

## Agenda Item

# 1-F.1

**Meeting:** IESBA Meeting  
**Meeting Location:** New York, USA  
**Meeting Date:** June 27-19, 2016

**Draft Minutes<sup>1</sup> of the Public Session of the Meeting of the  
INTERNATIONAL ETHICS STANDARDS BOARD FOR ACCOUNTANTS CONSULATIVE  
ADVISORY GROUP (CAG)**

**Held on March 7, 2016**

**Paris, France**

### **PRESENT**

Kristian Koktvedgaard (Chair)

Vânia Borgerth

Nicolaas van der Ende

Mohini Singh

Matthew Waldron

Dr. Juan-Maria Arteagoitia

Noémi Robert

Myles Thompson

Erik Bradbury

Francis Nicholson

Jean-Luc Michel

Atsushi Ilnuma

Nigel James

Huseyin Yurdakul

Jim Dalkin

### **Member Organizations**

BusinessEurope

Associação Brasileira de Instituições Financeiras de  
Desenvolvimento

Basel Committee on Banking Supervision (Basel Committee)

CFA Institute

CFA Institute and IAASB CAG Chairman

European Commission (EC)

Fédération des Experts Comptables Européens (FEE)

FEE

Financial Executives International (FEI)

Institute of Internal Auditors (IIA)

International Association of Financial Executives Institutes – Europe,  
Middle East, and Africa Region (IAFEI-EMEA)

International Organization of Securities Commissions (IOSCO)

IOSCO

IOSCO

International Organization of Supreme Audit Institutions (INTOSAI)

<sup>1</sup> The draft minutes are for information only. The IESBA CAG has not yet reviewed them. It will approve them at its September 2016 meeting.

**PRESENT**

Jaseem Ahmed

Sherif Ayoub

Gaylen Hansen

Lucy Elliott

Irina Lopez

Wei Meng

Simon Bradbury

Dawn McGeachy-Colby

**Member Organizations**

Islamic Financial Services Board (IFSB)

IFSB

National Association of State Boards of Accountancy (NASBA)

Organisation for Economic Cooperation and Development (OECD)

World Bank (WB)

World Federation of Exchanges (WFE)

**Observer Organizations**

International Monetary Fund (IMF)

IFAC Small and Medium Practices (SMP) Committee

**IESBA Members and Staff**

Dr. Stavros Thomadakis

Richard Fleck

Gary Hannaford

James Gunn

Ken Siong

Diane Jules

Kaushal Gandhi

IESBA Chairman

IESBA Deputy Chair

IESBA Member

Managing Director, Professional Standards

Technical Director

Deputy Director

Manager, Standards Development and Technical Projects

**Public Interest Oversight Board (PIOB)** Michael Holm

**APOLOGIES**

Marie Lang

Dr. Obaid Saif Hamad Ali Al Zaabi

Anne Molyneux

Patricia Miller

Sanders Shaffer

Anusha Mohotti

Lillian Ceynowa

**Member Organizations**

European Federation of Accountants and Auditors for SMEs (EFAA)

Gulf States Regulatory Authorities (GSRA)

International Corporate Governance Network (ICGN)

IIA

International Association of Insurance Supervisors (IAIS)

Sri Lanka Accounting and Auditing Standards Monitoring Board (SLAASMB)

**Observer Organization**

U.S. Public Company Accounting Oversight Board

## A. Opening Remarks

Mr. Koktvedgaard opened the public session, welcoming Representatives and thanking the OECD for hosting the meeting at their offices. He welcomed in particular Mr. Holm as the PIOB Observer; Dr. Thomadakis, the IESBA Chairman; Mr. Fleck, the new IESBA Deputy Chair; Mr. Nicholson, interim alternate for the IIA and new CAG Representatives: Messrs. van der Ende for the Basel Committee and E. Bradbury for the FEI, and Ms. Meng for the WFE. He also welcomed the official observers: Mr. S. Bradbury, for the IMF and Ms. McGeachy-Colby for the IFAC SMP Committee.

Mr. Koktvedgaard welcomed the opportunity for the CAG to meet outside the US, noting this as an opportunity to highlight the CAG as a global body and to undertake outreach to stakeholders within the EU. He noted that going forward, every third CAG meeting will be held outside the US. He also noted that he had worked closely with the IAASB CAG Chair in arranging a joint session with the IAASB CAG on Tuesday, March 8, 2016 regarding the topics of non-compliance with law and regulation (NOCLAR) and professional skepticism, and to receive a presentation, *The OECD Anti-Bribery Convention: Perspectives for Accountants and Auditors*.

The minutes of the September 2015 CAG meeting were approved as presented.

## B. Safeguards

### REPORT BACK ON SEPTEMBER 2015 DISCUSSION

Mr. Hannaford summarized the IESBA's proposals in the Exposure Draft, *Proposed Revisions Pertaining to Safeguards in the Code – Phase 1* (Safeguards ED-1).<sup>2</sup> He reminded the CAG that the purpose the project is to review the clarity, appropriateness and effectiveness of safeguards in the extant Code, including those safeguards that pertain to non-audit services (NAS) in Section 290.<sup>3</sup> He added that the proposals in Safeguards ED-1 were drafted in the proposed new structure and drafting conventions developed under the Structure of the Code project and took into account the feedback provided by the CAG at its September 2015 meeting.

Representatives complimented the IESBA on reaching a significant milestone. The following matters were raised:

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<sup>2</sup> The Safeguards ED-1 includes:

- Enhancements aimed at clarifying the conceptual framework (CF) by shifting the professional accountant's (PA's) focus to identifying, evaluating and addressing threats to compliance with the fundamental principles rather than just seeking to apply safeguards.
- New requirements in proposed Section 120 that more explicitly direct PAs to identify, evaluate and address threats to compliance with the fundamental principles.
- A requirement for PAs to re-evaluate those threats if new information becomes available, or if facts and circumstances change.
- An improved description of the following terms and concepts:
  - Reasonable and informed third party;
  - Acceptable level; and
  - Safeguards.
- A new requirement for the PA to perform an overall assessment (i.e., "step back") by reviewing judgments made and overall conclusions reached to determine that threats to compliance with the fundamental principles are eliminated or reduced to an acceptable level and that no further action is needed.

<sup>3</sup> Extant Section 290, *Independence – Audit and Review Engagements*

- Mr. Hansen and Ms. McGeachy-Colby complimented the Task Force on its thoughtful and thorough work. Ms. McGeachy-Colby indicated that the SMPC would be formally responding to the Safeguards ED-1. Referring to the response to a query from Ms. Lang in the Report Back section of the agenda materials regarding the description of a “reasonable and informed third party,” Mr. Hansen asked for further elaboration about the Task Force’s rationale for the use of the word “could” rather than “should” in the phrase “...This evaluation entails weighing all the relevant facts and circumstances that the accountant knows, or could reasonably be expected to know, at the time ....” He wondered why the bar was felt to be too high with the word “should” as he believed that professional accountants (PAs) should be expected to know as opposed to its being probable that they would know. Mr. Hannaford responded that the IESBA considered both words, and concluded that the intended work effort implied by the word “could” (currently used in the extant Code) remains appropriate. Nevertheless, the Task Force would consider the feedback from respondents on this particular point. Ms. McGeachy-Colby supported Mr. Hannaford’s explanation, noting that in some jurisdictions, the word “should” could be read to mean “shall.” As such, in her view the word “could” achieved an appropriate balance.
- Referring to the discussion about explicit requirements, Mr. Hansen wondered whether it would be useful for the Code to include a number of explicit prohibitions. Mr. James agreed, noting that the current approach seems to be for PAs to first seek to apply safeguards to address threats to compliance with the fundamental principles, as opposed to a mindset that would preclude consideration of safeguards if a relationship, interest or service is prohibited. Mr. Hansen concurred, noting that there are situations where the threats are so significant that PAs should not even perform the work. Acknowledging the points raised, Mr. Hannaford highlighted paragraph 120.7 A1 of Safeguards ED-1 which already states that there are some situations where the threat created would be so significant that no safeguards could reduce the threat to an acceptable level. He explained that Phase 2 of the project pertaining to NAS will deal with the prohibitions in the Code. Mr. Siong reminded Representatives that the Code already includes specific prohibitions for certain situations, and highlighted some examples of these prohibitions.
- Mr. Ahmed suggested that the IESBA consider mapping the key concepts that are included in the fundamental principles and conceptual framework (CF) (i.e., Part A of the Code) to the concepts that appear in subsequent sections of the Code (i.e., Parts B and C). For example, he questioned:
  - Why objectivity and integrity are included as fundamental principles, but not professional skepticism. He wondered whether the IESBA believed that professional skepticism was already covered within the fundamental principles of objectivity and integrity.
  - The IESBA’s rationale for including a reference to objectivity in the breaches to independence section of the Code, but not to integrity and professional skepticism.

Mr. Hannaford responded that the fundamental principles are the same as those included in the extant Code. He added that the IESBA is mindful that auditors are required to exercise professional skepticism in planning and performing audits of financial statements. He then highlighted the paragraphs in proposed Section 400 that deal with independence, objectivity and professional skepticism.

## PHASE 2 – PROPOSED CONSEQUENTIAL AMENDMENTS ARISING FROM SAFEGUARDS ED-1

### *Application of the CF to Independence – Proposed Section 400<sup>4</sup>*

Mr. Hannaford noted that consequential amendments were needed to some of the proposals in the Exposure Draft, *Improving the Structure of the Code of Ethics for Professional Accountants – Phase 1* (Structure ED-1) as a result of the Safeguards project.<sup>5</sup> He then drew the CAG's attention to the sections in the Structure ED-1 that addressed questions that had been raised by some CAG Representatives about the link between independence and the fundamental principles, in particular objectivity.<sup>6</sup> He explained that the Task Force was of the view that the provisions set out in Safeguards ED-1 (i.e., proposed Sections 120<sup>7</sup> and 300<sup>8</sup>) pertaining to threats to compliance with the fundamental principles should also apply with respect to threats to independence. He added that the Safeguards and Structure Task Forces were of the view that further revisions would be needed in the CF (i.e., proposed Section 120) to make it clear to users of the Code that the provisions in proposed Section 120 also apply with respect to threats to independence. He noted that the Task Forces believed that this wording could be:

“PAs are required to apply the CF in order to comply with the fundamental principles in a wide variety of roles and circumstances. ...Part C, *Professional Accountants in Public Practice*, including the International Independence in C1 and C2, set out additional requirements for applying the CF.”

Mr. Hannaford further explained that the Task Force believed that the overarching requirement to apply the CF set out in proposed Section 400 should also be supplemented by stand-alone provisions, drawing from the proposed requirements and application material in proposed Section 120 in order to emphasize how they apply in the context of threats to independence.<sup>9</sup>

Representatives generally expressed support for the Task Force's suggested consequential amendments to proposed Section 400. The following matters were raised:

- With respect to the Task Force's proposal to repeat certain provisions in proposed Section 400 that already exist in proposed Section 120, Ms. McGeachy-Colby expressed the view that anything important is worth repeating. Mr. Dalkin and Ms. Singh agreed.

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<sup>4</sup> Proposed Section 400, *Application of Conceptual Framework to Independence for Audit and Review Engagements*

<sup>5</sup> The Task Force suggested consequential amendments principally to proposed Section 400 of the Structure ED-1.

<sup>6</sup> See paragraphs 3 of the proposed Guide, and proposed paragraphs 112.A1 and 400.1–400.2 of the Structure ED-1. Those paragraphs correspondent to paragraphs 290.1, 280.2 and 290.4 of the extant Code.

<sup>7</sup> Proposed Section 120, *The Conceptual Framework*

<sup>8</sup> Proposed Section 300, *Application of the Conceptual Framework Approach by Professional Accountants in Public Practice*

<sup>9</sup> The Task Force believed that the consequential amendments to proposed Section 400 should include:

- A requirement for firms to perform an overall assessment by reviewing judgements made and overall conclusions reached to determine that threats to independence are eliminated or reduced to an acceptable level and that no further action is needed (i.e., a step-back provision).
- New application material to:
  - Explain that threats to independence are similar to threats to the fundamental principles;
  - Reinforce the importance of the reasonable and informed third party test in the context of dealing with threats to independence; and
  - Assist firms better evaluate threats to independence.

- Referring to the Report-Back on the September 2015 CAG discussion, Mr. Nicholson questioned whether the point raised by Ms. Miller regarding the distinction between independence and objectivity had been appropriately addressed.<sup>10</sup> Mr. Hannaford explained how the Task Force proposed to link the two concepts, inviting the CAG to respond to this proposal in Safeguards ED-1. Mr. Nicholson commented that the point was not so much the link between the two but rather the distinction between them. In his view, it is not appropriate for the Code to characterize threats to objectivity and threats to independence as being the same. He noted that the IIA standards make clear that these two concepts are different but equally important. He suggested that objectivity could be referred to as a state of mind. In contrast, independence is more about reporting lines, etc. He noted as example that a threat to objectivity could be time pressure whereas a threat to independence could be a conflict of interest.
- Mr. Ahmed wondered what the statement “independence is a measure of objectivity” in paragraph 400.1 meant. He commented that one could think about something that is intrinsically valuable, such as independence. One could also think about something that is intrinsically instrumental. He felt that there was a need to clarify the distinction. Mr. Yurdakul noted his personal view that independence should be a fundamental principle in the Code, in particular as it relates to audits of financial statements. He felt that subordinating independence to objectivity did not put the right focus on it, and it may be perceived as being less important. He added that in his view independence should not be linked to just objectivity, but also to integrity and professional skepticism. Mr. Hannaford acknowledged the comments raised and noted that they would be considered together with the feedback on the Structure ED-1.
- Mr. Yurdakul observed that the IESBA distinguishes requirements with an “R”, and application material with an “A”. He suggested that the IESBA consider distinguishing introductory or contextual information with an “I” so that it would be clear that that material is for information purposes. He also questioned the rationale for including application material to support some requirements but not others. Mr. Hannaford responded that the Task Force was following the Structure drafting guidelines. He also noted that proposed Section 400 is not a standalone section but must be read with the rest of the Code.
- Mr. Bradbury of IMF commented on the Task Force’s suggested wording in paragraph R400.11, “In deciding whether to accept or continue an audit engagement, or whether an individual may be an audit team member, the firm shall identify threats to independence,” noting that independence should be evaluated on an ongoing basis and not only when considering acceptance or continuance of an audit engagement.

#### *Communicating with Those Charged with Governance (TCWG)*

Mr. Hannaford noted that the Code acknowledges that requirements for communication between the firm and TCWG about independence matters may exist in applicable professional standards,<sup>11</sup> law or regulation.<sup>12</sup> He added that the Code encourages, but does not require such communication. He then asked Representatives for views about whether the Code should explicitly require auditor communication with TCWG about independence matters and whether such requirements should be aligned to the

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<sup>10</sup> See paragraph 3 of the Guide and paragraphs 112.A1 and 400.1–400.2 in Structure ED-1.

<sup>11</sup> For example, the IAASB’s ISA 260 (Revised) includes provisions, for audits of listed entities only, for auditors to communicate with TCWG about independence matters.

<sup>12</sup> See proposed R400.15 of Structure ED-1, formerly paragraph 290.28 of the extant Code.

provisions in the ISAs (i.e., apply to listed entities only).

Representatives generally expressed support for having more robust provisions in the Code for auditor communication with TCWG. The following matters were raised:

- Mr. van der Ende noted that it is important to consider enhancements to auditor communication with TCWG about the audit more broadly as the role of TCWG is becoming increasingly important in all types of activity and not just with respect to independence. He also agreed with the Task Force that consideration of possible enhancements to requirements for auditor communication with TCWG should involve close coordination between the IESBA and the IAASB in order to develop a common approach. With respect to the specific questions raised by the Task Force, Mr. van der Ende suggested that the IESBA spend more time to carefully consider the varying perspectives, including:
  - Whether the Code should require auditor communication about independence matters and whether those requirements should be for audits of listed entities, public interest entities (PIEs) or all entities.
  - How the provisions in the Code should accommodate the unique considerations for the various types of organizations and corporate governance structures, including SMEs that may not necessarily have a separate governance function in place.
- Mr. James agreed with Mr. van der Ende and suggested that in deciding the extent to which the IESBA should align with the IAASB, there should be an understanding of how the extant provisions are being applied in practice. He added that the IESBA should form a view about the specific matters that auditors should communicate to TCWG, and explore whether the extant provisions that encourage communication about independence matters is facilitating those communications. In this regard, he suggested that obtaining an understanding of the implications in those jurisdictions that have adopted the IESBA Code but not IAASB standards, and vice versa, would be particularly important. Mr. Ahmed questioned whether the need for the Code to be aligned with IAASB standards is a practical or real issue. Mr. Hannaford acknowledged the viewpoints, noting the particular challenge in obtaining information regarding the implementation of specific provisions. Further, while such information might be sourced from regulatory inspections, such inspections tend to focus on PIEs. He also clarified that the Task Force is not seeking to develop proposals that would be in conflict with IAASB standards.
- Mr. Ayoub felt it important to maintain consistency with the ISAs. He also felt that a differential approach could be taken, with a requirement with respect to PIEs but an encouragement with respect to entities that are not PIEs.
- In relation to the matter of alignment with ISAs, Mr. Hansen advised the IESBA to deal with what is within its purview. He added that as a matter of principle, if auditor communication with TCWG is important for PIEs, it should be equally important for all other entities. However, the communication could be less formal for the latter. Ms. McGeachy-Colby agreed, noting a concern about the need for potential conforming amendments to IAASB standards and the need to educate SMPs. Mr. Hannaford responded that there the IESBA is aware of implementation challenges that exist, in particular for SMPs, because for some organizations that they audit, a separate governance function may not exist.

- Mr. Dalkin felt that intellectually the communication principle should apply to all entities. He noted that public sector entities generally do not have audit committees. Accordingly, some guidance would be needed as to how to identify TCWG for such entities.
- Ms. Robert commented that from an EU perspective, enhanced communication between auditors and TCWG would be welcome, noting that the EU audit legislation already would require such communication. She cautioned that consideration should be given to varying corporate governance structures across jurisdictions when exploring changes to auditor communication with TCWG, as such communications are most effective with proper corporate governance structures.
- Mr. Bradbury of FEI believed that auditor communication with TCWG should apply with respect to all entities, viewing such communication as a protection for the entities themselves. He felt it important to think about *what* auditors should communicate.
- Mr. Ahmed agreed that communication with TCWG is an important topic. He noted that the extant Code contained a clear requirement as to how to communicate with TCWG about breaches in independence. He wondered whether this would strengthen or weaken the argument as to whether to require communication with TCWG. He was not persuaded that there should not be a communication requirement. In relation to the matter of consistency with the ISAs, he wondered why the IESBA would find it difficult to align the Code with the ISAs on this topic if the IESBA felt it sufficiently important to articulate these communication principles. Mr. Hannaford explained that the Code includes separate provisions in the proposed Section 404<sup>13</sup> for breaches of independence requirements. He added that the Task Force's suggestions pertain to those situations when there has not been a breach of an independence requirement. He accepted that a cross reference in proposed Section 400 to the relevant paragraphs in proposed Section 404 that deal with auditor communication with TCWG about breaches might be useful. Mr. Koktvedgaard added that there is a need to also consider the information needs of the entity.

#### *Documentation*

Mr. Hannaford noted that the Task Force was considering further consequential changes, including to further improve the proposed requirements for firms to document their conclusions regarding the independence requirements in paragraph R402.2.

The following matters were raised:

- Mr. Dalkin shared his perspectives about the benefits that have flowed from requiring documentation for audits of public sector entities. He expressed support for the Code to include an explicit requirement for firms to document *how* they have reached their conclusions with respect to the application of the CF to independence. He explained that the Code for public sector entities currently includes a similar requirement. Mr. Hannaford noted that paragraph R402.2 would address Mr. Dalkin's comment. Mr. Hansen expressed support for paragraph R402.2, adding that from his experience as a regulator it is not helpful if there is a lack of clarity regarding documentation.
- Mr. James was of the view that the proposed wording in paragraph 402.2 A1, "A lack of documentation does not determine whether a firm considered a particular matter or whether a firm is independent as required by C1," can be perceived by regulators as being defensive for the firms even if not so intended. He suggested that the IESBA consider revising it to be more neutral. He

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<sup>13</sup> Proposed Section 404, *Breach of an Independence Provision*



also felt that there should be greater clarity that paragraph R402.2 requires the documentation of all the conclusions, not only when these are significant, as the proposed wording seemed to send mixed signals.

## PHASE 2 – ISSUES AND TASK FORCE RECOMMENDATIONS PERTAINING TO SAFEGUARDS IN THE NAS SECTION OF THE CODE

Mr. Hannaford presented the Task Force's recommendation and its plans for revising the NAS section of the Code. He noted that the Task Force had done an extensive review of the extant NAS section of the Code. He then described the Task Force's preliminary views about the improvements that should be made to clarify the principles and criteria for determining acceptable levels of threats created from providing a NAS to an audit client.

The following matters were raised:

### *Principles and Criteria*

- Mr. Hansen was supportive of the Task Force's proposals, but noted that a question that continues to arise is how long a firm should cool off before coming back to provide the same NAS to the audit client. He added that this question might be outside the scope of this project but welcomed views on it. Mr. Hannaford pointed to proposed requirements and application material for engagement periods in paragraphs R400.17–400.19 A1.
- Mr. Dalkin noted that how a NAS should be described is an interesting question. He noted that in the public sector environment, there is a question as to whether auditor preparation of financial statement disclosures when management does not have the requisite expertise is a NAS or a part of the audit. Mr. Hannaford explained that this scenario is prohibited under the extant Code for PIEs and that the Task Force was not proposing to withdraw any of the existing prohibitions in the Code. He added that there is already guidance in the Code regarding what is considered to be of a routine or mechanical nature.
- Mr. Koktvedgaard noted that it is important for the IESBA to consider how its provisions pertaining to provisions of NAS to audit clients compare to ethical requirements in other jurisdictions.
- Mr. Thompson suggested that there be clarity regarding the distinction between non-audit and non-assurance services.

### *Materiality*

- Mr. James questioned how the IESBA determined the permissibility of a NAS from a materiality perspective. He also questioned why a reference is made to materiality in describing circumstances that create self-review threats, but not advocacy threats created for example by promoting, dealing in, or underwriting an audit client's shares. Ms. Soulier explained that the Task Force is of the view that for some threats such as a self-review threat, materiality is always a relevant factor in evaluating the level of the threat. However, in other cases, such as advocacy and self-interest threats, a more qualitative evaluation and scalable approach is needed given the stronger perceptions and the fact that it may not be practicable to consider materiality (for example, promoting an audit client's shares). Mr. Koktvedgaard noted that the Code there is already some scaling built into the Code, such as a prohibition in the preparation of accounting records for PIEs but not for other entities. He suggested that consideration could be given to providing guidance on factors to take into account. Mr. Hannaford agreed noting that the Task Force plans to consider

whether further guidance is needed in the Code to assist PAs in making this evaluation.

*Other Matters, Including Communication with TCWG about NAS Provided to an Audit Client*

- Mr. Inuma noted that the more a firm is global, the more its systems should monitor compliance with independence requirements. Accordingly, he suggested that the list of matters a firm should communicate to TCWG should include the systems and processes for monitoring compliance with independence requirements.
- Mr. James also noted that the list of what a firm should communicate to TCWG should include breaches to independence requirements arising from providing NAS to an audit client. He also expressed support for the planned outreach efforts and suggested that the IESBA engage in dialogue with TCWG, in particular audit committee members, as they will be impacted by the proposed changes.

PIOB OBSERVER'S REMARKS

Mr. Holm complimented the Task Force on its progress to-date, noting in particular the areas flagged for further coordination with the IAASB. He felt that 2016 would be a year of coordination and encouraged the IESBA to actively engage in dialogue with the IAASB as it progresses its projects.

WAY FORWARD

Mr. Hannaford thanked the Representatives for their input, noting that the Task Force would take into account the responses to Safeguards ED-1 in advancing the proposals for Phase 2. He noted that the IESBA would discuss the agenda material at its March 2016 meeting.

**C. Emerging Issues**

INSTITUTE OF CHARTERED ACCOUNTANTS OF SCOTLAND'S (ICAS) POWER OF ONE INITIATIVE<sup>14</sup> AND RELATED DISCUSSION PAPER

Mr. James Barbour, Director of Technical Policy at ICAS, introduced the topic by outlining the genesis of the "Power of One" initiative and the ICAS proposals. These proposals include a suggestion for the Code to include a new fundamental principle – moral courage. He explained that ICAS had commissioned research to inform its project. This research indicated that based on real life ethical dilemmas, there appears to be a lack of ethical leadership and personal responsibility within the accountancy profession. In response, ICAS took on the initiative with a view to helping shape individual PAs' ethical decisions and values.

Representatives expressed support for ICAS's efforts and provided a few editorial suggestions. They also asked questions about various aspects of ICAS' initiative, including the nature and extent of the research performed; and whether ICAS had considered issues around enforceability in developing its proposals.

With respect to the proposal to introduce moral courage as a new fundamental principle, the following matters were raised:

- Mr. Waldron noted that the CFA Institute had launched a significant campaign to emphasize the importance of ethics. He wondered how to raise the awareness of the general public regarding

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<sup>14</sup> An overview of the ICAS' *The Power of One* initiative is available at:  
[https://www.icas.com/\\_data/assets/pdf\\_file/0006/220110/ICAS-The-Power-Of-One.pdf](https://www.icas.com/_data/assets/pdf_file/0006/220110/ICAS-The-Power-Of-One.pdf)

what is now required of PAs. He acknowledged that besides PAs, there are others who also have a responsibility to contribute to quality financial reporting.

- Mr. Ahmed expressed support for recognizing the value of ethical conduct. He also expressed support for the proposals, noting a need to move to a world where there would be zero tolerance for moral laxity and where individuals would stand up to ethical issues.
- Mr. S. Bradbury expressed the view that “moral courage” is the missing piece of the jigsaw. However, he questioned the latter part of the proposed definition. He agreed that there is a need to exert courage to resist personal exploitation. He also highlighted a link to the fundamental principles of integrity and professional behavior.
- Mr. Ahmed noted that feedback from the IFSB’s constituencies indicates a need to address issues around remuneration, particularly incentives to achieve specific targets.
- Mr. Koktvedgaard wondered how ICAS had identified the concept of moral courage and whether professional skepticism should be treated in a similar vein. He also wondered why ICAS was not suggesting any change to the fundamental principle of professional competence and due care in the Code. In his view, in order for a PA to act with moral courage, it would be necessary for that individual to be competent. Mr. Barbour explained that there have been valid arguments for embedding the concept of moral courage within the existing fundamental principles. However, ICAS was of the view that treating moral courage as a separate fundamental principle would be the best way to give the concept the emphasis it needs.
- Mr. Thompson observed that the concept of “moral courage” is relevant to whistleblowing. In that regard, he was of the view that it would be useful for law and regulation to establish provisions that protect whistleblowers. Mr. Barbour agreed and explained that ICAS was of the view that all stakeholders, including regulators, need to be involved in order to effect meaningful change towards enhancing ethical responsibility. He added that by implementing a culture of “challenge” into organizations, PAs would be able to address ethical matters before the potential consequences become serious. Mr. Siong noted that feedback obtained from stakeholders during the IESBA’s outreach in connection with its NOCLAR project indicates that an environment with a robust rule of law is conducive to developing such a culture.
- Mr. van der Ende asked about ICAS’s perspectives with respect to how PAs should deal with ethical dilemmas, especially when they have taken certain steps to resolve the ethical issue but have not succeeded. Mr. Barbour explained that ICAS is of the view that the PA should first attempt to resolve the issue internally by consulting with various parties, including senior staff and TCWG before considering the need for legal advice. He noted that ICAS also provides support to its members in those situations wherever possible. He explained that ICAS believes that there is a role for all stakeholders in supporting PAs in resolving ethical issues.
- Mr. Dalkin noted that in his view it does not make a difference whether the Code is principles- or rules-based as some PAs may seek to intentionally violate the principles. He wondered whether there was anything in ICAS’ proposals that would lead individual PAs to change their ethical behavior. Mr. Barbour noted that while a small minority would always engage in morally unacceptable activities, the actions of many PAs are influenced by the facts and circumstances of a particular situation. He indicated that there is a need to move away from a mindset that rules exist to be broken. He explained that research indicates that the decision to engage in ethically

acceptable behavior often comes from the subconscious mind. Hence, educational establishments should be driven to teach the younger generation a basic grounding in ethics.

- Mr. Hansen asked whether the case studies with ethical dilemmas indicated successful or unsuccessful outcomes, and whether there are any lessons to be learned. Mr. Barbour explained that most of the recent case studies indicate that PAs generally resign their position when faced with an ethical dilemma, leaving another individual to inherit the unresolved ethical dilemma. ICAS' proposals were advocating transparency about the dilemma in order to increase awareness and stimulate debates about appropriate ethical behavior.

Dr. Thomadakis informed Representatives that the IESBA would also receive a presentation from ICAS on its initiative at the IESBA meeting the following week. He congratulated ICAS on taking the initiative to explore the topic, noting that moral courage can be much more challenging where the rule of law is not guaranteed. Mr. Barbour thanked the CAG for the various comments and suggestions. He noted that ICAS is aware that there is more work to be done on its proposals, but believed that they were sufficiently robust for publication in order to stimulate discussion among stakeholders. Mr. Koktvedgaard thanked Mr. Barbour for the informative and thought-provoking presentation.

#### THE IMPACT OF AUDIT REFORM ON AUDIT COMMITTEES IN THE EU

Ms. Robert introduced the topic, noting that FEE had performed a substantial amount of work to raise awareness about the EU audit reforms, including the impact that these reforms will have on audit committees and their oversight responsibilities. She presented highlights of the FEE publication, noting that the EU audit legislation requires all PIEs to have audit committees. As a result, some PIEs would need to establish an audit committee for the first time. She also noted that the legislation allows Member States to tailor the definition of PIEs. She summarized the additional responsibilities that the legislation imposes on audit committee members, including the requirement to recommend at least two auditors to management, assessment and monitoring of auditor independence against specific criteria, and monitoring the provision of NAS to audit clients against the specified threshold as well as against the "blacklist" of prohibited NAS.

The following matters were raised:

- Mr. Waldron asked whether the reforms were expected to affect the way audit committees communicate or report to investors. Ms. Robert indicated that the audit committee would have to report to the board of directors.
- Mr. Siong asked whether the impact of the additional responsibilities on the workload of audit committee members had been considered. Ms. Robert noted that in her view the regulators are monitoring how audit committees are operating by, for example, monitoring how the new provisions are being implemented and how audit committee members are discharging their responsibilities. She noted that some jurisdictions limited the number of audit committee memberships an individual could take on. She added that the EC might explore this particular matter in the future. Mr. Koktvedgaard commented that there is a need to establish the exact scope of the audit committee's responsibilities before considering the appropriate size of an audit committee and the expectations of its members. He noted that this should form part of a broader discussion about corporate governance.
- Mr. Ayoub asked whether the reforms included provisions for the training needs of audit committee members, both prior to and during their tenure. Ms. Robert responded that the FEE paper touches

on this matter but that the legislation does not address it. She agreed that there is further work to be done in that regard.

Mr. Koktvedgaard thanked Ms. Robert for her informative presentation.

#### EU AUDIT REFORM

Dr. Arteagoitia introduced the topic by informing the CAG that he had very recently attended a conference with stakeholders, including regulators, to assess the impact of the implementation of the new EU audit legislation and that his presentation would focus on conveying observations and key conclusions from this meeting.

He summarized the history of the EU Audit Reform process, noting that the process commenced in October 2010 in response to the global financial crisis, with documents being finalized in April 2014 and set to come into force in June 2016.

He then provided an overview of the audit industry in Europe. He noted that the EC was working to assist with the implementation of the new requirements among the EU Member States in an attempt to harmonize implementation. He indicated that Member State regulators are required to produce a monitoring report on how the new regulations are affecting three areas, namely risks to audit quality, market structure, and performance of audit committees. He explained that the first reports are due in June 2016 and will be consolidated to form a baseline for future monitoring exercises.

Dr. Arteagoitia also reported that a Committee of European Audit Oversight Bodies (CEAOB) will be created shortly after the implementation of the new requirements. One of the Committee's subgroups will consider issues related to standard setting. He concluded his presentation by informing the CAG that the EU is moving towards increased cooperation with non-EU countries on audit-related matters, including equivalence of supervisory approaches and exchange of information.

The following matters were raised:

- Mr. Ahmed observed that he anticipated that Member States would take a more harmonized approach. He wondered why the current situation had arisen and whether Member States were being pressured to change. Dr. Arteagoitia noted there will be a focus on harmonization in the area of professional qualifications. However, while broader harmonization would be ideal, he noted that the difficulty lies in national idiosyncrasies.
- Ms. Lopez requested an update on the status of the implementation of mandatory firm rotation (MFR) requirements in the EU. Dr. Arteagoitia summarized the MFR requirements and noted that the concept of MFR already existed in some Member States, so it was not new. In addition, audited entities can change their auditors themselves. However, it will be necessary to see how the implementation of the requirements plays out in practice.
- Mr. Iinuma asked whether the monitoring reports would be made available to the public. Dr. Arteagoitia responded that the legislation mandates their publication. He also noted that some stakeholders have expressed concern that the requirement for Member States to evaluate the new provisions go beyond the requirement for monitoring reports. He explained that the monitoring reports are intended to capture the impact that the new requirements are having on other areas, such as fees and concentration, as developments occur.
- Mr. Siong wondered whether representatives from the profession had attended the recent conference with stakeholders and whether consideration had been given to providing support to assist with the implementation of new provisions. Dr. Arteagoitia responded that the majority of

attendees at the conference were representatives from the profession. He also noted that the EC had been working with national authorities to consider implementation assistance, and has produced Q&As that are available on the EC's website.

- Noting that the IESBA would be keen to engage with the CEAOB, Dr. Thomadakis requested clarification about how the CEAOB would interact with the IESBA. Dr. Arteagoitia responded that this new body would focus on issues relating to the implementation of the ISAs, although he felt that a link could be made to the Code but not in the immediate future. Ms. Robert concurred, noting that the EC would need to further discuss this matter. Mr. Koktvedgaard noted that if the Code is consistent with the new requirements, there should be no problem in implementing EU audit reforms alongside the Code. Dr. Arteagoitia confirmed this view. He added that from the perspective of the EU, the Code is useful for audits of non-PIEs.
- Dr. Thomadakis wondered whether consideration had been given to an ethics code for audit committees given the additional responsibilities being placed on them. Dr. Arteagoitia responded that he was not aware of plans to develop such a code, but added that developing one might prove difficult because the structure of audit committees varies and the way they operate is very different. Ms. Robert noted that the European Confederation of Directors is exploring a project to consider best practices for audit committees. Mr. Koktvedgaard noted that audit committees in many jurisdictions are considered a subset of the joint supervisory board. Hence, in his view, there should be a joint responsibility for governance that may affect the development of an ethics code solely for audit committees. He added that the governance remit of audit committees in various organizations would need to be established before a code for audit committees could be implemented.

Mr. Koktvedgaard thanked Dr. Arteagoitia for his informative update.

#### **D. Report Backs**

##### STRUCTURE OF THE CODE

Mr. Siong summarized the report back on the September 2015 CAG discussion on the Structure of the Code project. He noted that the IESBA had approved the Exposure Draft, *Improving the Structure of the Code of Ethics for Professional Accountants – Phase 1* (Structure ED-1) at its December 2015 meeting, with a comment period ending in April 18, 2016. He noted that Structure ED-1 represented the first concrete application of the proposed new Structure format, which the IESBA hoped would lead to greater usability and understandability of the Code, and hence more consistent application and improved enforcement.

Mr. Siong noted that the second phase of the Structure project had already commenced. He drew Representatives' attention to the December 2015 IESBA Update that summarizes the Board's plans for coordination of the various work streams impacted by the restructuring efforts and the anticipated timelines. He noted that IESBA anticipates completion of its restructuring efforts by the end of 2017.

Mr. Siong then highlighted the key aspects of the proposed restructured Code, including:

- Its emphasis on the need to comply with the fundamental principles.
- The inclusion of application material to assist in understanding and applying the requirements, including the application of the Conceptual Framework.

- The inclusion of a new requirement to adequately consider actions needed to comply with the fundamental principles.

Mr. Siong concluded by noting that the Structure Task Force is coordinating the restructuring of other parts of the Code with other Task Forces to ensure a consistent approach to the restructuring work, as well as maintaining a list of matters that may merit future Board consideration.

The following matters were raised:

- Mr. Dalkin expressed support for the new structure that positioned requirements followed immediately by supporting application material, which he found helpful. He noted that INTOSAI was revising its own code of ethics and had considered the IESBA's work.
- Mr. Ahmed agreed with Mr. Dalkin. In his view, having explicit requirements that clarify how to apply the five fundamental principles, and the actions that PAs should take when they face threats to compliance with the fundamental principles, will enhance the usability of the Code. He was of the view that the use of examples in the proposed restructured Code reduces ambiguity and is an overall improvement.
- Mr. Nicholson informed that the IIA would be submitting a written response to Structure ED-1. He shared the IIA's views about how it believes the Code should describe the interaction between independence and objectivity.

#### LONG ASSOCIATION

Mr. Siong summarized the report back on the September 2015 Long Association CAG discussion. He noted that the IESBA had issued a re-exposure draft, *Limited Re-exposure of Proposed Changes to the Code Addressing the Long Association of Personnel with an Audit Client* (re-ED) in February 2016, with a comment deadline of May 9, 2016. He explained that the re-ED is limited in scope and addresses the following three specific issues:

- (i) A revised cooling-off period for Engagement Quality Control Reviewers (EQCRs) on the audit of PIEs.
- (ii) Alternatives to elements of the partner rotation requirements in the Code when jurisdictional safeguards are in place.
- (iii) Proposals regarding service in a combination of key audit partner roles.

Mr. Siong noted that the most controversial issue, in terms of responses received on the initial ED, related to the provisions for EQCR cooling off. The IESBA was proposing a "middle-ground" approach as set out in the re-ED, recognizing that a more stringent EQCR cooling-off regime could have significant practical implications given that the supply of individuals with the necessary qualifications and experience to act in an EQCR role is limited. Mr. Fleck further explained IESBA's rationale for its proposal, noting that the IESBA looked forward to feedback from respondents.

Ms. Borgerth congratulated the Board on addressing the topic of long association, noting that it is a very important issue. Representatives had no other comments on the Long Association report back.

#### REVISION OF PART C OF THE CODE

Mr. Siong summarized the report back on the September 2015 CAG discussion on the Part C project. He noted that the IESBA had approved at its December 2015 meeting, *Changes to Part C of the Code Addressing Preparation and Presentation of Information and Pressure to the Breach of the Fundamental*

*Principles* (close-off document).<sup>15</sup> Among other matters, the close-off document includes enhanced guidance to assist PAs in dealing with pressure from superiors in the work place. He explained that the close-off document will be restructured and will form part of the Structure of the Code Phase 2 exposure draft.

Mr. Siong concluded his remarks by noting that the Part C Task Force has commenced its Phase 2 work, which will address the matter of the applicability of Part C to PAs in public practice, and the topic of inducements.

Mr. Hansen asked a general question about the purpose of a close-off document. Mr. Siong explained that a close-off document indicates that the IESBA has concluded its deliberations on all substantive issues in a project under the extant drafting conventions. Absent the Structure of the Code project, the Part C close-off document would have been released as a final pronouncement after the PIOB has approved due process. However, there is a need to restructure the close-off document in the new Structure format before it is released. Mr. Gunn added that this approach is consistent with the approach that the IAASB used when clarifying its ISAs.

Representatives had no other comments on the Part C report back.

#### **E. PIOB Observer's Remarks**

Mr. Holm congratulated Mr. Koktvedgaard on his re-appointment as CAG Chair, subject to PIOB approval, and for a successful CAG meeting. He noted that in his view, the IESBA has been very responsive to input provided by the CAG. He was of the view that there were no new public interest concerns that were raised at this meeting, and that the CAG was operating well.

#### **F. Closing Remarks**

Mr. Koktvedgaard thanked the Representatives for their high level of participation and contributions to the discussions. He then closed the meeting.

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<sup>15</sup> The Part C Phase 1 close-off document was approved by IESBA at its November/ December 2015 meeting, and the Public Interest Oversight Board approved confirmation of due process during its March 2016 meeting. The close-off document was developed using the drafting conventions in the extant Code, and includes changes to the following sections of the extant Code:

- Section 320, *Preparation and Presentation of Information*;
- Section 370, *Pressure to Breach the Fundamental Principles*;
- Section 300, *Introduction*;
- Section 310, *Conflicts of Interest*;
- Section 330, *Acting with Sufficient Expertise*; and
- Section 340, *Financial Interests, Compensation and Incentives Linked to Financial Reporting and Decision Making*.