

Proposed Revised Section 290 Independence – Assurance Engagements
Detailed Cut and Paste of Comments Received

X ref	Par Ref	Issue	Respondent	Proposed Resolution
1.	General	The APB welcomes the new definition of network firm and supports the background material on the interpretation of this definition. This new definition reflects the operation of global accounting firms and recognises more clearly those firms which a reasonable and informed third party would consider to be part of the same network, notably including a consideration of the use of a common name and sharing of significant professional resources.	APB1	General comment
2.	General	The Institute of Certified Public Accountants of Singapore (ICPAS) appreciates the opportunity to comment on the IF AC Ethics Committee's Exposure Draft (ED) on the Proposed Revised Section 290 "Independence -Assurance Engagements".	ICPAS	General comment
3.	General	I am pleased to set out below the response of the CCAB Ethics Group to the IFAC Ethics Committee consultation on the above subject. The Ethics Group of the Consultative Committee of Accountancy Bodies (CCAB EG) is a co-ordinating group for the Ethics Committees of the six main accountancy bodies in the United Kingdom and Republic of Ireland. Individual accountancy bodies may submit separate responses to the consultation but as it is the intent of all of the CCAB bodies to harmonise their ethical guidance towards that promulgated by IFAC, it was thought useful to submit this combined response.	CCAB	General comment
4.	General	We agree with the underlying intent of the proposed revision to treat as network firms, those which, in essence, act together or purport to act together. However, as we point out below, we have concerns over the practical difficulties and potential problems that may arise because of the revised definition and we discuss these specific issues below.	ICAS	General comment
5.	General	We understand the need for further clarification of what constitutes a network of firms, given the requirement that network firms be independent of audit clients of firms within the network.	CPAAI	General comment

1 For legend of abbreviations see end of agenda paper

6.	General	The Hong Kong Institute of Certified Public Accountants is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. We welcome the opportunity to provide you with our comment on the captioned IFAC Exposure Draft.	HKICPA	General comment
7.	General	<p>The Basel Committee on Banking Supervision has a strong interest in high quality and independent audits of banks and has carefully analysed the proposals of the Ethics Committee pertaining to the proposed new definition of a network firm in the Code of Ethics for Professional Accountants and the related proposed revised Section 290, Independence-Assurance Engagements of the Code of Ethics.</p> <p>The Committee is pleased to note that the Ethics Committee initiated a project to review the definition of a network firm and welcomes the initiative to provide guidance on this important subject in Section 290 of the Code of Ethics.</p>	Basel	General comment
8.	General	IOSCO's Standing Committee No. 1 ("SC 1") is writing to provide comments regarding the Exposure Draft of proposed revisions to Section 290 of the IFAC Code of Ethics for Professional Accountants ("the Code"), concerning a proposed new definition for the term "network firm". Our comments reflect those matters on which we have reached a general consensus among Standing Committee No. 1 members and are not intended to include all the comments that might be provided by individual members on behalf of their respective jurisdictions. The focus of our comments is on independence standards provisions that should exist for audits of public listed companies.	IOSCO	General comment
9.	General	As acknowledged in the explanatory memorandum to the Exposure Draft professional firms frequently form associations in connection with the delivery of services. Associations with certain characteristics have become known as networks.	Moore Stephens	General comment
10.	General	The Ethics Committee of the South African Institute of Chartered Accountants (SAICA) called for comments on the Exposure Draft from the members of SAICA. The Committee received no comments of significance and therefore can suggest no changes to the proposed definition of a network firm.	SAICA	General comment

11.	Supportive Comment	<p>We strongly support the work of the IF AC Ethics Committee in the development of this ED, which proposes revisions to the definition of a network firm.</p> <p>We support the proposals in the ED on the basis that the proposals will serve to strengthen public confidence in the global accountancy profession and serve the public interest.</p>	ICPAS	General comment
12.	Supportive Comment	<p>The CCAB EG agrees with the underlying intent of the proposed revision to treat as network firms, those which, in essence act together or purport to act together. We believe that IFAC has achieved that underlying aim overall, in the exposure draft presented for comment. However, there are a couple of specific points that we believe should be addressed:</p>	CCAB	General comment
13.	Supportive Comment	<p>As an overall comment, we welcome the proposed revised definition as it is broadly consistent with the proposed definition provided by the draft directive on statutory audit in the provisional version of 7 December 2004.</p>	CNCC/OEC	General comment
14.	Supportive Comment	<p>The Korean Institute of Certified Public Accountants (KICPA) is pleased to comment on the above referenced exposure draft.</p> <p>We agree in general with the Ethics Committee’s position regarding the definition of “Network firm” and have no comments.</p>	KICPA	General comment
15.	Supportive Comment	<p>We are supportive of the proposed revisions to the Code of Ethics for Professional Accountants as contained in the ED and encourage the Ethics Committee to complete their promulgation in an expeditious manner.</p> <p>The ED pertains specifically to the concept of “network firms” and establishing a workable definition for such entities. Indeed, in paragraphs 290.14 through 290.19, the ED provides helpful analysis and examples of situations where firms may be thought to be part of a “network” and where nuanced differences would result in such firms not being a part of a ‘network’.</p> <p>We have four comments with respect to the ED:</p>	E&Y	General comment

16.	Supportive Comment	We respectfully submit our comments and recommendations below and commend the Committee on its efforts. We are supportive of the new definition of network firm but have some concerns about the impact that the definition may have in applying the safeguards set out in the Code of Ethics as further described below.	Grant Thornton	General comment
17.	Supportive Comment	The definition of network firm is relevant to independence in assurance engagements and it is thus appropriate that any definition takes into account the substance of any relationship, rather than just legal form, and also appearance. It is also important, however, that the extra independence requirements that derive from being a network firm, are not imposed needlessly in situations where there is no ability to influence the audit. We believe that the proposed IFAC definition and explanation has achieved the right balance overall. However, there are a number of specific drafting points that we believe should be addressed:	ICAEW	General comment
18.	Supportive Comment	We understand that the proposed revision to the definition of 'Network Firm' and the additional guidance set out in the new paragraphs 290.14 – 209.19 of the IFAC Revised Code of Ethics are intended to further strengthen the independence requirements in the Code. In the interest of clarity and from a developing nation's perspective, we would like to comment as follows:	MIA	General comment
19.	Supportive Comment	We have reviewed the abovementioned Exposure Draft and considered its implications for our Office. The implementation of the proposed standard will result in established independence requirements for professional accountants in public practice, who perform assurance engagements. It also provides a revised, broader definition of a 'network firm' with useful background material on the interpretation of this definition. The Victorian Auditor-General's Office (VAGO) reviewed each of the significant proposals of the abovementioned exposure draft and overall is in agreement with the views expressed in the exposure draft.	AG of Vic	General comment
20.	Supportive Comment	We believe the language contained in Sections 290.14, 290.15, 290.16, 290.18 and 290.19 and in the proposed revised definition of network firm speaks for itself and does differentiate between groups of firms that are networks and associations of firms, like our organization, where the member firms do not have a common name, do not share significant professional resources, and do not share profits or costs of significance with other firms within the larger structure.	CPAAI	General comment

21.	Supportive Comment	We agree with the proposed revised definition of “network firm”, and with the inclusion of the additional guidance in the proposed paragraphs 290.14-290.19 as they appear in the Exposure Draft.	NZICA	General comment
22.	Supportive Comment	We wish to record that we are supportive of the change to the definition of “Network firm” as proposed and conclude that the definition and supporting guidance in the Code provides an appropriate indication of what was intended by the term as used in the Code.	PwC	General comment
23.	Supportive Comment	We believe that the network firm definition is a significant improvement over the existing definition and more accurately reflects the way in which global accounting organizations operate today.	Grant Thornton	General comment
24.	Supportive Comment	SC 1 would like to express appreciation for the Ethics Committee’s efforts to improve the definition of “network firm.” We acknowledge this matter to be a difficult and challenging issue. We believe the definition in this ED is an improvement over the existing definition and have only a small number of changes to suggest for further improvement.	IOSCO	General comment
25.	Supportive Comment	<p>We would like to formally note our support for the initiative taken by the Ethics Committee in revising the definition of “Network Firm” within Section 290 of the IFAC Code of Ethics. We are convinced that the revision of this definition will result in a more robust framework for determining those firms that practice within a network, and are thus subject to the independence requirements related to network firms of the Code of Ethics. The revised definition is, in our opinion, an improvement on the extant definition and should also be able to serve as a basis for other regulatory authorities dealing with the issue of auditor independence.</p> <p>We support the thrust of the proposed revisions. We concur with part (b) of the proposed definition, however we would like to raise a number of matters in respect of part (a) of the definition, together with some amendments and are pleased to submit our comments as follows:</p>	IDW	General comment

26.	Disagree with Approach	<p>We support the IFAC Ethics Committee's initiative to clarify the definition of "network firm". With respect to the proposed revision of the definition we consider that:</p> <ul style="list-style-type: none"> • It should be principles-based such that a firm would be considered as a network firm if it gives the public at large a perception that it belongs to a larger structure so as to avoid a perceived threat to independence; • The criteria included in the proposed definition should be set out as examples of conditions, rather than criteria, that demonstrate that a firm belongs to a network and the examples are not all inclusive; • A firm can only be considered as a non-network firm when it does not make, either publicly or privately an association with any network. 	HKICPA	Isolated comment – not carried further
27.	Disagree with Approach	<p>The Exposure Draft appears to have been drafted on the premise that any impairment of the independence of a "network firm" (as defined) will, in some (but not all) assurance engagement scenarios <u>automatically</u> impair the independence of the firm undertaking the assurance engagement. Whilst we consider that this is a reasonable inference to draw based on the current definition of a network firm:</p> <p><i>"an entity under common control, ownership or management with the firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as being part of the firm nationally or internationally",</i></p> <p>we believe that there is a fundamental flaw in the logic of this conclusion when it is tested against aspects of the proposed new definition of network firm:</p> <p><i>"(a) a firm that is part of a larger structure and that:</i></p> <p style="padding-left: 40px;"><i>(i) uses a name in its firm name that is common to the larger structure; or</i></p> <p style="padding-left: 40px;"><i>(ii) shares significant professional resources with other firms in the larger structure; or</i></p> <p style="padding-left: 40px;"><i>(iii) shares profits or costs with other firms within the larger structure; or</i></p> <p><i>(b) an entity that controls, is controlled by, or is under common control with the firm through ownership, management or other means",</i></p>	Baker Tilly – Jones	Isolated comment – not carried further

28.	Disagree with Approach	<p>The proposed new definition seems, furthermore, to be contrary to the "conceptual framework approach" of the Code of Ethics, by creating an arbitrary black and white rule to cover what is, in reality, an exceedingly grey area. We refer in particular to paragraph 100,5 of the June 2005 Code of Ethics, which states that:</p> <p><i>"A conceptual framework that requires a professional accountant to identify, evaluate and address threats to compliance with the fundamental principles, rather than merely comply with a specific set of rules which may be arbitrary, is, therefore, in the public interest."</i></p> <p>For the purpose of this response, we have focussed primarily on the issue of whether there is or is likely to be any actual or perceived threat to a firm's independence as a consequence of the position of a network firm. However, we have also identified those situations where we consider that a threat to independence is potentially capable of being addressed by appropriate safeguards.</p>	Baker Tilly – Jones	Isolated comment – not carried further
29.	Disagree with Approach	<p>We also have a number of concerns regarding wording of the definition itself. We believe in developing the independence rules the Ethics Committee has departed from its conceptual framework and has ignored the threats and safeguards approach the code generally adopts. There is a presumption that network independence issues are so great that no safeguard can overcome the threat. We believe that this approach is flawed.</p> <p>For example, it would be possible for accounting services to be provided to a subsidiary by a member of a network and for that subsidiary to be audited by a member of another network.</p> <p>We believe that a more sound conceptual approach would be based on the extent to which the lead audit firm places on the other members of its network's work.</p>	Baker Tilly Barnes	Isolated comment – not carried further

30.	Alignment to EU 8 th Directive	<p>As an overall comment, we welcome the Committee's approach, which seems consistent with the definition provided in the draft of the 8th directive on statutory audit (version of July 2005).</p> <p>We hope that the final IFAC definition of a network firm will be aligned with it, and we draw your attention to the timing of the adoption of both the modification in section 290 and the directive to maintain a clear and complete consistency.</p> <p>However, we would express strong concerns with regard to the following issues:</p>	CGCI	See discussion of alignment to EU 8 th directive
31.	Alignment to EU 8 th Directive	<p>As an overall comment, we welcome the Committee's approach, which seems consistent with the definition provided in the draft of the 8th directive on statutory audit (version of July 2005).</p> <p>We hope that the final IFAC definition of a network firm will be aligned with it, and we draw your attention to the timing of the adoption of both the modification in section 290 and the directive to maintain a clear and complete consistency.</p> <p>However, we would express strong concerns with regard to the following issues:</p>	Groupe Excel	See discussion of alignment to EU 8 th directive

32.	Alignment to EU 8 th Directive	<p>Our main concern relates to the definition itself. The draft revision to the European 8th Directive states that a network “means the larger structure:</p> <ul style="list-style-type: none"> - [which is] aimed at cooperation to which a statutory auditor or an audit firm belongs, and; - which is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources.” <p>The substance of the proposed IFAC definition is similar to that included in the European definition (except as noted below, where we believe the EU definition is more appropriate). We are not aware of any other international definitions, and we believe that it would be very helpful to member bodies in Europe, and of no detriment to those elsewhere, if the IFAC definition used the same words as the European definition, above.</p> <p>In the United Kingdom, the auditor independence code is now set by the independent Auditing Practices Board, who will have regard to the finalised Directive. International harmonisation would be assisted here and in countries with similar arrangements to have the fewest number of competing definitions.</p>	ICAEW	See discussion of alignment to EU 8 th directive
33.	Alignment to EU 8 th Directive	<p>We, as have most others, recognised that the existing definition of a network firm for independence purposes is unsatisfactory.</p> <p>We also recognise that the term “network” has become the most commonly used term when referring to groupings of independent accounting firms. There is an implicit danger when using such a term in guidance.</p> <p>At the same time we note that others are developing definitions of network such as within the European Union. We believe strongly that a single definition should be agreed and we would urge IFAC to revisit its definition in the light of the shortly to be agreed EU directive on the regulation of Auditors. We believe that the role of the Ethics Committee should be to provide guidance to the auditing profession on such definitions. It is, however, essential that any such guidance is both credible and practical, in order for further damage to the profession to be avoided.</p>	Baker Tilly Barnes	See discussion of alignment to EU 8 th directive

34.	Alignment to EU 8 th Directive	<p>While we accept that IFAC needs to address the need for a global code, rather than one tailored only to European needs, we note that the substance of the definition given is essentially the same as that included in the draft revision to the European 8th Directive, except as noted below. We do not believe there are other competing definitions with international application, so in such circumstances, we believe that it would be helpful to use the wording of the draft 8th directive, adjusted only for the fact that IFAC defines network firm, but the EU defines network.</p> <p><i>Network “means the larger structure :</i></p> <ul style="list-style-type: none"> - <i>[which is] aimed at cooperation to which a statutory auditor or an audit firm belongs, and;</i> - <i>which is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources.”</i> <p>In a number of EU countries, including the UK and Ireland, independence codes for auditors are no longer set by the profession. It would not help international harmonisation for some codes to adopt the 8th Directive wording and others an IFAC variation, even if the substance of the wording is the same as regards audit engagements.</p>	CCAB	See discussion of alignment to EU 8 th directive
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35.	Alignment to EU 8 th Directive	<p>We believe the proposed revision to the definition of network firm should be aligned to the definition in the draft European 8th Directive.</p> <p>We appreciate that the Ethics Committee aims to serve the needs of the wider global community and not simply to European needs. However, the substance of the definition is the same except as noted below. While we have some reservations about the wording of the definition in the draft European 8th Directive, we believe it would be helpful to align the proposed revised definition of network firm to the draft European 8th Directive but amended only for the fact that IFAC Code of Ethics defines ‘network firm’ whereas the draft European 8th Directive defines ‘network’.</p> <p>In the draft European 8th Directive networks is defined as <i>‘the larger structure :</i> <i>- [which is] aimed at cooperation to which a statutory auditor or an audit firm belongs, and;</i> <i>- which is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources.’</i></p> <p>It does not aid international harmonisation if some codes adopt the draft European 8th Directive definition and others that in the IFAC Code of Ethics, even though the substance of the definitions is the same as regards financial statement audit engagements.</p>	ACCA	See discussion of alignment to EU 8 th directive
36.	Alignment to EU 8 th Directive	<p>We draw however your attention, on the fact that at this stage, this text is not yet completed, and it is expected to be finalised before the end of 2005. Therefore, we would strongly recommend the Ethics committee to consider the final definition of networks which will be adopted by the EU, and if necessary, to align the proposed definition to it. This would enable European audit firms to comply both with the compulsory provisions of the EU and with their IFAC statements of membership obligations requiring the implementation of the IFAC code.</p> <p>We would like to avoid any situation in which European auditing firms could legally be precluded to comply with the network definition of the IFAC code of ethics.</p>	CNCC/OEC	See discussion of alignment to EU 8 th directive

37.	Alignment to EU 8 th Directive	<p>We welcome the Proposed Revised Definition as it is broadly in line with the definition for a network as included in the proposed European Union (EU) Statutory Audit Directive (see the Appendix for further details). However, as the text of this proposed Directive is not yet completed but is expected to be finalised before the end of the year 2005, we recommend the IFAC Ethics Committee to consider in their deliberations the final definition of networks which will be included in the EU Statutory Audit Directive and to align the Proposed Revised Definition to it. This will enable European audit firms to comply both with the mandatory obligations following from the EU Statutory Audit Directive once approved and with their IFAC Statements of Membership Obligations (SMOs) requiring the application of the IFAC Code of Ethics.</p> <p>It should also be noted that in case the definition of a network for independence reasons, as stipulated by the IFAC Code of Ethics, would be different from the legal definition of a network, as stipulated by the EU Statutory Audit Directive, European Union audit firms could legally be precluded from exchanging information related to independence issues where the network definition of the IFAC Code of Ethics would require so. It is self-evident that such situations should be avoided.</p>	FEE	See discussion of alignment to EU 8 th directive
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38.	EU 8 th directive Larger Structure	<p>In substance, the IFAC definition is very similar to that found in the draft revision of the European 8th Directive on statutory audit except as noted below. Whilst we appreciate that IFAC has to develop a definition for global purposes, we believe that the proposed EU definition would be suitable for that purpose and at the same time ensure that European firms are not subject to different and not wholly-interlocking definitions. We do not believe that adopting the EU definition would be detrimental to IFAC's objective due to the substantial similarity that exists between the two definitions. The proposed EU definition is as follows:</p> <p><i>Network "means the larger structure:</i></p> <ul style="list-style-type: none"> - <i>[which is] aimed at cooperation to which a statutory auditor or an audit firm belongs, and</i> - <i>which is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources".</i> <p>In many European countries independence standards for auditors are now set by independent regulatory bodies but under the aegis of the EC Directive. The aim of international harmonisation will not be furthered by some codes having to adopt the 8th Directive wording and others an IFAC variation, even if, as in the case of audit engagements, the substance of the wording is the same.</p>	ICAS	See discussion of larger structure
39.	Larger Structure	<p>We are of the opinion that it would be useful to include in the explanatory material further clarification of the meaning of a 'larger structure' as well as a number of examples of what would constitute (or not) a 'larger structure' in order to enhance the practical application of the Proposed Revised Definition.</p> <p>It would be helpful to clarify whether or under which circumstances the following situations form a 'larger structure':</p> <ul style="list-style-type: none"> • Cooperation agreements or associations of audit firms or auditors with other professionals like lawyers, actuaries, valuation experts, etc; • Sharing of resources and costs for technology and IT purposes without otherwise forming a larger structure. 	FEE	See discussion of larger structure

40.	Larger Structure	<p>We share the opinion expressed by FEE in this respect that it would be useful to include in the explanatory material further clarification on the meaning of a "larger structure" as well as a number of examples of what would constitute (or not) a larger structure in order to enhance the practical application of the proposed definition.</p> <p>We also believe that it would be helpful to clarify whether or under which circumstances the following situations form a larger structure :</p> <ul style="list-style-type: none"> • cooperation agreements or associations of audit firms or auditors with other professionals like lawyers, actuaries, valuation experts, etc • sharing of resources and costs for technology and IT purposes without otherwise forming a larger structure 	CNCC/OEC	See discussion of larger structure
41.	Larger Structure	<p>Paragraph (a) of the definition applies to situations where firstly, a firm is ‘part of a larger structure’ and secondly, any of the criteria set out in sub-paragraphs (i), (ii) or (iii) apply. The phrase ‘larger structure’ which we believe is used to avoid a more legalistic definition, nevertheless requires either an express definition or further guidance in section 290 of the Revised Code. The lack of a definition gives rise to some uncertainty as to what is meant by or the scope of, this phrase. The lack of a precise definition or additional guidance also gives rise to the uncertainty as to whether the phrase ‘larger structure’ or ‘network’ is one and the same.</p>	MIA	See discussion of larger structure
42.	Larger Structure	<p>With respect to the use of the term “larger structure” in the definition, we believe further clarification is needed. It would be helpful to clarify that a larger structure would not have to be a legal entity or higher-level organizational structure, but could also be a contractual business arrangement or other operating affiliation that is created by management agreement of two or more firms. Such agreements could create a commonality of business interests without the firms being a part of a larger organization, e.g., a management agreement to share work in serving each other’s clients in a “brother and sister” network without a parent or higher level “umbrella group”. We suggest the Ethics Committee consider whether part A of the definition might be more readily applied if the term “larger structure” were amplified by additional wording indicating that the larger structure arises from a business arrangement creating a commonality of firm business interests.</p>	IOSCO	See discussion of larger structure

43.	Larger Structure	The definition of a network firm commences with the statement that “(a) a firm is part of a larger structure...”. The term “larger structure” is rather general and it could be clarified by adding a relevant, linked objective to the definition. This could be achieved by inserting the words “aimed at co-operation,” after “larger structure”. The definition would then commence as follows: “(a) a firm that is part of a larger structure aimed at co-operation, ...”.	Basel	See discussion of larger structure
44.	Larger Structure	Part (a) of the proposed revised definition introduces the concept of a 'larger structure'. This is, presumably, not intended to act in a restrictive way but is a necessary concept in order to word the remainder of part (a) of the definition in a clear fashion. Nevertheless, it may be preferable to use a definition that does not rely on the introduction of a new term.	ACCA	See discussion of larger structure

45.	Larger Structure	<p>We believe that the meaning of “larger structure” should be further explained and clarified to avoid any misunderstanding in the practical application.</p> <p>Besides the notion of “control” (firms controlled by the same person or group of individuals or controlling other firms), which in itself qualifies a network firm, we believe that the concept of a “larger structure” should be determined according to the following:</p> <ul style="list-style-type: none"> (a) A common management system: a common strategy, compensation based on a common wage scale, common and compulsory invoicing procedures, and a single chain of command; this common management may also include a common technical management, i.e., an authority in charge of drafting and monitoring mandatory technical policy for all firms, (b) Or through the use of a common name which is a trade name used or that could be used for marketing and commercial purposes, (c) Or through the existence of economic ties such as each firm being dependent on a long-term basis on other firms to perform its services: e.g., shared client base, shared employees, common engagements. <p>We feel that such notions as “duration” and “recurrent basis” should be explicitly addressed to qualify a network firm. For instance, sharing of staff on a one-off basis does not appear to form a basis for audit firms to be considered as network firms.</p> <p>Furthermore, we are of the opinion that the notion of cost sharing may not be relevant in most cases in the identification of a “larger structure”.</p> <p>Thus, the coexistence of the following:</p> <ul style="list-style-type: none"> - an association whose purpose is to share methodology, training courses, a documentation resource center and/or to implement quality control policies for each of its members - and the firms belonging to this association <p>does not constitute, in the absence of (a), (b) or (c) above, a “larger structure”.</p> <p>Accordingly, the last examples in paragraph 290-18 (quality control policies and procedures; technical departments; audit methodology, audit manuals or working papers; training courses and facilities) constitute the criteria of a simple technical association rather than a network.</p> <p>The attached chart illustrates such proceedings.</p>	CGCI	See discussion of larger structure
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46.	Larger Structure	<p>We believe that the meaning of “larger structure” should be further explained and clarified to avoid any misunderstanding in the practical application.</p> <p>Besides the notion of “control” (firms controlled by the same person or group of individuals or controlling other firms), which in itself qualifies a network firm, we believe that the concept of a “larger structure” should be determined according to the following:</p> <ul style="list-style-type: none"> (d) A common management system: a common strategy, compensation based on a common wage scale, common and compulsory invoicing procedures, and a single chain of command; this common management may also include a common technical management, i.e., an authority in charge of drafting and monitoring mandatory technical policy for all firms, (e) Or through the use of a common name which is a trade name used or that could be used for marketing and commercial purposes, (f) Or through the existence of economic ties such as each firm being dependent on a long-term basis on other firms to perform its services: e.g., shared client base, shared employees, common engagements. <p>We feel that such notions as “duration” and “recurrent basis” should be explicitly addressed to qualify a network firm. For instance, sharing of staff on a one-off basis does not appear to form a basis for audit firms to be considered as network firms.</p> <p>Furthermore, we are of the opinion that the notion of cost sharing may not be relevant in most cases in the identification of a “larger structure”.</p> <p>Thus, the coexistence of the following:</p> <ul style="list-style-type: none"> - an association whose purpose is to share methodology, training courses, a documentation resource center and/or to implement quality control policies for each of its members - and the firms belonging to this association <p>does not constitute, in the absence of (a), (b) or (c) above, a “larger structure”.</p> <p>Accordingly, the last examples in paragraph 290-18 (quality control policies and procedures; technical departments; audit methodology, audit manuals or working papers; training courses and facilities) constitute the criteria of a simple technical association rather than a network.</p> <p>The attached chart illustrates such proceedings.</p>	Groupe Excel	See discussion of larger structure
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47.	Overall comments on definition	<p>The Ethics Committee's rationale for the proposed revision to the definition of network firm is to address the concerns expressed by some that the existing definition was too narrow and did not appropriately consider the importance of the way firms present themselves.</p> <p>We support the Ethics Committee's objective to provide the necessary clarity regarding the nature of interests and relationships that may pose threats to independence.</p> <p>Similarly, we welcome the intent of the explanatory text to provide guidance to assist professional accountants to assess the significance of the interests and relationships that may pose a threat to independence.</p> <p>We are, nevertheless, concerned, in particular, that:</p> <ul style="list-style-type: none"> • the proposed revised definition appears to have moved away from being principles-based to a rules-based one. As a result there is lack of clarity, for example as a result of linking the word 'sharing' to the word 'costs' • there are unintended consequences of the definition of firm being unchanged and as a result there is duplication in the definition of firm and network firms • the proposed revision to the definition does not appear to take into consideration other definitions with international application • there are additional tests and inconsistencies in the explanatory text and • other IFAC pronouncements may not be consistent in the way network firm and terms that refer to similar concepts are used. 	ACCA	Overall comment on definition – each sub-point is discussed in more detailed by the respondent, accordingly each sub-point is addressed below.
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48.	Definition	<p>We recommend that you amend the definition of network firms following Section 290.19 to reflect the following:</p> <p>(a) a firm that is a member of, or affiliated with, a larger structure (i.e., another entity or group) and that:....or</p> <p>(b) an entity that controls, is controlled by, or is under common control with the firm either through operational control, significant influence with respect to operating revenues and/or profits, a direct or indirect financial interest, or other means.</p> <p>We believe that the above modification is necessary in order to include not only those firm relationships that are evidenced by legal and/or contractual arrangements but also those firm relationships that are less formal in nature yet are as operationally effective as the former.</p>	E&Y	Isolated comment – not carried further
49.	Def'n Ordering of subclasses	<p>The Proposed Revised Definition is currently subdivided in two subsection (a) and (b) of which we would recommend to reverse the order to first list (b) and then (a). We are of the opinion that the primary reason why an audit firm is to be considered a network firm is because it is an entity that controls, is controlled by, or is under common control with another firm through ownership, management or other means, currently subsection (b). Therefore, we believe that this condition sets the framework for any network and should be listed first.</p> <p>Similarly, we propose to reverse the order to current (a) (ii) and (a) (iii) as sharing profits or costs with other firms within the larger structure appears to be more important than the sharing of significant professional resources with other firms in the larger structure.</p>	FEE	See discussion under <i>Ordering of sub clauses</i>

50.	Def'n Ordering of subclasses	<p>The proposed revised definition is currently subdivided in subsections (a) and (b) of which we would recommend to reverse the order to first list (b) and then (a). We are of the opinion that the primary reason why an audit firm is to be considered a network firm is that it is an entity that controls, is controlled by, or is under common control with another firm through ownership, management or other means. As explained above, we believe that this condition sets the framework for any network and should be listed first.</p> <p>Similarly, we propose to reverse the order of current (a) (ii) and (a) (iii), as the sharing of profits or costs with other firms within the larger structure seems more important than the sharing of significant professional resources with other firms in the larger structure.</p>	CGCI	See discussion under <i>Ordering of sub clauses</i>
51.	Def'n Ordering of subclasses	<p>The proposed revised definition is currently subdivided in subsections (a) and (b) of which we would recommend to reverse the order to first list (b) and then (a). We are of the opinion that the primary reason why an audit firm is to be considered a network firm is that it is an entity that controls, is controlled by, or is under common control with another firm through ownership, management or other means. As explained above, we believe that this condition sets the framework for any network and should be listed first.</p> <p>Similarly, we propose to reverse the order of current (a) (ii) and (a) (iii), as the sharing of profits or costs with other firms within the larger structure seems more important than the sharing of significant professional resources with other firms in the larger structure.</p>	Groupe Excel	See discussion under <i>Ordering of sub clauses</i>

52.	Def'n Ordering of subclasses	<p>The proposed revised definition is currently subdivided in two subsection (a) and (b) of which we would recommend to reverse the order to first list (b) and then (a). We are of the opinion that the primary reason why an audit firm is to be considered a network firm is because it is an entity that controls, is controlled by, or is under common control with another firm through ownership, management or other means, currently subsection (b). Therefore, we believe that this condition sets the framework for any network and should be listed first.</p> <p>Similarly, we propose to reverse the order to current (a) (ii) and (a) (iii) as sharing profits or costs with other firms within the larger structure appears to be more important than the sharing of significant professional resources with other firms in the larger structure.</p>	CNCC/OEC	See discussion under <i>Ordering of sub clauses</i>
53.	Def'n Ordering of subclasses	We would like to suggest that sub-sections (ii) and (iii) of part (a) of the current definition be reversed in order to best depict their relative importance (our proposed definition below includes this reversal).	IDW	See discussion under <i>Ordering of sub clauses</i>
54.	Proposed revised definiton	<p>Based on our comments above, we suggest that the definition be amended to read as follows:</p> <p>“(a) a firm that uses a name in its firm name that is designed to enable that firm to operate under a common brand name with other firms; (b) a firm that is part of a larger structure in which the firm shares, on an ongoing basis, with other firms within the larger structure (i) profits and losses or significant costs in relation to professional activities, or (ii) significant professional resources; or (c) an entity that controls, is controlled by, or is under common control with, the firm through ownership, management or other means.”</p> <p>In our opinion, the effect of any subsequent amendments to, or deletions from, the explanatory material on the application of the definition must be carefully considered.</p>	IDW	See discussion under <i>Ordering of sub clauses</i>

55.	Network relationship	<p>The revised Code of Ethics for Professional Accountants issued in June 2005, together and with its predecessor, include as a defined term "Network firm". The definition, made in terms of ownership, management and control, is, broadly, comparable with those requiring the consolidation of respective financial statements. Consequently a network relationship is asserted only in limited circumstances; the inappropriate juxtaposition of the conflicting terms "network" and "firm" does not have particular adverse implications for the legal entities in question.</p> <p>With the intention to broaden very substantially the intended scope of an imputed network relationship the inappropriate continuation of a composite term "network firm" serves to perpetuate the confusion between a relationship term and a legal entity term and will carry significantly greater gratuitous liability risk for firms than was previously the case.</p> <p>It continues to be our view that a network relationship should be defined, rather than the creation of an artificial entity unfounded in either law or regulation in any jurisdiction, but with elements subject to both law and regulation in a range of jurisdictions. This minor change in approach could readily be achieved by accepting the current definition of a "firm" for this purpose. A "network relationship" would then be defined in terms of associations between two or more firms exhibiting the characteristics selected for the proposed expanded scope. This should mean that implications of the legal entity are less open to degradation by individuals seeking to assert that entities in a wide range of jurisdictions are all available for legal action in any legal jurisdiction, resulting in firms being brought into actions over matters with which they were not involved and, consequently incurring significant costs and inconvenience in having themselves removed from such actions.</p> <p style="text-align: right;">Continued</p>	Moore Stephens	Isolated comment – not carried further
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56.	Network relationship	<p>It would then follow that firms in a network relationship comprise a "network", and networks would comprise "network member firms". This precision in terminology would enable obligations between network member firms to be established to the extent considered necessary to address perceived issues. It would also facilitate a proper analysis of the common situation where there are jurisdictional barriers in criminal or civil law, or professional regulation, precluding the provision of the information between parties outside the direct client relationship that would be necessary to meet the obligations implicit in the IFAC Code of Ethics across the expanded scope of a network relationship.</p> <p>Such proper analysis is conspicuously absent from the resources presently provided within the Exposure Draft, or elsewhere, and should cover situations both (a) where there is no entitlement to receive the information across a network and (b) where there are explicit legal or regulatory prohibitions on the exchange of such information. A particular issue could arise where a firm provides, on a pragmatic basis, information to meet these proposed obligations. The consequence of this would be either to concede that the entities involved are so connected as to permit the provision of the information or that the firm providing the information has acted in breach of applicable law or regulation. The first would negate any possibility of the firm extracting itself from vexatious litigation, while the second would leave it open to immediate legal or regulatory consequences. In the absence of proper resolution of the issues arising from the restrictions on information exchange, the expectations created in many constituencies by the proposed substantial expansion of the network definition are unlikely to be met. There is also the increased probability of inconsistencies in interpretation, and application, between groupings of professional firms.</p>	Moore Stephens	Isolated comment – not carried further
57.	Interaction of Network firm Def'n & Firm Def'n	<p>The proposed definition of network firm includes, inter alia "an entity that controls, is controlled by...;the firm...". The existing definition of firm includes "(b) an entity that controls such parties; and (c) an entity controlled by such parties." The definitions seem to overlap, which could cause problems in view of the differing requirements for firms and network firms.</p>	CCAB	See discussion of interaction of definitions

58.	Interaction of Network Firm def'n & Firm Def'n	<p>We believe that, as a result of the definition of firm being unchanged, there are unintended consequences. In the extant definition of network firm some entities are not included because of overlap with the definition of firm. Thus an entity is a network firm if under common control; but part of the firm if it controls or is controlled by the firm (the latter use of the word 'firm' being understood to refer to that part of the firm that is not the entity under consideration). Part (b) of the proposed definition includes as a network firm an entity that controls or is controlled by the firm. There is, therefore, some duplication in the definitions.</p> <p>It is, however, not simply the case that the definition of network firm also includes some entities that would be part of the firm according to that definition. This is because the definition of network firm itself uses the word 'firm'. It is important to analyse whether the word 'firm' in the definition of network firm includes or excludes the entities that would reasonably be included.</p> <p>If the word 'firm' in the definition of network firm is intended to take a narrow meaning of the word 'firm' in the definition of firm (as it is used in order to test whether entities that control it or are controlled by it are also included in the definition of firm), this should be contrasted with the wider meaning of the word 'firm' after such controlling or controlled entities have in effect been consolidated.</p> <p>Under the narrow interpretation, a controlling entity would be included within the definition of network firm. The controlling entity would also be included within the definition of firm. Consequently, in such circumstances, network firm will include firm.</p> <p>Under the wider interpretation, the inclusion of controlling or controlled entities in the definition of firm removes the need for the wording in part (b) of the definition as it is not logically possible for there to be controlling or controlled entities that are different, (this follows irrespective of whether one considers the narrow or wider interpretation). Had the definition of firm included some limitation on the proximity of control, such that control had to be direct rather than indirect, this might not have been the case.</p>	ACCA	See discussion of interaction of definitions
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59.	Interaction of Network Firm def'n & Firm Def'n	It is tempting to suggest, therefore, that part (b) of the proposed definition is incorrect. The wording is redundant where a wider interpretation of firm is appropriate and inadvisable where the narrower interpretation applies, as an entity should not be both part of the firm and network firm simultaneously; this is because, section 290 requires a different independence provisions to be applied to network firms.	ACCA	See discussion of interaction of definitions
60.	Principles-based definition	<p>On a cautionary note, we are concerned that there is no equivalent test to that in the existing definition of what a reasonable and informed third party, having knowledge of all relevant information would reasonably conclude. As a result the definition appears to have moved from being principles-based to a rules-based one. For the principles-based approach to be robust, it should not be undermined by the proliferation of detailed underlying rules.</p> <p>We agree there are judgemental factors still in the definition, for example to what extent professional resources have to be shared for that sharing to be considered to be significant. There are, however, absolute rules - any sharing of profits or costs and any use in whole or in part of a name. It is important, therefore, to understand how these absolute rules would apply to see whether the stated intention of the change is achieved.</p> <p>By way of an example, if we consider firms in different countries which have different names but market themselves as being independent firms that are part of the XYZ International network. One of the firms would be a network firm in relation to the other if any costs were shared. For example, a subscription to the international organisation. Some might argue that this is not a sharing of costs in the same way as is understood in relation to profits in an industry where a partnership structure is common. For the avoidance of doubt, it may be helpful to reword the proposed definition to avoid connecting the word 'sharing' to the word 'costs'. The definition could refer to incurring costs in connection with being part of a larger structure. Again, for the avoidance of doubt, the word 'profits' should be replaced by 'profits or losses'.</p>	ACCA	Isolated comment – not carried further

61.	Convergence	<p>Audit quality is critical to the effective operation of the capital markets; however, market needs vary between investors in listed and non-listed entities. Maintaining objectivity is critical in ensuring audit quality and independence is an important element in retaining objectivity.</p> <p>The framework of threats and safeguards promoted by IFAC is sound public policy. However, we are concerned that as member bodies of IFAC adopt the new definition of network firm, inconsistencies in applying the IFAC framework of threats and safeguards will have unintended consequences. Specifically, we anticipate that the independence rules issued by a number of member bodies and other regulators, such as the Accounting Practices Board in the United Kingdom and the American Institute of Certified Public Accountants, do not make the same distinction that IFAC does between the independence requirements applicable to audit versus non-audit assurance engagements. The implication is that international accounting firms would need to develop controls to address threats to independence for non-audit assurance engagements across all network firms. The introduction of such controls would include:</p> <ol style="list-style-type: none"> 1. Developing systems and procedures for network firms to maintain lists of non-audit assurance engagement relationships and to communicate these lists to all network firms (or introduce systems and procedures to help ensure that all proposals for prohibited non-assurance services to international prospects first check with network firms to verify independence). 2. Developing monitoring procedures to ensure compliance with policies established in connection with (1) above. 3. Recruiting and training of personnel within member firms as well as at the global organization to communicate these changes in policy and procedures to member firms personnel and to execute monitoring responsibilities. 4. Developing policies and procedures to be followed in situations where threats to independence are identified or where inadvertent violations of policy occur. <p>The time and effort to put in place the controls described above is not proportionate to the relative independence threat. Therefore, we encourage IFAC to stress the importance in the uniformity and consistent application of the basic IFAC threats and safeguards requirements by the member bodies.</p>	Grant Thornton	<p>Network firms are required to be independent from audit clients – for other assurance engagements consideration is to be given to any threats that the firm “has reason to believe may be created by network firm interests and relationships.”</p> <p>See discussion on effective date</p>
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62.	Differentiate between listed & non-listed	<p>Paragraph 290.14 of the Code of Ethics states “...for financial statement audit clients the members of the assurance team, the firm and network firms are required to be independent of the financial statement audit client.” The likelihood of a network firm investing in a non-listed audit client would appear to be small. However, paragraph 290.113 of the Code of Ethics indicates that in the case of financial statement audit clients, a financial interest by a firm or network firm in the audit client results in a self-interest threat “so significant no safeguard could reduce the threat to an acceptable level”.</p> <p>We are concerned that the new network firm definition will, by virtue of paragraph 290.113, require a major investment in processes, systems and people similar to those mentioned above to address a relatively minor threat. Grant Thornton member firms collectively provide audit services to less than 2,000 listed clients but have more than 100 times this number of unlisted audit clients. Modifying paragraph 290.113 to differentiate between listed and unlisted audit clients would focus effort and cost where it is in the best public interest. We would also recommend that there be further development of guidance surrounding independence threats and safeguards relating to unlisted audit clients.</p>	Grant Thornton	The Code does distinguish between listed and non-listed audit client but only with respect to non-audit services. For shareholdings of non-listed audit clients it does not seem onerous to inquire whether any network firms are shareholders. No further action necessary.
63.	All firms within a network must be independent	<p>Additionally, we believe the Code of Ethics, when amended by the ED, may not clearly indicate that all firms within a network must be independent of each other’s financial statement audit clients. Accordingly, we recommend that the ED be clarified to specifically state this requirement</p>	E&Y	<p>Existing 290.14 (which would be renumbered) states “...for financial statement audit clients ... network firms are required to be independent of the financial statement audit client.”</p> <p>For further action necessary.</p>
64.	All firms in audit need to be independent	<p>We also think it would be helpful to state somewhere in Section 290 that the issue of identifying whether a group of firms constitutes a “network” for which <i>independence is required of every firm and its affiliates from all audit clients of all firms in the network</i> is a separate issue from the requirement that <i>all firms that participate in the audit of a particular group entity must be independent of that audited group entity</i>. (Firms participating in the same audit must all be independent of the audited entity regardless of whether they are part of a firm network.)</p>	IOSCO	See discussion of all firms need to be independent.

65.	Linkage between definition and background material	<p>The use of the “network firm” definition in the Ethics Code is relevant when judging whether it should be necessary for all audit firms and affiliates (including non-audit firms) in a network to be <i>independent of all of each others’ audit clients</i>. This is a much broader and more complex question than the network firm issue in a single audit as it involves both multiple firms and multiple audits and can reach out to involve affiliates of an audit firm even if that firm does not participate in a particular audit.</p> <p>In our discussions about the new definition, some members initially had a concern that the new definition might capture some firm networks where a closer examination identified that the network did not share client-related work and would not appear to have any effect on a firm’s objectivity or a public perception of independence. As we examined this issue further, we concluded that the definition in the ED was sound for use as a “presumptive definition,” particularly as it is further explained in paragraphs 290.14 to 290.19. We suggest that a way be found to link the discussion of network firms in paragraphs 290.14 to 290.19 more closely with the presentation of the definition in Section 290. We found the discussion in these paragraphs helpful in amplifying the intent of the definition.</p>	IOSCO	See discussion of <i>Linkage to definition</i>
66.	290.6	<p>We recommend that paragraph 290.6 be expanded to reflect the role a public accountant plays with respect to assertion-based assurance engagements. As the previous 290.5 paragraph states that all assurance engagements involve three separate parties (a public accountant, a responsible party and intended users), then reference should be made to the role of a public accountant within the context of paragraph 290.6.</p> <p>In order to clarify paragraph 290.6, it is suggested that the words “<i>that is verified by the public accountant</i>” be included just before the following sentence end: <i>that is made available to the intended users</i> “.</p>	AG of Vic	To be considered by the Accountants in Government TF – matter does not relate to the definition of network firm

67.	290.14	In paragraph 290.14, the term “correspondent firm” is introduced but is left undefined. It is not clear to us what is meant by “created only to facilitate referral of work”. Further, it is not clear to us what would be involved in such referral of work and whether the Ethics Committee believes that “correspondent firms” do or do not involve a commonality of business interests sufficient to create a network, or would it depend upon the terms on which the work is referred? In general, we believe any term used in the Code that is considered significant should be included in the definitions to avoid confusion about what is intended.	IOSCO	See discussion of correspondent firm
68.	290.14	At paragraph 290. 14, the spectrum of association is presented as being two-dimensional. In reality, association is multi-dimensional and can relate to such matters as identity, profit-sharing, degree of control, quality control, methodology and linguistic convergence. Also the term of ‘correspondence firm’ is irrelevant as it is only used by certain large networks. It may well be more important globally to examine the relationship between audit firms and tax firms that are part of the same larger structure. Presenting as one end of the spectrum firms operating under common brand name is paying too much attention to appearance. Control is by far the most important factor.	ACCA	See discussion of correspondent firm
69.	290.15	In paragraph 290.15, in the first sentence, we suggest that the phrase “is something to be judged in the circumstances” be revised to state “is a matter to be determined in light of the specific facts and circumstances” or otherwise convey the basis for the judgment. This would be consistent with the second sentence of that paragraph.	IOSCO	Change proposed
70.	290.15	Paragraph 290.15, reintroduces the judgemental test that was in the existing definition. Unfortunately, the proposed definition only requires judgment in relation to the degree of significance of sharing of professional resources. This is much narrower than a judgment about the ‘degree of association’. There is, therefore, inconsistency between the proposed definition and this paragraph that should be eliminated. We are also concerned that paragraph 290.15 is loosely worded. We do not see why it refers to ‘factual circumstances’ rather than just ‘facts’ or just ‘circumstances’. Is this intended to exclude consideration of circumstances that are not factual? Whatever these may be?	ACCA	To be considered if 8 th directive wording is not used Reference to factual circumstances is consistent with 8 th directive language

71.	290.15	Specific parts of the explanatory material in 290.14 – 290.19 are essential to the interpretation of the definition. As noted, we agree that when a firm practices under essentially the same name as other firms within the larger structure, it would ordinarily be considered to belong to a network as stated in 290.16. The example in the continuation of this paragraph depicting circumstances in which this is not the case underlines that the degree of association is to be judged in the circumstances as stated in 290.15 and provides essential guidance as to the application of sub-section (a) (i) of the current definition in practice. This guidance would benefit from a discussion as to why the example did not meet the criteria for defining the relationship as a network.	IDW	Isolated comment – not taken further
72.	290.15	Paragraph 290.15 provides useful guidance about “[w]hether the degree of association is sufficient to create a network that would require firms in the network to be independent of each other’s financial statement audit clients”. It would helpful to add to Section 290 of the Code of Ethics an example of where the “factual circumstances available” referred to in paragraph 290.15 would indicate that associated firms are part of a network, even if such a conclusion may not be obvious to the firms themselves.	Basel	Paragraphs 290.16, 18 and 19 provide additional guidance in this area.
73.	290.15	Consistent with the approach adopted in the IFAC Code, the guidance in proposed paragraphs 290.14 – 290.19 on the degree of association which is sufficient to create a network that would require firms in the network to be independent of each other’s financial statement audit clients, outlines a conceptual framework to use in making this assessment. Given the complexity and variety of relationships involved in network firms, it is appropriate for judgment to be applied in making this assessment. However, it is not clear as to who is required to make this judgment. It would clearly be inappropriate for individual audit partners to make their own differing judgments as to whether another firm is part of the network or not. The APB recommends that paragraph 290.15 should specify that this assessment is made once at a global firm level and the resulting list of who is included in the network should then be clearly communicated throughout the network (and to other associated firms not considered to be part of the network).	APB	Change proposed

74.	290.16	<p>Under the criterion (a) (i) of the proposed definition, a network firm is a firm that is part of a larger structure and that uses a name in its firm that is common to the larger structure. While we agree with the principle that firms sharing a common name constitute a network, we believe that certain improvements of the definition as well as the related guidance in paragraph 290.16 should be considered.</p> <p>First, we believe that the use of a common brand name represents a threat to independence in appearance, even if the firm is not part of a larger structure, because in effect the firm is “holding out” that there is such a larger structure regardless of whether one exists. For this reason, we suggest not subjecting the criterion “common brand name” to the precondition of being part of a larger structure.</p> <p>Second, the phrase “use a name...that is common” appears to be too vague, as it might be understood by some as treating as a network even those firms that do not have any relationships with one another with the exception that they only incidentally share the same name. While it follows from paragraph 290.16 that in such circumstances no network exists, the definition should nevertheless convey the idea that the crucial factor is the intentional use of a common name in the marketplace (that is, making use of branding). In relation to these first two points we refer to our amended definition below.</p>	IDW	<p>Reference to being part of a larger structure is needed because without such a reference two unrelated firms that just happen to be practicing under a common name might be captured as network firms. Not taken further.</p>
75.	290.16	<p>Third, we suggest that additional guidance explicitly state the reasons operating under a common brand name may create threats to the independence in appearance of firms using that brand name. Briefly stated, in our view, the independence threat is caused by the fact that network members are subject to a common reputation risk, which may cause dysfunctional effects through lack of independence. For example, one firm acting as auditor may have a disincentive to uncover mistakes of another firm that uses the same brand and acts as advisor of the same client, because in this case the firm would damage its own brand.</p>		<p>Isolated comment – not taken further</p>

76.	290.16	Paragraph 290.16 refers to ‘substantially the same firm name’. The proposed revised definition does not refer to this phrase and so the explanatory text appears to require a different test. This is inappropriate. Once that part of the definition relating to name is satisfied, it is not appropriate to then require consideration of the facts that might indicate otherwise. This paragraph exposes the need to remain principles-based as it introduces a further rule (giving exemptions) where the application of the primary rule results in circumstances which are inappropriate. We are also concerned that the wording in paragraph 290.16 could be used by firms to justify not being network firms because they make appropriate disclosure.	ACCA	See discussion under <i>Use of a common name</i>
77.	290.16	We notice an inconsistency between the definition, which effectively states that the use of a common name means that a firm is to be regarded as a network firm regardless of other facts, and 290.16, which states that the facts may prevail over appearance. We believe the EU definition, which links the name issue to co-operation, is preferable in this respect and would support the analysis in 290.16.	CCAB	See discussion under <i>Use of a common name</i>
78.	290.16	<p>It has been noted by a number of people that the effect of the definition and explanatory paragraphs is that in groups of firms where some firms use the ‘network’ name and others do not, then the former will be presumed to be part of the network for these purposes, whereas the latter may not be. The definition states that the use of a common name means that a firm is to be regarded as a network firm regardless of other facts. However, 290.16 indicates otherwise and we believe in this respect the EU definition is preferable, as it supports the explanation in 290.16.</p> <p>The perception aspect is rightly qualified in 290.15 by limiting it to reasonable and informed third parties. However, 290.16 considers at some length, situations where practices using the same name should be considered as networks, but there is no similar discussion of practices in groups that do not use the same name. This leads to an implication that perception should prevail over facts. Careful reading of 290.16 (though not of the definition) indicates that this is not IFAC’s intention but it might be helpful to add a short comment confirming that firms may be part of a network where the facts suggest, even if they use different names.</p>	ICAEW	See discussion under <i>Use of a common name</i>

79.	290.16	<p>We also note that there is an inconsistency between, on the one hand, the proposed IFAC definition of a network (which effectively states that the use of a common name means that a firm is to be regarded as a network firm regardless of other facts) and on the other hand, the content of paragraph 290.16 (which states that the substance of any given set of circumstances should prevail over the form adopted by the firm). We believe the EU definition, which links the name issue to co-operation, is preferable in this respect and would support the substance of the analysis contained in paragraph 290.16, which we believe to be the key requirement.</p> <p>We appreciate the sentiments behind the requirement for associations that are not networks to clarify that fact. However, we are concerned at the suggestion that they should explicitly use words to the effect of "an independent firm associated with...": we believe that that suggestion will metamorphose into a definitive rule, with the result that the presumption is created that a network firm exists unless that strap-line is applied. While we agree that in examples of that kind, appearance is doubtless relevant, consideration of the underlying facts would also be relevant and necessary. Therefore, we believe it would be useful to give the last sentence of 290.17 the character of a recommendation rather than an obligation and to clarify that ultimately it is the 'reasonable and informed tests' in 290.15 that should prevail.</p>	ICAS	See discussion under <i>Use of a common name</i>
80.	290.16	<p>In our view, it would be helpful to emphasize the significance of a firm using the larger network name as part of its own firm name in signing its audit opinions – for example, to stipulate that if the firm includes all or part of the network name in its firm name, or adds a statement regarding its network membership to the firm name in signing its audit opinions, a network firm relationship should be judged to exist. (We recognize that the definition part (a) (i) mentions “uses a name in its firm name that is common to the larger structure” but believe this could be made even more explicit in the accompanying text in paragraph 290.16)</p> <p>Some members have also suggested that if any examples are used, there should be multiple examples illustrating cases of “what is” as well as “what is not” intended to be considered a network firm for independence purposes. We believe the Code should also emphasize that any examples are only selected illustrations are not all-inclusive and the specific facts and circumstances prevailing in any particular case must always be considered.</p>	IOSCO	<p>See discussion under <i>Use of a common name</i></p> <p>This point is already mentioned in the Code – in paragraphs 200.1, 290.10 and again in 290.100 – additional emphasis is not considered necessary.</p>

81.	290.16	We recommend that paragraph 290.16 be amended for the inclusion of the word “ <i>of</i> ” at the following location, in order for the example provided to grammatically flow: <i>“As an example the component may continue the use f the name, or an element of the name, of the firm though they would otherwise be unconnected.</i>	AG of Vic	Isolated comment – not carried further
82.	290.16	Paragraph 290.16 could be made more precise by adding the word “normally” to the last part of the first sentence. This part of the sentence would then read as follows: “it would normally be considered to belong to a network”.	Basel	Proposed other changes to this paragraph address this point by making it clear that the reason the firms would not be considered network firms is that the larger structure is not one that is aimed at co-operation.

83.	290.16	<p>With regard to the specifics being proposed, we question the initial presumption of paragraph 290.16 that a name which is “substantially the same” creates in the users’ minds a need for independence, particularly when it is argued that by clearly stating, “an independent firm” and implied network link can be ignored.</p> <p>Any effective guidance must be transparent, it should not require knowledge of the extent to which the members of the a network share resources or systems.</p> <p>To give a very practical example; all of our members are required to state clearly that they are “an independent member of Baker Tilly International”. However, some members use the Baker Tilly as part of their of their name. Are we to assume that those members of the network using the name have to establish independence, while those who do not, would not have to? Further to complicate this evaluation some members only use the name for certain aspects of their work, so if their audit opinion was in the name of a firm not including the Baker Tilly name what would happen?</p> <p>We are aware that the Code is based on principles that should be applied in the spirit of the guidance, however we fail to understand the principles that are being proposed in the draft. We believe that the approach proposed IFAC lacks logic and ails to resolve the current confusion.</p> <p>We would like to propose an alternative approach. We suggest that where members of a network state clearly that they are independent if of each other, the independence requirements should not be based on the following, which allows for the recognition of safeguards to eliminate the threat to independence:</p> <p>No member of a network should provide prohibited services to an entity within the group on which that same member provides an audit opinion, on which the parent auditor is going to place reliance in forming their opinion on the group financial statements.</p> <p>Where a member of the network provides prohibited services to an entity within the group, that work must be subject to an independent audit; i.e. whatever firm is giving the audit opinion on that entity cannot rely on the work done by that firm to any greater extent than if it had not been done by a member of the network.</p> <p>We believe this guidance would than be consistent with the approach proposed by IFAC in respect to group audits.</p>	Baker Tilly Barnes	<p>Isolated comment.</p> <p>The group audits ED establishes standards for the type of work that should be performed by the group auditor and other auditors. The concepts are different from independence.</p> <p>Not carried further.</p>
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84.	290.17	We note and understand the requirement for associations that are not networks to clarify that fact. However, there is a danger that the suggestion that they should state words to the effect of "an independent firm associated with..." will be treated as a hard and fast rule so that there ends up being a presumption that they are network firms unless that comment is stated. While in such circumstances, appearance is relevant, the actual facts would also be relevant. We believe it would be useful to make the last sentence of 290.17 a suggestion rather than a requirement and to clarify that ultimately it is the reasonable and informed tests in 290.15 that prevails.	CCAB	See discussion under <i>Disclosure of being part of an association</i>
85.	290.17	Proposed paragraph 290.17 is very useful in highlighting that there are associations of firms that would not fall to be treated as network firms. However, as written, the paragraph could be interpreted as implying that unless stated otherwise, any reference to an association results in a presumption of a network unless stated otherwise. We believe it would be useful to make the last sentence of 290.17 a suggestion rather than a requirement.	ICAEW	See discussion under <i>Disclosure of being part of an association</i>
86.	290.17	In paragraph 290.17, a situation is discussed whereby <i>"a firm that does not meet the criteria of a network firm may describe itself as being a member of an association of firms (for example in its stationery or promotional material). This description may create the appearance that the firm is part of a larger structure. To avoid such an appearance, such a firm should clearly describe the nature of its membership of the association, for example, by stating on its stationery or promotional material that it is "an independent firm associated with XYZ Association of Accounting Firms".</i> We believe that such notification may be appropriate where the membership or association relates to a professional trade or self regulatory organization, but may well lead to abuse or confusion where the relationship exists between or among commercial or professional firms or entities. We believe the above quoted example should be clarified to further restrict the circumstances where references may be made to other organizations in promotional materials	E&Y	See discussion under <i>Disclosure of being part of an association</i>

87.	290.17	Paragraph 290.17 requires an independent firm that does not meet the criteria of a network firm, but is a member of an association of firms to “clearly describe the nature of its membership of the association” for example on its stationery or promotional material. However, the disclosure example at the end of the paragraph is ambiguous when it states that the firm is “an independent firm associated with XYZ Association of Accounting Firms”. As explained in paragraph 290.9, the use of the word “independence” on its own may create misunderstandings. Therefore it is suggested that this paragraph elaborate on the context in which the term “independent” is used and provide additional guidance on other acceptable terminology for clearly describing the nature of a firm’s association membership.	Basel	See discussion under <i>Disclosure of being part of an association</i>
88.	290.17	<p>However, we take exception to the language contained in Section 290.17 and recommend that this paragraph be deleted in its entirety.</p> <p>We believe the language suggested in 290.17 requiring firms describing themselves as members of an association to state specifically that they are an "independent firm associated with XYZ Association of Accounting Firms" so it doesn't create an appearance of the firm being part of a larger structure is unnecessary given the language already proposed for defining a network firm. Such language puts smaller firms that are members of associations at a competitive disadvantage if other language in the marketplaces of their respective countries would be more appropriate and helpful to the respective firm. In addition, this language may not be the most appropriate legally for a firm in its respective country or other jurisdiction. For example, our members in Australia, with advice from legal counsel, state they are "autonomous and separately accountable" members of our Association. If Section 290.17 is retained, we highly recommend that firms be allowed to state they are independent members of an association in the language that is most appropriate for their country or other jurisdiction.</p>	PCAAI	See discussion under <i>Disclosure of being part of an association</i>

89.	290.17	We consider that the draft paragraph 290.17 to be significantly unhelpful in the interpretation of the proposed requirements. In reality, members of many networks have long characterised themselves in such terms as part of their risk management strategies and have not promoted themselves as entities with common worldwide capabilities. The inclusion of this paragraph may be interpreted as indicating that the continuation of such a designation, or close equivalent, negates the expanded network definition by giving a proper recognition to the implications of the word "independent" that would not be consistent with the remainder of the Exposure Draft. Accordingly it should be removed from the draft.	Moore Stephens	See discussion under <i>Disclosure of being part of an association</i>
90.	290.17	There is some inconsistency in paragraph 290. 17 in that the second half of it seems to be unconnected to the first half. If the firm describes itself as being part of a network firm, either it is part of a network or it is doing so in a fraudulent way. For example, if ABC firm describes itself as part of XYZ International organisation but it has absolutely no connection with that organisation. In such a situation, the remainder of this paragraph is hardly likely to encourage it to make disclosures in its own stationery. It is our understanding that firms that wish to describe themselves as ‘an independent firm associated with XYZ association of accounting firms’ pay for the privilege. They, therefore, share costs and are considered to be a network firm. There is no ‘get out’. This paragraph should be deleted.	ACCA	See discussion under <i>Disclosure of being part of an association</i>

91.	290.17	<p>In considering the proposed Code definition, we discussed examples of situations in which firms may be part of an association of firms that does not create a commonality of business interests among the participants but rather exists to promote adherence to high quality professional standards and to advertise this to the public. We understand that member firms which are part of such associations need not be required to maintain independence from all of each other's audit clients solely because they belong to the same professional association. Paragraph 290.17 states that a firm that describes itself as a member of an association but "does not meet the criteria of a network firm" should clearly describe the nature of its membership of the association. The paragraph suggests as an example the descriptor "an independent firm associated with XYZ Association of Accounting Firms". We believe the Ethics Committee's intent was to illustrate the scoping out of "professional associations" that do not constitute networks. We are concerned, however, that the illustrative language chosen is similar to the language used today by some major global accounting firms that clearly have common business interests and should be considered network firms. We ask that this language be clarified to avoid any implication that major global accounting firm networks fall outside the network firm definition.</p>	IOSCO	See discussion under <i>Disclosure of being part of an association</i>
92.	290.18	<p>In paragraph 290.18, the words 'nature of the relationship thereby established' are inappropriate. The intent is to consider whether a relationship is established such that firms are network firms. In considering the significance of sharing of professional resources one has to consider the nature of the resources shared and the extent of that sharing in order to form a judgment on significance. For example, sharing resources unrelated to an assurance activity is likely to be less significant than one that is so related. Sharing resources that will amount to a material portion of the firm's resources are more likely to be significant than if the resources are much less.</p> <p>There is no natural order to the list noted in paragraph 290.18. It is normal in explanatory material to give an indication as to which factors are the more significant.</p>	ACCA	<p>Change proposed to align introduction with paragraph 290.16</p> <p>Isolated comment – not taken further</p>

93.	290.18	<p>Paragraph 290.18 gives examples of professional resources that firms may share. The first example is “Common systems that share information such as client data, billing and time recording”. It is not clear how to interpret “share information” in this example. Does it mean that one firm would have access to client data, billing, and time records for a client of another firm? If so, this would be a shared professional resource that should be considered in determining whether the shared resources are significant. However, if the common systems simply compile client data, billing, and time records, but a firm only has access to the information relating to its own clients and not to other firms’ clients, then it would not be appropriate to consider the common systems to be a shared professional resource. The second sentence of paragraph 290.19 mentions the exchange of client information in the context of determining whether shared resources would be considered significant. Thus, the first example in paragraph 290.18 would be clearer if it were revised to read “Common systems that enable firms to exchange information such as client data, billing and time recording.”</p> <p>In general the terminology used in the examples of paragraph 290.18 is not clear in all respects as the preceding comment illustrates. For example, the exact meaning of the term “technical departments” should be explained as it is not defined elsewhere in the Code of Ethics.</p>	Basel	Change proposed
94.	290.18	<p>The explanatory material in paragraph 290.18 and 290.19 refers to the "nature of the relationship" and to the "regular exchange of people or information". But the last examples in paragraph 290-18 (quality control policies and procedures ; technical departments ; audit methodology, audit manuals or working papers ; training courses and facilities) could perfectly constitute the criteria of a simple technical association and not of a network.</p> <p>It would hence be convenient to specify that the criteria in paragraph 290-18 are presented in order of importance.</p>	CNCC/OEC	Proposal to align language with EU 8 th directive wording

95.	290.19	<p>Paragraph 290.19 is unlikely to be used in practice. If no tests of significance are used elsewhere in the definition, all firms that would be considered under it will already have been classified as network firms.</p> <p>Paragraph 290.19 again introduces the term 'factual circumstance'. In particular the use of the word 'available' implies that there are some factual circumstances that are 'hidden' in some way. We assume that this is not the intent and perhaps is a consequence of a 'misunderstanding' in the use of the third-party viewpoint.</p> <p>Similarly, paragraph 290.19 strays into referring to using the term 'Association for promotional purposes'. This might be relevant to an overall consideration as was made in the existing definition, but paragraph 290.19 is merely considering the significance of sharing of professional resources.</p>	ACCA	See discussion under <i>Sharing of significant professional resources</i>
96.	290.19	<p>The third sentence of paragraph 290.19 states that “[t]here is little difference in practice between a group of firms combining to develop methodologies, and a number of firms independently purchasing proprietary audit methodology from a commercial developer and supplier”. When firms independently purchase proprietary audit methodology, none of the firms had a role in developing the methodology. In contrast, when a group of firms combines to develop methodologies, each is providing input to the development process. We believe there is a significant difference between these two situations and therefore recommend that the third sentence be deleted from the paragraph. The fourth sentence of the paragraph (“The same may well apply to common training endeavour”.) would then also need to be deleted.</p> <p>Although the guidance offered in Section 290.19 is helpful in concluding whether the professional resources shared are significant, it is not always clear how the guidance should be applied in some of the other examples mentioned in paragraph 290.18. Therefore, expanding the guidance on evaluating the significance of shared professional resources would be helpful.</p>	Basel	See discussion under <i>Sharing of significant professional resources</i>

97.	290.19	<p>The examples indicated in paragraph 290-19 are too obvious. It would be better to give more examples showing the complexity of the difference between network and technical associations.</p> <p>Finally, we are of the opinion that notions such as: duration, or recurrent basis should be explicitly addressed in those two paragraphs [290.18 and 290.19]. Sharing of cost for instance on a one-off basis, does not appear to form a basis for audit firms to be considered as network firms.</p>	CNCC/OEC	Proposal to align language to EU 8 th directive wording
98.	290.20 (New section)	<p>With respect to the issue of control, a new Section 290.20 would be added. The additional commentary should state “We are concerned that firms could avoid becoming a part of a network by the avoidance of control through the use of certain parties, other than defined immediate family or close family members, as the owners of record of the associated or affiliated firm(s). Accordingly, we suggest that the definition of a network firm include those situations where a firm (or its network) exerts significant influence over another firm or firms.</p>	E&Y	Isolated comment – this would extend the definition of a network firm beyond the 8 th directive. No further action taken

99.	Other	<p>In our view, it is of overriding importance that the Code of Ethics, the international standard on quality control and engagement standards, such as international standards on auditing, are consistent in the way network firm and terms that refer to similar concepts are used.</p> <p>In essence, firms that market themselves as being part of a network should not escape the obligations to independence which that implies. Conversely, ‘near membership’ of a network cannot be used by a firm as justification for reliance on the network or quality control and hence the ability to place reliance on the work of a network firm in connection with the audit of group financial statements.</p>	ACCA	<p>The group audits ED defines a related auditor as one an auditor from the group auditor’s firm or from a network firm who operates under, and complies with, common monitoring policies and procedures as provided by paragraph 87 of ISQC1. Therefore, the group audit definition is, appropriately, a sub-set of the independence definition – i.e. all related auditors would be network firms but not all network firms would be related auditors. The proposed text of changes to network firms will be sent to the IAASB before the February IESBA meeting to ensure that IAASB is comfortable with the proposal.</p>
100.	Other	<p>We note that the current definition of “network firm” in the IFAC Code of Ethics also appears in the IAASB’s International Auditing and Assurance pronouncement, in the Glossary of Terms and in the definitions contained in ISQC1. We presume that the intention of the Ethics Committee is that the revised definition will be introduced into there IAASB pronouncements by way of conforming changes made by the IAASB.</p>	NZICA	See comment above
101.	Other	<p><i>Developing nations</i> Not applicable from an Australian perspective.</p> <p><i>Translations</i> No issues on translation.</p>	AG of Vic	General comment

102.	Effective Date	<p>You will already be aware of the work that the APB has carried out in issuing Ethical Standards for Auditors in the UK and Ireland. In the original exposure draft of these standards, a similar definition of network firms was included to that proposed by IFAC and independence requirements were extended to all network firms falling within this definition. A significant number of respondents commented that this would be unworkable in practice. While the IFAC Code only extends a limited number of the independence requirements on audit engagements to network firms, the new definition will encompass a much larger number of network firms within these requirements. This may entail a number of practical issues for firms who will need to set up cross-border mechanisms of reporting the identity of audit clients and relationships that are held with these clients and confirming the safeguards that are put in place to reduce any threats to independence to an acceptable level. There may be practical difficulties experienced if network firms are consequently required to terminate a relationship that has been in existence for some time.</p> <p>While the APB supports the proposed revision to Section 290, in recognition of the practical difficulties of implementation that may arise, IFAC should give consideration to the need for providing transitional arrangements or changing the effective date of implementation.</p>	APB	See discussion of <i>Effective date</i>
103.	Effective Date	<p>Grant Thornton International has concluded that its member firms would fall under the revised definition of “Network Firm.” Previously, Grant Thornton International had not considered that our organizational structure met the definition. Therefore, we are concerned that significant time and effort will be required to evaluate the impact of the Proposed Revision on the organization in over 100 countries and to develop appropriate systems and controls to implement the new rules as further outlined above. The Proposed Revision states that it is effective for reports issued after December 31, 2006. We understand that for a calendar year end engagement, due to the period of the engagement rules requiring independence from the start of the client’s fiscal year, the rule is thereby in effect on January 1, 2006. We recommend that the effective date be extended by one year.</p>	Grant Thornton	See discussion of <i>Effective date</i>

104.	Effective Date	We note, however, that the amended definition may result in the creation of a potentially larger number of “networks” and we would advise that the smaller firms are likely to require more time than the proposed effective date to develop the systems needed to monitor the activities of the firms and personnel in their networks. Accordingly, we believe that a deferred effective date of one year would be appropriate. This would also give member bodies time to go through their own due process to consider and ultimately adopt the new requirement.	PwC	See discussion of <i>Effective date</i>
105.	Effective Date	The PEEC believes that the proposed definition of “network firm” and related guidance as set forth in proposed sections 290.14-290.19 is a reasonable and appropriate standard. However, we are concerned that the proposed effective date – <i>i.e., for assurance reports dated on or after December 31, 2006</i> – will not provide sufficient time for member bodies and their constituents to adopt and implement the revised standard. Specifically, many member bodies, including the AICPA, are required to perform specific due process procedures prior to adopting a new ethics standard. For example, the AICPA requires that proposed ethics standards be exposed to membership for comment; that all comments received be considered by PEEC at an open meeting; and public issuance of the final standard in the <i>Journal of Accountancy</i> .	AICPA	See discussion of <i>Effective date</i>
106.	Effective Date	In addition, to assure compliance with the proposed standard, we believe that many of our members who will be affected by the proposal will need time to implement tracking systems to monitor the clients and activities of firms within their networks. Therefore, we would expect to provide our members with a sufficient transition period to put such systems into place. We also note that the proposed effective date of December 31, 2006 would mean that our members would have to implement the new standard on January 1, 2006, since many of the independence requirements affected by the network firm definition would apply <i>during the period covered by the financial statements</i> . Accordingly, we recommend that the Committee consider extending the proposed effective date by one year and make it effective for assurance reports dated on or after December 31, 2007.	AICPA	See discussion of <i>Effective date</i>

107.	Effective Date	By setting the definition at a very wide level, a significant number of groups of accounting firms are likely to fall within the proposed definition. These groups have hitherto not considered independence across their groups and do not have systems in place to track these issues. If they are to be expected to comply with the code as proposed, they will need some time to put such systems in place and to educate their members. We do not believe that the proposed timescale for the introduction of the revised rule will allow these groups to be in a position to confirm their independence throughout the period covered by the audit. We believe that therefore these proposals are anti-competitive allowing the larger groups to benefit at the expense of the smaller groups.	Baker Tilly Barnes	See discussion of <i>Effective date</i>
108.	Effective Date	The logistical arrangements for firms who would fall within the definition of networks, having not previously done so, should not be underestimated. In finalising the implementation arrangements, IFAC should allow a transitional period of at least a year for the necessary arrangements to be put in place, for such firms.	ICAEW	See discussion of <i>Effective date</i>
109.	Client Confidentiality	The guidance as drafted would, we believe, also lead to problems as, in order to comply, a member of a network may have to breach client confidentiality in order to respond to a request from another member.	Baker Tilly Barnes	Isolated comment – Not carried further
110.	Add'n Guidance needed	Whatever the final conclusions, we believe that the Ethics Committee and IFAC need to consider issuing authoritative additional practical guidance on how members of “networks” should develop procedures to be able to comply with the guidance.	Baker Tilly Barnes	See discussion of <i>Additional guidance needed</i>
111.	Add'n Guidance needed	The necessity of the Code’s retaining application guidance applies equally in respect of 290.18 and 290.19 in relation to sub-section (a) (ii) of the current definition. As noted, we regard specific parts of the explanatory material as essential to an interpretation of certain aspects of the definition. In our opinion, similar guidance would be useful in respect of sub-section (a) (iii) and of part (b) of the current definition.	IDW	See discussion of <i>Additional guidance needed</i>

112.	Add'n Guidance needed	If an express definition for the phrase 'larger structure' is not appropriate, we recommend that additional guidance and examples are provided (in addition to the proposed guidance) in section 290 of the Revised Code. The proposed guidance in paragraphs 290.14 – 290.16 in the Exposure Draft is premised on an assumption that the phrase "larger structure" is understood as having a common or defined meaning.	MIA	See discussion of <i>Additional guidance needed</i>
113.	Add'n Guidance needed Sharing of profits and costs	The proposed additional guidance in section 290 of the Revised Code contains useful examples when the sharing of professional resources can be considered to be significant and when a firm practices under the same or similar firm name as other firms in the larger structure. Examples on when there is a sharing of profits or costs should also be included.	MIA	See discussion of <i>Additional guidance needed</i>
114.	Add'n Guidance needed Franchise Agreements	In addition, we recommend that further guidance be provided in respect of situations where a franchising arrangement exists, namely where there is common technical training or methodologies used by a number of firms who also share a common or similar brand name, but where there is competition between these firms and they are independent of each other in terms of ownership, management or sharing of profits and expenses. In this context, clarification or guidance may be required on whether such a franchising arrangement means these firms are within a larger structure or otherwise.	MIA	See discussion of <i>Additional guidance needed</i>
115.	Statements of Membershi P Obligations	<p>Similar issues also arise with the operation of quality assurance programmes across firms and access to working papers; perhaps the Statements of Membership Obligations should also include efforts to extend the regulatory exemptions to be found in much legislation to the operation of network-wide quality and ethical activities, subject to appropriate confidentiality safeguards in each relevant jurisdiction.</p> <p>The significant increase in risk management exposures may also deter firms from working together within a network structure, as defined, deterring the transfer of expertise and consistency across jurisdictions except within the very largest of professional groupings that have already conceded by their earlier promotional strategies that they are single composite entities.</p>	Moore Stephens	General comment

116.	Test for threats to Independence Control Test	We acknowledge that there will, inevitably, be potential for impairment of the independence of the firm undertaking the assurance engagement where the independence of a network Firm that falls within part (b) of the proposed definition is compromised, for the same reason as this is the case under the existing definition, namely that the nature of the relationship between the two firms must, necessarily, mean that their interests cannot be regarded as independent.	Baker Tilly - Jones	Isolated comment – not taken further
117.	Test for threats to Independence Profit/cost sharing test	We consider that part (a)(iii) of the proposed definition should leave room for judgement to be made on the materiality of any profit or cost sharing. Subject to that qualification, for a network firm that falls within this part of the proposed definition, we accept that the overlapping interests of the network firm and the firm undertaking the assurance engagement make it inevitable (where those interests are material) that any impairment of the independence of the network firm should be treated, in appropriate circumstances, as impairing the independence of the instructed firm, Whatever the nature of the threat to the independence of the network firm in either of the above two cases, we consider that the same threat potentially taints the independence of the instructed firm because of the close relationship between the two firms.	Baker Tilly - Jones	Isolated comment – not taken further
118.	Test for threats to Independence Professional resource sharing test	We do not, however, accept that this is necessarily the case where the network firm is one which falls within part (a)(ii) of the proposed definition. It seems to us that the most likely circumstance in which the impaired independence of a network firm of this type could pose a threat to the independence of the firm undertaking the assurance engagement would be where the essence of the threat to independence was a self review threat, For example, we see no reason why the fact that a network firm has a direct financial interest in the assurance client should compromise the independence of the instructed firm, simply because the instructed firm and the network firm share, for example, a common audit methodology. By contrast, where the network firm has been providing non-assurance services to the assurance client which would impair its independence if it were to be invited to undertake the assurance engagement, we acknowledge that this may give rise to a self review threat to the independence of the instructed firm, although we consider that there may be scope for putting in place appropriate safeguards.	Baker Tilly - Jones	Isolated comment – not taken further

119.	Test for threats to Independence Name sharing test	<p>Furthermore, we disagree fundamentally with the assumption implicit in part (a)(i) of the proposed definition, namely that any impairment of the independence of a network firm in this category automatically constitutes a threat to the independence of the firm undertaking the assurance engagement, simply because they have part of their respective trading names in common. In order to illustrate why we consider this premise to be unsustainable, we refer to the following scenario:</p> <ul style="list-style-type: none"> Four firms, ABC Limited, PQR & Co, XYZ LLP and XYZ (Germany) GmbH, are all independent members of an international network of accountancy firms, XYZ International. The independent members of XYZ International do not share either profits and/or costs or significant professional resources with each other. Self evidently, some but not all of the member firms have part of their name in common with the international network and each other, All member firms (regardless of whether they use the XYZ prefix) are required to describe themselves on their letterhead, website and promotional material as "<i>An independent member of XYZ International</i>". Although entry to and continuing membership of XYZ International is conditional upon compliance with certain minimum quality criteria, individual member firms are responsible for creating their own audit methodology and devising and implementing their own quality control systems. 	Baker Tilly - Jones	Isolated comment – not taken further
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120.	<p>Test for threats to Independence</p> <p>Name sharing test</p> <p>Cont</p>	<ul style="list-style-type: none"> Applying part (a)(i) of the proposed definition to this scenario would appear to produce the following results: <ul style="list-style-type: none"> (i) If ABC Limited was undertaking an assurance engagement, its independence would not be regarded as compromised if PQR & Co's independence was impaired, (ii) We assume that the definition is intended to be interpreted as requiring both the firm undertaking the assurance engagement and the network firm to use (in their respective firm names) a name that is common to the larger structure (although it does not expressly state this). If that is the correct interpretation of the definition, ABC Limited's independence would also not be regarded as being compromised by any impairment to the independence of either XYZ LLP or XYZ (Germany) GmbH. That said, on the current drafting of the definition, XYZ LLP and XYZ (Germany) GmbH might arguably be treated as network firms for the purposes of assessing ABC Limited's independence, even though ABC Limited itself does not satisfy the "network firm" criteria. (iii) If XYZ LLP was undertaking an assurance engagement, its independence would be regarded as compromised if XYZ (Germany) GmbH's independence was impaired but not if ABC Limited or PQR & Co's independence was impaired. 	Baker Tilly - Jones	Isolated comment – not taken further
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121.	<p>Test for threats to Independence</p> <p>Name sharing test</p> <p>Cont</p>	<p>We would argue strongly, based on the above example, that there is no justification for an assumption that a firm's independence may be compromised by the position of a fellow independent member of a larger structure, with which it shares part of its name but nothing else, To suggest that XYZ LLP might be any less likely to act with the requisite integrity, objectivity and professional scepticism in relation to an assurance client where XYZ (Germany) GmbH's independence is impaired than it would for a client where ABC Limited's independence is compromised is patently absurd.</p> <p>Whilst the above scenario may appear artificial, it in fact reflects the structure of Baker Tilly International (the international network of independent accountancy and business services firms of which Baker Tilly is a member), in which some but not all of the independent members are licensed to use the "Baker Tilly" prefix as part of their trading name but there is no sharing of profits and/or costs or significant professional resources.</p> <p>Whilst we acknowledge that a third party without knowledge of all the relevant information might assume that firms with parts of their names in common share other things as well (such as professional resources or profits and/or costs), thereby potentially impairing each other's independence, we do not believe that a reasonable and informed third party having knowledge of all the relevant information would reach that conclusion.</p> <p>We therefore consider that part (a)(i) of the proposed definition should be removed</p>	Baker Tilly - Jones	Isolated comment – not taken further
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122.	Safeguards	<p>In the event that our suggestion that part (a)(i) of the proposed definition should be removed does not find favour with the Ethics Committee, we would strongly urge that consideration be given to permitting network firm-related threats to independence to be addressed by way of appropriate safeguards, in the same way as is the case for many other potential threats to independence and in keeping with the conceptual framework approach of the remainder of the Code of Ethics.</p> <p>Possible safeguards could include:</p> <ul style="list-style-type: none"> • A requirement that network firms within part (a)(i) of the proposed definition include a clear statement of their independence on their stationery and promotional material (and, in this regard, we note the example given in paragraph 290.17 of the Exposure Draft, although we question whether there is any need for firms which do not meet the criteria of a network firm to identify their independence in this way, given that <u>by definition</u> the network firm restrictions will not apply); • Where a network firm within part (a)(i) and/or (a)(ii) of the proposed definition has provided non-assurance services, the firm Undertaking the assurance engagement satisfying itself that no reliance has been placed on the work of the network firm (or at least no more reliance than would be placed on it if the work had been done by the assurance client itself); • Where a network firm within part (a)(ii) of the proposed definition has provided non-assurance services, the firm undertaking the assurance engagement satisfying itself that the provision of such non-assurance services has not been supported by shared professional resources such as a common technical department. <p>We consider that all of these safeguards are consistent with the duty on firms to identify and evaluate threats to their independence before deciding whether to accept or continue with an engagement and the nature of any safeguards required.</p>	Baker Tilly - Jones	Isolated comment – not taken further
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123.	Identification of threats to independence	<p>The Code of Ethics quite properly requires a firm to identify and evaluate any potential threats to its independence. Whilst this may be relatively straightforward in a larger structure that has an element of centralised control and compulsory information sharing (all of which indicate a degree of lack of independence between the firms making up that larger structure), we consider that it raises significant issues of client confidentiality for larger structures whose members are, in practical terms, independent. In such a situation, it would potentially be a breach of client confidentiality for the firm proposing to undertake the assurance engagement to publish the fact that it was (or was expecting to be) so instructed in order to enquire into network firm-related threats to its independence and it would almost certainly be a breach of client confidentiality on the part of a network firm that had provided non-assurance services to respond to such an enquiry. We question whether it can possibly be appropriate to impose an obligation that would require firms to breach their duties of client confidentiality.</p> <p>Furthermore, by imposing an obligation that in practice only the Big 4 and perhaps one or two other international networks will be able to comply with, there is a real risk that competition in the international marketplace will be reduced. We do not believe that this can have been intended by IFAC</p>	Baker Tilly - Jones	Isolated comment – not taken further
124.	Inadvertent violation of the Code	<p>One further point which we would wish to make in passing concerns the requirement not only for independence but for the <u>appearance</u> of independence. We would simply comment that, where a firm's enquiries do not identify the existence of a network firm-related situation which could potentially constitute a threat to its independence, we do not consider that in practice the firm's independence can possibly have been impaired by the existence of such a situation. Accordingly, we consider that it should follow from this that where a firm inadvertently acts in breach of the Code of Ethics in this way, it should not be criticised for such inadvertent violation of the Code and its independence in relation to the work done without knowledge of the relevant situation should not be regarded as in any way compromised.</p>	Baker Tilly - Jones	Isolated comment – not taken further

125.	Conclusion	<p>Whilst we acknowledge that there was a need to broaden the definition of "network firm", we believe that the proposed new definition goes too far, identifying a perceived threat to independence where we do not believe one exists, namely through use of a common prefix by financially and professionally independent firms as a consequence of their both being members of the same network or association of firms. Perhaps more importantly, we consider that a reasonable and informed third party, having knowledge of all relevant information, would recognise that no threat to independence exists in those circumstances,</p> <p>If the Ethics Committee remains of the view that the mere use of a common prefix (without more) is sufficient to give rise to a threat to independence (whether actual or perceived), we consider that there are a number of potential safeguards which could be used to eliminate such a threat and believe that the proposals should be amended to permit the putting in place of appropriate safeguards. We consider that such an approach is consistent with the conceptual framework approach of the Code of Ethics.</p> <p>Finally, we consider that there is a real risk that the proposals, which are intended to protect the public interest, may in fact have anti-competitive consequences in the international marketplace. We believe that this would be very much contrary to the public interest.</p>	Baker Tilly - Jones	Isolated comment – not taken further
126.	Other Control	<p>Part of the definition relies on control of or by the firm. What is not made clear is what form of control is envisaged. We assume that it is intended to cover a form of management control that would allow, directly or indirectly, an audit to be influenced, rather than, say, control of the use of a group logo, or who may be a part of the group. We believe it would be useful to clarify the nature of the control required.</p>	ICAEW	See discussion under <i>Interaction of Network firm definition and firm definition</i>

127.	Sharing of costs	According to the Exposure Draft, a firm also would be a network firm if it “is part of a larger structure” and it “(iii) shares profits or costs with other firms within the larger structure”. “Sharing costs” with other firms may be too broad a criterion because the only costs that are shared might be the administrative costs of being part of a large structure. That may be the case with an association of firms, which is addressed in paragraph 290.17. However, to be a firm in an association of firms, the firm must not meet the criteria of a network firm, but the criteria for being a network firm includes sharing costs. Therefore, the definition of a network firm should include further guidance on the meaning of “costs”.	Basel	Proposal to add the term “aimed at co-operation”
128.	Degree of sharing of profits or costs	Part a (ii) of the proposed definition refers to ‘significant professional resources’. However, ‘significant’ is not repeated in a (iii) which refers to sharing of profits (and, presumably, losses) or costs. This implies that even the most immaterial sharing would result in a network, which seems unrealistic. We recommend inclusion of ‘significant’ in a (iii). The European 8 th directive definition, referred to above, has a slightly different construct and there is not the clear implication that insignificant profit sharing would be relevant, in that definition.	ICAEW	See discussion of <i>Profit or cost sharing</i>
129.	Degree of sharing of profits or costs	We are of the opinion that, in line with the language used in current (a) (ii) of the Proposed Revised Definition, it should be stipulated in the Proposed Revised Definition that the sharing of ‘significant’ costs could contribute to audit firms being considered as network firms. Sharing of costs, no matter how small, for instance on a one-off basis, does not appear in the Exposure Draft to form a basis for audit firms to be considered as network firms. We recommend the IFAC Ethics Committee to consider whether an appropriate reference should be introduced in this regard, for instance after paragraph 290.16.	FEE	See discussion of <i>Profit or cost sharing</i>

130.	Degree of sharing of profits or costs	Sub-section (iii) of the current definition would be more precise were it to read “shares profits and losses or significant costs in relation to professional activities on an ongoing basis with other firms within the larger structure”. In our opinion, sharing of profits or losses would, as a minimum imply a network relationship between firms regardless of any legal definitions in particular jurisdictions, as long as such sharing were with respect to professional (as opposed to other) activities and on an ongoing basis (as opposed to a one-off venture). In order that the sharing of insignificant costs not affecting professional activities (e.g., trivial costs, costs for a one-off re-search program, or greater costs for common administrative expenses, such as renting a common office), could not lead to the inaccurate classification of an association between firms as a network, we are also suggesting that the word “costs” be amended to read “significant costs”, and be linked to the professional activities, to incorporate the notion that the determination of both the nature and extent of cost sharing affects the consideration of this criterion. We refer to our proposed definition below, which depicts these amendments.	IDW	See discussion of <i>Profit or cost sharing</i>
131.	Other	In particular, the Code should provide guidance in respect of the “costs” named in sub-section (a) (iii) of the current definition. It is not clear whether the IFAC Ethics Committee views any sharing restricted to costs, such as of a purely administrative nature, as indicative of a network relationship. In our opinion, in the absence of supplementary factors as defined in (a) (i) or (a) (ii) this would not be the case. An example, along the lines of that in paragraph 290.16 would therefore provide useful application guidance.	IDW	See discussion of <i>Profit or cost sharing</i>
132.	ISQCI	It is not clear to what extent firms need to pro-actively seek out independence threats in their network firms. We do not believe that the Code of Ethics is the place for this, as this is a procedural matter. However, we believe that it may be appropriate for the IAASB to expand on its brief comments on the issue in ISQC1 and we would be grateful if the IFAC Ethics Committee could pass on such a request.	ICAEW	See discussion <i>Additional guidance</i>

133.	Other Effect of Litigation	We have concerns over the legal impact of the definition, i.e. the possible use of this definition in litigation against member firms of networks. The possibility exists that a member firm of a network situated in one country could become a defendant in litigation by a regulator or third party based in another jurisdiction on the basis of the ethical definition of a network, despite the fact that the two firms are entirely separate legal entities. We do not comment on the likelihood of success of any such action but merely illustrate the practical difficulties in this regard.	ICAS	Isolated comment – not taken further
134.	Other Potential affect on Competition	The definition may also lead to potentially unintended consequences in terms of the level of competition in the audit market if network firms are unnecessarily prevented from undertaking engagements without due regard to the potential safeguards that they could put in place to mitigate any potential threat that may exist or be perceived to exist. We would urge the IFAC Ethics Committee to ensure that it has fully considered the potential impact on competition of the proposed definition.	ICAS	Isolated comment – not taken further
135.		Also, we recommend IFAC to clarify in the explanatory material that it should be understood under current (a) (iii), that sharing of profits also includes the sharing of losses.	FEE	Isolated comment – not carried further

136.	Other Matters to be discussed by ITF	<p>As stated in our letter of response to a previous Exposure Draft, dated 21 October 2004, the APB believes that the work which has been undertaken within the EU and more recently by the APB has advanced the strength and clarity of ethical standards for auditors. We are disappointed that the work on revising Section 290 of the Code has not yet reflected any of this thinking and urge IFAC to consider the following points:</p> <ul style="list-style-type: none"> • Separate audit requirements. The APB is of the view that separating out the independence requirements for accountants carrying out statutory audits of financial statements from guidance and standards on independence for other assurance services, results in a much clearer and more robust set of standards. We urge IFAC to focus on standards of independence for auditors in its project to revisit the independence requirements in Section 290 of the revised Code. This will increase the clarity of prohibitions and assist in IFAC's objective to serve the public interest, through restoring credibility in financial reporting internationally. • Style of presentation. The IFAC Code does not clearly distinguish requirements from associated guidance. The APB has sought to address this by identifying the basic principles and essential procedures through the use of bold type – the existing IAASB convention. IAASB is currently undertaking a 'clarity' project to ensure the requirements of ISAs are clearly communicated and we believe this should be extended to the IFAC Code. • Responsibilities in respect of auditor independence. In some cases the IFAC Code is not clear whether the responsibility for specific requirements rests with a firm, a network firm, an individual, or all of the parties concerned. The APB has taken the view that clarity as to responsibilities is a key element in ensuring that its standards are applied in practice. Consequently the bold letter requirements of APB Ethical Standards specify whether they apply to the audit firm, the audit engagement partner, members of the engagement team or the wider group of those in a position to influence the conduct and outcome of the audit. The APB has also established a requirement for firms to appoint an ethics partner to oversee the development and communication of ethics policies within a firm and to provide a point for consultation by individual audit partners. We recommend that these clarifications of responsibility should be incorporated in the IFAC Code. <p>Continued</p>	APB	Matter communicated to independence Task Force
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137.	Other Matters to be discussed by ITF	<ul style="list-style-type: none"> • The provision of non-audit services by the audit firm. The APB has introduced a new threat – ‘the management threat’ and has developed new standards and guidance with respect to: <ul style="list-style-type: none"> ○ Tax services, ○ Remuneration services, and ○ Corporate finance services. • The nature of applicable safeguards. The APB has taken the view that the safeguards created by the profession, legislation or regulation and firm-wide safeguards in the work environment (which are included in Sections 100 and 200 of the IFAC Code respectively), will not be adequate to reduce specific threats to auditor independence to an acceptable level. In APB Ethical Standards, firm-wide policies and procedures are not positioned as safeguards, but are required in all audit firms as part of their control environment to ensure integrity, objectivity and independence. Additionally, communication with those charged with governance about threats to independence is not treated as a safeguard in its own right, but as a necessary step to take in order to ensure that all users of the accounts are kept fully informed. • Other requirements. The APB has tightened requirements with regard to: <ul style="list-style-type: none"> ○ Employment by the audit client, ○ Rotation requirements for listed companies, ○ Economic dependence, and ○ Remuneration and evaluation policies. 	APB	Matter communicated to independence Task Force
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138.	Other Matters to be discussed by ITF	In conclusion, we note that several securities regulators and auditor oversight bodies have established requirements for auditor independence that may not be fully addressed by Section 290 of the Ethics Code, including the new Network Firms definition. We are pleased that the Ethics Committee is undertaking additional work to examine and improve the independence requirements in Section 290. As this work proceeds, we look forward to providing additional input.	IOSCO	Matter communicated to independence Task Force
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Legend

ACCA	Association of Chartered Certified Accountants (UK)
AG of Vic	Auditor General of Victoria
APB	Auditing Practices Board (UK)
Basel	Basel Committee on Banking Supervision
Baker Tilly	Two response letters received – one under signature of Jones ones under Barnes
CCAB	Consultative Committee of Accountancy Bodies (UK)
CNCC/OEC	Comagnie Nationale des Commissaires aux Comptes/Ordre des Expertes-Comptables (France_
CGCI	Comité des Groupements de Cabinets Indépendants (France)
CPAAI	CPA Associates International
IDW	Institut der Wirtschaftsprüfer (Germany)
E&Y	Ernst & Young
FEE	Federation des Experts Comptables Europeens
Groupe Excel	Groupe Excel (France)
HKICPA	Hong Kong Institute of Chartered Accountants
IOSCO	International Organization of Securities Commissions
ICAEW	Institute of Chartered Accountants of England and Wales
ICAS	Institute of Chartered Accountants of Scotland
ICPAS	Institute of Chartered Accountants of Singapore
KICPA	Korean Institute of Certified Professional Accountants
MIA	Malaysian Institute of Accountants
SAICA	South African Institute of Chartered Accountants