vast amounts of data</p>

\*\* The likely payor for the "service" that would be involved in meeting the primary customer's information/d. esion-making need is identified with a (P).

Table 5 - Cont.

Identified Customer Needs  
Triangulation of Findings of Phase I

Need ID	The Customer's Need			Substantiation of Customer's Need		
	Customer**	Statement of primary customer's decision problem	Desired information set	Customer needs interviews	External factors analysis	Info, tech, analysis
#3	<p><b>Primary:</b></p> <ul style="list-style-type: none"> <li>-Individual consumers (including parents) of primary, secondary, post-secondary education (including life long learning - reooling- programs)</li> </ul> <p><b>Secondary:</b></p> <ul style="list-style-type: none"> <li>-gov't (national, state, local)</li> <li>-educational institutions (P)</li> <li>-corp's and unions representing consumers</li> </ul>	<p><b>Quality of education</b> - What is the relative quality of education being provided by various (competing) educational institutions? Ultimately, the consumer's decision involves the selection of particular institutions at all three levels of education.</p>	<p>Comparative information about various program offerings and the success of those programs in building knowledge, skills, and values, and for adult programs the success of programs in achieving employment.</p>	<p>-SUNY</p> <p>-Personal life needs identified by various interviewees</p>	<p>-Increasing public demands for accountability</p> <p>-Cuts in funding of education places a premium on program effectiveness</p> <p>-Movement towards alternative forms of education</p> <p>-Increasing pace of change leads to a need for frequent retooling</p>	<p>- Shift in power from producers to consumers who now have easy access to enormously more data</p> <p>-emergence of electronic distance education- anytime, anywhere, self-paced</p>
#4	<p><b>Primary:</b></p> <ul style="list-style-type: none"> <li>-Senior mgmt. (P)</li> </ul> <p><b>Secondary:</b></p> <ul style="list-style-type: none"> <li>-Boards of directors</li> <li>-Customers</li> <li>-Suppliers</li> <li>-Investors</li> <li>-Creditors</li> </ul>	<p><b>Quality of internal processes and controls</b> - Are internal processes [i.e., sets of activities that produce results of value to "customers" ] and controls designed and operating effectively in terms of specified objectives regarding customers, suppliers, employees, and other stakeholders? (An overview of various activities/processes that might be the focus of this decision are presented in the COSO activity model -Exhibit 2 - attached.) Ultimately, management's decision is whether to make significant changes in processes (reengineer) and/or controls, or possibly to outsource the process.</p>	<p>Information about the design and operating performance characteristics of key internal processes (e.g., cost, quality, service, cycle time, customer satisfaction, percent of on-time deliveries, etc.) and related comparative (benchmark) data reflecting best practices.</p>	<p>-Cenith</p> <p>-Northwest Bank</p> <p>-Harris Bank</p> <p>-Ultrak</p> <p>-Alcoa</p> <p>-Eastman Kodak</p> <p>-U.S. Home Corp.</p> <p>-CBI Industries</p>	<p>-Competition intensifying</p> <p>-Increasing pace of change (significant reductions in product and service life cycles)</p>	<p>-Shift in power from producers to consumers who now have easy access to enormously more data</p> <p>-Need for integrity of processing and controls</p> <p>-User needs for a much broader range of information for decision-making, including operational information</p>

Table 5 - Cont.

**Identified Customer Needs  
Triangulation of Findings of Phase I**

Need ID	The Customer's Need			Substantiation of Customer's Need	
	Statement of primary customer's decision problem	Desired information set	Customer needs interviews	External factors analysis	Info. tech. analysis
#5	<p><b>Customer**</b></p> <p><b>Primary:</b> -U.S. Gov't (P)</p> <p><b>Outcomes of gov't programs - Ar:</b> individual government programs effective in achieving desired outcomes?</p>	<p>Information/measurements about program costs (including aggregations across agencies related to a particular program) and related impacts/outcomes</p>	<p>-GAO -OMB</p>	<p>-Government Performance and Resp. Act (1997 budget process) --Increasing public demands for accountability in gov't programs</p>	
#6	<p><b>Primary:</b> -Individual consumers of products/services <b>Secondary:</b> -Producers of the products/services</p> <p><b>Product/service, quality</b> - What is the relative quality of a product/service being provided by various (competing) producers? Ultimately, the consumer's decision involves the selection of a particular product/service from among a range of possibilities.</p>	<p>Comparative information about various dimensions of quality (reliability, durability, serviceability, operating performance characteristics, esthetics, etc.)</p>	<p>-Personal life needs identified by various interviewees</p>	<p>-Increasing public demands for accountability -Aging of the population: more emphasis on frugality, thriftiness, leading to more comparison shopping</p>	<p>-Shift in power from producers to consumers who now have easy access to enormously more data</p>

Other primary customer decision problems that have surfaced in customer needs interviews but have not yet analysed include the following:

7. Senior management
  - quality of **supplier** processes/products
8. Various levels of management
  - quality of **lower level management**, e.g., BofD==>senior mgmt.; senior mgmt. ==> lower level mgmt.
9. Senior management
  - quality/reliability of potential or engaged **outsorce**
10. Boards of directors
  - quality of company's **strategic planning processes**
11. Senior management
  - progress/outcomes of **alliances**

## **“First-cut” Business Plan for Non-financial Performance Measures - Health Care**

Presently, the health care industry accounts for one-seventh of the US economy; total expenditures exceed one trillion dollars per year. The industry is in a state of transition. In the past, a large portion of individuals' health services were provided through fee-for-service arrangements involving employer-paid health insurance companies or government-sponsored programs (Medicare and Medicaid). Presently, a dramatic shift towards managed care networks is taking place. In this new “model,” networks negotiate on behalf of consumers with health care providers to establish cost and terms of coverage. Since “cost” (i.e., revenue to the health care provider) becomes fixed in advance, the incentive for health care providers becomes one of reducing their service expenses, which may lead to reductions in quality of service.

### **Assurance Service Definition**

CPAs would report on a set (yet to be established - see below) of “quality measures” deemed to be important to consumers of health care services. Measures might include global outcomes, such as mortality statistics, length of stay, patient satisfaction scores, and specific outcomes related to specific diseases (see further below). The health care provider might accumulate and present the data on which the CPA reports (as in current audits and attestation services). Alternatively, the CPA might accumulate relevant data on an entity's performance and report directly.

### **Who Pays**

Although CPAs might be paid by individual consumers, it is more likely that the health care provider would pay for assurance services. Since an obvious conflict of interest arises when providers make claims about the quality of their services, users may demand that providers obtain outside assurance with respect to those claims. Even if not forced to offer outside assurance, providers may find it in their best interests to obtain assurance on their “quality of care” reports because it gives them a competitive advantage in the market place.

### **Market Size**

SCAS is in the process of developing estimates of the revenue potential for assurance services in this market.

### **Measurement Standards**

Measurement standards for the quality of health care are being developed by various organizations. For example, a group of major purchasers of health services recently formed an alliance to evaluate the quality of services provided by health-maintenance organizations (HMOs). Participants include the Health Care Financing Administration, which oversees Medicare and Medicaid, the Federal Employees Health Benefits Plan, the California Public Employees Retirement System, and several large private corporations. Altogether, the alliance represents 80 million Americans. The participants have formed an organization called the Foundation for Accountability that will develop a new generation of measures for evaluating the performance of health plans. The new measures will move away from existing input or process measures (e.g., frequency of emergency room visits, mammography-screening rates) and towards outcome measures that will track the impact of a disease on a person's productivity and quality of life. In short, the new measures will attempt to identify whether HMO services are having a positive impact on the health of people. The first few medical conditions for which outcome measures will be developed include breast cancer, asthma, diabetes, cardiovascular disease, low-back pain, and depression.

The National Committee on Quality Assurance has also developed some rudimentary criteria for measuring the quality of care provided by HMOs. This committee reviews the data provided by HMOs through location visits and examination of patient records.

### **Market Permission and Market Access**

CPAs would appear to face serious permission problems. On the positive side, CPAs may be recognized as having integrity and objectivity as well as being competent in testing and reporting results. On the negative side, CPAs will certainly be viewed as lacking subject matter expertise. As the above discussion of measurement standards indicates, performance measures in health care are beginning to focus on specific diseases and will attempt to measure a health care provider's impact in treating those diseases.

CPAs might attack the "permission" problem and gain access to the market by: i) leveraging their present expertise in the health care consulting area; ii) getting involved in the health care performance standard-setting process and thereby become recognized as a "player" in this arena; iii) outright hiring of MDs to work on health care assurance engagements; and iv) forming alliances with health care entities that would bring the necessary subject matter expertise to the assurance function. Another entry point for individual CPA firms might be based on current audit services and other services presently provided to hospitals and other health care entities

### **Competition**

Other players besides the Foundation for Accountability and The National Committee on Quality Assurance (see above) have recognized this market and are moving quickly to fill demand. The Joint Commission for Accreditation of Health Care Organizations, which was established by the American Medical Association and various hospital groups, performs a similar function for hospitals and reports on more than 11,000 organizations in a three-year cycle. In some areas, local providers have also emerged. For example, in Cleveland, hospitals have joined together in providing an annual report: *Cleveland Health Quality Choice, the Cleveland Area Hospital Quality Outcome Measurements and Patient Satisfaction Report*. In sum, competition appears to be substantial. However, the range of proposed solutions and the infancy of proposed outcome measurements suggests that the market is fluid and that no organization has yet established a dominant position.

### **Competencies**

CPA competencies in business processes, model building, measurement, analysis, and reporting would be helpful in entering the health care performance market. As indicated above, the primary new requirement would be to add subject matter expertise, either by outright hiring or by forming alliances.

## V - Summary of Paper

SCAS is approximately two-thirds of its way towards completion of its charge. This paper provides brief overviews of several items that represent “work in process” of the committee. Although much work remains, this paper highlights some of the major ideas that are beginning to take shape:

- The future demand for assurance regarding the quality of information used in decision-making appears to be very strong.
- Information technology will provide decision makers with ready access to vast amounts of information (much of it derived from systems of high reliability), which will create major user needs for assurance regarding relevance.
- The current audit is expected to change significantly and, at the same time, will provide the foundation upon which a range of new assurance services will be built.
- The profession needs to put in place a process for the orderly identification and development of new assurance services.
- The health care industry appears to be a very promising arena for the introduction of new assurance services.

## Appendix Assurance vs. Consulting Services

Professional standards define consulting services as:<sup>8</sup>

Professional services that employ the practitioner’s technical skills, education, observations, experiences, and knowledge of the analytical approach and procedures used in a consulting engagement. [Those procedures may involve determining client objectives, fact-finding, definition of problems or opportunities, evaluation of alternatives, formulation of proposed action, communication of results, implementation, and follow-up.]

A comparison of the procedures involved in consulting with the types of assurance shown in the middle column of Table 1, above, indicates considerable potential overlap. Indeed, there are many similarities between consulting and assurance services since both are delivered using similar knowledge and skills. However, the two services may be distinguished as follows:

- **Parties involved** - Consulting services typically involve two parties, the consultant and client. An assurance service involves three parties, the preparer, the user, and the assurer (the preparer and user may be members of the same entity, e.g., top management vs. middle management). Moreover, the need for the assurer arises because of the user’s perception that user and preparer interests are in direct conflict, or are not completely congruent.
- **Engagement focus** - Consulting services focus on outcomes. Assurance services focus on the quality of information (including decision models) used in decision making.
- **Primary output** - A consulting engagement generally leads to a set of recommendations. An assurance engagement results in the assurer providing some level of assurance regarding the quality of information used by the decision maker.

The “universe” of CPA services, involving assurance, consulting, tax and other services may be graphically represented as shown in Figure 3, below. In this figure, the largest rectangle represents the “universe of CPA services.” The left and right circles represent the totality of assurance and consulting services, respectively. The rectangles within the assurance circle explicitly identify currently offered assurance services. The areas of overlap between the assurance and consulting circles, as well as the overlap between the attestation rectangle and the consulting circle represent service possibilities that, if structured one way, represent assurance, and, if structured differently, represent consulting.

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<sup>8</sup> AICPA Professional Standards, CS Section 100.

Figure 3

The Universe of CPA Services

