Déclarations de principes

(La présente documentation est disponible en anglais seulement)

Comité technique
Organisation internationale des commissions de valeurs

Principles for Ongoing Disclosure and Material Development reporting by Listed Entities……………………………………………….. 1

Principles of Auditor Independence and the Role of Corporate governance in Monitoring an Auditor's Independence ……………….13

Principles for Auditor Oversight……………………………………………………………………..21

Principles for Ongoing Disclosure
and
Material Development Reporting
by
Listed Entities

OICV-IOSCO

A Statement of the Technical Committee
of the
International Organization of Securities Commissions

October 2002

I – Introduction

1. The Technical Committee recognizes that reliable, timely and readily accessible information is fundamental for investors. Information should be disclosed on a timely basis, whether in connection with an initial public offering or listing, continuously, currently or periodically, and in a form or manner either prescribed by accounting standards, regulations, listing rules or law, together with the information that is provided by the management under the principles of fair presentation.

2. In 1998, IOSCO endorsed the International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers for equity securities (IDS98), which set forth non-financial statement disclosure standards for offerings and listings of equity securities. The Disclosure Subcommittee of Standing Committee No. 1 is currently developing a comparable set of international disclosure standards for cross-border offerings and initial listings of debt securities by foreign issuers that would be based on the IDS98. The adoption of both sets of non-financial statement disclosure standards by jurisdictions would facilitate cross-border offerings because a foreign issuer could use one disclosure document that would be accepted in multiple jurisdictions. At the same time, adequate investor protection would be assured through the use of the high quality disclosure standards of the IDS98.

3. However, the volume of secondary trading far exceeds the amount of offerings, and protection of investors therefore requires ongoing provision of material information. Because most investors participate in the market through secondary trading rather than initial public offerings, providing high quality information to the markets on a periodic basis is crucial, even if a company only infrequently makes public offerings.

   In particular, most retail investors participate in the securities markets through the secondary trading that occurs in the markets, rather than through initial offerings of securities. An initial offering prospectus or listing document that satisfies the requirements of IDS98 provides high quality, material information for investors who participate in initial public offerings ("IPOs"). Material information should also be updated and provided on an ongoing basis to the public, so that retail investors who participate through secondary trading, and who are most in need of regulatory protection, can benefit from this same type of disclosure on an ongoing basis. In other words, the body of information available to an investor should contain both information disclosed at the IPO stage, covered under IDS98, as well as information disclosed on an ongoing basis. The fundamental principle of full and fair disclosure is that the listed entity should provide all information that would be material to an investor's investment decision. Such information also includes management's discussion and analysis (MD &A), where required, which could be disclosed in a separate report or included as part of a periodic report.

4. Consequently, the Technical Committee has developed a set of common high level principles for ongoing disclosure and, in particular, material development disclosure by all listed entities, leaving the possibility for individual jurisdictions to add further requirements. For convenience, this set of principles is referred to in this document as the International Ongoing Disclosure Standards or IODS.

5. The term "ongoing" is defined in this report to include generally all current, continuous[1] and periodic disclosures, other than that disclosed at the IPO stage.[2] The term "periodic" used in this report refers to information required to be disclosed at specified dates or intervals.

6. Competent authorities in different jurisdictions have used two basic approaches, as well as a combination of the two, in order to ensure appropriate disclosure of information by listed entities in view of the interest of investors:

   - a "general obligation" approach and
   - a "prescription approach".

   Some information on these two approaches is provided in the Appendix.

   Such differences in regulatory approaches evolved due to differences in the characteristics of each market and its legal and institutional history. The Technical Committee recognizes that there is no "one-size fits all" approach for all IOSCO members. No one approach is necessarily better than any other, because individual market characteristics and regulatory regime are different. Notwithstanding different definitions and concepts, the information disclosed may be similar in nature and extent under the different approaches.

7. In spite of the different approaches used, most jurisdictions agree that listed entities should have an ongoing obligation to disclose information that would be material to an investor's investment decision and that is necessary for full and fair disclosure. *IOSCO, while acknowledging the different regulatory approaches taken by various jurisdictions with respect to ongoing disclosure, notes that these different approaches do not preclude agreement on what events should be disclosed in an effective disclosure scheme. It is therefore possible to identify common principles of ongoing disclosure that would facilitate IOSCO members to develop their own disclosure regimes, in the light of their own unique market characteristics.*

8. Accordingly, the purpose of this Statement is:

   - To develop a companion set of International Disclosure Standards to IDS98 – namely setting high level principles in "International Ongoing Disclosure Standards for ongoing disclosure and material development reporting by listed entities" (IODS); and
   - By means of IODS to:
     (a) Facilitate the agreement on minimum standards for ongoing disclosure and material development reporting for listed entities; and
     (b) Provide guidance to jurisdictions reviewing and/or developing an ongoing disclosure and material development reporting regime for listed entities.

9. The Technical Committee notes that:

[1] "Continuous disclosure" refers to the disclosure regimes of certain jurisdictions in which information is provided under a general principle of materiality, without reference to a specific timeframe.

[2] In the US, the terms "ongoing" or "current" normally refer to disclosure other than that required for periodic disclosure, such as quarterly and annual reports. However, for the purpose of this report, "ongoing" also includes periodic disclosure requirements that apply in the United States.

(a) IODS does apply in relation to all entities with shares listed in a recognized exchange. It does not apply in relation to foreign or domestic unlisted entities.

(b) IODS does not address how competent authorities (including exchanges and SRO market operators) should monitor and enforce the ongoing disclosure obligations.

(c) IODS does not apply to collective investment schemes (CIS).

(d) IODS does not apply to suitability criteria that may be imposed by listing authorities.

* * *

II – Principles for Ongoing[3] Disclosure and Reporting of Material Developments

1. The key elements of an ongoing disclosure obligation

Listed entities should have an ongoing disclosure obligation requiring disclosure of all information that would be material to an investor's investment decision.

This principle is typically implemented either by a comprehensive list of prescribed disclosure items that are presumptively material or by a general obligation to disclose all information that may affect an investor's assessment of a listed entity's value and prospects. In addition to this general obligation, some jurisdictions have indicated a list of events that typically can be considered material. More information is provided in the Appendix.

The subject matter of material information disclosed in periodic disclosure documents should be carefully monitored to identify specific events or developments that are time-sensitive and should be disclosed more promptly, under any applicable general disclosure obligation. Examples include certain off-balance sheet arrangements, changes in the valuation of non-market traded contracts, and events related to stock options including stock option arrangements.

2. Timeliness

The listed entity shall disclose ongoing information on a timely basis, which could require disclosure on an:

(a) immediate basis for disclosure of material developments, where such a term could be defined as "as soon as possible" or prescribed as a maximum of specified days (such as 2 business days, as proposed in the USA); and

[3] For the purpose of this document, ongoing disclosure means periodic disclosure which has to be provided at set dates and current disclosure which must be provided on a as needs and immediate basis. Although in the United States the term "ongoing disclosure" normally refers to disclosure of information other than that provided through annual and quarterly reports, in these Principles the term "ongoing" also includes the periodic disclosure requirements that apply to companies listed in the United States.

It is outside the scope of this report to provide general guidelines for periodic disclosure. It aims only to define that periodic disclosures and reports are also a useful channel to disclose the information discussed in the body of this report.

(b) *periodic basis, prescribed by law or listing rules, such as quarterly or annual reports. Such information would also include management discussion and analysis (MD&A), where required, which can be disclosed in a separate report or included in a periodic report. The disclosure obligation may require disclosure of relevant information on an immediate basis even when it belongs to periodic reporting.*

Under the general ongoing obligation approach disclosure may be subject to delay, to be granted in some jurisdictions by the competent authority, if:

(a) the information is confidential under legislation;

(b) the information concerns an incomplete proposal or negotiations or the disclosure of particular information is such as to prejudice the legitimate interests of the entity's investors; in such cases the listed entity must ensure that the information is maintained strictly confidential.

3. Simultaneous and identical disclosure

If the entity is listed in more than one jurisdiction, the information released under the ongoing disclosure obligation of one jurisdiction where it is listed should be released on an identical basis and simultaneously in all the other jurisdictions where it is listed. This obligation should not be dependent on where the listed entity is principally listed.

This will mean disclosing information in a jurisdiction where:

(a) the obligation may not technically require disclosure but disclosure is required in another jurisdiction in which the entity is listed; or

(b) such information is exempted from ongoing disclosure obligation but it is not exempted in another jurisdiction in which the entity is listed.

This principle should be applied pragmatically to take into account factors such as different time zones and trading hours.[4]

4. Dissemination of information

Under the ongoing disclosure obligation listed entities should ensure that full information is promptly made available to the market by using efficient, effective and timely means of dissemination.

[4] Trading halts are separately considered by the IOSCO Technical Committee.

5. Disclosure criteria

Ongoing disclosure of information should be fairly presented, not be misleading or deceptive and contain no material omission of information.

6. Equal treatment of disclosure

The information to be disclosed in compliance with the ongoing disclosure obligation should not be disclosed to selected investors or other interested parties before it is released to the public. Certain narrow exceptions may be permitted to this principle to allow communications with advisers and rating agencies or, in the ordinary course of business, communications with persons with whom the listed entity is negotiating, or intends to negotiate, a commercial, financial or investment transaction or representatives of its employees or trade unions acting on their behalf. In all these cases, the recipients have a duty to keep the information confidential.

7. Allocation of accountability

The listed entity is responsible for compliance with the ongoing disclosure obligation. In some jurisdictions, specific persons have been identified as also being responsible for the disclosure of such information.

Appendix

Different Approaches to Disclosure Requirements

The Prescription Approach

In the prescription approach a set of rules specify the disclosures that issuers must provide to investors and the public, and which are presumptively material.

The U.S. Securities and Exchange Commission for example requires all public domestic companies to file annual and quarterly periodic reports that address certain specified disclosure items. In addition, all public domestic companies must file current reports on Form 8-K in the intervening period between periodic reports to disclose a specific, comprehensive list of events that are presumptively material: the list is reproduced in the annex to this Appendix. Such disclosure must be made within a few business days after occurrence of the corporate event that must be disclosed[5]. That list has recently been proposed to be substantially increased. The U.S. exchanges require disclosure of price sensitive information. The definition of materiality that is used by the SEC has been developed by the courts and is not delimited by the notion of the effect on the price of an issuer's securities. Thus, while the listed entity is required by the U.S. SEC's rules to disclose specific information or events in a prescribed manner, if investors feel that the disclosure is inadequate or misleading they can take legal action against the issuer and the courts will determine the materiality of the disclosure or non-disclosure.

Also Japan provides a list of corporate events which are presumed to be material and require compulsory disclosure. The list is reproduced in the annex to this Appendix.

The General Obligation Approach

In the European Union and in other jurisdictions, regulators require listed entities to disclose information under a general obligation of materiality comprising price sensitive information, without specifically describing the types of events that would be deemed material. Such information, if determined price sensitive or material, would have to be disclosed immediately by issuers without any further qualification.

This approach includes information which is typically assessed against (i) the likely effect of the information on the price or value of the relevant equities and (ii) the information expectations of a reasonable investor in the market and (iii) the information to be disclosed has not been made available to the public. Some jurisdictions have indicated events that typically can be considered material. An example (Brazil) is included in the annex to this Appendix.

Under such a general obligation approach delays may be permissible under certain conditions, subject in some jurisdictions to approval by the competent authorities.

[5] The SEC has proposed to shorten the deadline for such reports to two business days after the occurrence of the event.

It is recognized, however, that even under the general obligation approach, a body of accounting standards, listing rules, legislation or regulation may prescribe certain types of information, including specific events, which should be disclosed either in the form of immediate disclosure using the price sensitivity or materiality test, or through periodic disclosure in annual accounts or MD & A reports.

Annex to the Appendix

Examples of comprehensive lists of prescribed disclosure items

1. USA

Material events that are reported to the U.S. Securities and Exchange Commission on Form 8-K

The comprehensive list of prescribed corporate events that are presumptively material and that must be disclosed, or will likely be required to be disclosed, with the U.S. SEC on Form 8-K is as follows:

- Changes in control of a company;
- A company's acquisition or disposition of a significant amount of assets;
- A company's bankruptcy or receivership;
- Changes in a company's certifying accountant;
- Resignations of a company's directors, circumstances for the departure of a director, the appointment or departure of a principal officer, and the election of new directors other than pursuant to a vote of security holders at an annual meeting;
- Change in a company's fiscal year and amendments to a company's articles of incorporation or bylaws that were not previously disclosed in a proxy statement or other such disclosure document;
- Entry into a material agreement not made in the ordinary course of business;
- Termination of a material agreement not made in the ordinary course of business;
- Termination or reduction of a business relationship with a customer that constitutes a specified amount of the company's revenues;
- Creation of a direct or contingent financial obligation that is material to the company;
- Events triggering a direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation;
- Exit activities including material write-offs and restructuring charges;
- Any material impairment;
- A change in a rating agency decision, issuance of a credit watch or change in a company outlook;
- Movement of the company's securities from one exchange or quotation system to another, delisting of the company's securities from an exchange or quotation system, or a notice that a company does not comply with a listing standard;
- Conclusion or notice that security holders no longer should rely on the company's previously issued financial statements or a related audit report;
- Any material limitation, restriction or prohibition, including the beginning and end of lock-out periods, regarding the company's employee benefits, retirement and stock ownership plan;

- Unregistered sales of equity securities by the company;
- Material modifications to rights of holders of the company's securities;
- Earnings releases;
- Changes in earnings guidance; and
- Other materially different information regarding key financial or operations trends from that set forth in periodic reports.

2. Japan

Comprehensive list of corporate events that are presumed to be material
On a solo basis

- Public offering or selling of securities to be made abroad
- Issuance without public offering
- Grant of the subscription rights to new shares as stock options
- Change of its parent company or subsidiary
- Change of major shareholders
- Occurrence of serious disaster (1)
- Lawsuit raised or settled (2)
- Conclusion of agreement on exchange of shares (3)
- Resolution of transfer of shares
- Approval to the plan or conclusion of an agreement on corporate separation (4)
- Conclusion of an agreement on merger (5)
- Conclusion of an agreement on business transfer (6)
- Change of representative directors
- Claim to bankruptcy, etc.
- Credits become likely to be in default (7)
- Significant change in the company's financial condition and business performance(8)
- Occurrence of any event to correct the information described in the registration statement before the offered securities are listed.

On a consolidated basis

- Occurrence of the serious disaster for subsidiary (9)
- Lawsuit for subsidiary raised or settled (10)
- Conclusion of an agreement by subsidiary on exchange of shares (11)
- Resolution of transfer of shares of subsidiary (12)
- Approval to the plan or conclusion of an agreement for subsidiary on corporate separation (13)
- conclusion of an agreement for subsidiary on merger (14)

- conclusion of an agreement for subsidiary on business transfer [15]
- claim to bankruptcy, etc. of subsidiary [16]
- credits of subsidiary become likely to be in default [17]
- significant change in the consolidated financial condition and business performance [18]
- occurrence of any event to correct the information described in the registration statement before the offered securities are listed

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Notes

(1) the amount of damages is 3% or more of the net assets

(2) claimed the amount of 15% or more of the net assets or paid compensation the amount of 3% or more of the net assets

(3) resulting to be 100% parent company or to be 100% subsidiary

(4) estimated to cause increase or decrease of the assets in 30% or more of the net assets or of the gross sales in 10% or more

(5) estimated to cause increase of the assets in 30% or more of the net assets or of the gross sales in 10% or more

(6) estimated to cause increase or decrease of the assets in 30% or more of the net assets or of gross sales in 10% or more

(7) the amount of the credits is 3% or more of the net assets

(8) effecting 3% or more of the net assets and 20% or more of the average of the net income in last 5 years

(9) the amount of damage is 3% or more of the consolidated net assets

(10) claimed the amount of 15% or more of the consolidated net assets or paid compensation the amount of 3% or more of the consolidated net assets

(11) estimated to cause increase or decrease of the consolidated assets in 30% or more of the consolidated net assets or of the consolidated gross sales in 10% or more

(12) estimated to cause increase or decrease of the consolidated assets in 30% or more of the consolidated net assets or of the consolidated gross sales in 10% or more

(13) estimated to cause increase or decrease of the consolidated assets in 30% or more of the consolidated net assets or of the consolidated gross sales in 10% or more

(14) estimated to cause increase or decrease of the consolidated assets in 30% or more of the consolidated net assts or of the consolidated gross sales in 10% or more

(15) estimated to cause increase or decrease of the consolidated assets in 30% or more of the consolidated net assets or of the consolidated gross sales in 10% or more

(16) the net assets or the deficit of which is 3% or more of the consolidated net assets

(17) the amount of the credits is 3% or more of the consolidated net assets

(18) effecting 3% or more of the consolidated net assets and 20% or more of the average of consolidated net income in last 5 years

3. Brazil

Material events that are considered to be material in the context of the general disclosure obligation. According to the legislation, material events may include, but are not limited to:

- Signature of agreements or contracts regarding the transfer of the company's control, even if under conditional provisions;
- Changes in the control of the company, including celebration, amendments, or cancellation of shareholder agreements.
- Celebration, amendments, or cancellation of shareholder agreements in which the company takes part in or are intervenient, or if they have been registered in the appropriate book maintained by the corporation;
- Admission or departure of shareholders maintaining contracts or operational collaboration regarding financial, technological or administrative issues with the company;
- Authorization for listing securities issued by the company in any domestic or foreign market;
- Decision to go private;
- Incorporation, merger or spin-off involving the company itself or linked corporations;
- Transformation or dissolution of the company;
- Changes in the company's assets;
- Changes in accounting criteria;
- Renegotiations of debts;
- Approval of stock options plans;
- Changes of the rights and privileges of the securities issued by the company;
- Splits, reverse splits or the issue of share dividends;
- Acquisition of shares for the purpose of increasing treasury stock or cancellation, and the selling of shares so acquired;
- Amount of profits or losses and the distribution of dividends;
- Celebration or termination of contracts, or failure to close a deal, when the expectation for such is of public knowledge;
- A project's approval, alteration or abandonment, as well as a delay in its implementation;
- Starting, retaking or suspending the manufacturing or commercialization of products or of services rendered;
- Discoveries, changes or developments regarding technology or companies' resources;
- Modification of disclosed projections by the company;
- Reorganization arrangements, bankruptcy, or any lawsuit that alters the corporation's financial situation.

Principles of Auditor Independence and the Role of Corporate Governance in Monitoring an Auditor's Independence

OICV-IOSCO

**A Statement of the Technical Committee
of the
International Organization of Securities Commissions**

October 2002

Introduction

1. The International Organization of Securities Commissions' Objectives and Principles of Securities Regulation recognize that issuers should make full, accurate and timely disclosure of financial results and other information that is material to investors' decisions. The principles also recognize that accounting and auditing standards of a high and internationally acceptable quality contribute to promoting relevant and reliable financial information useful to a wide range of users for decision-making purposes. Specifically, the principles note that, among other things, regulation should be intended to ensure:

   - An independent verification of financial statements and compliance with accounting principles through professional external auditing.
   - Any audit is conducted pursuant to well-defined and internationally acceptable standards.
   - Rules designed to ensure the independence of the auditor.
   - A mechanism for enforcing compliance with accounting and auditing standards.

2. The purpose of this Statement is to build on these principles by setting forth the views of the IOSCO Technical Committee on the principles that should govern independence of auditors of financial statements of listed entities. It reflects the interest of securities regulators in ensuring that auditor independence requirements contribute to promoting investor confidence in published financial statements, irrespective of whether such requirements are the responsibility of securities regulators in their jurisdictions. The Technical Committee recognizes that, while regulations on auditor independence exist in many individual jurisdictions, these regulations may differ in approach, scope, terminology and substance. Accordingly, the Statement also sets forth principles relating to the oversight of an external auditor's independence by a body or bodies within an entity's corporate governance structure. For ease of reference, this Statement uses the term "audit committee" to refer to such a governance body or bodies. The Technical Committee believes these principles and the supporting guidance are relevant regardless of the specific auditor independence regulations that exist in a particular jurisdiction.

3. The principles and supporting guidance relating to audit committees and similar governance bodies address such a body's role in relation to auditor independence only; they do not describe other significant functions that may be performed in overseeing the quality and integrity of an entity's financial reporting.

Principles of auditor independence

4. The external auditor plays a critical role in lending independent credibility to published financial statements used by investors, creditors and other stakeholders as a basis for making capital allocation decisions. Indeed, the public's perception of the

credibility of financial reporting by listed entities is influenced significantly by the perceived effectiveness of external auditors in examining and reporting on financial statements. While any consideration of the effectiveness of external audits involves a wide variety of issues, it is fundamental to public confidence in the reliability of financial statements that external auditors operate, and are seen to operate, in an environment that supports objective decision-making on key issues having a material effect on financial statements. In other words, the auditor must be independent in both fact and appearance.

5. The importance of auditor independence standards that are reasonable and yet comprehensive, rigorous, robust and enforceable has been underlined by several significant corporate failures in which questions have been raised about the quality of financial reporting and, in particular, the independence of the auditor. The Technical Committee therefore encourages national and international professional accounting bodies to continue to work with regulators to strengthen existing national and international standards governing independence. Strengthened independence standards that, to the extent possible within the constraints of national laws, are consistent internationally, are a necessary element in reassuring the investing public that auditors are in a position to exercise objective judgment in concluding on management's representations in an entity's financial statements.

6. *Auditors of listed entities should be independent, both in fact and in appearance, of the entity being audited.*

7. *Standards of independence for auditors of listed entities should be designed to promote an environment in which the auditor is free of any influence, interest or relationship that might impair professional judgment or objectivity or, in the view of a reasonable investor, might impair professional judgment or objectivity.*

8. At present, the details of specific regulations and professional standards governing auditor independence vary from jurisdiction to jurisdiction, sometimes significantly. Differences relate to matters such as:

- the scope of persons and entities, both within and outside the audit firm, to whom independence rules apply;
- the types of financial, business or other relationships that an audit firm or individual within a firm may have with an entity that the firm audits;
- the types of non-audit services that can be provided by an auditor to an entity that it audits; and
- the safeguards that need to be implemented to protect against threats to independence.

9. Despite these differences, the Technical Committee has noted a growing consensus among securities regulators as to the nature of the threats to an auditor's independence and the limitations on the extent to which those threats can be mitigated by voluntarily applied safeguards of various types. Further, there appears

to be a growing consensus among securities regulators that a framework of principles governing independence is not sufficient in itself to protect investors without the greater clarity provided by specific prohibitions on activities and relationships considered unacceptable regardless of any safeguards applied.

10. The Technical Committee believes there is also a growing consensus that:

- establishment of standards governing auditor independence is not sufficient of itself to provide assurance that auditors are in fact independent; the standards must be supported by rigorous requirements for audit firms to establish and maintain internal systems and processes for monitoring, identifying and addressing threats to independence and ensuring compliance with the standards.
- the adequacy and effectiveness of audit firms' internal systems and processes relating to independence must be assessed and evaluated by an external oversight body (see IOSCO Technical Committee Statement on Principles for Auditor Oversight, October 2002).
- a governance body independent of management of an entity being audited should oversee both the process of selection and appointment of the external auditor and the conduct of the audit.

11. The Technical Committee has not in this Statement attempted to prescribe comprehensive standards of auditor independence and nor is it endorsing any particular existing set of auditor independence standards. The Committee notes, however, that the Code of Ethics for Professional Accountants of the International Federation of Accountants provides a useful analysis of potential threats to an auditor's independence under the following headings:

- Self-interest, where an auditor could benefit from a financial or other form of interest in or relationship with the company being audited, e.g., an investment in the company or undue dependence on fees from assurance or non-assurance services
- Self-review, e.g., performance of services for an audit client that result in the audit firm auditing its own work
- Advocacy, e.g., acting as an advocate for an audit client's position in dealings with third parties
- Familiarity, e.g., long association of an audit engagement partner or other key engagement personnel with a particular client or a recent former partner or senior staff member of an audit firm serving as CFO or in some other key management role at an audit client
- Intimidation, e.g., threat of replacement of an auditor over a disagreement on the application of accounting principles.

12. *Standards of auditor independence should establish a framework of principles, supported by a combination of prohibitions, restrictions, other policies and procedures and disclosures, that addresses at least the following threats to independence:*

    - *self-interest;*
    - *self-review;*
    - *advocacy;*
    - *familiarity; and*
    - *intimidation.*

13. *Standards of auditor independence should identify appropriate safeguards that the auditor should implement in order to mitigate threats to independence that arise from permissible activities and relationships.*

14. *Standards of auditor independence should address specifically the need to ensure appropriate rotation of the audit engagement team such that senior members of a team do not remain in key decision-making positions for an extended period.*

15. *Standards of auditor independence should require the auditor to identify and evaluate all significant or potentially significant threats to independence, including those arising from recent relationships with the entity being audited that may have preceded the appointment as auditor, and document how the auditor has applied safeguards to mitigate those threats.*

16. *Securities market regulators should ensure that there is a system in place to require prompt disclosure of information about the replacement of an auditor of a listed entity.*

17. In some jurisdictions, replacement of an auditor requires the prior approval of a regulator. In other jurisdictions, when an entity replaces its auditor, it must disclose whether within a defined period of time prior to the change there were any disagreements with the former auditor on any matter relating to accounting principles or practices, financial statement disclosure or auditing scope or procedure and whether any disagreements were resolved to the former auditor's satisfaction. The former auditor may be required to confirm assertions by the former client's management concerning any matters of disagreement.

The audit committee

18. The governance structure of an entity can play an important role in monitoring and safeguarding the independence of its external auditor. The exact form of an entity's governance structure and the roles that any individual governance bodies perform in relation to the external auditor may vary depending on the requirements of national laws. In some jurisdictions, a single body commonly known as an "audit committee"

oversees all matters relating to the external auditor. In other jurisdictions, more than one body within the governance structure of a listed entity may assume this responsibility. For ease of reference, this paper uses the term "audit committee" to refer to any governance body or bodies with responsibilities for overseeing the external auditor, regardless of whether they have that title.

19. *The Technical Committee believes that, regardless of the particular legal structure in a jurisdiction, a governance body that is in both appearance and fact independent of management of the entity being audited and acts in the interests of investors should oversee the process of selection and appointment of the external auditor and the conduct of the audit.*

20. While the auditor is accountable and commonly reports to the shareholders, he or she does not in practice have a direct relationship with them. The audit committee should therefore serve as a proxy for the shareholders.

21. *The audit committee should be the key representative body with which the external auditor interacts.*

22. *The audit committee should be established with a mandate that permits it to carry out its responsibilities free of any unreasonable restraints. Those responsibilities should include matters such as evaluating whether the audit fees charged by the auditor appear adequate in relation to the work required to support an audit opinion without regard to fees that might be paid to the auditor for other services.*

23. *The audit committee should on a regular and frequent basis meet with the auditor without management present and discuss with the auditor any contentious issues that have arisen with management during the course of the audit and whether they have been resolved to the auditor's satisfaction.*

24. *When selecting an auditor to recommend for appointment or reappointment, the audit committee should satisfy itself that the auditor is independent in accordance with applicable standards.*

25. Examples of procedures the audit committee might follow to satisfy itself, both initially and on an ongoing basis, as to the auditor's independence include:

- obtaining an understanding of professional and regulatory requirements pertaining to objectivity and independence that apply to the auditor in the entity's home jurisdiction. When an entity's securities are offered or listed in one or more foreign jurisdictions, the audit committee would also consider any additional requirements that may apply in those foreign jurisdictions;
- considering all relationships between the auditor[1] and management that might affect the auditor's ability to act objectively, discussing those relationships with

[1] The term "auditor" should be broadly construed to include not only an individual engagement partner but also the firm itself, including related entities such as what is sometimes termed a "network firm".

the auditor and obtaining an understanding of how the auditor would guard against any identified threats;

- seeking from the audit firm information about policies and processes for maintaining independence and monitoring compliance with relevant requirements, including how its incentive and compensation policies for partners and senior staff align with the interest of the audit committee in ensuring independence;
- seeking from the audit firm information about how it monitors compliance with independence requirements by foreign affiliated or unaffiliated firms that carry out significant portions of the audit work required in order to permit the auditor to express an opinion on the consolidated financial statements of the entity; and
- discussing with the audit firm the findings of quality control inspections of the firm's systems and processes for maintaining independence.

26. To monitor independence effectively, it is good practice for the audit committee to discuss with the auditors, at least annually, matters relating to their independence, including all significant threats to independence identified by the auditors and the safeguards implemented. To provide support for such discussions, the audit committee may wish to consider obtaining a written statement from the auditors:

    - confirming that they are, and have been throughout the conduct of the audit engagement, independent in accordance with the terms of all relevant professional and regulatory requirements; and
    - summarizing all significant services provided to the entity and its affiliates, together with related fees, identifying separately audit services, other services required to be provided by the entity's auditor, such as in connection with an offering of securities, and other non-audit services grouped according to the nature of the services provided.

27. *The audit committee should oversee establishment of the entity's policies governing the circumstances in which contracts for the provision of permitted non-audit services can be entered into with the company's external auditors and the procedures that must be followed before doing so. The audit committee should also monitor compliance by management with those policies and procedures.*

28. To ensure it is satisfied the auditor's independence will not be compromised, the audit committee might consider, for example, the desirability of implementing a policy that all material non-audit services to be provided by the auditor must be approved in advance by the audit committee. The audit committee may also wish to consider requiring an open tendering process for all contracts with the auditor in excess of a specified monetary value. When the skills and expertise required to provide a particular non-audit service are readily available on similar terms from service-providers other than the entity's external auditor, even the appearance that independence could be compromised may be sufficient to militate against engaging the auditor.

29. *The audit committee should establish policies relating to the hiring from an entity's audit firm of senior officers for the entity, including the Chief Executive Officer and the Chief Financial Officer.*

30. In establishing such policies, the audit committee may wish to consider in particular matters relating to the hiring of senior members of the audit engagement team and the safeguards that could be put in place to mitigate any potential for compromising the independence of the audit.

31. *The audit committee should report to the shareholders on the actions it has taken to safeguard the independence of the auditor, including satisfying itself that the auditor is independent in accordance with applicable standards.*

32. Such reports to shareholders should, inter alia, describe the policies and procedures followed to establish that any contracts for non-audit services to be provided by the auditor do not compromise the auditor's independence. The nature of any non-audit service contracts entered into and the amount of the related fees should be disclosed.

Principles for Auditor Oversight

A Statement of the Technical Committee
of the
International Organization of Securities Commissions

October 2002

Introduction

1. Investor confidence is fundamental to the successful operation of the world's financial markets. That confidence depends on investors having credible and reliable financial information when making decisions about capital allocation.

2. The objectives of securities regulation include the protection of investors; ensuring that markets are fair, efficient, and transparent; and the reduction of systemic risk. In pursuit of these objectives, in the area of reporting to investors, there should be full, timely, and accurate disclosure of financial results and other information that is material to investors' decisions. Full and fair disclosure is essential to investor protection, enhances investor confidence, and promotes market liquidity and efficiency.

3. Independent auditors play a critical role in enhancing the reliability of financial information by attesting as to whether the financial statements prepared by management fairly present the financial position and past performance of the public enterprise in compliance with accepted accounting standards.

4. Effective oversight of the accounting profession and of independent audits is critical to the reliability and integrity of the financial reporting process. The Technical Committee of the International Organization of Securities Regulators ("IOSCO") has developed a list of general principles for oversight of audit firms and auditors that audit financial statements of companies whose securities are publicly traded in the capital markets (hereinafter referred to as "auditors").

5. At the present time, a variety of systems for auditor oversight exist among the IOSCO Technical Committee members. In many cases, these existing systems are undergoing review as a result of financial reporting failures, weaknesses discovered in self-regulatory structures, changes in public expectations, requirements of new legislation, or for other reasons. One jurisdiction has reported that firm-on-firm peer review under self-regulation failed and that new legislation has directed the creation of an auditor oversight body, independent of the accounting profession, with strengthened powers for rulemaking, inspection and disciplinary authority. A number of other jurisdictions have announced that changes will be made in auditor oversight processes and structures. The Technical Committee believes that there is a growing consensus internationally as to the benefits of an auditor oversight system that is not based exclusively or predominantly on self-regulation.

6. The principles set forth herein are intended to assist securities market regulatory authorities, and other authorities with responsibility for auditor oversight, in developing and enhancing regulatory structures for auditor oversight in the wide range of different legal, business and professional environments that exist in IOSCO member jurisdictions. The Technical Committee encourages IOSCO members to work towards implementing these principles in their own jurisdictions. In jurisdictions in which the securities regulator does not have primary responsibility for auditor oversight, it will nevertheless

have an interest in ensuring that the oversight system is consistent with maintaining and enhancing investor confidence in published financial statements.

Principles for auditor oversight

7. Oversight of auditors can occur in several ways, including within audit firms, by professional organizations and public or private sector oversight bodies, and through government oversight. In addition, oversight may be provided by supervisory boards and audit committees representing investors in matters relating to individual companies.

8. Within a jurisdiction, auditors should be subject to oversight by a body that acts and is seen to act in the public interest. While the nature of an auditor oversight body and the process through which it carries out its activities may differ among jurisdictions, IOSCO believes that effective oversight generally includes the following:

I. A mechanism to require that auditors have proper qualifications and competency before being licensed to perform audits, and maintain professional competence. A mechanism also should exist to withdraw authorization to perform audits of publicly traded companies if proper qualifications and competency are not maintained.

IOSCO believes establishing qualification requirements and requiring maintenance of professional competency should improve the quality of auditing. Moreover, the risk that authorization can be revoked for failure to have or maintain the necessary qualification should be an incentive for compliance and adherence to auditing standards.

II. A mechanism to require that auditors are independent of the enterprises that they audit, both in fact and in appearance. Effective standards, regular assessments, and regulatory oversight generally increase the likelihood that independence is maintained.

III. A mechanism should exist to provide that a body, acting in the public interest, provides oversight over the quality and implementation of auditing, independence, and ethical standards used in the jurisdiction, as well as audit quality control environments.

IV. A mechanism should exist to require auditors to be subject to the discipline of an auditor oversight body that is independent of the audit profession, or, if a professional body acts as the oversight body, is overseen by an independent body. Such an auditor oversight body must operate in the public interest, and have an appropriate membership, an adequate charter of responsibilities and powers, and adequate funding that is not under the control of the auditing profession, to carry out those responsibilities.

An auditor oversight body should establish a process for performing regular reviews of audit procedures and practices of firms that audit the financial statements of listed public companies. This oversight process may be performed in coordination with similar quality control mechanisms that are in place within the audit profession, provided the oversight body maintains control over key issues such as the scope of reviews, access to and retention of audit work papers and other information needed in reviews, and follow-up of the outcome of reviews. Reviews should be conducted on a recurring basis, and should be designed to determine the extent to which audit firms have and adhere to adequate quality control policies and procedures that address all significant aspects of auditing. Matters to be considered include:

a. Independence, integrity and ethics of auditors
b. Objectivity of audits
c. Selection, training, and supervision of personnel
d. Acceptance, continuation and termination of audit clients
e. Audit methodology
f. Audit performance, that is, compliance with applicable generally accepted auditing standards
g. Consultation on difficult, contentious or sensitive matters and resolution of differences of opinion during audits
h. Second partner reviews of audits
i. Communications with management, supervisory boards and audit committees of audit clients
j. Communications with bodies charged with oversight over the financial reporting process, for example, on matters such as regulatory inquiries, changes in auditors, or other matters as may be required
k. Provisions for continuing professional education.

An auditor oversight body also should address other matters such as professional competency, rotation of audit personnel, employment of audit personnel by audit clients, consulting and other non-audit services, and other matters as deemed appropriate.

V. An auditor oversight body should have the authority to stipulate remedial measures for problems detected, and to initiate and/or carry out disciplinary proceedings to impose sanctions on auditors and audit firms, as appropriate.

VI. In relation to companies operating or listing on a cross-border basis, IOSCO members are encouraged to provide each other, whether directly or through coordinating with the auditor oversight body in their jurisdiction, with the fullest assistance permissible in efforts to examine or investigate matters in which improper auditing may have occurred and on any other matters relating to auditor oversight. Members are also encouraged to explore approaches to enhance cooperation among jurisdictions.