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C/O International Organization of Securities Commissions  
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Submitted Electronically: MG2017consultation@iosco.org

***JICPA Comments on “Monitoring Group Consultation: Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest”***

Dear Mr. Everts:

The Japanese Institute of Certified Public Accountants (JICPA) is grateful for the opportunity to comment on the Monitoring Group's consultation paper (CP) entitled "Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest."

JICPA endorses the seven objectives stated in the CP: *public interest, independence, credibility, cost effectiveness, relevance, transparency, and accountability*. Whilst we commend the fact that the current model has enabled a large number of high-quality standards to be developed and implemented internationally, we also recognize that there is room for improvement with regard to setting international standards that can achieve these objectives. We hope that discussion over this CP will result in appropriate revisions, leading to greater trust in audit among stakeholders.

In these comments, we present a new framework for standard-setting that we believe will help enhance audit quality, followed by our responses to the questions posed in the CP. When making changes to the governance of standard-setting, a key concern is the need to set standards that incorporate the view of a diverse range of stakeholders from a variety of regions to ensure that they are implemented as international standards across a wide area. Moreover, making changes to the current governance structure of standard-setting comprising of three different tiers that function as an integrated system—monitoring of standard-setting as a whole, oversight of due process in standard-setting, and

standard-setting itself - would require not small, targeted changes, but across-the-board optimization.

JICPA believes that in order to achieve the above seven objectives stated in the CP, the standard-setting framework needs to meet the following requirements:

- All stakeholders, under multi-stakeholder engagements, cooperate in standard-setting and its related oversight activities in order to increase transparency, and ensure that standard-setting is conducted in line with the public interest.
- As governance is premised on separation of execution and oversight to avoid conflict of interest, the roles of standard-setting boards and of their oversight are clearly differentiated.
- Diversity, including regional diversity, is ensured during the standard-setting process to ensure that the standards set can be accepted as international standards.
- A stable, broad, sustainable framework for collecting funds is in place to avoid causing any suspicion that certain stakeholders are exerting undue influence.

JICPA suggests the following framework to meet the above requirements:

#### **Multi-stakeholder involvement**

- Use the Public Interest Oversight Board (PIOB) and standard-setting boards as the organizations that secure involvement of a large number of stakeholders, while at the same time, retaining the three-tiered structure comprising of monitoring of standard-setting as a whole by the Monitoring Group, oversight of due process in standard-setting by the PIOB, and standard-setting by standard-setting boards.
- To set standards that win support as global standards reflecting multiple viewpoints and regional perspectives, the boards and their oversight body, the PIOB, should have sufficient members to secure the participation of stakeholders with a range of viewpoints representing multiple positions and a variety of regions.
- To ensure that standard-setting is not overly influenced by particular stakeholders, the membership of the PIOB and the boards should be configured such that balance among the different types of stakeholders can be assured across the entire three-tiered structure (comprising of monitoring of standard-setting as a whole, oversight of due process in standard-setting, and standard-setting itself).

#### **Separation of execution and oversight**

- Employ a process of decision-making by boards comprising of multi-stakeholder memberships to set standards, and maintaining a high degree of transparency to achieve better accountability. The PIOB should not become involved with the details of the standards themselves, but should instead focus exclusively on the oversight of due process. This will clearly distinguish the respective roles of standard-setting and oversight, making the efficacy of oversight more reliable.

- To ensure that a high degree of independence is maintained in selecting members of standard-setting boards, nomination of board members should be undertaken by a nominating committee that comprises of multi-stakeholder members and a chairperson independent of the Monitoring Group, the PIOB, and the International Federation of Accountants (IFAC).

#### **Retaining multiple standard-setting boards**

- In order to facilitate engaged discussions on audit and ethics as individually different, albeit correlated, subjects, and given that the members of standard-setting boards need to possess highly specialized expertise to take responsibility for such standard-setting based on sophisticated expert judgments, JICPA recommends having a board dedicated to set auditing and assurance standards and a separate board which sets ethics standards for all accountants. In other words, retain two boards as currently, and retain the same scope of work for the International Ethics Standards Board for Accountants (IESBA). The boards should deliberate on standards relating to both public interest entities (PIEs) and non-PIEs, setting standards consistently with a view to applying them to all entities.

#### **Roles and responsibilities with regard to standard-setting**

- Establish an environment in which a wide range of talented individuals can easily participate in boards by increasing the number of technical staff to reduce the burden on board members of standard drafting and related tasks. Although members of boards must find time to undertake planning and to discuss policy involving decisions on the need for new standards or changes to existing standards, they are also responsible for the final wording of standards. Highly specialized expertise is therefore required of them.
- The boards should have final decision-making authority and responsibility with regard to the standards, as every single word is critical when standards are implemented. The members of the boards, who are ultimately responsible, should engage in sufficient discussion with the aim of setting high-quality standards.
- In order to draw up standards that are highly relevant and can meet the demands of the financial markets and of users of financial statements based on careful deliberations, the boards' resolutions should require approval by at least two-thirds of members.

#### **Attainment of the necessary financial resources, and budget management and its execution**

- Since multiple stakeholders are involved in setting standards, the necessary financial resources should also be provided by multiple stakeholders. A sustainable framework should therefore be ensured by obtaining contributions from a broad range of stakeholders, in addition to accountancy organizations (via IFAC) and audit firms (via the Forum of Firms).
- To prevent excessive influence from the accounting profession, the financial

resources contributed for standard-setting should be paid into a fund kept completely separate from IFAC's accounts. Attainment of the financial resources necessary for standard-setting should be coordinated by the multi-stakeholder PIOB described above, with the support of IFAC, and the standard-setting boards' budget management and execution should also be under the PIOB's oversight.

- To ensure that day-to-day tasks are handled smoothly and cost efficiency is improved, IFAC should hire the personnel necessary for operating the boards. Such personnel would support the boards with required technical knowledge and undertake administrative works including collection and allocation of financial resources. The boards themselves should be responsible for instructing and appraising such personnel, and personnel expenses and other necessary costs should be paid from a fund kept separate from IFAC's accounts.

JICPA's answers to the questions posed in this CP are provided below. Our answers are focused on employing the above framework to maintain a high degree of transparency to set auditing and assurance standards and ethics standards aligned with the public interest.

**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.**

— JICPA supports the retention of separate boards: the one to set auditing and assurance standards, and the other to set ethics standards for all professional accountants, not just for auditors.

Reasons:

Although standards relating to auditing and assurance and to ethics are all similar in that they should be developed with consideration for the public interest, the issues they address and the perspectives they require are discrete. Given that auditing and assurance standards deal with issues relating to the norms in practice and ethics standards deal with rules relating to mentality or attitudes, there is a risk that discussing them in a single standard-setting board might result in dispersed and imprecise dealing of subject matters. Furthermore, highly specialized expertise is required of individual board members, partly to ensure prompt decision-making. Even if they engage in strategic debate, as long as board members are also responsible for standard setting based on sophisticated expert judgments, narrowing down the matters handled by the board could enable a discussion of higher quality. Accordingly, we believe that if the two different areas are handled by separate boards, the credibility of standard setting can be further enhanced by organizing the composition of these boards in such a way that their members' skills, experiences, and knowledge can provide a basis for public trust.

Issues common to the areas of auditing and assurance and of ethics could be addressed by strengthening the current ties between the International Auditing and Assurance Standards Board (IAASB) and the IESBA.

In setting standards relating to auditing and assurance and to ethics, these retained boards should deliberate on standards for both PIEs and non-PIEs, engaging in consistent discussion with a view to applying the standards to all entities.

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

— JICPA believes that ethics standards should target not only professional accountants in audit, but all professional accountants, and should be developed by a single board. Consequently, we argue that there will be no need to change the current framework.

Reasons:

Regardless of whether professional accountants are in audit or in business, the ethics standards that apply to them do not change according to the types of work they do. In addition, various laws that stipulate the status of professional accountants in many parts of the world generally do not distinguish between accountants in audit and those engaging in other areas. The standards may be applied slightly differently in the two different cases, but the ethics required of all professional accountants should be discussed exhaustively and ethics standards set accordingly. This would enable accounting professionals with strong ethical values to be engaged in the preparation of financial statements, which could contribute to enhancing their credibility. If a board encompassing ethics standards for all professional accountants is to be sustained, changing the current framework would not be necessary.

**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?**

— JICPA thinks it is necessary, first of all, to clearly define what is meant by "strategic." We agree with a general policy that board members should focus their efforts on discussions, rather than on drafting. In addition, remuneration for board members should be determined only after a careful calculation of expected costs for entire standard-setting activities is conducted against the actual funding available.

Reasons:

Increasing the number of technical staff would free board members from detailed drafting work, enabling them to devote more time to planning and to discuss policy involving decisions on the need for new or changed standards. We believe that this can result in higher quality standards.

At the same time, board members should take responsibility for the wording of the standards they set, as every single word is critical when standards are implemented.

Remunerating board members would encourage participation by stakeholders with diverse viewpoints who represent multiple regions. If members were appointed full-time, however, costs would inevitably inflate, while it is likely that inability to pay attractive levels of remuneration would make it extremely difficult to secure highly talented individuals required.

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

— JICPA suggests that boards adopt standards not on the basis of a simple majority, but on the basis of a supermajority, requiring approval by at least two-thirds of members.

Reasons:

We believe that the reason why the non-binding international standards set under the existing model have been adopted in numerous jurisdictions around the world is that careful consensus-building has been conducted among a large number of interested parties. Likewise, we believe that the adopting of standards by two-thirds approval of board members is imperative to better serve the aim of international standards, as it encourages careful deliberations and the development of highly relevant standards that will meet the demands of the financial markets and users of financial statements, and this in turn, also forms the basis for a wider adoption in numerous jurisdictions.

**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?**

— As indicated in our answer to Question 4 above, JICPA suggests retaining two boards—the one to set auditing and assurance standards, and the other to set ethics standards—and suggests keeping the number of members at 18 for both boards. With regard to including both full-time and part-time members, we are against appointing any full-time members other than the chairperson.

Reasons:

Boards need to set standards that can be implemented globally as international standards. Participation by stakeholders with diverse viewpoints who represent multiple regions ensures that the standards they set are highly relevant and better able to meet the demands of the financial markets and of users of financial statements, enhancing widespread implementation in many jurisdictions. Over narrowing down of the number of boards will result in hindering this broader application. Accordingly, it is necessary to maintain the number of board members at around the existing level of 18.

We believe that appointing members other than the chairperson on a part-time basis will dramatically increase the likelihood of participation by talented individuals including investors, resulting in high quality standard setting.

**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?**

— JICPA agrees with retaining the concept of a CAG.

Reasons:

Even if boards come to comprise of multi-stakeholder memberships, the process of listening to the opinions of a wider range of experts will still be crucial.

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

— JICPA suggests a separate method to ensure multi-stakeholder involvement.

Reasons:

We have concerns about the PIOB administering the nomination process due to the lack of clear separation between the roles of standard setting boards and their oversight. It is desirable that a nominating committee that comprises of multi-stakeholders and a chairperson independent of the Monitoring Group, the PIOB, and IFAC designates the members of the boards, as the committee can conduct the nominating process with enhanced independence.

**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?**

— The PIOB should not have the right of veto, and should instead focus exclusively on the oversight of due process. JICPA believes that if new boards were to conduct multi-stakeholder discussions, there would be no need to change the PIOB's roles and responsibilities with regard to oversight of due process.

Reasons:

When developing standards—by engaging in planning or discussions related to policies or decisions on the need for new or revised standards—new boards comprising of multi-stakeholder memberships could improve upon current levels of transparency and provide better accountability. In this case, PIOB oversight of due process alone would suffice. There would be little need to enable the PIOB to veto the adoption of standards debated by these boards through an open process. At the same time, involvement of the PIOB in the contents of standards would make the separation between the roles of standard setting boards and their oversight unclear, and could also compromise the timeliness with which standards are set. Furthermore, if the PIOB were to exercise its right of veto under its existing structure, lack of transparency regarding the reasons for the veto decision would be problematic. If the boards themselves exercise final decision-making authority, this clarifies where responsibility for standard setting resides, thereby helping to ensure credibility.

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

— If it is to be assumed that, as stated in the CP, the composition of the PIOB's membership will not be changed significantly, JICPA believes that the nomination of a PIOB member by IFAC should definitely be continued.

Reasons:

As indicated in our answer to Question 17, we recommend that, like the standard setting boards, the PIOB should comprise of a multi-stakeholder membership and oversee the standard setting process from a perspective reflecting a range of viewpoints. We believe that when the PIOB conducts such oversight, the presence of a member nominated by IFAC—which represents a particular stakeholder, the accounting profession,—would strengthen the oversight in terms of professional expertise.

**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?**

— JICPA suggests that, like the standard setting boards, the PIOB should comprise of a multi-stakeholder membership. We believe that PIOB members should have consideration for the public interest and a big-picture perspective, as well as an ability to understand what is important and what is to be prioritized. These attributes need to be combined with a degree of aptitude for accounting and auditing.

Reasons:

We believe that independent, highly transparent oversight aligned with the public interest can be conducted by ensuring multi-stakeholder representation to oversee the standard setting process from diverse viewpoints and represents multiple regions. In our opinion, this would also enhance the oversight's credibility.

Furthermore, we believe that PIOB oversight will reinforce standard setting's contribution to the public interest if the PIOB's members comprise individuals who have consideration for the public interest; an unbiased person with a big-picture perspective; a project manager's mindset and skills to understand what is important and what is to be prioritized; and a degree of aptitude for accounting and auditing.

**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?**

— JICPA suggests that, even if some members within a multi-stakeholder PIOB are appointed through individual Monitoring Group members, the other members should be identified through an open call for nomination, targeting a diverse range of stakeholders, after clearly prescribing the requirements and the appointment process.

Reasons:

We believe that ensuring a multi-stakeholder membership of the PIOB by employing highly transparent methods of appointment is essential to better align its oversight with the public interest and to enhance the public's confidence in its processes.

**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?**

— JICPA agrees with the option of an expanded technical staff supporting the work of the standard setting boards. In increasing technical staff, the relevance of standards will be enhanced when staff members are also diverse in terms of their backgrounds and the geographical representations; care is therefore required in this regard.

Reasons:

The same as our answer to Question 8.

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

— JICPA suggests that IFAC should support boards, rather than staff being directly employed by boards.

Reasons:

It is difficult that the standard-setting boards themselves directly employ permanent staff, and if permanent staff is employed in a way different from the current practice, it is likely that administration cost will increase. To ensure that day-to-day tasks are handled smoothly, IFAC should hire the personnel necessary for the operation of the boards. Such personnel would provide the boards with support backed by technical knowledge and undertake administration works including collection and allocation of financial resources. The boards themselves should be responsible for instructing and appraising such personnel, and personnel expenses and other necessary costs should be paid from a fund kept separate from IFAC's accounts. This would enable sustainable, more cost-effective standard setting.

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

— JICPA suggests that, once the PIOB has been changed to a multi-stakeholder membership, management and execution of budget could be entrusted to such PIOB, with those funds supported by contributions from accountancy organizations (via IFAC), audit firms (via the Forum of Firms), and other stakeholders. These funds would be kept completely separate from IFAC's accounts and used to cover the costs of running the boards. In this way, appropriate checks and balances will be put in place.

Reasons:

If the aim is to eliminate concerns about the influence of the accounting profession, relying exclusively on financial resources collected directly from the accounting profession is not going to help the situation. Instead, an independent fund could be set up using financial resources contributed by accountancy organizations, audit firms, and other stakeholders, and its budget management and execution could be under the oversight of a multi-stakeholder PIOC or other organization. This could enable the funding structure to be based on multi-stakeholder representation as well, assuaging concerns about the influence of the accounting profession and enhancing the independence of standard setting.

Reforms should be undertaken only after verifying that it would be possible to create a framework of this type. And if IFAC staff were to provide support to standard setting, as suggested in our answer to Question 22, it would be possible to avoid an increase in the indirect costs required to run a new organization.

**Question 25: Do you support the application of a "contractual" levy on the profession to fund the board and the PIOC? 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?**

— Applying a "contractual" levy on the accounting profession will not help eliminate concerns about the influence of the profession.

Reasons:

Using contractual levies on audit firms to cover the costs of standard setting and its oversight would mean that the boards and the PIOC were run using financial resources collected not from IFAC, the organization that represents the accounting profession as a whole, but directly from the audit firms that actually use the auditing standards. Thus, far from quelling concerns, this could actually be regarded as an example of their exercising undue influence. If the aim is to eliminate concerns about the influence of the accounting profession, relying exclusively on financial resources obtained directly from the accounting profession is not going to help the situation. We believe that establishing a fund whose budget management and execution is under PIOC's oversight and supported by contributions from accountancy organizations, audit firms, and other stakeholders is a method more aligned with the overall aims in relation to independence and cost effectiveness.

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

— As the three tiers—monitoring of standard setting as a whole, oversight of due process in standard setting, and standard setting itself—need to function as an integrated system, reforms should involve comprehensive and exhaustive deliberation on the pros and cons of making changes throughout the entire three-tiered structure. We have some concerns regarding the feasibility of implementing reforms based on the proposals in the CP; realistic

reforms backed up by reliable funding should be sought.

Reasons:

The CP does not refer to any reforms of the PIOB's membership, and the long-term prospects for ensuring financial resources are unclear. If considerable discussion is likely to be required to resolve issues relating to the PIOB and attainment of financial resources, one option would be to give precedence to reforming the process whereby board members are appointed as a means of eliminating the issue of perception that has led to concerns regarding the boards' independence from the accounting profession. In so doing, the long-term issues should be clearly defined and a process for considering them indicated, while in the short term, the existing governance set-up is retained as a foundation.

In addition to the issues referred to above, there are other proposals in the CP that we believe should be resolved from a feasibility perspective, such as the issues relating to the attainment of financial resources detailed below. If a levy is to be imposed across a wide range of organizations, there will be no choice but to require various advance preparations in the different jurisdictions, and procedures for achieving this should therefore be established ahead of time. Matters need to be taken forward in a measured way by clearly establishing an overall picture of the situation including the future outlook, taking the steps required to make the transition, and ensuring that during this period no adverse effects in the form of standard setting delays are caused.

- Wouldn't payment of remuneration to both full-time and part-time board members combined with an increase in the number of technical staff lead to a substantial increase of costs?
- Board members' traveling expenses and other costs are often paid by the organizations that have nominated the members in question, but according to the proposal, wouldn't those costs also be paid by a new organization?
- Is it possible to legislate for and collect a contractual levy on a worldwide basis?
- Is it possible to calculate contractual levy amounts fairly and appropriately among different jurisdictions?

We wish to express, again, our appreciation for this opportunity to comment on this CP.

Sincerely,



Aiko Sekine

Chairman and President

The Japanese Institute of Certified Public Accountants