

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.