

*International Ethics Standards Board for Accountants*

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# Proposed Changes to the Code of Ethics for Professional Accountants Addressing Conflicts of Interest

## REQUEST FOR COMMENTS

The International Ethics Standards Board for Accountants (IESBA) approved this exposure draft, *Proposed Changes to the Code of Ethics for Professional Accountants Addressing Conflicts of Interest*, for publication at its October 2011 meeting. This proposal may be modified in light of comments received before being issued in final form.

Respondents are asked to submit their comments **electronically** through the IFAC website ([www.ifac.org](http://www.ifac.org)) using the “Submit a Comment” link on the Exposure Drafts and Consultation Papers page. Please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the IFAC website. Although the IESBA prefers that comments be submitted electronically, comments also may be submitted by e-mail to [janmunro@ifac.org](mailto:janmunro@ifac.org).

Comments should be submitted by **March 31, 2012**.

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# **EXPLANATORY MEMORANDUM**

## **Introduction**

This memorandum provides background for, and an explanation of, the proposed changes to various sections in the Code of Ethics for Professional Accountants (the Code) related to provisions addressing conflicts of interest. The International Ethics Standards Board for Accountants (IESBA) approved these proposed changes for exposure in October 2011.

The IESBA welcomes all comments on the proposed changes. In addition to general comments, the IESBA welcomes comments on the specific questions that are contained at the end of this memorandum.

## **Background**

The Code contains two sections that address conflicts of interest, Section 220 for professional accountants in public practice and Section 310 for professional accountants in business.

Section 220 states that a professional accountant shall take reasonable steps to identify circumstances that could pose a conflict of interest, and that such circumstances may create threats to compliance with the fundamental principles. The section also states that a professional accountant shall evaluate the significance of threats and apply safeguards to eliminate them or reduce them to an acceptable level. Potential safeguards are provided in the section and it is stated that, depending on the circumstances giving rise to the conflict, obtaining consent from all relevant parties is generally necessary. If threats to the fundamental principles cannot be eliminated or reduced to an acceptable level or consent is refused by the client, the professional accountant shall not accept a specific engagement or shall resign from one or more conflicting engagements.

Section 310 of the Code describes a professional accountant's responsibility to an employing organization and professional obligations to comply with the fundamental principles. Certain examples are provided of where these two requirements might be in conflict and certain pressures a professional accountant in business may face. The section provides examples of safeguards that may be applied to reduce the threats to the fundamental principles that might arise from a conflict of interest.

Failure to identify and address conflicts of interest on a timely basis may result in an accountant having to withdraw from an arrangement at a point in time where the affected parties have insufficient time to effect an orderly transition to an alternative service provider. In October 2009, the IESBA approved a project proposal to provide additional guidance for all professional accountants in identifying and addressing conflicts of interest. The purpose of the project is to examine Sections 220 and 310 and revise them to provide more comprehensive guidance in identifying, evaluating and managing conflicts of interest.

## **Significant Matters**

### **General Approach and Scope**

The IESBA is not proposing changes to the general approach to identifying, evaluating and managing conflicts of interest set out in the extant Code. That approach requires the application of the conceptual framework set out in Part A of the Code, and the IESBA believes it continues

to be appropriate. The proposed changes will, however, provide more specific requirements and guidance for a professional accountant in applying the conceptual framework when identifying, evaluating, and managing conflicts of interest, as explained below. In the IESBA's view the approach to be taken by a professional accountant in public practice and a professional accountant in business should be broadly similar. The proposals recognize, however, that conflicts of interest will typically arise in different circumstances for accountants in public practice due to the different nature of professional services and the wider range of parties for which the firm may act.

### **Description of a Conflict of Interest**

Extant Sections 220 and 310 do not describe a conflict of interest or provide examples of conflicts of interest. The proposal includes a description of circumstances that might create a conflict of interest for the professional accountant together with examples of such circumstances. The purpose is to help the professional accountant to identify a potential conflict of interest at a sufficiently early stage to be able to take any actions necessary to comply with the fundamental principles. The description developed for this purpose specifically includes conflicts between:

1. The interests of two or more parties for whom the professional accountant undertakes professional activities<sup>1</sup>; and
2. The interests of the professional accountant and the interests of a party for whom the professional accountant undertakes a professional activity.

The proposal includes a description of a conflict of interest in paragraph 100.17 and in each opening paragraph of Sections 220 and 310.

In the extant Code, the first paragraph of Section 220 states that conflicts of interest could create threats to compliance with the fundamental principles and specifically mentions the fundamental principles of objectivity and confidentiality. Section 310 refers to conflicts creating threats to the fundamental principles. The proposed description of a conflict of interest states that a conflict of interest "creates a threat to objectivity and may create threats to other fundamental principles." The IESBA believes that while a conflict of interest may create a threat to any of the fundamental principles, the most relevant and significant threat when a conflict of interest arises is to the professional accountant's objectivity, i.e. the ability to undertake a professional activity without allowing bias or undue influence of others to override professional or business judgments.

### **Matters Specific to Professional Accountants in Public Practice**

#### *Reasonable and Informed Third Party*

The proposed revision to Section 220 requires the professional accountant to take into account whether a reasonable and informed third party, weighing all the specific facts and circumstances

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<sup>1</sup> Under the extant Code professional services are performed by professional accountants in public practice and professional accountants in business. Professional services are defined as "Services requiring accountancy or related skills performed by a professional accountant including accounting, auditing, taxation, management consulting and financial management services." The IESBA is of the view that the term professional services does not resonate well with professional accountants in business and proposes that the term "professional services" be replaced with the term "professional activities" in Parts A and Part C of the Code. The term "professional services" will continue to be used in Part B of the Code.

available to the professional accountant at that time, would be likely to conclude that compliance with the fundamental principles is compromised. This would be required both when identifying and evaluating conflicts of interest and when implementing safeguards to address them. In the IESBA's view it is appropriate for the professional accountant to consider how a conflict of interest would be viewed by a third party. Additionally, this is consistent with the application of the conceptual framework and the determination of whether threats to compliance with the fundamental principles are at an acceptable level.

#### *Identifying and evaluating a threat*

The proposed revision to Section 220 requires the professional accountant to understand the nature of the relationships and services in identifying whether a conflict of interest exists or may be created. It also requires the professional accountant to evaluate the significance of the relevant interests or relationships.

#### *Network Firms*

The IESBA considered what standard should apply with respect to potential conflicts of interest that might be created by the interests and relationships that a firm that is a member of a network of firms, has with a client. The IESBA considered the following points and is of the view that potential conflicts of interest within a network of firms should be evaluated when the professional accountant has reason to believe that a conflict of interest exists because of interests or relationships that another firm in the network has with a client. The "reason to believe" test requires the professional accountant to consider the facts available to the professional accountant at that time. The proposal recognizes that the extent of client information exchanged will vary between different networks depending on legal and contractual constraints. It would, therefore, be disproportionate to require a firm before accepting a new engagement to undertake a search across the network to identify any interests or relationships that might create a conflict of interest regardless of whether the firm has reason to believe that a conflict exists.

When evaluating whether the professional accountant has reason to believe that a conflict of interest may exist or be created due to interests and relationships of a network firm, the proposal requires the accountant to take into account factors such as the nature of the professional services provided, the clients served, and the geographic locations of all relevant parties.

#### *Guidance on Safeguards to Manage Conflicts of Interests, including Obtaining Consent*

The proposal expands on the guidance in the extant Code regarding the nature of safeguards that may be available to manage conflicts of interest within firms. The IESBA believes that it is generally necessary to disclose the nature of the conflict to the client and all known relevant parties and to obtain written consent from the client and such parties before performing the professional service. Implicit in providing consent is that the consenting parties believe the firm can carry out the activity in compliance with the fundamental principles in the Code, particularly objectivity.

The proposal recognizes that in certain circumstances the consent obtained from any relevant party may be implied by the party's conduct in keeping with common commercial practice. The proposal also encourages the professional accountant to document such consent when it is obtained verbally or implied by the party's conduct.

The proposal recognizes, however, that in certain circumstances the professional accountant will not be able to obtain consent because requesting consent would in itself result in a breach of confidentiality. Two examples referred to in the proposal where this situation might arise are:

- When performing a transaction-related service for a client in connection with a hostile takeover of another client of the firm.
- Performing a forensic investigation for a client where the firm has confidential information obtained by having performed a professional service for another client who would be the subject of the investigation.

The proposal provides that the firm shall only accept such an engagement if certain conditions are met. These conditions are:

- The firm does not act in an advocacy role for one client which is adversarial to the interests of another client;
- Specific mechanisms are in place to prevent disclosure of confidential information between the engagement teams serving the two clients; and
- The firm is satisfied that a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at that time, would conclude that it is appropriate for the firm to accept the engagement in the particular circumstances.

### **Matters Specific to Professional Accountants in Business**

The IESBA concluded that the material in extant Section 310 addresses conflicts of duty rather than conflicts of interest as described above. As this material is already addressed in other sections of the Code, the IESBA proposes to delete the content of the extant section and replace it with guidance for professional accountants in business on identifying, evaluating, and managing conflicts of interest.

In the view of the IESBA it is important to read proposed Section 310 in conjunction with Section 300, which has not been amended. In particular, Section 300 notes that the professional accountant in business has a responsibility to further the legitimate aims of the accountant's employing organization. The proposal does not preclude a professional accountant in business from properly fulfilling this responsibility. However, proposed Section 310 addresses circumstances in which conflicts of interest might arise when performing professional activities that compromise compliance with the fundamental principles. It requires the professional accountant in business to take steps to identify, evaluate, and manage those situations.

#### *Reasonable and Informed Third Party Standard*

Proposed Section 310 requires the professional accountant in business to be alert to all interests and relationships that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, might compromise compliance with the fundamental principles. This is in contrast to the proposed requirement for a professional accountant in public practice, which is to take reasonable steps to identify such circumstances, due to the different nature of the professional services and the wider range of parties for which a firm may act. However, in the IESBA's view it is appropriate for the professional accountant in business to also consider how a conflict of interest would be viewed by a third party.



### *Identifying and evaluating a threat*

The proposed revision to Section 310 requires the professional accountant to understand the nature of the relationships and activity in identifying whether a conflict of interest exists or may be created. It also requires the professional accountant to evaluate the significance of the relevant interests or relationships.

### *Conforming Changes to Sections 320 and 340*

In proposing revisions to Section 310 to address conflicts of interest, the IESBA recognizes that professional accountants in business may encounter other threats to compliance with the fundamental principles. Certain ethical conflicts might arise, such as undue pressure and self-interest threats, when preparing financial information. For example, this may be the case if an arrangement exists whereby compensation is linked to the results of financial reporting.

The IESBA notes that these types of ethical conflicts are addressed in Sections 320, *Preparation and Reporting of Information*, and 340, *Financial Interests*, of the Code. The IESBA has made some conforming changes to these sections to improve the alignment between those sections and Sections 220 and 310. For example, paragraph 310.3 calls for the professional accountant to be alert to all interests and relationships that might give rise to a conflict of interest. A conforming change has been made to Section 340 to include a similar requirement for the accountant to be alert to the principle of integrity, which imposes an obligation to be honest and straightforward in the face of, for example, pressure from a superior to manipulate price sensitive information in order to gain financially. The IESBA has not, however, undertaken a comprehensive revision of these sections as this would be beyond the scope of this project.

## **Analysis of Overall Impact of the Proposed New Guidance<sup>2</sup>**

The IESBA is pilot testing the use of impact analysis to convey the results of its assessment of the potential impact that proposed amendments to the Code may have.

The work effort involved should not be excessive in terms of time of professional resources, however the impact should be significantly positive in avoiding or managing a potential conflict of interest. There are few new requirements and no changes that would significantly alter the ethical responsibilities of professional accountants. For example, for all professional accountants the new guidance contains a description of a conflict of interest. This description has been included to facilitate compliance with the Code and early detection of a conflict of interest. The impact on all other parties, such as those for whom the professional accountant undertakes professional activities and users of information produced by the professional accountant is indeterminate, as the impact would be based on how the guidance affects the actions of the professional accountant. However, since the guidance should improve the professional accountant's ability to effectively avoid or manage a potential conflict of interest, the impact should be significantly positive.

### **Analysis of Overall Impact Specific to Section 220**

The proposal would require a professional accountant in public practice to consider the views of a reasonable and informed third party when identifying and evaluating potential conflicts of

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<sup>2</sup> Impacts are presented in tabular format in the Appendix

interest. The work effort involved should not be excessive in terms of time or use of professional resources.

Professional accountants in public practice who are employed by a firm within a network are required to evaluate conflicts of interest that the professional accountant has reason to believe may exist due to certain relationships and interests within the network, taking into account certain factors. As this new requirement essentially requires the professional accountant to take into account information known at that time, and does not call for extensive investigations to uncover conflict situations within the network, it is considered to be low in impact.

The new guidance in Section 220 addresses certain instances where a firm may be unable to obtain consent from all relevant parties prior to accepting or continuing with an engagement because this might in itself breach confidentiality. This guidance is contained in paragraph 220.8. While the paragraph does contain new requirements, it is limited to very specific situations as described in the paragraph. Thus, the impact is considered to be significantly positive.

### **Analysis of Overall Impact Specific to Section 310**

The guidance in Section 310 of the extant Code has been deleted for the reasons stated above. This change streamlines the Code and therefore has a low impact on professional accountants in business, or any other users of the Code.

The guidance in proposed Section 310 contains a requirement for professional accountants in business to be alert to interests and relationships that a reasonable and informed third party would be likely to conclude might compromise compliance with the fundamental principles. This proposed requirement should not require a significant amount of time or resources to make the necessary considerations. The effect on those parties for whom the professional accountant in business undertakes professional activities or on those who use information obtained from the professional accountant in business is indeterminate as the impact would be based on how the guidance affects the actions of the professional accountant. However, since the guidance should improve the professional accountant's ability to effectively avoid or manage a potential conflict of interest, the impact should be significantly positive.

### **Effective Date**

The IESBA proposes that the effective date for the changes be eighteen months after approval of the final standard. The IESBA is of the view that implementation would not require major changes to established procedures and therefore a relatively short transition period is appropriate.

### **Project Timetable**

Subject to comments received on exposure of proposed changes, the IESBA intends to finalize the revisions to the Code in the first half of 2012.

### **Guide for Respondents**

The IESBA welcomes comments on all matters addressed in the exposure draft. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this exposure draft (especially those calling for change in current practice), it will be helpful for the IESBA to be made aware of this view.

## **Request for Specific Comments**

The IESBA would welcome views on the following questions:

1. Do respondents find the description and examples of conflicts of interest helpful?

### *Matters specific to professional accountants in public practice (Section 220 of the Code)*

2. Do respondents find the reasonable and informed third party standard appropriate?
3. Do respondents find the “reason to believe” threshold for network firms in evaluating conflicts of interest appropriate?
4. Do respondents find the guidance concerning safeguards to manage conflicts of interest and obtaining and documenting consent, as set out in paragraph 220.7, appropriate?
5. Do respondents concur with the three conditions set out in paragraph 220.8 required to be met before a professional accountant can proceed to accept or continue with an engagement when a conflict of interest exists but consent cannot be obtained because it would in itself breach confidentiality? Are the examples within paragraph 220.8 helpful?

### *Matters specific to professional accountants in business (Section 310, 320 and 340 of the Code)*

6. Do respondents agree with the general requirement to identify, evaluate and manage conflicts of interests as set out in proposed Section 310 of the Code?
7. Do respondents find the reasonable and informed third party test appropriate?
8. Do respondents find the conforming changes proposed for Sections 320 and 340 useful? Are they appropriate and adequate?

### *Other*

9. Do respondents agree with the impact analysis as presented? Are there any other stakeholders, or other impacts on stakeholders, that should be considered and addressed by the IESBA?

## Analysis of Impacts of Revisions to the Code Addressing a Conflict of Interest

### Significant Matters

Current Standard	Proposed Change	Impact	Party Impacted	Significance	Duration of Impact
The Code currently does not describe a conflict of interest as addressed by the IESBA's proposed guidance.	The proposal includes a description of a conflict of interest in paragraph 100.17: A professional accountant may be faced with a conflict of interest when undertaking a professional activity. A conflict of interest creates a threat to objectivity and may create threats to other fundamental principles. Such threats may be created by: Conflicts between the interests of two or more parties for whom the professional accountant undertakes professional services; or conflicts between the interests of the professional accountant and the interests of a party for whom the professional accountant undertakes professional services.	The description of conflicts of interest that a professional accountant may face facilitates compliance with the code and early detection of conflicts. It does not create a new requirement.	Professional accountants in public practice and business.  All parties for whom the professional accountant undertakes a professional activity.  Users of information obtained from a professional accountant.	Professional accountants – significantly positive in avoiding or managing a potential conflict of interest.  Impact on other parties is indeterminate, as the impact would depend on how the guidance affects the actions of the professional accountant.	Ongoing

### Matters Specific to Section 220 of the Code

Current Standard	Proposed Change	Impact	Party Impacted	Significance	Duration of Impact
The Code currently does not require the professional accountant in public practice to consider the reasonable and informed third party when identifying and evaluating conflicts of interest and implementing safeguards as addressed by the IESBA's proposed guidance.	Paragraph 220.4 requires the professional accountant to take into account whether or not a reasonable and informed third party would be likely to conclude that compliance with the fundamental principles is compromised.	The work effort involved should not be excessive in terms of time or professional resources.	Professional accountants in public practice.	Low impact.	Ongoing
Paragraph 220.2: Before accepting or continuing a client relationship or specific engagement, the professional accountant in public practice shall evaluate the significance of any threats created by business interests or relationships with the client or third party.	Paragraph 220.5 requires, amongst other things, that professional accountants in public practice who are employed by a firm within a network are required to evaluate conflicts of interest that the professional accountant has reason to believe may exist due to certain relationships and interests within the network, taking into account certain factors.	As this new requirement essentially requires the professional accountant to take into account information known at that time it is considered to be low impact.	Professional accountants in public practice, and network firms.	Professional accountant in public practice and network firms - low impact.	Ongoing
Paragraph 220.4 The Code provides guidance on safeguards.	Paragraph 220.7 develops the guidance on the nature of safeguards that may be available. Disclosure and written consent is	Paragraph 220.8 does contain new requirements when consent would in itself	Professional accountants in public practice and all parties for whom the	Professional accountant in public practice - low impact.	Ongoing.

	<p>generally necessary from the client and all known relevant parties. Documentation is encouraged.</p> <p>However, paragraph 220.8 recognizes that in certain circumstances, requesting consent would in itself result in a breach of confidentiality. Such engagements are prohibited unless three conditions are met.</p>	<p>be a breach of confidentiality, but this is limited to very specific situations. Thus the impact is considered to be low.</p>	<p>professional accountant provides professional services and users of information obtained from a professional accountant in public practice.</p>		
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### Matters Specific to Section 310 of the Code

<b>Current Standard</b>	<b>Proposed Change</b>	<b>Impact</b>	<b>Party Impacted</b>	<b>Significance</b>	<b>Duration of Impact</b>
The entire text of Section 310 of the extant Code.	It is proposed that the entire section be deleted and replaced with text which is broadly consistent with Section 220.	The deletion of the section streamlines the Code for the professional accountant in business and all other users of the Code. The deletion creates efficiency for the user by removing guidance that is redundant.	Professional accountants in business and all others users of the Code.	Professional accountants in business - low impact—the changes streamline the information of the Code.	Ongoing
The Code currently does not specifically address the “reasonable and informed third party” relating to conflicts of interest as addressed by the IESBA’s proposed guidance.	Paragraph 310.3. A professional accountant in business shall be alert to all interests and relationships that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, might give rise to a conflict of interest.	Requiring a professional accountant in business to be alert to interests that a reasonable and informed third party would be likely to conclude might give rise to a conflict of interest, enhances compliance with the fundamental principles.	Professional accountants in business and all parties for whom the professional accountant undertakes a professional activity and users of information obtained from a professional accountant.	Professional accountants in business – the proposed new requirement should not cause a significant burden on the professional accountant.  Guidance should improve accountant’s ability to avoid or manage a conflict of interest – significant positive impact.	Ongoing

## **PROPOSED CHANGES TO THE CODE OF ETHICS FOR PROFESSIONAL ACCOUNTANTS ADDRESSING CONFLICTS OF INTEREST**

Additions to extant paragraphs are underlined

*Paragraphs 100.17-100.18 and their heading below would be inserted before the heading Ethical Conflict Resolution and extant paragraphs 100.17-100.22 would be renumbered as paragraphs 100.19-100.24.*

### *Conflicts of Interest*

100.17 A professional accountant may be faced with a conflict of interest when undertaking a professional activity<sup>1</sup>. A conflict of interest creates a threat to objectivity and may create threats to other fundamental principles. Such threats may be created by:

- Conflicts between the interests of two or more parties for whom the professional accountant undertakes professional activities; or
- Conflicts between the interests of the professional accountant and the interests of a party for whom the professional accountant undertakes a professional activity.

100.18 Parts B and C of this Code discuss conflicts of interest for professional accountants in public practice and professional accountants in business, respectively.

## **SECTION 220**

### **Conflicts of Interest**

*Paragraphs 220.1-220.6 would be deleted and replaced with the following paragraphs 220.1-220.10:*

220.1 A professional accountant in public practice may be faced with a conflict of interest when performing a professional service<sup>2</sup>. A conflict of interest creates a threat to objectivity and may create threats to other fundamental principles. Such threats may be created by:

- Conflicts between the interests of two or more clients; or
- Conflicts between the interests of the professional accountant and the interests of the client.

A professional accountant shall not allow a conflict of interest to compromise professional or business judgment.

220.2 Examples of situations in which conflicts of interests may arise include:

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1 **New Definition:** Professional Activity: An activity requiring accountancy or related skills undertaken by a professional accountant, including accounting, auditing, taxation, management consulting, and financial management.

2 **Revised Definition:** Professional Services: Professional activities performed for clients.



- Advising two shareholders in dispute over the distribution of assets on the dissolution of the company;
- Preparing valuations of assets for different parties in adversarial proceedings;
- Performing litigation services for the plaintiff in connection with a lawsuit filed against a client of the professional accountant's firm;
- Representing two clients who are trying to acquire the same company;
- Representing two clients who are in a legal dispute with each other;
- Recommending a client to invest in a business in which the professional accountant in public practice has a financial interest; or
- Advising a client on the purchase of an information system while having a license agreement with a potential software vendor.

220.3 A professional accountant in public practice shall take reasonable steps to identify circumstances that might create a conflict of interest. This includes potential conflicts of interest when accepting a new engagement and conflicts of interest that may arise during the course of an engagement. The nature of the services and the relevant relationships may change during the course of the engagement. This is particularly true when a professional accountant is asked to conduct an engagement in a situation that may become adversarial, even though the parties who engage the professional accountant may not initially be involved in a dispute.

220.4 When identifying and evaluating the interests and relationships that might create a conflict of interest and implementing safeguards, when necessary, the professional accountant in public practice shall take into account whether a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, that compliance with the fundamental principles is compromised.

220.5 In identifying whether a conflict of interest exists or may be created, and evaluating the significance of any threat to objectivity or compliance with other fundamental principles, in particular before accepting a new client relationship, engagement, or business relationship, a professional accountant in public practice shall:

- Understand the nature of the relationships between the parties involved and any relevant interests;
- Understand the nature of the service and its implication for relevant parties;
- Evaluate the significance of relevant interests or relationships. In general, the more direct the relationship between the professional service and the matter on which the clients' interests are in conflict, the more significant the threats may be;
- Evaluate the extent to which a professional service performed for more than one client may result in a conflict of interest; and
- Evaluate any potential conflicts of interest that the professional accountant has reason to believe may exist due to interests and relationships of a network firm,

taking into account factors such as the nature of the professional services provided and the clients served, and the geographic locations of all relevant parties.

220.6 An effective conflict identification process assists a professional accountant in public practice to identify potential conflicts prior to accepting an engagement and throughout an engagement. The earlier a potential conflict is identified, the greater the chance the professional accountant will be able to apply safeguards, when necessary, to eliminate the threat to objectivity and any threat to compliance with other fundamental principles or reduce them to an acceptable level. The process to identify conflicts of interest will vary and depend on such factors as:

- The nature of the professional services provided;
- The size of the firm;
- The size and nature of the client base; and
- The structure of the firm, for example the number and geographic location of offices, and whether the firm is a member of a network.

220.7 The professional accountant in public practice shall evaluate the significance of the threat to objectivity and any threat to compliance with other fundamental principles created by a conflict of interest and shall apply safeguards, when necessary, to eliminate the threat or reduce it to an acceptable level. It is generally necessary to disclose the nature of the conflict to the client and all known relevant parties and to obtain written consent from the client and such parties to perform the professional service. In certain circumstances the consent obtained from any relevant party may be implied by the party's conduct in keeping with common commercial practice. If the consent is obtained verbally or is implied by the party's conduct, the professional accountant is encouraged to document such consent. Examples of other safeguards include:

- Use of separate engagement teams when performing professional services for two or more clients with conflicting interests;
- Implementing mechanisms to prevent unauthorized disclosure of information when performing professional services for two or more clients with conflicting interests. This could include the creation of separate areas of practice for specialty functions within the firm, which may act as a barrier to the passing of confidential client information from one practice area to another within a firm. This could also include establishing policies and procedures to limit access to client files, the use of confidentiality agreements signed by employees and partners of the firm and/or the physical and electronic separation of confidential information; and,
- Seeking guidance of third parties, such as consulting with a professional regulatory body or another professional accountant.

220.8 In certain circumstances, requesting consent would in itself result in a breach of confidentiality. Examples of such circumstances may include:

- Performing a transaction-related service for a client in connection with a hostile takeover of another client of the firm;

- Performing a forensic investigation for a client where the firm has confidential information obtained through having performed another professional service for another client who would be the subject of the investigation.

The firm shall not accept such an engagement unless the following conditions are met:

- The firm does not act in an advocacy role for one client by assuming an adversarial position against the other client;
- Specific mechanisms are in place to prevent disclosure of information between the engagement teams serving the two clients; and
- The firm is satisfied, weighing all the specific facts and circumstances, that a reasonable and informed third party would conclude that it is appropriate for the firm to accept the engagement in the particular circumstances.

220.9 If safeguards cannot eliminate the threat to objectivity and any threat to compliance with other fundamental principles created by a conflict of interest or reduce it to an acceptable level, the professional accountant in public practice shall decline to perform or discontinue professional services that could result in the conflict of interest; or terminate certain relationships or dispose of certain interests to eliminate the conflict.

220.10 When identifying and evaluating conflicts of interest and applying appropriate safeguards, including making disclosures or sharing information within the firm or network and seeking guidance of third parties, the professional accountant in public practice shall remain alert to the fundamental principle of confidentiality.

## **SECTION 310**

*Paragraphs 310.1-310.3 and their heading would be deleted and replaced by the following heading and paragraphs 310.1-310.8:*

### **Conflicts of Interest**

310.1 A professional accountant in business may be faced with a conflict of interest when undertaking a professional activity. A conflict of interest creates a threat to objectivity and may create threats to other fundamental principles. Such threats may be created by:

- Conflicts between the interests of two or more parties for whom the professional accountant undertakes a professional activity; or
- Conflicts between the interests of the professional accountant and the interests of a party for whom the professional accountant undertakes a professional activity.

A party may include an employing organization, a vendor, a customer, a lender, a shareholder, or another party.

A professional accountant shall not allow a conflict of interest to compromise professional or business judgment.

310.2 Examples of situations in which conflicts of interest may arise for a professional accountant in business include:

- Serving on the Board of Directors of two companies and acquiring confidential information from one company that could be used by the professional accountant to the advantage or disadvantage of the other company;
- Undertaking a professional activity for each of two parties to assist them to dissolve their partnership;
- Preparing financial information for certain members of management who are seeking to undertake a management buy-out;
- Being responsible for selecting a vendor for the accountant's employing organization and an immediate family member of the professional accountant owns one of the potential vendors; and
- Serving on a Board of Directors that is approving certain investments for the company where one of those specific investments will increase the value of the professional accountant's own personal investment portfolio.

310.3 A professional accountant in business shall be alert to all interests and relationships that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances available to the professional accountant at that time, might compromise compliance with the fundamental principles.

310.4 In identifying whether a conflict of interest exists or may be created and evaluating the significance of any threat to objectivity or compliance with other fundamental principles, the professional accountant in business shall:

- Understand the nature of the relationships between the parties involved and their relevant interests;

- Understand the nature of the activity and its implications to relevant parties;
- Evaluate the significance or materiality of relevant interests or relationships;
- Evaluate the extent to which a professional activity for more than one party may result in a conflict of interest. In general, the more direct the relationship between the professional activity and the matter on which the parties' interests are in conflict, the more significant the threats may be.

When identifying and evaluating a conflict of interest, the professional accountant may wish to consult within the employing organization or with others, such as another professional accountant or a professional body.

- 310.5 The professional accountant in business shall evaluate the significance of the threat to objectivity and any threat to compliance with other fundamental principles created by a conflict of interest and shall apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level. The professional accountant shall determine whether to discuss the nature of the conflict of interest at the appropriate levels within the employing organization, where relevant. Depending on the circumstances giving rise to the conflict of interest, application of one or both of the following safeguards may be appropriate:
- Disclosing the nature of the conflict of interest to the relevant parties and obtaining their consent to undertake the professional activity. In certain circumstances consent may be implied by a party's conduct; or
  - Structuring certain responsibilities and duties to reduce the threat to an acceptable level. This could include segregation of duties or obtaining appropriate oversight.
- 310.6 If safeguards cannot eliminate the threat or reduce it to an acceptable level, the professional accountant in business shall decline to undertake or discontinue the professional activity or terminate the interest or relationship that creates the conflict of interest.
- 310.7 When identifying and evaluating conflicts of interest and applying appropriate safeguards, the professional accountant in business shall remain alert to the fundamental principle of confidentiality.
- 310.8 A professional accountant in business may encounter other threats to compliance with the fundamental principles. This may occur, for example, when preparing or reporting financial information as a result of undue pressure from others within the employing organization or financial, business or personal relationships that close or immediate family members of the professional accountant have with the employing organization. Guidance on managing such threats is covered by Sections 320 and 340 of the Code.

## SECTION 320

### Preparation and Reporting of Information

- 320.1 Professional accountants in business are often involved in the preparation and reporting of information that may either be made public or used by others inside or outside the employing organization. Such information may include financial or management information, for example, forecasts and budgets, financial statements, management's discussion and analysis, and the management letter of representation provided to the auditors during the audit of the entity's financial statements. A professional accountant in business shall prepare or present such information fairly, honestly and in accordance with relevant professional standards so that the information will be understood in its context.
- 320.2 A professional accountant in business who has responsibility for the preparation or approval of the general purpose financial statements of an employing organization shall be satisfied that those financial statements are presented in accordance with the applicable financial reporting standards.
- 320.3 A professional accountant in business shall take reasonable steps to maintain information for which the professional accountant in business is responsible in a manner that:
- (a) Describes clearly the true nature of business transactions, assets, or liabilities;
  - (b) Classifies and records information in a timely and proper manner; and
  - (c) Represents the facts accurately and completely in all material respects.
- 320.4 Threats to compliance with the fundamental principles, for example, self-interest or intimidation threats to integrity, objectivity or professional competence and due care, are created where a professional accountant in business is pressured (either externally or by the possibility of personal gain) to ~~become associated with misleading information~~ prepare or report information in a misleading way or to become associated with misleading information through the actions of others.

*Paragraph 320.5 as amended would become 320.5 and 320.6*

- 320.5 The significance of such threats will depend on factors such as the source of the pressure ~~and the degree to which the information is, or may be, misleading,~~ and the culture within the employing organization. The professional accountant in business shall be alert to the principle of integrity, which imposes an obligation on all professional accountants to be straightforward and honest in all professional and business relationships. Where the threats arise from compensation and incentive arrangements the guidance in section 340 is relevant.
- 320.6 The significance of ~~the threats~~ any threat shall be evaluated and safeguards applied when necessary to eliminate ~~them~~ the threat or reduce it ~~them~~ to an acceptable level. Such safeguards include consultation with superiors within the employing organization, the audit committee or those charged with governance of the organization, or with a relevant professional body.

*Paragraph 320.6 as amended would become 320.7*

- 320.7 Where it is not possible to reduce the threat to an acceptable level, a professional accountant in business shall refuse to be or remain associated with information the professional accountant determines is misleading. A professional accountant in business may have been unknowingly associated with misleading information. Upon becoming aware of this, the professional accountant in business shall take steps to be disassociated from that information. In determining whether there is a requirement to report the circumstances to a proper authority, the professional accountant in business may consider obtaining legal advice. In addition, the professional accountant may consider whether to resign.

## **SECTION 330**

### **Acting with Sufficient Expertise**

[No amendments made]



## SECTION 340

*The heading would be amended as follows:*

### **Financial Interests, Compensation and Incentives Linked to Financial Reporting and Decision Making**

340.1 Professional accountants in business may have financial interests, including those arising from compensation or incentive arrangements, or may ~~know-of financial interests-of~~ have immediate or close family members with such interests, that, in certain circumstances, may create threats to compliance with the fundamental principles. For example, self-interest threats to objectivity or confidentiality may be created through the existence of the motive and opportunity to manipulate price sensitive information in order to gain financially. Examples of circumstances that may create self-interest threats include situations where the professional accountant in business or an immediate or close family member:

- Holds a direct or indirect financial interest in the employing organization and the value of that financial interest could be directly affected by decisions made by the professional accountant in business;
- Is eligible for a profit related bonus and the value of that bonus could be directly affected by decisions made by the professional accountant in business;
- Holds, directly or indirectly, deferred bonus share entitlements or share options in the employing organization, the value of which could be directly affected by decisions made by the professional accountant in business;
- ~~Holds, directly or indirectly, share options in the employing organization which are, or will soon be, eligible for conversion; or~~
- ~~May qualify for share options in the employing organization or performance related bonuses if certain targets are achieved.~~
- Otherwise participates in compensation arrangements which provide incentives to achieve performance targets or to support efforts to maximize the value of the employing organization's shares, for example through participation in long term incentive plans which are linked to certain performance conditions being met.

*Paragraph 340.2 as amended would become 340.4. Paragraph 340.3 would be deleted. They would be replaced with the following paragraphs 340.2-340.3:*

340.2 Self-interest threats arising from compensation or incentive arrangements may be further compounded by pressure from superiors or peers in the employing organization who participate in the same arrangements. Such arrangements often entitle participants to be awarded shares in the employing organization at no cost to the employee provided certain performance criteria are met. In some cases these may be awarded at multiples of base salary.

340.3 A professional accountant in business shall not manipulate information, for personal gain or for the financial gain of others. The more senior the position that the professional accountant in business holds, the greater the ability and opportunity to influence financial reporting and decision making and the greater the pressure there might be from superiors and peers to manipulate information. In such situations, the

professional accountant in business shall be particularly alert to the principle of integrity, which imposes an obligation on all professional accountants to be straightforward and honest in all professional and business relationships.

340.4 The significance of any threat arising from compensation or incentive arrangements shall be evaluated and safeguards applied, when necessary, to eliminate the threat or reduce it to an acceptable level. In evaluating the significance of any threat, and, when necessary, determining the appropriate safeguards to be applied, ~~to eliminate the threat or reduce it to an acceptable level,~~ a professional accountant in business shall evaluate the nature of the ~~financial~~-interest arising from compensation or incentive arrangements. This includes evaluating the significance of the ~~financial~~-interest ~~and determining whether it is direct or indirect~~. What constitutes a significant ~~or valuable stake in an organization will vary from individual to individual, depending~~ interest will depend on personal circumstances. Examples of such safeguards include:

- Policies and procedures for a committee independent of management to determine the level or form of remuneration of senior management.
- Disclosure of all relevant interests, and of any plans to exercise entitlements or trade in relevant shares, to those charged with the governance of the employing organization, in accordance with any internal policies.
- Consultation, where appropriate, with superiors within the employing organization.
- Consultation, where appropriate, with those charged with the governance of the employing organization or relevant professional bodies.
- Internal and external audit procedures.
- Up-to-date education on ethical issues and on the legal restrictions and other regulations around potential insider trading.



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