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Mr Gerben J. Everts
Chairman
Monitoring group
c/o IOSCO
Calle Oquendo 12
28006 Madrid
Spain

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Subject: Monitoring Group Consultation for strengthening the governance and oversight of the international audit-related standard-setting boards in the public interest

Dear Mr Everts,

The European Banking Authority (EBA) welcomes the opportunity to comment on the Monitoring Group ('MG') proposal for reforming the governance and oversight of the international audit-related standard-setting boards in the public interest.

The EBA has a strong interest in having sound and high quality auditing standards for the banking industry. These standards are key for market confidence and discipline and they contribute to banking institutions providing high quality prudential reporting to banking supervisors.

The EBA welcomes the proposal. The changes proposed by the MG are a first step in the right direction to improve the governance, effectiveness and relevance of the current international audit standard-setting process, as well as increase the independence and public accountability of standard-setting bodies. The EBA takes note that several aspects of the proposal, in particular as regards funding, membership of the bodies, public interest, roles and responsibilities of the PIOB and MG remain to be settled. The EBA encourages the MG to finalize its proposal by specifying further these remaining open aspects. Developing a comprehensive proposal would be beneficial for the second public consultation as envisaged in the consultation paper. However the EBA acknowledges that it will be difficult to execute all the changes involved in a single step, and therefore encourages the MG to set out a transition plan in the next consultation, showing how the entire set of changes will be broken down into steps and how and when they will be addressed and executed. That said, this should not hinder the changes that are agreed upon to be set in motion where possible.

The EBA considers it important that the next public consultation is launched on a proposal which further details, where it is possible, the expected roles, objectives, responsibilities, compositions,

and tasks of each of the bodies in the future standard-setting framework, and how all of them would interact. The EBA stands ready to provide further more detailed responses when a new proposal, together with a transition plan, a funding plan, and an impact assessment, is released by the MG for public consultation.

The EBA supports the establishment of an independent single and multi-stakeholder standard-setting board to develop and adopt the international auditing, assurance and ethical standards for auditors. It might be appropriate to expand and strengthen the role of the PIOB so as to carry out amongst other things a sound oversight over the standard-setting process and ensure its adherence to the public interest framework. This will contribute to mitigating the risk that auditing standards are developed without appropriate consideration of public interest. Standards that are not developed in the public interest will lack credibility, will not be high quality and may hamper further adoption of the standards by jurisdictions.

Public interest is an abstract concept the fulfillment of which is difficult to assess. Furthermore, unless the concept of public interest is understood, it will be difficult to ensure it is properly represented in the development of standards and all board members act in the public interest. That is why the EBA stresses the need to further specify the concept of public interest by explaining how public interest is best served in practical terms, in relation to both the due process and the content of the standard themselves, and by characterizing situations of breach of public interest and what action can be taken and by whom. The public interest framework should not be developed by the PIOB alone, given the risk of conflict of interests arising from the fact that the PIOB would define its own mission. The PIOB should be properly accountable to the MG, both in the development of a public interest framework and in its operation.

The future board should be supported by a permanent administrative and technical staff composed of experts able to discharge board members from all operational and procedural tasks. This staff should not be provided by audit firms and professional bodies. Instead, they should be employed, compensated and evaluated directly by the board so as to preserve the board's independence from the auditing and accounting professions.

To mitigate the risk of developing an overly complex structure, the mandates, resources and tasks assigned to each of the bodies involved in the standard setting process will have to be determined in a clear, detailed manner so as to avoid any risk of duplication of work or overlap of competences. The overall standard setting architecture should be as lean, simple and understandable as possible with a clearly established chain of responsibilities so as to ensure a successful new standard-setting framework and guarantee a transparent, fast and efficient development of the auditing standards. Given the probable interactions between the various bodies involved in the standard setting process, it would be useful to determine the rules governing their membership, resources, roles and responsibilities conjointly, if possible.

Funding will be crucial for the success of the reform and the EBA believes that the funding mechanism needs to be changed and set up in such a way that the actual or perceived independence of standard setting is not compromised. While being aware of the difficulties in implementing a sustainable, diversified funding mechanism in the short term, the EBA encourages the MG to continue carefully exploring all options with all relevant stakeholders by assessing feasibility, pros and cons of each option.

Our detailed comments on the consultation paper are set out in the Appendix.

If you have any questions regarding our comments, please do not hesitate to contact us.

Yours sincerely

[SIGNED]

Andrea Enria
For the EBA Board of Supervisors

Encl: Appendix

Appendix

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?

The EBA agrees that the current standard-setting model raises the following risks:

- risk of undue influence by the auditing and accounting professions
- risk that audit standards are not fully developed in the public interest
- risk that audit standards are not relevant and developed in a timely way

Particular attention should also be paid to the risk of auditing standards being of low quality (due to, for instance, lack of sufficient resources).

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

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 EBA agrees that the MG should be guided by the principles set out in the consultation paper except when the public interest principle is in conflict with the cost-efficiency principle, priority should be given to the public interest principle. However, in order to increase the confidence of users in financial statements, the MG should also build into the framework that auditing standards should be of high quality and enforceable.

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

The EBA is in favor of establishing a single board in charge of developing and adopting the international auditing, assurance and ethical standards for auditors for the following reasons:

- A single board would contribute to making ethics a permanent and noticeable feature of auditing and assurance standards; auditing, assurance and ethical standards are very closely related (the quality of audits depends on the conduct of auditors as well);
- A single board would eliminate risks which might arise from separate boards: risk of conflicts of competences, risk of insufficient coordination or communication between separate boards, risks of inconsistent or redundant provisions in both audit and ethical standards;
- A single board would ensure that auditing, assurance and ethical standards are subject to equal consideration from external stakeholders;
- A single board would ensure that the development of both audit and ethical standards is subject to similar process, while allowing for economies of scale;
- A single board remains compatible with an internal organization comprising separate divisions dedicated to the development of standards in specific areas (e.g. one board's division for auditing, another one for ethics);
- A single board could be justified by the synergies between auditing and ethical standards.

5. Do you agree that responsibility for the development and adoption of educational standards and the IFAC compliance programme should remain a responsibility of IFAC? If not, why not?

The EBA is of the view that the development and adoption of international educational standards should remain a responsibility of IFAC, provided that this does not interfere with the existing national rules applicable to auditors.

The IFAC could continue running the current international compliance programme aiming to ensure that its members comply with the standards.

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

The ethical responsibilities of the professional accountants in business are of critical importance in establishing reliable financial statements so satisfying the interests of a wide range of external stakeholders: investors, suppliers, customers, government, financial institutions and employees. As for auditors, professional accountants in business should act with objectivity, integrity, honesty,

and competence for delivering reliable financial statements. However, the EBA believes that the responsibility for developing and adopting ethical standards for professional accountants in business could remain in the remit of IFAC as the public interest concerns as regards accountants are less and to some extent different from those for auditors.

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.

No further options to be considered for reform.

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?

Focus of board members

The EBA considers that the board as a whole should be able to handle both strategic and technical matters, given the responsibility the board will have for issuing technical auditing standards. The board should be able to determine its strategic vision and set the pace for its future development, while ensuring that its organizational structure and resources are appropriate for implementing the set strategy. The board should also be able to deal with developments in the audit landscape and prioritize its projects.

Being sufficiently technical does not mean that the board members should be drafting auditing standards – the EBA agrees with the MG in this regard. The board members should be technically strong enough to provide technical direction, oversee the permanent technical staff, properly debate and give their consent to technical elements set out in the various papers (e.g. draft standards, draft consultation papers, draft annual work programmes) submitted to them for approval or discussion.

In any case, in order to be able to pay sufficient attention to strategic aspects or important technical issues, the board should be supported by a permanent administrative and technical staff composed of experts able to discharge board members from all operational and procedural tasks such as the drafting of standards, legal and quality checks, and the running of public consultations (see also our response to question 21).

Remuneration arrangements

The EBA believes that any remuneration arrangements of board members should be carefully designed, implemented and disclosed. The amounts of fees which would be awarded to board members should reflect the individual responsibilities and time commitment of each board member. Thus, additional fees could be granted to those taking further responsibilities such as the

chairperson or representing the board on additional standard-setting groups, and fees would vary depending on whether the person was a full-time or part-time board member. That apart, all board members should be paid the same amount because the expertise and time commitment are expected to be the same. Fees only based on meeting attendance should be discouraged. The remuneration policy and the amounts of fees should be subject to full disclosure. It is worth stressing that remuneration rules should be determined together with the membership of the board and funding arrangements.

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

The EBA is of the view that the board should strive for consensus upstream before taking its decisions. However, if consensus was not reachable, the chairperson should be allowed to initiate a voting procedure. The decision of the board should be taken by simple majority of its members, with dissenting members permitted to publish their dissenting views. Abstentions would not be counted as approvals or objections and would not be considered when computing the number of votes.

Each member (excluding observers) should have one vote. In order for the board to proceed to a vote, there should be a quorum of members with a right to vote (e.g. two-thirds as currently).

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?

Size of the board

The EBA does not have a strong view on the optimal size enabling the board to effectively lead the development of standards. The board should be large enough to have a broad range of skills and produce deep analyses and discussions, while being small enough to facilitate the exchanges of views among members.

Full-time versus part-time status

The EBA is of the view that the chairperson of the board should be full time, given his or her responsibilities for representing the board to the outside world and possible responsibilities for the day-to-day management of the structure. Some board members might not need to be full time, but should be able to allocate sufficient time to the board to perform their responsibilities properly.

The EBA also believes that sufficient attention should be paid to define what a ‘non-practitioner’ means in practice as well as an appropriate cooling-off period so as to ensure the independence of those who were previously practitioners.

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

The EBA considers that an appropriate balance of technical and strategic skills in both auditing and ethics should be required from board members.

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?

The concept of a Consultative Advisory Group, that would provide board members with opinion, advice or views on the various projects and deliverables in auditing, assurance and ethical areas, should be maintained. However, the existence of a CAG should not prevent the standard-setting board from conducting open public consultations. Collecting inputs from a broad range of stakeholders is paramount to the concept of addressing public interest issues by the board. In order to provide a diversity of views, the members of the CAG should be appointed to represent, in appropriate proportions, auditors, investors, preparers, academics as well as persons charged with governance. The role and position of the CAG in the upcoming governance structure should be carefully designed to ensure that all relevant inputs are provided in an appropriate manner during the process of development of standards.

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

The EBA considers that any task forces set up by the board should act in the public interest without undue influence from the auditing or accounting professions (as should all those involved in the entire standard setting process). If the board decided to set up task forces, their members should be suitably senior and have the necessary expertise and experience in the areas relevant to the tasks and deliverables to be provided. The interactions between the task forces and the permanent staff should also be considered so as to avoid any duplication of work.

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

The EBA considers it important to remove the IFAC from the nomination process so as to mitigate risks of undue influence from the auditing and accounting professions and ensure that the board acts in the public interest. However, before investing the PIOB with the administration of the nomination process, the MG should verify whether the PIOB needs to be structured and skilled differently in order to properly take on any new responsibilities and roles.

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?

The future role and responsibilities (especially veto rights over standard adoption) of the PIOB should be determined together with those assigned to the MG and after determining the structure, role and composition of the standard-setting board. In any case, the current PIOB's approach for overseeing the existent standard-setting boards should evolve in the new framework. The PIOB currently operates in a context in which standard setting boards may at least be perceived to not be independent of the auditing profession. That may drive the PIOB to get involved in standard setting at a detailed level. In a reformed framework, with an independent standard setting board, the approach adopted by the PIOB may be more 'trustee' in nature, with the establishment of a trustee-type body monitoring due process and the content of the standards rather than getting actively involved in putting forward what it thinks is the public interest in individual meetings.

The EBA agrees that it might be appropriate to strengthen the PIOB's role of ensuring that standards are developed in the public interest as this will contribute to reinforcing the credibility of the standards themselves. The PIOB should be required to report to the board any identified breach of public interest (with all the necessary elements enabling board members to have a full, clear understanding of the issues raised by the PIOB).

Allowing the PIOB to veto the adoption of a standard or instruct the board to take remedial actions could be envisaged, but only where there is a proven severe breach of public interest. If so, the PIOB should have to demonstrate the existence of a severe breach of public interest with due documentation. Such veto could not be exercised in the other situations. In other words, the PIOB could not be allowed to use veto for challenging technical judgments where the public interest is not at stake.

Before envisaging the possibility to grant veto power to the PIOB, the MG should further specify the concept of public interest, in relation to both the due process and the content of the standard themselves, by explaining how public interest is best served in practical terms and by characterizing situations of breach of public interest. Clarity is needed as to whether breach of public interest may arise from the process around developing standards or from the content of the standards themselves or both, and as to what possible actions serve public interest goals (possible actions might be the submission of draft standards to public consultations, public hearing with the audit and accounting professions, transparency of decisions and decision-making process, submission of board's work plans and strategies to the PIOB for approval, monitoring by the PIOB of the execution of board's work plans).

The public interest framework should not be developed by the PIOB alone, given the risk of conflict of interests in case the PIOB defined its own mission. The PIOB should be properly accountable to the MG, both in the development of a public interest framework and in its operation. As noted above, with different role and responsibilities, it is likely that the PIOB will need to be constituted differently in terms of skills and memberships, and a new PIOB will need to be in place before it is given a different mandate.

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

The EBA considers that IFAC representation should be removed from the PIOB. This removal would help address the risk of undue influence from the auditing and accounting professions and reinforce the credibility of the audit standards themselves. However, the EBA considers that the future composition of the PIOB will depend on the role and responsibilities which will be assigned to both PIOB and MG and on the future board's membership.

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?

The EBA considers that the future composition of the PIOB will depend on the role and responsibilities which will be assigned to both the PIOB and MG, and the future board's membership.

The EBA agrees to develop a skill matrix identifying appropriate skills and attributes to enable PIOB members to fulfil the PIOB's role. However, the level of seniority and skills required from PIOB members are difficult to judge at this stage since the role of the PIOB in the new framework has yet to be fully developed.

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?

The EBA considers that the PIOB members should be appointed by the MG following an open call for nominations. In any case, the EBA considers that the nomination aspects depend on the role and responsibilities which will be assigned to both the PIOB and MG, and the future board's membership.

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?

The EBA is of the view that the PIOB's scope of oversight should be consistent with the board's scope of responsibilities. It would be confusing for the PIOB to also monitor the activities of IFAC. Consequently, the EBA considers that the development and adoption of international educational standards (see question 5), as well as for ethical standards for professional accountants in business (see question 6) should be excluded from the PIOB's scope.

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?

The EBA agrees that the MG should continue monitoring the implementation and effectiveness of the standard-setting reform process, appointing the members of the PIOB, ensuring the PIOB's accountability to stakeholders, and monitoring the execution of the PIOB mandate. These responsibilities could not be discharged to non-public authorities.

To exercise its functions, the MG is expected to be composed of senior representatives of its members, who are empowered to take decisions on behalf of the organization they represent. However, the EBA highlights that the determination of the roles, responsibilities, and resources of the MG should be determined together with aspects as regards the future structure, composition, role and responsibilities of the PIOB and the board. In this regard, the EBA stresses it is important that the next public consultation is launched on a full proposal detailing the expected roles, objectives, responsibilities, compositions, and tasks of each of the bodies involved in the future standard-setting framework, and how all of them would interact.

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?

The EBA agrees that the board should be supported by a permanent administrative and technical staff composed of experts who are not provided by audit firms and professional bodies. The staff size needs to be large enough to enable board members to pay sufficient attention to strategic aspects or important technical issues by discharging them from administrative and procedural tasks (e.g. drafting of standards, legal and quality checks, running of public consultations). The permanent staff needs to be highly qualified with a full-time status. However, this issue should be linked together with funding considerations.

22. Do you agree the permanent staff should be directly employed by the board?

The EBA considers that the permanent staff should be employed, compensated and evaluated directly by the board so as to preserve the independence of the board from the audit profession. However, this issue should be linked together with funding considerations.

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

No any other areas to be improved

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 (eg independent approval of the budget by the PIOB, providing the funds to a separate foundation or the PIOB which would distribute the funds)?

The EBA welcomes the MG's willingness to reform the current funding arrangements to strengthen the independence of the board from the audit and accounting professions. The EBA supports the proposal to introduce a clear separation between those funding board's work and those appointing board members so as to mitigate the risk of fund providers influencing the work of the board.

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?

The EBA is of the view that voluntary contributions from audit and accounting professions might weaken the independence of the future board and accomplishment of the reform, while being aware of the difficulties in implementing a sustainable, diversified funding mechanism in the short term. As funding is crucial for the success of the reform, the EBA encourages the MG to continue carefully exploring all options with all relevant stakeholders by assessing feasibility, pros and cons of each option. In particular the possibility to apply a levy on the profession collected on a jurisdiction basis on behalf of the MG or PIOB should be explored. In this regard, the EBA stresses that the concept of 'contractual levy' is unclear and needs specifying further.

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

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

The EBA invites the MG to elaborate a more detailed proposal specifying all remaining open aspects, in particular as regards funding, membership, public interest, and responsibilities of the

PIOB and MG so that all of those involved could have sufficient certainty as to the overall shape of what they are commenting on and how it will work. The final proposal should be subject to a new public consultation in due course and accompanied with an impact assessment, and funding and transitional plans.