

Environment Facing the Profession & IFAC: Appendix to the IFAC Strategic Plan for 2007-2010

IFAC recognizes the environment in which it operates and seeks to proactively shape that environment through the way it operates and the services it delivers in order to generate global economic growth and stability. This is consistent with its fundamental goal to put the public interest first, with recognition that this will be achieved most effectively through a strong accountancy profession worldwide comprised of highly qualified and competent individuals.

In order to achieve this, IFAC routinely considers the environmental factors that effect it and the wider accountancy profession. These factors are summarized below. Section 1 seeks to articulate the impact these factors; Section 2 outlines how these factors effect IFAC's approach to delivering on its mission.

Section 1 Environmental Factors

General Environmental Factors

- **Globalization:** The increasingly global flow of capital and pressure for consistency of approach of regulatory regimes and uniformity of financial reporting structures highlight that globalization continues to be a strong driving force in the international economy. It is also recognized that as part of globalization there are shifts in the direction of global capital resulting from economic cycles and the addition of major economic powers. While this reinforces the continuing need for uniformity in financial information and the quality of that information, it also highlights the variation in the level of development across the global economy. Globalization has also encouraged the use of outsourcing/off-shoring of business services, providing opportunities for professionals in emerging markets.
- **Regionalization:** As a consequence of globalization many nations have recognized the benefits of co-operation with neighbors. This has led to the development of regional trade and professional groupings that can permit economies of effort for the participants. In some cases, this cooperation can strengthen support for convergence to international standards; in other cases, it is a hindrance.
- **Distribution of Wealth:** As all countries, especially the major economic powers, seek to attract global capital there is an ever increasing awareness of disparity in income levels, both between and within countries. In many countries this disparity is widening, with an increasing proportion of the world falling below poverty levels.
- **Technological Advances:** All accountants and other professionals, whether they operate in public practice firms, corporations, small- and medium- sized enterprises, governments or not-for-profit organizations, are fundamentally affected by technological advances. Examples include the application of web-based technologies for collecting, managing, enhancing and disseminating information and advancements in expert-based systems that reduce workloads but enhance the need for professional judgment. Technological advances have also increased the speed at which business is conducted, which could potentially affect the quality of services or products.

Environmental Factors Common to the Wider Profession

- **Credibility of Financial Reporting and the Worldwide Accountancy Profession:** Recent business failures around the globe and inaccuracies in financial reporting have undermined

the perceived value of the information provided by financial reporting and those that have a role in determining its content, including the worldwide accountancy profession. The credibility of the profession in turn influences the level and strictness of regulation, the ability of the profession to self-regulate, public confidence and the viability/sustainability of the profession, as well as the independence of standard setters.

- **Corporate Credibility:** Over the past few years corporations have been required to comply with increasing regulatory requirements in many jurisdictions. These requirements have been implemented in an effort to address issues of corporate credibility, such as governance and management practices, specifically in relation to financial reporting, internal control and financial management, and corporate ethics. This has resulted in an increase in compliance costs in many of the world's major economies and has had a dramatic impact on professional accountants operating in business and in practice. This is leading to assessments of the impact of this increased regulation on global markets. The inevitability of another public scandal underscores the importance of planning the profession's responses to governance failures and the public and political repercussions of such an event.
- **Regulation of the Worldwide Accountancy Profession:** There continues to be an increasing regulation of the accountancy profession by government and others. In many jurisdictions, this has resulted in a change from self-regulation by the local accountancy profession to one of the following: monitored self-regulation; joint regulation shared between the local accountancy profession and government agencies; or regulation by entities completely outside the local accountancy profession.
- **Convergence:** The importance of global convergence in standards to users, preparers and auditors of financial information, regulators and others continues to be extremely high. Many jurisdictions are in the process of implementing processes to convergence of international standards or have made commitments to convergence on a relatively short timeframe. However, varying definitions of convergence continue to affect this progress.
- **New Needs of Information Users:** New forms of information to enhance business reporting as a whole continue to be identified in order to meet the needs of organizations, investors, capital markets, governments, the wider public and others. For example, many of these groups seek a better understanding of wider organizational performance through the provision of information on sustainable development, management of organizational risks and narrative reporting, governance practices and structures, performance indicators and other value drivers, and compliance with regulations, which is not always provided by the conventional accounting and financial reporting model. Call for these new tools and data can also blur the lines between areas of expertise traditionally reserved for accountants and other business professionals, allowing encroachment into products and services previously only provided by accountants and auditors.
- **Technological Advances:** Technologies, in particular business-enabling technologies and electronic commerce, are fundamentally reshaping the timing and content of reporting operating and financial performance, the ability and methods used to provide assurance over that performance, and the availability of information. These technology advances have had a dramatic effect on the way the worldwide accountancy profession operates, the competencies required by professional accountants and the expectations of the public. Many of these advances have prompted the marketplace to increase pressure on audit committees, management, auditors and others to deliver information more quickly, which may ultimately

affect the quality of the job performed. There are also pressures for those sectors of the profession that at times find it difficult to meet the challenge of keeping pace with technological advances, including, for example, many small- and medium- sized practices and enterprises. Advances in technology have also allowed non-accountants to encroach upon the traditional role of the accountant by automating previously complex processes which required specialized knowledge or skills. As automation allows broadening of the services offered by professional accountants, it becomes more important to maintain public confidence and clearly define the skills unique to the professional accountant.

- **Continual Enhancement of the Value of a Professional Designation:** The value placed on a professional accountancy designation is determined both by the holders of the designation and their clients. IFAC recognizes that the profession continually needs to build on the value of professional accountants to global labor markets. In recent years this has been demonstrated through improvements in educational systems used to train and maintain the skills of professional accountants and through the strengthening of ethical principles required by the profession. Additional pressure in this area stems from competition for new entrants to the profession. Strict regulation and the blurring of areas of expertise have made accountancy a less attractive career path in some regions.
- **Litigation:** Litigation against firms in public practice and individuals sitting on boards of directors continues to be a significant issue for the profession. While this affects firms and directors globally, the intensity of the effect varies across jurisdictions depending on a variety of factors, in particular, the method of liability apportionment in place and the state of the regulatory environment in an individual jurisdiction. If the apportionment of liability in some jurisdictions continues to be inequitable, professional accountants at senior levels within firms and those sitting on boards of directors may not continue to accept the level of risk.

Environmental Factors Specific to Audit

- **Scope of Services:** Firms in public practice are increasingly under pressure from regulators, investors, corporations and others to ensure that their independence, perceived and actual, is not compromised by the scope of services they provide.
- **Audit Performance Gap:** The profession has a role to address instances where there has been a clear failure to deliver against realistic expectations. Here again, the relationship between regulators and standard setters becomes crucial, as coordinated responses to failures and proper planning for certain inevitabilities can temper the backlash to such events.
- **The Expectations Gap:** In many jurisdictions, a gap continues to exist between what regulators, preparers and investors expect to receive as the result of the assurance process and what auditors believe can be realistically provided by assurance services, especially audits. The need to educate those parties as to the realistic expectations of an assurance engagement continues to be an issue. Care needs to be taken, however, to distinguish this from instances of audit performance failure.
- **Concentration of Large Firms:** Many of the pressures on the worldwide accountancy profession have been directed toward the larger audit firms by regulators, the media, investors and others. These firms are giving renewed emphasis to the issues of quality control, scope of services, rotation of engagement partners, underlying risks associated with performance of audit work and litigation risk. There are concerns that competition, and therefore the quality of audits, could suffer if the number of large firms is reduced further.

The same concerns would also result should any of the large firms stop providing public company audits.

Environmental Factors Specific to Accountants Operating in Business, the Public Sector, the Development of the Profession and Small- and Medium- Sized Practices

- **Changing Roles of Professional Accountants Operating in Business:** Accountants are performing many different roles compared to those performed just a decade ago. This is a result of greater recognition of a professional accountant's education, expertise and knowledge and how these can be applied to the growing complexity of organizational needs in areas such as management, governance, planning and technology. It is also as a result of greater efficiencies and refinements in roles that were previously performed by professional accountants through, for example, improved technologies. These efficiencies and refinements have enabled organizations and professional accountants to identify more clearly those aspect(s) of their role where application of professional judgment remains critical. Professional accountants in business face the challenge of increasing efficiency while broadening the services they offer, and still maintaining accuracy. These changes have direct impact on the type and scope of education required of new and continuing accounting professionals. An additional challenge lies in balancing this broader and deeper education and testing with the attractiveness of the profession in relation to other business management educations, e.g., MBAs.
- **Growing Emphasis on Improved Governmental Financial Reporting:** Federal (national), state, provincial and local governments are increasingly under pressure within their constituencies and from other stakeholders to improve their general governance practices and, more specifically, their governmental accounting and financial reporting. Cooperative efforts with international funders and development banks can affect the decisions made in the implementation of governmental accounting standards, both in developing economies and, through political pressures, developed economies. Increase in tax competition between governments of different governments.
- **Effect of Globalization on Developing and Emerging Economies:** The development of cross-border markets has had significant implications for developing and emerging economies as well as for developed economies. It is increasingly important for developing and emerging economies to have in place strong regulatory and enforcement processes, institutions, standards and overall educational levels to meet the demands of donor agencies, encourage foreign investment and aid in the implementation of social and economic improvements within the wider domestic environment. In many of these economies the profession is often less developed than in other countries. This directly impacts on the operation of the capital and labor markets in these economies and therefore the level of economic growth and stability. Development banks and other international funders, however, could require that governments in these economies properly implement accepted international accounting and financial reporting standards.
- **Application of Standards by Small- and Medium- Sized Practices:** The increasing acceptance of international standards, particularly in the areas of accounting, auditing and ethical standards presents both knowledge and relevancy issues for small- and medium- sized practices (SMPs). The increase in volume and complexity of international standards is providing an ever growing challenge to SMPs in maintaining a high level of competency in the provision of services to their clients. Further, the nature and content of the international

standards that SMPs are increasingly required to comply with or apply in servicing their clients are increasingly considered less relevant.

- **Application of Standards by Small- and Medium- Sized Enterprises:** As international standards gain greater acceptance, there are increasing issues regarding the applicability and relevance of accounting and auditing standards to small- and medium- sized enterprises. Standard setters, particularly those developing accounting standards, are increasingly being asked to develop standards for application by small- and medium- sized enterprises and ensure that those standards are appropriate from the cost-benefit perspective appropriate to the user audience.

Section 2 Environmental Factors – Implications for IFAC

Each of the above environmental factors impacting the profession has implications for IFAC, particularly in terms of the strategies it adopts and the resulting services that it provides. IFAC is aware that there are other organizations that have an active interest in addressing these factors and that IFAC’s role will vary—between leader, facilitator or collaborator—depending on the nature of the activity and the parties involved. IFAC remains conscious of the strategic choices it has in the services and other actions that it undertakes in delivery of its mission. It is also committed to maximizing its own effectiveness and efficiency.

Listed below are some of the implications for IFAC arising from the environmental factors highlighted above:

- **Building Public Confidence and Serving the Public Interest:** IFAC has made significant commitments towards serving the public interest. This commitment is particularly evident in the oversight mechanisms of the PIOB and the continual enhancement and maintenance of strong standard-setting processes. Supporting these activities as well as continually identifying other initiatives and opportunities aimed at building public confidence will continue to be a top priority of IFAC in the coming years.
- **Relationships with the Regulatory Community:** For the past few years IFAC has strived to enhance its relationship with the international regulatory community, reinforcing the role that the accountancy profession can play in serving the public interest. Enhancing these relationships continues to be critically important for IFAC as a mechanism for constructively engaging with regulators on issues that have an impact on IFAC and the profession, and ensuring that the public interest is served.
- **Developing High Quality Auditing Standards that Serve the Public Interest:** IFAC’s highest priority is the continued development of high-quality International Standards on Auditing (ISAs) that serve the public interest. IFAC, through the International Auditing and Assurance Standards Board (IAASB), is increasingly recognized as the organization best qualified to develop ISAs as a result of its expertise, quality output and rigorous due process. To continue to develop high-quality standards that serve the public interest, IFAC and the IAASB are committed to: strengthening its due process, including obtaining adequate input from external parties; keeping transparency paramount; and making available adequate resources to the standard-setting processes. These efforts are also reinforced through the oversight provided by the PIOB over the IAASB standard-setting processes.
- **Serving as the Global Standard Setter:** In addition to IFAC’s role in developing ISAs, there is increasing recognition of the value of its other standard-setting roles — assurance,

ethics, education and public sector accounting. More and more organizations, such as international financial institutions, regulators, governments and aid agencies are looking to IFAC to provide strong leadership in these areas. As with the IAASB, the strengthening of the standard-setting processes, including oversight by the PIOB for the International Accounting Education Standards Board (IAESB) and the International Ethics Standards Board for Accountants (IESBA), is critical to increasing the international acceptance of IFAC's standards.

- **Developing the Worldwide Accountancy Profession:** The continued move towards convergence of standards relevant for the accountancy profession has underlined the importance of providing assistance to all parts of the profession which enables successful convergence. Building on its understanding of the barriers to implementation of international standards (based on results from the Report, *Challenges and Successes in Implementing International Standards: Achieving Convergence to IFRSs and ISAs* published in 2004) and identifying solutions to those barriers will be important for all IFAC activities in the coming years. In particular the work of the Developing Nations Committee, Small and Medium Practices Committee, the Member Body Compliance program and IFAC's standard-setting boards will be instrumental in achieving this goal.
- **Acting as Spokesperson:** Many of the environmental factors identified require that IFAC is in a position to comment on appropriate regulatory and public policy matters on behalf of the worldwide profession and engage in dialogue with the appropriate parties on these matters. The IFAC Board will provide direction on these regulatory and public policy matters where the profession has a level of expertise, with a view to ensuring that the public interest is served.
- **Serving as a Facilitator:** In developing the worldwide accountancy profession IFAC needs to determine how it can best facilitate the exchange of information and foster relationships between numerous parties: whether it be between member bodies in initiatives such as those that support professional accountants in business or small- and medium- sized practices or in bringing the development agencies together with member bodies in developing and emerging economies.
- **IFAC Expertise:** The increasing focus on IFAC and its achievement of its mission means it is essential for IFAC to continue to recruit the best individuals for IFAC committees, boards and task forces, ensuring that there is an appropriate balance of backgrounds and qualifications. Continuing to appoint highly qualified staff to undertake both technical and operational roles is also critical. IFAC's ability to recruit staff continues to be impacted by the United States work visa restrictions. It remains a high priority of the IFAC Board and management that this situation is resolved in an acceptable manner as quickly as possible.
- **Enhancing Communications:** Many of the environmental factors require that IFAC has in place mechanisms that achieve effective two-way communications with its main stakeholders, such as its member bodies, firms, regulators, professionals and leaders in commerce and industry and international financial institutions. It is an important process not only for disseminating information and generating awareness and support, but also for obtaining input from IFAC's key constituencies.
- **Changing Knowledge Requirements of Accountants:** As the roles performed by professional accountants change and the expectations for reliability and transparency

increase, IFAC needs to consider its role in assisting professional accountants in further developing their knowledge base and in reflecting these changing roles in the education requirements. This may, for example, influence the nature of guidance produced and the topics for which IFAC seeks to act as facilitator. It also underlies the importance of continuing professional education/development both for member bodies in terms of implementing a regime in line with the recently approved International Education Standard and for individual professional accountants in terms of their need to commit to ongoing education to maintain a high level of competence.

- **Maintaining Relevance to Member Bodies:** Several of the environmental factors identified how, for example, the move away from total self regulation of the accountancy profession in many jurisdictions, has affected the role of individual IFAC member bodies. To continue being relevant to member bodies, IFAC will continue to engage in regular dialogue with its member bodies through various forums and respond to their concerns in a positive and realistic manner.
- **Operating within Resource Constraints:** IFAC continues to experience resource constraints, both financial and human. The Board and management are determined that IFAC will continue to deliver its mission and strategies, while operating within and maximizing the value obtained from available resources. IFAC will achieve this by continually prioritizing its strategies and services, and assessing the efficiency with which it is carrying out its activities. Additionally, IFAC continues to assess existing and potential revenue sources, while ensuring that its ability to act in the public interest is not compromised. In order to achieve the strategies and services identified in this plan, IFAC will need to extend the level of financial resources received from current sources and identify and utilize other sources as appropriate for a specific activity.