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Comments to the Monitoring Group consultation paper “strengthen the governance and oversight of the international audit-related standard-setting boards in the public interest”

Dear Sir or Madam!

AFRAC encloses the comments to the Monitoring Group consultation paper which include the following aspects:

- Establishing a multi-stakeholder board
- Separate boards for (i) auditing and assurance and (ii) ethics
- Separate boards for oversight and standard-setting
- Support by expanded professional technical staff
- Support by Technical Advisory Groups
- New mechanism for collecting and allocating funding
- Remuneration of the board(s) members
- Adopting standards on the basis of a qualified majority
- A trustee body that serves as the guardian of the model

If you have any further questions, please do not hesitate to contact us.

Yours faithfully,

Romuald Bertl
Chairman

Enclosures

Attachment 1: General remarks
Attachment 2: Detailed responses

Attachment 1: General remarks

General remarks of AFRAC to the Monitoring Group consultation paper “Strengthen the governance and oversight of the international audit-related standard-setting boards in the public interest”

We understand that the proposed options of the Monitoring Group have been developed to strengthen the public interest in the standard-setting process and improve its responsiveness to user needs. A transparent and high-quality international standard-setting is of fundamental public interest. It is important that the standards affect the timeliness and relevance of standards/of the standard-setting process in order to support audit quality and user confidence.

The current model has definitely helped to create a framework and governance structure for the development and adoption of independent international standards. Nevertheless, we are of the opinion that the existing model design has unresolved vulnerabilities. In addition, there are various risks that weaken the legitimacy, the timeliness of the international standards and the credibility of standard-setting boards. Therefore, we favor a reform of the standard-setting model. We believe that a change is necessary and that we need to ensure that all key stakeholders can participate in standard-setting on an equal footing.

We broadly agree with the supporting principles set out in the consultation paper: independent, credible, cost effective, relevant, transparent and accountable, as well as with the additional point that, to be sustainable in the long term, long term secure funding, a clear long-term strategy and technical competence are necessary to support a demanding and growing workload.

In our opinion the following **core attributes** of a sustainable and credible standard setter are the basis for some of our most important comments:

- **Due process**, which must be perceived as fair, transparent and able to balance competing interests, without the influence of undue external intervention. Due process is failing, if the perception exists that there is a need for an oversight body to intervene or override due process in order to achieve standards set with due regard to the public interest.
- It is critical to implement **technical expertise** in the standard-setting process. Audit, assurance and ethics standards determine technical requirements and guidance for professionals and will only be effective if the professionals can achieve the objectives agreed-upon by the boards in a workable way and if standards are capable to evoke the desired behaviors of the professionals. That requires the involvement of those with deep insight in the matters concerned.
- **Balanced representation** on both the standard-setting board(s) and the oversight and governance body.
- A balanced and **sustainable funding** model that is equitable and free from conflicts of interest.

We propose to consider the following **structural changes**:

1. Establishing a **multi-stakeholder board** with an appropriate participation of all relevant stakeholders.
2. The board is responsible for the governance and adoption of international auditing and assurance standards. There should be **separate boards** responsible for setting (i) auditing and assurance and (ii) ethical standards (including independence).
3. The boards' operations need to be changed, so that their remit focuses more on strategic decisions and is less operable. **Oversight** and **standards development** need to be kept **separate**. The board has to reduce its involvement in standards development and wording. Thus, public perception about the board's contribution in this process also decreases. To have a truly multi-stakeholder standard-setting model, all key stakeholders can participate in the oversight and standard-setting on an equal footing to ensure representative diversity.
4. The work of the multi-stakeholder board should be supported by an **expanded professional technical staff** who can pursue project development and related stakeholder outreach.
5. **Technical Advisory Groups** need to be added, by which the board(s) can exercise its/their due diligence that appropriate technical challenges are addressed as options are considered and standards are drafted.
6. To ensure that the standard-setting reforms are successful a new mechanism for collecting and allocating **funding** of the board(s) will be necessary.
7. Furthermore, the **remuneration** of the board members needs to be adequate and fair.
8. The board should adopt standards on the basis of a **qualified majority**.
9. Our proposal for a robust governance model that complements a reformed standard-setting process would require a **trustee body** that serves as the guardian of such a model and its effectiveness on behalf of all stakeholders. This proposal is a step in the direction towards the IFRS Trustees in the IASB.

The proposed structural changes require the following points in **detail**:

1. Multi-stakeholder board

On the board a multi-stakeholder representation by all global standards' key stakeholders should be guaranteed. The board should include members with authority to adopt, regulate and enforce standards as well as people who benefit from the standards and use them. These members should not represent any specific group or organization. Furthermore, the composition of the board should take account of a representative geographic diversity that reflects the range of jurisdictions that adopt the standards and of a diversity of views to provide differing perspectives of the public interest. The members should be drawn from the following three key stakeholder groups and must be equally represented: users, regulators and auditors. Users should not be related to regulators and auditors. The partici-

pative people would be responsible for strategic decision-making and for giving direction to the staff concerning project development. They need to have a high character, expertise and respected reputation in order to gain respect across all key stakeholder.

2. Separate boards for (i) auditing and assurance and (ii) ethics

We support the retention of separate boards for (i) auditing and assurance and (ii) ethics (including independence). There may be various advantages due to this option. One benefit is that separate boards are more attractive to potential members who may have an area of expertise in one but not in all of the areas of a single board's remit. Furthermore, separate boards could also provide more time and resources to handle the work.

3. Separate boards for oversight and standard-setting

There should be separate roles for the oversight and governance, on the one hand, and for standard-setting and the technical competence, on the other hand. A future oversight body should be responsible for the governance and oversight of the standard-setting process. It should not intervene in the work of standard-setting but should (i) observe the due process and (ii) oversee that the model is robust, the relevant stakeholders have confidence and the standard-setting serves the public interest. It could be a self-standing organization akin to the IASB Board.

4. Expanded professional technical staff and 5. Technical Advisory Groups

The board as a whole needs to have sufficient strategic and technical competence to effectively administer the development of standards. The key safeguards we believe to be necessary for the proposed standard-setting board(s) and for its (their) operation include:

- **Technical Advisory Groups** need to be added, by which the board(s) can exercise its/their due diligence that appropriate technical challenges are addressed as options are considered and standards are drafted. Any board member – particularly non-practitioners – should ask as part of their due diligence: “Will this action/amendment achieve the objective we set out?”, “Are these requirements going to function?” and “What are the possible disadvantages?”.
- Highly competent professional technical staff and project task forces that include practitioners will be critical in order to lead project development. But, in our view, this is not enough. Repeatedly, experience in the current model demonstrates the importance of technical challenge to proposals to ensure they are robust and workable. Relying on discussion papers or exposure drafts alone may result in the need for multiple consultations and the process could be streamlined with more dialogue throughout the process.

6. Funding

The funding of standard-setting needs to be supported by a new model in order to address stakeholders' concerns as to their confidence in the standards. Furthermore, funding needs to be diversified as much as possible. However, primarily, there should be a good and clear estimation of the budget and the expected costs to secure the funding needed to cover it and to find out about the best way of diversifying the funding.

7. Remuneration

The board members should be remunerated at a level commensurate with comparable public interest corporate governance roles. The people in the standard-setting process need to be acknowledged for their skill, experience and knowledge.

8. Qualified majority

We agree that the board should adopt standards on the basis of a qualified majority. Although the current practice is a required reinforced majority, the proposals are usually approved unanimously. A qualified majority could allow the board to be more decisive, to avoid unnecessary delays and to prevent the exclusion of a group of stakeholders and, thus, standards, which are not generally accepted, may be eliminated. The required qualified majority would affect the timeliness and relevance of standards.

9. Trustee body

As discussed in more detail in our responses to the questions asked in the consultation in appendix 2, a robust governance model would require a trustee body that serves as the guardian of such a model and of its effectiveness on behalf of all stakeholders.

Conclusion:

Summarizing, we support the initiative to reform the standard-setting model. We are in favor of a remunerated multi-stakeholder strategic board with an appropriate participation of all relevant stakeholders. It will be supported by Technical Advisory Groups and expanded professional technical staff to have an appropriate technical expertise while writing the standards. The board will be responsible for the development and adoption of international auditing and assurance standards. The multi-stakeholder board, the professional staff and the technical input will ensure that all key stakeholders can participate in standard-setting on an equal footing. A trustee body serves as the guardian of the model and of its effectiveness on behalf of all stakeholders.

Attachment 2: Detailed responses

Our opinions on options for reform in detail and our answers to the questions of the Monitoring group are as follows:

(1) Key areas of concern

Question 1: Do you agree with the key areas of concern identified with the current standard setting model? Are there additional concerns that the Monitoring Group should consider?

- We agree with the following key areas of concern identified with the current standard-setting model:
 - The adverse effect on stakeholder confidence in the standards as a result of a perception of undue influence by the profession. Nobody, neither the profession, nor regulators, nor users should exercise undue influence on the boards.
 - If such undue influence exists, then there is a risk that standards are not developed fully in the public interest.

(2) Guided principles

Question 2: Do you agree with the overarching and supporting principles as articulated? Are there additional principles which the Monitoring Group should consider and why?

- In general, we agree with the overarching and supporting principles of the Monitoring Group.
- We would like to add the following missing aspect:
 - The oversight body should be responsible for the oversight of the standard-setting process.
 - It should not intervene in the work of the standard-setting but should (i) observe the due process and (ii) oversee that the model is robust, the relevant stakeholders have confidence and the standard-setting serves the public interest.

Question 3: Do you have other suggestions for inclusion in a framework for assessing whether a standard has been developed to represent the public interest? If so what are they?

- The right balance needs to be found when addressing the public interest in standard-setting. In standard-setting the quality of standards, applicability of standards in practice and their enforceability need to be balanced.
- Public interest is also about SMEs' audit as well as about the public sector and about other services and standards need to take into account their independence. It is not only about the audit of PIEs.

(3) Options for reform of the standard-setting boards

Question 4: Do you support establishing a single independent board, to develop and adopt auditing and assurance standards and ethical standards for auditors, or do you support the retention of separate boards for auditing and assurance and ethics? Please explain your reasoning.

We support the retention of separate boards for (i) auditing and assurance and (ii) ethics for the following reasons:

- One benefit is that separate boards are more attractive to potential members who may have an area of expertise in one but not in all of the areas of a single board's remit.
- Furthermore, separate boards could also provide more time and resources to handle the work.
- On the contrary, a single independent board for the development and adoption of auditing and assurance standards and ethical standards for auditors will require too much responsibility.

All in all, we are against a complex and costly model of standard-setting.

Question 5: Do you agree that responsibility for the development and adoption of educational standards and the IFAC compliance program should remain a responsibility of IFAC? If not why not?

- We agree that the development and adoption of educational standards should remain a competence of IFAC.

Question 6: Should IFAC retain responsibility for the development and adoption of ethical standards for professional accountants in business? Please explain your reasoning.

- Ethics is not only about independence and is not only relevant to audit and assurance.
- Ethical principles should be addressed and dealt together with principles of independence as they apply to audit, assurance and other services provided by professional accountants as well as by accountants in business.
- IFAC could retain responsibility for the development and adoption of ethical standards for professional accountants in business.

Question 7: Do you believe the Monitoring Group should consider any further options for reform in relation to the organization of the standard setting boards? If so please set these out in your response along with your rationale.

- We refer to our responses already given to previous questions, where we included further relevant considerations.

Question 8: Do you agree that the focus of the board should be more strategic in nature? And do you agree that the members of the board should be remunerated?

- The board's operations need to be changed, so that the remit focuses more on the strategic decisions and are less operable.

- The board has to reduce its involvement in standards development and wording. Thus, public perception about the board's contribution in this process also decreases.
- The work of the board should be supported by an expanded professional technical staff.
- The board should not intervene in the work of the standard-setting but should (i) observe the due process and (ii) oversee that the model is robust, the relevant stakeholders have confidence and the standard-setting serves the public interest.
- The board members should be remunerated at a level commensurate with comparable public interest corporate governance roles. The people in the standard-setting process need to be acknowledged for their skill, experience and knowledge. However, the funding for remuneration will only be secured, if funding will be supported by a new model.

Question 9: Do you agree that the board should adopt standards on the basis of a majority?

- We agree that the board should adopt standards on the basis of a qualified majority. A qualified majority could allow the board to be more decisive, to avoid unnecessary delays and to prevent the exclusion of a group of stakeholders and, thus, standards, which are not generally accepted, may be eliminated.

Question 10: Do you agree with changing the composition of the board to no fewer than twelve (or a larger number of) members; allowing both full time (one quarter?) and part-time (three quarters?) members? Or do you propose an alternative model? Are there other stakeholder groups that should also be included in the board membership, and are there any other factors that the Monitoring Group should take account of to ensure that the board has appropriate diversity and is representative of stakeholders?

- 12 members will not be enough to take account of a representative geographic diversity that reflects the range of jurisdictions that adopt the standards and of a diversity of views to provide differing perspectives of the public interest.
- On the board a multi-stakeholder representation by all global standards' key stakeholders should be guaranteed. To ensure this, the members should be drawn from the following key stakeholder groups and must be equally represented: users, regulators and auditors. In this context the category "users" may include any persons using and benefiting from the financial information being audited (e.g. such as "those charged with governance") or practitioners involved in the preparation of the financial information and similar groups. In other words, "users" should not be related to regulators and auditors.
- The board should include members with authority to adopt, regulate and enforce standards as well as people who benefit from the standards and use them.

Question 11: What skills or attributes should the Monitoring Group require of board members?

- The participative people need to have a high character, expertise and respected reputation in order to gain respect across all key stakeholder and in the standard-setting process.

- Furthermore, the composition of the board should take account of a representative geographic diversity that reflects the range of jurisdictions that adopt the standards and of a diversity of views to provide differing perspectives of the public interest.

Question 12: Do you agree to retain the concept of a CAG with the current role and focus, or should its remit and membership be changed, and if so, how?

- Having a governance and oversight body with a broad multi-stakeholder representation, as proposed from our side, we do not need to keep the CAG.
- However, technical advisory groups should support the work of the boards together with an enhanced staff.

Question 13: Do you agree that task forces used to undertake detailed development work should adhere to the public interest framework?

- We agree that small task forces or expert groups should undertake detailed development work.
- The work of the multi-stakeholder board should be supported by an expanded professional technical staff.
- It should be ensured that the technical capability of the staff remains up to date and fully aware of the needs of the market and the issues it needs to address.

Question 14: Do you agree with the changes proposed to the nomination process?

- Our proposal for a robust governance model that complements a reformed standard-setting process would require a trustee body that serves as the guardian of such a model and of its effectiveness on behalf of all stakeholders.

(4) Role of the PIOB

Question 15: Do you agree with the role and responsibilities of the PIOB as set out in this consultation? Should the PIOB be able to veto the adoption of a standard, or challenge the technical judgements made by the board in developing or revising standards? Are there further responsibilities that should be assigned to the PIOB to ensure that standards are set in the public interest?

- We think that the PIOB in itself needs to be reformed.
- The governance body and the oversight body need to be a multi-stakeholder board representing all relevant stakeholders.
- A future oversight board should be responsible for the governance and oversight of the standard-setting process. It should not intervene in work of the standard-setting but should (i) observe the due process and (ii) oversee that the model is robust, the relevant stakeholders have confidence and the standard-setting serves the public interest.
- There should be separate roles for the oversight and governance, on the one hand, and for standard-setting and the technical competence, on the other hand.

- We agree to the specific tasks of the new multi-stakeholder governance and oversight body to fund and approve the board's budget.
- Having a veto right would interfere with the standard-setting process. However, the governance and oversight body should only oversee the operations of the board and should not intervene in the work of the standard-setting. For these reasons, the PIOB or any other newly established oversight body should not be able to veto the adoption of a standard.
- There are no other responsibilities that should be assigned to the governance and oversight body.

Question 16: Do you agree with the option to remove IFAC representation from the PIOB?

- As the adoption of standards is voluntary, it is critical to establish trust in the standard-setting process. The new governance and oversight body should be a multi-stakeholder board to build confidence across all stakeholders.
- Thus, the auditing profession should be part of the multi-stakeholder board.

Question 17: Do you have suggestions regarding the composition of the PIOB to ensure that it is representative of non-practitioner stakeholders, and what skills and attributes should members of the PIOB be required to have?

- See questions 15 and 16.

Question 18: Do you believe that PIOB members should continue to be appointed through individual MG members or should PIOB members be identified through an open call for nominations from within MG member organizations, or do you have other suggestions regarding the nomination/appointment process?

- We believe that PIOB or other oversight body members should not be appointed through individual Monitoring Group members.
- An extra board ("board of trustees") should decide who should be appointed. Furthermore, the nomination process itself should be designed in a wider, more public and transparent way.
- The nomination process should include a call for nominations of people with authority to adopt standards, of those who regulate and enforce them and of those who benefit from and use the standards.
- Responses from key stakeholders' groups on nominations could provide useful feedback.

Question 19: Should PIOB oversight focus only on the independent standard setting board for auditing and assurance standards and ethical standards for auditors, or should it continue to oversee the work of other standard-setting boards (e.g. issuing educational standards and ethical standards for professional accountants in business) where they set standards in the public interest?

- We propose to leave considerations about the organisation of the oversight to IFAC.

(5) Role of the Monitoring Group

Question 20: Do you agree that the Monitoring Group should retain its current oversight role for the whole standard-setting and oversight process including monitoring the implementation and effectiveness of reforms, appointing PIOB members and monitoring its work, promoting high-quality standards and supporting public accountability?

- If the Monitoring Group and the PIOB remain, then there is a need for a clear distinction between the roles of the oversight bodies.

(6) Administration including standard-setting board staff

Question 21: Do you agree with the option to support the work of the standard setting board with an expanded professional technical staff? Are there specific skills that a new standard setting board should look to acquire?

- We agree with the proposed option to support the work of the standard-setting board by an expanded professional technical staff.
- A new standard-setting board should look to acquire more, better and longer term staff with appropriate technical and writing skills. It should be ensured that the technical capability of the staff remains up to date and fully aware of the needs of the market.

Question 22: Do you agree that permanent staff should be directly employed by the board?

- We agree that permanent staff should be directly employed by that board to which it is accountable.

(7) Process considerations

Question 23: Are there other areas in which the board could make process improvements – if so what are they?

- If the board decides that a standard needs to be revised or issued, clear objectives for its revision or issuance need to be made.
- The board should decide about the major projects that require fundamental changes and standards should be issued when they are needed. Further, the standards could be more timely and responsive to current developments and innovation in the market.
- The timeliness of standards should be improved in order to support audit quality and user confidence and it is necessary to have highly developed governance and standard-setting processes respecting legitimacy and due process.

(8) Funding

Question 24: Do you agree with the Monitoring Group that appropriate checks and balances can be put in place to mitigate any risk to the independence of the board as a result of it being funded in part by audit firms or the accountancy profession (e.g. independent approval of the budget by the PIOB, providing the funds to a separate foundation or the PIOB which would distribute the funds)?

- First, there should be a good and clear estimation of the budget and the expected costs to secure the funding needed to cover it and to find out about the best way of diversifying the funding.
- Funding needs to be diversified as much as possible. Potential contributors of funding could be the following groups: the public sector, audit firms, national standard setters, securities market regulators, large and small businesses, etc.
- Covering the costs by the accountancy profession on a sole basis cannot be in the public interest, as the profession would pay for the standards with which it will be evaluated. There is need for steps to broad-based funding within a foreseeable timeframe.

Question 25: Do you support the application of a "contractual" levy on the profession to fund the board and the PIOB? Over what period should that levy be set? Should the Monitoring Group consider any additional funding mechanisms, beyond those opt for in the paper, and if so what are they?

- As already mentioned, all relevant stakeholders need to be a part of the funding.
- Funding needs to be diversified as much as possible to address the perception of undue influence.
- Irrespective of the finally proposed funding mechanism, we need further information on expected costs before having an opinion about this proposal.

(9) Open questions

Question 26: In your view, are there any matters that the Monitoring Group should consider in implementation of the reforms? Please describe.

- The reform of the standard-setting board, of its operations as well as of the governance model needs to be an integrated package. As such, we do not support considerations of any graduated reform or a multiple step approach. It is vital to a successful implementation that the governance structure is reformed at the same time as the standard-setting board and its operations.
- However, any reforms need to be implemented over a transitional period and should have a clear timeline to ensure stability and to secure the quality of future standard-setting.

Question 27: Do you have any further comments or suggestions to make that the Monitoring Group should consider?

- We refer to already given responses to previous questions where we included further relevant considerations.