

Monitoring Group Consultation

Strengthening the Governance and Oversight of the International Audit-related Standard-setting Boards in the Public Interest

Response by Mark Spofforth OBE FCA CTA

26th January 2018

Dear Sir

I welcome the opportunity to comment on the Monitoring Group Consultation. For the avoidance of doubt I am content that this response should be made available publicly, and believe that all responses should be publicly available.

My name is Mark Spofforth. I am a third generation U.K. Chartered Accountant in public practice who trained with a large firm and then joined and ran my family firm until a recent merger with a network member of the Forum of Firms, of which I remain a partner. I have 35 years' experience of audit and general practice. I am a past Deputy Chairman of IAESB, the ICAEW Observer to the IFAC Board, and a past President of the ICAEW.

The views expressed in this response are my personal views and do not necessarily represent the views of any organisation of which I am a member.

CONCLUSION

In summary, my view is that the proposals in this document are severely flawed, and might lead to a catastrophic destruction of trust in the standard setting process by practitioners, leading to a consequential loss of trust by the public in a valuable and valued control over corporate activity. The funding proposals will lead to a reduction in competition in the audit market and a consequent reduction in audit quality and increase in costs.

The proposals are revolutionary, not evolutionary, and focus entirely on the audit of large capital market companies to the detriment of other important sectors of the economy.

MAJOR POINTS

QUESTIONABLE AUTHORITY?

The timing of this consultation is unfortunate. It comes at a time of a public backlash against globalisation, and the inability of governments and regulators to demonstrate that globalisation of business leads to rewards that can be shared to improve the lives of all. A time when nationalistic fervour argues against any rules that might govern global business, and leads a reversion to national/tribal structures.

It can be argued that although globalisation has led to substantial improvements in living standards, those benefits have been counter-balanced by job losses due to technological change; but the impact on citizens is the same. A large proportion of the public feel that they are now worse off than before. Consequently, at present the public does not trust "big" business or "big" government and any changes to a regulatory system must therefore be well evidenced, well constructed, and well tested before implementation. Any revisions to the framework must be proposed by a democratically accountable and globally diverse body representing those who will be affected by the change, and cover all auditing and reporting so as to avoid consequential harm to global reporting of SMEs, for example.

It is far from clear in this consultation paper that The Monitoring Group itself is accountable, transparent, or globally diverse. The self-selected organisations involved were included and are subject to a Charter that mandates *monitoring*, *advice* and *oversight* of the IOB, but does not mandate the re-design of a regulatory framework.

The individual members on the Monitoring Group are not identified (as far as I can see,) anywhere. Despite various internet searches the individuals stay in the shadows, seeking to exercise power without any apparent accountability or transparency. Readers will be rightly sceptical about the quality of knowledge and experience that has led to these proposals.

My understanding for many years has been that it was the role of the IOB to exercise oversight of the public interest in the standard setting process, including such matters as the speed of response and the topics of debate, and that stakeholders exercised influence over the Agendas of the Standard Setting Boards and monitored performance through the Consultative and Advisory Groups, (CAGs), committees of interested stakeholders meeting regularly and making well informed judgements about the direction and progress of standard setting.

The Monitoring Group's Mission, as set out in its Charter, talks about *assessing* the effectiveness of standard setting, about *monitoring* the IOB, about *convening* debates relating to audit quality. This consultation appears to suggest that Monitoring Group is now taking for itself much greater powers to mandate processes, without accepting greater accountability.

My reading of the governance documentation is that it is the role of the IOB to protect the public interest, not that of the Monitoring Group, although the Monitoring Group is charged with assessing how effective the IOB is in that respect.

ARE THE STANDARD SETTERS TOO CLOSE TO THE PROFESSION?

My experience is that the Standard Setting Boards guard their independence of thought jealously, and refuse to be influenced by firms, IFAC or individual professional accountants. As a result the standards themselves have been remarkably successful and free of controversy. However, the Monitoring Group clearly feel that the standard setters are too close to the profession, and that there are flaws in the current standards.

If there is a failure in the governance of the Boards, and there is no first hand evidence presented in this paper to that effect, then surely it is a failure of the CAGs to influence the Boards and present other stakeholders' dissatisfaction? The proposals here will simply drive the "soft power" into the hands of technical staff, who may themselves have trained with (and may hold some allegiance to) the Big 4 firms, concealing such influence rather than retaining transparency.

There is no doubt that many of the inputs to the standards have come from practitioners in the Big 4 firms, and this may well be as a result of a weak model for funding the SSBs. But in over 40 years the standards themselves have not been the subject of criticism by audit regulators.

Such criticisms of audit have tended to revolve around the exercise of professional judgement – valuation judgements for example, or reliance on specialist experts, insufficient scepticism, rather than weaknesses in the standards. The problems lie with the application of the standards rather than in the drafting of the standards themselves. What are these weaknesses that have been caused by being too close to the profession?

STANDARDS ARE NOT MANDATORY BUT HAVE BEEN VOLUNTARILY ACCEPTED

My overriding impression when reading this paper is that it has been written and compiled by a largely European-centric body with an appetite for over-regulation, who assume that standard setting boards have had the power to mandate the application of regulation and compliance with audit regulation, rather than understanding the requirement for a consensus between countries/governments/professional bodies/and auditors, and the voluntary nature of acceptance and compliance with standards.

EVIDENCE BASED?

There is no evidence presented that there is a problem that needs solving by the use of such a major reorganisation. I agree that improvements could and should be made, but evolution rather than revolution has always worked well in the past, and has less chance of a dramatic collapse in confidence by stakeholders.

The paper states that “questions have been raised about the independence of the standard setting process and its responsiveness to the public interest”. Neither supposed weakness is supported by evidence to that effect, but we must assume that it exists. At some point it will be necessary for that evidence to be articulated and published.

“Independence” is of course shorthand for expressing an absence of control for selfish profit or advantage. It is unfortunate shorthand, as it leads one to conclude that only laymen, ignorant of the service, can ever be truly independent. Ignorance, though, is not a necessary condition for independence. Independence is a state of mind, and professionals are taught throughout their career to exercise independence of thought, even though they perpetually have a fundamental conflict of interest because they are paid for their service.

I would suggest that effective regulation of any profession is impossible without the advice and input of experts in that profession, albeit with the assistance of a small number of laymen whose role is simply to identify conflicts of interest and enunciate them, and with the ability to state to the public if they feel that independent thought is not being demonstrated.

“Responsiveness to the public interest” is also an interesting choice of words – clearly there is no evidence to be adduced that any action contrary to the public interest has occurred in standards drafting, but merely an impression that the speed of response has been slow. That may be valid criticism, because the process of gaining consensus around the world, arguing the issues properly, does take time and arguably too long. But an assessment of how the process can be speeded up does not seem to have formed part of the thought process behind this report, other than a proposal to appoint paid staff in place of volunteers. Those involved could no doubt assist by explaining exactly where the project timelines could be accelerated.

However, even if the standard setting process has been largely successful over the last 50 years funded by, and implemented by, many voluntary hours input from members of the profession there are clear defects, some of which are identified as the cause of the proposed changes. The PIOB “Feedback

Statement and PIOB strategy 2017-19" states that "The quality of the current body of standards is not questioned..." and yet the chair of the Monitoring Group has stated publicly that he believes there "are weaknesses in the current standards". This conflict between oversight bodies needs to be resolved before further proposals are made.

I deplore the sentence in the introduction to this consultation that states "standard setting Boards, nominated, funded and staffed by IFAC were set up". This is totally misleading to the lay reader as a summary of the current position. My own experience as the Deputy Chair of the IAESB gives me the ability to state without any doubt that the Boards have a fundamental belief in their independence, and a recognition that it is the practising members who have paid for standard setting, but in a way in which they have no control or influence as a result of being the funders. The money comes through a levy on their firm, payable to a professional body which then pays an unrelated membership fee to IFAC, who have funded the Boards on demand with little or no comment on how and when the money is spent. IFAC have supported the Boards and not controlled them, a model that has been demonstrably successful in the main.

FUNDING THE REVISED FRAMEWORK?

Any new system must adequately deal with the perception that "he who pays the piper plays the tune" and continue with that space between the funders and the standard setters. There is little comment about how the Monitoring Group intend to have their proposed framework funded.

There is little acknowledgement of the enormous value of voluntary input from individuals and firms, both in setting standards and in commenting on Exposure drafts, and the potential cost of a structure that includes remunerated staff to carry out those roles. In section 8 a figure of \$12.5m is given for estimated "contributions in kind" which I find inexplicably low as an estimate. I'm sure that all those firms and individuals would prefer to be paid the proper rate for such work, but there is major question about what that cost is and who is going to pay, and how the pursuit of excellence in the standards remains independent of the funding model, both in perception and in reality.

Much more consultation needs to be carried out with the profession about the appetite to pay more for regulation. My impression in talking to fellow members is that they are at a tipping point in their willingness to continue to fund the further production of standards and guidelines that they feel have less and less practical application in their day to day roles as they deal with smaller and smaller details. Maintaining the support of the profession is absolutely critical in the process of any change, and currently the Monitoring Group does not command that confidence.

Front line practitioners repeat regularly that they are explaining to their clients that their accounts have become so voluminous and convoluted because the regulators demand it, and not because it is reflecting the needs of stakeholders. The cost of audit to the mid-sized sector has increased dramatically while the management advice arising from the financial reporting and audit that added value to the service has reduced. While that criticism is aimed primarily at accounting standards, whoever is to blame for that outcome it is critical that the way in which these proposals and consultations proceed does not destroy what little faith remains with users in the current process.

The profession understands that there was a need for standards, has played their part in introducing them, but is now concerned that very few stakeholders benefit from further descent into detail.

Any direct levy on audit firms will give an increased perception of control by the professions. At the moment there is distance and controls are in place to prevent the public interest being subverted.

PUBLIC UNDERSTANDING

Public understanding of the system must come with a simple framework, and attributable authority.

The standard setting Boards should be independent as far as possible in their operation, and this can be progressed. Discussions about nominating processes and policies are a distraction, but if changes help to improve the perception of independence without reducing the efficacy of recruitment, then they should be pursued.

The process seems to have worked well so far given that the number of appropriately skilled applicants for roles is low. Chairs must possess sufficient knowledge and expertise in the area for which they set the standards if the Board is to be effective and efficient.

Oversight of the Boards is important and the PIOB should be sufficiently powerful to ensure that the Public Interest is maintained and protected. The CAGs should be sufficient to ensure that the work plans of the boards are meeting the stakeholder interests. No Monitoring Group should be necessary other than to drive a process for the recruitment of PIOB members (which there doesn't appear to be for the Monitoring Group). We have ended up with an extra layer of governance which is unnecessary, expensive, and lacking in accountability.

The Monitoring Group advocates a "step by step" approach to reviewing the total framework, moving to look at the role and composition of the PIOB and Monitoring Group itself in due course. Is this a logical approach to regulation? Is it sensible to redesign the SSBs without understanding how they will be overseen and reviewed?

MAINTAINING AUDIT QUALITY?

Again, the timing is unfortunate. There are many debates taking place in firms such as mine (a not insubstantial provincial firm with £30m turnover), about the place of audit as a continuing service line.

As I have explained, I was born into and brought up in a family of practising accountants. Inevitably there were many conversations about the future of the profession, about professional integrity and the challenges to objectivity, and the meaning of independence.

Traditional audit was the mainstay of the professional accounting firms, for a number of reasons. It was a profitable service. It allowed a deep understanding of the clients and their business, so that advice could be given to them about how to improve profitability and efficiency, and protect the public who held direct shareholding investments in companies. Audit staff were trained not just in the language of accountancy and the way that numbers provide a basis for decision making, but with an ability to investigate a business from the shop floor to the board room, making due sceptical enquiry of staff about systems, and making professional judgements about the appropriateness of business decisions, and the way that they were presented in year-end financial statements.

That training was a great basis for a career in business, not just in audit, so it was attractive to the brightest and best graduates, who in turn gave the audit profession a reputation for intellectual analysis and probity.

The changes to the audit process driven by increased technology, different valuation models, and (some would argue) inappropriate regulation, has led to more of a "tick box" mentality in the audit profession. More time is spent by staff designing and completing programme driven audit programs than in making audit judgements and thinking about the output.

Audit is no longer attractive to bright graduates looking for careers in the best businesses.

So for firms like mine, audit is no longer the training model that we would see going forward. Increased costs, or a reduction in trust in the regulators, or a belief that audit is to be regulated by laymen without proper input from the experts (however "independent" that makes the regulator) will accelerate the exodus of firms from the audit service, and will increase the price and reduce the quality of audit.

In the UK, of course we already have an audit threshold below which audit is not mandatory. That is not so in many, many countries, so it needs to be understood that auditing standards often designed for large capital markets are being applied to much smaller entities, and at varying levels of quality around the world. To my mind, issues of audit quality now relate to how standards are implemented rather than how they are drafted, so this paper is focussed on the wrong issue.

COMBINING AUDIT STANDARDS WITH ETHICS STANDARDS?

Of all the suggestions made in this paper, this one has to be the oddest and least well considered. Audit is a service, one of many supplied by the accountancy profession. The number of members of the profession working in the audit service is a minority. Ethics and ethical probity are part of being a professional, and ethical standards apply equally well to those in business or in the not-for profit sector, in general practice outside audit, in financial services, and all the other accountancy related service lines. Appropriating ethics standards solely to the audit profession is extraordinarily arrogant of auditors, and betrays the background and experiences of the authors of this consultation.

There is no way that any practitioner could ever envisage the same people being responsible for both areas. The conflict in priorities and resource allocation would be far too great, the expertise needed is completely different, and the public interest would never be served by combining two such different areas.

And in addition to IESBA rules applying to non-audit services as much as to audit, the IAASB sets standards for reporting assignments other than audit, and other than the audit of large global companies, such as "agreed upon procedures", "compilation reports" etc. There is clearly overlap between the work of the Boards and it makes sense for them to co-operate on specific projects, but it is nonsensical to amalgamate them.

The logic seems to be that audit requires professionalism, so therefore the consideration of the audit service and the behaviour of professionals must be combined. But professionalism is not exclusive to audit. The logic is so, so wrong.

The Monitoring Group believes that audit requires extra ethical standards over and above other professional work, a principle with which I disagree. If Ethical Standards are principle based, then the ethical standards apply to all professional work, even though there may be a need for service specific guidelines.

Are speed and independence the biggest issues facing audit regulation at present?

I would argue that there are two more important, much more challenging, issues facing the audit profession today:

TECHNOLOGICAL CHANGE

Recent advancements in Artificial Intelligence, Blockchain, and in the analysis techniques of Big Data have irrevocably changed the accounting and auditing process, and will continue to do so. An assessment of how these tools are best used, best controlled for the public benefit, and how the results of investigations are fed back into audit committees and impact Board decisions needs to be made urgently.

Audit used to focus on the production of an audit report some months after the year end validating the truth and fairness of Financial Statements, leading to stability in stock market valuations. The measure of the success of that process could be seen in, for example, comparing the market in shares with the market in Fine Art, and the confidence in valuations available to the investor.

To be useful to the public, that service now needs to focus on validating messages impacting on the prices paid by investors, messages that are more immediate, more susceptible to "fake news", and more complex in the effect on valuations.

I do not consider that the IAASB is sufficiently well constituted to step back from detailed drafting of standards and guidelines and to consider this bigger picture. Arguably the CAG might have flagged this up as a significant change to the work programme of the Board, but all the Boards seem to be targeting efforts at the latest big debate within the profession, at reacting to potential or present issues, drafting ever more detailed guidelines on narrow matters, rather than stepping back and taking a broader view.

Nothing in this paper will address this issue.

It is a fundamental flaw in the present framework. Nobody has the authority nor the influence to say to a Board – stop what you are doing, it's very technically challenging and intellectually interesting, but of limited application and a lower priority than other "big picture" matters. At some point there needs to be a cost/benefit analysis of the Board work programmes, a role that I believe should be undertaken by the CAGs who properly represent a broad spectrum of stakeholders.

The danger of not anticipating the impact of technological change lies in the fact that the process of standard setting is to set out expected behaviours and decisions where there are areas in which judgements need to be applied. As more detailed standards and guideline are drafted, the ability to use professional judgement to justifiably vary audit work or processes in specific situations and specific industries is taken away, reducing all judgements to an algorithm that can be carried out technologically.

But major audit issues rely on individuals professional judgements based on experience and understanding that is (anyway not yet) capable of being reduced to an algorithm. Many audit teams are now effectively divided into two teams – one tasked with completing audit documentation in case of a review by the regulator, the other dealing with the difficult judgements and producing value for the audit client. However much we might like to assume that different businesses can be described in a consistent manner using the accounting language, it is a language, not a series of logical yes/no gateways, and a language can have different dialects and idioms that effect the way a message is heard. Businesses differ, and so their financial statement should be allowed to differ to a reasonable extent – but as decades go by, standard setters drive further down into detailed guidance inappropriately. When do we stop and say that we have enough guidance or standards at the correct level of detail to ensure comparability and consistency without further guidance?

The way that technology impacts on the audit service will determine how we draw the line in the tension between individuality and consistency/comparability.

LAW MAKING VS IMPLEMENTATION

The second major issue is that the regulatory focus seems to be entirely on drafting the rules/ principles that govern reporting.

Using Criminal or civil law as an analogy, over the years the law has developed a framework where governments and parliamentary draftsmen design the rules, debate their potential impact, and eventually bring them into the body of law by which we all abide.

There is a separate independent police force tasked with catching those that transgress.

Once a transgression is identified there is a separate judicial body, independent of either the government or police, who make a decision about the fine or punishment that is appropriate, but more importantly also serve as a mechanism for debating whether the law is properly drafted, and feeding back changes as a result of developing case law.

In the audit and accounting profession we have not matured to the point where this framework is in place. Regulator bodies are immature and focussed entirely on where proper regulatory checks and processes are in place, whether a rule has been broken, and imposing a fine. Independence is compromised because often that fine is received by the regulator itself, and some regulators have seats on Standard Setting Boards.

But the point is that a change to the overall framework which aimed to implement a "feedback mechanism" to focus on implementation issues rather than on expected or theoretical law design would also increase efficiency and speed, increase responsiveness, and conserve resources by focusing on practical issues. Too few of the standard setting volunteers are front line auditors or audit partners or Finance Directors.

Less time could be spent on writing the law and more on ensuring consistent and practical implementation.

POSITION OF IFAC

On page 12 of the consultation, there is a statement that "IFAC will continue to play an important role in working with the profession and national regulatory authorities to ensure that global standards are consistently adopted and applied". I do not see that IFAC will in fact necessarily continue in any role dealing with standards if Standard Setting Boards are entirely independent, other than perhaps being a lobby group to voice the profession's concerns about standards. IFAC will have to develop a completely revised mission and purpose and re-negotiate funding arrangements with member bodies, creating demonstrable value under the new structure which would probably include being a regular critic of regulation, albeit constructively.

Certainly the IFAC Compliance Programme referred to in this paper is completely misunderstood. My understanding is that it is not a regulatory tool as suggested, but simply an internal measure of readiness of a member body to be accepted as a member of IFAC, and to monitor their development and maturity.

IFRS FOUNDATION AS A MODEL

It is clear that the Monitoring Group believes that the model used for accounting standard setting, the IFRS model, as a better framework than that of the IAASB; it is seen as a "model of best practice". But in the two critical areas identified as a weakness – speed to market and innovative thought to cope with

technological change, the IFRS model has not performed well. Accounting Standard production is equally slow. The Integrated Reporting initiative did not start within the IFRS Foundation. A standard setting committee is probably not the best place to foster strategic debate; by necessity it considers detail. Arguably the IFRS model has led to a dramatic reduction in the quality of communication between preparers and users using the accounting language, and less confidence in the statutory environment among practitioners; with substantial disadvantage to SMEs, the engine of economic growth in developing nations.

I would also question whether having 22 Trustees is a sensible model, and ask the simple question of that model – whose job is it to stay “stop”, don’t go further into detail because the costs outweigh the benefits, don’t develop more any more detailed standards but look at implementation?

Even the Chair of the Foundation has said that it is very “process driven”.

RESPONSES TO QUESTIONS

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?

Response: After 50 years of standard setting, there needs to be evidence that standards are not developed in the public interest. If there is a risk, then surely that risk must by now be capable of being demonstrated as being a real and not a theoretical risk?

I agree that the Boards are slow to respond to systematic issues such as technological change, but that is not an issue for a particular standard but a fundamental shift in the nature of audit that the Board is currently not tasked with addressing nor, probably, constituted to address. Don’t change the standard setting process to deal with a fundamental paradigm shift.

The other two key concerns are set out above. One is indeed the response to technological advances, the other is to address issues of implementation and standard improvement as a result of practical implementation.

A further paradigm shift is the disconnect between financial statements/ profitability and share valuations in the market.

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

Response: I do not agree that “the importance of high quality auditing is now better appreciated than before the financial crisis”. My discussions with clients and their parliamentary representatives in Government lead me to believe that they do not see audit as any more of a safeguard to a financial crisis than before, so I would need to see some market research outside the profession to believe that statement.

The financial and banking sector are still blamed for the crisis and there is little faith that it could not and will not recur.

Generally the supporting principles are sensible. There are no practical proposals here as to how long term sustainable funding might be obtained outside the profession, and I doubt that this is possible, but am willing to be convinced. This appears to be the only example given where those principles are not currently met, so gives little cause for the creation of an entirely new framework.

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?

Response: There is no mention in the supporting principles of the exercise of professional judgement or of the need for audit to remain a profession, putting the public interest before the client's interest and the client's interest before the practitioners self-interest.

Standards need to be principles based and not rules based; rules based standards leads to gaps that can be exploited (c.f. Enron's accounting)

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?

Response: I absolutely dismiss the idea of amalgamating the Ethics Board and the Auditing Standards Board as illogical. Just because ethical rules are crucial to the proper performance of an audit does not mean they are congruent with audit process rules. Amalgamation would detract from the performance of both Standard Setting Boards and would not be in the public interest.

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?

Response: The Education Standards Board is very different in operation and impact to the Auditing Standards Board. It seeks to ensure that the knowledge, skills and ethical understanding of all practitioners meet consistent basic educational standards globally, despite the many different educational models around the world. The same logic should apply to Education as to Ethics in that both are part of the make-up of the individual practitioner, and success in both is paramount in meeting the public interest.

However, the IAESB standards are written for, and apply to, member bodies not to members so do not guide professional accountants in their day to day work, nor do most professional accountants read or need to be aware of them.

I agree that this Board does not require the same perceived independence of funding required by the auditing standards board, but its future would depend on the future role of IFAC, who may not wish to solicit funding from member bodies to carry out this task; the implementation of the proposals would require IFAC to reappraise its mission and strategy fundamentally, and this may not be a priority.

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

Response: My opinion is that the Standard Setting Boards should be independent and funded by stakeholders more generally and more broadly. However, if no new funding mechanism can be found to maintain sustainable (and demonstrably independent) funding from outside the profession, then the current position should remain.

IFAC is not "responsible for" ethical standards at the moment, the IESBA is responsible, but supported by IFAC, despite the view put forward in this paper.

I believe that the Board is sufficiently independent in thought and action to continue to set Ethical Standards and that there should be no difference between the standards that apply to members in business, in the "not for profit" sector or in practice more widely – auditors are not the only people who think they know how to act ethically.

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.

Response: The framework is currently too complex and expensive for the current funders to continue to pay without seeing practical beneficial output. There should be no need for such a proactive Monitoring Group taking to itself powers not originally granted. Instead, more power and authority should be given to the CAGs and the PIOB to represent stakeholders' views to Boards.

Page 13 of the consultative document sets out the Monitoring Group understanding that CAGs exist to assist with consultation; it would be preferable if they were given wider powers to approved agendas and work plans on behalf of stakeholders. The wording in the paper puts them as subservient to Boards, while the framework diagram clearly shows them in an oversight and managing role. If such power is delegated, then those committees need to be more diverse and more widely distributed globally.

If a Monitoring Group continues in being, it should remain consultative and advisory.

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?

Response: Again, I object to the wording on the first paragraph under "Current Composition and Role" that implies that Board members are not remunerated because IFAC declines to do so. IFAC does not pay Board Chairmen, the Boards do from funds directed through IFAC, but born by the member bodies and ultimately the professional accountants who pay for an audit licence, or a membership subscription.

The only exception to this is the funding provided by the UK regulator to secure a seat on the Board, which as stated elsewhere, I believe should cease and regulators should be independent of the rule drafting, but able to feedback improvements where needed.

The detailed composition of the Boards is a difficult judgement, balancing the need for diversity and attracting global consensus with the need for technical expertise and the perception of independence. There needs to be evidence that the current composition is wrong before a new

formula is put forward. By itself, size is not necessarily the cause of slow law-making, neither is the need for unanimity. A much greater cause of delay is the need to consult globally with member bodies which themselves comprise committees of volunteers. I am not convinced that changing the Board composition would speed up the process.

If sustainable funding could be provided from outside the profession then of course contributors should be paid. There is considerable personal cost incurred by volunteers, and insufficient representation from small firms and business as a result. Indeed it can also be argued that the big firms put forward technical experts who are not on the front line of auditing, and that this leads to standards that are too academic and theoretical. Experience of difficult audit judgements and how they impact on reporting is important in the design of standards.

But this report fails to propose a sustainable funding model, so while fully remunerated Boards would be an advantage, who will pay?

Should the Boards be more strategic – yes, they should encompass a strategic view as well as dealing with the detail of standard setting, but it is not clear to me that they are not already strategic in their thinking about rule making. If greater strategic thinking about new paradigms is needed, or more resource should be put into strategy, then the CAGs should say so and discuss with the Chairs.

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

Response: The Board should be able to adopt standards on the basis of a majority, but only after reaching a global consensus and only if the composition of the Board prevents it from being hijacked, for example by Western democracies, by Euro-centric members, or by other special interest groups. How will this be guaranteed? As soon as a country or a group of countries feels that their views are in a minority and are not being taken into account, they will simply drop out of a global standards regime and revert to a national one, especially given the current nationalist feelings. Decreasing the size of the Board is a high risk strategy, and using the timeliness of standard setting as the reason without evidence that the current size is the cause of slow development of standards risks breaking the whole consensus.

This is a very dangerous direction to follow, and could result in the breakdown of the acceptance of global standards. It seems to me that there are no other professions who have yet succeeded in agreeing global standards and it would be a great shame if audit and accountancy reverted to national standard setting having making such advances.

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?

Response: It is difficult to propose an alternative model without evidence that the existing model is flawed. What is that evidence, and if the number of members is a problem, why is it? If we knew what the problem was, an answer could be put forward.

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

Response: A sufficient number of Board members need front line experience of being an auditor or being audited, of reaching professional judgements, and of a deep understanding of independence and objectivity. The addition of somebody who has worked as an analyst and understands the impact of financial reporting and how it has changed would be helpful. However, the point of this report is that the skills and knowledge of members needs to change in the light of technological advances and should not be allowed to be static.

A decision to bar all members of the profession from the PIOB and reduce the number of informed and experienced Standard Setting Board members will simply drive the influence of experienced personnel into the technical staff body, who will become the only source of technical expertise.

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?

Response: Stakeholder representation should be by CAGs, and stakeholder diversity should not be a driver of Board composition. Sectoral interests should not drive standard setting, but it is critical that there is influence and advice by the ultimate users of the trust provided by audit. That should be via the CAGs which need to be more assertive in their input to the agendas and priorities of the Board's work plans. The paper confuses the process of setting/drafting the rules and the "law" of auditing with the identification of issues that need resolving and their relative priorities.

It can be argued that in 50 years the vast bulk of the law has been agreed and is in place, and that current work strands should be restricted to resolving practical issues identified to be causing problems in the market, and to listening to feedback from regulators as to why some law needs to be updated or amended.

Working on more detailed rules, greater guidance at a lower level, and trying to reduce audit to an algorithmic, mechanical process is not productive. Struggling to describe frameworks and theories of audit in ever more clever ways does little to impact on the day to day business of auditing and the impact of the audit process in management.

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

Response: I see no reason why task force composition needs to be restricted. Their role should be mostly technical, so expertise is more important than accountability. Above them is a structure that ensures the public interest is taken in to account by the Board, the PIOB, the CAGs, etc. Again, where is the evidence that any standard has been drafted against the public interest? If it has happened, why did it happen and therefore how should the framework be charged to ensure it doesn't recur? Without evidence that there is a problem, why amend the structure?

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

Response: My experience is that the nominations process is exceptionally rigorous and completely open. However as long as the process remains unchanged, it might look more independent if it was administered by the PIOB, assuming that they have the resources to take this role.

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?

Response: I have no experience of the activity of the PIOB, except where advice has been given to a Board on due process. Interestingly the only example of a disagreement between a Board and the PIOB that I can recall was when the PIOB refused to allow a small drafting amendment of a proposal to be ratified by a telephone conference call after a physical meeting, explaining that the Board rules did not allow for virtual meetings or conference calls. The end result was the same, but some three months later. Was this ultimately in the public interest or was it an unnecessary adherence to out of date rules, just to be able to say the "due process" had been followed?

Clearly the PIOB should have regular and transparent feedback to the Boards, and as long as no great delay is incurred in the usual process, should be able to veto a standard if they feel it is against the public interest. By which I mean that if, in order to allow the PIOB time to consider and approve a standard, another six month delay has to be built in, I would regard that as being against the public interest in itself. Having on the one hand the power to veto, thereby ensuring better communication between the Board and the PIOB, and on the other building in a delay to exercise a conscious PIOB vote on each standard are two different things.

I do not agree that trying to make the Board multi stakeholder as well as geographically and racially diverse, as well as diverse in experience and technical expertise, is a practical possibility, so my response to the options for reform are that I do not agree the basis on which the proposals are made, no evidence has been presented, and therefore I cannot agree to the options as set out.

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

Response: No

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?

Response: No

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?

Response: PIOB members should be appointed by an open call for members

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 (eg issuing educational standards and ethical standards for professional accountants in business) where they set standards in the public interest?

Response: The PIOB should oversee all standard setting Boards

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?

Response: I agree that the Monitoring Group should retain a consultative and advisory role to the PIOB. I'm afraid that the content and lack of comprehension or evidence displayed in this report about the standard setting process itself leads me to confirm that no further powers should be devolved to a Monitoring Group that is itself not properly accountable. It should however become more public and accountable by publishing its membership, and how its members are appointed and their qualifications and experience so that they are accountable to the public they serve.

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?

Response: I agree that if more resource can be provided, then more technical staff should be paid, and that they should be employed by the Boards.

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

Response: Yes

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

Response: The exposure draft process requires review. Responses tend to come from technical departments or volunteer committee of member bodies, with little extra weight given to responses from front line preparers, auditors or users rather than academics and technical staff. Responses are low in volume. It is difficult for task forces to disagree with comments made, in case they are criticised for not listening.

Timelines are elongated and the time needed to build consensus can be extended where there is disagreement about the best alternative presentation or activity. Indeed, to my mind it is the exposure process that leads to a lack of timeliness in production of standards, not the composition of the Boards, the oversight arrangements or whether staff are paid or not. Much more attention and research needs to be put into identifying the bottlenecks in standard development lies; I suspect it is not in the Committee.

The POB also need to consider the possible impact of these reforms on the shape of the audit market, the ability to attract talent to the audit service, and the business model for audit in the future. It is the PIOB who need to articulate the Public Interest clearly and articulate the threats to the Public Interest, not the Monitoring group.

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)?

Response: I do not agree that the public understand or appreciate the route that funding takes to standard setting, and changes such as those suggested will do nothing to argue that the profession is no longer gaining influence by funding the process. They see that the profession pays and standard setting takes place. The structure in between is labyrinthine and difficult to explain the layman. So the fewer the "layers" of management, the better, but it does help that the ultimate bearer of the cost (the member) cannot trace that payment through to standard setting directly.

If the proposed levy is implemented the vast majority of the levy will be paid by the Big 4 audit firms, and the critical press will easily be able to argue that the standards are set by the audit firms. When the next big audit failure occurs the Monitoring Group will be in the front line for criticism having designed a flawed and self-interested process.

I do believe that the law making, the policing and regulation, and the disciplinary processes should be independent of each other, and that it is this process rather than a criticism of how the model is funded, that gives rise to greater public concern over undue influence.

The example of a regulator paying funds to IFAC and that regulator being the only regulator with a seat on the Board, raises suspicions of undue influence that need to be answered.

I do not agree that the audit profession is any longer the main beneficiary of high quality globally accepted standards. It is true that the main body of standards gave rise to efficiencies in the audit market, but recent new standards have brought no benefit to audit firms, and indeed are leading to a reduction in the number of audit firms in the UK, and probably elsewhere. I believe that a reduction in competition in the audit market will ultimately lead to less innovation, higher costs to companies, and lower quality audits.

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?

Response: The transparency of costs that comes with a contractual levy just to fund audit regulation will focus the mind of many mid-sized firms on the relative profitability and risk of continuing to carry out audits, and on the current spending decisions on whether to invest large sums in audit related technology. It is likely that many firms will then leave the market, leaving the very largest global firms as the only auditors, and denying those skills and expertise to the SME sector, the driver of economic growth. I believe this to be against the public interest.

Any report needs to identify clearly and articulate the current controls that stop funders from having excess authority in standard setting and then explain why these are not working, rather than just tinker with a nomination process.

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

Response: No

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

Response: No