

A Revised Section 340: Pressure to Engage in Unethical or Illegal Acts**Background**

1. The project proposal approved by the IESBA in March 2013 stated the following:

Consideration should be given to whether the motivations of professional accountants in business (PAIBs) as addressed in Section 340¹ should be expanded beyond financial interests. These motivations are closely linked to the pressure to act inappropriately in Section 320,² and in extant Section 310³ (which will be replaced by the revised provisions on conflicts of interest). Dealing with these motivations, under one heading related to pressure may make the Code clearer. This could include threats and safeguards to help the PAIB who is being pressured to act inappropriately by those in a superior position.

A senior PAIB may pressure a subordinate in relation to an accounting irregularity. Paragraph 300.5 of the Code refers to the importance of encouraging an ethics-based culture, but there is no requirement for a senior PAIB not to inappropriately pressure subordinates. Consideration should be given to whether the Code should require a senior PAIB not to inappropriately pressure subordinates.

2. It is expected that Section 340 will be deleted and replaced with a revised section addressing pressure to engage in unethical or illegal activities.”

A Structure for a Revised Section 340

3. Section 310, as revised by the Conflicts of Interest project, is consistent with the Code’s conceptual framework and provides guidance to PAIBs. It is proposed that the revised Section 340 should follow the structure used in Section 310, as revised, thus providing a framework which is consistent with the Code’s conceptual framework and other sections of the Code. The proposed structure is as follows:
 - (a) Description of pressure and linkage to fundamental principles
 - (b) Examples of pressure
 - (c) Identification of threats to compliance
 - (d) Evaluation of threats
 - (e) Application of safeguards
4. The Task Force recognizes that pressure is subjective and is influenced by the perception of the person who believes he or she is being pressured, by the subject matter of the demand and by the intentions of the person exerting the “pressure”. For example, one person could perceive a reasonable request as inappropriate pressure while another person may thrive while under pressure. Therefore, the Task Force is of the view that a “threats and safeguards” approach would better address the subjective nature of pressure than bright line requirements.

¹ Section 340, *Financial Interests*

² Section 320, *Preparation and Reporting of Financial Information*

³ Section 310, *Potential Conflicts*

5. Changes to Section 340 have been approved by the IESBA as a result of the Conflicts of Interest project but these are not effective until July 1, 2014. The Task Force expects that these pending changes to Section 340 would be superseded by this project.
6. The Task Force will also consider how those sections in Part C, such as the new Section 310 and the proposed Section 360,⁴ which focus solely on PAIBs, would fit into a revised Part C which focuses on all professional accountants, because Section 220 addresses conflicts of interest for professional accountants in public practice (PAPPs) and Section 310 addresses conflicts of interest for PAIBs. However, if Part C applies to all professional accountants, it will also apply to PAPPs. The exposure draft on responding to a suspected illegal act similarly has different sections which apply to PAPPs and PAIBs.

Matters for Consideration

1. Does the IESBA agree with the Task Force that:
 - (a) Because pressure is subjective, a threats and safeguards approach is more appropriate than a bright line/requirement/prohibition approach?
 - (b) The structure of the section addressing pressure should follow the five stage process of a description, examples, identification, evaluation and safeguards?
2. Does the IESBA have views as to how the Task Force should address those Sections of Part C, pending and proposed, that focus solely on PAIBs?

Description of Pressure and Link to Fundamental Principle(s)

7. Section 340 is currently about manipulating price sensitive information when the PAIB has financial interests. The project proposal recognizes that pressure is not limited to manipulating price sensitive information nor that financial interest is the only, or main, motive. The first paragraph of a revised Section 340 would describe pressure.
8. The Task Force considered the following matters in preparation for drafting a description of pressure:
 - Pressure could cause a breach of any of the fundamental principles (paragraph 100.5 of the Code). Pressure is not limited to objectivity. A professional accountant could be pressured to compromise integrity, confidentiality or to act without due care.
 - Paragraph 100.12 categorizes threats. Pressure may create threats which fall into any of the five categories of threat. Extant Section 340 focusses on the self-interest threat of manipulating price sensitive information for financial gain, which continues to be relevant. Intimidation threats have been identified, such as threats of job loss. Familiarity threats can arise through working closely as part of the management team. Advocacy threats can arise if the PAIB furthers the legitimate interests of the employing organization beyond an acceptable level.
 - Skepticism is expected of auditors. If a professional accountant does not apply skepticism there is a risk that he or she could facilitate financial irregularities. Professional accountants

⁴ Section 360, *Responding to a Suspected Illegal Act*

should be expected to apply skepticism in using professional judgment to determine if orders to undertake professional activities are inappropriate. The Task Force is of the view that acting without skepticism could be a breach of professional competence and due care. Accordingly, Section 130⁵ could be expanded beyond its focus on training and development, with examples included in Part C. However, this matter extends beyond pressure and is more relevant to the review of Section 300.⁶

- The Task Force considered how the Code could help a PAIB judge whether pressure is inappropriate. Describing inappropriate pressure is very difficult because whether pressure is inappropriate or not is subjective. Examples were identified where pressure was superficially inappropriate but which yielded real benefits. It was also noted that apparently reasonable pressure could be inappropriate, but disguised. Although understanding the motivation of supervisors or management when judging whether pressure is inappropriate can be helpful, it may not always be possible if the PAIB is not in a senior position or is working in a functional silo.

The Task Force does not believe any description of pressure exists that will objectively distinguish between appropriate and inappropriate pressure. It tentatively concluded that the first stage of the process would be to recognize pressure. Whether the pressure is inappropriate would be determined at the evaluation stage. The Task Force has tentatively concluded that the focus should be on pressure to engage in unethical or illegal acts, rather than on inappropriate pressure, on the grounds that pressure to engage in unethical or illegal acts is by definition inappropriate.

- Section 340 is about pressure from others to act illegally or unethically. This is different from the proposed Section 360 which is about responding to the suspected illegal acts of others. However, there may be overlap as the PAIB may face pressure to assist with, or hide, the illegal act of others.
- The matter of a professional accountant not putting inappropriate pressure on others, such as peers or subordinates, would be considered at the drafting stage.

Examples of Pressure

9. This paragraph would provide examples of pressure. Extant paragraph 310.2 (deleted by the Conflicts of Interest project) includes the following examples of pressure, which apply more specifically to Section 320.
 - Act contrary to law or regulation.
 - Act contrary to technical or professional standards.
 - Facilitate unethical or illegal earnings management strategies.
 - Lie to others, or otherwise intentionally mislead (including misleading by remaining silent) others, in particular the auditors of the employing organization or regulators.
 - Issue, or otherwise be associated with, a financial or non-financial report that materially misrepresents the facts, including statements in connection with, for example:

⁵ Section 130, *Professional Competence and Due Care*

⁶ Section 300, *Introduction*

- The financial statements;
 - Tax compliance;
 - Legal compliance; or
 - Reports required by securities regulators.
10. The examples paragraph should include examples which relate to professional accountants other than those working in traditional business roles, including:
- Public practice (subject to IESBA's guidance on the proposals in Agenda Item 4-A).
 - Government, local and /or central.
 - Not-for-profit, including government agencies, education and charities.
11. There should also be examples of accountants being pressured by non-accountants and of accountants pressuring others (both accountants and non-accountants).
12. The Task Force recognized that pressure may be intangible and also may be the result of unrealistic expectations from inside or outside the organization. The following list demonstrates the wide range of sources of pressure from which the Task Force will select around ten examples of pressure:
- Investor/analyst expectations
 - Upward pressure from management to those charged with governance
 - Next higher level of authority
 - Those charged with governance
 - Peers
 - Culture of the organization as a whole
 - Culture of a subset within the organization
 - A chain of individuals, some of whom act inappropriately and some of whom act appropriately – “pressure laundering” (e.g. a CEO applies inappropriate pressure to the CFO whose orders to a subordinate may appear to be appropriate)

Identification of threats to compliance

13. This paragraph would explain how a PAIB should identify the threats arising from inappropriate pressure. Examples of threats include:
- Financial gain
 - Fear of job loss
 - Bullying
 - Career enhancement/promotion
 - Respect for authority
 - Inappropriate targets/budgets

- Being a “team player”
- Conflict Avoidance
- Harassment

Evaluation of threats

14. This paragraph would provide guidance in determining the seriousness of the pressure to engage in unethical or illegal acts. It is noted that when under such pressure, objectivity is more difficult to achieve. This demonstrates why it is important for the professional accountant to have guidance in the Code. For example, this may include looking for support outside the organization, although it was noted that this could breach the fundamental principle of confidentiality
15. The Task Force is of the view that although it may be helpful in some instances to understand the motives of the person exerting the pressure, this may be a less reliable indicator of whether pressure is inappropriate than the professional accountant’s professional judgment of whether what is being demanded would create a threat to the fundamental principles.

Application of safeguards

16. This paragraph would provide examples of safeguards. The safeguards in extant paragraph 340.2 are specific to financial interests and linked to financial reporting and decision making. The Task Force plans to draft a wide range of safeguards, ideally mirroring the wide range of examples of pressure.

Matters for Consideration

3. Does the IESBA have any views on the Task Force’s tentative conclusions related to description, examples, identification, evaluation and safeguards with respect to pressure as set out above?