

Basis for Agreement in Principle
Prepared by the Staff of the IESBA
January 2017

*International Ethics Standards Board
for Accountants®*

**Improving the Structure of the
Code of Ethics for
Professional Accountants—
Phase 1**



International
Ethics Standards
Board for Accountants®

This document was prepared by the Staff of the International Ethics Standards Board for Accountants® (IESBA®).

The IESBA is a global independent standard-setting board. Its objective is to serve the public interest by setting high-quality ethics standards for professional accountants worldwide and by facilitating the convergence of international and national ethics standards, including auditor independence requirements, through the development of a robust, internationally appropriate *Code of Ethics for Professional Accountants™* (the Code).

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BASIS FOR AGREEMENT IN PRINCIPLE: IMPROVING THE STRUCTURE OF THE CODE OF ETHICS FOR PROFESSIONAL ACCOUNTANTS—PHASE 1

CONTENTS

	Page
I. Introduction	4
II. Background.....	4
III. Basis for Agreement in Principle.....	5
Key Elements of the Restructuring	5
The Conceptual Framework, the Fundamental Principles and the IIS.....	6
Ordering of Requirements and Application Material.....	7
Clarity of Responsibility for Compliance with the Code.....	8
Use of the Phrase “Generally Necessary” in the Code	8
Suggestions to Avoid Possible Changes of Meaning and Other Drafting Suggestions .	9
The Guide to the Code	10
Use of “May” versus “Might”	10
Navigability	11
Audit Includes Review	12
Title	12
Exceptions	13
Other Matters.....	13

I. Introduction

1. It is in the public interest for the Code to be understandable and usable. In restructuring the Code, the IESBA is aiming to enhance the understandability and usability of the Code, thereby facilitating its adoption, effective implementation, consistent application and enforcement.
2. At its December 2016 meeting, the IESBA agreed in principle the new structure and drafting conventions for the Code and the text of Phase 1 of the Structure of the Code project ("Structure project"), taking into account respondents' feedback on the December 2015 Exposure Draft [Improving the Structure of the Code of Ethics for Professional Accountants – Phase 1](#) (Structure ED-1) as well as input from its Consultative Advisory Group (CAG). This Basis for Agreement in Principle has been prepared by staff of the IESBA. It summarizes the feedback received from respondents to Structure ED-1 and explains the rationale for the IESBA's decisions in agreeing in principle the new structure and drafting conventions for the Code and the text of Phase 1 of the Structure project.
3. A Basis for Conclusions document for the Structure project will be prepared once Phase 2 of the project is completed.

II. Background

4. Structure ED-1 included:

- A proposed Guide to the Code.
- The proposed restructured Part A of the extant Code.¹
- The proposed restructured text of most of Part B² of the extant Code.

Fifty comment letters were received from various respondents, including regulators and audit oversight authorities, national standard setters, firms, public sector organizations, preparers, IFAC member bodies and other professional organizations. Several comment letters reflected the collective input of a group.

5. There was widespread support for the key features of the restructuring, including an enhanced focus on the fundamental principles, requirements distinguished from application material, enhanced clarity and improved usability. Respondents, including representatives of the small and medium practices (SMP) community, appreciated that the improvements in terms of understandability of the Code would facilitate compliance and enforcement.
6. While expressing support for the proposals in Structure ED-1, some respondents requested that the complete proposed restructured Code be made available when they review the proposals in Phase 2 of each of the Structure and Safeguards projects. In response to this request, and to assist respondents in better understanding how the provisions in the texts of Phases 1 and 2 of the Structure project relate to each other, and to the work on the Safeguards Project, IESBA Staff has prepared a number of resources, including this document, that are available at: www.ethicsboard.org/restructured-code. Other resources include:
 - A [mark-up](#) draft to show the revisions made to the text exposed in Structure ED-1.

¹ Extant Part A – *General Application of the Code*

² Extant Part B – *Professional Accountants in Public Practice*, Sections 200 to 290 (excluding paragraphs 290.500 to 290.514, *Reports that Include a Restriction on Use and Distribution*)

- A [compilation of the proposed restructured Code](#). This document includes the agreed-in-principle text of Phase 1 of each of the Structure and Safeguards projects, and the proposed texts issued for exposure in January 2017 under Phase 2 of the project ([Structure ED-2](#)), Phase 2 of the Safeguards project ([Safeguards ED-2](#)), and the Part C project ([Applicability ED](#)). The compilation includes comments alongside each paragraph to explain the derivation of the restructured provisions, i.e., whether they are from particular paragraphs in the extant Code or represent new material. These comments are intended to facilitate review and comparison of the material in the extant Code and the proposed restructured Code.
- A [mapping table](#) to facilitate tracking of the changes from the extant Code to the proposed restructured Code. The mapping table complements the compilation of the proposed restructured Code.
- A Basis for Agreement in Principle document to explain the rationale for the IESBA's decisions following exposure of the proposals included in the December 2015 Exposure Draft, [Proposed Revisions Pertaining to Safeguards in the Code—Phase 1](#).

III. Basis for Agreement in Principle

Key Elements of the Restructuring

7. Key elements of the restructuring include:
 - (a) Increased prominence of the requirement to comply with the fundamental principles and apply the conceptual framework;
 - (b) Requirements in paragraphs identified with an “R,” distinguished from other material;
 - (c) Application material generally positioned next to the relevant requirements – paragraphs identified with “A;”
 - (d) Increased clarity of responsibility – more clearly enabling identification, where relevant, of a firm’s responsibilities and, together with firms’ policies and procedures, the responsibilities of particular professional accountants; specific references to network firms to clarify when the Code applies to them; reduction of the use of the phrase “generally;” and
 - (e) Increased clarity in drafting – where possible: simpler and shorter sentences; simplifying complex grammatical structures; increased use of the active voice; avoiding legalistic and archaic terms.
8. Additional aspects of the restructuring are as follows:
 - The addition of a *Guide to the Code*.
 - Reorganizing the Code as appropriate, to enhance clarity and usability, positioning the Code to take advantage of forthcoming electronic features.
 - Organization of the material into more self-contained sections and subsections so that:
 - Each Section has its own introduction to provide an overview and context, including the threats that might exist, and references the fundamental principles.
 - Revised numbering to facilitate revisions.
 - Re-ordering of extant Parts B and C to recognize the relevance of the material applicable to professional accountants in business (PAIBs) to professional accountants in public practice in

certain circumstances. This also facilitates presentation of the independence sections of the Code after other material.

- Independence sections moved to the end of the Code, re-titled as the *International Independence Standards* (herein referred to as “IIS”).³
 - Definitions section enhanced and presented as a glossary, which also includes descriptions of terms used.
 - A new title for the Code.
9. The sections below explain the main refinements to the text of Phase 1 of the Structure project that the IESBA agreed in principle in the light of respondents’ feedback on Structure ED-1.

The Conceptual Framework, the Fundamental Principles and the IIS

10. Structure ED-1 promoted the importance of applying the conceptual framework and proposed emphasizing this by including a requirement to apply the conceptual framework at the beginning of each section. To remind professional accountants of this requirement, a sentence was included in the header of each page in Structure ED-1. While there was widespread support from respondents for this proposal, some respondents made specific suggestions, including that:
- The overarching requirement to comply with the fundamental principles be given even greater prominence.
 - Unnecessary repetition be avoided – for example, positioning requirements appropriately to obviate the need for the banner heading regarding applying the conceptual framework.
 - The overarching requirement to be independent when providing audit and assurance services be given greater prominence.
 - The description of the linkage between independence and the fundamental principles be enhanced.
 - The application of the conceptual framework in the context of independence be clarified. Respondents to Safeguards ED-1 made a similar comment (see paragraph 8 of the Basis for Agreement in Principle for Phase 1 of the Safeguards project (Safeguards BFAP)).
 - The interaction between the conceptual framework and specific requirements and application material be clarified so as not to lose the focus on the fundamental principles when setting out specific requirements and application material.

IESBA Agreement in Principle

11. The IESBA agreed:
- To revise the introductory material in each section throughout the Code to remind users of the requirement to comply with the fundamental principles.
 - To retain the reminders to apply the conceptual framework, with a focus on the overall objective and not simply the process of achieving the objective.

³ The independence sections in the proposed restructured Code are included in the IIS, which comprise Part 4A – *Independence for Audits and Reviews* (i.e., Sections 400 to 899) and Part 4B – *Independence for Other Assurance Engagements* (i.e., Sections 900 to 999).

- To remove the banner heading at the top of each page.
- To add revised introductory material in each independence section throughout the Code reminding users of the requirement to be independent.
- To delete the statement in paragraph 400.1⁴ of Structure ED-1 that “independence is a measure of objectivity.”
- To revise Section 120⁵ to repeat the definition of independence from paragraph 400.2 (which links independence to the fundamental principles of integrity and objectivity) to create a clearer linkage between Section 120 and the independence sections relative to the application of the conceptual framework to maintain independence when performing audits, reviews or other assurance engagements.
- To include as part of the revisions to Section 120 a requirement for professional accountants to apply the conceptual framework to threats to compliance with independence standards as well as threats to compliance with the fundamental principles when performing an engagement requiring independence (see also paragraph 11 of the Safeguards BFAP).
- To revise the introductory part of each section to clarify that complying with the fundamental principles, maintaining independence when required to be independent, and applying the conceptual framework are overarching requirements in addition to the need to comply with specific requirements.
- To add a cross-reference from Section 120 to other areas of the Code that provide additional requirements and application material relevant to the application of the conceptual framework.

Ordering of Requirements and Application Material

12. Structure ED-1 maintained the extant Code’s principles-based approach. It also highlighted requirements and gave more prominence to prohibitions and the overarching requirement to comply with the fundamental principles. This took into account comments from respondents to the November 2014 Consultation Paper, [Improving the Structure of the Code for Professional Accountants](#).
13. Respondents to Structure ED-1 supported and emphasized the importance of a principles-based approach and the overarching requirements to comply with the fundamental principles and apply the conceptual framework. Respondents were concerned that the Code should not be structured in a way that might imply that specific requirements could be applied without consideration of these overarching requirements. Some respondents to the December 2015 ED, [Proposed Revisions Pertaining to Safeguards in the Code – Phase 1](#) (Safeguards ED-1) emphasized the importance of giving appropriate prominence to prohibitions.

IESBA Agreement in Principle

14. In the light of the support from respondents, the IESBA agreed to retain the principles-based approach for the Code, its scalability and the overarching requirement to apply the conceptual framework. The IESBA agreed that the order of the requirements and application material within each section of the proposed restructured Code be as follows:

⁴ Section 400, *Applying the Conceptual Framework to Independence for Audits and Reviews*

⁵ Section 120, *The Conceptual Framework*

- The requirements and application material related to applying the conceptual framework are set out first, followed by specific requirements.
- Recognizing the need for scalability, requirements that apply to firms when providing professional services to public interest entities are located after requirements that apply to other entities.
- Application material that is specific to a particular requirement follows the related requirement as closely as possible.

Clarity of Responsibility for Compliance with the Code

15. Structure ED-1 proposed reducing the use of the passive voice and retaining the extant Code's reference to ISQC 1⁶ to clarify responsibility for compliance in the Code in paragraph 400.7 of Structure ED-1. It also included the following new explanatory material: "Although firms and professional accountants within those firms each have responsibilities for compliance, for ease of reference, many of the provisions of C1 (Part 4B in Structure ED-2) refer to "firm," even if the main responsibility rests with an individual within the firm."
16. Respondents supported the reduced use of the passive voice and the continued reference to ISQC 1. Many respondents supported or accepted the proposed restructured Code's use of the word "firm" for ease of reference. Some respondents did not support the approach to refer to "firm" in C1 when responsibilities for compliance rest with individuals. A few respondents expressed the view that Structure ED-1 did not use consistent terminology to clarify responsibility.
17. Structure ED-1 proposed that the term "network firm" be distinguished from the term "firm." Respondents to Structure ED-1 supported this proposal. In some instances, respondents indicated that this proposal required further clarification with respect to the application of a materiality or significance test to network firms.

IESBA Agreement in Principle

18. The IESBA:
 - Reaffirmed its view that the proposal in Structure ED-1 properly reflects professional accountants' responsibilities for compliance with the Code while recognizing that assignment of certain specific aspects of the responsibilities will be impacted by firms' policies and procedures.
 - Reaffirmed its view that, as explained in paragraph 400.4 (400.7 in Structure ED-1), it is appropriate for drafting purposes to use the term "firm" for ease of reference. For greater clarity, an explanation of this approach is now included in Section 120.
 - Clarified the application of materiality or significance tests to network firms so as to avoid inadvertent change in meaning or any unintended consequences.

Use of the Phrase "Generally Necessary" in the Code

19. A respondent suggested that the phrase "generally necessary" should be converted into a requirement because it is unclear in its meaning. The phrase "generally necessary" was only used in

⁶ International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*

in Structure ED-1 in the context of the application material to the requirement regarding disclosure of a conflict of interest (see paragraph 310.9 A3 of Structure ED-1). The IESBA had considered that:

- Providing guidance in the international context on how professional accountants should deal with conflicts of interest is difficult given the variation in practice across jurisdictions and disciplines, and the varying nature of conflicts of interest that might arise.
- Disclosure and consent can take a number of forms which vary across jurisdictions, disciplines and service types.
- Obtaining consent is not always a practical proposition, for example if there are multiple users of the report (particularly where a report is to be made public) and the professional accountant will not be interacting with each and every user.
- The need for disclosure and consent will depend on the significance of the conflict.
- Although not a safeguard, disclosure to and consent of parties potentially affected by a conflict of interest play a part in managing a conflict and are generally desirable if not actually required. However, disclosure might conflict with the fundamental principle of confidentiality.

IESBA Agreement in Principle

20. The IESBA concluded that it is appropriate to retain the phrase “generally necessary” in the two remaining instances in the proposed restructured Code (see paragraphs 310.9 A3 of the agreed-in-principle text and 210.8 A1 of Structure ED-2). The IESBA decided that it is not possible to define all the circumstances in which disclosure and consent are or are not necessary. Rather, it is a question of professional judgment. Accordingly, the Code requires the professional accountant to exercise professional judgment in determining whether the nature and significance of a conflict of interest are such that specific disclosure and explicit consent are necessary when addressing the threat created by the conflict of interest. The section then provides guidance on factors to consider in making that determination.

Suggestions to Avoid Possible Changes of Meaning and Other Drafting Suggestions

21. Structure ED-1 proposed to improve the understandability and usability of the Code by restructuring it without changing its meaning, except in limited circumstances where determined necessary by the IESBA. In the Structure ED-1 proposals, the IESBA had sought to avoid inadvertent changes in the meaning of the Code, including inadvertent reduction in requirements or other weakening of the Code.
22. A number of respondents flagged areas where they perceived possible changes of meaning. Respondents also made a number of other drafting suggestions, including suggestions aimed at reducing duplication of material and improving the flow and readability of the text. The IESBA gave careful consideration to each of the comments and suggestions.

IESBA Agreement in Principle

23. The IESBA agreed to revisions to Structure ED-1 where respondents were of the view that its initial proposals might have inadvertently changed the meaning of the Code. The IESBA also agreed to revisions to its initial proposals to incorporate respondents’ drafting suggestions when they improved the readability and usability of the proposed restructured Code.

The Guide to the Code

24. Structure ED-1 proposed that the Guide be included within the body of the proposed restructured Code. The IESBA had considered that it was important that the Guide should be read with the proposed restructured Code. However, respondents commented that the Guide was a navigational aid and should not contain application material as it does not have the same authority as the Code. In addition, it was felt that placement of application material in the Guide could also change its meaning.
25. Certain application material relating to disproportionate outcomes and ethical conflict resolution was located in the Guide (paragraphs 10-12). Respondents considered this to be important material which should be located in the body of the Code.

IESBA Agreement in Principle

26. The IESBA determined to separate the Guide from the Code. The IESBA also decided to return the material regarding disproportionate outcomes and ethical conflict resolution to the body of the Code (see paragraphs 100.3 A2, and paragraphs 110.3 A2-A3 of the agreed-in-principle text). In addition, the IESBA decided to add to the Guide material from the Code to clarify that requirements paragraphs are designated with an 'R', as well as material to explain the relationship between requirements and any specific exceptions (see paragraphs 9-10 of the Guide). The IESBA also added material in the How to Use the Code Section of the Guide (paragraphs 7 and 8) to explain that:
 - All of the requirements and application material are to be read and applied in the context of complying with the fundamental principles, applying the conceptual framework and, in relation to audit, review and other assurance engagements, being independent.
 - Proper application of a particular section of the Code requires knowledge and understanding of the relevant section and the entire text of Part 1. The requirements and application material set out in any subsection are to be read in conjunction with the requirements and application material set out in the related section.

Use of “May” versus “Might”

27. In Structure ED-1, the IESBA had proposed limiting the use of the term “may” to denote permission under the Code to undertake a specific action, and the use of the term “might” to refer to possible matters, events or actions. The IESBA had proposed taking this approach to eliminate the ambiguity under the extant Code where the term “may” can denote both a permission and a possibility.
28. A respondent queried whether using “might” instead of “may” implied a weakening of some of the extant Code’s provisions.

IESBA Agreement in Principle

29. The IESBA determined to add descriptions of the terms “may” and “might” to the Glossary. To minimize the risk of ambiguity and confusion through inconsistent use of those terms, the IESBA agreed to limit the use of the term “may” in the Code only to circumstances where it intends that the Code grant a professional accountant specific *permission* to take a particular action in certain circumstances, including as an exception to a requirement. It also agreed that the term “might” should be used in all other cases to denote the possibility of a matter arising, an event occurring or a course of action being taken.

30. The IESBA does not believe that changing “may” to “might” in the relevant provisions in accordance with the specific description of “might” in the Glossary results in a weakening of the Code because it believes the restructured provisions retain the same original intended meaning under the extant Code.

Navigability

31. There was widespread support from respondents concerning the navigability of the proposals in Structure ED-1. The principles underlying the approach to the restructuring were broadly supported as being simple, clear, adequate, more conducive to navigation, and similar to those in other standards and codes. Respondents, however, had mixed views about the proposed numbering system. Among respondents who did not support the proposed numbering system, there was no consensus as to what it should be.
32. Separately, respondents made suggestions for further structural improvements, including:
- Raising the profile of the fundamental principles and the IIS. They suggested giving the IIS more recognizable titles than “C1” and “C2”.
 - The use of bold font or other highlighting for requirements.
 - Keeping subsections to a minimum and improving the linkage between subsections and overall sections where unclear or weak.

IESBA Agreement in Principle

33. The IESBA noted the widespread support from respondents for the restructuring proposals. In response to the suggestions made, the IESBA agreed to rename the various parts of the Code as follows:
- Part 1 – *Complying with the Code, Fundamental Principles and Conceptual Framework* (Sections 100 to 199)
 - Part 2 – *Professional Accountants in Business* (Sections 200 to 299)
 - Part 3 – *Professional Accountants in Public Practice* (Sections 300 to 399)
 - International Independence Standards
 - Part 4A – *Independence for Audits and Reviews* (Sections 400 to 899)
 - Part 4B – *Independence for Other Assurance Engagements* (Sections 900 to 999)
34. The IESBA reaffirmed its view that the numbering system used in Structure ED-1 is appropriate because it accomplished a number of objectives, including simplicity, enhanced visibility of requirements versus application material, and flexibility to add future material, both within an existing section and when introducing new sections.
35. The IESBA debated at some length the use of bold font to denote requirements. The IESBA noted that the use of bold font could increase the risk that the application material would be overlooked. In addition, the IESBA noted that during its project to clarify its standards (the “Clarity” project), the International Auditing and Assurance Standards Board (IAASB) had acknowledged that if the text of a standard is in the same font, this would eliminate debate about the relative importance of text in bold font and text in regular font. The IESBA therefore concluded that the use of the prefix “R” and

the suffix “A” sufficiently differentiated requirements from application material in the restructured Code.

Audit Includes Review

36. Structure ED-1 proposed placing most definitions and descriptions in the Glossary, including words that were included in the “Terms Used” paragraphs. It proposed that descriptions from the Glossary be included in the body of the text and be flagged in a footnote the first time that they occur in a section. One such term is “audit.” Similar to the extant Code, the IESBA is of the view the term “audit” should continue to mean “review” for the purposes of the IIS.
37. There was widespread support from respondents who commented on this proposal. Some respondents felt that the clarification indicating that the term “audit” includes “review” should be in the body of the Code in addition to the Glossary and should not be limited to a footnote. Other respondents expressed the view that distinguishing audits from reviews enhanced clarity. A respondent suggested that the restructured Code state that C1 (Part 4B in the agreed-in-principle text) equally applies to review engagements instead of indicating that references to an audit engagement include a review engagement.

IESBA Agreement in Principle

38. The IESBA agreed that:
 - Certain terms should be included in both the Glossary and the body of the Code.
 - It is appropriate for the restructured Code to deal with audits and reviews in the same standards, and that this be clarified in the body of the Code.
 - The restructured Code should state that the standards continue to apply equally to audit and review engagements, and note that adopting organizations, if they so wished, could choose to distinguish “audit” and “review” separately in their versions of the Code.
 - Descriptions would be included in the body of the restructured Code when they first appeared rather than being denoted by a footnote.

Title

39. Structure ED-1 proposed that the restructured Code be titled *International Code of Ethics Standards for Professional Accountants*. Respondents were supportive of inclusion of the word “International” in the title. However, views on other elements of the title varied, with a few respondents finding the proposed title cumbersome and others expressing particular concern about combining the two terms “Code” and “Standards.”

IESBA Agreement in Principle

40. The IESBA determined that the new title be as follows:

International Code of Ethics for Professional Accountants
(including *International Independence Standards*)
41. The IESBA determined that using the above title appropriately emphasizes the principles basis of the Code. The revised title also makes clear that the Code includes standards addressing independence, thereby signaling that the Code contains requirements for which compliance is subject to specific regulatory oversight and enforcement.

Exceptions

42. A few respondents suggested that permitted exceptions to requirements in the Code be included in or placed adjacent to the relevant requirement.

IESBA Agreement in Principle

43. The IESBA determined that:
- Exceptions be located as close as possible to the related requirement, with only necessary application material in between.
 - Requirements be linked to their exceptions by the use of the words “subject to” and that exceptions be linked to their requirements by the use of the phrase “as an exception to” so as to improve the clarity of the Code.

Other Matters

44. During the restructuring work, the IESBA identified a number of matters that could involve potential changes to the Code outside the scope of the Structure project. The IESBA is considering these matters as it develops its next strategy and work plan.

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