
**STRENGTHENING THE
INTERNATIONAL AUDIT AND
ETHICS STANDARD-SETTING
SYSTEM**

THE MONITORING GROUP

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A. Purpose of the paper

The purpose of this Paper is to present the Monitoring Group's recommendations to strengthen the international audit-related standard-setting¹ system, including the Public Interest Framework, so that future development and oversight of international audit-related standards can be more responsive to the public interest.

The Monitoring Group is committed to advancing the public interest in international audit-related standard-setting and improving audit quality. The members of the Monitoring Group are the Basel Committee on Banking Supervision, European Commission, Financial Stability Board, International Association of Insurance Supervisors, International Forum of Independent Audit Regulators, International Organization of Securities Commissions, and the World Bank Group. The Monitoring Group's mission² is to:

- Cooperate in the interest of promoting high-quality international auditing and assurance, ethical and education standards for accountants;
- Monitor the implementation and effectiveness of the International Federation of Accountants (IFAC) Reforms, and in that connection, to undertake an effectiveness assessment of the IFAC Reforms and other aspects of IFAC's operations that involve the public interest;
- Through its Nominating Committee, appoint the members of the Public Interest Oversight Board (PIOB);
- Monitor the execution by the PIOB of its mandate;
- Consult and advise the PIOB with respect to regulatory, legal and policy developments that are pertinent to the PIOB's public interest oversight; and
- Convene to discuss issues and share views relating to international audit quality as well as to regulatory and market developments having an impact on auditing.

¹ We use this term in the paper to refer to standards issued by the International Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants, which include standards for audit, review, other assurance, and related services engagements, standards on quality control for those engagements, and ethics and independence requirements for accountants.

² See https://www.iosco.org/about/monitoring_group/pdf/monitoring_group_charter.pdf.

The Monitoring Group began to consider the need for further reforms to the audit-related standard-setting system in support of its mission in 2015. It developed a public consultation in November 2017³ to address the following perceptions: (1) the public interest is not given sufficient weight throughout the standard-setting process, (2) stakeholder confidence in the standards is adversely affected as a result of the perception of influence of the accountancy profession on two grounds: (a) IFAC's role in funding and supporting the standard-setting boards and running the standard-setting board nomination process; and (b) audit firms and professional accountancy bodies providing a majority of standard-setting board members and input to the consultation processes for development of standards, and (3) in a constantly changing audit and business environment, standards as currently developed might lack the necessary relevance and timeliness to underpin audit quality and user confidence.

The consultation was supplemented by outreach including regular meetings with IFAC, the PIOB and the Global Public Policy Committee (GPPC).⁴ The MG received 179 responses to the public consultation that are available on the Monitoring Group website.⁵ After analysis and release of a summary of the responses in May 2018,⁶ the Monitoring Group continued to undertake further work and engage in discussion and consultation with a wide range of stakeholders. The Monitoring Group has given careful consideration to and analyzed the feedback from these consultations in developing these recommendations. As a result, the Monitoring Group believes it is in the public interest to issue these recommendations such that these improvements can be implemented as soon as reasonably possible.

³ See <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD586.pdf>.

⁴ The Global Public Policy Committee (GPPC) of the six largest international accounting networks comprises representatives of BDO, Deloitte, EY, Grant Thornton, KPMG and PwC.

⁵ See the responses at http://www.iosco.org/about/?subSection=monitoring_group&subSection1=reforms-to-the-global-audit-standard-setting-process.

⁶ See https://www.iosco.org/about/monitoring_group/pdf/2018-05-31-Monitoring-Group-publishes-Summary-of-Feedback.pdf.

B. The Monitoring Group's Approach

Objectives

The Monitoring Group's recommendations are consistent with its commitment to advancing the public interest in international audit-related standard-setting and improving audit quality. The Monitoring Group recognizes the importance of an independent standard-setting process that provides for the establishment and maintenance of high quality principles-based standards, developed in the public interest by standard setters safeguarded from undue influence. In this regard, these recommendations are principally designed to support and enhance the following objectives associated with the development of high quality standards that are widely adopted and implemented:

- To achieve an independent and inclusive, multi-stakeholder standard-setting structure;
- To reinforce the consideration of the public interest within the standard-setting process and throughout the full cycle of standards' development, including through appropriate independent oversight; and
- To foster the development of timely, high quality standards that respond to an accelerating pace of change.

Scope

The scope of the recommendations covers the responsibilities of the:

- International Auditing and Assurance Standards Board (IAASB);
- International Ethics Standards Board for Accountants (IESBA); and
- Public Interest Oversight Board (PIOB).⁷

The IAASB and IESBA are referred to as the Board or jointly as the Boards in this paper.

⁷ The PIOB refers to the Public Interest Oversight Board, housed within the PIOB Foundation. See <https://www.ipiob.org/>.

C. The Monitoring Group's Recommendations

The Monitoring Group's recommendations are organized to consider the following:

- Accountability, public interest oversight, and governance;
- Purpose, structure, and process of standard-setting;
- Funding; and
- Transition.

Accountability, Public Interest Oversight, and Governance

Accountability

1. The Monitoring Group recommends all levels of the governance and oversight framework be subject to transparent accountability processes, including regular effectiveness reviews and enhanced reporting in the public domain.

2. Specifically, the Monitoring Group recommends to retain the three-tier model,⁸ with the roles and responsibilities of each level clearly delineated and properly balanced, to demonstrate transparency and accountability. The aim of the Monitoring Group is to provide a formal link between the PIOB and public authorities in order to protect the PIOB from undue influence while also enhancing its public accountability.

3. The Monitoring Group will periodically review⁹ the effectiveness of the system as a whole to address any public concerns and to safeguard the effectiveness of oversight. The Monitoring Group will perform its effectiveness review of these recommended reforms no later than five years after their implementation.

⁸ The three-tier model is described at <https://www.ipiob.org/index.php/global-standard-setting-in-the-public-interest/three-tier-standard-setting-model>.

⁹ See the Monitoring Group Charter located at https://www.iosco.org/about/monitoring_group/pdf/monitoring_group_charter.pdf for effectiveness assessment responsibilities.

Public Interest Oversight

4. The PIOB will provide oversight of the standard-setting process to ensure that international audit-related standards are responsive to the public interest, including that they are developed in accordance with the principles of the Public Interest Framework.¹⁰ It shall oversee that the standard-setting activities follow due process throughout the standard-setting development cycle, including that the Boards appropriately considered and balanced input from stakeholders.¹¹

The PIOB's remit will retain the direct oversight of the public interest responsiveness of final standards, including through ongoing engagement with the standard-setting Boards throughout the standard-setting development cycle.

The PIOB's governance responsibilities will include the nomination and appointment process for Board members,¹² protecting the Boards from undue influence, such as commercial, political, and economic influence, in the public interest and overseeing the administration that supports standard-setting, including the ethics and conduct criteria for the PIOB, Boards and staff.

The PIOB will have the appropriate powers, resources, staffing, and expertise to support these additional responsibilities.

Governance

5. The PIOB will include ten¹³ objective and gender diverse members, including the Chair, committed to the public interest. Members shall be drawn from a geographically and experientially diverse variety of stakeholder groups, with experience in the preparation, audit, oversight, delivery and use of financial statements, and with the ability to analyze if the work of the Boards is responsive to the public interest and undertaken in accordance with the Public Interest Framework.

¹⁰ See Section D for the Public Interest Framework.

¹¹ The PIOB will develop operating procedures to support the delivery of its remit.

¹² For the nomination and appointment of Board members other than the Chair, the PIOB will consult with the standard-setting Board Chair. The PIOB will establish and appoint a Nominating Committee (with consideration of diversity in stakeholder groups) to be responsible for facilitating the nomination process and recommending for appointment of members of the Boards, following clearly articulated guidelines. Reference is made to recommendation 8 in relation to conflicts of interest. As described in the "Transition" section of the paper, administrative support may be provided under a service level agreement with IFAC.

¹³ The PIOB Chair will hold a casting vote in the case of a tie.

6. The IOB Chair will demonstrate significant experience in identifying and understanding:

- Interests of users of financial statements;
- The regulatory framework in which capital markets operate; and
- The importance of reliable financial information to transparent markets and thus contributing to promoting financial stability.

7. The IOB members, including the Chair, will be identified through an open call for nominations with clearly articulated guidelines. The method for appointment will be determined by the Monitoring Group with consideration of a skills matrix that fosters leadership, expertise, and diversity of thought and geography. IOB appointments will be made by the Monitoring Group, consistent with currently established terms of three years, renewable once.¹⁴

8. The IOB Foundation¹⁵ will have a written policy on conduct that governs potential conflicts of interest for the IOB, standard-setting Boards, and staff.¹⁶ The Foundation's policies and procedures should set forth a responsibility of members of the IOB, standard-setting Boards and staff to act in the best interest of the Foundation by not putting any personal interest ahead of the interests of the Foundation.¹⁷ These policies must balance the IOB Foundation's role, responsibilities, threats, and safeguards so that the competence and expertise needed for high quality standard-setting is achieved while addressing conduct that raises legitimate concerns regarding the potential for conflicts of interest. Among other topics, the policies should address where conduct associated with outside employment or other outside activities actually conflict or appear to conflict with duties owed to the IOB Foundation.

¹⁴ See Article 10 of IOB consolidated bylaws at [https://www.ipob.org/media/files/about/IOB%20consolidated%20bylaws%20\(English%20Version\)%20092018.pdf](https://www.ipob.org/media/files/about/IOB%20consolidated%20bylaws%20(English%20Version)%20092018.pdf).

¹⁵ The IOB Foundation is the legal entity that houses the IOB. See also footnote 7.

¹⁶ In establishing the conflict of interest policies, the IOB shall consider the responsibilities of each group individually as well as collectively. Such policies shall maintain the principles established in the recommendations outlined herein.

¹⁷ See also recommendation 12 on the relationship of the standard-setting board legal entity structure to the IOB Foundation.

9. The PIOB will assess each Board's effectiveness. The PIOB will:

- Assess the effectiveness of each Board's Chair, taking input from stakeholders;
- Assess each Board's delivery against its agreed strategy and workplan;
- Hold the Boards accountable for the use of its approved budget; and
- Hold the Boards accountable for the results of periodic effectiveness reviews.

10. PIOB meetings will be open to the public with the summaries of minutes published on its website. The PIOB may, at its discretion, hold certain sessions of meetings in private.¹⁸ PIOB will post briefing and observation memos on its website explaining how it discharges its oversight role. The PIOB Foundation will make publicly available an annual report and related financial statements.

Purpose, Structure, and Process of Standard-Setting

Purpose

11. International audit-related standard-setting activities will be undertaken in accordance with the Public Interest Framework. International audit-related standard-setting should reflect the importance of serving the needs of the primary users of general-purpose financial reports, i.e., existing and potential investors, lenders, and other creditors, while also recognizing the needs of other relevant stakeholders to underpin trust in the capital markets.¹⁹ The standards serve the needs of both developed and developing financial markets and all types of entities, including public interest entities, smaller and medium sized enterprises, government and public sector bodies, and not-for-profit institutions.

Structure

12. The PIOB will be responsible for the governance of the Boards and public interest oversight of their agreed responsibilities. The recommendations are written with an over-arching objective

¹⁸ For example, certain sessions of meetings can be held in private if the session is likely to result in discussion of administrative matters including personnel matters.

¹⁹ See Section D for the Public Interest Framework.

that standard-setting activity would be independent from IFAC and that the associated governance and public interest oversight activities will reside within the PIOB Foundation legal entity. The legal structure should be defined considering that the standard-setting Boards should be housed in a separate legal entity outside of and independent from IFAC. The form of the legal structure for standard-setting needs to ensure that recommendations established in this document can be effectively discharged.²⁰

For future fundamental changes to the standard-setting structure, the PIOB, IFAC, and the Monitoring Group will sign a Memorandum of Understanding which will set out, among other things, the due process to accomplish any such fundamental future change. For clarity, this would not change the existing responsibilities of the Monitoring Group, including its ability to perform periodic effectiveness assessments as described in Recommendation 3 and the right to make future recommendations.

13. The governance structure will include a separation between the source of funding and the management of the funds, including their allocation to oversight and standard-setting activities.

Process of Standard-Setting: Board Remit and Composition

14. Standard-setting activities will be carried out by two expert and objective multi-stakeholder Boards. One Board would continue to be responsible for setting audit, review, assurance, and quality control standards and the other Board would continue to be responsible for setting international ethics standards for professional accountants, including auditor independence requirements. In this regard, the Boards will retain the current mandates of the IAASB and IESBA, respectively. Continued enhanced coordination between the Boards is essential to enable each to work more closely on key projects that impact their respective mandates.

15. Each Board will comprise 16 remunerated members, all appointed to act in the public interest.

²⁰ Similar to the existing IFAC reforms that are embedded in the Monitoring Group Charter, the Monitoring Group envisages that these recommendations will be a component of the legal arrangements and statutes of the new structure, in order to ensure stability and legal certainty.

Each board will be composed of a full-time independent Chair,²¹ one part-time Vice Chair, and 14 part-time members.²²

All members will be nominated through an open call and appointed using a skills matrix to be developed for each Board that prioritizes the public interest and fosters leadership, expertise, and diversity of thought and geography. The multi-stakeholder Boards shall be comprised of a balanced group of individuals drawn from diverse stakeholder groups including for example: investors and other users of the financial statements, accountants, regulatory members,²³ audit committee members, academics in the field of accounting or auditing, and audit practitioners.²⁴

16. In order to balance the risk of undue influence by the audit profession with the need for relevant technical expertise in setting high quality international audit-related standards, appointments to each Board are limited to five audit practitioners, including those with recent experience in audits of small and medium sized enterprises and public sector organizations. In this regard, an audit practitioner is defined as an individual who is or has been a member or employee of or otherwise affiliated with a public accounting firm within the last four years, determined at the time of appointment. The classification of a Board member as an audit practitioner shall remain unchanged throughout the individual's board term, including during a period of his/her reappointment.²⁵

Appointments will be for three years, renewable once. Initial appointments may be for a shorter period to allow for a gradual rotation of Board members.

²¹ Existing independence requirements shall be considered. For example, see <https://www.ifac.org/system/files/uploads/IAASB/Independence%20Requirement%20for%20IAASB%20Chair%20-%20Jan%202012.pdf> and <https://www.iaasb.org/publications/call-applications-iaasb-chair>.

²² As part of its periodic effectiveness review, the Monitoring Group will consider whether the part-time nature of members provides the Boards with sufficient capacity and independence.

²³ The reference to regulatory members encompasses the different regulatory and supervisory institutions, and their respective constituents, including those represented in the Monitoring Group. It shall also encompass national standard setters.

²⁴ Individuals might not have just one background, but often – over the course of their careers – individuals will have a combination thereof.

²⁵ For example, an appointed Board member who was employed by a public accounting firm within the last two years prior to appointment would be considered an audit practitioner during all of his/her initial term of three years and the term of reappointment, notwithstanding that it would have been five years since he/she had been employed by a public accounting firm at the date of his/her reappointment to the Board.

17. The Chair, Vice Chair, and members will bring a strategic mindset to each Board and, as a body, advance the timely development in the public interest of new or revised standards. As a whole, each Board along with its staff collectively must have the necessary technical competence, and appropriate expertise to be able to deliver their roles effectively.

For each Board, a two-thirds majority²⁶ of all Board members is required to vote in favor for the issuance of due process documents, such as an exposure draft, final standard, or amendment.

18. The Boards will have sufficient resources and be supported by an expanded and enhanced technical staff, with the capability to take forward the development of relevant, timely, high-quality standards. This can also lead to removing reliance on technical advisors that exists today. Each Board should determine the staffing needed to address the demands and expertise required to support its project work plan. The staff will work under the direction of the respective Board within the new legal entity housing the Boards.

19. Throughout the full development cycle of each standard, the PIOB will engage with the Boards on a timely and ongoing basis to ensure the public interest responsiveness of standards. Notwithstanding the certification process described in Recommendation 21, the Boards will have the ultimate responsibility and accountability for the approval and withdrawal of standards.

Process of Standard-Setting: Board Operating Procedures

20. Each Board will develop a comprehensive and integrated strategy for standards and related agenda priorities. The approach will balance the priorities including of smaller and medium sized enterprises, in a way that serves the public interest. Board meetings will continue to be open and the Boards will consider video streaming. Further, the Boards shall consider enhanced use of their basis for conclusion documents to provide context surrounding the objectives of a new or revised

²⁶ A two-thirds majority of a fully appointed Board (with 16 members) requires 11 Board members to vote in favor for the issuance of due process documents such as an exposure draft, final standard or amendment. A two-thirds majority is needed to prohibit a blocking minority by the accountancy profession. This principle of prohibiting a blocking minority shall be maintained and managed through the establishment of operating procedures which will address more specific fact patterns and required remedies to uphold this principle.

standard, key requirements and issues the standard intends to address, and enhanced transparency as to how the Boards considered and responded to input received during the consultation process.

21. The Boards will regularly engage with the PIOB throughout the full development cycle of each standard to ensure its public interest responsiveness. The Boards will have the responsibility for consideration of public interest responsiveness within the standard-setting process. In its oversight role, the PIOB will timely communicate to the relevant Board any concern around how the public interest is being captured during development of a particular standard and the relevant Board will seek to find an agreed upon solution.

Once a new or revised standard is approved, the relevant Board will provide a public written statement that:

- The Board developed the new or revised standard in accordance with agreed due process; and
- The new or revised standard is responsive to the public interest, in accordance with the Public Interest Framework.²⁷

Subsequently, the PIOB will provide a separate public certification on the approved new or revised standard. The certification will state that:

- The PIOB oversaw the standard-setting process throughout the full development cycle;
- The PIOB considered that the new or revised standard was developed in a manner consistent with agreed due process; and
- The PIOB considered that the new or revised standard is responsive to the public interest, in accordance with the Public Interest Framework.

These operating procedures should contribute to the outputs of the relevant Board's deliberations being appropriate in light of public interest considerations. Considering that the PIOB oversees the standard-setting process throughout the full development cycle, it will timely communicate to the relevant Board any concern around how the public interest is being captured. This would reinforce

²⁷ Existing standards will be grandfathered.

the role of the oversight body in ensuring transparent deliberations of the Boards and evaluating the degree to which standard-setting operates independent of undue interference and remains accountable to the public interest.²⁸ As a consequence of timely communication by the PIOB to the relevant Board throughout the standard-setting process, as well as the multi-stakeholder composition of each Board,²⁹ the Monitoring Group anticipates non issuance of PIOB certification to be very unlikely. If the PIOB is unable to issue a certification, the PIOB will publicly state its reasons.³⁰ In this very unlikely circumstance, the relevant Board will consider the issues identified by the PIOB in determining the best way to resolve the matter, including whether revisions to the standard are appropriate.

22. The Boards will have access to stakeholder advisory councils reflecting diverse stakeholders including national standard setters. The Boards and PIOB will discuss and finalize the nature and form of these advisory councils with consideration that members of the councils will have a term, periodically rotate, be appointed through an open call for nominations, and subject to periodic effectiveness reviews. As standard-related needs arise, the Boards shall have flexibility to appoint ad-hoc advisory groups.

Process of Standard-Setting: Adoption of Standards

23. The adoption and implementation of the standards will be fostered through multiple stakeholders, including IFAC and the PIOB. IFAC will maintain its role in promoting global adoption, convergence, education, implementation, and compliance to ensure that professional accountancy organizations comply with their membership obligations, advocacy, non-

²⁸ See page 7 of the Monitoring Group's 2013 Statement on Governance, https://www.iosco.org/about/monitoring_group/pdf/Monitoring-Group-Statement-on-Governance-and-Feedback-Statement.pdf?v=1.

²⁹ See, for example, the IFRS Due Process handbook- Section 2 at <https://www.ifrs.org/-/media/feature/about-us/legal-and-governance/constitution-docs/due-process-handbook.pdf>.

³⁰ The reason for not issuing a certification shall not be based on a technical disagreement. For further consideration of technical matters and oversight of due process, see also page 7 of the Monitoring Group's 2013 Statement on Governance, https://www.iosco.org/about/monitoring_group/pdf/Monitoring-Group-Statement-on-Governance-and-Feedback-Statement.pdf?v=1.

authoritative guidance, sharing of best practices, surveying for implementation challenges and building capacity of professional accountancy organizations.

Funding

24. Availability of sufficient financial resources will be essential for funding the recommended structure, both initially and over time. The Monitoring Group, giving consideration to the views of IFAC and the PIOB, will continue working for the development of an appropriate, long-term, sustainable funding policy. Acknowledging its key importance to the standard-setting process, the Monitoring Group will prioritize approaches that result in a funding mechanism consistent with the guiding principles of these recommendations, specifically to:

- Strengthen the international audit-related standard-setting system through an independent and inclusive, multi-stakeholder standard-setting structure;
- Enhance the consideration of the public interest throughout the full cycle of standards' development, including through appropriate independent oversight; and
- Foster the development of timely, high quality standards that respond to an accelerated pace of change.

Such a structure, which is key to the successful implementation of the recommended reforms, will have the following features:

- Diversification of contributions from around the world received from the following groups of stakeholders: investors and other users of financial statements, regulators,³¹ and the accountancy profession;
- Stability through medium and long term commitment from contributors and adequate reserves built over time; and
- Prudence and public accountability in the use of funds.

Funding commitments should foster the independence and continuity of the standard-setting activities. This will enable the development of high quality standards as a result of inclusive and

³¹ See footnote 23.

comprehensive consultation with stakeholders globally, public interest oversight and activities in support of wide adoption of the standards.

25. The Monitoring Group acknowledges that achieving the aforementioned funding goals will require time and in the short and medium term recommends to enhance the diversification of funding for the activities of the PIOB, with a goal that contributions from the accountancy profession will become less than fifty percent of the total budget of those activities. The accountancy profession funding should further diminish over the longer term. In order to achieve this goal, the Monitoring Group will perform outreach with stakeholder groups to seek commitments on funding for the PIOB. The Monitoring Group anticipates such outreach to include the regulatory and investor community, including Monitoring Group member organizations. Additionally, the Monitoring Group will aspire to achieve its funding goals for the PIOB by two years after the publication of these recommendations.

26. While IFAC continues to fund standard-setting activities and part of PIOB activities, in order to mitigate risk of undue economic influence, there will be separation between the source of funding and the management of the funds, including their allocation to oversight and standard-setting activities (PIOB and the standard-setting Boards' structure).

Transition

27. The Monitoring Group acknowledges the importance of timely implementation of these recommendations. With this in mind, the Monitoring Group will leverage the support of IFAC and the PIOB, along with input from the standard-setting Boards, in developing a transition plan within nine months from the publication of these recommendations. The transition plan will address the critical components of transition.³² The Monitoring Group, giving consideration to the importance of timely implementation of these recommendations, would not expect implementation to extend beyond a period of three years after the development of the transition plan. While these changes

³² The Monitoring Group anticipates the recommendations in this paper will result in an increase in cost associated with international audit-related standard-setting due mainly to expanded technical staff and remuneration of the Boards' members. The estimation of funds for the revised structure will be developed as a component of transition.

are coming into effect, we expect that the current standard-setting agendas and work of the existing Boards will continue to be delivered. Further, to mitigate disruption risk, the Boards and the PIOB Foundation will continue to be based in their current respective locations.

28. The Monitoring Group anticipates that the new structure will enter into a service level agreement with IFAC for necessary support services (for example, nominations, staffing, communications, and facilities) provided at fully transparent cost. This would be subject to the oversight of the PIOB to advance standard-setting activities while safeguarding against any threat to independence.

D. Public Interest Framework (Framework) for the Development of International Audit-Related Standards

The Framework's Context

All parties who have interest in international audit-related standards recognize that the public interest is best served when the standards are developed by *independent, transparent and publicly accountable* boards that set standards with the *relevant expertise focusing on the public interest* and are subject to *direct oversight* by an independent oversight body, which is equally focused on the public interest, ensuring that the standards appropriately address all stakeholder needs and that no undue influence is exercised by any stakeholder.

This Framework sets out the way development and oversight of international audit-related standards are responsive to the *public interest*.³³

The Framework has been developed in the context of the Monitoring Group recommendations presented in the previous sections. The Monitoring Group also contemplates that in order to maintain its relevance, the Public Interest Framework should periodically be evaluated and refreshed as deemed necessary by the PIOB and the standard-setting Boards. Changes to the Public Interest Framework shall be made in accordance with normal due process requirements.

The Framework sets out considerations essential to the judgments needed by the Boards when developing their standards and by the PIOB in its oversight of the responsiveness of the standard-setting process to the public interest. The Framework, together with due process,³⁴ articulate the public interest responsiveness of international audit-related standard-setting.

The Framework recognizes the criticality of well-functioning, competent and authoritative standard-setting boards, and a competent, alert, and well-informed oversight body, with clarity

³³ This would include standards for audit, review, and related services engagements. This would also include standards on quality control for those engagements along with ethical and independence requirements for accountants.

³⁴ The Boards follow due process as approved by the PIOB and subject to Monitoring Group oversight. Adherence to, and oversight of, due process by the Boards ensures that all necessary procedures for the development of high-quality international standards have been executed, thereby enabling the appropriate evaluation, balancing and weighing of evidence and diverse stakeholder viewpoints.

around their respective roles. A public interest mindset must permeate both. Transparency, monitoring and continuous dialogue are essential.

The Framework's Goal, Approach and Structure

The goal of the Framework is to ensure that standards are responsive to the public interest, through:

- Reinforcement of the importance of independence in a standard-setting process benefitting from deep technical expertise and diversity of perspectives;
- A common understanding by the Boards and PIOB about the meaning of responsiveness to the public interest and which judgments are required for achieving that objective;
- Focus by the Boards on the public interest in their development of the standards;
- Independent PIOB oversight, giving stakeholders confidence that the two Boards set standards that are in the public interest; and
- Appropriate accountability of the PIOB and the two Boards in fulfilling their mandates.

The Framework is developed with the view that the public interest is observed throughout the full cycle of a standard's development: this includes the standard-setting planning, structure and process level, as well as the PIOB's independent oversight.

The Framework is structured around responses to the following questions:

- For whom are standards developed?
- What interests need to be served?
- How are the interests of users best served?
- What qualitative characteristics should the standards exhibit?
- How is the public interest responsiveness of a standard assessed?
- What special considerations are required for international audit-related standards, given their particular public interest relevance?

For whom are standards developed?

Different classes of stakeholders can have legitimate interest in the adequacy of any given standard. For the purposes of this Framework, five broad groups of stakeholders are considered:

- *Users of financial statements* (“the users”) – mainly investors, lenders, and other creditors, who rely on the audited financial statements to make resource allocation decisions.
- The *profession* – all auditors and assurance providers, and other professional accountants in public practice and business who apply the standards.
- Those in charge of *adoption, implementation and enforcement* of the standards as well as monitoring of the capital markets who rely on such standards– including national standard setters, regulators and audit inspectors, market authorities, public sector bodies, and professional accountancy organizations.
- *Preparers* – management and professional accountants in business, for entities of all sizes, in either the public or private sectors, as well as those charged with governance (e.g., audit committees who oversee the audit process), the latter group being relevant to addressing the information asymmetries among different parties involved in the functioning of companies, and who also provide the basis for the auditor’s work.
- *Other users* – the reliability of financial and non-financial information affects a very wide range of interests in society, including consumers, taxpayers, employees, competition and prudential authorities, central banks and bodies in charge of financial stability oversight, and those granting public contracts.

The public interest of standards cannot be ensured through a mere aggregation of all stakeholder interests. Such interests may be mutually inconsistent; some will reflect a stakeholder group’s ability and resources to access the information necessary to protect their interests, while others may have limited capacity to do so; and different stakeholders have different capacities to convey their views. The public interest therefore requires weighing and balancing all stakeholder views.

While the Framework recognizes the importance of all of the above stakeholders, it focuses primarily on the interests of users, and more specifically the longer-term interests of creditors and

investors and the protection of those interests. Creditor and investor decisions are key to the correct functioning of financial markets, but there are creditors and investors who may not always be equipped to contribute effectively to the standard-setting process. These include direct shareholders, debt holders, and those indirectly holding a company's equity or debt, for instance through investment funds or pension funds.

What interests need to be served?

Standards are more likely to respond to users' needs when developed primarily with a view to building trust in the financial and non-financial reporting process. This compels standard setters to carefully consider input from stakeholders seeking standards that:

- Promote consistent practice and behaviors by auditors and assurance providers, other professional accountants in public practice, and professional accountants in business across jurisdictions;
- Facilitate identification of areas most relevant to the business of an audited company, and drive effective measures to respond to related risks;
- Reinforce the professional accountant's role and mindset and the auditor's professional skepticism needed in gathering evidence, challenging assumptions, and developing conclusions; and
- Ensure transparent, independent, rigorous and balanced reporting that prompts the adoption of appropriate measures by those charged with governance, as well as corrective action by oversight bodies, including prudential and market authorities, also to address any potential threat to financial stability.

How are the interests of users best served?

In order to address those interests, the development of standards requires:

- A permanent *structure* that commits explicitly to pursuing the public interest through: i) independence of the Boards in making decisions concerning the standards, ii) balanced, diverse and global participation of stakeholder groups while preventing undue and

dominant influences; iii) stable funding, adequate resources, and appropriately skilled and experienced staff; iv) mechanisms to ensure adherence to sound governance and operating procedures; v) meaningful accountability; and vi) appropriately diverse expertise in board members.

- A standard-setting *process* to ensure that the defined structure: i) considers all stakeholder input and identifies the different stakeholder interests that affect the public interest; ii) defines relevant public interest criteria to consider how to appropriately weigh the input received in terms of the public interest impact of the relative interests; and iii) appropriately balances alternative outcomes and interests in terms of their expected responsiveness to the public interest. This process should recognize the importance of all stakeholders referred to previously but it should focus primarily on the interests of users.
- *Independent, direct oversight* by the PIOB of the Boards' adherence to their agreed strategies, due process, and responsiveness to the public interest, during the development of a standard and, on reflection, upon the final outcome of the process.

User needs, and therefore the public interest, are dynamic, societal concepts that evolve over time. The entire system comprising independent standard-setting and oversight therefore must also remain alert to shifting needs and perceptions and be capable of flexibility of responses; the system must, however, also maintain fundamental stability and the long-term validity and credibility of principles-based standards in order to ensure continuity and inspire confidence.

What qualitative characteristics should the standards exhibit?

A set of qualitative characteristics are to be used as criteria by the Boards and PIOB to assess a standard's responsiveness to the public interest. A non-exhaustive list of such characteristics includes a standard's:

- *Consistency* with priorities established through a strategic planning process, based on the assessment of public interest and stakeholder needs;
- *Coherence* with the overall body of standards, including that requirements addressing the same subject matter are not in conflict;

- Appropriate *scope* to address the identified key issues, and to clearly specify to whom the standard applies;
- *Scalability*, including the proportionality to the standard's relative impact on different stakeholders, e.g., how a standard addresses the audit or assurance needs of small and medium sized enterprises (SMEs) as well the needs of complex, listed entities;
- *Timeliness* in addressing identified needs without sacrificing quality;
- *Relevance*, through recognizing and responding to emerging issues, changes in business or public practice environments, developments in accounting practices, or changes in technology, and developing principles-based requirements that enable the objectives of those requirements to be achieved in differing circumstances;
- *Completeness*, in reflecting the results of broad consultation and in balancing stakeholder priorities;
- *Comprehensiveness*, through limiting the extent to which there are exceptions to the principles set out;
- *Clarity and conciseness*, to enhance understandability and minimize the likelihood of differing interpretations, and thus supporting proper intended application and facilitating implementation;
- *Implementability*, and ability of being *consistently applied and globally operable* across entities of all sizes and regions, respectively, as well as considerations of the different conditions prevalent in different jurisdictions. Standards that cannot be adopted, or cannot be implemented by practitioners are not of much use; and
- *Enforceability*, through clearly stated responsibilities that make it possible to ascertain the extent to which an auditor or professional accountant has complied with the standards.

How is the public interest responsiveness of a standard assessed?

The public interest responsiveness of any new or revised standard is assessed through the Boards considering the qualitative characteristics discussed above and the following steps:

- Identify the varying perspectives and needs of groups with legitimate interests in relation to each standard, throughout the full cycle of its development;
- Define the desired goal that would allow the standard to best serve users' needs. Such goal could be defined in terms of a required audit or assurance practice or auditor/professional accountant behavior, or the introduction of guidance informing the application of practice or behavior already agreed upon;
- Identify criteria to assess the standard's responsiveness to the defined goal, in terms of the qualitative characteristics that the standard should exhibit;³⁵
- According to the criteria, reasonably weigh input from the different groups; and
- Given the defined goal, assess the expected contribution of the standard to users' needs, and consider whether it is responsive to the public interest according to this Framework.

Assessing whether standards are in the public interest requires careful application of judgment, which this Framework seeks to guide both for the Boards and for the PIOB. This judgment is best informed when the standards' development and consultation process elicits all stakeholder views and focus is placed on assessing the merits of the various views, irrespective of whether the views are a minority or majority.

The PIOB should provide oversight of the standard-setting process, by ensuring that due process has been followed by the Boards in developing a standard and that the standards respond to the public interest in accordance with steps and qualitative characteristics set out above. For that purpose, the PIOB has full access to all necessary information of the Boards.

The PIOB communicates its views and the basis thereof to the Boards, in a timely manner throughout the standard-setting process and works collaboratively with the Boards to understand the input received, how decisions were made and then to resolve any remaining differing views.

³⁵ As an example, if reinforcing the auditor's exercise of professional skepticism was considered a goal to be pursued through a particular standard, ensuring that auditors remained professionally skeptical in the wake of changes in measurement bases would be key to determining the standard's responsiveness to public interest, and hence the qualitative characteristics of *timeliness* and *relevance* would be important assessment criteria.

What special considerations are required for international audit-related standards, given their particular public interest relevance?

External audit is intended to provide reasonable assurance around management's fair representation of a company's financial position and performance in all material respects, in the context of the applicable financial reporting framework and taking account of its business model and risk profile. It improves transparency, mitigating the risks of particular information being obscured to the detriment of users of financial statements, and thus enhancing their confidence and ability to make efficient resource allocation decisions. High quality external audit supports the smooth functioning of capital markets, overall economic performance and financial stability.

The Framework assumes that external audits should contribute to mitigating the information asymmetries among different parties involved in the functioning of companies, thus enhancing the reliability of financial information and contributing to more efficient resource allocation decisions. This contributes to the efficient functioning of capital markets, improving overall economic performance and financial stability. This Framework seeks to ensure high quality and relevance through internationally recognized and accepted standards that are consistently applied, and considers the interests of users of financial statements, particularly a broad range of creditors and investors irrespective of their size and sophistication, as those most likely to contribute to such goal. Giving those interests prominence when developing a standard is in accordance with the remit of the Monitoring Group member organizations.

Standards setting out the appropriate requirements and guidance, and promoting consistent audit practice across jurisdictions, are a necessary step to the development of audits that reassure the confidence of users in the reliability of financial statements. When appropriately implemented and enforced, standards contribute to ensuring the high quality of external audits. International audit-related standards promote the integrity and consistency of practices in capital markets, and encourage mobility of auditors between different jurisdictions.

In the long term, standards also enhance the confidence in, and reputation of the global auditing and assurance profession, promoting trust in the decisions of those tasked with enforcement, and contributing to the recognition of management's stewardship role.

E. Appendix: Impact Assessment

The Monitoring Group's impact assessment setting out the benefits of its recommendations is conducted in relation to the status quo. The anticipated benefits of the recommendations set out in this paper are:

- Greater focus on public interest, which may in turn result in standards requiring an increased work effort, likely to have a mitigating impact on the risk of audit failure in future;
- A transparent and accountable process which sets out the importance of the Boards' carrying out impact assessments and post-implementation reviews which demonstrate how effective a standard has been in meeting the objectives set for it. That process also includes public accountability for the PIOB in the allocation of resources to further the public interest;
- Enhanced staffing capacity, providing greater flexibility in resource allocation to reduce the development time for new or revised standards, better supporting the needs of the market through more timely and relevant material;
- The use of a multi-stakeholder model for the Boards, PIOB and due process that broadens participation and the diversity of views available to support the standard-setting process in a way that better serves the public interest. This in turn is supported by advisory councils, which include stronger participation by national standard setters; and
- Through addressing stakeholder concerns, maintaining the value to the global economy of a high-quality and consistent approach to deliver audits.

The Monitoring Group does not have data which would support the accurate estimation of the benefits that arise from the recommendations in this paper, as they have yet to be implemented. However, the Monitoring Group believes those benefits would be significant in qualitative terms to stakeholders, and strongly align to matters of (a) stakeholder confidence, and in particular that of primary users of financial statements, as defined in the Public Interest Framework; and (b) the effective functioning of capital markets and resulting economic and financial stability.

Additionally, as the starting point for standard-setting remains the existing standards, we do not believe this would be disruptive to those who use these standards for the delivery of audits and other assurance-based engagements, thus minimizing costs. Indeed, the Monitoring Group believes that a new model that is better resourced to bring revised standards to market more quickly, and better respond to the increasingly complex needs of audits will deliver a further benefit.