Public consultation on the governance (with special focus on organisational aspects, funding, composition and the roles) of the Monitoring Group, the PIOB and the standard setting boards and Compliance Advisory Panel operating under the auspices of IFAC

Response by David Swanney

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Section 1: The structure, objectives, legal nature and name

Q1: Do you consider it necessary to enhance representation of the public interest? If so, which additional actions, apart from the appointment of an independent IESBA Chair and redefining the nature of non-practitioner board members, would you suggest to reinforce the mechanisms to safeguard the public interest?

I do not believe that it is necessary to 'enhance' representation of the public interest, but there is a need to clarify the roles/responsibilities of those currently undertaking or representing (aspects of) this role. There has always seemed apparent confusion between the role/purpose – as regards the public interest - of public members of the PIACs (as I was for six years on IAASB), the PIOB observer attending each PIAC meeting[1], the PIOB as a whole, and the Monitoring Group. [See my response to Q3.]

As part of balancing the perception of the extent to which practitioners can or do reflect public interest, then as well as the proportions of practitioner and non-practitioner, the background of each Chair is also important. The appointment of independent chairs will show that the influence that this role exercises on the operation of the PIAC will be denied to a practitioner, thus perhaps contributing to a greater sense to the outside world that the PIAC will prioritise the public interest over private interests.

Achieving a true balance between practitioners and non practitioners is, however, difficult. Getting 'true' non practitioners (especially on a volunteer basis) with the necessary ability to contribute in a meaningful way to standard setting (perhaps especially in auditing) is not easy. The present belief that 50/50 has been achieved requires some heroic assumptions having to be made on the extent to which some individuals are sufficiently disassociated from the profession.

Q2: In the long term, would you favour a different and fully independent standard-setting model completely outside the IFAC structure and if so how could such a structure be funded?

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[1] PIOB claim in their work program 2012 and beyond that 'the knowledge that PIOB were observing each meeting assured stakeholders that the public interest was being protected.' (page 8). For this rather sweeping claim to be true, every single meeting of each PIAC would need to be observed. I know from my own knowledge that this is not the case in practice.

I have no strong view as to whether, as a matter of philosophy, a model independent of IFAC would of itself deliver better standards (or a perception of more public-interestedly developed standards). It is the way that the model works, and is seen and believed to work, that will determine this. A model independent of IFAC will necessarily be expensive (just see the IASB model, although this may differ in important aspects) and it is very difficult to see how – even if it were believed to be a better model than the existing – such a model could be substantially financed outside of the accounting/auditing profession. I agree with the caveats regarding the different perceptions of accounting and auditing standards summarised halfway down page 31 of the consultation paper.

Moreover, being able to attract sufficient (volunteer) members of the right calibre, with the necessary technical knowledge to develop quality standards, may be more difficult without the 'IFAC' connection.

Q3: Do you consider the current three-tier system adequate for achieving its objectives, or an alternative model could be more adequate? In the latter case, which model would you suggest?

I think that three tiers have to exist in the system – whether one judges that the present three-tier system is adequate will depend on how the system is perceived to operate. There has to be one tier that 'does the work' of developing standards: a second tier has to have some level of 'hands on' oversight of this work (in terms of ensuring that due process is followed): and a third, overarching tier has to oversee the broader effectiveness of the entire structure – all within the public interest.

It is arguable that the present model does not work in a truly effective way, as there are many overlaps between tiers: the PIOB observers seem in many ways to duplicate the role of the public interest members on PIACs (largely because of the amount of time they spend observing meetings) and they can (and have in my experience) easily stray into opining on the technical merits of various courses of action being discussed (rather than, as their remit requires, restricting themselves to the observation of due process); and the MG seems to be less of an 'overseer' of the whole structure than a 'second-guesser' of whether *the process* is perceived to be 'working', which to my mind is the fundamental role of the PIOB. So I see a lot of confusion in the present structure – but this is more in terms of clarity of role, rather than a view that there are too many (or too few) tiers.

In practice, the way the present three-tier system appears to operate is actually more akin to a two-tier model, given the duplication/overlap in the way that the MG and the PIOB actually appear to work. It may also raise questions about the present level and granularity of contact and communication between the MG and the PIOB.

Q4: Would you support the IPSASB being subject to PIOB oversight? Why? What conditions, if any, would you impose on such oversight? Would you see as a factor to take into account the fact that IPSASB deals with accounting rules instead of auditing ones?

I have no strong view on this question. At one level, there would appear to be a lack of symmetry in the IPSASB not being subject to PIOB oversight. I suspect (but I do

not know) that the starting point for many IPSASB standards is one or other standard developed by one of the existing PIACs, so these will have been subject to such oversight already.

Q5: Do you see merit in having a "Compilation document" for the whole structure? In this case, which alternative would you prefer for organising the structure and nature of the Compilation document?

In principle, it would be helpful to have all the various 'foundation' material in respect of the PIACs available in one place. That said, I would not see this as a matter that demands priority in the use of resources, given that this material is already publicly available (albeit subject to a search). Setting up a Compilation document would also involve ongoing maintenance costs, which will have to be borne somewhere.

Q6: Given the breadth of the current mandate, would you consider it helpful to modify the name of the structure to improve its visibility? In this case, what name would you suggest?

I have no view on this – it is the structure and its effectiveness that is important, not its name.

Section 2: Bodies in the structure (role and composition)

Q7: Do you agree with the proposal that the MG should have a more strategic role?

As presently structured, I see the MG's role as in fact strategic – and therefore at one level requires no change. It is important to distinguish the role of the MG from that of the PIOB, which has the (more granular) responsibility for monitoring that due process is followed by the PIACs. The 'proposal' at the top of page 19 of the consultation paper encapsulates what I see as the kernel of the MG's role. To move into a closer relationship with the PIOB (as the first bullet on page 19 suggests) would blur the distinction even further, and would seem to invite the two bodies being collapsed into one single body.

Q8: Do you agree with the objectives proposed and, specifically, with the MG having the possibility of conferring with the PIOB on the PIACs' agendas and receiving appropriate feedback?

This specific proposal would seem to bring too granular a role to the MG. There has to be a reason to have two bodies…….

Q9: Do you agree with the suggested ways of improving the communication activities? Would you consider it useful for the MG to have in the special occasions above described direct involvement with PIACs?

The proposal to have more direct contact with the PIACs would seem to bring into question the need to have two separate bodies, and therefore I would not support it. It is the present role of the PIOB to be satisfied as to due process. It would, however, be acceptable for the MG to meet the independent Chairs from time to time.

Q10: Do you have any specific suggestions on how liaison with investors could be improved? In this sense, do you see merit in some portions of the MG meetings having the public in attendance?

I have no suggestions to make regarding improving liaison with investors. I do not, however, believe that it is necessary – indeed it would be likely to inhibit debate – for meetings of the MG to be open to the public.   I would have thought that most of the MG's meetings are likely to involve confidential discussions. Increased frequency of press releases, plus perhaps an expanded session at IFAC's annual conference (or perhaps something in parallel with it, in the form of a public Annual Meeting) should provide stakeholders with sufficient opportunity to question the MG about its activities.

Q11: Would you find it useful that the MG engages with organizations representing governmental institutions? Would the G20 be the most appropriate or, should others bodies be considered instead?

Without going overboard on such communication, there would be some merit in opening some link to the G20, in order to raise the international profile of the effective development of international standards in the public interest.   G20 has

called for international adoption of ISAs, and so it follows that they ought to have some interest in being 'assured' that adequate and appropriate due process is followed in the development of such standards.

Q12: What is your opinion about the current composition of the MG? (i) Do you believe that other organisations (i.e., national or regional regulators) should or could be represented in the MG? If so, which criteria do you think new members should fulfil to become MG members? (ii) Should a maximum be set to the number of MG members? (iii) Would you favour a change on how the Chairperson is appointed?

I see no reason why one would want to expand the membership of the MG. The purpose of the MG is to oversee a structure, with monitoring of due process delegated to the PIOB. It would be wrong and confusing, in my view, to mix membership of the MG between representative international bodies and national or regional regulators (accepting as a fact that the EU is a present member). Most national or regional regulators are likely to be represented in some way through international organisations that are already members of the MG.

Q13: Do you see a problem in MG members appointing full time employees of organisations represented in the MG as PIOB members?

There is a perception issue here – if the PIOB is there to ensure due process is followed in the public interest (itself subject to MG oversight), why is it necessary to have two levels of 'MG organisational' representatives? Quite apart from the conflict of interest point, I see an overlap between the way the MG and PIOB appear to have been working. For the MG to appoint their 'employees' as members of the PIOB should in principle make it unnecessary for the MG itself to get into much of the detail – it should concentrate on a more strategic assessment of whether the 'structure' under which the PIACs work is effective. But my experience suggests that the MG has, in fact, gone into a level of detail that is more appropriately the responsibility of the PIOB. Maybe, however, the real issue is the level of communication (or perhaps the lack of communication) between the MG and the PIOB…..

At one level, I can see that (senior) employees of the organizations represented in the MG will have a good understanding of the objectives of these organizations, which is an advantage. On the other hand, I find it difficult to see how it is justified to allocate quite so much (valuable) time of very senior employees to the task of sitting in on a large number of meetings – especially where they are not permitted to directly contribute to, or influence, the content of these meetings, but are largely there to observe that due process is followed. I would have thought that such a 'process ensuring' role could more cost-effectively be delegated to less expensive staff. There must also be ways of getting the necessary assurance on the proper observation of due process through some form of delegation – for example, the chairs of the CAGs seem to already spend much time on the business and papers of the PIACs, and could have a more formal role in reporting back to the PIOB on how, for example, comment letters are dealt with. There could also be some leveraging on the role of the existing public members of the PIACs. PIOB members sitting in on just

the occasional PIAC meeting should be enough for them to 'take the temperature' of how these meetings are run.

Q14: Would you consider convenient to avoid direct hierarchical relationship between the PIOB and the MG members?

My comment on the previous question [Q13] might suggest that I believe it would be better to avoid this.

Q15: Do you think that the roles and responsibilities of MG and PIOB should be further clarified? Do you have specific suggestions regarding which areas this clarification should address?

[See my responses to Q3 and Q13]. I agree with the suggestion in the consultation paper that the MG's relationship with the PIOB should be 'reinforced'. I believe there should be much greater accountability by PIOB to the MG than appears to be the case at present, so that the MG can acquire an ongoing understanding of how the PIACs are 'performing'.

Q16: Do you see merit in the PIOB undertaking a regular review of its due process and oversight framework through its strategy document?

In any organization, it is good practice that its due process is kept under regular review; this applies equally to the PIOB. It seems to me, therefore, to be essential that its due process and oversight framework should be kept under regular review – for example, whilst it may have made sense in its early years to observe every PIAC meeting for 'educational' purposes, as PIOB's experience of how these meetings 'work' develops, it should not be necessary to invest so much expensive resource in observation, as opposed to other forms of assessment (including through discussion with, and feedback from, other participants in the process, such as CAG chairs and public members).

In addition, it seems to me that the level of 'public interest' in the work and output of all the PIACs is not the same: for example, I would suggest that the level and nature of public interest in education is quite different from that in auditing standards. These differences should be reflected in the PIOB's own due process and oversight arrangements.

Q17: Do you see merit in the PIOB periodically producing a strategy document that would supplement the yearly business plan and budget? What should the involvement of the MG be in the production of these documents?

Given the nature of its activities, a PIOB 'strategy document' has to have limited objectives – it will describe its due process and oversight framework, but PIOB has little opportunity to develop a wider 'strategy' beyond refining such due process. Moreover, PIOB is not 'producing' anything – and so the oversight of due process does not in my view lend itself to a normal 'business plan' approach. It is the PIOB's own due process and oversight framework which is important and of wider interest.

Q18: Do you think that the current composition of the PIOB could be enhanced? Would you consider convenient that the PIOB's composition is reviewed each time a new body becomes full member of the MG?

I cannot see any reason why the membership of the PIOB need be enhanced. Rather, as my responses to Q13-15 imply, I see the current composition as overlapping with that of the MG, and it is this that should be reviewed.

Q19: Would you consider the current composition of the PIACs appropriate? Do you see merit, in the context of a second effectiveness review, in exploring the idea of having a majority of non-practitioners and a majority of public members?

As I said in my response to Q1, getting the right balance between practitioners and non practitioners is difficult. I can see that it is undesirable to have a PIAC entirely comprised of practitioners (for all the obvious reasons), but I am not sure that it is obvious that a 50/50 split between practitioners and non practitioners (or any other arbitrary proportion) will of itself persuade outsiders that the process operates more in the public interest. It is important above all – unless one moved to a model where the technical staff did all the drafting - to have a PIAC that has sufficient technical knowledge amongst its members (as opposed to *available* to members through technical advisers) that standards can be developed that have technical integrity as well as coherent and practical presentation. The higher the proportion of non practitioners (bearing in mind the definition of such persons) the greater is the risk of diluting the available technical knowledge. I am therefore not persuaded that even a 50/50 split is of itself a priority, especially when it seems to me that some of those categorized as non practitioners can only just (on a generous interpretation) be classified as truly non practitioner. But equally, we are where we are, so I accept we have to live with 50/50, with an independent Chair, but I could not see a case for increasing the proportion of non practitioners without risking jeopardising the technical integrity of the PIAC process.

Q20: Do you consider best practice a nine years period for rotation of the representatives of CAG member organisations?

I believe there should be a finite length of appointment for any individual that represents CAG member organisations. The length might vary between CAGs, depending on the size of a particular PIAC's agenda, and the level of engagement that CAG members are required to have.

Q21: Would you agree that it is not realistic at the current time to attempt to alter the funding structure of standard setting activities in any substantial fashion?

For all the reasons and difficulties noted in the consultation paper, I do not believe that it is realistic at the current time to try to alter the funding structure. In particular, I agree with the observation in the paper about the difference in perception between accounting and auditing standards. I can see that it could be very difficult to persuade external funding sources of the similarity, in terms of the public interest, of

these standards, and therefore to get these sources to agree that they should contribute with equal enthusiasm.

Q22: Do you consider appropriate that IFAC finances the largest part of the PIOB budget? If not, do you consider appropriate that IFAC launches an external fundraising having some contributions of the MG members in the mean time?

As a matter of practical necessity, I believe that this has to be considered appropriate. I would be happy to see IFAC launch an external fund raising program, but I would be cautious in assuming it would deliver anything approaching 51% of the MG/PIOB costs.

Q23: Do you think it feasible to have a similar funding structure in place for the PIOB to that in place for funding the IFRS Foundation?

As my response to Q21 implies, I would regard seeking to replicate the IFRS Foundation arrangements as just not likely to attract sufficient funding.

Q24: Do you see the need for and/or merit in having a permanent Secretariat for the MG? In this case, do you think IOSCO should provide resources for a permanent Secretariat to the MG?

I am not persuaded that there is a case for the MG having a permanent Secretariat. Given the role of MG, which is to 'oversee' a PIOB sitting below it, a permanent secretariat would – not least to justify its existence – be sorely tempted to involve itself with the detailed work of PIOB, which would complicate an already difficult relationship. I believe it is sufficient for the MG to oversee the PIOB and the PIAC structure 'from a distance' – based on regular reports and updates from PIOB – with a closer review taking place at periodic intervals, at which time a small 'task force' could be appointed to carry this out.

Section 3: Final questions

Q25: How do you think the governance of the international auditing, ethics and education standards setting process could improve audit quality? What are the main objectives that those responsible for governance should take into account?

The contribution that the governance of the PIACs make to audit quality is through ensuring the development of high quality standards, drawn up under a due process that ensures the right balance between the technical quality of standards, the most appropriate consultation arrangements, and that are 'flexible' enough to reflect changing market conditions and user expectations (especially where these change suddenly due to external developments).

Above all, the development process must reflect, in all its stages, the public interest, rather than any private interests, where these interests diverge from those of the public.

The main objectives that those responsible for governance should take into account are therefore those that ensure the above aspects are reflected in the current structure, membership and due process of each PIAC.

Q26: What is your opinion about the current structure? Do you think the current structure is appropriate in order to improve audit quality? If not, what changes, suggestions or remarks would you propose?

In my view the current structure does allow for the development of appropriate standards that meet the objectives set out above. I am strongly of the view, however, that the provision of high quality standards (in all three areas) is only one part of what delivers audit quality. Education, ethics and auditing standards are clearly the base on which audit quality is built (albeit each contributing quite differently to the broad aim), but there are many other factors that affect audit quality (as recent publications by IAASB point out). It would be wrong, in my view, to believe that standards alone – however 'improved' - will of themselves deliver audit quality.   There has to be discussion and communication (as IAASB well understands) with other bodies and structures that influence audit quality, to achieve the result that everyone wishes (however difficult it is, in practice, to measure!).

Q27: Do you agree that the current levels of empowerment and responsibility of the bodies that compose the current structure (MG, PIOB and PIACs) are appropriate? If so, do you have any suggestions for improving the dialogue and interaction between the different bodies? If not, how these levels of empowerment and responsibility could be improved?

As my responses to earlier questions imply, I do not believe that the present structure operates in an optimal way. There may on paper be defined roles, but in the way the various bodies (PIOB and the MG) appear to operate in practice, there are overlaps which diminish the clarity of the empowerment and responsibility of each body.

Q28: Do you think that there is any other overall structure that could achieve improvement in audit quality more efficiently? If so, what could they be and how might they be financed?

There is no 'silver bullet' that will deliver audit quality. I believe that the present structure of the PIACs is well placed to deliver what any standard setting bodies could that will contribute in the best way to audit quality. Provided that these bodies follow appropriate due process (and that there is a mechanism that confirms this to the outside world), and there is the right level of communication (and shared objectives) with those other bodies and structures that affect audit quality, I believe the standard setting community will have done all it can.