

PROFESSIONAL SKEPTICISM: STANDARDSETTERS' RESPONSIVENESS TO STAKEHOLDER COMMENT LETTERS

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ABSTRACT

Auditing standards direct auditors to exercise professional skepticism (PS) in all facets of an audit. However, until the 2020 revisions to both US and global auditing standards were issued, there were no clear definitions of or guidance on how PS can be demonstrated and documented. How to exercise PS was left to the individual auditor to decide. Ironically, the same regulatory bodies often criticized and, occasionally, took punitive action against auditors, citing a lack of PS. To close this expectation gap, both the International Ethics Standards Board for Accountants (IESBA) and the American Institute of Certified Public Accountants (AICPA) issued proposals to define, demonstrate, and appropriately apply PS. This paper provides an overview of both proposals, analyzes comment letters submitted by constituents at the exposure draft stage of the due process, and describes how and to what extent constituent input impacted the final standards issued in 2020. The results suggest that constituents generally supported both proposals. While the AICPA and IESBA incorporated some of the constituent input in their final standards, several major stakeholder recommendations were ignored. Stakeholder feedback overwhelmingly suggests that added guidance for the proper application of PS is needed, along with education and training programs.

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KEYWORDS: IESBA, AICPA, Professional Skepticism, Audit Engagements, Audit Standards

INTRODUCTION

For more than five decades, exercising due professional care has been one of the foundations of performing financial statement audits and issuing audit reports. Both US and international auditing standards state that to exercise due professional care an auditor must use professional judgement (PJ) and professional skepticism (PS). However, prior to the issuance of the latest revisions of US auditing standards (AICPA, 2020) and the international ethics code (IESBA, 2021), available guidance merely stated that auditors should exercise professional skepticism during the audit. Thus, both the US and global auditing codes lacked clear and consistent practical application guidance of both PJ and PS (Omer, Sharp, and Wang, 2018). In addition, according to the Public Company Accounting Oversight Board (PCAOB), applying PS appropriately is ultimately the responsibility of each individual auditor (Gissel, 2018). Thus, public and private US regulators and global regulatory bodies generally left the 'how to' exercise PJ and PS up to the auditors. However, the same regulatory bodies routinely criticized auditors for their lack of PS at seemingly every turn, without providing specific guidance concerning regulatory expectations and without providing examples of how auditors can demonstrate that they exercised PJ and PS. To compound

the problem, alleged failure to properly exercise PS has led to numerous litigation actions against auditors, including enforcement actions by the Securities and Exchange Commission (SEC) and the PCAOB (Brazel, 2019).

To eliminate this gap between existing guidance for exercising PJ and PS during an audit and the expectations of the regulatory bodies, both the AICPA (2019, June) and the IESBA (2018) issued exposure drafts to revise the existing codes. Both documents received many comment letters. While there was widespread stakeholder support for both proposals, some recommended changes in the proposed standards while others opposed them. After considering the comments, both the AICPA (2020) and IESBA (2021) issued their final standards. In the remainder of this paper, the main focus of the study is PS because it is a critical component of PJ in every facet of each audit engagement, and lack of PS has been the basis of many legal and negative peer review actions.

This paper first examines the comment letters submitted in response to the exposure drafts issued by the AICPA and IESBA. Both proposals posed questions about how individual auditors, auditing firms, financial statement users, and other stakeholders viewed the importance and the appropriate application of PS. The paper provides insight into the due process of standard setting by analyzing how the comment letters impacted the final standards as compared to what was proposed concerning PS. While the analysis of the comment letters indicates that a majority of participants agree there should be a regulated set of standards for applying PS during an audit, several respondents recommended specific revisions, additions, and deletions to the exposure drafts. Thus, it is warranted to identify any changes made to the proposals prior to the issuance of the final standards. Finally, the paper addresses the perceived need for improvement in and standardization of professional guidelines for PS and proposes a path forward for training and education programs that aim to enhance the exercise of PS by public and private accountants.

LITERATURE REVIEW

The AICPA's Auditing Standards Board (ASB) issues Statements of Auditing Standards (SAS) that are used by auditors to conduct all audits except the audits of public companies. Public companies are audited using the standards set forth by the PCAOB. Currently, AICPA auditing standards (hereafter referred to as the Code) sections AU-C 200 (pars. .A22-.A31) and 230 (pars. .07-.13) state that PS requires the auditor to question evidence, be alert to documentation and transactions that may lead to misstatements or be used to commit fraud, and always critically assess audit evidence (AICPA, 2011). In addition, the ASB (AICPA, 2019, May) issued SAS 134 (Code sections 700-706) to revise the auditor's report effective December 15, 2021. One of the major changes is a new requirement that the audit report state that PJ was exercised and PS was maintained throughout the audit.

According to the PCAOB (2021, section 1015), PS reflects a questioning mindset that critically assesses audit evidence. While both sets of standards have several paragraphs of discussion, neither supplies a scale of PS to be used in various audit areas and there are no specific examples of actions that can be taken when auditing different financial statement accounts. In addition, there is scant discussion of how exercising PS enhances the auditors' ability to meet their obligations under the fundamental principles of auditing and ethics requirements.

The IESBA issues ethics standards that govern the conduct of global accountants who are in public or private practice. IESBA (2021) defines PS as the attitude of professional auditors who are always questioning evidence obtained, critically assessing audit evidence, and making decisions based on their expertise. This document clearly states that skepticism does not mean disbelieving, but looking for proof before being able to trust a statement.

Thus, current versions of the standards issued by regulators in the US and world-wide include definitions of PS that are vague and include references to an attitude of a questioning mindset, critically assessing evidence, and being alert to inconsistencies that may indicate the existence of misstatements and fraud. While the AICPA goes into slightly more detail discussing conditions that may indicate fraud, the IESBA focuses on the idea that to exercise PS, audit expertise should be used to ensure that all doubts and questions are resolved when critically assessing audit evidence (Yazid and Suryanto, 2017). Given the difficulties surrounding the proper application of PS, numerous research studies have examined various aspects of PS, as we review below.

Literature on Professional Skepticism

Extant academic research has employed surveys, simulations, cognitive constructs, and descriptive approaches to examine various aspects of PS. Boyle and Carpenter (2015) define PS as an attitude that includes a questioning mind and a critical assessment of audit evidence. While not novel, the main contribution of the study is the description of various methods, actions, and evidence analysis steps that auditors can undertake and document when exercising PS. The authors conclude that auditors must recognize that material misstatement can in fact exist, regardless of their prior experiences with and assessment of management's integrity.

In a survey study, Gissel (2018) aimed to gain insights on participants' perceptions of PS and the value of training practices they undertook. Survey participants spanned the spectrum of practicing auditors, including firm partners, audit managers of all ranks, and staff auditors. Gissel (2018) aimed to learn whether audit professionals viewed PS as a well-defined concept or as a subject that is left up to interpretation. After much analysis, she concluded that the majority (70%) of participants perceived PS to be a subjective concept and open to individual or regulatory interpretation.

In a simulation study, Eutsler, Norris, and Trompeter (2018) investigated how social relationships and interactions between auditors and management impact the auditor's exercise of PS. The authors found that auditors are more or less likely to recommend intensive follow-up when undertaking audit procedures depending on their level of social interactions, with a low level of social interactions leading to more intensive follow-up and a high-level of social interactions leading to less intensive follow-up. While anecdotal evidence existed that such social interactions could be a threat, Eutsler et al. (2018) was the first academic study to demonstrate that social relationships between client management and the auditor can be a threat to PS.

Dimitrova and Sorova (2016) examined the critical elements of attributes, mindset, and actions that underlie PS. The auditor must have the knowledge and skills to conduct the audit, gather persuasive evidence because a skeptic does not assume honesty or the lack thereof on the part of management, and objectively evaluate the evidential matter for competency and sufficiency to arrive at an audit opinion. Thus, an auditor should have a questioning mind that looks at evidence without judgment (avoiding biases that may be present), have interpersonal understanding and self-confidence to interpret and evaluate the evidence, and self-determination to judge the adequacy of the evidence to issue an opinion. Hence, the appropriate level of PS to be exercised depends on the risk of the area under audit, resulting in a PS continuum.

Glover and Prawitt (2014) published a skepticism continuum map with PS being defined as an attitude that includes a questioning mind. The continuum ranges from complete trust which would call for less audit evidence and documentation to neutral, presumptive doubt, and complete doubt which would necessitate the most extensive audit evidence and documentation. In another study, Nolder and Kadous (2018) aimed to analyze PS using a dual conceptualization approach. This approach uses cognitive processing employing different mindsets and personal attitudes to determine their impact on the subject's perception of PS. The authors conclude that using this approach would help improve standard setting and audit quality.

Brazel (2019) summarizes various regulatory and legal actions against auditors world-wide to demonstrate that the failure of auditors to exercise an appropriate level of PS is a major global issue. However, he also explains that the more PS is exercised, progressively higher levels of audit evidence are required to justify opinions. Therefore, without a scale provided by regulators depicting what degree of PS is acceptable in different audit areas, some auditors overcompensate using unwarranted efforts and time. Ironically, this is the same conclusion Nelson (2009) reached more than a decade ago when he noted that application of PS is evident when auditors reflect increased risk assessments in their judgments, given the information that is available. The author concluded that auditors who exhibit high levels of PS in all areas of the audit need more hard evidence in order to accept an assertion, which then can lead to auditors unnecessarily exceeding budgeted hours.

In an opinion piece published for an online accounting newsletter, Lord (2018) states that the future of auditing will mainly depend on how auditors exercise PS and whether they can convince regulators and users of financial statements that their opinions are based on persuasive evidence. The author points out that PS is one of the main pillars of the auditing profession that must continuously evolve and be maintained to support the audit of the future. She concludes by suggesting example steps auditors can take, such as use of probing questions, critical assessment of evidence, and increased attention to inconsistencies.

The review of both professional and academic literature indicates that while US and world regulators criticize auditors for not exercising appropriate PS, auditing standards lack a clear, consistent definition (Nelson, 2009; Hurtt, Brown-Liburd, Earley, and Krishnamoorthy, 2013), leaving application of PS open to interpretation (Brazel, 2019; Glover and Prawitt, 2014). If individual auditors view PS as open to interpretation and subjective, auditors may believe they are appropriately applying PS based on their individual circumstances. However, as Gissel (2018) suggests, if regulators have interpretations that differ from those used by individual auditors when exercising PS, the consequences of regulatory evaluation of audit quality will be negative and occasionally punitive. Below we review literature that has explored the education and training of accountants on PS.

Literature on PS Education and Training

Findings from extant research suggests that many accounting firms have some type of PS training. For example, in Gissel (2018), thirty-two firms were surveyed, ranging from Big-4 to small regional accounting firms, on their perception of and training for PS. Twenty-five of the thirty-two firms had training for PS. However, most of the training consisted of mentoring from senior professionals and was done on an annual basis, with very few firms conducting ongoing training. In addition, individual auditors surveyed universally stated that they believe PS is subjective and they would like to have scalar guidance when applying PS in different risk and account areas.

Hayes (2016) performed a study showing the impact of increasing instructional content of PS on students. Using a sample of senior-level undergraduate auditing students across three different sections, Hayes had participants first self-assess their own level of skepticism and then complete a management fraud risk assessment for a hypothetical scenario. However, one of these sections had additional PS instruction prior to participating in the study. These students were shown concrete examples that demonstrated the importance of PS and the consequences of not having PS. The results showed that the section with added PS instruction had significant improvement in skepticism and in the accuracy of the assessed level of management fraud risk.

Glover and Prawitt (2014) promote the idea of training accountants' framing where different perspectives are visible using various window frames. By understanding, for example, how journal entries look like from different perspectives, accountants can better question their own and others' conclusions and effectively approach management explanations with a questioning mind. A follow-up study by Nolder and

Kadous (2018) examined different components of PS and found that PS is mainly comprised of an individual's mindset and attitude. The authors suggest that mindset consists of an individual's cognitive processes, procedures, and judgment criteria used to complete a specific task while attitudes are evaluative responses that include beliefs and feelings that drive an individual's intentions and actions. The authors point out that future research that measures mindset by cognitive processing variables and attitude by evaluative responses associated with a target situation is needed to develop a more complete view of PS and a better understanding of how PS is exercised.

Indeed, professional skepticism is a concept that is inherently determined by the mental processes of an auditor. To better understand how to improve the exercise of PS, Olsen and Gold (2018) proposed the use of cognitive neuroscience research given that cognitive neuroscience has furthered the understanding in other areas that require a mental focus, such as psychology, economics, and consumer research.

Another study explored ways of teaching auditing students and professionals to change the manner in which they process information and the steps of their thought processes (Hurt et al., 2013). According to the authors, law students are less prone than accounting students to be biased toward an advocacy position because law schools emphasize the understanding of both positive and negative precedents, and law students are trained in advocating their position as well as explaining why contrary positions are incorrect. This approach is also used in the instruction of forensic accounting courses. Brazel (2019) proposed that auditors should be educated and trained like forensic accountants and lawyers, where viewing the situation from both sides results in more skeptical and less biased judgements. Hurt et al. (2013) also proposed a potential link between moral reasoning and behavior and skeptical judgment. In particular, auditors with high moral development are more sensitive to information about the client's competence and integrity while obtaining evidence. Furthermore, the environmental and social conditions in which auditors interact with clients can negatively affect the level of PS they exercise (Eutsler, Norris, and Trompeter, 2018).

Finally, Lee, Welker, and Wang (2013) examined the possible inclusion of interview process interpretations in the PS training of accountants. They observed how auditors perceive deception while interviewing other individuals, which can be comparable to performing inquiries of an audit client. The study found that auditors who had more training in risk assessment and in identifying the behavioral traits of deception exercised more appropriate presumptive doubt in an interview/inquiry situation.

Both the AICPA (2019, June) and the IESBA (2018) addressed the perceived need to enhance the exercise of PS in audits and issued exposure drafts for proposed standards that achieve this goal. In the remainder of this paper, we analyze comment letters filed in response to both proposals, providing insight into the extent to which stakeholders agreed, partly agreed conditional on certain changes (i.e., recommended revisions, deletions, and/or additions to the proposals), or disagreed with the proposals. Next, we analyze the impact of feedback from comment letters on the final standards issued, and we discuss a proposed path forward including the implications of the final standards issued for the application of PS in practice and the need for further guidance and training. We close with concluding comments.

DATA AND METHODOLOGY

International Ethics Standards Board for Accountants (IESBA) Data

In May 2018, the IESBA released the consultation paper *Professional Skepticism – Meeting Public Expectations*, which sought input on the IESBA's consideration of the long-term PS issues. The consultation paper explored three distinct topics concerning PS: 1) behavioral characteristics underlying PS; 2) whether such characteristics should be followed by all accountants in public and private practice; and 3) whether the Board should take further actions, within or beyond the Code, to deal with the behaviors that enable professional accountants to execute suitable levels of PS. The IESBA gave individuals and

organizations the ability to supply feedback on the consultation paper from May 2018 through August 15, 2018 (IESBA, 2018). Sixty-two comment letters were filed in response to the questions posed in the consultation paper. Of the ten questions posed, we analyzed the nine listed in Table 1 (one question, question 9, asked for open-ended answers that could not be quantified).

The IESBA received a total of 62 comment letters. A review of the 62 comment letters revealed that 9 comment letters did not respond in the format requested by the IESBA and could not be used in our analysis; hence, our analysis is based on 53 usable comment letters. Of the 53 comment letters in our sample, 32 were professional accounting societies or organizations, consisting of 4 that were based in the US and 28 that were based in other countries. In addition, 10 accounting firms responded, including all Big-4 accounting firms and others, with 3 firms being based in the US and 7 in other countries. Other respondents included 6 governmental organizations, 3 of which are based in the US, and 5 academic/other individuals, 2 of whom are based in the US. Besides the US, 19 other countries are represented in the sample, including Canada, Argentina, England, Belgium, Germany, Denmark, Ethiopia, Nigeria, Ghana, Zimbabwe, Uganda, South Africa, Iran, Pakistan, Australia, New Zealand, Japan, Malaysia, and Singapore.

Table 1: IESBA Questions Analyzed

Question 1: Do you agree with the premise that a key factor affecting public trust in the profession is whether information with which a professional accountant is associated can be relied upon for its intended use?
Question 2: Do you agree with the behavior associated with public expectations of professional accountants? Are there aspects that should be included or excluded from the summary?
Question 3: Do you agree that the mindset and behavior described in paragraph 10 should be expected of all professional accountants?
Question 4: Do you believe the fundamental principles in the Code and related application material are sufficient to support the behaviors associated with the exercise of appropriate "professional skepticism?"
Question 5: Do you believe professional skepticism, as defined in International Standards on Auditing, would be the appropriate term to use?
Question 6: (a) Do you believe that the Code should retain/use the term "professional skepticism" but develop a new definition? (b) If so, do you support a new definition along the lines set out in paragraph 19? (c) If you do not support a definition along the lines described, could you please provide an alternative definition?
Question 7: (a) Would you support an alternative term to 'professional skepticism,' such as 'critical thinking,' 'critical analysis' or 'diligent mindset?' (b) If not, what other term(s), if any, would you suggest which focusses on the mindset and behaviors to be exercised by all professional accountants?
Question 8: Should the IESBA develop additional material, whether in the Code or otherwise, to highlight the importance of exercising the behavior and relevant professional skills as described?
Question 10: Should the Code include the application or other material to increase awareness of biases, pressure and other impediments to approaching professional activities with an impartial and diligent mindset and exercising appropriate professional skepticism in the circumstances?

This table reflects a verbatim reproduction of the questions asked to stakeholders for feedback in the IESBA consultation paper 'Professional Skepticism – Meeting Public Expectations' (IESBA, 2018). Question 9 is omitted because it asked for open-ended answers that could not be quantified for purposes of our analysis.

American Institute of Certified Public Accountants (AICPA) Data

In June 2019, the AICPA's Auditing Standards Board (ASB) released an exposure draft – *Audit Evidence*, which asked for feedback on a proposed SAS, which, if issued, would supersede *SAS No. 122: Clarification and Recodification* (AICPA, 2011). This proposal was the result of the ASB's response to the evolving nature of business and audit services and the perceived need to revise AU-C section 500 (Audit Evidence) (AICPA, 2011). One of the key issues addressed for revision was the application of PS by auditors. The AICPA described PS as being attentive to assertions and documents that are contradicted by other evidential matter obtained or information indicating that the reliability of the audit evidence obtained cannot be

trusted. The exposure draft aimed to resolve issues related to how auditors can more clearly demonstrate PS, how auditors can better describe the basis for their professional judgments, and how auditors' mindset affects the nature, timing, and extent of procedures performed as well as the critical evaluation of audit evidence. Underlying the proposal was a concern about the large number of audit quality inspection findings that assert lack of PS on the part of auditors. Finally, the ASB intended to clearly articulate PS in the auditing standards. Individuals and organizations were asked to submit feedback on the exposure draft by September 2019 (AICPA, 2019, June).

The AICPA received a total of 41 comment letters. Of the 41 comment letters submitted, 38 were usable for purposes of this study. Three comment letters did not respond in the format requested by the ASB and were therefore excluded from our sample. Respondents in our sample consist of 15 accounting firms (including all Big-4 firms and others), 9 professional accounting organizations, 5 governmental organizations, and 9 academic/other individual. While the exposure draft posed 15 questions about audit evidence, our analysis focuses on questions 7 and 8, which are specifically related to PS and listed in Table 2.

Table 2: AICPA Questions Analyzed

Question 7: Do you agree with the approach taken by the ASB in addressing the topic of professional skepticism?
Question 8: If the guidance in the proposed SAS is implemented, would the application of professional skepticism be enhanced and more clearly understood in evaluating whether sufficient appropriate audit evidence has been obtained?

This table reflects a verbatim reproduction of the two questions related to professional skepticism asked to stakeholders for feedback in the AICPA exposure draft 'Audit Evidence' (AICPA, 2019, June).

The feedback to the IESBA's consultation paper and the AICPA's exposure draft is described and summarized in the next section. We categorized stakeholder responses to posed questions at three levels based on the degree of agreement with the posed question: 1) those agreeing with the question (Agree), 2) those partially agreeing with the question conditional on certain revisions (Partially Agree), and 3) those not agreeing with the question (Disagree).

Impact of Stakeholder Comments on Final Standards Issued

We compare and contrast each proposal to the final standards issued by the IESBA (2021) and the AICPA (2020) and use the analysis of the degree of stakeholder agreement with the proposals to provide insight into the responsiveness of the standard-setting process to stakeholder input. Specifically, we use the recommendations for proposal revisions from the comment letters to see whether standard setters amended their proposals and included stakeholder suggestions in the final standards they issued. The aim is to understand the efficacy of constituent comments in shaping the standards that govern PS and describe the state of general acceptance of audit standards. General acceptance facilitates the conduct of high quality audits which form the foundation of financial market efficiency by giving financial market participants the confidence they need to trust the information based on which they make investment decisions.

RESULTS

The nature of stakeholder comments received by the IESBA and AICPA in response to each of the questions posed in the respective proposals are discussed below. We describe the actions taken by the IESBA and AICPA in response to stakeholder suggestions and recommendations by comparing the final standards (IESBA, 2021; AICPA, 2020) to the original proposals (IESBA, 2018; AICPA, 2019, June).

IESBA Responsiveness to Stakeholder Feedback

Table 3 tabulates stakeholder responses to the posed IESBA questions by level of agreement (agreed fully versus partially agreed versus disagreed) and stakeholder type (professional accounting organization, accounting firm, governmental organization, or academic/other individual). Respondents who did not respond to a particular question are reflected in the ‘N/A’ column in the table. Note that of the 53 respondents, only one respondent (a professional accounting organization) consistently answered all nine questions in the same response category, which was ‘Agree.’ All other IESBA respondents gave varied answers across the nine questions. As can be gleaned from Table 3, except for questions 5, 6, and 7, a majority of the 53 respondents fully agreed with the posed questions and this result holds true for each stakeholder type. On the other hand, respondents more frequently disagreed with questions 5, 6, and 7. Below, we discuss results for each question.

Table 3: Extent of Stakeholder Agreement with IESBA Consultation Paper

Question	Agree					Partially Agree					Disagree					N/A				
	P	F	G	A	All	P	F	G	A	All	P	F	G	A	All	P	F	G	A	All
Question 1	27	9	4	4	44 (83%)	2	0	0	0	2 (4%)	3	1	2	1	7 (13%)	0	0	0	0	0 (0%)
Question 2	21	9	4	2	36 (68%)	1	0	0	0	1 (2%)	7	1	2	3	13 (25%)	3	0	0	0	3 (6%)
Question 3	28	9	5	1	43 (81%)	2	1	1	2	6 (11%)	1	0	0	2	3 (6%)	1	0	0	0	1 (2%)
Question 4	14	9	4	2	29 (55%)	4	0	1	1	6 (11%)	14	1	1	2	18 (34%)	0	0	0	0	0 (0%)
Question 5	6	2	2	2	12 (23%)	2	0	2	1	5 (9%)	24	8	2	2	36 (68%)	0	0	0	0	0 (0%)
Question 6	18	4	1	3	26 (49%)	1	0	1	0	2 (4%)	11	6	4	2	23 (43%)	2	0	0	0	2 (4%)
Question 7	10	4	2	2	18 (34%)	0	0	0	0	0 (0%)	20	6	4	3	33 (62%)	2	0	0	0	2 (4%)
Question 8	26	8	6	5	45 (85%)	0	0	0	0	0 (0%)	3	2	0	0	5 (9%)	3	0	0	0	3 (6%)
Question 10	25	9	6	5	44 (83%)	0	0	0	0	0 (0%)	4	1	0	1	6 (11%)	3	0	0	0	3 (6%)

This table tabulates a breakdown of the 53 comment letters in our sample that agree, partially agree, or disagree with each of the nine questions analyzed from the consultation paper ‘Professional Skepticism – Meeting Public Expectations’ (IESBA, 2018). Counts are reported in total and by category of respondent of either Professional Accounting Organization (denoted P; n=32), Accounting Firm (denoted F; n=10), Governmental Organization (denoted G; n=6), or Academic/Other Individual (denoted A; n=5). The category ‘Partially Agree’ reflects instances where the respondent agreed with the question but conditional on certain revisions. N/A reflects respondents who did not respond to a particular question. See Table 1 for details of the nine questions analyzed from the exposure draft (question 9 from the exposure draft was excluded from the analysis because it asked for open-ended answers that could not be quantified).

Among those responding to question 1, 83% agreed that public trust in the profession is affected by the degree of reliability of the financial information with which accountants are associated. While this question does not directly address PS, a certain degree of PS on the part of accountants is necessary for the information with which they are associated to be reliable. Four percent of respondents only partially agreed and 13% of respondents disagreed with question 1. The two professional accounting organizations that partially agreed recommended a separate statement for business accountants. The IESBA positively addressed this issue in a later question. The respondents that disagreed had objections concerning the term “associated with” when referencing the information professional accountants audit. Since the term is not defined in the Code, its interpretation is unclear. These respondents believe that since the information provided by accounting professionals widely varies, how much association a professional should have with

that information for it to be able to be relied upon by an investor is impossible to determine. The IESBA responded positively to this objection and this term does not appear in the final standard issued.

For question 2, 68% of the respondents agreed that the public expects accountants to behave in the manner described in the proposal. Having an inquiring mind, exercising professional judgment, and using the help of informed third parties ensures that accountants follow the principles of integrity, objectivity, competence and due care, confidentiality, and professional behavior required during the conduct of an audit. In addition, having an inquiring mind requires that accountants act with PS, which includes a critical assessment of evidence. Finally, exercising PJ and PS ensures that accountants are aware of threats to their compliance with the principles to which they must adhere and the behaviors they have to display. Those threats include self-interest, advocacy, familiarity, and intimidation. One professional accounting organization only partially agreed and suggested addition of the redundancy threat whereby the auditor may collect excessive evidence that does not enhance the quality of the audit. The IESBA did not agree. The 13 respondents who disagreed with the question objected to the undue reliance on PS and the inclusion of detailed discussions of biases and threats in the fundamental principles of the standard. Despite such objections, the IESBA's final standard includes these discussions in the fundamental principles (section 110) and the conceptual framework (section 120) (IESBA, 2021).

For question 3, responding individuals and organizations were 81% in agreement that the mindset and behaviors described in the proposal should be expected of all accounting professionals. The six respondents who only partially agreed recommended that the IESBA include specific examples in the discussions concerning PS, PJ, and various biases that only apply to business accountants. One of the arguments made by the three respondents who disagreed was that the term mindset is not appropriate and discussion concerning fundamental principles such as competence, integrity, and objectivity should be sufficient. In addition, those three respondents stated that the IESBA should present a new approach to describe the behavior expected of all professional accountants. Despite these stakeholder suggestions, the IESBA final standard does not contain specific examples concerning PS, PJ, and various biases that only apply to business accountants and contains the discussions and terms opposed by the respondents.

For question 4, only 55% of the respondents agreed that the fundamental principles described in the Code along with the available application material related to PS sufficiently support the appropriate exercise of PS in practice. The IESBA wanted to ensure the Code contains adequate material and discussion of the fundamental principles concerning PS and clearly articulates the specific behavior set that should be exercised by accountants. In addition, the IESBA wanted to be certain that accountants understand and adhere to the Code. For the six respondents who only partially agreed and recommended revisions to the proposal, the main area of concern was that the principles are seen through a narrow audit lens whereas a wider lens that addresses both public and private accountants would be more appropriate. The 18 constituents who disagreed were primarily professional accounting organizations that cited the lack of explicit examples of exercising PS in different audit areas, the anxiety of being subjected to legal action, and a lack of different scales and levels of PS to be exercised when auditing various financial statement items. Nonetheless, the final IESBA standard provides neither specific audit examples nor scales and levels of PS to be exercised when auditing specific financial statement accounts. However, IESBA Code section 120.16 A2 specifically discusses how PS and the fundamental principles of auditing are interrelated and how behaving with integrity, objectivity, and professional competence and due care contributes to the exercise of PS (IESBA, 2021). At the same time, the exercise of PS enhances the ability of the accountant to adhere to these fundamental principles.

Question 5 garnered the most disagreement of all the questions. Only 23% of the respondents agreed with question 5 that professional skepticism as defined in the International Standards on Auditing is the appropriate term to use, and another 9% only partially agreed conditional on recommended revisions. The recommended revisions center on the complaint that the proposal is audit-centric and propose discussions

that would address the behavior of private accountants or the organizational environment of the audit firms and their clients. The 68% of the respondents who disagreed maintained that: 1) it is impossible to cure the audit-centricity of the proposal; 2) additional definitions and discussions of PS are required for non-attestation engagements; and 3) using the proposed definition of PS across other engagement areas of practice would risk confusion for users and professionals alike. In response to those recommending revisions, the IESBA added section 200.5 A3 to the final standard which addresses accountants in business and includes detailed discussions of how they can promote and implement an ethics-based culture in business (IESBA, 2021). To address the concerns of those who disagreed, the IESBA included a requirement that professional business accountants present information that does not mislead or influence a desired behavior, exercise professional judgment to present all facts accurately, refrain from omitting information to support a predetermined point of view, avoid undue influence of individuals or technology, and be aware of risks of personal bias (Code Section R220.4, IESBA, 2021). It is noteworthy that the glossary of the Code does not include a definition of PS. Thus, the standards communicate behaviors and characteristics underlying PS to professional accountants solely through the discussions in the main Code sections.

For a related question, question 6, stakeholders were only 49% in agreement that the Code should retain/use the term PS but develop a new definition. The two who only partially agreed conditional on recommended changes were concerned that the new definition may not apply to non-attest engagements. The 43% who disagreed universally stated that a new definition should have more clarity and be expanded. In the final standard, the IESBA does not include a definition of PS and instead relies on extensive discussions that illustrate how PS enhances adherence to fundamental principles of auditing and support the exercise of PJ and due care during the conduct of an audit. Finally, additional discussions illustrate how PS supports the conduct of business accountants under the Code (sections 200 and 220, IESBA, 2021).

In question 7, the IESBA asked stakeholders if they would support an alternative term to PS, such as, critical thinking, critical analysis, or diligent mindset. Of the 53 respondents, 34% agreed that they would support an alternative term, while 62% disagreed and would like the term PS to remain. The respondents who agreed with changing the term PS stated that a new term would allow applicability across all different circumstances and not just to audit and assurance engagements. They also made it clear that an alternative term would strengthen the definition of PS and better describe what is expected of all accounting professionals. However, most respondents felt that the fundamental principles described in the Code are sufficient to support behaviors associated with exercising appropriate PS.

Question 8 asked stakeholders whether the IESBA should develop added guidance to emphasize the importance of applying PS. This question received the most agreement among respondents, with 85% agreeing that additional materials should be developed. It is evident that the respondents do not feel that the PS discussion included in the Code clearly describes what behaviors constitute appropriate professional skepticism. Most respondents asked the IESBA to provide case studies that give examples of exercising appropriate PS, materials that are readily implementable, and short videos that would help in understanding the exercise of PS. Additionally, respondents requested some hypothetical examples which illustrate how cases can be handled in regards to exercising PS in such areas as loan loss allowance determination, impaired inventory and intangibles, and fair values of financial instruments. While the final standard does not include specific examples, the IESBA meeting agendas indicate that developing additional materials concerning PS is under consideration.

The last question asked whether the Code should include application or other material to increase awareness of biases, pressures, and other impediments to approaching professional activities with an impartial and diligent mindset and exercising appropriate PS in the circumstances. Among those who responded, 83% agreed that the Code should include discussions that address personal and organizational biases. The 11% who disagreed stated that the psychological concepts should not be included in an accounting Code and one

of those respondents felt that the term PS should not apply outside the context of providing assurance services. The IESBA agreed with the majority and included extensive discussions of four threats to compliance with fundamental principles (Code Section 120.6 A3) and eight threats and biases that may exist when exercising PJ and PS (Code Section 120. 12 A2) (IESBA, 2021).

The process that started with the IESBA's consultation paper concerning PS culminated in major revisions to the Code that improve accountants' understanding of PS and how to appropriately apply it. The Code requires that accountants exercise PS by approaching a task with a diligent and impartial mindset and applying this mindset along with professional expertise to properly evaluate information and perform duties. Further, the Code requires that all professional accountants apply these concepts in discharging their responsibilities. While the IESBA considered changing the term PS, the revised Code retains the term and describes how the fundamental principles are associated with the exercise of appropriate PS. Constituent reaction to questions 5, 6, and 7 clearly indicates that while the term PS is well regarded, the definition of PS does not have general appeal. One of the main objections is that the definition, underlying characteristics, and application of PS as described in the Code is assurance-centric. The IESBA responded to these concerns by including behaviors and characteristics in the Code that would apply in all circumstances across accounting practice. Overall, a large majority of stakeholders feel that there is an overwhelming need to provide additional material to illustrate how to appropriately exercise PS and PJ in various settings and how to train professionals about biases that impede the proper exercise of PS.

AICPA Responsiveness to Stakeholder Feedback

In the US, the professional ethics codes for accountants practicing in public and private sectors are issued by different organizations. While the AICPA audit code may inform the behavior of business accountants, it does not apply to them. First, the AICPA institutionalized the use and application of PS in financial statement audits by revising the auditor's report (Code sections 700-706, AICPA, 2019, May). Under these revisions that will become effective for years ended December 15, 2021, the audit report must state that the auditor exercised PJ and maintained PS throughout the audit. Next, the AICPA issued a proposal to revise how audit evidence is obtained and assessed to ensure sufficient and appropriate evidence exists to render an audit opinion (AICPA, 2019, June). Contained in the exposure draft were extensive revisions to existing Code sections 500-585, including those concerning the use of due professional care and exercise of PJ and PS during audits. The discussion below describes how those submitting constituent input responded to the two exposure draft questions concerning proposed revisions to PS.

The proposal interweaved the concepts surrounding PS throughout the exposure draft released for comment. This was accomplished by including additional guidance about the auditor's evaluation of whether sufficient appropriate audit evidence has been obtained and demonstrating the application of PS when obtaining and evaluating sufficient appropriate audit evidence. In addition, there was discussion of four biases that may impede the exercise of PS.

Question 7 asked whether the stakeholders agreed with the approach taken by the ASB in addressing the topic of PS. As reported in Table 4 below, of the 38 respondents, 76% agreed with the approach taken by the ASB, 5% partially agreed, 5% disagreed, and 13% did not respond to this question. Question 8 follows up question 7 by asking stakeholders whether implementation of the proposal would improve the application of PS and help accountants better understand how to exercise PS when evaluating whether sufficient appropriate evidence has been gathered. Only 55% of respondents agreed that implementation of the proposed SAS would provide an enhanced application and clearer understanding of PS. Another 18% partially agreed, while 8% disagreed, and 18% did not respond to this question.

Table 4: Extent of Stakeholder Agreement with AICPA Exposure Draft

Question	Agree				Partially Agree				Disagree				N/A							
	P	F	G	A	All	P	F	G	A	All	P	F	G	A	All					
Question 7	6	11	5	7	29 (76%)	0	1	0	1	2 (5%)	1	0	0	1	2 (5%)	2	3	0	0	5 (13%)
Question 8	6	7	4	4	21 (55%)	0	4	1	2	7 (18%)	1	0	0	2	3 (8%)	2	4	0	1	7 (18%)

This table tabulates a breakdown of the 38 comment letters in our sample that agree, partially agree, or disagree agree with each of the two questions analyzed from the AICPA exposure draft ‘Audit Evidence’ (AICPA, 2019, June). Counts are presented in total and by category of respondent of either Professional Accounting Organization (denoted P; n=9), Accounting Firm (denoted F; n=15), Governmental Organization (denoted G; n=5), or Academic/Other Individual (denoted A; n=9). The category “Partially Agree” reflects instances where the respondent agreed with the question but conditional on certain revisions. N/A reflects respondents who did not respond to a particular question. See Table 2 for details of the two questions analyzed from the exposure draft.

Overall, constituent input was positive with most respondents agreeing with the two questions in each of the four respondent categories. In addition, 21 respondents spanning all respondent categories fully agreed with both questions and another 8 respondents fully agreed with at least one of the two questions. This sentiment suggests that the AICPA and ASB did an excellent job in explaining and incorporating PS in the proposed revisions to code section 500 (AICPA, 2019, June). In general, stakeholder comment letters reveal the following:

The proposed statement clearly explains the importance of exercising PS in each of the concepts and principles included in the statement;

There are excellent examples of activities that demonstrate the application of PS in obtaining and assessing audit evidence;

The discussion and examples include how technological advances need to be used when exercising PS;

The proposal makes it clear that the persuasiveness of the evidence, not the quantity, must be emphasized which clearly demonstrates why exercising PS is important;

The proposal clearly describes ways to obtain audit evidence while applying PJ and PS; and

The discussion of management’s biases is important for the exercise of PS.

However, two respondents (one accounting firm and one academic/other individual) only partially agreed to question 7 while seven other respondents spanning most respondent categories (with the exception of the professional accounting organization category) only partially agreed to question 8. Across the two questions, only one respondent, an accounting firm, partially agreed with both questions. Respondents partially agreeing suggested the following recommended revisions to the proposed changes:

The discussions concerning PJ and PS (Code sections 200.A22-.A26 and .A27-.A32) should be reiterated in the final standard for audit evidence (Code sections 500-585) as it is important to showcase this discussion;

The discussion related to auditors’ four biases should either be deleted or removed from section 500 and relocated to section 200. If included, to increase the auditor’s understanding of the four biases listed (availability, anchoring, confirmation, and overconfidence), familiar examples should be included in addition to the definitions provided;

The final standard should include more guidance, examples, and explicit mention of scales or benchmarks on which the auditor's evaluations and exercise of PS must be based;

The evaluation of whether sufficient appropriate evidence is obtained should document the evaluation of the risk of material misstatement, the nature of audit procedures performed in response to this risk, and an analysis whether the evidence obtained corroborates or contradicts management's assertion; and

There should be a requirement that auditors document the extent to which evidence collection was driven by available evidence rather than the most persuasive evidence.

On the other hand, two respondents (one academic/other individual and one professional accounting organization) completely disagreed with both questions and another academic/other individual who had partially agreed with question 7, completely disagreed with question 8. These respondents cited that the discussion of biases and mindsets should not be included in auditing standards (question 7) and that the material in the proposal would require the Code to be completely rewritten so the proposal should be delayed until the AICPA decides to do a complete rewrite (question 8).

In response to recommendations for modifications to the exposure draft and opposing comments, the AICPA made certain revisions to the proposed standard before issuing the final standard (AICPA, 2020). First, the AICPA retained the definition and discussion concerning the four biases but moved it to code section 200 .A27. In addition, the AICPA added a fifth bias (automation bias). Furthermore, the AICPA added to code sections 330, 500, 520, and 540 requirements for documenting the evaluation of misstatement risk, audit procedures performed, and nature of the evidence. Lastly, unlike the IESBA, the AICPA glossary (section 200 .14) includes a definition of PS (questioning mind, alertness to conditions that may indicate misstatement or fraud, and critical assessment of evidence).

However, the AICPA declined to include specific examples of biased behavior and scales of exercising PS in different areas of audits. In addition, there is no detailed discussion of PJ and PS in section 500. Auditors must use the relevant material in section 200 for this purpose. Finally, despite the suggestions from stakeholders, the final standard does not require the auditor to document whether evidence collection was driven by the availability rather than the persuasiveness of evidence.

A PATH FORWARD

People respond to how they are evaluated and rewarded. The application and exercise of PS by professional accountants is ensured when the ethical values that align with the fundamental principles are supported throughout the accountant's organization. Thus, audit firms and private businesses must have an organizational environment and culture that enhance accountants' principles and minimize individual biases. The organization's leaders must promote the importance of, and hold themselves accountable to, a system of quality management they design and implement. These systems must encompass education and training programs, appropriate reward criteria, effective whistleblower policies, processes that are designed to prevent non-compliance with rules and regulations, and clearly stated ethical values. And importantly, these systems must facilitate the appropriate exercise of PS. Nonetheless, to consistently effectuate the proper application of PS in practice, professional standards and supporting materials must be unambiguous in defining PS and establishing how it is properly applied in various circumstances.

Reviewing the proposals, constituent feedback, and the final standards issued, the IESBA and AICPA both clearly emphasize the importance of exercising PS, and they have accomplished much headway in clarifying the concept of PS. Both governing bodies appear to have been responsive to a majority of constituent feedback. However, although the final standards have been issued, much remains to be done to help accountants execute a proper level of PS. In the case of the IESBA standards, we agree with

respondents that the term PS is generally more applicable in an assurance setting and view the changes the IESBA incorporated into the Code to address this concern in a positive light. Because PS results from a cognitive process, we also concur with both standard setters that cognitive biases and other threats to PS should be acknowledged in the standards. On the other hand, constituent calls for PS scales were seemingly ignored within the final standards of both governing bodies. Even though scales such as the Hurtt PS scale (Hurtt, 2010) have been developed, such a scale has not been incorporated into professional standards. In our opinion, the inclusion of agreed-upon PS scales in either the standards or supporting materials would be tremendously helpful in attaining a consistent execution of PS in practice. Additionally, specific examples of how the appropriate application of PS is demonstrated in different audit areas would help practicing auditors. Thus, both the IESBA and the AICPA have further opportunities to revise their respective codes and/or create materials that may include PS scales and real or hypothetical case studies. At the same time, all stakeholders play a role in facilitating the proper execution of PS. In the following paragraphs, we explore other aspects that may assist auditors in their quest to effectively execute PS.

Without a doubt, regulators, educators, and professionals must collaborate to develop applied guidance for PS in different practical scenarios. In public and private organizations, boards of directors and audit committees can influence auditors to exercise PS by supporting the auditors in their pursuit to gather appropriate and sufficient evidence that is persuasive to render an opinion. They may ask probing questions during meetings and not shy away from disagreeing with management. Directors and committee members should be educated in areas of PJ and PS, along with accounting, auditing, technology, and financial practices. All stakeholders must understand that while professionally skeptical actions can be documented, it is difficult to document skeptical thinking until it manifests itself in actions. Currently, one avenue open to accountants to demonstrate the use of PS is to document actions taken, the nature of the critical evidence that led to each action, and the final decisions made to expand, reduce, or leave unchanged the type of evidence needed during the course of the audit. Since professionally skeptical thought processes occur in the mind and are not directly observable, it is important to include in the documentation a description of how the auditor overcame certain biases when evaluating evidence and exercising professional judgment.

Gissel (2018) provided insights into the types of training desired by accountants, which included mentoring by experienced senior professionals, lectures and presentations, conferences or off-site continuing professional education, and self-study cases on the subject. The education and training of professional accountants flow from academia and standard setting. To ensure that the proper application of PS is thoroughly integrated into the fabric of audit practice, accounting curricula of both undergraduate and graduate programs must address this topic and there should be training in all workplace settings. Too often, the teaching of PS in accounting classes at the undergraduate and graduate levels is limited to defining PS (although there is not one clear and universally agreed-upon definition) and identifying the threats that can impede PS. Coverage of threats should be expanded to include how they impact an auditor's level of PS depending on the risk area and financial statement account being audited. In addition, academicians should work to implement curricula that reflect a framework for PS and focus on its application. Indeed, both Brown-Liburd (2017) and Gissel (2018) show that hands-on applied practice of PS across varied scenarios is needed in audit classrooms for budding audit professionals to build the skill of PS. In addition, as recommended by Hayes (2016), direct classroom instruction on PS in an applied audit setting such as risk assessment would better prepare students to be professionally skeptical.

The PS literature points to a host of factors that play a role in and may help with PS. For example, auditors should be trained on the impact that other factors besides cognitive biases may have on PS, such as moral characteristics and social factors. In addition, incorporating deception risk and detection concepts into PS training could increase the questioning mind of an auditor. In applying PS, it may also be helpful for auditors to be trained to routinely consider how management, regulators, and investors would view an accounting choice and how this choice would look like in the press. In fact, one approach that can aid auditors in being more skeptical and less subject to biases is to train them to analyze any situation from

multiple perspectives. A multi-perspective analysis can be particularly useful for the evaluation of evidence when consideration of both confirming and disconfirming evidence is important.

In summary, a multitude of possible factors interact in the application of PS, which brings to light the complexity of PS. Stakeholders are clearly voicing a need for additional and pointed training and support regarding the exercise and documentation of PS in practice that will hold up in the face of regulatory inspections or peer reviews. Stakeholders are also calling for the incorporation of a PS scale into the standards as a needed step in the path forward. Pointed and improved education and training practices and further research are needed to help constituents successfully apply PS in the performance of audit engagements. Herein lies an important opportunity for standard setters, audit and accounting organizations, academics, and businesses to work together to develop a globally recognized PS framework that supplies practical implementation examples, illustrations, and other relevant material demonstrating the appropriate level and exercise of PS across various risk settings and audit areas. Thankfully, the professional, academic, and organizational accounting environments have a long history of cooperation in such matters and are likely to meet this challenge.

CONCLUDING COMMENTS

This paper presents an overview of the proposals by the IESBA and AICPA to enhance the exercise of PS by accountants and describes how and to what extent the comment letters submitted by constituents at the exposure draft stage of the due process impacted the final standards issued. First, we analyzed the constituent input, tabulating the responses to the nine IESBA and two AICPA questions by level of agreement (agree, partly agree, or disagree) and by type of constituent (professional accounting organization, accounting firm, governmental organization, academic/other individual). Next, we compared the final documents issued by both standard setting bodies to the respectively proposed standards and we identified the impact of the constituent input on the final standards issued.

While the results suggest that constituents generally supported both proposals, there were a few who opposed the proposals and several respondents partly agreed conditional on recommended changes to be included in the final standards. Both the IESBA and the AICPA were responsive in incorporating some of the constituent input in their final standards. However, some major constituent suggestions were not incorporated into either set of final standards. Stakeholder feedback overwhelmingly suggests that 1) a PS scale is needed to facilitate the measurement of PS in practice, and 2) additional authoritative guidance for the proper application of PS is needed, along with education and training programs that can be provided in academic accounting curricula and professional organizations. These findings carry implications for regulators, auditors, and other constituents, all of whom play an important part in advancing the profession's skillfulness in applying PS.

Our study is subject to certain limitations. One limitation is the fact that the IESBA and AICPA due process in setting standards is not entirely observable from the outside. It is likely that both the IESBA and AICPA used sources besides constituent input from comment letters to revise the proposals and issue the final standards. In addition, the basis for why the standard setting bodies did not incorporate some constituent suggestions from comment letters is not known. One possibility is that standard-setters will address such feedback outside of the Code. Another possibility is that further research is needed before something can be considered for standard-setting purposes. For example, future research is needed to establish a universally appealing and practically applicable scale for PS that will enable auditors to document and demonstrate in a straightforward way that they applied an effective level of PS during audit engagements. This is important given that failure to properly apply PS is a major criticism auditors routinely receive from regulators. In addition to PS scales, it may be helpful for regulators to use as examples prior audit engagements for which auditors were cited to have lacked PS as a basis for development of training materials for how auditors could demonstrate appropriate PS in such circumstances. Ultimately, PS should

become a more standardized, concrete, and implementable concept that can be measured and documented with consistency in practice, and that can be taught in the classroom and in life-long continuing professional training.

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