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The Monitoring Group

Submitted electronically to MG2017consultation@iosco.org

Dear Sir

Comments on the Consultation Paper on Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest

The Independent Regulatory Board for Auditors (IRBA) is both the audit regulator and national auditing standard setter in South Africa. One of its statutory objectives is the protection of the public by regulating audits performed by registered auditors, and the promotion of investment and employment in South Africa.

We appreciate this opportunity to comment on the Consultation Paper. Our comments are presented under the following sections:

A. General Comments; and

B. Request for Specific Comments and Responses.

We remain available to discuss our comments.

Yours faithfully

Bernard Peter Agulhas
Chief Executive Officer

A. General Comments

1.1. The IRBA notes and commends the Monitoring Group (MG) on its evaluation of the current auditing and assurance and ethics standard-setting processes (the standard-setting processes) and the oversight thereof. This evaluation is in keeping with good governance.

1.2. We appreciate that this is a consultation paper (CP) and that it indicates that decisions have not yet been made and conclusions have not yet been drawn.

1.3. South Africa adopted all the IAASB's International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements as the standards to be applied by all auditors in South Africa from 1 January 2005. The South African Code of Professional Conduct was gazetted on 18 June 2010. The IRBA has adopted the IESBA Code of Ethics for Professional Accountants and published it as the IRBA Code of Professional Conduct for Registered Auditors with additional requirements for auditors in South Africa. The IRBA is therefore committed to audit quality through recognising the value of the International Pronouncements and Code of Ethics.

1.4. The proposals include a "big bang'' approach to implementing changes to the standard-setting boards (SSBs) and PIOB simultaneously. While we appreciate the need to effect change sooner rather than later, we recommend an approach which will not dilute the confidence in the standard-setting process.

1.5. The current standards are of a high quality, and therefore the strengths of the standards and the standard-setting process should be drawn on when implementing further improvements to the standard-setting processes and the relevant structures.

1.6. We believe that, in addition to improving the standard-setting processes and structures, strengthening the oversight process is equally important. There already are several oversight and monitoring mechanisms in place, and if the perception still exists that the standards have not been developed in the public interest, then these oversight and monitoring mechanisms, including its composition, may need to be strengthened.

B. Request for Specific Comments and Responses

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 key areas of concern, namely, the need for the standard-setting process to be independent of undue influence from the profession, the importance of standards being developed in the public interest, and that standards should be issued more timely.

There appears to be a concern that there is undue influence by the profession on the standard-setting process. This may be as a result of the voice of the profession on the SSBs of the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA).

We understand that even if it is a perception, the perception by and in itself is enough to indicate that there may be a need for a review. However, as already mentioned, it is important that any changes draw on the current strengths and respond to the key areas of

concern in a manner that will not dilute those elements of the processes and structures that are working effectively.

This will equally apply to the many checks and balances which currently exist in the due process to ensure that the public perspective is taken into account, such as the public consultation process.

While we support the need for greater independence of members on the various structures, we should also ensure that the technical skills which are required in the process are retained. The ideal solution should therefore have the appropriate balance of technical skills and independence.

QUESTION 2

*Do you agree with the overarching and supporting principles as articulated, **and that all these principles are in the public interest**? Are there additional principles which the Monitoring Group should consider and why?*

Bold has been added

We agree with both the overarching principle of serving the public interest and the supporting principles. Independence and credibility are of the utmost importance.

Additional principles to consider may be integrity and transparency, which go hand-in-hand with independence. Practicality and scalability should also be considered.

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?

It might have been more useful if the MG had a proposed public interest framework for the PIOB, instead of leaving it to the PIOB to establish.

We agree that a public interest framework will be a critical tool in the standard-setting process, especially since developing a definition for "public interest" has proved to be challenging.

The following could be considered for inclusion in a public interest framework:

- Wide consultation with multiple stakeholders and processes to ensure that important stakeholders are included. Therefore, if responses from a particular stakeholder grouping are insufficient, there should be some form of follow up to encourage increased participation in the comment process.

- Provision in the process to ensure that the appropriate weighting is given to particular categories of stakeholders. For example, if 80% of the comments are received from the profession, it should not mean that those comments outweigh fewer comments received from other stakeholders.

- Cost versus benefit analysis (to society).

- Recognition of cultural and ethical diversity.

- In depth consultation on the strategies and work plans of the SSBs.

- Impact analyses which would include any potential unintended consequences prior to a standard being issued.

- Due consideration to the public interest representation on the Boards, for the chairmen and the task forces, and on Steering Committees.

- Sufficient geographical representivity in comment letters.

- Greater public education on the standard-setting process as the public might believe that they do not have a sufficient understanding to comment on exposure drafts.

Our experience has been that comments on proposed standards are often received only from certain constituencies. Also, comments on international exposure drafts are generally obtained only from certain countries, meaning they do not always represent the views of the wider IFAC member bodies. As there is a perception that there is a lack of input in the process of standard-setting from the investing public and from preparers of financial information, a solution to this would be greater outreach efforts and follow-up.

Public interest cannot be served when those who will be using the standards do not generally provide their views on the standards. This is, however, not a failure on the part of the standard setters, but rather a shortcoming on the part of the public.

The problem appears to be that users of financial information who are most impacted by potential business and/or audit failures appear unwilling or believe that they are unable to be involved in the process of standard-setting. This is despite there being participation opportunities throughout the whole process and the need for early involvement. All public interest stakeholders need to cooperate and take responsibility for their role in standard-setting.

The CP states that "the Monitoring Group expects this framework to be at the very heart of any reformed standard-setting process …" Therefore, the development of the framework should be a priority of the MG as it will go a long way to address actual or perceived lack of independence in the standard-setting process.

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.

As the skills might be different for audit and ethics standards, we support separate boards. We also support that ethics standards for auditors and accountants should be dealt with by one board (see response to question 6) as both auditors and accountants operate in the public interest. This strengthens the argument that ethics should be separated from audit standards since the ethics board should deal with ethics for accountants and auditors and it might make the workload of one single board too cumbersome.

Both areas are of great importance and establishing a single board would present some challenges, such as the following:

- In one board, there would be a focus on one area at the expense of the other. Ethics standards could take the "back seat" to audit standard-setting. Less time could be

allocated and taken for ethics discussions/projects. Ethics would possibly not be seen as the primary or equal function of the board, and the required emphasis would then be lacking.

- Although it would be one board, it would end up working as two boards in any event, because the agenda would have to be split in such a way that it allows for a focus on both areas. On paper the SSBs would have been combined, but in reality they would still function separately. Sub-committees that effectively mirror the current board structure would likely be formed.

- With a single board, there could be a loss of expertise. This may occur as one tries to balance the required expertise to cover both areas in one board. Those current members and technical advisors who may not have the required expertise for both boards may not be appointed to the new single board. Also, board members in the new single structure could likely not have experience in both ethics and auditing standard-setting.

- There could be a loss of interest in joining the combined board.

- Ethics standard-setting could become more reactive than proactive, "following" the audit standard-setting projects.

- Certain countries adopt the auditing and assurance standards and not the ethics standards, or *vice versa*. This would create an implementation challenge.

Separate SSBs may be more attractive to potential members who may have an area of expertise in one but not all of the areas.

We believe that the separation of the SSBs *adds* to the independence, transparency, accountability and robustness of the standard-setting process. The SSBs are a "check" for each other. Processes can be instituted that ensure that there is extensive consultation between the SSBs on all projects.

An exercise could be undertaken to assess which of the auditing and assurance standards need a stronger ethics component.

QUESTION 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?

We do not support education standards remaining the responsibility of IFAC as this is the starting point where competency requirements could be influenced. The independence requirements for members of audit and ethics standards boards should therefore be equally applicable to the education standards board (see also response to question 19 below).

We agree that the IFAC compliance programme remain the responsibility of IFAC as part of their function to monitor their member bodies.

QUESTION 6

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

> Both PAIB and professional accountants in public practice (PAPP) act in the public interest and therefore ethics standards for accountants should be independent of IFAC for the same reasons that ethics standards for auditors should be independent of IFAC. We contend that ethics standard-setting for both PAIB and PAPP should be set by the same board.
>
> Although the ethics considerations for PAIB differ in some respects from those for PAPP, the ethics standards should still be aligned with those for PAPP. The fundamental principles must be the same - only the environment in which they are applied is different. There should not be different fundamental principles for PAIB and PAPP.
>
> The responsibility for the development and adoption of ethics standards for PAIB rests with professional bodies and not audit regulators.
>
> Two sets of ethics standards could have wider negative consequences, and imply that PAPP need to be more ethical than PAIB. There must be one ethics standard that all professional accountants must comply with; whether they are PAPP or PAIB should not be a differentiating factor. Therefore, we do not support the move to have two sets of ethics standards.
>
> A PAPP has different functions. He/she may be a PAPP to clients and a PAIB within the firm. Separating the IFAC Code of Ethics creates a possibility of a future where there are two codes – the codes having diverged. The PAPP would need to apply two different codes, depending on what role is being filled.

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.

> Additional reforms for SSBs should include independence requirements for chairs of SSBs, and composition of task forces and steering committees.
>
> We propose the following further options for reform:
>
> - The MG should set project deadlines.
>
> - Task forces should be open to observers.
>
> - Oversight structures should be reformed.
>
> - Attendance of members at CAG and PIOB meetings should be monitored.
>
> - Role of public members should be defined.

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?

Added to the question: If yes, on what basis should the members of the board be remunerated?

Oversight should be strategic but the SSBs should be technical and not rely only on the technical expertise of the secretariat.

Technical expertise should not be confused with wordsmithing, which remains critical to ensure that the intended requirements and guidance is conveyed, ambiguity is removed, that there is consistency of the use of certain terminology amongst the standards, drafting conventions have been complied with and that there is consistency in application. It is suggested that the task forces perform most of the wordsmithing.

It will be useful if a skills matrix is developed for members of the boards and the oversight structures, to ensure that all skills are present at the right levels, that there is no duplication or that there are no missing skills.

Usually we would not support the remuneration of board members, but given the envisaged changes, and increased independence of the SSBs, we will support remuneration of board members. Full time members could be remunerated on the same basis as for positions of individuals in other corporate governance roles, and part time members at a flat rate. However, this would be dependent on the funding model which still needs to be established.

QUESTION 9

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

Added to the question: Do you agree that this will allow the board to be more decisive, avoid unnecessary delays and reflect the fact that acting in the public interest requires standards that not all stakeholders necessarily agree with? Please explain your answer.

The current model for the IAASB is a two-thirds majority vote. The IAASB currently has 18 members, and 12 members need to approve a standard. In the past, some members have abstained from voting or opposed a decision. This has not prevented standards from being issued. The aim, however, is to reach consensus.

We believe that unanimous approval for the adoption of a new standard is the ideal, for the following reasons:

- Consensus strengthens public interest. All stakeholders would have to agree.

- Reaching consensus promotes more discussion and debate.

- It would promote adoption of the standard in more jurisdictions.

- It would reduce multiple interpretations.

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?

Our response is in the context of the two SSBs remaining separate.

We believe that 12 members are too few for the SSBs when taking into account the geopolitical landscape. Various geographical regions and constituencies need to be accommodated in order to establish global buy-in and adoption of standards. A board of 12 will not necessarily be representative of all stakeholders. It is important to ensure that there is at least one member per stakeholder category and possibly two for larger stakeholders. Also, a small committee may lead to group think.

We support a larger board to ensure wider representation. However, instead of determining a fixed number and then filling the positions, it should rather be determined which representatives are required on the boards and ensured that all the required constituencies are represented.

Although a smaller board is easier to manage, we suggest that a larger board could be equally managed provided that there is closer oversight, managed decision-making, and monitoring of streamlined and efficient processes.

Multi-stakeholder considerations could include the following:

- Improving representation from developing countries, as it appears that standards are primarily focused on large developed economies, and the perception is that they are not scalable enough.

- Consideration of gender diversity.

- Placing an imperative on the representation of small and medium practitioners (SMPs).

- Representation from Those Charged With Governance (TCWG).

With respect to full-time versus part-time membership, the following considerations are relevant:

The case for full-time membership includes:

- Continuity between meetings and decision-making.

- Part-time members would not partake in all the discussions/decisions and may therefore be less effective.

- Dedicated members.

- More time for discussions, debates and wordsmithing.

The case for part-time membership:

- Part-time members could contribute "on-the-job", practical and current experience which the full-time members might not necessarily be able to provide.

- Full-time membership may not be feasible and practical. It could be argued that individuals with the appropriate skills would not be prepared to sacrifice three to six years of secure employment to become a full-time board member.

- Full-time members could immerse themselves in detailed standard-setting and not concentrate on strategic matters.

- Part-time members step away and have time to reflect objectively.

- Full-time members may not keep in touch with the stakeholder group they represent.

On balance, we propose that part-time membership would be the most effective solution.

Finally, the role of technical advisors should not be underestimated. We do not believe that substituting technical advisors to the board members with the assistance from the technical staff would achieve the same objectives.

QUESTION 11

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

Added to the question: *Do you agree with a formal development of a skills matrix to drive the assessment of potential members? Please explain your answer.*

Required skills and attributes could include:

- Technical skills – experience in standard-setting and knowledge to contribute towards specific projects.

- Practical experience and application.

- Strategic thinking.

- Public interest/user focused.

- Independent in all respects.

- Ability to have a regulatory or governance mind-set.

We support the development of a formal skills matrix, which should be assessed continually for relevance.

QUESTION 12

Do you agree to retain the concept of a Consultative Advisory Group (CAG) with the current role and focus, or should its remit and membership be changed, and if so, how?

If the CAGs are to remain, then there should be clarity on the roles of the CAGs, PIOB and the MG. The role of the CAGs does not appear to be fully understood.

As such, the CAGs should also undergo an assessment to determine if reforms are required.

QUESTION 13

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

The overarching principle is acting in the public interest; therefore, we agree that task forces should adhere to a public interest framework.

QUESTION 14

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

We agree with the proposed changes to the nomination process. IFAC should not be included in the nominations process. The PIOB appears to be the most independent body focusing on public interest. The open call for nominations would be more transparent and in the public interest. The nomination process should result in all stakeholders (including PAPP) being represented equally.

We also suggest that the performance of members be evaluated by an independent body. Members should be evaluated on criteria such as their contribution to and influence on meetings, and how effectively they have collected and contributed a consolidated view from their constituencies.

QUESTION 15

Do you agree with the role and responsibilities of the Public Interest Oversight Board (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 PIOB should not be able to veto the adoption of a standard, but ensure that it has sufficiently competent members to engage and intervene at an early stage. For example, for the IESBA's *Long Association* project, after 2 public exposure periods, the PIOB stopped the adoption of the amendments and required further amendments. It would have been more efficient if the PIOB shared their views at an earlier stage.

The PIOB should strengthen its oversight role and processes to ensure that it fulfils its mandate. It should have set criteria against which it will sign off on standards. One of these criteria could be the public interest framework that is still to be developed. Some of the perceived weaknesses that have been identified could already be addressed by the PIOB.

QUESTION 16

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

There is a potential conflict of interest (actual or perceived) if IFAC is represented on the PIOB. Removing the IFAC member could ensure heightened independence and improved public interest.

However, the IFAC represents a key stakeholder that also has to act in the public interest. Therefore, we suggest that IFAC be invited to attend or report at PIOB meetings.

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?

PIOB members should understand the public interest and have strategic and some technical skills to appreciate how technical standards impact the public interest.

The composition should include representatives from regulators, investors, users, major geographic locations, SMPs, TCWG and business, and have no gender majority.

Skills and attributes could include:

- Objectivity.

- Independence.

- Demonstrated experience in serving the public interest.

- Representation of a multi-stakeholder community.

- Accountable to a range of users.

- Financial literacy.

- Industry experience in auditing and ethics.

- Legal experience.

- Being able to obtain representative comments from the applicable wide stakeholder group, and then provide feedback to that wide stakeholder group.

It is important to note that non-practitioner stakeholders are not necessarily public interest stakeholders.

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?

There should be an open call for nominations, both through MG organisations and directly to the public. The nomination process should be open and transparent. Appointments should be assessed using a formal skills matrix (see above).

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?

The PIOB should continue overseeing the work of other SSBs. It should represent the public interest at large; and with a wide view on global issues, it can ensure that common outcomes are achieved. This will ensure consistency in standards and provide strengthened public protection.

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?

We agree. We think that the MG should consider:

- If it reflects on a globalised world.

- If it has met its objectives.

- The impact of government reforms.

QUESTION 21

*Do you agree with the option to support the work of the standard-setting board with an expanded professional technical staff, **and whether doing so will address stakeholder concerns about independence**? Are there specific skills that a new standard-setting board should look to acquire?*

Bold has been added

SSB members should have technical skills, otherwise the secretariat can influence SSB members.

However, the following supports an expanded staff complement:

- The staff would perform all the drafting work. Our view is that the staff complement is currently insufficient to respond to workload requirements. The result is that, because the SSBs do not have sufficient full-time staff, the work sometimes ends up being done at the firms. Therefore, independence can be improved with less staff from the firms working on the drafting.

- The standard-setting process can be fast-tracked if more man hours are expended, thus addressing the timing concern.

- Project management skills will be key to ensure project risks are managed and timelines are achieved.

- An auditing and assurance related background would be a prerequisite.

- The work of the staff can be further streamlined through improved project management and the use of technology, as is currently being explored.

QUESTION 22

*Do you agree the full-time staff should be directly employed by the board, **or do you have other suggestions regarding the employment process?***

Bold has been added

> We think that full-time staff should be directly employed by the SSBs. The SSBs would set their strategies and as such understand their requirements to ensure the achievement of the strategies.
>
> There would have to be a needs analysis to determine how many staff members would be required for each board. As different projects arise and are completed, and new skills, knowledge and experience are required, a plan would need to be put in place to either upskill the full-time staff or hire additional resources.

QUESTION 23

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

> The board could make better use of technology to solicit views and opinions, as well as to share ideas, issues and concerns.

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)?

> Even if the checks and balances are in place, the perception will still be that there is no independence if the source of the funds is still the firms.

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?

> The funding model explored in the CP has not been fully developed nor sufficiently explored. The proposals addressing the concerns depend heavily on a transformed funding model so it is important that the funding model is prioritised.
>
> We do not believe that a contractual levy on the profession would be an appropriate mechanism to secure funding. More levies will strain the auditing profession further. SMPs are, in many cases, already struggling financially. The mechanism to determine which firms in the profession should be levied may prove to be complex. Also, such a levy would not remove the motivation for firms to influence the standard-setting processes – it would likely increase it.

Research should be performed to determine who the beneficiaries of audits are, as they should fund the standard-setting process. One suggestion would be that listed entities or their security exchanges should fund audits as they benefit from the audit.

A wider funding model should be developed. This would eliminate the practical risk of relying on a few parties for most of the funding. The risk is that funding is not forthcoming, or that these funders unnecessarily attempt to influence the SSBs and the PIOB, again impacting on independence.

Diverse funds from different sources will ensure that the concerns or needs of the wider public are addressed. Additional funding could include:

- Donations.

- Levy on securities exchanges.

- Levy on governments: levy the countries that require audits based on the IAASB and IESBA standards in their corporate laws.

- Funding from the MG.

QUESTION 26

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

- The MG should perform a more detailed analysis of the issues that it is trying to address. It could do this by obtaining empirical evidence that proves whether there is a problem with the standards and/or the standard-setting process, with the oversight of the standard-setting process, or both.

- An impact assessment on the current process and structures in place should be conducted, applying the proposed reforms.

- A detailed risk assessment should be performed in relation to the new proposals.

- There should be a leveraging of technology to improve efficiencies and decision-making.

- Our experience has been that many auditors do not apply the standards correctly. Even if the standards are perfect, how the standards will be enforced has to be considered. Strong enforcement strategies should be in place to ensure compliance, i.e. rules without consequences for breaking them are ineffective.

QUESTION 27

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

Cooling off periods for changes in membership should be introduced, preventing rotation between these roles:

- Staff to the Board and vice versa.

- The Board to Technical Advisor.

- CAG, PIOB and MG to Board.

The IAASB performs functions other than standard-setting, for example, implementation of standards and support. Consideration should be given to which entity would be performing the roles of these other functions under the proposed reforms.