

## **CONFLICTS OF INTEREST – IESBA PROJECT PROPOSAL**

### **I. Subject**

1. The consideration of the nature and extent of guidance appropriate for professional accountants when dealing with conflicts of interest. This project will result in, as appropriate:
  - (a) Revisions to Section 220 *Conflicts of Interest* to provide additional guidance to professional accountants in public practice when faced with a conflict of interest; and
  - (b) Revisions to Section 310 *Potential Conflicts* to provide additional guidance to professional accountants in business when faced with a conflict of interest.

### **II. Background**

2. All professional accountants may face conflicts of interest. Section 220 of the Code addresses conflicts of interest for professional accountants in public practice. Section 310 of the Code addresses potential conflicts for professional accountants in business.
3. Section 220 provides that a professional accountant in public practice shall take reasonable steps to identify circumstances that would pose a conflict of interest. The section further provides that an accountant shall evaluate the significance of any threat created and apply safeguards to eliminate the threat or reduce it to an acceptable level. The section indicates that notifying the relevant parties and obtaining consent is generally necessary and provides examples of other safeguards that the accountant shall determine whether to apply. The section also states that if consent is denied the accountant shall not continue to act for one of the parties in the matter giving rise to the conflict of interest.
4. Section 310 deals with situations where a professional accountant's responsibilities to an employing organization and professional obligations to comply with the fundamental principles contained in the Code. The Section provides example of pressures that a professional accountant in business might face and examples of safeguards that might be applied.
5. Section 220 was revised under the revisions to the Code that were exposed in July 2003 and completed in June 2005. Section 310 is largely unchanged from the July 1996 Code.

### **III. Project Objective and How It Serves the Public Interest**

#### **A. Project Objective**

6. The objective of the project is to revise Sections 220 and 310 as appropriate so that they provide helpful and up-to-date guidance for professional accountants in public practice and in business to identify and address conflicts of interest.

#### **B. How the Project Objectives Serve the Public Interest**

7. As the roles of accountants expand and as public accounting firms expand in size and areas of practice, conflicts of interest is an area where attention is needed. The need to identify and appropriately address conflicting interests has become increasingly relevant. For example, the failure to identify or address conflicts of interest, on a timely

basis, may require a firm to have to withdraw from a client relationship with insufficient time for the client to effect an orderly transition to an alternative service provider.

## **IV. Outline of the Project**

### **A. Project Scope**

8. The scope of this project is to provide guidance for professional accountants when faced with conflicts of interest by revising Sections 220 and 310.

### **B. Revision of Sections 220 and 310 – Major Problems and Key Issues that Will Be Considered**

#### **B.1 AREAS FOR ADDITIONAL CONSIDERATION**

9. The task force will address the extent to which additional guidance is needed on the following:

- *Definition or Description of a Conflict of Interest* – At an early stage in the project, the task force will consider whether the Code should contain a definition of a conflict of interest. For example “A conflict of interest arises from an interest or relationship that would be seen by a reasonable and informed third party to influence a professional accountant’s objectivity.” The task force will also consider whether it would be useful if the Code described different categories of conflicts. For example: professional conflicts, legal conflicts and business conflicts.
- *Linkage to Fundamental Principles* – The task force will consider whether guidance is needed to provide a linkage to the fundamental principles.

The principle of objectivity imposes an obligation on all professional accountants not to compromise their professional or business judgment because of bias, conflict of interest or the undue influence of others. This principle requires accountants either to be free of conflicts of interest or if potential conflicts exist to observe methodologies or procedures for resolving them.

The principle of confidentiality imposes an obligation on all professional accountants to refrain from:

- (a) Disclosing outside the firm or employing organization confidential information acquired as a result of professional and business relationships without proper and specific authority or unless there is a legal or professional right or duty to disclose; and
  - (b) Using confidential information acquired as a result of professional and business relationships for their personal advantage or the advantage of third parties.
- *Examples of Conflicts*– The task force will consider whether the Code should provide examples of conflicts and whether the examples should be sub-classified by category of conflict and/or, in the case of professional accountants in public practice, by professional services area. Examples of conflicts could include:
    - Acting for two or more parties on a matter in which the parties have a competing interest (eg competing bidders in a corporate finance transaction)
    - Acting for two or more parties on a matter in which the parties have an adverse interest (eg opposing parties in a dispute)

- Acting for a party where some aspect of the professional accountant's commercial or business arrangements (such as an investment or a business alliance) gives rise to a conflict in relation to the professional activity
- Acting when a prior engagement could represent a threat to objectivity
- A professional accountant possessing confidential information about one party that would be useful to another party, for example:
  - An auditor possessing confidential client information about one client that is important to the fulfillment of an engagement for another client; or
  - A professional accountant in business is a director of company X and company Y. The director acquires confidential information from company X that is relevant to company Y.
- *Situations in which a conflict might arise* - The task force will consider whether the Code should provide examples of situations in which a conflict might arise. Examples could include:
  - Conflicts arising from a firm merger;
  - Conflicts arising from a client merger; and
  - Conflicts arising in an SMP environment where there may be few service providers in the market.
- *Identification of Conflicts* – Identification of conflicts is a particularly challenging area and the task force will consider whether the Code should contain guidance on how the professional accountant should or could identify conflicts of interest. The task force will consider:
  - Whether the standard for identification for conflicts should be the same for professional accountants in practice and professional accountants in business;
  - The extent to which the Code should address steps that a professional accountant should or could take to identify conflicts of interest. For example:
    - Seeking information from others within the organization, where this is possible;
    - Maintaining a data base with relevant information; and
  - Network firm considerations, if any.
- *Evaluating the Conflict* – The task force will consider whether the Code should provide guidance on how a professional accountant should evaluate an identified conflict. The task force will consider matters such as:
  - Whether the conflict is such that it is common commercial practice and consent can be implied (for example acting as auditor for several clients that compete in the same industry). The task force will consider whether the Code should address implied consent, and, if so, whether examples of such situations should be provided;
  - Whether the conflict is such that explicit consent is necessary;
  - Whether the conflict could be managed through institutional processes;
  - Whether there are specific considerations in managing conflicts in SMP environments.
- *Addressing the Conflict* - The task force will consider whether the Code should provide guidance on how a professional accountant should address an identified conflict. For example whether the conflict is such that the matter giving rise to the

conflict needs to be terminated, whether the conflict is such that it can be managed or whether the conflict is such that no action is needed. The task force will also consider whether the Code should provide examples of conflicts that would require these types of action.

- *Conflict Management* - The task force will consider whether the Code should provide guidance on how conflicts can be managed. The task force will consider matters such as:
  - Firm structure – a firm may structure itself in a variety of ways to deal with conflict issues
  - Mitigation strategies including safeguarding confidential information
  - The desirability of an organization having a conflicts policy
  - Recusal from the issue giving rise to the conflict
  - Disclosure and client consent:
    - General consent – for example in an engagement letter;
    - Specific consent - possibly required where the conflict relates to a matter than will be resolved to the benefit of one client and the detriment of the other.

## B.2 STRUCTURE OF THE GUIDANCE

10. Sections 220 and 310 provide guidance for professional accountants in public practice and business respectively. The task force will consider whether guidance that is common to both types of accountants (for example, the definition of a conflict of interest) should be repeated in both sections or whether it should be included in Part A (which applies to all professional accountants).

## V. Implications for Any Specific Persons or Groups

11. The project has particular implications for the following:
  - (a) Forum of Firms and auditors in general.
  - (b) National standards setters.
  - (c) Regulatory bodies.

## VI. Development Process, Public Consultation, Project Timetable and Project Output

12. The revision of Sections 220 and 310 will follow due process for the development of a pronouncement. Specific consideration will be given to the need to hold focus groups or roundtables to ensure relevant feedback is obtained to from those with direct experience in conflicts of interest.

## A. Tentative Project Timetable

Project Stage	Timing
Approval of project proposal by IESBA	Q4 2009
Issues Paper and First Read	Q2 2010
Exposure Draft First read	Q1 2011
Approve exposure draft	Q4 2011
Full review of exposure draft comments and first read post-exposure	Q2 2012
Approve final standard	Q4 2012

## B. Project Outputs

13. Revisions, as appropriate, to Sections 220 and 310 of the Code.

## VII Impact Analysis Considerations

14. The primary benefit in identifying and developing up to date guidance for professional accountants regarding conflicts of interest is that it will improve accountants' ability to identify and manage conflicts of interest. Users of services of professional accountants will benefit from receiving objective services.

## VIII. Resources Required

15. A project task force consisting of up to 6 individuals, including a member of the IESBA as chair.
16. IESBA technical staff will provide staff support to the task force.

## IX. Relevant Sources of Information that Address the Matter Being Proposed

17. Relevant sources of information include the following:
  - Review of selection of relevant legal cases addressing matter
  - Canadian Institute of Chartered Accountants – Conflicts of Interest a Task Force Report  
[http://www.cica.ca/multimedia/Download\\_Library/About\\_the\\_Profession/HOPPEN\\_CICA\\_oCT31.pdf](http://www.cica.ca/multimedia/Download_Library/About_the_Profession/HOPPEN_CICA_oCT31.pdf)
  - Institute of Chartered Accountants of Ontario – Rule of Professional Conduct 210 Conflict of Interest and Related Council Interpretation  
<http://www.icao.on.ca/Resources/Membershandbook/1011page2635.pdf> and  
<http://www.icao.on.ca/Resources/Membershandbook/1011page2642.pdf>
  - Institute of Chartered Accountants in Australia – Values, Codes of Ethics and the Law – Discussion Paper:  
[http://www.charteredaccountants.com.au/files/documents/ethics%20paper\\_final.pdf](http://www.charteredaccountants.com.au/files/documents/ethics%20paper_final.pdf)

- Institute of Internal Auditors – Internal Organization Conflicts of Interest  
<http://www.irs.gov/instructions/i1023/ar03.html>
- New Zealand Institute of Chartered Accountants – Code of Ethics Rule 5 Conflicts of Interest  
[http://www.nzica.com/AM/Template.cfm?Section=Professional\\_standards\\_files&Template=/CM/ContentDisplay.cfm&ContentID=15545](http://www.nzica.com/AM/Template.cfm?Section=Professional_standards_files&Template=/CM/ContentDisplay.cfm&ContentID=15545)
- OECC Managing Conflicts of Interest in the Public Sector:  
<http://www.oecd.org/dataoecd/51/44/35365195.pdf>
- UK ICAEW – Code of Ethics Section 220 Conflicts of Interest  
[http://www.icaew.com/index.cfm/route/162805/icaew\\_ga/Members/Member\\_support/Professional\\_conduct/Members\\_handbook/3\\_3\\_Members\\_handbook\\_2009/pdf](http://www.icaew.com/index.cfm/route/162805/icaew_ga/Members/Member_support/Professional_conduct/Members_handbook/3_3_Members_handbook_2009/pdf)
- US AICPA ET Section 102 Interest and Objectivity Interpretation 102.-2 Conflicts of Interest: [http://www.aicpa.org/about/code/et\\_102.html](http://www.aicpa.org/about/code/et_102.html)
- US Internal Revenue Service Sample Conflict of Interest Policy:  
<http://www.irs.gov/instructions/i1023/ar03.html>

## **Appendix 1**

### **COMMENTS BY TECHNICAL MANAGERS**

The comments of Technical Manager from each technical area are required before this Project Proposal is considered by the board or committee proposing to undertake the project.

#### **Technical Manager to the Compliance Advisory Panel**

Signed: Sylvia Barrett

Date: October 7, 2009

#### **Technical Manager to the Developing Nations Committee**

Signed: Russell Guthrie

Date: October 5, 2009

#### **Technical Manager to the IAESB**

The IAESB supports the completion of this guidance project on updating sections 220 and 310 of the Code. Any additional guidance or knowledge that increases awareness or sensitivity and improves professional judgment in the area of conflicts of interest for the professional accountant would be welcomed by the IAESB. The IAESB requests that the IESBA keep the Education Board informed of the direction of the guidance, especially in areas where there may be an impact on the learning, development, and assessment of the professional accountant. The IAESB pronouncements currently include IES 4, a practice statement, and the ethics education tool kit. As a result we will be monitoring the impact of any additional guidance in the area of conflicts of interest to ensure that the IAESB's pronouncements are properly aligned with the IESBA's guidance.

Signed: David McPeak

Date: October 1, 2009

#### **Technical Manager to IAASB**

Signed: James Gunn

Date: October 5, 2009

#### **Technical Manager to the PAIB Committee**

The nature of conflicts and independence is not the same for PAIBs (compared to auditors) and the kind of guidance that is required over and above the Code needs to be evaluated, including in light of the resources available at a national level;

There needs be adequate PAIB representation when discussing conflicts of interest in relation to PAIBs and the PAIB Committee supports IESBA in ensuring that there is adequate PAIB input (over and above the PAIB members of IESBA) in identifying appropriate remedies/mitigation strategies for PAIBs.

Signed: Stathis Gould

Date: October 5, 2009

**Technical Manager to the IPSASB**

Signed: Stephenie Fox

Date: October 7, 2009

**Technical Manager to the SMP Committee**

We support the timely completion of this project but at this time can't foresee specific SME/SMP issues.

Signed: P. Thompson

Date: Sept. 10, 2009

**Technical Manager to the Transnational Auditors Committee**

Signed: Barry Naik

Date: October 10, 2009