
Review of the IFAC Reforms– Consultation Paper

The Monitoring Group

10 June 2010

TABLE OF CONTENTS

Invitation to Comment	3
Introduction	4
The Monitoring Group’s Approach to Conducting the Effectiveness Review	6
The Monitoring Group’s Preliminary Conclusions	8
<i>Section I. Composition of the Standard-Setting Boards</i>	11
<i>IFAC Reform Implementation Assessment</i>	11
<i>IFAC Reform Opportunities for Further Improvement</i>	12
Mix of Board Member Backgrounds	13
Assignment of Board Seats	13
Ability to Attract Public Board Members	14
Setting a Code of Ethics for Accountants	15
<i>Section II. Operating Procedures of the Standard-Setting Boards</i>	16
<i>IFAC Reform Implementation Assessment</i>	16
<i>IFAC Reform Opportunities for Further Improvement</i>	17
Role of Technical Advisors to Board Members	17
Participation of Audit and Ethics Board Members in Board Meetings	17
Role of the Audit and Ethics Boards’ Consultative Advisory Groups	18
Meetings of the Audit and Ethics Boards’ Consultative Advisory Groups	19
Analysis of Comment Letters	20
Feedback on the Monitoring Group Member’s Input to the Boards	20
Finalization of Standards	21
Voting by Board Members	22
<i>Section III. Implementation of the Standards</i>	23
<i>IFAC Reform Implementation Assessment</i>	23
<i>Section IV. Oversight</i>	24
<i>IFAC Reform Implementation Assessment</i>	24
<i>IFAC Reform Opportunities for Further Improvement</i>	25
Role of the PIOB Members in the PIOB’s Oversight Work	25
Role of the PIOB Staff Members in the PIOB’s Oversight Work	26
Diversity among the PIOB Members	26
Funding of the PIOB	27
<i>Section V. Monitoring</i>	28
<i>IFAC Reform Implementation Assessment</i>	28
<i>IFAC Reform Opportunities for Further Improvement</i>	29
Interaction between the Monitoring Group and the PIOB	29
Longer Term Operation of the Monitoring Group	30
List of the Monitoring Group’s Preliminary Recommendations	32

Invitation to Comment

The purpose of this Consultation Paper (this Paper) is to seek input from any interested party to the Monitoring Group's preliminary conclusions resulting from its assessment of the implementation of the set of 2003 IFAC Reforms (the Reforms).¹ Input is sought on the merit of the preliminary conclusions as well as practical suggestions on how to implement the proposed recommendations. The Monitoring Group welcomes responses to this Paper by 15 August 2010.

The Monitoring Group is a consensus-based group that brings together the regulatory and international public interest organizations responsible, *inter alia*, for monitoring the implementation of the Reforms. The Monitoring Group is composed of six members and one observer. The members are the Basel Committee on Banking Supervision (the Basel Committee), the European Commission, the Financial Stability Board, the International Association of Insurance Supervisors (IAIS), the International Organization of Securities Commissions (IOSCO) and the World Bank. The International Forum of Independent Audit Regulators (IFIAR) is an observer. The Monitoring Group is chaired by IOSCO. The Chair is currently the Vice Chairman of IOSCO's Technical Committee, who is Mr. Hans Hoogervorst.² He is Chairman of the Executive Board of the Netherlands Authority for the Financial Markets.³

The Reforms provided for changes to the standard-setting, implementation, oversight and monitoring processes associated with producing International Standards on Auditing, the international Code of Ethics for Professional Accountants and International Education Standards. These changes were born out of the erosion of confidence that arose from the financial reporting problems reported by some issuers in and around 2002 and 2003. The changes were aimed at supporting confidence by increasing the quality of financial statement audits. It is timely that the Monitoring Group performs its assessment at this time when confidence is negatively affected by the financial reporting problems that have come to light during the recent credit crisis. Thus, the Monitoring Group members are again focused on the importance of high quality financial statement audits.

¹ The text of the Reforms, including a diagram of the resulting relationships, is available at www.ifac.org/MediaCenter/?q=node/view/339.

² Mr. Hoogervorst was appointed Chairman of IOSCO's Technical Committee with effect from 11 June 2010.

³ Information about the Monitoring Group, including its Charter, is available at www.iosco.org/news/pdf/IOSCONEWS144.pdf.

As part of conducting its assessment of the implementation of the Reforms (the Effectiveness Review) the Monitoring Group has reviewed whether the provisions of the Reforms have been implemented as well as identified some associated recommendations for additional changes; both are contained in this Paper.

Via this Consultation Paper the Monitoring Group seeks input on:

- (i) Its assessment of the implementation of the Reforms, including any other matters which the Monitoring Group might take into account.
- (ii) Its eighteen recommendations for further improvements which are set out in the body of this Paper along with the analysis underpinning them, as well as other opportunities for further improvements that the Monitoring Group might identify.
- (iii) Its conclusion that the Monitoring Group initiate a future effectiveness review approximately three years after its completion of this one, unless circumstances indicate that the Monitoring Group should initiate such a review sooner.

The Monitoring Group may modify its preliminary conclusions or add practical implementation ideas to its proposed recommendations in light of the comments received. The Monitoring Group expects to draw its final conclusions and issue an associated report in November 2010. Immediately thereafter the Monitoring Group expects to carry out the commitments that it will undertake as an outcome of this Effectiveness Review, including further assessing its own role and approach to monitoring.

Responses should be submitted electronically to MonitoringGroup@iosco.org. The Monitoring Group anticipates making the responses publicly available unless the commenter requests confidentiality and that is appropriate in the view of the Monitoring Group.

Introduction

The subject of the Reforms and thus of this Effectiveness Review is the public interest activities of the International Federation of Accountants (IFAC) that support auditing; more specifically, IFAC's International Standards on Auditing, its international Code of Ethics for Professional Accountants and its International Education Standards which are established by three respective standard-setting boards that each operate under the auspices of IFAC. The names of these three Boards are the International Auditing and Assurance Standards Board (Audit Board), the International Ethics Standards Board for Accountants (Ethics Board) and the International Accounting Education Standard Board (Education Board),

respectively (collectively, the three Boards). IFAC's Compliance Advisory Panel assesses adoption and implementation of these standards by the IFAC members. IFAC is a global association of the accountancy profession. IFAC's members are professional bodies from 124 countries.⁴

The history of the Reforms goes back to late 2002, after a number of highly publicized corporate financial reporting failures occurred that undermined confidence in financial reporting and auditing. At that time IFAC and a group of six regulatory and international financial public interest institutions began a dialogue regarding the importance of having high quality audits of the financial statements of public companies and the need to restore and enhance public confidence in financial reporting and auditing. IFAC had at the time a number of boards and committees within its organization that were developing auditing standards, an ethics code for accountants which contained independence requirements for external auditors, and other forms of standards and guidance for accountants and auditors. IFAC and this group of regulators and financial public interest institutions deemed these activities to be important to support the public interest. Accordingly, all these activities became the subject of the Reforms.

The objective of the Reforms was to increase confidence that these activities of IFAC were properly responsive to the public interest and would lead to the establishment of high quality standards and practices in auditing and assurance. A central question explored in the dialogue leading up to the Reforms was how enhancements could be made to IFAC's standard-setting structures and processes to retain the expertise of the audit profession in setting the standards that would govern IFAC members' performance in their service to the public, yet counteract some of the effects of the fact and appearance of auditor self-interest in setting such standards. The practical constraint to addressing this question was the continued use of the standard-setting committees within IFAC's professional organization. This approach, versus starting over to establish new standard-setting boards, provided immediacy to the implementation of the enhancements. Thus, the solutions were to utilize the then existing IFAC committee structures but in a way that would involve greater participation of financial statement users, of regulators and of other non-practitioners in the standard-setting process and to interject above those committee structures a layer of public interest oversight from a body of experienced senior leaders in regulation and finance who had no ties to the accounting and auditing profession.

Implementing these solutions meant changes to the composition and functioning of the three Boards, including a strengthening of the arrangements for their respective Consultative Advisory Groups (CAGs). Also, the international Public Interest Oversight Board (PIOB) was created to oversee the Board member

⁴Information about IFAC, including about the three standard-setting boards, is available at www.ifac.org.

appointments and the processes associated with the work of these Boards.⁵ The PIOB was also assigned to oversee IFAC's membership compliance program for adoption and implementation of their professional standards. The PIOB's activities were to be and are monitored by the Monitoring Group and funded largely by IFAC in a "blind trust" type arrangement agreed by IFAC and the Monitoring Group. Under this arrangement IFAC does not have a role in deciding whether and how the PIOB spends its annual funding.

The Reforms were agreed between IFAC and the six regulatory and international financial public interest organizations which, as a result, meant that the six organizations became the founders of the Monitoring Group. IFAC had an interest in accepting its rights and responsibilities under the Reforms as this would increase confidence in standard-setting processes and therefore in financial statement audits, as described above. The Monitoring Group, after formal considerations by its founders, had an interest in accepting its rights and responsibilities under the Reforms because these organizations are concerned with the quality of financial statement audits, which are affected by the quality of audit and audit-related standards.⁶ All of these changes collectively became known as the "IFAC Reforms." They were published in a 2003 document entitled "Reform Proposals"; this also became the final Reforms document. The provisions of the Reforms were implemented from effectively 2005.

As set out in Section 13 of the Reforms, "five years after the formation of the PIOB [Public Interest Oversight Board], the MG [Monitoring Group] shall perform a review of the effectiveness of the PIOB and the PIACs [Public Interest Activity Committees]. This review shall include consideration of all of the items discussed in this paper, as well as any other aspects of IFAC's operations thought appropriate by the MG, and shall also include an assessment of the continuing need for and role of the MG. The MG shall have the right to make recommendations to IFAC and the PIOB based on this assessment." The Monitoring Group's Effectiveness Review, which is the subject of this Paper, is in response to this five-year review provision.

The Monitoring Group's Approach to Conducting the Effectiveness Review

With respect to its scope, the Monitoring Group's assessment work encompasses four matters; namely:

⁵ Information about the PIOB is available at www.ipiob.org.

⁶ See Section 3.1 of the Reforms which states in part, "...all members of the MG are committed to strongly support the development and issuance of high quality international auditing and assurance standards ..." and "...all members of the MG are also committed to strongly support high quality practices by the international auditing profession...".

- (i) Whether the provisions of the Reforms were in fact implemented;
- (ii) The manner in which the Reforms were implemented relative to achieving the aims of the Reforms;
- (iii) A comparison of the original features of the Reforms to features that the Monitoring Group believes have today come to be associated with credible international standard-setting processes; and
- (iv) Whether new factors that exist today in the global capital markets may warrant a future review of the overall standard-setting governance, structure and arrangements set out by the Reforms.

The Monitoring Group's assessment does not judge outcomes in terms of either the quality of the standards produced by the Boards during the assessment period or their appropriate use. The views of individual Monitoring Group member and observer organizations on these matters are subject to their own considerations and due process.

Further, the scope of the Monitoring Group's assessment does not involve revisiting the overall standard-setting governance, structure and arrangements set out by the Reforms. This is because recent developments in the global capital markets that might help inform such an analysis—such as those associated with the credit crisis—are still settling.

The Monitoring Group began its assessment work by receiving self-assessments from IFAC and from the PIOB with respect to implementation of the Reforms and discussing them with each, respectively. Further, the Monitoring Group had access to the minutes of the PIOB meetings. The Monitoring Group also informally collected thoughts of members of each standard-setting Board's CAG and of some members of IFIAR. The Monitoring Group added to this the experiences and observations of its own members because after implementation of the Reforms they continued to follow the standard-setting work in varying ways, such as through membership in the Audit and Ethics Boards' CAGs, participation in the Audit and Ethics Boards' constituent roundtables and Task Forces, periodic attendance among the public audience members at board meetings and submission of comment letters on proposals.

Due to the Monitoring Group members' lesser day-to-day involvement with the work of the Education Board and of the Compliance Advisory Panel, the Monitoring Group also had separate discussions with the Chairs of each. Lastly, the Monitoring Group had a discussion with the Chair of IFAC's International Public Sector Accounting Standards Board to follow-up on a matter that IFAC raised in its self-assessment.

In organizing its preliminary conclusions the Monitoring Group has ordered its assessment around five dimensions of standard setting, namely:

- I. Composition of the Standard-Setting Boards
- II. Operating Procedures of the Standard-Setting Boards
- III. Implementation of the Standards
- IV. Oversight
- V. Monitoring

Accordingly, this is the organization of the latter Sections of this Paper.

The Monitoring Group's Preliminary Conclusions

The overall preliminary conclusions of the Monitoring Group are that:

- (i) Virtually all of the Reform provisions have been implemented;
- (ii) There are opportunities for fine tuning and adjustment to the manner in which some of the Reform provisions were implemented to better achieve their aim, and correspondingly to allow all of the elements of the Reforms to better integrate with each other;
- (iii) There are opportunities to add features to what is provided for in the Reforms to encompass practices that, given the experiences of other international standard setters since 2003, have come to be associated with more credible international standard-setting processes; and
- (iv) There are new factors which exist today in the global capital markets that may warrant a future review of the overall standard-setting governance, structure and arrangements set out by the Reforms.

Each of these overall conclusions is further described, below.

While determining that virtually all of the Reform provisions have been implemented, the Monitoring Group noted three areas of the Reforms that do not yet appear to be fully implemented, as described in the following three paragraphs.

The first area relates to the composition of the Boards, specifically the provision of the Reforms to add a specialist in business ethics to the Ethics Board. The Monitoring Group did not identify any of the Ethics Board's members who had been designated as this specialist per se; however, one or two individuals appointed to the Ethics Board have significant related academic and practical experience.

The second area relates to the operating procedures of the Boards, specifically their responsibility under Section 3.2 of the Reforms to provide feedback to individual Monitoring Group members with respect to any of their input that the Board does not take up in a final Standard. The Monitoring Group observes that some of this feedback occurs during the normal course of discussion at Audit and Ethics Board CAG meetings. These discussions do not, however, completely fulfill the Reform provision for two reasons. First, the range of issues on which the Boards provide feedback in a CAG meeting is geared to matters discussed in previous CAG meetings rather than encompassing all input given to the Boards, such as via comment letters. Further, the group setting of a CAG meeting does not provide an opportunity for interchange with Board members regarding an individual constituent's—in this case the Monitoring Group member's—points.

The third area relates to oversight of the Boards, specifically the PIOB's responsibility under Section 2.2 of the Reforms to evaluate the adequacy of funding provided to support the three Boards and the Compliance Advisory Panel. The Monitoring Group acknowledges that the standard-setting Boards have received resources beyond those provided for in the Reforms, such as travel subsidies for developing country Board members. However, the Monitoring Group also acknowledges that what constitutes adequate funding is a matter of significant judgment and thus warrants ongoing evaluation by the PIOB.

The Monitoring Group also concluded that while the other provisions of the Reforms were indeed implemented, the manner of implementation of some of the Reforms has not completely achieved their aim. The Monitoring Group acknowledges that implementation of the Reforms has improved the overall transparency of and broadened the external participation in the work of the Boards, but not always to the degree that the Monitoring Group anticipated in agreeing to the Reforms' design. Areas in which the Monitoring Group suggests that fine tuning and adjustment would be helpful relate to:

- Mix of Board member backgrounds
- Ability to attract public Board members
- Participation of Audit and Ethics Board members in Board meetings
- Role of the Audit and Ethics Boards' CAGs
- Meetings of the Audit and Ethics Boards' CAGs

- Analysis of comment letters
- Feedback on the Monitoring Group member's input to the Boards
- Role of the PIOB members in the PIOB's oversight work
- Role of the PIOB staff members in the PIOB's oversight work
- Interaction between the Monitoring Group and the PIOB

These areas are each described within Sections I thru V of this Paper.

There are also opportunities to add features that would further advance the objectives of the Reforms but that were not part of their original design. These opportunities relate to what the Monitoring Group has learned since 2003 from the experiences of others who set international standards about what standard-setting, oversight and monitoring processes contribute best to credible international standards. Areas in which the Monitoring Group suggests that features could be modified or added relate to:

- Assignment of Board seats
- Setting a Code of Ethics for Accountants
- Role of Technical Advisors to Board members
- Finalization of Standards
- Voting by Board members
- Diversity among the PIOB members

These areas are each described within Sections I thru IV of this Paper.

While the Monitoring Group concluded that new factors exist today that may bear upon the overall standard-setting governance, structure and arrangements set out by the Reforms, the Monitoring Group did not at this time consider whether fundamental changes to that governance and structure and those arrangements were appropriate. Nonetheless, the Monitoring Group has noted two matters that are associated with the PIOB's and its own work that it believes should commence upon completion of this Effectiveness Review. They are:

- Funding of the PIOB
- Longer term operation of the Monitoring Group

These two areas are described within Sections IV and V of this Paper. Further with respect to the PIOB, the Monitoring Group notes that in its self-assessment IFAC suggested revisiting the fact that the Reforms preclude the PIOB from assuming an oversight role for IFAC's Public Sector Accounting Standards Board. The Monitoring Group believes that this provision of the Reforms is an entire matter unto itself which is affected by the objectives of the Reforms, how the role of accounting standards in the public sector differs from that of audit-related standards, the demand for and thus benefits brought by such PIOB oversight, and so forth. The Monitoring Group has not taken onto its agenda the matter of revisiting this provision of the Reforms.

The Monitoring Group also foresees that matters associated with the work of the Boards would be within the scope of a future effectiveness review. Factors informing these matters could include the Monitoring Group's additional experience with the work of the Education Board and the Compliance Advisory Panel, the experiences with the implementation of the outcomes of this Effectiveness Review, the future experiences of national audit oversight functions, and views around the long-term optimal architecture and arrangements for balancing the competing pressures that arise in setting high quality international audit and audit-related standards. Accordingly, the Monitoring Group proposes to initiate a subsequent effectiveness review approximately three years after the completion of this one unless circumstances indicate that it should initiate such a review sooner.

Section I. Composition of the Standard-Setting Boards

IFAC Reform Implementation Assessment

The Monitoring Group's assessment is that all of the measures described in the Reforms relating to composition of the three Boards have been implemented, except for one which has been substantially implemented. These included changes such as the addition of a full-time chair for the Audit Board; the addition of two public members to the Ethics Board and one to the Education Board (which brought the number of public members to a total of three on all three Boards); a provision that each of the CAG Chairs would attend their respective Board's meetings as observers with speaking rights; a change in the role of the Forum of Firms members who were previously observers to the Ethics Board to become voting members; and a change to require that members of all three Boards sign a declaration that they will act with integrity and in the public interest in the discharge of their role within IFAC. Reform measures were also provided for an appropriate balance of members from business and government and from small and medium-sized firms on the Ethics Board and that this notion would also be applied to the Education Board. Previous to the Reforms the Audit Board had taken steps to improve the balance of board member

backgrounds and this was understood to continue. Beyond the provisions of the Reforms the Boards have also achieved greater geographical balance among their members.

The element of the Reforms concerning Board composition that could be considered substantially implemented based upon the experience of some members is the provision that one of the public members added to the Ethics Board would be a specialist in business ethics. However, in subsequent consideration of this issue, the Monitoring Group notes that there are many types of ethics experts and service providers on ethics issues, and it is unclear what would be a valid reason for choosing one over the other. The Monitoring Group believes that rather than designate board seats to a particular specialty, the issue of who can best contribute to a diverse mix of individuals on the Boards should be evaluated in reviewing Board candidates.

The manner of implementation of the Reform provisions to bring an appropriate balance of Board member backgrounds has sought to achieve parity between “practitioners” (members currently employed in auditing) and “non-practitioners” (generally, members who had not been employed as auditors during the previous three years, but who could be persons whose earlier careers had been as an auditor). Currently, the Audit Board and the Ethics Board each have eighteen Board members, with thirteen members of each Board being current or former employees of audit firms or current or former employees of auditor professional organizations. While the composition of both the Audit Board and the Ethics Board has become more varied over time as the Reforms were implemented, the Monitoring Group believes that the aims of the Reforms to counteract some of the effects of the fact and appearance of auditor self-interest in setting such standards have yet to be fully realized because in practice many of the “non-practitioners” do not have substantive professional career experience outside of auditing.

The implementation experiences have also provided a base of information that can be used to build on past accomplishments and enhance future public contributions by the Boards. These experiences and resulting recommendations are described in the remainder of this Section. These recommendations emphasize the work of the Audit Board and the Ethics Board versus that of the Education Board given the focus during the past five years by Monitoring Group members on the work of these two Boards because their work has a more direct effect on the conduct of financial statement audits. Nonetheless, the Monitoring Group acknowledges the importance to serving the public interest of auditors’ educational qualifications and thus notes the future anticipated work of the Education Board.

IFAC Reform Opportunities for Further Improvement

Mix of Board Member Backgrounds

Observation: Both the Monitoring Group and IFAC have stated that they seek to achieve an appropriate balance in the composition of the Board members on each Board between those who are “practitioners” and those who are “non-practitioners.” In essence this is a balance between Board members who have the greatest technical expertise and Board members who are in a position to evaluate issues based upon other professional experiences and thus perhaps more objectively. Also, IFAC has identified certain non-practitioner Board members as “public members” on its current website listing of Board members for each of the three Boards. These public members have typically had substantive amounts of experience in academia, financial supervisory institutions, governmental bodies and/or user groups.

Implications: While it is understandable that a “non-practitioner” may have served as an auditor at one time, if essentially their only experience outside of auditing is the last three years away from it then the differing and more objective perspective sought for this role may not materialize in the Board’s work. The quality of the standards may at least appear to be affected as well, thereby potentially undermining confidence in the standards and audits. This is made more manifest if each of the Boards’ Task Forces, which take the lead on carrying out the various Board projects, is composed of a diverse group of Board members.

Recommendation 1: The Monitoring Group recommends that IFAC appoint a mix of Audit Board and Ethics Board members appropriate to the need for both technical competence and objectivity in the work of each respective Board such that there is parity—or perhaps even a majority—of Board members with professional career experience that substantively goes beyond that of an auditor.

Assignment of Board Seats

Observation: The Monitoring Group notes that prior to the Reforms a group of the largest international audit firm networks had come together within IFAC as the “Forum of Firms” and established a formal linkage with IFAC through the Transnational Auditors Committee. Formally established in 2002, the Forum of Firms (FOF) is an association of international networks of accounting firms that perform audits of financial statements that are or may be used across national borders. Members of the FOF agree to meet certain requirements as detailed in the FOF Constitution. Since establishment, the FOF has held “rights” and assumed the associated responsibilities to have individuals chosen from among their members occupy a certain minimum number of Board member seats; currently five of the eighteen Board seats on each of the Audit and Ethics Board.

Implications: While Board members from the FOF members bring helpful expertise to the respective Boards' work, and as such are to be expected to continue to be interested in becoming and make desirable Board members, the practice of specific allocation of Board seats to a particular group seems inconsistent with fostering credibility through an open process that secures the best mix of Board members from among all those available to serve. The latter seems a more desirable practice for an organization that aims to set standards to serve the public interest.

Recommendation 2: The Monitoring Group recommends that IFAC discontinue the practice of reserving a specific allocation of Audit Board and Ethics Board seats for a particular type of background—in this case for FOF nominees—and instead consider FOF nominees among all the candidates it evaluates in deciding upon the optimal mix of Board members based upon all the relevant dimensions of balance and diversity.

Ability to Attract Public Board Members

Observation: The Monitoring Group notes that most of the practitioner Board members are paid and made available by their audit firms to devote considerable time to the development of auditing and ethical standards at the Audit Board and Ethics Board; in contrast, public members within the non-practitioner group who are not otherwise employed are providing their Audit and Ethics Board service on the basis of travel expense reimbursement only, and often must forego other economic opportunities in order to devote such a significant amount of time in a volunteer effort.

Implications: A remuneration policy which under the current overall funding arrangements for the standard-setting Boards is limited to travel expense reimbursement reduces the number of highly-qualified people who as a practical matter can serve as public members within the non-practitioner group. Further, the additional opportunity costs of their time once joining the Board further places them at a disadvantage in being able to participate actively in additional Board efforts such as the Task Forces that lead the Board's considerations on each of their projects. The Monitoring Group notes that it is possible that additional measures could help balance the number of and time available from public members if changes could be made in order to provide some compensation to those who are not already employed by an organization that supports their Board service. In particular, public interest organizations—even national audit standard setters or national audit oversight authorities—could be asked to identify potential candidates for service on the Boards, and would possibly find this easier if some compensation were available for Board service. Any measures introduced to provide compensation to public members would

need to be designed in a manner to protect the appearance and substance of the independence of such members.

Recommendation 3: The Monitoring Group recommends that IFAC explore financial measures, such as reasonable stipends if they would not raise questions about independence and objectivity, to accompany travel cost reimbursement for Board members who are public members that are employed by an organization that cannot provide financial support for their participation as a Board member.

Setting a Code of Ethics for Accountants

Observation: In considering the Ethics Board's overall work to establish and then continually improve the Code of Ethics for Professional Accountants, the Monitoring Group has discussed whether it is necessary or desirable to have the same degree of practitioner involvement in setting auditor ethics and independence standards by the Ethics Board as is the case for setting audit practice standards by the Audit Board. The principles and requirements for good professional conduct and for avoiding conflicts of interest can be viewed as broader and more general in nature than the more process-oriented requirements of how best to carry out an audit of a company's financial statements. Further, the practitioner pressures are arguably greater in setting auditor ethics and independence standards because of what is often at stake. Specifically, what is often at stake in setting auditor ethics and independence standards are the effects on an audit firm of being able to engage or not engage in a particular non-audit line of business. By way of contrast, what is at stake in setting audit practice standards are the future costs of being required (versus not required) to carry out a particular procedure or provide a particular form of report in completing an audit of a company's financial statements.

Implications: A great deal of audit profession involvement in the Ethics Board's work raises the issue of whether this work might be perceived to lack the credibility it otherwise would have with less such involvement, even despite the series of checks and balances instituted by the Reforms. This perception can arise out of a concern that the pressures associated with this involvement result in decisions that are sub-optimal relative to serving the public interest. This is the case for situations in which a matter's optimal outcome to strengthen the worldwide accountancy profession may contribute to the public interest in some way but still may run counter to the optimal public interest outcome. This appearance especially manifests itself if the Ethics Board's decision about how to handle a matter differs in direction relative to that recommended by its regulatory and other public interest constituents.

Recommendation 4: The Monitoring Group will evaluate how the expertise and perspective of those who are or have been auditors is best included in setting ethics and auditor independence standards, and thus

whether the trade-offs indicate it would be advisable for other structures for ethics and independence standard setting—or at least for the composition of the Ethics Board—to be utilized.

Section II. Operating Procedures of the Standard-Setting Boards

IFAC Reform Implementation Assessment

The primary aims of the Reforms with respect to the standard-setting activities of all three Boards were to increase the transparency of their activities and to achieve broad-based external participation in their work. These aims were envisioned to be achieved through expanding and enhancing the CAGs such that they are composed of a wide range of stakeholders, increasing the number of non-practitioner Board members, and implementing other measures designed to increase public input to and the transparency of their work. In addition, measures were provided regarding the establishment of CAGs for the Ethics and Education Boards and the roles of their respective Chairs as observers to the associated Boards with speaking rights. Further, a number of improvements were identified and recommended for the Audit Board CAG, which was already in existence at the time of the Reforms. While the Education Board was not fully formed at the time of the Reforms, it was envisioned to eventually have procedures similar to those of the Audit and Ethics Boards.

Since the time that these basic procedural changes were implemented, the Audit, Ethics and Education Boards have continued to implement and refine a number of transparency improvements, including posting of Board papers on the IFAC website in advance of each meeting, posting a brief summary of Board meeting actions on the public website after a meeting, opening Board and CAG meetings to the public, and increasing the amount of public explanation given for Board decisions. The proceedings of many Audit Board meetings are also made available to the general public via an audio tape posted to its web pages after the meeting.

Specific changes to foster broad-based external participation have also occurred. For example, the Chair of the Audit Board is now a full-time position paid by IFAC; arrangements for liaison between the Audit Board and national audit standard setters are developed and formalized; and public fora or roundtables are held if the nature of the standard, the level of interest or some other reason indicates that wider consultation is warranted.

The experience of the Audit and Ethics Boards, and their related CAGs, has indicated that the Reform measures adopted have had a positive effect on the transparency and effectiveness of Board protocols and processes, but that the original aims of the Reforms have not yet been fully met. The Monitoring Group's

assessment is that opportunities exist for refinements and further improvements to enhance standard setting in the public interest. These opportunities are described in the remainder of this Section. These recommendations do not emphasize the work of the Education Board given the focus during the past five years by Monitoring Group members on Audit and Ethics standards because they have a more direct effect on the conduct of financial statement audits. Nonetheless, the Monitoring Group acknowledges the importance to serving the public interest of auditors' educational qualifications and thus notes the future anticipated work of the Education Board.

IFAC Reform Opportunities for Further Improvement

Role of Technical Advisors to Board Members

Observation: Technical Advisors are the persons who are assigned to inform and advise individual Board members. Most Board members choose to have a Technical Advisor. Often Technical Advisors are employed in the audit profession, most typically by the larger audit firms. Technical Advisors sit “at the table with privilege of the floor with the consent of the Board member he or she advises” and participate actively in Board discussions. At times Technical Advisors are former Board members and therefore are very familiar with Board projects and active in Board discussions.

Implications: The use of Technical Advisors both potentially enhances and complicates the Board deliberations. It is understandable that expert technical support is needed in a standard-setting process; however, if Technical Advisors have very active roles, they effectively multiply the number of Board members involved in decision making. Because Technical Advisors are often experienced professionals employed by audit firms, they multiply the effects of those firms' perspectives in the standard-setting process.

Recommendation 5: The Monitoring Group recommends that IFAC change the manner in which expert technical information and support is made available to the Boards. This would make it clearer that the Board members themselves, and not the Technical Advisors, are the principals in the Board's discussions, deliberations and decision making.

Participation of Audit and Ethics Board Members in Board Meetings

Observation: A particular challenge in a Board's deliberations is to maximize the understanding and participation of all Board members in Board discussions and therefore enhance the dynamics of the Board meeting process. The manner in which Board proposals are developed—that is, by a Task Force which brings the proposals to the Board for discussion—can place Board members who are not on the Task

Force at an informational disadvantage because they have not had occasion to be as involved in studying the issue.

Implications: Upfront involvement by all Board members could be facilitated if presentations about the subject matter are an initial process step which occurs before a Board Task Force begins drafting or revising a Standard. Such presentations would enable all members of the Boards to give direction to a Task Force at the outset of a project. Doing so might encourage and facilitate more interaction among practitioner and non-practitioner Board members on the merits of an individual standard's issues as well as inform and increase the understanding of Board members from all countries.

Recommendation 6: The Monitoring Group recommends that IFAC institute a practice among all of its Boards whereby they invite both Task Force members and external guest speakers—who might be users, members of auditor oversight bodies, regulators and other public interest representatives, or technical subject matter experts—to regularly conduct technical sessions for all Board members on key issues that are on the Board's agenda.

Role of the Audit and Ethics Boards' Consultative Advisory Groups

Observation: Input from the CAGs to the Boards was one of the features of the Reforms designed to increase external participation in the standard-setting work. The Terms of Reference of each CAG describe the approach for receiving this input. External participation in providing such input has in fact increased through the operation of the CAGs; however, over the last years there appears to have been a continued expansion of expectations regarding the contribution of the CAGs to the standard-setting process. Monitoring Group members have directly observed this for the Audit and Ethics Board CAGs. As an example, there seems to be a perception that the CAGs serve as the guardian of technical content in standards, ascribing to the CAGs more of a technical signoff or governance role than the broad technical advisory input role contemplated in the Reforms. The CAGs were designed to be bodies that provide a wide range of useful technical advisory input on standards issues, and may also at times be able to alert the Boards to additional matters that need attention. They do, in fact, carry out this role as evidenced by the lively debate at CAG meetings, subsequent discussion by the Boards of points raised by CAG members, a feedback mechanism from the Boards to the CAGs, and so forth. The CAGs were not, however, constituted in terms of either composition or procedures such that they or their Chairs or members should verify how issues are processed or resolved, the resulting quality of the standards, or the completeness of the steps of the associated due process.

Implications: Differences in understanding of and communications about the role of the Audit and Ethics Board CAGs could lead to a false impression and mistakes in fact about what is contributed by the CAG function. This could give the appearance of a greater degree of credibility to audit standards and the Ethics Code than is warranted; an implied positive assurance with respect to their content and the due process steps taken to handle issues raised by constituents.

Recommendation 7: The Monitoring Group recommends that IFAC revise the manner in which the CAGs determine their agenda items, the manner in which discussion matters are presented to the CAGs, and the manner in which the CAG input is summarized and presented to Board members so that the approaches used do not appear to go beyond the CAG's technical advisory input role.

Meetings of the Audit and Ethics Boards' Consultative Advisory Groups

Observation: It is evident that valuable insight from the comments of and interchange among CAG members can contribute to the standard-setting efforts of the Boards. However, one difficulty with the manner in which the Audit and Ethics Board CAGs operate relates to the quantity of meeting papers that are put to the CAG members. The amount is often very voluminous; for example, equaling or exceeding the volume of papers for a Board decision-making meeting. Further, it is not unusual for CAG papers to sometimes arrive only days or one or two weeks before a CAG meeting. This does not provide sufficient time to enable CAG members to read the papers and consult within their member organizations, thus providing the full potential benefit of informed external participation and the opportunity for a CAG member to fulfill his or her responsibilities.

A second difficulty is that the timing of CAG and Board meetings is such that each CAG meeting occurs shortly before the next Board meeting. This has been the practice so that CAG members may review and comment on certain papers that are being prepared for that forthcoming Board meeting. However, because the Audit and Ethics Board meeting occurs shortly thereafter, it is usually the case that the CAG meeting minutes are not available at the time of those meetings. Thus, Board members often receive summary oral reports, typically relayed by either the CAG Chair or the Board Chair who attended the CAG meeting. Although comprehensive minutes of the CAG meetings are reviewed by the CAG at a later time, the minutes often do not reach the Board members until some decisions have been made to which the record of discussions would have been relevant.

Implications: These difficult circumstances limit the effectiveness of the CAG meeting process and the CAG members in providing the most effective input into Board deliberations. Further, the discussions at a CAG meeting are often summarized as "the CAG members did not object" or "the CAG members did

not express any additional views” or “no other CAG members had comments.” All of these phrases sound quite positive and supportive given that often CAG members cannot realistically consult within their CAG member organizations given the time they are allowed.

Recommendation 8: The Monitoring Group recommends that IFAC revise the approach to CAG meeting content to provide for a more realistic and effective participation approach on the part of CAG members and revise the approach to the CAG meeting process to provide for the submission of final CAG meeting minutes to the Board members before the Board meeting in which they discuss the related topics.

Analysis of Comment Letters

Observation: The Boards’ standard-setting processes include public exposure of all proposed standards, the posting on the IFAC website of comment letters that are received, and organized processes to summarize the comment letters on a particular proposal for consideration by that project’s Task Force and for consideration by the CAGs of matters on which views are more divided. The comment letter summaries are made available to all Board members. The Monitoring Group understands that comment letters are routinely read by project Task Force members and the letters are sometimes also read by Board members who are not members of a project’s Task Force.

Implications: The Monitoring Group’s experience with this comment letter summary process shows that at times only short Board meeting time slots are allowed for commentary to be made to all Board members on points that were made in stakeholder comment letters. Further, these reports at times focus more on the quantity of commenters expressing certain views than on the groupings of comments by type of commenter, thus there may not be enough recognition of various stakeholder perspectives. User and regulator comment letters are almost always outnumbered greatly by letters from members of the audit profession. There are seldom summaries of comments grouped by stakeholder to aid in the consideration of various perspectives on a standard’s issue according to the role in the capital markets of the commenter.

Recommendation 9: The Monitoring Group recommends that IFAC change how comment letter input is summarized and provided to Board members so that the necessary amount of time is allotted to discuss a summary that highlights the arguments made; the roles of the submitters; the frequency with which the point was raised; and whether the Board’s Task Force has taken up the input in the manner recommended, and why.

Feedback on the Monitoring Group Member’s Input to the Boards

Observation: As provided for in the Reforms, various Monitoring Group members have provided input to the Audit and Ethics Boards as they worked to improve the auditing and assurance standards and the Code of Ethics, respectively. These inputs were provided through participation in Task Forces, participation in the CAGs, submission of comment letters on proposals, and through informal meetings and discussions with the Board Chairs and the associated IFAC staff. As might be the case with any standard-setting committee, the Boards have not followed all of this advice in making decisions. Section 3.2 of the Reforms, however, indicates that a standard-setting Board should give strong consideration to Monitoring Group member comments, and, if the comment is not to be taken up in the final Standard, should explain to the relevant Monitoring Group member the reasons for that decision. Most commonly the Audit and Ethics Boards have in essence provided this feedback as part of reporting at the associated Board's CAG meeting on the Board's handling of matters raised in previous CAG meetings. One drawback of utilizing such a public group meeting to provide feedback to Monitoring Group members on their individual advice is that meeting time and agenda constraints prevent this feedback from being complete and specific to the Monitoring Group member who provided the advice and there is no practical opportunity for mutual discussion. A further drawback is that this approach is not designed to encompass matters raised in Monitoring Group member comment letters unless those matters were also discussed at a CAG meeting.

Implications: Providing for a mutual discussion of potential differing views on a matter has the benefits of both groups better understanding the factors each has identified and the trade-offs each is evaluating in drawing their conclusions. These discussions are also helpful in identifying whether there is a potential "third way" that is satisfactory to all involved. Regardless of the outcome of such discussions, the Boards would have a better appreciation for some of the aspects of their standards that run counter to what is seen as acceptable by regulators and/or other public interest organizations, and why.

Recommendation 10: The Monitoring Group recommends that IFAC put in place the arrangements for the Boards to provide direct feedback to individual Monitoring Group members regarding a member's input to the Boards if it does not appear that the Boards will take up the input in a final Standard in the manner that the Monitoring Group member recommended.

Finalization of Standards

Observation: The process of finalizing decisions on a Standard or other pronouncement is not always clear and explicit to public observers at the Board meetings and to others who monitor the standard setting of the Audit and Ethics Boards. Sometimes a number of changes will be discussed, even debated,

and it is not completely clear how a discussion has been resolved. And on occasion, following a discussion of many points for which the resolution is not completely clear, Board members will be asked “Does anyone object to proceeding on the basis of what we have discussed?” At other times relatively significant changes are agreed to be made to a draft Standard early during the week of a Board meeting with the revised wording considered, and if needed revised, and then approved by Board members a couple of days later. It is sometimes difficult for even those members of the public who are attending the Board meeting in person to keep up with these changes.

Implications: As deliberations on a standard are concluding and then ultimately when a final Standard is issued, ambiguity regarding how matters have been resolved can impair understanding among Board members and Board transparency for observers and those who use the final Standards. Further, if ambiguity does exist or drafting work is necessary, then framing the summary of a Board discussion as an expression of a view by the Board may not be practicable.

Recommendation 11: The Monitoring Group recommends that IFAC implement refinements to the manner in which a Standard or other pronouncement comes together—for example, by utilizing feedback statements—so there is a better opportunity for its constituents to anticipate what the content will, and then does, encompass.

Voting by Board Members

Observation: The Board member voting process was not addressed in the Reforms and thus the Reforms did not consider the use of proxy voting. The Terms of Reference for Board members permit those who miss a meeting or leave a meeting early to give a proxy for their vote to another Board member or even to a Technical Advisor.

Implications: This proxy voting practice can result in the vote of a Board member who misses a meeting or leaves a meeting early to be cast without the Board member being present for the full discussion of the issues involved or, if a document under consideration is revised within the several days of the Board meeting, without his or her knowledge of other’s comments on the final version. Accordingly, the Monitoring Group believes the use of proxy voting to be a less than optimally effective practice for a standard setter.

Recommendation 12: The Monitoring Group recommends that IFAC remove the provision for proxy voting by the Boards. Correspondingly, IFAC would likely need to think about the timing and manner in

which Board members themselves vote on a final document—either in or outside of Board meetings—and how the Board reports the results.

Section III. Implementation of the Standards

IFAC Reform Implementation Assessment

The Reforms provided for IFAC to establish an IFAC member compliance function to focus on long-term improvement in the practice of accounting in all spheres of its members' professional activity. The compliance program's primary objective is one of encouragement to and improvement by IFAC members. Through a process of self-assessment and gap analysis, followed by the development and implementation of an action plan by each member body, it is IFAC's objective to improve each member's capacity to support and enforce compliance with the standards produced by the IFAC boards and committees and with International Financial Reporting Standards. The Statements of Membership Obligations (SMOs) issued by the IFAC Board establish requirements for, among other things, members and associates to promote, incorporate, and assist in implementing these international standards. The information gathered in this member compliance program forms the basis for evaluating whether members and associates have used their best endeavors to meet the SMO requirements.

The Reforms placed this IFAC member compliance function within the oversight of the PIOB. To help implement this program, the Reforms established the five-member (now six-member) IFAC Compliance Advisory Panel to take the lead in this area; management of this function is the responsibility of the IFAC staff. IFAC and the PIOB, respectively, have implemented these provisions. This Compliance Advisory Panel oversees the work to monitor compliance and to create mechanisms for investigation and discipline of instances of non-compliance with standards at a national level. Compliance of each member body is communicated via publication of its self-assessment on the IFAC web site.

Although these efforts associated with IFAC member compliance have a public interest connection they are, at least at this stage of their development, largely oriented toward serving IFAC as a membership organization. Accordingly, the Monitoring Group did not assess this area beyond understanding the parameters of the program and noting that it is now operational. Thus, the Monitoring Group was not in a position to identify any associated opportunities for further improvement as part of this Effectiveness Review. The Monitoring Group members do, however, acknowledge the benefits of member compliance assessment programs thus the Monitoring Group also takes note of the future anticipated work of the Compliance Advisory Panel.

Section IV. Oversight

IFAC Reform Implementation Assessment

The PIOB has accomplished a great deal in its first five years in supporting the aims of the Reforms with respect to making changes that could improve audit quality. In the Reforms the PIOB was given various specified responsibilities which can broadly be described as overseeing the public interest activities of IFAC related to auditing. This work has encompassed overseeing the member appointment processes and deliberative due processes associated with the three Boards and the activities of its member compliance program.

To carry out its responsibilities the PIOB has established its operating procedures and has also carried out a wide range of legal and organizational start-up activities, including incorporation as a Foundation in Spain, the selection and hiring of staff, and the development of budgetary and administrative processes that enable it to operate separately and independently from IFAC. The PIOB meets at least four times a year. The PIOB prepares an annual Public Report and disseminates information about itself on its website. The Monitoring Group renewed the terms of the initial PIOB members, thus most PIOB members are now serving their second three-year term.

In terms of its oversight responsibilities, the PIOB oversaw creation of new Terms of Reference and operating procedures for the three Boards as well as the process of nominations to each Board. On an ongoing basis it approves the new members of the Boards, including their Chairs, as well as the new members of and Chairs of each CAG. The PIOB has instituted procedures to verify that certain steps have taken place within the due process of the standard-setting activities with the aim of satisfying itself that the procedures ensure that the views of stakeholders are sought and considered and that the Boards are accountable for the dispositions of those views. Because the PIOB provides oversight and not management, pursuant to the Reforms it does not have the right to require changes in processes although it can approve or reject changes that are proposed. Pursuant to the Reforms it also does not have the right to require—albeit it can suggest—that particular projects are taken on the Boards’ agendas, although it may recommend that a matter be taken up and is entitled to receive an explanation if this does not occur. Likewise, the PIOB’s responsibilities do not entail providing technical input or suggestions on the design or content of individual standards or approving the content of proposed or final Standards. Under the Reforms the PIOB does, however, have a responsibility to evaluate the adequacy of funding provided to support the three Boards and the Compliance Advisory Panel. The Monitoring Group acknowledges that the standard-setting Boards have received resources beyond those provided for in the Reforms, such as

travel subsidies for developing country Board members. The Monitoring Group also acknowledges that what constitutes adequate funding is a matter of significant judgment.

Under the Reforms, provision was made for the possibility that in the future the PIOB's oversight role could extend to other public interest activities of IFAC that relate to auditing. To-date the PIOB has not had occasion to make use of this provision. Further, the Reforms specified that the PIOB shall not oversee the accounting standard setting activities of IFAC's Public Sector Committee (now named the International Public Sector Accounting Standards Board). In its self-assessment for this Effectiveness Review IFAC did, however, raise the possibility that this prohibition be removed.

The implementation experiences of both the PIOB and Monitoring Group members in the years since the PIOB's formation have provided a base of information that can be used to build on past accomplishments and enhance its future public interest contributions. These experiences and resulting recommendations are described in the remainder of this Section.

IFAC Reform Opportunities for Further Improvement

Role of the PIOB Members in the PIOB's Oversight Work

Observation: The primary strategy used by the PIOB to conduct oversight of the due process of the three Boards is to have a member of the PIOB attend nearly all of the Board and associated CAG meetings, with individual PIOB members attending particular meetings on a rotating basis. Some PIOB members are able to attend more meetings than others depending upon the nature of their commitments outside of their PIOB work. Broadly speaking, this deployment of PIOB members brings to the oversight process their personal standing derived from their broad background and significant experience. These qualities enable PIOB members to credibly offer observations and insights regarding due process at a broad and strategic level—such as how a Board sets and prioritizes its agenda and whether among the three Boards this is complementary—but less regarding the consultation, deliberation and evaluation processes applied to each of the individual technical issues. The costs associated with deploying PIOB members in this way are their daily meeting stipends and the costs of travel.

Implications: The PIOB's current approach to oversight brings the insight of broadly experienced PIOB members to the standard-setting process but it also raises a question about the level of oversight of the processes associated with resolving individual technical issues. Oversight of the resolution of a technical issue encompasses the thoroughness and objectivity of the processes used by the Boards to resolve an issue; in particular, to address the points raised by constituents in their comment letters. Under the design

of the Reforms this technical issue resolution oversight role is not filled by the CAGs since the Reforms call upon them to supply advice to—as opposed to do the necessary work to certify—the standard-setting processes. Further, this role is not filled by the Monitoring Group nor its members, as the Reforms gave Monitoring Group members the opportunity to provide input to the Boards and receive associated feedback from the Boards, but not to certify the processes associated with their work.

Recommendation 13: The Monitoring Group will consult with the PIOB and speak to IFAC to discern how to most effectively and efficiently draw upon and focus the talents of the PIOB members in carrying out the PIOB’s core activity, its oversight work.

Role of the PIOB Staff Members in the PIOB’s Oversight Work

Observation: The oversight fieldwork performed by the PIOB members has been complemented in some cases by attendance at Board and CAG meetings by the PIOB staff.

Implications: Deploying PIOB staff brings to the oversight process their available time and orientation to familiarize themselves with all the technical issues in the projects and the points made in the comment letters, thus focusing the PIOB’s fieldwork to the consultation, deliberation, evaluation and constituent feedback processes by which the Board members identify and consider individual technical issues.

Recommendation 14: The Monitoring Group will consult with the PIOB regarding how best to orient the efforts of the PIOB staff members to technical issue resolution in performing oversight fieldwork, with an emphasis on starting their involvement as early as possible within the life cycle of a project and following it through to the points of considering comment letters, taking decisions, and then providing feedback.

Diversity among the PIOB Members

Observation: The Monitoring Group appointed the initial slate of PIOB members, and all but two have been able to continue to serve for a renewed second term. The two openings have been filled by appointments since then. The manner in which the Monitoring Group selects PIOB members is specified as part of the Monitoring Group’s Charter. In summary, the Basel Committee, the European Commission, IAIS, IOSCO and the World Bank are each responsible to nominate a specified number of individuals who have a background that would contribute to public interest oversight. These individuals can be either currently employed inside Monitoring Group member organizations or be from outside those organizations. In addition, one PIOB Member is to have recent and significant auditing experience in the private sector and is selected by the Monitoring Group from among candidates recommended by IFAC.

Implications: The implications of each Monitoring Group member identifying nominees and doing so largely with reference to an individual's professional background is that other dimensions of diversity—such as geographic affiliation—may not always be directly coordinated by the Monitoring Group's Nominating Committee for PIOB members. This is evident among the current PIOB, which lacks a complete geographic balance among its members. Another implication of the composition of the current PIOB is that the terms of all of its members expire together in 2011. In the longer term, perpetuation of an approach to establishing PIOB member terms that essentially makes the entire PIOB one cohort runs the risk of less opportunity for continuous input of a fresh perspective.

Recommendation 15: The Monitoring Group will take a broader approach to identifying and appointing the next set of PIOB members such that factors related to geographical background, staggering of membership terms and other aspects of diversity are considered.

Funding of the PIOB

Observation: Under the Reforms the total amount the PIOB would potentially spend each year on its oversight work—originally USD 1.5 million with future adjustments for inflation and currency fluctuations—was agreed between IFAC and the Monitoring Group. This amount was (and continues to be) underwritten primarily through a “no conditions attached” guarantee from IFAC. The funds to support this guarantee are contributions IFAC collects from its members and remits for the benefit of the PIOB in a “blind trust” type arrangement. Under this arrangement IFAC does not have a role in deciding whether and how the PIOB spends its annual funding. The Monitoring Group fulfills an intermediary role in reviewing the reasonableness of how the PIOB will spend the total amount provided. This arrangement is in effect until early 2015. The PIOB also receives donations-in-kind of its office facilities from the Government of Spain and the assumption of some Board member travel costs and stipends from certain Basel Committee member authorities and from the World Bank. Associated with its initial operations the PIOB also received cash contributions in 2006 and 2007 from the U.S. Federal Reserve and from the World Bank. It also received contributions of legal services from the IAIS and 30,000 Euros from the PIOB founders (the Basel Committee, the IAIS and IOSCO) to form the minimum endowment needed to establish the PIOB under Spanish law. Further, the European Commission has recently made provisions to provide 1.2 million Euros over the period 2010 - 2013 under defined conditions, including diversification of the sources of PIOB funding.

Implications: This combination of funding sources for the PIOB raises questions in terms of trade-offs between the reliability, adequacy and independence of the sources. While the current approach has come

together via the results of best efforts from various parties, and is likely sustainable in the shorter term, a question that arises is whether for the long term it would be better if the PIOB were funded with clear public monies. On the other hand, at present the three Boards endeavor to fulfill the role of producing standards that serve the public interest but within a private sector organization whose stated mission involves other activities, for example, strengthening the worldwide accountancy profession. The current PIOB funding from IFAC members via the “blind trust” type of arrangement that is in place reflects this duality.

Recommendation 16: The Monitoring Group will, in consultation with the PIOB and IFAC, determine what longer term neutral funding arrangements can be put in place for the PIOB.

Section V. Monitoring

IFAC Reform Implementation Assessment

The Reforms contained provisions calling for the identified group of international public interest organizations to establish operations as the “Monitoring Group” so that they would have an aegis within which the organizations could monitor the PIOB’s oversight work and the overall operation of the Reforms. The Reforms also gave the individual Monitoring Group members the opportunity, but not the obligation, to provide advisory input to the Boards during the normal course of their work. The Monitoring Group and its members, respectively, have implemented these provisions.

The Monitoring Group began official operations at the time the Reforms were finalized, in November 2003, although its members had met informally on previous occasions. In 2004 the Monitoring Group selected the PIOB Chair and its members, and the full PIOB commenced operation in February 2005. In 2007 the Monitoring Group added an intermediary role in reviewing the PIOB’s annual oversight budget. In due course the Monitoring Group documented these and other provisions of its operations in its Charter. It developed this Charter in 2008 and adopted it in May 2009.

As provided for in the Reforms, the Monitoring Group’s responsibilities entail selecting the PIOB members and monitoring the PIOB oversight activities relative to their principal purpose as well as ongoing communications with IFAC through an IFAC Regulatory Liaison Group (RLG). The Reforms envisioned that carrying out this work would entail Monitoring Group communication with the PIOB and/or its staff to provide updates regarding the regulatory environment as well as an annual meeting with the RLG to provide an ongoing dialogue between regulators and the international accountancy profession. The Monitoring Group has communicated with the PIOB in meetings with its Chair and Secretary

General as well as by Monitoring Group member staffs interacting with its Secretary General. The Monitoring Group has communicated with the RLG in annual discussions.

The opportunity for technical advisory input to the three Boards that the Reforms granted to Monitoring Group members involved the opportunity to participate in their CAGs, submit comment letters on proposals, and be available to meet with the Boards. All the Monitoring Group member organizations are members of the Audit and Ethics Board CAGs and—while not members of the Education Board CAG at this time—have that opportunity. Monitoring Group member organizations have submitted comment letters on Board proposals as they judged appropriate and have had a number of meetings with the Boards, typically via a meeting with its Chair and the associated IFAC staff member(s).

The implementation experiences of the Monitoring Group have provided a base of information that can be used to build on past accomplishments and enhance its future public contributions. These experiences and resulting recommendations are described in the remainder of this Section.

IFAC Reform Opportunities for Further Improvement

Interaction between the Monitoring Group and the PIOB

Observation: In monitoring the PIOB's oversight work the Monitoring Group has sought to avoid any appearance of duplicating the PIOB's oversight role, and has endeavored to provide a degree of distance from the PIOB's operations so that the PIOB might organize itself and "find its own voice" with respect to how it carried out its role. Accordingly, the form of the Monitoring Group's communication with the PIOB has relied primarily upon discussions with the PIOB Chair and Secretary General at meetings of the Monitoring Group, and outside these meetings by the Monitoring Group Chair for other matters that arose. Periodically, Monitoring Group member staff has also had discussions with the PIOB Secretary General and staff. While the logistics of this interaction benefited from being kept simple, the trade-off involved in this approach is that the Monitoring Group and the full PIOB have not had the opportunity to establish a more comprehensive and exploratory dialogue about current and future developments mutually affecting the PIOB and Monitoring Group members in their respective work. Such a dialogue could benefit both parties for considering the role the Monitoring Group or its members should have in the governance of the PIOB Foundation, including evaluating a more formally documented link between the Monitoring Group and the PIOB; understanding mutual expectations between the Monitoring Group and the PIOB; and better defining and providing for the Monitoring Group's review of the PIOB's annual oversight costs.

Implications: The initial Monitoring Group approach for communication between the Monitoring Group and the PIOB—while viewed as appropriate and desirable in the PIOB’s start-up phase and early operations—may not be sufficient to support an ongoing, sustainable and comprehensive relationship that will serve the public interest, particularly if the IFAC standards begin to become more widely utilized around the world. A deeper, more sustainable and comprehensive communication approach would also help to set a good foundation for continuity in ongoing Monitoring Group and PIOB operations as personnel changes occur due to term expirations for the initial PIOB members and the inevitable eventual turnover of personnel at Monitoring Group member organizations.

Recommendation 17: The Monitoring Group will consult with the PIOB as it looks at how it can best bring efficiency and effectiveness to its interactions with the PIOB on governance of the PIOB Foundation, the PIOB’s oversight work, and the Monitoring Group’s review of PIOB oversight costs. Regardless, the Monitoring Group and the PIOB will carry out the provision in the Monitoring Group’s Charter that it meet with the PIOB by having the appropriate mix of individuals from all the Monitoring Group member and observer organizations meet with the full PIOB (or based upon practical considerations, at least a substantial majority of its members) at least once a year for a strategic discussion on market and regulatory developments, opportunities and challenges for the future, and opportunities for mutual improvement.

Longer Term Operation of the Monitoring Group

Observation: The Monitoring Group notes that many events have transpired in the landscape of the international capital markets and financial reporting environment since its members came together in 2002, including developments and features that have come to be associated with credible international standard-setting functions and related oversight and monitoring. These developments include establishment of the Monitoring Board for the International Accounting Standards Committee Foundation (IASCF); the development and formal establishment of IFIAR; and the addition of several emerging market country members to various international groups. Further, the roles and responsibilities of Monitoring Group members have evolved; for example, the Financial Stability Forum has become the Financial Stability Board. We think the confluence of these developments may require additional clarity as to how the Monitoring Group fits into the mosaic of international regulation and financial reporting organizations and infrastructure.

Implications: The contribution that the work of the Monitoring Group can make to market confidence will be enhanced if the Monitoring Group’s role is well crafted, well articulated, easily understood and

accepted by all stakeholders. Such a role encompasses not only the Monitoring Group's organizational provisions and membership, but also its accessibility and the efficiency and effectiveness of its operating procedures.

Recommendation 18: Immediately following its completion of this Effectiveness Review the Monitoring Group will undertake to further assess its role and its approach to monitoring in light of its members' experiences; specifically, capital market developments and events since the time of the Reforms as well as what the Monitoring Group learns from completing this review. The Monitoring Group expects that its work will be conducted at the same time as the Monitoring Board of the IASCF will conduct its own structure review of its organization, resulting in possible synergies to the Monitoring Group's efforts.

List of the Monitoring Group's Preliminary Recommendations

This is a compilation of the Monitoring Group's preliminary recommendations, which are contained under the *Opportunities for Further Improvement* headings within Sections I thru V of this Paper. The compilation is presented for convenience, as the preliminary recommendations should be considered in conjunction with the observations and implications that accompany each recommendation in the Paper.

Composition of the Standard-Setting Boards

Recommendation 1: The Monitoring Group recommends that IFAC appoint a mix of Audit Board and Ethics Board members appropriate to the need for both technical competence and objectivity in the work of each respective Board such that there is parity—or perhaps even a majority—of Board members with professional career experience that substantively goes beyond that of an auditor.

Recommendation 2: The Monitoring Group recommends that IFAC discontinue the practice of reserving a specific allocation of Audit Board and Ethics Board seats for a particular type of background—in this case for FOF nominees—and instead consider FOF nominees among all the candidates it evaluates in deciding upon the optimal mix of Board members based upon all the relevant dimensions of balance and diversity.

Recommendation 3: The Monitoring Group recommends that IFAC explore financial measures, such as reasonable stipends if they would not raise questions about independence and objectivity, to accompany travel cost reimbursement for Board members who are public members that are employed by an organization that cannot provide financial support of their participation as a Board member.

Recommendation 4: The Monitoring Group will evaluate how the expertise and perspective of those who are or have been auditors is best included in setting ethics and auditor independence standards, and thus whether the trade-offs indicate it would be advisable for other structures for ethics and independence standard setting—or at least for the composition of the Ethics Board—to be utilized.

Operating Procedures of the Standard-Setting Boards

Recommendation 5: The Monitoring Group recommends that IFAC change the manner in which expert technical information and support is made available to the Boards. This would make it clearer that the Board members themselves, and not the Technical Advisors, are the principals in the Board's discussions, deliberations and decision making.

Recommendation 6: The Monitoring Group recommends that IFAC institute a practice among all of its Boards whereby they invite both Task Force members and external guest speakers—who might be users, members of auditor oversight bodies, regulators and other public interest representatives, or technical subject matter experts—to regularly conduct technical sessions for all Board members on key issues that are on the Board’s agenda.

Recommendation 7: The Monitoring Group recommends that IFAC revise the manner in which the CAGs determine their agenda items, the manner in which discussion matters are presented to the CAGs, and the manner in which the CAG input is summarized and presented to Board members so that the approaches used do not appear to go beyond the CAG’s technical advisory input role.

Recommendation 8: The Monitoring Group recommends that IFAC revise the approach to CAG meeting content to provide for a more realistic and effective participation approach on the part of CAG members and revise the approach to the CAG meeting process to provide for the submission of final CAG meeting minutes to the Board members before the Board meeting in which they discuss the related topics.

Recommendation 9: The Monitoring Group recommends that IFAC change how comment letter input is summarized and provided to Board members so that the necessary amount of time is allotted to discuss a summary that highlights the arguments made; the roles of the submitters; the frequency with which the point was raised; and whether the Board’s Task Force has taken up the input in the manner recommended, and why.

Recommendation 10: The Monitoring Group recommends that IFAC put in place the arrangements for the Boards to provide direct feedback to individual Monitoring Group members regarding a member’s input to the Boards if it does not appear that the Boards will take up the input in a final Standard in the manner that the Monitoring Group member recommended.

Recommendation 11: The Monitoring Group recommends that IFAC implement refinements to the manner in which a Standard or other pronouncement comes together—for example, by utilizing feedback statements—so there is a better opportunity for its constituents to anticipate what the content will, and then does, encompass.

Recommendation 12: The Monitoring Group recommends that IFAC remove the provision for proxy voting by the Boards. Correspondingly, IFAC would likely need to think about the timing and manner in which Board members themselves vote on a final document—either in or outside of Board meetings—and how the Board reports the results.

Oversight

Recommendation 13: The Monitoring Group will consult with the PIOB and speak to IFAC to discern how to most effectively and efficiently draw upon and focus the talents of the PIOB members in carrying out the PIOB's core activity, its oversight work.

Recommendation 14: The Monitoring Group will consult with the PIOB regarding how best to orient the efforts of the PIOB staff members to technical issue resolution in performing oversight fieldwork, with an emphasis on starting their involvement as early as possible within the life cycle of a project and following it through to the points of considering comment letters, taking decisions, and then providing feedback.

Recommendation 15: The Monitoring Group will take a broader approach to identifying and appointing the next set of PIOB members such that factors related to geographical background, staggering of membership terms and other aspects of diversity are considered.

Recommendation 16: The Monitoring Group will, in consultation with the PIOB and IFAC, determine what longer term neutral funding arrangements can be put in place for the PIOB.

Monitoring

Recommendation 17: The Monitoring Group will consult with the PIOB as it looks at how it can best bring efficiency and effectiveness to its interactions with the PIOB on matters such as governance of the PIOB Foundation, the PIOB's oversight work and the Monitoring Group's review of PIOB oversight costs. Regardless, the Monitoring Group and the PIOB will carry out the provision in the Monitoring Group's Charter that it meet with the PIOB by having the appropriate mix of individuals from all the Monitoring Group member and observer organizations meet with the full PIOB (or based upon practical considerations, at least a substantial majority of its members) at least once a year for a strategic discussion on market and regulatory developments, opportunities and challenges for the future, and opportunities for mutual improvement.

Recommendation 18: Immediately following its completion of this Effectiveness Review the Monitoring Group will undertake to further assess its role and its approach to monitoring in light of its members' experiences; specifically, capital market developments and events since the time of the Reforms as well as what the Monitoring Group learns from completing this review. The Monitoring Group expects that its work will be conducted at the same time as the Monitoring Board of the IASCF will conduct its own structure review of its organization, resulting in possible synergies to the Monitoring Group's efforts.