

Improving the Clarity of the IESBA Code—Issues Paper**A. Background**

1. At its April 2014 meeting, the Board approved a project proposal on restructuring the Code. Among other matters, the Board provided further input on the topics of clarifying responsibility for compliance with the Code's requirements; clarifying the language in the Code; reorganizing parts of the Code; and an electronic Code. A Consultation Paper was scheduled for Board approval in October 2014. In the process of drafting the Consultation paper, the Task Force has identified a number of issues on which it is seeking the views of the Board.

B. Safeguards

2. Some regulators have expressed concerns about whether safeguards in the Code are effective or enforceable. Concerns were also expressed at the May 2014 IESBA-National Standard Setters (NSS) meeting. Safeguards currently include matters that may simply help deter unethical behavior (100.16), for example educational requirements for entry into the profession (100.14). Some regulators believe that safeguards are limited to engagement-specific actions that eliminate threats, thus reducing the types and examples of safeguards used in the Code.
3. The project proposal only included safeguards in "that in reviewing the clarity of language it would be helpful to consider any significant identified inconsistencies in the Code, for example, in references to safeguards and documentation." Therefore, addressing the effectiveness of safeguards in the Code is outside the scope of this project. The proposed Strategy and Work Plan 2014-2018 includes a potential project on safeguards (see Agenda Item 3-A):

In response to regulatory feedback, the Board plans to undertake a comprehensive review of the safeguards in the Code, particularly in relation to auditor independence. The regulatory concerns revolve around the appropriateness and effectiveness of safeguards throughout the Code, the need to ensure that safeguards are appropriately correlated with threats, and the need to make clear that not every threat can necessarily be addressed by a safeguard. The Board acknowledges that there are a number of practical issues regarding safeguards. In addition, the matter concerns not only the firms that undertake the largest and most complex audits, but also SMPs including sole practitioners. The Board plans to start this new work stream with a first discussion of relevant matters for consideration in Q4 2014 and consideration of a project proposal for approval in Q1 2015.

4. The Task Force believes that safeguards should be addressed before the structure project is completed because it will have a pervasive impact.

Matter for Consideration

1. Does the Board support the timeline of a safeguards project being aligned with the timeline of the structure project?

C. Responsibility in Independence (Section 290)¹

5. The Code is largely directed at professional accountants but many engagements, particularly audit, are undertaken in the name of a firm. In order for the Code to be implemented effectively in a firm, the responsibility for compliance within the firm needs to be clearly articulated by the firm. This also facilitates enforcement of the Code's requirements. Accordingly, the Task Force believes that the Code should be clear when responsibility is at the firm level and, secondly, include a requirement for the firm to have policies and procedures to implement the Code by assigning responsibility for its provisions to particular individuals in the firm. At the May 2014 IESBA-National Standard Setters (NSS) meeting, a participant questioned whether requiring a firm to have policies and procedures would be sufficient, because this leaves the firm to decide who is responsible. Some jurisdictions are clear about who should be responsible and there was doubt as to whether the current proposals would be acceptable. It was suggested by an NSS participant that the Code should be clear about when the lead audit engagement partner is responsible.
6. The Task Force recognizes that some stakeholders do not agree that allocating responsibility to the firm and requiring the firm to have policies and procedures allocating responsibility is sufficient of itself, but is of the view that in an international code, assigning responsibility to the firm and requiring the firm to have policies to do its own assignment is appropriate. The Board was supportive of the Working Group's recommendation of assigning responsibility to the firm and requiring the firm to have policies and procedures assigning responsibility. If there is support for going further, as some national regulators have done, and in addition to the firm having responsibility for policies and procedures for the Code to assign certain additional responsibilities to engagement partners, this would be a change to the structure and nature of responsibility in the Code, which would likely require a separate project.
7. The IAASB approach to responsibility, included in International Standard on Quality Control (ISQC) 1,² is that the firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including network firm personnel) maintain independence where required by relevant ethical requirements.
8. The Code is consistent with ISQC 1 in establishing policies and procedures designed to provide reasonable assurance that the firm and its personnel comply with relevant ethical requirements. However, ISQC 1 also has additional requirements that apply to engagement partners and personnel, although there are no instances in the Code where the engagement partner is assigned responsibility for any particular action.

¹ Section 290, *Independence – Audit and Review Engagements*

² ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

9. The Task Force plans to review the positions taken by other standard setters and take these into account when finalizing its proposals and the Consultation Paper discussion.
10. The uses of the passive voice in Section 290 have been reviewed to identify who may be responsible. In many instances, it is expected that “the firm” would be the most appropriate alternative to the passive voice, thereby allowing the firm to determine whether responsibility should fall to the engagement team, engagement partner or the firm, as appropriate in the individual circumstances.
11. The Task Force believes its proposals are an improvement on the current Code and the Consultation Paper should be issued on that basis. The Task Force will consult the CAG on the extent of support for the Board’s proposals in September 2014. The Task Force believes that how the Board addresses responsibility is likely to remain a matter of continuing debate with stakeholders and is one of the main issues on which responses will be solicited.
12. The Planning Committee has considered the potential impact of addressing responsibility on the project timeline.

Matter for Consideration

2. IESBA members are asked whether they agree with the direction that the Task Force proposes and, if necessary, to take up the matter with regulators.

D. Definition of Firm³

13. The Task Force has identified that the definition of Firm may also be an issue that should be addressed. As noted above, the Code is written for individual professional accountants but the Independence section refers to firms. The definition of professional accountant in public practice includes firms and therefore it is unclear whether references to a professional accountant in public practice are to an individual or to the firm. Although not a fatal flaw, this may need to be addressed by a separate project. The Task Force currently proposes to change the references to professional accountant in public practice to either professional accountant or firm as appropriate.
14. The Task Force notes that one Board member expressed concern about the proposal in the drafting conventions to change references in the code from “professional accountant” to “accountant” because it differentiates qualified from unqualified accountants. The Task Force is continuing to consider this matter again in the context of the definition of firm, because the definition of professional accountant in public practice is also used to refer to a firm.
15. It is unclear if a possible project on the definition of firm would be an IFAC-wide issue because it is related to the definition of a professional accountant, which is an IFAC issue. A project would need to address how the Code applies to non-accountants in the firm and how the Code applies to related firms.
16. The Task Force believes it may be difficult to align the definition of firm with the IAASB Glossary of Terms as this would change the scope of the Code. The Code definition of firm is wider and more precise than that in the IAASB Glossary of Terms. Alignment of the definitions would require liaison with IAASB, possibly involving consideration of how each Board uses the definition in its standards.

³ See Appendix for definitions

E. Other Definitions⁴

17. The Task Force recommends aligning other definitions in the Independence sections with definitions in the International Standards on Auditing (ISAs). A preliminary review has identified six other differences in definitions between the Code and the IAASB Glossary of terms. The review is limited to terms in the Definitions section of the Code and the IAASB Glossary of Terms. It excludes terms which are currently defined in the body of the Code. The definitions that are not expected to be difficult to align and where IESBA may choose to follow IAASB are:
- Assurance engagement
 - Engagement quality control review
 - Financial statements
 - Special purpose financial statements
18. Alignment of the definition of “review engagement” may result in a change to the scope of the Code because IAASB refers to auditors while IESBA refers to professional accountant in public practice.
19. Differences in the definitions of “Independence” between IESBA and IAASB appear to be small nuances. It will be necessary to determine whether the nuances are fundamental or superficial before deciding on alignment.
20. The Engagement Team and Those charged with Governance definition alignments each had a separate project and due process for each change. Seven further unresolved differences between IESBA and IAASB definitions have been identified to date. To address each change with the same due process as was applied to the previous two alignments of definitions between IESBA and IAASB would not be possible within an October 2014 deadline for a Consultation Paper. Alternatively, a statement could be made that they will be addressed at a later date, either before or after the Exposure Draft in October 2015.

Matters for Consideration

3. Should this project include a comprehensive alignment of definitions between the Code and the ISAs?
4. Should the alignment precede the Consultation Paper and/or the ED?

F. Drafting Conventions

21. As the Task Force’s work proceeds, the drafting conventions will continue to evolve. Although the drafting conventions will not be published as part of the Consultation Paper, it will be essential that those consulted understand the bases on which changes to the Code are made in order to limit comments to those that are within the project. If not, those consulted may choose to comment on any matter within the Code that they wish to see changed. It will be essential to explain that the project is redrafting and not revising the Code.

⁴ See Appendix for definitions

G. Separation of Sections 290 and 291⁵

22. Integrating Sections 290 and 291 may reduce duplication and the length of the Code. Section 290 addresses auditor independence for audit and review engagements. Section 291 addresses auditor independence for other assurance engagements. Prior to 2009, the Code combined audit and other assurance engagements' independence provisions in one section. The Ethics Board approved the separation because "this split provides more direct and understandable guidance for those who perform only audit and review engagements." However, it does repeat much similar text which makes the Code longer. Although the length of the Code is not a problem in an electronic Code that allows navigation to the relevant section, it remains an issue for a paper version of the Code.
23. Integrating 291 with 290 would combine audit and review with assurance for public interest entities (PIEs) and non-PIEs in one section and so create long and complex wording that is more difficult to understand and translate. As restructured in this way, the Code would start with assurance as a base (the "minimum" requirement) that applies to all assurance engagements, then add requirements for audits/reviews where necessary as a separate 'layer' of additional requirements and then requirements for audits of PIEs as another layer. One difficulty with this approach is that there are also a few areas where an "assurance" requirement applies ONLY to an assurance engagement that is NOT an audit or review, because a similar but "not layered" requirement applies to an audit or review (for example, addressing a breach or holding a financial interest as a trustee or acquiring a financial interest unintentionally). In these cases, the examples describe the provisions as applying to "assurance engagements that are not audit or review engagements" and not simply as applying to "assurance engagements." Understanding this "layering" is fundamental to applying the combined sections properly, and although professional accountants in some jurisdictions are familiar with this approach, others may find it more confusing.
24. Integrating Section 291 with Section 290 would also make it more difficult for jurisdictions that have responsibility only for audit engagements to extract the relevant text.
25. The Task Force has reviewed this matter and recommends that Sections 290 and 291 remain separate because:
 - Merging the two sections creates greater levels of complexity and this project is aiming to clarify the Code;
 - Greater levels of complexity would make translation more challenging;
 - A split provides more direct and understandable guidance for those who perform only audit and review engagements or only assurance engagements;
 - The major benefit of combined sections would be to reduce duplication and unnecessary length in the Code, but the Task Force notes that length is of less concern with an electronic Code.

Matter for Consideration

5. IESBA members are asked whether they agree with maintaining the separation of Section 290 and Section 291.

⁵ Section 291, *Independence – Other Assurance Engagements*

H. Renumbering of Sections

26. The current numbering of the Code paragraphs is not conducive to changes to Section 290. The Task Force proposes changing the current numbering methodology and references to Parts A, B C and D to a sequential numbering system that preserves the individual numbering through 100 and 200:
- 100 is Part A
 - 200 is Part B 200 to 280
 - 300 is Part C
 - 400 is Part D which derives from the extant audit independence provisions (s.290)
 - 500 is Part D which derives from the extant assurance independence provisions (s. 291)
27. The examples in Agenda Paper 5-C use the proposed renumbering system.
28. The order of the sections was chosen to allow the Independence provisions to remain part of the Code but facilitate its separation if that were the wish of a jurisdiction or Board in the future. This resulted in Part C sitting between Part B and Independence. It is unhelpful to users to bifurcate the parts relevant to professional accountants in public practice with Part C in the middle, but the Task Force was mindful of the decision of the Board to defer to a later date a decision as to whether Part C is relevant to all professional accountants and therefore follow Part A.

Matter for Consideration

6. IESBA members are asked whether they support renumbering the Code.

I. Additional Matters Identified in Restructuring the Code

29. The Task Force draws the following matters to the notice of the Board:
- The phrase “professional accountant or firm” is used in the examples to replace “professional accountant in public practice” in some provisions in the restructured Code to avoid using “professional accountant” when it means “firm.” However, the Task Force finds this term ungainly and will reconsider the use of professional accountant; professional accountant in public practice and firm in the search for wording that avoids using one word to mean itself and another word, but is also clear.
 - Extant paragraph 210.14 “generally need to obtain the client’s permission” is not clear whether it is a requirement for a prospective professional accountant to obtain a client’s permission to initiate a discussion with the existing accountant unless there are overriding reasons not to do so, or if it might be a good idea to ask to speak to the existing accountant.
 - Revised paragraph 110.14 states: “Paragraph 110.006(a) requires a professional accountant or firm to evaluate any threats to compliance with the fundamental principles when the professional accountant or firm knows, or could reasonably be expected to know, of circumstances that may compromise compliance with the fundamental principles.” The Task Force is concerned that this might be read as meaning that the professional accountant has to take into account all information known to the firm. Although the extant wording might be read as applying to the firm as well as the professional accountant, the revised wording

seems to place more emphasis on this being potentially a firm-wide evaluation. The Task Force preference is to be consistent in using professional accountant throughout.

- The Task Force has noted that the content of paragraph 110.021 (extant paragraph 100.18) is rather irrelevant in an ethics code. In particular, it is obvious to state that the relevant facts, alternative courses of action or consultation with appropriate persons may be relevant to the resolution process. The Task Force would prefer to include it in the introduction but this would be a change to the meaning of the Code.
- Paragraph 400.001 sets out the purpose of the Independence Section: “Independence is linked to the fundamental principle of objectivity, but in the context of this Code, it is possible for independence to be compromised while objectivity remains uncompromised.” The Task Force believes that this goes beyond the meaning of the extant Code and will continue to address this paragraph.
- Paragraph 420.004b may be a change in meaning to extant paragraph 290.126. The Task Force intends to address this further.

Matter for Consideration

7. The Task Force requests comments from the Board on the above additional matters identified in restructuring the Code.

Appendix

Definitions

	IESBA Definition	IAASB Definition
Firm	<p>(a) A sole practitioner, partnership or corporation of professional accountants;</p> <p>(b) An entity that controls such parties, through ownership, management or other means; and</p> <p>(c) An entity controlled by such parties, through ownership, management or other means.</p>	<p>A sole practitioner, partnership or corporation or other entity of professional accountants.</p> <p>(ISQC 1 references the IESBA definition of firm and users are instructed to apply the IESBA definition in complying with relevant ethical requirements in ISQC1.</p>
Independence	<p>Independence is:</p> <p>(a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism</p> <p>(b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit or assurance team's, integrity, objectivity or professional skepticism has been compromised.</p>	<p>Comprises:</p> <p>(a) Independence of mind—the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.</p> <p>(b) Independence in appearance—the avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.</p>
Assurance engagement	An engagement in which a professional accountant in public practice expresses a conclusion	An engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of

	IESBA Definition	IAASB Definition
	designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria.	the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. The outcome of the evaluation or measurement of a subject matter is the information that results from applying the criteria (also see <i>Subject matter information</i>). Under the <i>International Framework for Assurance Engagements</i> there are two types of assurance engagement a practitioner is permitted to perform: a reasonable assurance engagement and a limited assurance engagement
Engagement quality control review	A process designed to provide an objective evaluation, on or before the report is issued, of the significant judgments the engagement team made and the conclusions it reached in formulating the report.	A process designed to provide an objective evaluation, on or before the date of the report, of the significant judgments the engagement team made and the conclusions it reached in formulating the report. The engagement quality control review process is for audits of financial statements of listed entities and those other engagements, if any, for which the firm has determined an engagement quality control review is required
Financial statements	A structured representation of historical financial information, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term can relate to a complete set of financial statements, but it can also refer to a single financial statement, for example,	A structured representation of historical financial information, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term "financial statements" ordinarily refers to a complete set of financial statements as

	IESBA Definition	IAASB Definition
	a balance sheet, or a statement of revenues and expenses, and related explanatory notes.	determined by the requirements of the applicable financial reporting framework, but it can also refer to a single financial statement
Special purpose financial statements	Financial statements prepared in accordance with a financial reporting framework designed to meet the financial information needs of specified users	Financial statements prepared in accordance with a special purpose framework. <i>(Special purpose framework—A financial reporting framework designed to meet the financial information needs of specific users. The financial reporting framework may be a fair presentation framework or a compliance framework).</i>
Review engagement	An assurance engagement, conducted in accordance with International Standards on Review Engagements or equivalent, in which a professional accountant in public practice expresses a conclusion on whether, on the basis of the procedures which do not provide all the evidence that would be required in an audit, anything has come to the accountant's attention that causes the accountant to believe that the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework.	The objective of a review engagement is to enable an auditor to state whether, on the basis of procedures which do not provide all the evidence that would be required in an audit, anything has come to the auditor's attention that causes the auditor to believe that the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework.