

November 2012 Staff Questions & Answers (Q&A)—Matter for Consideration

Background

1. A substantive matter has recently been raised regarding the response to Question 4 in the November 2012 IESBA Staff Q&A Publication, *Implementing the Code of Ethics, Part II*. Question 4 in the Q&A and the related staff response are as follows:

Q4. Under paragraph 290.151,¹ an individual shall not be a key audit partner for an audit client that is a public interest entity for more than seven years. After serving in such a role for seven years, paragraph 290.151 requires a two-year “time-out” period. Could that individual have a role in which he or she would have regular or ongoing contact with management or the audit committee of the client (for example, as the “client relationship partner,” “client service partner” or “senior advisory partner”) during the two year time-out period?

No. Paragraph 290.151 states that during the time-out period the individual cannot be a member of the engagement team, be a key audit partner for the client, participate in the audit of the entity, provide quality control for the engagement, consult with the engagement team or the client regarding technical or industry-specific issues, transactions, or events, or otherwise directly influence the outcome of the engagement. This would preclude having any role that would enable the individual to exercise the duties or responsibilities of someone in those positions. An individual with a high level of contact with management or the audit committee, such as a client relationship partner, would be able to directly influence the outcome of the engagement.

2. The matter has been raised by two Board members who have challenged the appropriateness of the response to this question. The matter has arisen because the response appears to imply that a “client relationship” or “advisory” partner always meets the definition of a key audit partner (KAP)² or a member of the engagement team, which it is felt would not be correct. The view held is that a relationship partner would not make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion, nor necessarily influence the outcome of the audit. It has also been argued that the fact that an individual is in a role that involves ongoing contact with management does not mean that he or she is a KAP or a member of the engagement team. Accordingly, it has been suggested that the staff’s interpretation has extended beyond the technical application of the Code.

¹ Paragraph 290.151 of the Code states the following: “In respect of an audit of a public interest entity, an individual shall not be a key audit partner for more than seven years. After such time, the individual shall not be a member of the engagement team or be a key audit partner for the client for two years. During that period, the individual shall not participate in the audit of the entity, provide quality control for the engagement, consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events or otherwise directly influence the outcome of the engagement.”

² The Code defines a KAP as follows: “The engagement partner, the individual responsible for the engagement quality control review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, “other audit partners” may include, for example, audit partners responsible for significant subsidiaries or divisions.”

3. The Planning Committee considered the matter at its March and April 2013 meetings. While generally sharing the view that the response remains appropriate, the Planning Committee acknowledged that the question posed in the Q&A document could be clarified as it seems to allow for the possibility that the “regular or ongoing contact” that is envisaged could be mere friendship, whereas the response actually suggests it would be more than friendship.
4. Staff therefore proposes the following clarifications to the Q&A, which the Planning Committee has considered and with which it concurs:
 - (a) Emphasizing that what is envisaged in the Q&A is regular or ongoing contact *in a business or professional sense*; and
 - (b) Recognizing that while a relationship partner may not necessarily influence the outcome of the audit, it is that partner’s *ability* to do so via his or her ongoing or regular business or professional contact with management, or because of the partner’s previous relationship with the client as a KAP, that is the determining factor. Because of this ability, even if that influence were never exercised in practice, it would not be appropriate under the Code for that individual to serve in a “client relationship partner” or similar capacity.
5. The proposed clarifications to the Q&A are as follows:

(Mark-up version)

Q4. Under paragraph 290.151, an individual shall not be a key audit partner for an audit client that is a public interest entity for more than seven years. After serving in such a role for seven years, paragraph 290.151 requires a two-year “time-out” period. Could that individual have a role in which he or she would have regular or ongoing business or professional contact with management or the audit committee of the client (for example, as the “client relationship partner,” “client service partner” or “senior advisory partner,” or where he or she performs non-audit services for the client) during the two year time-out period?

No. Paragraph 290.151 states that during the time-out period the individual cannot be a member of the engagement team, be a key audit partner for the client, participate in the audit of the entity, provide quality control for the engagement, consult with the engagement team or the client regarding technical or industry-specific issues, transactions, or events, or otherwise directly influence the outcome of the engagement. This would preclude having any role that would enable the individual to exercise the duties or responsibilities of someone in those positions. While an individual with a high level of contact with management or the audit committee, such as working in a “client relationship” partner role or similar capacity, may not necessarily directly influence the outcome of the engagement, that individual would be able to directly influence the outcome of the engagement have, or could be perceived to have, the ability to do so through his or her high level of business or professional contact with management or the audit committee, and because of his or her previous relationship with the client as a key audit partner. Accordingly, even if that influence were never exercised in practice, paragraph 290.151 would preclude that individual from serving in a “client relationship partner” or similar capacity.

(Clean version)

Q4. Under paragraph 290.151, an individual shall not be a key audit partner for an audit client that is a public interest entity for more than seven years. After serving in such a role for seven years, paragraph 290.151 requires a two-year “time-out” period. Could that individual have a role in which he or she would have regular or ongoing business or professional contact with management or the audit committee of the client (for example, as the “client relationship partner,” “client service partner” or “senior advisory partner,” or where he or she performs non-audit services for the client) during the two year time-out period?

No. Paragraph 290.151 states that during the time-out period the individual cannot be a member of the engagement team, be a key audit partner for the client, participate in the audit of the entity, provide quality control for the engagement, consult with the engagement team or the client regarding technical or industry-specific issues, transactions, or events, or otherwise directly influence the outcome of the engagement. This would preclude having any role that would enable the individual to exercise the duties or responsibilities of someone in those positions. While an individual working in a “client relationship” partner role or similar capacity may not necessarily directly influence the outcome of the engagement, that individual would have, or could be perceived to have, the *ability* to do so through his or her high level of business or professional contact with management or the audit committee, and because of his or her previous relationship with the client as a key audit partner. Accordingly, even if that influence were never exercised in practice, paragraph 290.151 would preclude that individual from serving in a “client relationship partner” or similar capacity.

6. The IESBA Q&A Working Group has also considered the above clarifications and generally concurs with them.
7. While agreeing that the question and the related response, as clarified, should continue to be included in the Staff Q&A publication, the Planning Committee believes the matter should be considered by the Long Association Task Force as part of the Long Association project.

Matters for Consideration

1. IESBA members are asked:
 - (a) Whether they agree with the Planning Committee’s recommendation to continue to include this Q&A in the Staff Q&A publication; and
 - (b) For views as to the appropriateness of the proposed clarifications to the Q&A above?