

Ethics Committee Project Proposal

1. Subject

IFAC Code of Ethics - Independence

2. Reasons the Subject Should Be Studied Now

IFAC Code of Ethics Section 8 Independence was issued in November 2001 with an effective date for assurance engagements when the assurance report is dated on or after December 31, 2004. Earlier application was encouraged.

Section 8 provided a framework, built on principles, for identifying, evaluating and responding to threats to independence. The Section also provides examples of circumstances that may be faced by assurance providers. It recognizes that in certain circumstances the threats created would be so significant that not safeguards would be able to reduce the threats to an acceptable level. In such circumstances, the only possible action is to eliminate the activity or relationship creating the threat or refuse to continue or accept the assurance engagement.

Since Section 8 was issued there has been a loss in credibility in financial reporting and many jurisdictions have taken steps to restore this credibility. Some of these steps have related to auditor independence requirements.

3. Scope of Project

(a) LIST THE MAJOR ISSUES THAT SHOULD BE ADDRESSED

Implementation

Information on member body and firm experience will be gathered through surveys (see Appendix). The surveys will contain an open-ended question to solicit any other comments or issues encountered in implementing Section 8.

Clarity of Prohibitions

Section 8 contains prohibitions – examples of circumstances that would create a threat that is so significant safeguards could not eliminate the threat or reduce it to an acceptable level. The experience of member bodies and other standard setters should be reviewed to determine any change should be made to the style of presenting the prohibitions.

Scope of Services

Section 8 requires guidance on the independence implications of providing non-assurance services to an assurance client. It also provides some specific prohibitions on such services. The experience of member bodies and other standard setters should be reviewed to determine whether any addition guidance, or prohibitions, should be provided in this area.

Rotation

Section 8 currently requires rotation of the engagement partner on the audit of a listed entity after a predefined period of time, normally no more than seven years, and further provides that after rotating such an individual should not serve on the assurance team until a further period of time, normally two years, has passed. The Ethics Committee has also approved a requirement to rotate the person responsible for the engagement quality control on a similar basis.

The experience of member bodies and other standard setters should be reviewed to determine whether the rotation period (including the cooling off period) is appropriate and whether the rotations requirements are broad enough or whether there should be rotation requirements for other members of the assurance team for listed audit clients.

Application to Public Interest Entities

Section 8 paragraph 23 states that consideration should be given to the application of the principles related to the audit of listed entities to other audit clients that may be of significant public interest. The experience of member bodies and other standard setters should be reviewed to determine whether additional guidance should be provided in this area.

(b) DESCRIBE IMPLICATIONS FOR ANY SPECIFIC PERSONS OR GROUPS

- CAG and IOSCO, due to stakeholder and regulatory interest in auditor independence.
- SMP Task Force, particularly with regard impact of any changes on small and medium practitioners.

(c) CONSIDER WHETHER IT REQUIRES PARTICULAR CONSIDERATION

There are no specific IT considerations.

4. Indicate the Type of Material to Be Published and Timeline

Revision of the independence requirements of Code of Ethics

Proposed timeline:

- Send out questionnaire – September 30, 2004
- Questionnaire deadline – November 15, 2004
- Consideration of findings – February 2005
- Discussion with Forum – June 2005
- Exposure – September 2005
- First Read – February 2006
- Final – June 2006

5. Resources Required

- An Ethics Committee task force, including a public member.
- One staff support.

6. List Important Sources of Information That Address the Matter Being Proposed

- Survey results
- Independence requirements established by standard setters that are not member bodies
- Recent research on independence

7. Factors That May Add To Complexity or Length of Project

- None noted.

Prepared by Jan Munro Date July 28, 2004

Comments by Technical Managers/Committee Secretaries

The comments and sign-off of *each* Technical Manager are required before this Project Proposal is considered by the Ethics Committee.

IAASB

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Professional Accountants in Business

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Education Committee

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Compliance Committee

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Trans-National Auditors' Committee

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

SMP Committee

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Public Sector Committee

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Developing Nations Task Force

CLASSIFICATION *Class:*

SUGGESTED PRIORITY

COMMENTS

Signed Date

Project Classifications

All activities of IFAC have the same overall objectives. When a project involving more than one committee is approved, there must be close co-ordination to minimize schedule disruptions and to avoid inconsistent conclusions. The following procedures are designed to try to ensure the smooth co-ordination of joint projects.

Standards and Guidelines

A project is put forward for approval only when a Project Proposal has been completed; each Project Proposal includes space for the recommendation of each committee secretary on the proposed nature of a project under one of the following classifications:

Class A Project: entirely the responsibility of only one committee.

Class B Project: mainly the responsibility of one committee but with important implications to at least one other committee.

Class C Project: a joint project—the priority, work and conclusions are of importance to two or more committees.

Approval of the classification of a project lies with the responsible committee(s).

1. CLASS A PROJECTS

Full details of a Class A project will be sent only to the committee responsible for its development and approval but the committee secretaries of the other committees will be kept informed by the responsible committee secretary, at all significant points, of the project's progress by distribution of committee agenda papers.

2. CLASS B PROJECTS

Since the degree of “jointness” can vary substantially in a Class B project (from being almost a Class A to almost a Class C project), the Project Proposal form should indicate which of the two following routes is proposed for handling the project:

B1: The work will be handled entirely by a subcommittee of the “primary” committee but at significant points in the development of the project (statement of principles, exposure draft, final recommendations) the “primary” committee will ascertain from the other committee(s) whether the proposals would create significant difficulties for the other committee(s) before the “primary” committee approves the material.

B2: The subcommittee of the “primary” committee responsible for the project will have added to it one or two representatives of the other committee(s).

Whichever route is approved, comments by the other committee(s) will be considered by the “primary” subcommittee and the “primary” committee.

3. CLASS C PROJECTS

[Process under discussion]

4. SIGNIFICANT DIFFICULTY

To avoid the possibility of inconsistencies in Recommendations between standard-setting committees, on any project on which one of the standard-setting committees has indicated to another that the project would create a significant difficulty,* the difficulty must be resolved to the satisfaction of both committees before the project proceeds.

If an irreconcilable difference occurs between committees, the matter can be referred, by either or both of the committees concerned, to the Board for an opinion but in no case will amendments or additions be made to the IFAC Handbook or to other official pronouncements as long as there remains a significant difficulty between committees.

Discussion Papers and Other Information Documents

The same procedures as for Standards and Guidelines (including the classification of a project) will be followed in the preparation and approval of these publications.

* A significant difficulty is considered to have been created when a proposed Recommendation from one committee will, in the opinion of the other committee, undermine or contradict a Recommendation of another committee.