Firm Culture and Governance (FCG)
Proposed Provisions – Third Read
(Mark-Up from October 2026 Agenda Item 1A)

Overview of Key Changes Since October 2026

Following the IESBA's discussions at its October 2026 meeting and feedback received during Q4 stakeholder outreach, the Project Team (PT) and Board Advisors (BAs) have proposed changes to the October proposals in Part 3 of the Code while retaining the overall direction. The key proposed changes, which aim to enhance clarity, enforceability and proportionality, are summarized below:

1. **Overarching requirement:** Refining the structure and wording of the requirement to emphasize the critical roles of ethical leadership and governance, alongside the exercise of professional judgment. The addition of "uphold" is also proposed to emphasize the importance of reinforcing and giving effect to an ethical culture in practice, beyond establishing and maintaining supporting arrangements.
2. **Descriptions of ethical culture and governance:** Introducing descriptions of these concepts in the draft provisions and in the Glossary to clarify their intended meaning and provide a clearer basis for interpreting, applying and enforcing the proposed provisions.
3. **Descriptions of the interconnected elements:** Refining the lead-in sentence to recognize that the eight interconnected elements may not be the only way to establish, maintain and uphold an ethical culture, while retaining the relevance of the identified elements. Further drafting adjustments address comments raised on terminology relating to governance and the descriptions of certain elements.
4. **Proportionality considerations:** Clarifying the link between the overarching requirement and the proportionality considerations. New considerations related to external transparency and the formality of governance arrangements were also incorporated.

The rationale for these changes, including how they respond to the IESBA's October discussion and subsequent stakeholder feedback, is explained in the grey boxed sections that follow.

Key questions and comments raised during Q4 stakeholder outreach that are not directly addressed through the proposed changes set out below will also be explained in the explanatory memorandum (EM).

Other Proposed Changes to the Code

The other proposed changes to the Code set out in this paper include other consequential amendments to Parts 1 to 3 of the Code that were previously presented at the September 2026 IESBA meeting.

SECTION 300

…

300.4 A1 Compliance with the fundamental principles and the application of the conceptual framework within a firm are influenced by its ethical culture and related governance. Such culture and governance play an important role in shaping the mindset, behaviors and professional judgments of a firm's personnel, and help ~~them~~ the firm to meet ~~their~~ its responsibility to act in the public interest.

Proposed paragraph 300.4 A1 – Bridge provision to explain why the culture and related governance of a firm are relevant to an individual's compliance with the fundamental principles

At the October 2026 meeting, IESBA members shared the following key comments:

- That the Code places the responsibility to act in the public interest on professional accountants (PAs) and firms, and therefore the latter part of the last sentence was not technically consistent with the Code.

  The PT and BAs acknowledge that referring to "personnel" encompasses those professionals who work in the firm but are not PAs. Accordingly, the latter part of the paragraph was revised to refer to the firm's public interest responsibility, consistent with the rest of the Code.

- Differing views on whether to retain references to "related governance" alongside ethical culture:
  - Some considered the references unnecessary, as governance is one of the FCG elements, and its removal would better align with the focus on ethical culture in the proposed requirement.
  - Others considered the references appropriate and suggested giving governance greater prominence, recognizing its critical role as a means of achieving an ethical culture.

  The PT and BAs are of the view that, on balance, the reference to "related governance" should be retained alongside ethical culture to consistently emphasize, throughout the FCG provisions, the essential role of governance as a conduit for ethical culture.

In addition, the PT and BAs added the word "professional" before "judgments" to align with the term "professional judgement" used in the Code (see extant paragraph 120.5 A4 and the Glossary).

Ethical Culture and Related Governance within Firms

R300.5 A firm shall take appropriate steps to establish, ~~and~~ maintain and uphold an ethical culture throughout the firm that supports compliance with the fundamental principles by its personnel. In doing so, the firm shall:

(a) Adopt ethical leadership and governance as key drivers of such an ethical culture; and

~~(a)~~(b) ~~e~~Exercise professional judgment, taking into account the nature and circumstances of the firm and its professional services. ~~Ethical leadership and governance are key drivers to establishing and maintaining such an ethical culture.~~

300.5 A1 An ethical culture includes the values, behaviors, policies and practices within a firm that the firm develops and maintains to support and guide the firm's personnel to comply with the fundamental principles.

300.5 A2 Governance as it relates to a firm's ethical culture is the system of processes, practices or other arrangements by which the firm is led, overseen and held accountable for its ethical culture throughout the firm.

300.5 A3~~1~~ The ultimate responsibility for establishing, ~~and~~ maintaining and upholding an ethical culture and related governance rests with the firm's leadership, such as the senior or managing partner (chief executive or equivalent) or, if appropriate, the managing board of partners (or equivalent). However, all personnel have a role in contributing to and reinforcing the ethical culture of the firm.

300.5 A4~~2~~ An approach for a firm to establish, maintain and uphold an ethical culture and related governance ~~are more likely to support compliance with the fundamental principles when the firm~~is to take~~s~~ appropriate steps in relation to the following interconnected elements:

- *Ethical leadership:* The firm's leadership setting the tone at the top and every leader at all levels within the firm demonstrating ethical behavior in their judgments, decisions and actions, thereby setting the expectation for all personnel to act ethically.
- ~~*Oversight and g*~~*G*~~*overnance arrangements:*~~ The firm's leadership establishing and maintaining arrangements ~~that~~ to effectively oversee and monitor the ethical culture throughout the firm and embed ethics in conduct and decision-making.
- *Independent input:* ~~For significant strategic, governance and business decisions of the firm on matters involving the public interest, c~~Considering obtaining input from individual(s) or other sources that are impartial and free from actual or perceived conflicts of interest with respect to significant strategic, governance and business decisions of the firm on matters involving the public interest~~such matters~~.
- *Accountability across the firm:* Setting clear expectations for all personnel to act ethically and holding all personnel responsible for meeting those expectations.
- *Incentives and disincentives*
  - *Incentives:* Designing and implementing performance evaluation and compensation practices that reinforce ethical behavior alongside financial and non-financial targets and do not ~~motivate~~ inadvertently lead personnel to act unethically.
  - *Disincentives:* Deterring unethical behavior and responding to it in a consistent and timely manner with appropriate communications, measures and consequences.
- *Open discussion and challenge:* Fostering an environment where personnel feel safe to discuss ethics-related matters, raise concerns or challenge decisions from an ethical perspective without fear of adverse consequences.

- *Education and training:* ~~Taking appropriate steps to r~~Regularly educating~~e~~ and training personnel to develop an ethical mindset and professional judgment that help them identify and address ethical dilemmas when performing their professional activities.
- *Transparency*
  - *Internal transparency:* Having regard to the principle of confidentiality, ~~S~~sharing ethics-related learnings and experiences within the firm~~, as appropriate,~~ to reinforce ethical behavior.
  - *External transparency:* Considering publicly disclosing relevant information on how the firm demonstrates its commitment to establishing~~, and~~ maintaining and upholding an ethical culture and related governance throughout the firm.

300.5 A5~~3~~ The steps that the firm might take in relation to ~~the elements referred to in~~ paragraph R300.5 ~~A2~~ and how they are implemented will vary according to the nature and circumstances of the firm. Relevant factors the firm might consider include:

- The size and structure of the firm.
- The size and nature of the firm's client base.
- The nature of the professional services provided by the firm.
- Whether the firm is part of a network~~ and considerations that might be relevant in establishing and maintaining an ethical culture in such circumstances~~.

300.5 A6~~4~~ The nature and circumstances of the firm are particularly relevant~~, especially for small and medium practices including sole practitioners,~~ when determining:

- The type and formality of arrangement(s) for ~~oversight and~~ governance.
- If independent input is sought, the source(s) of that input.
- In relation to external transparency, if public disclosure is made, the extent and manner of such disclosure regarding the firm's ethical culture and related governance.

This is especially the case for small and medium practices, including sole practitioners.

Proposed paragraph R300.5 – Overarching requirement

During the October 2026 meeting, IESBA members shared the following key comments:

- To emphasize more prominently the role of governance in enabling an ethical culture.

  To balance the differing Board member views (ranging from making governance the subject of the requirement, to removing it because it is already addressed in the application material), the PT and BAs propose combining the second and third sentences of the October draft. Under the revised structure, the second "shall" precedes the references to leadership and governance as the two key drivers of an ethical culture, as well as the proportionality considerations for a firm.

  This gives greater prominence to leadership and governance as the key means to enabling an ethical culture, while retaining ethical culture as the focus of the requirement in the first sentence of the requirement. The PT and BAs consider it important to retain references to ethical leadership and governance in the requirement, notwithstanding their inclusion in the application material,

reflecting their critical significance to ethical culture as highlighted in the FCG Working Group Final Report.

- To more clearly articulate the purpose of the FCG project, including "to maintain the credibility of the profession which is the foundation for the firm to act in the public interest."

  The PT and BAs considered that proposed paragraph 300.4 A1 which references the firm's responsibility to act in the public interest, and proposed requirement R300.5 which explains that an ethical culture supports compliance with the fundamental principles by the firm's personnel, provide a sufficient basis within the Code to further elaborate on the underlying purpose and intended outcomes of the FCG project in the EM. This also recognizes that the fundamental principle of professional behavior requires a PA:

  - To avoid any conduct that the PA knows or should know might discredit the profession; and
  - To not knowingly engage in any business, occupation or activity that impairs or might impair the integrity, objectivity or the good reputation of the profession.

  See extant paragraph R115.1.

- That the reference to "circumstances" in the second sentence of the proposed requirement, which is intended to address proportionality, could be interpreted as allowing firms to selectively implement or not implement certain elements of an ethical culture based on their external circumstances.

  The PT and BAs observe that the term "circumstances" is widely used throughout the Code and is relevant to the exercise of professional judgment in applying its provisions. In the context of R300.5, the reference is intended to recognize that a firm's nature and circumstances inform the appropriate steps it takes to establish, maintain and uphold an ethical culture. It is not intended to suggest that a firm may use its circumstances, such as commercial or profitability considerations, as a justification for disregarding particular elements of an ethical culture.

  In a few jurisdictions, certain firms are also subject to an Audit Firm Governance Code established by a regulatory authority. This is an example of a circumstance that the firm may take into account.

  The EM will include the above explanation.

Upholding an Ethical Culture

During Q4 stakeholder outreach, a suggestion was received from a jurisdictional standard setter (JSS) to incorporate "uphold" in the proposed requirement alongside "establish" and "maintain," drawing on enforcement cases in which firms had established and maintained relevant processes and procedures but failed to implement and follow them adequately.

On reflection, the PT and BAs propose adding "uphold" to strengthen the enforceability of the requirement (PIF characteristic). While acknowledging some overlap between the dictionary definitions of "maintain" and "uphold," the PT and BAs consider that the three verbs emphasize distinct but complementary aspects of a firm's responsibility for its ethical culture:

- Establish[1] means to start or create an ethical culture and putting in place appropriate arrangements

[1] Merriam-Webster.com Dictionary, "Establish," https://www.merriam-webster.com/dictionary/establish; Cambridge Dictionary, "Establish," https://dictionary.cambridge.org/dictionary/english/establish.

to foster it.

- Maintain[2] means to keep the ethical culture in good condition, including regularly reviewing and updating such arrangements.
- Uphold[3] means to actively support and give effect to an ethical culture in practice, including ensuring that relevant arrangements are implemented, followed through and brought to life through actions such as delivering training and assessing understanding, monitoring ongoing compliance, and taking appropriate action in response to non-compliance.

The PT and BAs also considered the potential implications of a firm determining that it had not complied with R300.5. As explained in October 2026 Agenda Item 1A (page 5), an individual breach of a fundamental principle does not automatically constitute non-compliance with R300.5, although it might suggest a deeper problem with the firm's ethical culture and related governance. In further considering this question, the PT and BAs observed that:

- The requirement to "establish, maintain and uphold" an ethical culture recognizes that establishing, maintaining and upholding an ethical culture is an ongoing journey and can never be a "one and done thing," simply because firms are people businesses.
- This is reinforced by the element of governance, which contemplates arrangements for overseeing and monitoring ethical culture. Such arrangements could help a firm identify matters requiring attention and consider whether improvements to its ethical culture and related governance are necessary.
- Where an instance of non-compliance with a fundamental principle has arisen, the PT and BAs observed that the firm would be expected to consider the nature and circumstances of the non-compliance and determine, through a root-cause analysis, whether the non-compliance is an isolated case or a systemic issue with the firm's ethical culture. This is what the reference to "maintaining" and "upholding" an ethical culture is intended to achieve. It is through taking remedial action that the firm is able to maintain and uphold an ethical culture.

Proposed NEW paragraphs R300.5 A1 and A2 – Descriptions of ethical culture and its related governance

During the October 2026 meeting, a Board member expressed the view that the proposed requirement would be challenging to enforce because the meanings of "ethical culture" and "governance" are not clear. Accordingly, the PT and BAs propose to add descriptions of ethical culture and related governance as a way to enhance clarity and enforceability of the proposed requirement (PIF characteristics).

Both descriptions are proposed to be added in the context of a firm (i.e., for the purposes of the FCG provisions only) and therefore will not apply to other instances where "ethical culture" or "governance" are used in the Code outside the context of a firm or individual PAs in public practice. These proposed descriptions were also added to the glossary (see below), similar to other descriptions in the Code – see e.g. "professional judgement" in the glossary.

---

[2] Merriam-Webster.com Dictionary, "Maintain," https://www.merriam-webster.com/dictionary/maintain; Cambridge Dictionary, "Maintain," https://dictionary.cambridge.org/dictionary/english/maintain.

[3] Merriam-Webster.com Dictionary, "Uphold," https://www.merriam-webster.com/dictionary/uphold; Cambridge Dictionary, "Uphold," https://dictionary.cambridge.org/dictionary/english/uphold.

In relation to the description of governance in proposed paragraph 300.5 A2, the PT and BAs note that it is intended to be broader than the description of the FCG element of governance set out in proposed paragraph 300.5 A4:

- While 300.5 A2 describes what governance is more broadly in the context of a firm's ethical culture, 300.5 A4 focuses on the intended outcome of each FCG element, including for governance.
- Additionally, as the FCG elements are interconnected, certain aspects of the description of governance are also reflected in multiple FCG elements, such as the elements of accountability as well as governance.

Finally, the PT and BAs note that the IAASB Handbook includes a definition of governance[4] in its glossary. In coordination with IAASB staff, the PT and BAs consider that both the IAASB definition and the proposed description are complementary – the IAASB's definition is general, while the IESBA's proposed description is specific to the context of a firm's ethical culture.

Proposed paragraph 300.5 A4 – Elements of an ethical culture and related governance

The adjustments proposed to the lead-in sentence aim to address the differing views expressed by IESBA members at the October 2026 meeting, where:

- Some members noted that the expression "more likely" was not strong enough to reflect the almost three years of information gathering leading to the identification of these FCG elements.
- Other members considered that the same expression might be interpreted as the IESBA's FCG elements constituting the only acceptable FCG framework. In this regard, a few members noted that even if other frameworks exist, they broadly consist of the same core notions articulated by the FCG elements.

Accordingly, the proposed revised wording – "*An approach for a firm… is to take appropriate steps…*" – aims to address the different views expressed by the Board by removing the qualifier "more likely" to provide a more direct link to the requirement, while referring to "an approach" recognizes that other approaches may also exist. The formulation also draws on the language used to introduce the conceptual framework in paragraph 120.2 of the Code.[5]

While the PT and BAs acknowledge the IESBA FCG framework might not be the only relevant framework relating to an ethical culture for a firm, paragraph 100.7 A1 of the Code[6] recognizes that there might be provisions in jurisdictions that cover or go beyond provisions in the Code and that PAs need to be aware of the differences and comply with the more stringent provisions.

---

4 Governance—Describes the role of person(s) or organization(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity.

5 Paragraph 120.2 of the Code states:

> *"The conceptual framework specifies an approach for a professional accountant to: (…).*"

6 Paragraph 100.7 A1 of the Code states:

> *"The principle of professional behavior requires a professional accountant to comply with relevant laws and regulations. Some jurisdictions might have provisions that differ from or go beyond those set out in the Code. Accountants in those jurisdictions need to be aware of those differences and comply with the more stringent provisions unless prohibited by law or regulation."*

Second bullet – Governance

At the October 2026 meeting, an IESBA member observed that differing references to governance throughout the proposed provisions could cause confusion. Accordingly, the PT and BAs propose adjusting the title of this FCG element to "governance" to align with the proposed requirement. The reference to "oversight" is incorporated into the description, while the term "arrangements" is removed from the title to avoid duplication. These changes aim to enhance the clarity, consistency and conciseness of the proposed standard (PIF characteristics).

The PT and BAs also considered whether to incorporate "uphold" alongside "establishing and maintaining" in this element, but determined it was not necessary because "establishing and maintaining" in this bullet describe what the firm's leadership does with respect to its *governance*: setting up those arrangements and keeping them in good working condition. Those arrangements then help establish, maintain and uphold the firm's ethical culture.

In summary, proposed paragraph 300.4 A1 explains why governance matters; R300.5 identifies governance as a key driver of ethical culture; 300.5 A2 describes what governance means; and 300.5 A4 illustrates how governance can be put into practice through arrangements for overseeing and monitoring ethical culture.

Third bullet – Independent input

The PT and BAs propose an editorial change to emphasize the proportionality incorporated in the description by making it clearer that this element is for firm consideration at the start of the sentence (similar to external transparency). This aims at enhancing clarity of the proposed standard (PIF characteristics).

Fifth bullet – Incentives and disincentives

The PT and BAs suggest two adjustments aimed at addressing comments from a few IESBA members at the October 2026 IESBA virtual meeting:

- Adding "non-financial" targets in addition to financial targets, for completeness.
- Replacing "motivate" with "inadvertently lead" to avoid the perception noted by a Board member that the previous wording could be interpreted as assuming that firms were designing performance incentives to motivate personnel to act unethically, which is not the case.

Seventh bullet – Education and training

The PT and BAs propose a minor editorial change to avoid repetition with the lead-in sentence which already mentions taking "appropriate steps."

Eighth bullet – Transparency

Regarding internal transparency, the PT and BAs suggest making it clear that confidentiality is considered in the element, which had been implicit in the expression "as appropriate." This aims at enhancing the clarity of the proposed standard (PIF characteristic).

The PT and BAs also note a suggestion from an IESBA member at the October 2026 meeting to emphasize the importance of firm leadership's participation in sharing ethics-related learnings. As

explained in previous Agenda Items in September and October 2026, unless otherwise specified, each FCG element as drafted applies to the firm and its personnel, including firm leadership.

Other considerations

An IESBA member also suggested including "employee wellbeing" as an FCG element. However, the PT and BAs note that while a firm's ethical culture (e.g., leadership's approach to working hours and conditions) and aspects of the FCG elements (e.g., psychological safety under the element of open discussion and challenge) can influence employee wellbeing, employee wellbeing is a broader concept that extends beyond a firm's ethical culture. Accordingly, the PT and BAs do not consider it necessary to include employee wellbeing as an additional element, as the existing elements sufficiently address aspects of employee wellbeing relevant to a firm's ethical culture.

Proposed paragraph 300.5 A5 – Proportionality considerations

The adjustment proposed in the lead-in sentence aims to address a comment from an IESBA member at the October 2026 IESBA meeting, that the wording seemed to limit proportionality to the IESBA FCG framework only. The PT and BAs therefore propose cross referencing to the requirement, whose first sentence also mentions "steps."

The PT and BAs propose removing the last part of the last bullet on network firms – which had been added to clarify the scope of considerations relating to network firms in the second read draft – following comments from some IESBA members at the October 2026 meeting that it did not provide the intended clarity. The PT and BAs therefore propose retaining a succinct bullet on network firms that can provide a basis for the development of non-authoritative material outside the Code, including considerations relating to the global firms operating through networks, as highlighted by the PIOB.

Proposed paragraph 300.5 A6 – Proportionality considerations

The PT and BAs propose moving part of the lead-in sentence to a separate sentence at the end of the paragraph to improve readability and clarity of the proposed standard (PIF characteristic).

The PT and BAs propose two changes in the first bullet:

- Adding "and formality" to clarify – particularly to smaller firms – that the level of formality (i.e., informal or formal) of the governance arrangements will depend on the firm's nature and circumstances.
- Removing "oversight and" for consistency with the change proposed in the title of the FCG element described in the second bullet of paragraph 300.5 A4.

In addition, the PT and BAs propose adding a bullet for external transparency that reinforces that this element may not apply in all situations (per the respective bullet in proposed paragraph 300.5 A4) and that speaks to the different level of comprehensiveness and formats that the public disclosure, if made, can follow (e.g. transparency report, online announcement at the firm's website, etc.).

GLOSSARY

Engagement team	(…)
Ethical Culture *(In the context of a firm)*	*An ethical culture includes the values, behaviors, policies and practices within a firm that the firm develops and maintains to support and guide the firm's personnel to comply with the fundamental principles.* *This term is described in paragraph 300.5 A1.*
(…)	(…)
Governance *(In the context of a firm's ethical culture)*	*Governance as it relates to a firm's ethical culture is the system of processes, practices or other arrangements by which the firm is led, overseen and held accountable for its ethical culture throughout the firm.* *This term is described in paragraph 300.5 A2.*
Group	(…)

Proposed new descriptions of "ethical culture" and "governance" in the glossary aligned with the new proposed paragraphs 300.5 A1 and A2.

Other Related Revisions and Consequential Amendments
Mark-Up from Extant Code
(Minor Changes from September 2026 Agenda Item 2A)

Highlighted in Aqua to Align with Proposed Provisions

PART 1

…

General

…

120.13 A3 Professional accountants are expected to:

(a) Encourage and promote an ethical ~~ethics-based~~ culture in their organization, taking into account their position and seniority; and

(b) Exhibit ethical behavior in dealings with individuals with whom, and entities with which, the accountants, the firm or the employing organization has a professional or business relationship.

Considerations Relating to Ethical Culture and Related Governance within Firms

120.14 A1 Paragraphs R300.5 to 300.5 A6 set out a requirement and application material relating to the establishment, maintenance and upholding of an ethical culture and related governance throughout a firm.

Considerations for Audits, Reviews, Other Assurance and Related Services Engagements

Firm Culture

120.14 A1 ISQM 1 sets out requirements and application material relating to firm culture in the context of a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements.

…

PART 2

…

General

…

200.5 A3 The more senior the position of a professional accountant, the greater will be the ability and opportunity to access information, and to influence policies, decisions made and actions taken by others involved with the employing organization. To the extent that they are able to do so, taking into account their position and seniority in the organization, accountants are expected to encourage and promote an ethical ~~ethics-based~~ culture in the organization and exhibit ethical behavior in dealings with individuals with whom, and entities with which, the

accountant or the employing organization has a professional or business relationship in accordance with paragraph 120.13 A3. Examples of actions that might be taken include the introduction, implementation and oversight of:

…

PART 3

…

General

…

Considerations for Professional Activities Pursuant to the Professional Accountant's Relationship with the Firm

R300.~~5~~6 When dealing with an ethics issue, the professional accountant shall consider the context in which the issue has arisen or might arise. Where an individual who is a professional accountant in public practice is performing professional activities pursuant to the accountant's relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions in Part 2 that apply to these circumstances.

300.~~5~~6 A1 Examples of situations in which the provisions in Part 2 apply to a professional accountant in public practice include:

…

300.~~5~~6 A2 The more senior the position of a professional accountant, the greater will be the ability and opportunity to access information, and to influence policies, decisions made and actions taken by others involved with the firm. To the extent that they are able to do so, taking into account their position and seniority in the firm, accountants are expected to encourage and promote an ethical ~~ethics-based~~ culture in the firm and exhibit ethical behavior in dealings with individuals with whom, and entities with which, the accountant or the firm has a professional or business relationship in accordance with paragraph 120.13 A3. ~~Examples of actions that might be taken include the introduction, implementation and oversight of:~~

- ~~Ethics education and training programs.~~
- ~~Firm processes and performance evaluation and reward criteria that promote an ethical culture.~~
- ~~Ethics and whistle-blowing policies.~~
- ~~Policies and procedures designed to prevent noncompliance with laws and regulations.~~