United Nations TD/B/C.II/ISAR/63

United Nations Conference on Trade and Development

Distr.: General
21 August 2012

Original: English

Trade and Development Board
Investment, Enterprise and Development Commission
Intergovernmental Working Group of Experts on
International Standards of Accounting and Reporting
Twenty-ninth session
Geneva, 31 October–2 November 2012
Item 3 of the provisional agenda

Regulatory and institutional foundations for high-quality corporate reporting: Main trends and challenges

Issues note prepared by the UNCTAD secretariat

Executive summary

Over the last three years, UNCTAD's Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) has been working on an Accountancy Development Toolkit for high-quality corporate reporting with a view to supporting member States in their efforts towards the adoption and implementation of international standards and codes. The two main components of this tool are (a) an accountancy development framework and (b) a set of accountancy development indicators. The Toolkit is built around the core pillars of the accountancy foundation for high-quality corporate reporting: a legal and regulatory framework, an institutional framework, human capacity, and a capacity-building process. In concluding its twenty-eighth session, the Group of Experts proposed to focus its deliberations during the twenty-ninth session on the regulatory and institutional pillars.

This issues note was prepared by the UNCTAD secretariat in order to facilitate ISAR discussions on this topic, to raise awareness of main issues and share good practices in this area in order to assist developing countries and countries with economies in transition in formulating national policies on accountancy development. It provides a general overview of major recent trends in and challenges relating to regulatory and institutional developments at the global, regional and national levels. It highlights such trends as the strengthening of institutional standard-setting at the global level and the growing role of reporting standards in the international financial architecture; the increasing role of international bodies, not only in standards formulation, but also in the area of

enforcement and implementation; the increasing role of national State regulations and institutions, and that of regional organizations. It also discusses some of the major challenges in regulatory and institutional capacity-building, such as the need to develop mechanisms to ensure the consistent application of international standards and monitoring of compliance. Other issues discussed include the higher demand for non-financial reporting, increased pressure for stakeholder coordination at all levels, the need for a coherent strategic approach to building national regulatory and institutional capacity, and issues of sustainability of accounting reforms. The examples given in this note serve to illustrate some of the regulatory and institutional developments of corporate reporting rather than provide a comprehensive list of good practices that could be a subject for further research and discussions.

Contents

Introduction and background

1. In the wake of the financial crisis, continued efforts are being made to improve the quality of corporate reporting as an essential component of measures aimed at strengthening the international financial architecture. High-quality corporate reporting is key to improving transparency, facilitating the mobilization of domestic and international investment, creating a sound investment environment, fostering investor confidence and promoting financial stability. A strong and internationally comparable reporting system facilitates the international flows of financial resources, while at the same time helping to reduce corruption and mismanagement of resources. It also strengthens the international competitiveness of enterprises by attracting external financing and benefiting from international market opportunities.

2. In this regard, the implementation and consistent application of internationally recognized standards, codes and good practices in the area of corporate reporting have been strongly encouraged. However, the effective adoption of such standards and codes remains a challenge for many developing countries and economies in transition, as they lack some critical elements of corporate reporting infrastructure – from weaknesses in their legal and regulatory frameworks, to a lack of human capacity and relevant institutional arrangements.

3. With a view to supporting countries in their efforts towards the adoption and implementation of international standards and codes, UNCTAD, through ISAR, has been working on an Accountancy Development Toolkit for high-quality corporate reporting over the past three years. The two main components of this tool are (a) an accountancy development framework and (b) a set of accountancy development indicators. The Toolkit is built around the core pillars of the accountancy foundation: a legal and regulatory framework, an institutional framework, human capacity and a capacity-building process. It provides guidance on the key elements of each of the pillars, international benchmarks for relevant policies and capacity-building, and measurement indicators to identify gaps and priorities and to monitor progress. UNCTAD/ISAR have been conducting pilot tests over the past two years on the practical application of the Toolkit in countries such as Brazil, China, Côte d'Ivoire, Croatia, Mexico, the Netherlands, the Russian Federation, South Africa and Viet Nam. The Toolkit was launched at the High-level Meeting on Accounting for Development, held on 22 April 2012 in Doha at UNCTAD XIII.

4. As agreed by member States at the twenty-eighth session of ISAR, the topic proposed for the main agenda item at the twenty-ninth session is "Regulatory and institutional foundations for high-quality corporate reporting". The aim of this paper is to provide a background document for this discussion. It builds further on the framework document on capacity-building for high-quality corporate reporting contained in document TD/B/C.II/ISAR/56[1] and its addendum TD/B/C.II/ISAR/56/Add.1; and on document TD/B/C.II/ISAR/59,[2] where indicators and a measurement methodology for accountancy development are explained. Therefore, this note should be considered in conjunction with the above documentation. It also reflects further UNCTAD research on the topic as well as the initial feedback from the pilot tests.

[1] http://archive.unctad.org/en/docs/ciiisard56_en.pdf.

[2] http://archive.unctad.org/en/docs/ciiisard59_en.pdf.

I. Major trends in and challenges relating to regulatory and institutional developments for high-quality corporate reporting

5. The legal and regulatory framework covers laws, regulations, standards, codes, requirements and guidelines that incorporate the body of requirements to be followed by all participants in the corporate reporting chain to produce high-quality reports, including financial and non-financial information. It should "be set to ensure that participants along the reporting chain perform certain tasks at a required level of quality. For example, it should provide the framework to:

(a) Develop, enact or amend appropriate laws and regulations;

(b) Endorse and enforce accounting and auditing standards and ethical norms;

(c) License and monitor statutory auditors in line with quality control requirements;

(d) Review statutory financial statements and reports (for example, pertaining to prudential regulation) and/or listed company financial statements and reports in line with accounting standards and disclosure requirements;

(e) Qualify accountants at the professional level by both examinations and practical training as well as others, e.g. regulators;

(f) Discipline individuals and firms;

(g) Ensure continuing professional development;

(h) Ensure good governance in both the private and the public sector".[3]

6. A certain institutional foundation should be in place to ensure that such regulatory requirements exist, are enforced and duly complied with. While particular institutions and bodies that deal with different aspects of accountancy regulations differ depending on the civic architecture of a country, key institutional functions and arrangements are required along the reporting chain in order to produce high-quality corporate reports. In particular, institutional responsibilities for each of the aforementioned regulatory functions should be clearly spelled out; a good governance system within each of the regulatory bodies should be developed; mechanisms should be put in place to ensure sustainability of the functions and bodies, including financial sustainability; systems for quality control and performance measurement should be set up; and efficient coordination among these institutional functions and bodies ensured.

7. In recent years, a number of further developments have promoted the strengthening of regulatory and institutional foundations for corporate reporting, facilitated by lessons learned during the global economic and financial crisis.

8. The crisis showed beyond any doubt that the financial system is truly global. It is evident that the financial situation in one country is driven by what happens in others, and it follows that the financial regulations of one country can affect all others. This has underlined the need for a far greater standardization of corporate reporting requirements and coordination among regulators on a global basis to avert future worldwide economic disasters.

[3] TD/B/C.II/ISAR.56.

9. The economic and financial crisis has also brought into sharp focus the reality that the regulation of corporate reporting is just one piece of a larger regulatory configuration, and that forces are at play that would subjugate accounting standard-setting to broader regulatory demands. Today, in the aftermath of the crisis, financial accounting standard-setting finds itself drawn into the orbit of complex political processes focused on restructuring the regulation of the world's financial markets. Proposals abound on how regulation of financial markets and financial institutions should be changed to mitigate the potential for such large-scale financial meltdowns in the future. The crisis has galvanized politicians, regulators and economists to scrutinize financial accounting standards as never before, creating significant pressure for change.

A. International and regional developments

10. In this regard, a major trend has emerged since the crisis: accountancy development policies and policies affecting accounting regulations are being increasingly crafted by international groups.

11. Another important trend is a growing understanding that a regulatory system is not just about standard-setting but also about the enforcement and the monitoring of the consistent application of such standards, and compliance with requirements.

12. Historically, issues of compliance with standards were not given much importance at the global level, reflecting a range of factors such as the desire to increase the number of countries adopting such standards, limited available resources, traditions of self-regulation and professional peer reviews, and the clear positioning of responsibilities for compliance, regulation, and oversight activities at the national, rather than the international level. However, in recent years, a number of developments have taken place that reflect a growing need for accountancy, regulatory and institutional arrangements at the global level, including a need for further guidance to ensure the consistent application of international pronouncements. A recent example of the latter is provided by the letter[4] sent by the Chairman of the International Accounting Standards Board (IASB) to the European Securities and Markets Authority in 2011 on International Accounting Standard 39 for banking concerning fair value measurement in European countries. IASB found inconsistencies, particularly in accounting for distressed sovereign debt, including Greek government bonds. Therefore, even though IASB does not have the authority to ensure compliance with International Financial Reporting Standards (IFRSs), due to the relevance of the issue and the interest in ensuring the highest quality in the application of such standards, it decided to bring the matter to the attention of the Authority. This unprecedented action underscores yet again the relevance of the appropriate application of standards in ensuring high-quality corporate reporting.

13. A number of activities are under way to improve and strengthen institutional arrangements at the global level. Most of them address the need for better institutional coordination and cooperation, for improvement of governance and monitoring arrangements for the standard-setting processes for high-quality corporate reporting, and for monitoring and compliance with international standards.

14. The Financial Stability Board was established to coordinate, at the international level, the work of national financial authorities and international standard-setting bodies and to develop and promote the implementation of effective regulatory, supervisory and

[4] http://www.ifrs.org/Current-Projects/IASB-Projects/Financial-Instruments-A-Replacement-of-IAS-39-Financial-Instruments-Recognitio/correspondence/Documents/LettertoESMA4August2011.pdf.

other financial-sector policies. It brings together national authorities responsible for financial stability in significant international financial centres, international financial institutions, sector-specific international groupings of regulators and supervisors, and committees of central bank experts.

15. The Board is responsible for coordinating and promoting the monitoring of the implementation of agreed financial reforms, of which convergence towards a single set of high-quality global accounting standards is an essential part, and its reporting to the Group of Twenty (G-20). In order to strengthen the coordination and effectiveness of this monitoring process, the Board, in collaboration with the standard-setting bodies, established a framework for monitoring and reporting on the implementation of the G-20 financial reforms in October 2011 called the Coordination Framework for Implementation Monitoring. This framework was subsequently endorsed by the G-20 at the Cannes Summit in November 2011.

16. IASB has been focusing its activities on completing the projects it agreed to work on jointly with the Financial Accounting Standards Board (FASB) of the United States of America under their memorandum of understanding as well as other joint projects, such as insurance contracts. In the third quarter of 2012, the remaining issues of the memorandum of understanding and joint projects on the IASB agenda were financial instruments, leasing, revenue recognition and insurance. During the first-half of the year, IASB and FASB strove to reach a consensus on impairment accounting, classification and measurement. The two bodies expect completion of the new impairment requirements in the first half of 2013. The IFRS on general hedge accounting is due for completion by the end of 2012 or in early 2013. An exposure draft on macrohedge accounting is targeted for publication in the autumn of 2012. The proposed standard on revenue recognition had been re-exposed for comment, and a final standard is expected by early 2013. A final standard on leases is also expected in mid-2013. In relation to insurance, IASB will re-expose the draft standard in the last quarter of 2012.

17. The IFRS Foundation Monitoring Board has been conducting a review of the Foundation's governance arrangements to assess whether they promote the primary mission of the IASB of developing high-quality, understandable, enforceable and globally accepted accounting standards. In February 2012, the Monitoring Board announced the conclusion of its review of the governance of the IFRS Foundation and published its final report.[5] The Monitoring Board made a number of decisions regarding the Monitoring Board itself, the IFRS Foundation Trustees and IASB. The Monitoring Board decided to limit membership to capital market authorities responsible for setting the form and content of financial reporting, to continue with the consensus-based decision-making process and to coordinate its periodic governance review with the Foundation's five-yearly Constitution Review.

18. The International Federation of Accountants (IFAC) has moved towards establishing an active Public Interest Oversight Board (PIOB) starting in February 2005. PIOB members have been selected by leading institutions in the international regulatory community, including the International Organization of Securities Commissions (IOSCO), the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors, the European Commission, the World Bank, the Financial Stability Forum and the Financial Stability Board. One of the activities of PIOB is to monitor all the meetings of the IFAC standard-setting committees, making this a very active process of public oversight.

[5] http://www.ifrs.org/NR/rdonlyres/2CABFD51-7F0E-47A5-BA99-F7A8B4E99C6F/0/GovernanceReviewFinalReportFeb2012.pdf.

19. IFAC increased its focus on global compliance issues with the launch in 2004 of its compliance programme, overseen by the Compliance Advisory Panel, which seeks to ensure that member bodies meet their membership obligations. In October 2011, the Panel published its Member Body Compliance Strategy for 2011–2014. According to the strategic plan, a revision of the statements of membership obligations is to be concluded by October 2012. The Panel plans to intensify its cooperation with independent standard-setting boards with a view to providing them with important feedback on successes and challenges in terms of adoption and incorporation, and implementation of the respective boards' standards.

20. The objectives and principles of IOSCO stress enforcement of securities regulation and information-sharing. IOSCO provides a set of principles for cross-border cooperation, but also notes the complications caused by the differences in national legislative regimes within which regulators work. These include differences in approach to enforcement and constraints relating to information sharing; resources available to the regulator may also impede cooperation. In May 2012, IOSCO announced a new transitional board that will implement a new structure for the organization. The Transitional Board will subsume the functions of the Technical Committee, the Executive Committee, and the Emerging Markets Committee Advisory Board. IOSCO indicated that the restructuring measures were being taken with a view to ensuring that IOSCO is structured and positioned to continue providing the lead in the development of regulatory standards for capital markets; that it has the requisite resources needed to engage in the identification of emerging securities markets risks; that it possesses the capacity to meet the needs of its members; and that it is prepared to respond to requests for project work by the G-20 and the Financial Stability Board.

21. The issue of public oversight was developed further on the international stage by the establishment in September 2006 of the International Forum of Independent Audit Regulators. The Forum provides a means for independent national audit regulatory agencies to share their knowledge and experience of the audit market and associated regulatory activities. It seeks to promote collaboration and consistency in regulatory activity and to act as a platform for dialogue with other organizations with an interest in auditing quality. There are currently 28 independent national regulators that are members of this new international organization, including the Public Company Accounting Oversight Board (PCAOB). Observers at meetings of the Forum include the Financial Stability Forum, IFAC, PIOB, IOSCO, the International Association of Insurance Supervisors, the World Bank, the European Commission, and the Basel Committee, again reflecting the increasingly interlocking nature of international regulatory relationships.

22. A distinct trend in regulatory and institutional developments is thus the facilitation of global institutional standard-setting and the growing role of international bodies, not only in formulating the standards, but also in relation to their enforcement, consistent application and compliance.

23. Therefore, in creating and strengthening national regulatory and institutional foundations, national regulators need to increase communication and cooperation with the relevant international organizations. At the same time, international bodies need to further improve and expand means of ongoing interaction with national standard-setters. This poses challenges for both sides, as more resources are needed, including financial resources and technical expertise.

24. One means of addressing these challenges is to develop more international guidance on the application of international standards and codes by international bodies. For example

in July 2012, the United States Securities and Exchange Commission issued a final report[6] in which it discusses its work plan for considering the adoption of IFRS for United States companies. The report states that diversity in the application of IFRS poses comparability challenges across countries and industries. Among the different causes of these variations, the Commission mentions the lack of guidance in some areas, in addition to the set of options allowed by IFRS and, in some cases, the lack of compliance with those standards.

25. Another means of assisting countries in their regulatory and institutional capacity-building is to provide forums and opportunities for national regulators on sharing good practices. Take the ISAR standing group of experts, for example, a forum that since 1982 has been helping developing countries and countries with economies in transition implement international standards on accounting and reporting. Many developing countries and countries with economies in transition need to re-build or upgrade their national regulatory and institutional standard-setting towards standards and codes formulated by international standard-setters based on the most advanced international requirements and practices. Consequently, sharing good practices and lessons learned is of crucial importance for them. Another example is the Emerging Economies Group, discussed below. Comparative views of other regulatory systems enable regulators to develop a more tailored approach to their own system.

26. For over a decade, the World Bank has been conducting a report on the observance of standards and codes (ROSC) in accounting and reporting[7] with a view to assisting its member countries in implementing international accounting and auditing standards to strengthen the financial reporting regime. The objectives of this programme are to analyse the comparability of national accounting and auditing standards with international standards; to determine the degree of compliance with applicable accounting and auditing standards to assess the strengths and weaknesses of the institutional framework in supporting high-quality financial reporting; and to assist a country in developing and implementing a country action plan for improving institutional capacity with a view to strengthening its corporate financial reporting regime. To date, the World Bank's ROSC programme has covered over 90 countries, publishing over 100 reports.

27. Another important means of creating a sound institutional and regulatory foundation is to facilitate further the participation of less developed countries in the international processes and to better understand and consider their needs. Reflecting this need in 2009, the G-20 advised IASB to include emerging economies in the standard-setting process. As a result, the Emerging Economies Group[8] was created in 2011. Its activities focus on issues relating to the application and implementation of IFRSs in emerging economies, including suggestions of how IASB can provide educational guidance on these matters. The current members of the Group are Argentina, Brazil, China, India, Indonesia, Malaysia, Mexico, the Republic of Korea, the Russian Federation, Saudi Arabia, South Africa and Turkey. The group is chaired by the Director of International Activities at IASB, and the Vice-Chair is the Director-General of the Accounting Regulatory Department, Ministry of Finance, China.

28. Another recent trend in the area of regulatory standard-setting is a growing interdependence of national regulatory requirements and the increasing impact of the regulatory requirements of one country on another's jurisdiction. This situation is particularly true in countries hosting the world's leading stock exchanges. Such is the case of PCAOB in the United States of America, which inspects accounting firms that audit

6 http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf.
7 http://www.worldbank.org/ifa/rosc_aa.html.
8 http://www.ifrs.org/The+organisation/Advisory+bodies/EEG/About-the-EEG.htm.

companies listed on the United States market. In fact, companies listed on United States exchanges are required to be audited by an audit firm registered with PCAOB. These inspection activities are also applicable to foreign issuers listed in the United States, as a result of which PCAOB has been trying to conclude bilateral agreements with other countries in order to be able to review foreign accounting firms. Currently, more than 900 audit firms registered with the PCAOB are located outside of the United States, in 87 countries.[9] Of these, 59 firms are located in the United Kingdom of Great Britain and Northern Ireland, 8 in Switzerland and 110 in China and Hong Kong (China).

29. Recently, PCAOB, the Swiss Federal Audit Oversight Authority and the Swiss Financial Market Supervisory Authority entered into a cooperative agreement that includes the sharing of confidential information. Indeed, the Dodd-Frank Wall Street Reform and Consumer Protection Act[10] signed into law in July 2010 amended the Sarbanes-Oxley[11] Act to allow the Board to share confidential information with its non-United States counterparts. Under the cooperation agreement, United States regulators will be able to perform joint inspections with Swiss authorities of Swiss firms auditing companies listed in the United States. The Board expects that these agreements will encourage other countries to accept similar agreements. For example, negotiations have been renewed with China, and the representatives of both regulators met in July to discuss a bilateral cooperation agreement.[12]

30. An important development in the area of regulatory and institutional standard-setting is the growing role of regional bodies aiming to carry out and coordinate efforts related to IFRS implementation and the consistent application of standards.

31. In Europe, an example of enforcement and coordination at the regional level is given by the Committee of European Securities Regulators,[13] known as CESR, since renamed the European Securities and Markets Authority, which conducted a review of European enforcers' experience during the first year of IFRS adoption for issuers listed in the European Union. This report showed that 20 out of 27 member States had introduced an enforcement mechanism by 2006 that met, at least in part, the requirements laid down by standards of the European Securities and Markets Authority on enforcement.

32. The Authority in 2004 set up a forum, the European Enforcers Coordination Sessions (EECS) to enable its members and other enforcers of the European Union that are not members of the Authority to exchange views and discuss their experiences relating to the enforcement of financial information. EECS aims to promote a high level of consistency among enforcers' decisions. Cases discussed by EECS are registered in a confidential database, which can be accessed by all European enforcers.

33. Another example of regional institutional standard-setting is the European Financial Reporting Advisory Group, established in 2001. It is a technical committee and advises the European Commission on the endorsement of new or amended IFRSs and IFRS interpretations. It also provides an input to IASB/FASB convergence efforts and holds observer status in certain IASB working groups.

---

9 http://www.big4.com/deloitte/pcaob-strikes-swiss-deal-extending-oversight-into-switerland-721/.
10 http://www.sec.gov/about/laws/wallstreetreform-cpa.pdf.
11 http://www.soxlaw.com/.
12 http://pcaobus.org/News/Releases/Pages/07062011_China.aspx.
13 CESR's review of the implementation and enforcement of IFRS in the EU (European Union). November 2007. Available from http://www.esma.europa.eu/system/files/07_352.pdf.

34. The Asian-Oceanian Standard-Setters Group[14] was formed in 2009 to reach the following objectives:

(a) To promote the adoption and convergence with IFRSs by jurisdictions in the region;

(b) To encourage consistent application of standards;

(c) To coordinate input from the region on technical activities to IASB;

(d) To collaborate with governments, regulators and other regional and international organizations in improving the quality of financial reporting.

35. The educational sessions of the Group are designed to help members build capacity and more developed jurisdictions and to support others by sharing experiences and examples of implementation.

36. The Group of Latin American Accounting Standard-Setters[15] was set up on 28 June 2011. Its 12 members are Argentina, the Plurinational State of Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Panama, Paraguay, Peru, Uruguay and the Bolivarian Republic of Venezuela. Its objectives include the following:

(a) Interacting with IASB by providing technical input to all documents published for comments;

(b) Promoting the adoption and/or convergence with IFRSs in the region as well as their consistent application;

(c) Cooperating with governments, regulators and other regional, national and international organizations in contributing to the improvement of quality of financial statements;

(d) Collaborating in the dissemination of the standards issued by IASB in the region, particularly in member countries;

(e) Providing proposals for the IASB agenda, and coordinating its alignment with that of the region;

(f) Taking part in the technical meetings of the National Standard-Setters and World Standard-Setters, as appropriate, respecting the national sovereignty of each member country participating in both groups;

(g) Interacting with other organizations in Latin America, such as the Union of South American Nations, the Southern Common Market and the Andean Community, on issues related to accounting standards.

37. In the case of Africa, the West African Economic and Monetary Union[16] aims to achieve the economic integration of its members: Benin, Burkina, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo.

38. In 1998, the West African Economic and Monetary Union also created a common accounting system, called the West African Accounting System, or SYSCOA, aimed at standardizing accounting practices in the region. SYSCOA is a reference framework,

---

[14] A Vision Paper of the Asian–Oceanian Standard-setters Group 2011– A Driving Wind for IFRS From Asia– Oceania.

[15] http://www.glenif.org/es/index.php?option=com_content&view=article&id=52&Itemid=56.

[16] Moussa B (2010). On the development of the West African Accounting System. *International Journal of Business and Management*. Vol. 5. May. Economics and Management School, Wuhan University. China.

covering bookkeeping and the legal aspects of accounting. It obliges all companies, except those in the financial and insurance sectors, to use the same accounting method.

39. Cooperation and coordination within a region can provide a number of benefits for countries at the national level, facilitating the implementation of standards and economies of scale. A major trend is the extension of activities to areas of implementation and the application of reporting standards and regulations. However, it is important to consider and address some potential risks associated with regional institutional standard-setting, as arrangements should be in place to avoid delays in the unilateral adoption and implementation of international requirements. For example, complications are evident where a common stock exchange exists: if one country wishes to move to IFRSs ahead of other countries belonging to a common accounting system, listed companies would find themselves facing a double set of requirements.

B. Developments at the national level

40. The development of sound regulatory and institutional frameworks at the national level is a complex and challenging exercise. According to the Accountancy Development Toolkit, the following aspects and related indicators should be taken into the consideration in assessing the regulatory and institutional standard-setting for high-quality corporate reporting.

41. Indicators on legal and regulatory requirements:

(a) Financial reporting and disclosure;

(b) Audit;

(c) Environmental, social and governance reporting;

(d) Enforcement, monitoring of implementation, and compliance;

(e) Licensing of auditors;

(f) Corporate governance;

(g) Ethics;

(h) Investigation, discipline and appeals;

(i) Indicators on institutional arrangements;

(j) Clear institutional responsibilities;

(k) Efficiency of coordination mechanisms;

(l) Efficiency of funding arrangements;

(m) Professional accounting organizations.

42. Various factors concerning the development of regulatory and institutional foundations at the national level should be borne in mind; they are described below.

43. Given the continuous changes taking place at the international level, demand countries must to be able to adapt quickly if they are to keep up with all new regulations and benchmarks generated in the reporting arena. In this regard, it is important, as mentioned above, to ensure that national regulatory and institutional standard-setting include arrangements for regular and efficient communication with the international standard-setters and other international bodies in the area of corporate reporting.

44. Another important trend is the growing role of State regulators. In response to the problematic audits of Enron, Global Crossing and other large companies, the enactment of

the Sarbanes-Oxley Act in July 2002 replaced the self-regulation of the United States auditing profession with a system of independent inspection by PCAOB. Similar initiatives have followed in other countries, and there is now emphasis worldwide on making auditor oversight an essential feature of audit regulation. Auditor oversight is, for obvious reasons, carried out at the local level on a national basis. However, the Sarbanes-Oxley Act did not exclude foreign registrants on United States stock exchanges from the requirement for oversight by PCAOB. This appears to have encouraged a number of large countries to establish their own auditor oversight systems in the hope that they would mutually recognize each other's systems. Yet this has only occurred to a limited extent, resulting in a considerable amount of extraterritorial activity by PCAOB audit inspectors.

45. All European Union member States[17] have established public audit oversight bodies responsible for the training, certification, education, qualification, quality assurance and disciplinary procedures concerning statutory auditors and audit firms as well as for relevant standard-setting.

46. In the area of financial reporting and disclosure requirements, further efforts are being made towards the adoption and implementation of international standards.

47. With regard to accounting standards, progress in global convergence has remained constant in recent years, and according to IASB, more than 100 countries already require, permit or are in the process of implementing IFRSs. The proliferation of International Standards on Auditing developed by IFAC's International Auditing and Assurance Standards Board has not abated. The Clarity Project, designed to promote understanding of those standards, has contributed to such proliferation.

48. Countries are continuing to take different approaches towards the implementation of IFRSs. For example, two out of nine pilot test countries use the IFRSs as developed by IASB, three implement them after an endorsement process has been completed, one uses a convergence approach to align its standards with the IFRSs, one issues national accounting standards based on the IFRSs and one implements regional accounting standards.

49. Non-financial reporting remains a major challenge. Over the past decade, a number of jurisdictions have introduced or strengthened non-financial disclosure requirements related to environmental, social and corporate governance issues. As UNCTAD's research[18] on corporate governance disclosure has shown, many countries around the world, developed and developing countries alike, have mandatory requirements for corporate governance disclosure. Such requirements are often found in company law or stock exchange listing requirements. However, social and environmental issues are among the least required subjects. Nevertheless, member States have placed an emphasis on promoting such sustainability reporting at a number of international forums.

50. In this regard, most recently in the outcome document of the 2012 United Nations Conference on Sustainable Development, or Rio+20, Member States declared:

> We acknowledge the importance of corporate sustainability reporting and encourage companies, where appropriate, especially publicly listed and large companies, to consider integrating sustainability information into their reporting cycle (para. 47, *The Future We Want*).

[17] http://www.fee.be/publications/default.asp?library_ref=4&content_ref=1537.

[18] UNCTAD (2011). *Corporate Governance Disclosure in Emerging Markets: Statistical analysis of legal requirements and company practices*. United Nations publication. New York and Geneva. Available from: http://unctad.org/en/docs/diaeed2011d3_en.pdf.

51. A number of member States and/or stock exchanges are pioneering sustainability reporting by means of either regulatory initiatives or listing requirements. The most popular tool for stock exchanges is sustainability indices that rank the performance of leading companies on environment, social and corporate governance issues. While not a form of mandatory disclosure, these indices have been successful in promoting voluntary disclosure among companies.

52. In 1995, Denmark became one of the first countries to introduce legislation (Danish Environmental Protection Act) mandating environmental reporting for very large companies. This law has been updated to expand the scope and depth of reporting. In South Africa, to highlight another example, the Johannesburg Stock Exchange has since 2010 required that all companies listed on its exchange produce “integrated reports” that include sustainability information. In June 2012, the United Kingdom introduced regulation requiring listed companies to report on greenhouse gas emissions; such reporting is expected to go into force for listed companies on the London Stock Exchange in 2013. In 2012, the Organization for Economic Cooperation and Development published a stock taking of more examples from its member countries.[19] In Brazil, Bovespa has introduced mandatory reporting around sustainability issues, on a “comply or explain” basis. Bovespa[20] also introduced a climate change-related index that led to a threefold increase in climate change-related reporting among the top 100 companies. Almost half of the 30 largest exchanges in the world have environment, social and corporate governance indices, and many more exchanges are planning to introduce them.[21]

53. However, pilot test findings show that regulations on non-financial disclosure remain a challenge. Even in leading countries in this area, there is a lack of regulatory requirements. As member States around the world seek to address growing sustainability concerns, environmental, social and corporate governance reporting is expected to continue to be the subject of regulatory initiatives and listing requirements.

54. National efforts to build regulatory and institutional foundations for enforcement, monitoring of standards implementation and compliance are ongoing.

55. In this regard, a major trend is the expanded role of stock exchanges, which have established themselves as promoters of the relevant governance recommendations for listed companies through their listing rules and maintenance requirements, as well as through the exercise of enforcement powers entrusted to them in some jurisdictions.

56. Listing requirements on stock exchanges can serve a similar function as regulatory initiatives in promoting high-quality corporate reporting and should be considered in any assessment of the overall corporate reporting infrastructure. This is especially the case in markets where only one stock exchange has a monopoly or near monopoly.

57. The facilitated coordination among all institutions involved in the corporate reporting process has proven to be another major trend as well as a remaining challenge in many countries.

58. In general, several institutions are involved in regulatory activities in the area of corporate reporting.

59. For example, in Japan, the accounting regulatory system consists of three legislative components:

[19] OECD (2012) *Corporate Greenhouse Gas Emission Reporting: A stocktaking of government schemes* http://www.oecd.org/investment/investmentpolicy/50549983.pdf.

[20] http://www.bmfbovespa.com.br/indices/ResumoIndice.aspx?Indice=ICO2&Idioma=en-us.

[21] Responsible Research (2012). *Sustainable Stock Exchanges: A Report on Progress*, p. 29.

(a) The Securities and Exchange Law, enforced by the Financial Services Agency, a subagency of the Ministry of Finance;

(b) The Commercial Code, enforced by the Ministry of Justice;

(c) The Corporation Tax Law, enforced by the National Tax Administration, a largely autonomous agency reporting to the Ministry of Finance.

60. In Turkey, the institutional setting related to financial reporting includes the following:

(a) Institute of Accounting, Istanbul University;

(b) Expert Accountants' Association of Turkey;

(c) Capital Markets Board of Turkey;

(d) Turkish Accounting and Auditing Standards Board;

(e) Banking Regulation and Supervising Agency;

(f) Turkish Accounting Standards Board.

61. In China, the following institutions, among others, play important roles in corporate reporting:

(a) Ministry of Finance;

(b) China Securities Regulatory Commission;

(c) China Banking Regulatory Commission;

(d) China Insurance Regulatory Commission;

(e) Chinese Institute of Certified Public Accountants (CPAs).

62. In South Africa, some of the key institutions that are involved in corporate reporting matters are as follows:

(a) Ministry of Trade and Industry;

(b) Financial Services Authority;

(c) Financial Reporting Standards Council;

(d) Financial Reporting Investigations Panel;

(e) Independent Regulatory Board for Auditors;

(f) South African Reserve Bank;

(g) South African Institute of Chartered Accountants.

63. In Côte d'Ivoire, institutions that deal with matters of corporate reporting include the following:

(a) Ministry of Finance and Economy;

(b) National Treasury;

(c) National Accountancy Council;

(d) Ordre des Experts Comptables et Comptables Agréés de Côte d'Ivoire;

(e) Several regional organizations.

64. A coordinating mechanism between different institutions in the reporting chain is critical to avoid overlapping of activities and contradictions and to improve the efficacy of

efforts and resources used. Coordination is necessary in issuing legislation affecting corporate reporting, ensuring its implementation, carrying out investigations, imposing punitive action and sharing information, for example. As indicated by the pilot test results, a number of countries have made significant progress in this regard, while others need to strengthen their capacity further.

65. Coordination plays a critical role is the development and implementation of a national strategy and an action plan. Some countries participating in the pilot tests expressed a need for a better understanding of what should be included in a national strategy. In some, action plans have been designed and implemented for a specific segment of activity, such as the IFAC action plans developed by professional accountancy organizations to become IFAC members; however, these do not constitute a national strategy. Other countries have partial action plans involving only some institutions participating in the reporting chain or including only some areas of reporting.

66. The action plan refers to a comprehensive effort at the country level aiming at the improvement of the current status of accountancy infrastructure based on a national strategy and identified priority areas. This plan should also include the participation of all key institutions involved in corporate reporting. For example, some pilot countries, such as Côte d'Ivoire, Croatia and the Russian Federation, have used the results of the pilot tests of accountancy development indicators to identify priority areas for developing national action plans.

67. An example of an action plan agreed on a national level comes from Singapore. The Committee to Develop the Accountancy Sector[22] was set up by the Government of Singapore in 2008 to conduct a holistic review of the accountancy sector with a view to positioning Singapore as a leading international centre for accountancy services and professionals.

68. The Committee made 10 recommendations to transform Singapore into the leading global accountancy hub for the Asia-Pacific region by 2020. The recommendations seek to deepen expertise in the accountancy sector, upscale the value of services provided from the Singapore-based public accountancy entities and promote the regionalization of accountancy services. The Committee determined that in order to enhance the public accountancy entities' capability and productivity, incentives should be given to encourage incremental investments in human capital development and building technical expertise.

69. The Committee recommended the creation of a new institution to accomplish the transformation of the country: the Singapore Accountancy Council. This central body should be supported by a full-time secretariat comprising representatives from the public accountancy profession and sector, the business and financial community, academia and the public sector. It should be appointed by the Government and established by legislation to give it formal oversight responsibilities over the administration of the following:

(a) Accountancy Sector Development Fund;

(b) Accountancy Services Research Centre;

(c) Globally-recognized, Singapore-branded post-university professional accountancy qualification and the necessary accreditation processes;

(d) Specialization pathways for the accountancy sector.

[22] Transforming Singapore into a leading global accountancy hub for Asia-Pacific. Final report of the Committee to Develop the Accountancy Sector. 12 April 2010.

70. Another example of a coordinated approach towards regulatory requirements is Croatia's action plan for the implementation of the Audit Act Amendments. The activities included in the plan are listed below:

(a) Enacting the Audit Act Amendments (aligned with the Eighth Council Directive 84/253/EEC);

(b) Establishing a service for audit and accountancy public policy issues within the Ministry of Finance;

(c) Submitting the 2009 Budget Proposal to the Public Oversight Committee;

(d) Completing preparatory work to provide administrative and technical support to the Public Oversight Committee;

(e) Setting up the Public Oversight Committee;

(f) Employing a quality assurance team leader in the Croatian Chamber of Auditors;

(g) Holding a general assembly of the Croatian Chamber of Auditors;

(h) Electing a new Chamber of Auditors Board in line with the Audit Act Amendments;

(i) Concluding a cooperation Agreement between the Public Oversight Committee and the Croatian Chamber of Auditors;

(j) Developing a public oversight implementation plan;

(k) Designing a quality assurance implementation plan;

(l) Ensuring the quality assurance team within the Croatian Chamber of Auditors is fully staffed (up to five members).

71. One of the most important tasks required for regulatory and institutional developments at the national level has to do with institutions in charge of education and training. Most of the pilot tests countries reported an insufficient supply of qualified accountants, particularly for small and medium-sized enterprises and the public sector. This clearly reflects a further need for institutional building in this area. Maintaining programmes up to date according to international benchmarks, whether at the university or the professional accountancy organization level, is very important. In this regard, coordination between key institutions involved in this process – the Ministry of Education and professional accountancy organizations, for example – is essential to guarantee that the educational curriculum is always aligned with the latest national and international regulations and requirements. This will ensure that professionals obtaining certification are in a position to efficiently apply standards.

72. In this regard, some pilot tests pointed to the need to strengthen coordination between professional accountancy organizations and universities at the national level. Complications arise when courses and training sessions cannot keep pace with new requirements coming from a continuously changing regulatory environment. The lack of a standardized model curriculum for accountancy and audit studies adds to the problem. Part of the difficulty in assessing the current situation in the relevant countries lies in the existence of different systems in place in the same country, especially in countries with a large number of universities and educational institutions.

73. Another important aspect of regulatory and institutional foundations relates to sustainable and independent funding mechanisms for accountancy development. When establishing adequate regulatory and institutional arrangements, it is essential to make sure that these institutions will be able to carry out their duties in an objective manner. In

relation to standard-setters, these bodies should have a secure and stable source of funding that is not dependent on voluntary contributions of those subject to the standards.

74. Independence means that the funding must come with no strings attached. For example, in 2006, the IASB Foundation established four funding principles:

(a) Funding must be broad-based. A sustainable long-term financing system must expand the base of support to include the major participants in the world's capital markets;

(b) The funding system should be compelling. In this regard, support from relevant regulatory authorities would be required;

(c) Funding should be open-ended and not contingent on any action that might infringe on the independence of standard-setting bodies. The idea is that funding should be shared by the world's major economies, using gross domestic product as a parameter to determine the level of their contribution;

(d) Moving to a simple levy system would add an element of automaticity to the funding system and reduce any future claims of dependence on single-company contributions. Moreover, all companies, who benefit from IFRSs would contribute.

75. IASB's principles could be used for other international, regional and national organizations conducting activities in different areas. However, at the national level and especially in developing countries, obtaining adequate funding can be a major challenge not only for ensuring independence but particularly for securing the sustainability of these institutions. For instance, many professional bodies in developing countries are often small with few members. Lack of funding is a major challenge to their survival and development.

76. In other countries, the government provides funding for several institutions or carries out the functions on its own. In these cases, it is important to pay attention to possible conflicts of interest that could arise from situations related to the process of appointment of chairman or director of those institutions. Independence could also be compromised when there is only one government regulator carrying out activities such as setting up and enforcing standards and taking disciplinary action.

77. A critical element of a sound accounting infrastructure is the set of punitive actions that can be taken in a country when a case of misconduct is identified. In addition, procedures related to obtaining and maintaining membership, licensing and certification play a key role in the quality and credibility of corporate reports. Findings from pilot tests show that building such system is a daunting challenge for some countries, as it relates to the withdrawal of certification, licensing or membership of auditors and accountants. In some countries, membership of a professional organization is indefinite and cannot be taken away. Thus, continuing professional development programmes are not required to maintain membership and certification; as a result, there is no mechanism ensuring that members have the ability to perform their duties according to the latest requirements.

78. In this regard, sharing good practices would be useful. For example, in Japan the Financial Services Agency oversees auditing standards and the practice of CPAs and audit corporations. The legislative framework for the accounting profession and CPA qualification is set out in the Certified Public Accountants Law. The practice of the CPAs, among others, is overseen by the Financial Services Agency. The Agency has a subcommittee called the Certified Public Accountant System of the Financial System Council that establishes the policies for governing CPAs. The Japanese Institute for Certified Professional Accountants is the only professional accounting body in Japan, and its key role is to keep a register of all CPAs in that country; further, it has the authority to revoke the registration of any CPA who has been disciplinarily sanctioned.

79. In the United Kingdom, disciplinary activities are conducted by the Accountancy and Actuarial Discipline Board of the Financial Reporting Council. Proceedings related to investigations of misconduct can become public, as illustrated by the recent appeal made by Deloitte in the MG Rover case. In the United States, PCAOB goes so far as to publish all correspondence with companies under investigation.

II. Conclusions

80. Building a sound regulatory and institutional foundation for high-quality corporate reporting is a complex and challenging exercise. The following points should be taken into account:

(a) The need to pay greater attention to sound accounting and reporting requirements based on convergence towards a single set of high-quality global accounting standards as a key factor in strengthening the international financial regulatory system and ensuring global financial stability;

(b) The need to strengthen and better coordinate institutional arrangements at the global level, supported by the establishment of a number of bodies and functions to facilitate and improve international standard-setting processes with an increased focus on enforcement and monitoring of compliance at the global level;

(c) The growing interdependence of regulatory regimes of different jurisdictions;

(d) More attention of users and preparers of corporate reports towards non-financial disclosure;

(e) The increased role of State regulators;

(f) At the national level a growing understanding of the importance of a strategic long-term approach towards national regulatory and institutional building, based on a comprehensive and consistent assessment of needs, gaps and priorities;

(g) The increased need and pressure to strengthen national regulatory and institutional requirements with regard to enforcement, compliance, investigation, discipline and appeals;

(h) The growing role of regional organizations;

(i) The need to further facilitate better coordination among all national stakeholders;

(j) The need to further strengthen the growing role of regional organizations in the coordination of countries' efforts to standardize reporting requirements.

81. These developments pose many challenges to stakeholders at the global and national levels with regard to regulatory and institutional building, for example:

(a) It is necessary to further facilitate communication between national regulators and international standard-setters, in view of the growing role of international bodies, particularly in ensuring compliance and the consistent application of standards;

(b) New institutional arrangements may be needed to ensure the beneficial implementation of international pronouncements, given that these issues have traditionally been dealt with at the national rather than the global level and that there are differences in the national legal and institutional systems;

(c) Given the increasing focus on enforcement and compliance, countries – particularly developing countries and countries with economies in transition – must further develop national expertise in enforcement, monitoring of compliance, investigation and discipline; and further improve coordination between all stakeholders in those areas of corporate reporting;

(d) More guidance is necessary to assist countries in developing regulatory and institutional foundations that would enable them to meet requirements for high-quality corporate reporting. This includes not only technical guidance on standards application, but also guidance on good practices in national institutional arrangements on standards implementation, including enforcement, monitoring of compliance, investigation and discipline;

(e) A more comprehensive and long-term approach to strengthening regulatory and institutional foundations requires further development of adequate tools to help countries measure and monitor progress in a consistent manner. This also includes the formulation of clear criteria and guidance on which the stakeholders of a country could develop consensus on the current status of accounting reforms and further priorities.[23]

(f) International discussions and processes relating to building regulatory and institutional foundations should be further enhanced to ensure that they involve the participation of developing countries and countries with economies in transition and that international requirements meet the needs of all countries;

(g) Another challenge is to improve and enlarge educational and training systems for professional accountants and auditors in order to deal with the insufficient supply of trained professionals with respect to market demand, in particular for small and medium-sized enterprises and the public sector, as reported by most of the pilot test countries; this also includes better coordination between universities and providers of professional training;

(h) Non-financial and sustainability reporting, including issues such as the environment, corporate governance and corporate social responsibility, should be better integrated into accounting development policies;

(i) Financial and human resources should be secured to ensure adequate quality and the sustainability of national regulatory and institutional foundations, given the magnitude and complexity of developments;

(j) The growing role of regional coordination poses a challenge to the efficient utilization of the facilities of regional organizations in assisting countries in their efforts to standardize accounting and reporting systems, with international requirements based on common needs and development objectives.

82. Delegates at the twenty-ninth session of ISAR may wish to consider the issues outlined in this note. They may also wish to consider the following conceptual questions:

(a) What major challenges do national regulators face in the area of regulatory and institutional developments for high-quality corporate reporting?

(b) What kind of support with regard to corporate reporting would they welcome from international standard-setters and other international bodies?

(c) What mechanisms are needed to facilitate coordination at the national, regional and international levels?

---

[23] For example, some of the pilot tests reflected contradictory views of major national stakeholders in answering the same question of the questionnaire. Some would agree that a particular element of national regulatory or institutional settings meets a specified requirement for high-quality corporate reporting, while others would not.

(d) How to ensure that regional and international settings meet the needs of all countries?

(e) What kind of institutional arrangements could ensure the consistent implementation of the international standards worldwide?

(f) Is there a need to issue regulatory requirements concerning non-financial disclosure, or does listing requirements guarantee compliance in this area?

(g) What are the main challenges to be addressed by regulatory and institutional foundations concerning public-sector reporting and small and medium-sized enterprises?

(h) How can countries ensure sufficient funding for their institutions so that they can become sustainable without compromising their independence?