

**INTERNATIONAL FORUM OF
INDEPENDENT AUDIT
REGULATORS
(IFIAR)**

ACTIVITY REPORT 2011

www.ifiar.org

INTRODUCTION

The International Forum of Independent Audit Regulators (IFIAR) was established on 15 September 2006 by independent audit regulators from 18 jurisdictions. Since its creation, IFIAR's membership has grown in light of the establishment of new independent audit regulators in different jurisdictions around the globe, bringing together independent audit regulators from a total of 41 jurisdictions by the end of 2011.¹

IFIAR focuses on the following activities:

- Sharing knowledge of the audit market environment and practical experience of independent audit regulatory activity with a focus on inspections of auditors and audit firms,
- Promoting collaboration and consistency in regulatory activity, and
- Providing a platform for dialogue with other international organizations that have an interest in audit quality.

Since its creation, IFIAR has convened on a bi-annual basis for high-level plenary meetings and on an annual basis at an Inspection Workshop to exchange information and experiences relating to inspections of audit firms. IFIAR plans to move to annual plenary meetings from 2013. IFIAR has established a number of Working Groups that address various work streams important to audit regulators and form the core of IFIAR's activities alongside its plenary meetings and workshop.

IFIAR became a Member of the Monitoring Group during 2011; the Group oversees audit and accounting related standard setting activities of the International Federation of Accountants (IFAC), monitors the activities of the Public Interest Oversight Board (PIOB), and convenes to discuss issues and share views relating to international audit quality and regulatory and market developments having an impact on auditing.²

OFFICE BEARERS:

The Chairman until April 2011 was Steven Maijoor, Managing Director, the Netherlands Authority for Financial Markets. After April 2011, Paul George, Director of Audit at the UK's Financial Reporting Council was elected IFIAR Chairman, having previously served as Vice-Chairman. Dan Goelzer, Board Member of the US Public Company Accounting Oversight Board (PCAOB) was elected as Vice-Chairman in April 2011.

The Chairman and Vice-Chairman are assisted and advised by an Advisory Council in pursuing their responsibilities as set out in the Charter. In 2011, the Advisory Council comprised IFIAR Members from Germany and Japan throughout 2011; France, Norway, Singapore and

¹ A full list of IFIAR Members as of 31 December 2011 can be found in Annex 2.

² Further information about the Monitoring Group, including its Charter, is available at www.iosco.org/monitoring_group/.

the United States of America were members until April 2011; Abu Dhabi, the Netherlands, Canada and Spain joined the Council in April 2011.

The Chairman and Vice-Chairman have two-year terms which expire in April 2013 when new Officers will be elected.

IFIAR FINANCIAL STATEMENTS:

The financial statements for the IFIAR Verein for 2010, covering the provision of administrative resources for the year funded jointly by membership fees, were approved. Annex 1 to this report gives details of IFIAR's joint funding arrangements and references IFIAR's financial results for 2011, available on the IFIAR website at <https://www.ifiar.org/reports/index.cfm>.

IFIAR WORKING GROUPS:

IFIAR currently has the following Working Groups:³

- **Investor Working Group**
 - Responsible for organizing IFIAR's dialogue with investor representatives.
- **Global Public Policy Committee (GPPC) Working Group**
 - Responsible for coordinating IFIAR's ongoing dialogue with the member firms of the GPPC, which comprise the six largest international audit networks (BDO, Deloitte Touche Tohmatsu, Ernst & Young, Grant Thornton, KPMG and PricewaterhouseCoopers).
- **Standards Coordination Working Group**
 - Responsible for establishing a forum for IFIAR Members to share views and concerns about pronouncements from the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA), with a view to helping members consider and incorporate concerns from other members in their submissions to the IAASB or IESBA.
- **Inspection Workshop Working Group**
 - Responsible for organizing the annual Inspection Workshop in coordination with an IFIAR Member serving as the Workshop host.
- **International Cooperation Working Group**
 - Responsible for considering the ways in which IFIAR Members can cooperate and share information relating to audit firm inspections and audit engagements and identifying areas where IFIAR Members can work more efficiently in collaboration.

Updates on the activities of each Working Group are included in the review of activities below.

³ The names of the Groups' member jurisdictions and the Chairs of the Working Groups are listed in Annex 3.

IFIAR ACTIVITIES IN 2011

In 2011, IFIAR held two plenary meetings and an Inspection Workshop, and the IFIAR Working Groups continued to make progress both in support of the plenary meetings and through their own activities.

IFIAR PLENARY MEETINGS:

In 2011, the IFIAR Members gathered on two separate occasions for three-day plenary meetings. The first plenary meeting, organized in April, was hosted by Germany's Auditor Oversight Commission in Berlin, and the second plenary meeting, organized in September, was hosted by Thailand's Security and Exchange Commission in Bangkok.

Consistent with the IFIAR Charter, representatives of the Basel Committee on Banking Supervision, the European Commission, the Financial Stability Board, the International Association of Insurance Supervisors, the International Organization of Securities Commissions, the Public Interest Oversight Board, and the World Bank participated as Observers, and updated members on their work in relation to audit.

The meetings provided the opportunity for IFIAR Members to inform each other about recent national developments, including inspection findings. Some IFIAR Members presented their recently published reports; at the firm level, examples of findings included concerns about:

- Engagement Quality Control Reviews;
- the firms' own internal inspection processes; and
- the firms' incentive and remuneration structures.

Examples of further areas of inspection findings at the engagement level in these reports included deficiencies in:

- The exercise of professional scepticism;
- The audit of fair values;
- Group audits;
- Auditing of disclosures;
- Quality of audit evidence;
- The use of auditors' experts; and
- The provision of non-audit services and other threats to auditor independence.

Some Members noted concerns that audit fee pressure resulting from the on-going challenging market conditions may have a negative impact on audit quality.

IFIAR Members also discussed audit policy topics including issues relating to the sovereign debt crisis, the role of the auditor, the auditor's reporting model, enhancing auditor independence, objectivity and professional scepticism and improving audit transparency.

IFIAR Work Plan to 2013

IFIAR Members agreed in Bangkok on the IFIAR work plan for the period to April 2013. Major activities will include:

- Moving to one plenary meeting each year from 2013
- Reviewing IFIAR's communication activities
- Continuing the progress of the working groups

Core Principles

In Berlin, IFIAR Members discussed and agreed upon a set of Core Principles for Independent Audit Regulators.

The Core Principles are intended to promote the common goal shared by IFIAR Members, as set forth in the IFIAR Charter, to serve the public interest and enhance investor protection by improving audit quality globally, including through independent inspections of auditors and/or audit firms. The Core Principles cover the following areas: (i) the structure of audit oversight, (ii) the operations of audit regulators and (iii) principles for inspection processes.

The Core Principles are not binding on IFIAR Members; however, Members are encouraged to comply with the Core Principles in their own jurisdictions, subject to local requirements or legislation. The Core Principles are enclosed in Appendix 2 to this Report and are available on the IFIAR website <https://www.ifiar.org/aboutus/index.cfm>.

Dialogue with Investors

At the IFIAR Plenary meeting in Berlin, and following the recommendations of investor representatives at the previous IFIAR plenary meeting, discussions focussed on improving the Auditor's Report. For these discussions, IFIAR was joined by Vincent Papa representing the CFA Institute, Martin Baumann, Chief Auditor of the PCAOB, and Dan Montgomery representing IAASB. The European Commission, the UK FRC and IOSCO provided updates on their work in this area.

IFIAR Members agreed with the importance of continued dialogue with investors and will consider further the issues raised.

IFIAR's dialogue with investors is prepared and led by the Investor Working Group . The group is Chaired by Steven Harris, Board Member of the US PCAOB, and includes IFIAR members from Brazil, Dubai, France, Japan, the Netherlands and the United Kingdom.

Dialogue with the International Networks

IFIAR has an ongoing dialogue with the international audit networks that are members of the GPPC. Discussions have included meetings with the chief executives and senior representatives of individual firms and with representatives of the GPPC firms collectively. The focus has been on understanding the role of global networks in audit quality and the response to audit issues arising from the economic downturn. The plenary meetings have included sessions devoted to meeting with the international network firms.

The Global CEO's from each of the international networks of BDO, Deloitte Touche Tohmatsu, Ernst & Young, Grant Thornton, KPMG and PricewaterhouseCoopers participated in the IFIAR plenary meeting in Bangkok.

Discussion topics included issues relating to the role of the auditor, auditor communications, audit committees and their processes surrounding sovereign debt. The Members also discussed a report from the IFIAR GPPC working group on the actions that the networks have taken with regard to frequently-occurring issues discussed with the networks at the Abu Dhabi IFIAR meeting in March 2010. These issues are professional scepticism, group audits, engagement quality control review and revenue recognition. Each of the networks has agreed to meet periodically with the working group to provide an update on their progress in addressing the issues and to discuss policy issues.

The working group now meets with the networks up to three times each year, in addition to GPPC attendance at plenary meetings.

IFIAR's dialogue with the GPPC is prepared and led by the **GPPC Working Group**. The group is Chaired by Brian Hunt, CEO of the Canadian Public Accountability Board (CPAB), and includes IFIAR members from Australia, Brazil, France, Germany, Japan, the Netherlands, Singapore, the UK and the USA.

Discussions with the IAASB and IESBA

The Chairman of the IAASB and the Chairman of the IESBA were invited to IFIAR's September meeting to inform on their work carried out in their respective areas, and for IFIAR Members to provide input to the IAASB and IESBA standards.

Prof. Arnold Schilder, IAASB Chair, provided IFIAR with a presentation on the IAASB work programme, its strategy and its process to consider comments from audit oversight bodies. IFIAR members provided feedback based on their inspection findings on topics including ISA implementation, auditor reporting, disclosures and audit quality.

Ken Dakduk, IESBA Chair, informed IFIAR about the IESBA's current work and the status of the Code of Ethics. IFIAR members provided feedback based on their inspection findings on topics including the provision of non-audit services, audit firm rotation, inadvertent breaches of the IESBA Ethics Code and the enforceability of the Code.

Discussions with the Chairs of IAASB and IESBA provide important feedback from IFIAR Members' inspection activity into the Boards' standard setting activities.

IFIAR's dialogue with the IAASB and IESBA is prepared and led by the **Standards Coordination Working Group**. The group is Chaired by Bernard Agulhas, CEO of the South African Independent Regulatory Board for Auditors (IRBA), and includes IFIAR members from Canada, France, Germany, Italy, Japan, Singapore, Switzerland, UK and USA.

International Cooperation

With regard to international cooperation, IFIAR Members agreed to the proposal that the International Cooperation Working Group study examples of ways in which Members might exchange information, including inspection reports, and how Members may cooperate in the oversight of global firms. These topics are currently being considered further by the International Cooperation Working Group.

The working group holds frequent meetings by conference call throughout the year and plans to hold a workshop on these issues in 2012.

IFIAR's work on international cooperation between regulators is prepared and led by the **International Cooperation Working Group**. The group is Chaired by Doug Niven from the Australian Securities and Investment Commission (ASIC), and includes IFIAR members from Canada, France, Italy, Japan, Korea, Sweden, Switzerland and UK. The European Commission is an Observer to the working group.

Future meetings

IFIAR plenary meetings in 2012 will be in Busan, Korea in April, at the invitation of the Financial Services Commission and the Financial Supervisory Service of Korea, and in London in October at the invitation of the UK's Financial Reporting Council.

IFIAR INSPECTION WORKSHOPS

A core activity of independent audit regulators is the ongoing inspection of audit firms. The development and organization of a robust and sustainable inspection workshop model is central to IFIAR's aim to enhance investor protection by improving audit quality. With member countries from all continents, IFIAR is in a unique position to provide a forum through the inspection workshops for independent audit regulators to meet and discuss inspections processes, learn and leverage from each other, and consider similarities and differences among their practices and methodologies. This information sharing is leading to a better understanding of the Members' respective oversight regimes and the identification of better practices in inspecting audit firms. It is also promoting greater consistency across regulators.

Washington Inspection Workshop

In 2011, IFIAR held its 5th inspection workshop in Washington, DC. The workshop included an induction workshop, a key note address by Mr. John Lipsky, the First Deputy Managing Director of the International Monetary Fund, specific topics and elective topics.

The half-day induction workshop addressed eight common inspection process elements over four hour-long sessions. The main inspection workshop included a total of five plenary sessions, three breakout sessions and eleven elective sessions held over two and a half days. The second half of the first day was dedicated to discussing the current global financial market conditions, along with current and emerging issues relevant to audit inspections. The second day covered four specific topics – undertaking risk based inspections, professional scepticism, inspecting audits of financial institutions, and major recommendations to improve audit quality. The third day covered eleven elective sessions – assessing the effectiveness of external inspections, audit documentation vs. audit evidence, inspection of audits using the work of internal auditors, inspection findings related to partner compensation, international colleges of audit regulators, key elements in the individual inspection reports, non-audit services and its impact on independence, quality monitoring of the audit regulator, reliance on internal controls, supervision of non-PIE audit engagements, and using the work of specialists.

The attendees of the inspection workshops are generally managers of inspection programs and their senior staff, representing almost all IFIAR Members reflecting the high-level interest and value of the inspection workshops. The level of participation, as well as feedback from each workshop, is indicative of Members' broad interest in continuing to share information about their inspection programs.

The 2012 workshop is in March in Abu Dhabi at the invitation of the Abu Dhabi Accountability Authority.

IFIAR's inspection workshops are prepared and led by the **Inspection Workshop Working Group**. The group is Chaired by Tim Volkmann of the German AOC, and includes IFIAR members from Australia, Canada, France, Japan, Norway, UK and USA.

OTHER ACTIVITIES OF IFIAR

On December 5, 2011, the Vice Chair represented IFIAR at a conference on financial institution risk disclosure sponsored by the Financial Stability Board in Basel, Switzerland. In his presentation, the Vice Chair discussed the extent to which auditors in various jurisdictions are responsible for reviewing financial institution risk disclosures and the oversight role of audit regulators. He also summarized the results of an informal survey in which IFIAR members were asked to describe the responsibilities of auditors in their country for risk-related financial institution disclosures and steps taken to enhance auditor compliance with these requirements since 2007.

Monitoring Group Activities

IFIAR joined the Monitoring Group following the Bangkok Meeting in September 2011. It has actively participated in Monitoring Group meetings and activities during 2011, initially as an Observer then as a Member. One of the main initiatives of the Group during the year has been the preparation of a consultation by the Group on its governance arrangements.

For further information on IFIAR, please contact Jon Hooper at the IFIAR Secretariat (j.hooper@frc.org.uk).

Annex 1

IFIAR VEREIN AND FINANCIAL RESULTS:

In order to facilitate the collection and disbursement of membership fees to jointly fund IFIAR's organizational and administrative support, IFIAR formally established the IFIAR Verein, a legal entity under Swiss law, at the IFIAR plenary meeting in Abu Dhabi in March 2010. At that meeting, Frank Schneider (Chief Executive Officer, Swiss Federal Audit Oversight Authority) was elected as Treasurer for the IFIAR Verein for the years ending 31 December 2010 and 2011. The IFIAR Chair and Vice Chair serve as the Executive Committee of the Verein.

In addition to the joint funding of IFIAR's administrative expenses, IFIAR relies upon Members' voluntary sharing of resources to ensure the smooth operation of IFIAR activities. Member contributions include the organization and hosting of plenary meetings and workshops, chairing working groups and hosting working group meetings and conference calls, maintaining Member Profiles and the IFIAR website, and reviewing new membership applications.

The Financial Statements of the IFIAR Verein can be found at <https://www.ifiar.org/reports/index.cfm>.

Annex 2

IFIAR MEMBERS

IFIAR Members are independent audit regulators that are:

- Independent from the audit profession⁴, which means that a majority of the relevant governing body should be non-practitioners (with an appropriate cooling-off period for former auditors) and funding should be free of undue influence by the profession; and
- Engaged in audit regulatory functions in the public interest, in particular responsible for the system of recurring inspection of audit firms undertaking audits of public interest entities, and exercising that responsibility either directly or through oversight of inspections undertaken by professional bodies.

IFIAR continues to monitor the development of new audit oversight bodies around the world and responds to enquiries from potential members or parties interested in information about IFIAR.

In 2011, IFIAR Members were the following:

ABU DHABI

Abu Dhabi Accountability Authority (ADAA)
www.adaa.abudhabi.ae

ALBANIA

Albanian Public Oversight Board

AUSTRALIA

Australian Securities & Investments
Commission (ASIC)
www.asic.gov.au/asic/asic.nsf

AUSTRIA

Austrian Auditors Supervisory Authority
(ASA)
www.bmwfj.gv.at/qkb

BRAZIL

Comissao de Valores Mobiliarios Securities
(CVM)
www.cvm.gov.br

BULGARIA

Commission for Public Oversight of Statutory
Auditors (CPOSA)
cposa.bg/en/

CANADA

Canadian Public Accountability Board (CPAB)
www.cpab-ccrc.ca

CROATIA

Croatian Audit Public Oversight Committee

DENMARK

The Danish Commerce and Companies
Agency (DCCA)
www.eogs.dk

DUBAI INTERNATIONAL FINANCIAL CENTRE

Dubai Financial Services Authority (DFSA)
www.dfsa.ae

⁴ Profession includes, for example, audit firms, professional bodies and bodies or entities associated with the profession.

EGYPT

Auditors Oversight Board (AOB)
www.efsa.gov.eg

FRANCE

Haut Conseil du commissariat aux comptes
(H3C)
www.h3c.org

GREECE

Accounting and Auditing Standards Oversight
Board
www.elte.org.gr

IRELAND

Irish Auditing & Accounting Supervisory
Authority (IAASA)
www.iaasa.ie / www.iaasa.eu

JAPAN

Certified Public Accountants & Auditing
Oversight Board (CPAAOB)
www.fsa.go.jp/cpaaob

Financial Services Agency (FSA)
www.fsa.go.jp

LITHUANIA

The Authority of Audit and Accounting
(AAA)
www.aat.lt

MALAYSIA

Audit Oversight Board (AOB)
www.sc.com.my

MAURITIUS

Financial Reporting Council
www.frc.mu

FINLAND

The Auditing Board of the Central Chamber
of Commerce of Finland (AB3C)
www.ab3c.fi

GERMANY

Abschlussprueferaufsichtskommission -
Auditor Oversight Commission (APAK-AOC)
www.apak-aoc.de

HUNGARY

Auditors' Public Oversight Committee
(APOC)
www.kormany.hu/hu/nemzetgazdasagi-miniszterium/ado-es-penzugyekert-felelos-allamtitkarsag/hirek/knyvvizsgaloi-kozfelugyeleti-bizottsag/

ITALY

Commissione Nazionale per le Società e la
Borsa (CONSOB)
www.consob.it

KOREA

Financial Services Commission (FSC)
www.fsc.go.kr

Financial Supervisory Service (FSS)
www.fss.or.kr

LUXEMBOURG

Commission de Surveillance du Secteur
Financier (CSSF)
www.cssf.lu

MALTA

The Accountancy Board of Malta (ABM)
www.accountancyboard.gov.mt

NETHERLANDS

Autoriteit Financiële Markten (AFM)
www.afm.nl

NORWAY

Financial Supervisory Authority of Norway
(FSA)

www.finanstilsnyet.no

PORTUGAL

Portuguese Audit Oversight Board (Conselho
Nacional de Supervisão de Auditoria – CNSA)

SLOVAK REPUBLIC

Auditing Oversight Authority

www.udva.sk

SPAIN

Accounting and Auditing Institute (ICAC)

www.icac.meh.es

SWEDEN

Supervisory Board of Public Accountants

www.rn.se

CHINESE TAIPEI

Financial Supervisory Commission

www.fsc.gov.tw

TURKEY

Capital Markets Board of Turkey (CMB)

www.cmb.gov.tr/index.aspx

USA

Public Company Accounting Oversight Board
(PCAOB)

www.pcaobus.org

POLAND

Audit Oversight Commission (AOC)

www.mf.gov.pl

SINGAPORE

Accounting and Corporate Regulatory
Authority (ACRA)

www.acra.gov.sg

SOUTH AFRICA

Independent Regulatory Board for Auditors
(IRBA)

www.irba.co.za

SRI LANKA

Accounting and Auditing Standards
Monitoring Board (AASMB)

www.slassmb.org

SWITZERLAND

Federal Audit Oversight Authority (FAOA)

www.revisionsaufsichtsbehoerde.ch

THAILAND

Securities and Exchange Commission

www.sec.or.th

UK

Financial Reporting Council (FRC)

www.frc.org.uk

OBSERVERS:

IFIAR may invite as Observers organizations that have demonstrated an interest in the integrity of the financial reporting system and the quality of the audits through their activities or mandate.

The following international organizations were Observers at IFIAR meetings in 2011:

Basel Committee on Banking Supervisors

European Commission

Financial Stability Board

International Association of Insurance Supervisors

International Organization of Securities Commission

Public Interest Oversight Board

World Bank

IFIAR WORKING GROUPS

○ **GLOBAL PUBLIC POLICY COMMITTEE (GPPC) WORKING GROUP MEMBERS**

CHAIR	:	Brian Hunt	CPAB - Canada
MEMBERS	:	ASIC	Australia
		CVM	Brazil
		H3C	France
		AOC	Germany
		CPAAOB/FSA	Japan
		AFM	the Netherlands
		ACRA	Singapore
		FRC	United Kingdom
		PCAOB	United States

○ **INSPECTION WORKSHOP WORKING GROUP MEMBERS**

CHAIR	:	Tim Volkmann	AOC, Germany
MEMBERS	:	ASIC	Australia
		CPAB	Canada
		H3C	France
		AOC	Germany
		CPAAOB/FSA	Japan
		FSA	Norway
		FRC	United Kingdom
		PCAOB	United States

○ **INTERNATIONAL COOPERATION WORKING GROUP MEMBERS**

CHAIR	:	Doug Niven	ASIC – Australia
MEMBERS	:	CPAB	Canada
		H3C	France

CONSOB	Italy
CPAAOB/FSA	Japan
FSC/FSS	Korea
ACRA	Singapore
SBPA	Sweden
FAOA	Switzerland
FRC	United Kingdom

OBSERVER : European Commission

○ **INVESTOR WORKING GROUP MEMBERS**

CHAIR	:	Steven Harris	PCAOB – US
MEMBERS	:	CVM	Brazil
		DFSA	Dubai
		H3C	France
		CPAAOB/FSA	Japan
		AFM	the Netherlands
		FRC	United Kingdom

○ **STANDARDS COORDINATION WORKING GROUP MEMBERS**

CHAIR	:	Bernard Agulhas	IRBA - South Africa
MEMBERS	:	CPAB	Canada
		H3C	France
		AOC	Germany
		CONSOB	Italy
		CPAAOB/FSA	Japan
		ACRA	Singapore
		FAOA	Switzerland
		FRC	United Kingdom
		PCAOB	United States

Annex 4

IFIAR Core Principles:

Core Principles for Independent Audit Regulators

Introduction

IFIAR is an organization of independent audit regulators (hereinafter, 'audit regulators'). The organization's primary aim is to enable its Members to share information regarding the audit market environment and practical experiences of independent audit regulatory activity, with a focus on inspections of auditors and audit firms.

Consistent with the IFIAR Charter, the Core Principles (hereinafter, 'Principles') seek to promote effective independent audit oversight globally, thereby contributing to Members' overriding objective of serving the public interest and enhancing investor protection by improving audit quality.

An audit regulator's membership in IFIAR is not dependent on its status in implementing the Principles. However, Members are encouraged to work towards implementing them where appropriate in their own jurisdictions, taking account of the risk profile, size and complexity of audit firms in their market. It is recognized that legislative change or other measures by national authorities not in control of the audit regulator may be required to achieve adherence to the Principles.

The Principles are intended to:

- Assist Members in developing their own national arrangements through being able to draw on and hence benefit from the experience of other members;
- Advance widespread adoption of high quality audit oversight practice aimed at fostering high quality audits and promoting public trust in the financial reporting process; and
- Support cooperation between regulators and promote greater consistency of audit oversight.

The Principles may also assist audit regulators who are not already Members of IFIAR to develop effective independent audit oversight arrangements.

The Principles are presented in bold lettering followed by an explanatory text that provides further explanation.

A system of audit oversight and audit regulation can only be effective subject to certain preconditions; that is if it exists within an appropriate external environment. Such preconditions, although often outside the control of the national audit oversight system, in practice have a direct impact on the effectiveness of that system. The main precondition is the existence of a well-developed legal and corporate governance framework as to provide necessary support for high quality auditing. Elements of this framework will cover the following:

- Comprehensive and well defined accounting and auditing principles and standards that are generally accepted;

- Legal requirements for the preparation and publication of financial statements according to those principles and standards;
- An enforcement system for preparers of financial statements to ensure compliance with accounting standards (e.g. fines, shareholder redress or penalties on responsible managers for non-compliance);
- Corporate governance arrangements and practices that support high-quality corporate reporting and auditing practice; and
- Effective educational and training arrangements for accountants and auditors.

Where shortcomings exist, audit regulators should make the government or other relevant decision makers aware of such matters and their potential impact on audit quality or the operation of an effective audit oversight system. Audit regulators should also act, as part of their normal activities, with the aim of mitigating the effects of such shortcomings on the effectiveness of their oversight, regulation and inspection.

Part A. Structure

Principle 1: The responsibilities and powers of audit regulators should serve the public interest and be clearly and objectively stated in legislation.

Audit regulators should have a mandate to work in the public interest and protect investors by seeking to improve audit quality. The responsibilities and powers of audit regulators should, at a minimum, require independent oversight of the audits of public interest entities.

The legal framework for audit oversight should set forth the audit regulator's mandate and responsibilities, and provide the regulator with adequate powers and authority that enable the regulator to perform its audit oversight duties, including powers to address, through inspection and enforcement, compliance with the requirements for the authorization/registration of auditors/audit firms and compliance with applicable auditing, professional and independence standards.

Principle 2: Audit regulators should be operationally independent.

Independence means the ability to undertake regulatory activity and to take and enforce decisions without external interference by those regulated. The audit regulator should be operationally independent from external political interference and from commercial, or other sectoral interests, in the exercise of its functions and powers, including not being controlled in its governance by audit practitioners. The audit regulator should have a stable source of funding, which is secure and free from influence by auditors and audit firms and sufficient to execute its powers and responsibilities.

Principle 3: Audit regulators should be transparent and accountable.

The audit regulator should have public accountability in the use of its powers and resources to ensure that the audit regulator maintains its integrity and credibility. Further, the decisions and actions of the audit regulator should be subject to appropriate scrutiny and review, including appeal to a higher authority. Transparency should include the publication of annual work plans and activity reports, including the outcome of inspections either in the aggregate or on a firm by firm basis.

Part B. Operations

Principle 4: Audit regulators should have comprehensive enforcement powers which include the capability to ensure that their inspection findings or recommendations are appropriately addressed; these enforcement powers should include the ability to impose a range of sanctions including, for example, fines and the removal of an audit license and/or registration.

Audit regulators should at a minimum be responsible for the system and conduct of recurring inspection of audit firms undertaking audits of public interest entities. Audit regulators should have the authority and ability to enforce inspection findings and recommendations. The audit regulator should have comprehensive enforcement arrangements such as fines, suspensions and the removal of an auditor's or audit firm's license or registration.

Audit regulators should have adequate and appropriate mechanisms for enabling information to be brought to their attention by third parties and for then dealing with such information, such as through complaints procedures or through whistle blowing arrangements. These mechanisms should act in a timely and effective manner and their results followed up through an appropriate system of investigations and penalties in relation to cases of inadequate or noncompliant execution of an audit.

Principle 5: Audit regulators should ensure that their staff is independent from the profession and should have sufficient staff of appropriate competence.

Audit regulators should have arrangements in place to ensure that inspection staff members are independent of the profession. These arrangements will, as a minimum, include ensuring that staff members should not be practicing auditors or employed by or affiliated with an audit firm, and that the arrangements are not controlled in any form by a professional body.

In order for audit regulators to be effective, it is a prerequisite that there is sufficient staff of appropriate competence. The persons carrying out the reviews of quality assurance systems of audit firms should have appropriate professional training and relevant experience in auditing and financial reporting, and training in regulatory quality assurance reviews.

This also means that adequate arrangements for consultation and discussion amongst inspectors are in place. New inspectors should be subject to proper supervision and appropriate training.

Principle 6: Audit regulators should be objective, free from conflicts of interest, and maintain appropriate confidentiality arrangements.

Audit regulators should maintain the highest standards of ethical conduct to provide the public with confidence in the objectivity of their decisions. Audit regulators should have in place prohibitions against conflicts of interest by its governing body and staff and ensure that appropriate arrangements are in place to protect confidential information from public dissemination.

Principle 7: Audit regulators should make appropriate arrangements for cooperation with other audit regulators and, where relevant, other third parties.

Taking into account the global nature of the financial markets, where necessary and relevant, cooperation and information sharing with other audit regulators and other third parties, including financial market regulators, is helpful to improve audit quality.

Audit regulators should provide timely assistance to each other within reasonable limits. Arrangements should be in place for sharing information between audit regulators and other regulators (or between parts of the audit oversight system if it involves more than one body), and for protecting the confidentiality of such information.

Part C. Principles for inspections

Principle 8: Audit regulators should as a minimum, conduct recurring inspections of audit firms undertaking audits of public interest entities in order to assess compliance with applicable professional standards, independence requirements and other laws, rules and regulations.

The recurring inspections should be conducted pursuant to a process comprising the selection of the audit firms to inspect, appointment of an inspection teams with appropriate expertise and competence, notification to the audit firm, advance documentation request, notification of selection of audit engagements for review, meetings with management, and on-site inspection arrangements. The inspection process should be subject to appropriate internal quality control within the audit regulator to ensure high quality and consistency.

Principle 9: Audit regulators should ensure that a risk-based inspections program is in place.

Audit regulators should have a process for assessing risks in the audit environment and audit risks in individual regulated firms and their audit engagements. Audit regulators should have a process for taking into account their risk assessment in allocating their inspection resources and in the inspection approaches they adopt. These processes should be commensurate with the size and complexity of the audit firms and their clients. Audit regulators should have an established minimum cycle regarding the frequency of inspections.

Principle 10: Audit regulators should ensure that inspections include effective procedures for both firm wide and file reviews.

The risk-based inspection approach should also be reflected in both firm wide and audit file inspection procedures. The firm wide procedures should address the audit firm's quality control system as reflected in the firm's organization, policies and procedures. ISQC 1 or similar standards should be used as a benchmark in performing firm wide procedures. The inspection process should also include adequate testing of selected audit files in order both to determine the effectiveness of the firm's quality control system and to assess compliance with applicable laws, rules and professional standards.

Principle 11: Audit regulators should have a mechanism for reporting inspections findings to the audit firm and ensuring remediation of findings with the audit firm.

Audit regulators should have a process that ensures that criticisms or potential defects in an audit firm's quality control systems and issues related to an audit firm's performance of audits that are identified during an inspection are reported to the audit firm. Audit regulators' reporting processes should include the preparation and issuance of a draft inspection report, a process for the audit firm to respond, and the preparation and issuance of a final inspection report. In addition, audit regulators should have a process for ensuring that audit firms satisfactorily address inspection findings that were reported to the audit firm by the audit regulator.