

---

**Intergovernmental Working Group of Experts on  
International  
Standards of Accounting and Reporting  
(ISAR)**

**31st SESSION**  
15 - 17 October 2014  
Room XVIII, Palais des Nations, Geneva

Wednesday, 15 October 2014  
Morning Session

**Key foundations for high-quality reporting: Good practices  
of monitoring and enforcement, and compliance**

Presented by

Gonzalo Ramos  
Secretary-General  
Public Interest Oversight Board (PIOB)

*This material has been reproduced in the language and form as it was provided.  
The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.*

---



**INTERGOVERNMENTAL WORKING GROUP OF EXPERTS ON  
INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING  
15 OCTOBER 2014  
GENEVA**

**MONITORING COMPLIANCE AND ENFORCEMENT: CHALLENGES TO ACHIEVE HIGH-QUALITY CORPORATE REPORTING IN THE AREAS OF AUDIT, ASSURANCE AND ETHICS**

GONZALO RAMOS  
SECRETARY GENERAL-PUBLIC INTEREST OVERSIGHT BOARD

Setting out a global framework for the audit profession requires not only developing standards that are responsive to the public interest, but, equally importantly, their adoption, implementation and enforcement.

My main message to you today is that these tasks are each at a different stage of development, but should all be closely linked to each other. Close coordination between them is critical for the global audit framework to work to produce quality audit. For instance, *adoption* will depend on the extent that standards are developed in the public interest, that is, with the objective of investor protection and avoidance of audit failure. Alternatively, *implementation* can be facilitated through monitoring compliance, more specifically through inspection of audits and *enforcement* measures.

Equally, standard development will benefit from external quality assurance systems and the lessons learnt from inspections.

The generalized creation of audit oversight bodies with the objective to enforce implementation of standards is a very recent phenomenon. The current system of standard development in the field of audit, assurance and ethics works well, but it could work better. What was missing is a system of enforcing the effective implementation of these standards. So I think we should be very optimistic, looking forward, at the prospects of audit quality improving as a result of putting into practice enforcement systems. The main challenge is ensuring that the lessons acquired from inspections find their way into standard development, that is, to develop the processes to feed inspection findings into standard setting.

Let me turn your attention to **the regulatory revolution** that has taken place in the world of audit. The audit profession has evolved, in a very short period of time, hardly ten years, from a self-regulated to a regulated activity. This development started after Enron in 2001 with the creation of the PCAOB in 2002. Its rationale was then to protect investors and try to prevent audit failures. More recently, the absence of any alarm signals from auditors prior to the Global Financial Crisis has generated new expectations amongst regulators that auditing could and should make a greater contribution to detecting and anticipating risks. Today there are more than 50 national audit oversight bodies worldwide which



have in common the power to carry out inspection functions. Most have appeared only over the past 10 years or less.

At the same time, during the same time period, a less visible revolution, perhaps, has also taken place in **standard setting in the field of audit, ethics and education standards**.

The IFAC reforms initiated in 2003 were based on the idea that the audit profession would continue to set professional standards, but subject to independent oversight of the PIOB. The PIOB was created by the Monitoring Group<sup>1</sup> in 2005 with the mandate to oversee standard-setting by the IAASB, IESBA, IAESB and the CAP as well as the nominations processes to these boards.

Since then, under independent oversight, the composition of SSBs has evolved to include 50% non-practitioners; the structures of the CAGs have been created or strengthened to bring stakeholders' representation into standard setting; processes have been developed to ensure that stakeholders are consulted and that their input is considered by the SSBs; and the PIOB has focused its oversight mandate on trying to ensure the public interest responsiveness of the standards under its oversight.

Under these new conditions, all International Standards on Audit were redrafted and reissued under the Clarity project, which was completed in 2008. The new redrafted ISAs were ready to be used when the GFC hit, but it is impossible to say what effect they may have played through improved financial reporting. Since the GFC, the PIOB has responded by further strengthening oversight of the work programs of the SSBs and of the standards under development.

Standard development will continue to be a major challenge for the IESBA and IAASB. For instance, regarding ethics standards, requirements with respect to reporting suspected fraud (NOCLAR) or in relation to auditor independence are being discussed by the IESBA. The Board is also ready to embark on a restructuring of the Code, a review of its threats and safeguards approach, and should also respond to the concerns that have motivated the regulation of independence requirements that is taking place in the EU. With regard to the IAASB, requirements of the new Auditor Report intend to enhance the current report to genuinely offer more and better information. It would also be desirable to see more emphasis placed on audit standards focused on the financial sector by the IAASB to respond to regulatory concerns. Finally, all Education Standards have been recently re-issued under PIOB oversight.

I would like to emphasize here the importance of international standards: Financial regulation rests in the hands of national authorities. However, adopting an international set of standards implies the voluntary acceptance by national regulators of a shared international code. Agreements on international standards are rare and one of the few common financial regulatory frameworks the world has in place. Main examples are the Basel Accords, international accounting standards, and international audit standards. So I

---

<sup>1</sup>The Basel Committee on Banking Supervision, the European Commission, the International Organization of Securities Commissions, the International Association of Insurance Supervisors and the World Bank



speak under the responsibility, which we all share, to preserve and improve this common framework, especially in the current period of financial market fragmentation.

Most national jurisdictions have a strong interest in adopting audit standards that are globally recognized, but are only willing to do so to the extent that these are of high quality and fully responsive to the public interest. This is why independent oversight of the structures and processes just described are so important.

The combination of these two evolutions I have referred to – the regulatory revolution and the evolution of standard setting to respond to the public interest- has **produced a hybrid system that works**, and works well: first, the development and issuance of international standards in the field of audit, assurance, ethics and education is essentially self-regulated by the profession, but takes place under structures and processes subject to PIOB oversight that ensure the public interest responsiveness of these standards; secondly, at national level, domestic jurisdictions may develop or adopt standards, and audit oversight bodies enforce them through inspections. The link is that the international standards developed by the IAASB and IESBA are widely adopted<sup>2</sup> and enforced within domestic jurisdictions. International standards on auditing (ISAs), for instance, currently have a very high rate of implementation – over 100 countries, and their use in Europe will be firmly consolidated after the new EU Audit Directive.

Let me now focus on the **challenges of monitoring compliance and enforcement of international standards**.

IFAC holds responsibility for monitoring compliance by their members regarding the adoption of standards. Through its compliance program and its Compliance Advisory Panel (CAP), IFAC monitors to what extent national professional bodies have adopted and implemented the standards required in the “Statements on Membership Obligations (SMOs)”, which include compliance with quality assurance review systems, international education standards, ISAs, Code of Ethics, IPSAS, and IFRs.

Audit firms hold responsibility for the effective implementation of standards, and apply their own internal systems of quality assurance.

The creation of Audit Oversight Bodies in the last decade has opened a new area of regulatory activity: subjecting audit firms to external quality assurance systems with the power to carry out inspections and impose penalties. These systems provide a strong incentive to firms to implement standards applying sound judgment and increase audit quality. Audit quality indicators are now a reality and will have a significant impact on the industry, since audit firms can ultimately be rated on the basis of uniform quality indicators.

As the excellent paper produced by the Secretariat points out, AOBs face significant challenges in current times of budgetary restrictions. They must have the appropriate legal base and be empowered to impose sanctions. They must also have the technical

---

<sup>2</sup> With different degrees of add-ons and carve-outs



expertise and develop adequate inspection processes. Further, in a globalized industry like audit, where national AOBs are overseeing transnational firms, cooperation amongst AOB is essential. Global international cooperation started in 2005 with the creation of IFIAR, which recently issued its second report on the results of inspections and is currently developing a set of basic principles to promote inspection programs and share results and methodologies. Cooperation within the EU takes place mainly through the EAIG.

The appearance of international bodies that coordinate the systems and findings of AOBs can contribute very significantly to improve the global architecture of standard setting. A main challenge for AOBs is to coordinate internationally to ensure that their findings find ways to influence standard setting in order to correct detected weaknesses. This is a difficult task, because differences in domestic jurisdictions and industries do not make it easy to identify generalized weaknesses in audit. However, the objective is well worth the effort, because standard development will benefit greatly from the results of external quality assurance systems.

Some of these weaknesses have started to appear and are motivating the current debate on audit quality. For instance, it has become evident that professional skepticism needs to be strengthened, that the audit of valuation of financial instruments requires skills that are not always there, or that sometimes independence issues affect audits. What contribution can SSBs make to eliminate these weaknesses?

There are various ways to channel the input from inspections into standard setting and have the SSBs consider whether standards should be amended or developed in line with the inspection findings. It is important here to mention that SSBs are independent in their decision making capacity. The clearest way is for IFIAR and EAIG to become members of the IAASB and IESBA CAGs, which are the structures in place to gather public interest input into standard setting. International organizations members of the MG are already permanent members of the CAGs. Other avenue already being used by EAIG and IFIAR is to provide comments to exposure drafts of standards under development. Finally, IFIAR and EAIG could consider nominating public members to standard setting boards in order to strengthen the voices representing the public interest.

The PIOB has developed processes to monitor the disposition by the SSBs of input from international organizations such as EAIG and other stakeholders like MG members, and stands ready to do the same with other international groups of AOBs.

To conclude, the prospects to improve audit quality are excellent as a consequence of the generalized appearance of AOBs, if only we can get the right global coordination with the SSBs. In the near future we can expect to see the discussions within the IAASB or the IESBA benefiting from the results of the inspections carried out by AOBs.

Finally, before I finish, I would like to mention IPSAS, the International Public Sector Accounting Standards, since I have noted there is a briefing session on Friday which I encourage you to attend. As part of ongoing reforms, it is essential and urgent that the public sector adopts the principle of accrual. The IMF has concluded that the fiscal



Public Interest Oversight Board

response to the GFC would have been less costly if only the real costs had been known, including the guarantees provided to the banking system. It is in everyone's interest that public accounts are subject to similar criteria to those of the private sector. We should extend this demand to all public sector accounts, including central banks and sovereign debt issuers. Adoption of IPSAS by the public sector first needs their being subject to independent oversight that can attest their public interest responsiveness. One could then think of how best to apply external quality assurance systems also to the public sector.

Thank you very much.