

**October 31, 2019**

**IFAC Small and Medium Practices (SMP) Committee Response to the International Ethics Standards Board for Accountants (IESBA) Exposure Draft: *Proposed Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants***

**INTRODUCTION**

The SMP Committee (SMPC) is pleased to respond to the IESBA (the Board) on this Exposure Draft (ED). The SMPC is charged with identifying and representing the needs of its constituents and, where applicable, to give consideration to relevant issues pertaining to small-and medium-sized entities (SMEs). The constituents of the SMP Committee are small-and medium-sized practices (SMPs) who provide accounting, assurance and business advisory services principally, but not exclusively, to clients who are SMEs. Members of the SMP Committee have substantial experience within the accounting profession, especially in dealing with issues pertaining to SMEs, and are drawn from IFAC member bodies representing 22 countries from all regions of the world.

**GENERAL COMMENTS**

The SMPC has closely followed the IESBA's current project on Role and Mindset Expectations of Professional Accountants (PAs) from the beginning when it was known as the "Professional Skepticism" project. We have provided a number of comment letters for the Board and Task Force's consideration, as well as feedback during our various SMPC meetings.

The SMPC [response](#) to the Consultation Paper on *Professional Skepticism – Meeting Public Expectations* highlighted the importance for the public to have an appropriate level of trust in the information provided by a PA as being of a standard where they can have confidence that it has been prepared with the necessary integrity and due care to enable quality and reliable reports to be produced.

We believe where the problem can arise is that the public may not understand the different types of reports and roles of PAs in practice. This includes an awareness that the depth of work performed and the individual degree of reliance on information provided by the client differs significantly depending on the type of the role or engagement. Therefore, the issue of addressing public trust in the profession is also one of educating the users of information prepared by PAs of these differences and at the same time, acknowledging there is an underlying requirement that certain standards must be adopted by a PA in order to prepare quality output.

The SMPC is supportive of the Board's conclusion that the Code is not an appropriate place to promote any form of mission statement or professional oath as suggested in some round table sessions last year.

We continue to believe that the fundamental principles already in the extant Code (especially integrity, objectivity and professional competence and due care) are sufficiently robust to meet the standard of behavior expected of PA's. We support the IESBA's decision not to expand these principles to include "moral courage", for the reasons outlined in the Explanatory Memorandum.

It is important that the Board continues to maintain a principles-based approach in proposing any changes to the Code and does not impose requirements that may prove difficult for SMPs to apply and which have an adverse impact on SMEs.

The IFAC [Global SMP Survey 2018](#) highlighted that one of the top challenges faced by SMPs is keeping up with changes in regulation and law. We encourage the Board to be sensitive to balancing the pace of change, the impact on firms and Professional Accountancy Organizations (PAOs), particularly in relation to translation and training, as well as the overall global adoption and implementation of the Restructured Code. In our [comment letter](#) to the IESBA Strategy 2019-2023 we supported a pause in new changes to the Code and acknowledge that in the final version, IESBA agreed that new projects would not become effective before June 15, 2020 unless there is an urgent need to respond to new or unforeseen circumstances. The Board may wish to reflect on whether this timeframe remains appropriate. There is a risk that jurisdictions or other users may not adopt or translate the Code in a timely manner because of the frequency of changes, therefore delaying the impact for the overall accountancy profession.

While the SMPC generally supports the proposition that the mindset and behavioral characteristics set out in the ED should be expected of all PAs when performing professional activities, the lack of a clear definition and common understanding of public interest remains an issue as the interpretation of acting in the public interest can be highly subjective.

While the SMPC is supportive of the Board exploring concepts other than professional skepticism to capture the behavior expected of all PAs, we are not convinced it is necessary to add a standalone requirement in the way currently proposed outside of the fundamental principles. We are concerned that the proposed approach (described as inquiring mind) may have a number of unintended consequences, including for regulators to expect PAs to document how they have exercised such behavior every day on every task performed. It may also create a need to go beyond what the client/ employer asked of the PA and "critically assess" or "investigate" further without having been instructed to do so (possibly without informing that party beforehand). This involves issues such as who bears the costs (especially if the PA's extra work results in being able to allay any fears he or she had, of a client or employer) and requires careful consideration of the potential adverse consequences to the individual arising from standing his or her ground (para. 120.16 A2).

We are also concerned about changes related to upholding ethical values. The proposed amendment states that "*compliance with the Code... involves upholding the ethical values upon which the Code is based...*", which we understand is intended to ensure that PAs comply not only with the letter of the Code but also its spirit. Further explanation of what the ethical values upon which the Code is based may be required; otherwise there is a further risk of confusion. A requirement to "do more" beyond what is already required within the Code is very unclear. Also, it is debatable whether this can be legally enforced.

These points are expanded on below in response to the specific questions.

## **SPECIFIC COMMENTS**

- 1. Do you support the proposals in Section 100 that explain the role and values of professional accountants as well as the relationship between compliance with the Code and professional accountants acting in the public interest? Are there other relevant matters that should be highlighted in these paragraphs?**

While we consider the statement in Para 100.1 A1 that “*Compliance with the Code enables accountants to meet their responsibility to act in the public interest and involves .....*” has some merit, the Committee does not support the subsequent sentence “*In acting in the public interest, a PA’s responsibility is not exclusively to satisfy the preferences or requirements of an individual client or employing organization when performing professional activities*”. Without appropriate explanation of what this shall involve in practical terms (i.e., what is the trigger for action, what exactly is the work effort and how shall the PA address the situation - to resign/ speak to client or TCWG/ employer/ withhold work-to-date etc.), it sets a very wide expectation on how a PA is expected to discharge their responsibility vis-à-vis the client or the employing organization when viewed from a mostly undefined, public interest perspective. There is also a question of legal enforceability without a clear direction within the Code.

The Code is principles-based and includes fundamental principles. One of the main reasons for this structure is that it is intended to stay robust even when times and expectations are changing. We believe the Code is already robust enough to meet these challenges. Highlighting the importance of acting in the public interest when this term does not have a definition that meets a global standard would be extremely challenging for PAs and will likely be interpreted very differently from jurisdiction to jurisdiction.

A PA needs to be seen as trustworthy by clients and employing organizations. So, when a PA knowingly acts contrary to the preferences or requirements of an individual client or employing organization, there needs to be a robust mechanism that will drive the PA to act in such a manner. It should not be something that happens regularly and, hence, the Code should acknowledge that such situations would be expected to relate to serious matters and be relatively rare. At most, a PA could be expected not to act in such a way as would be contrary to his or her understanding of the public interest in the specific circumstances (i.e., the PA’s action(s) would involve consideration of the public interest). We suggest IESBA consider rephrasing this aspect along these or similar lines.

The proposed amendment also states that “*compliance with the Code... involves upholding the ethical values upon which the Code is based...*”, which we understand is intended to ensure that PAs follow the spirit of the Code rather than just following the Code to the letter. Further explanation of what these ethical values are may be required; otherwise there is a further risk of confusion. To “do more” beyond what is already in the Code is very unclear. Also, it is debatable whether this can be enforced in a court of law.

We are not convinced with the need for para.100.1 A3 and feedback indicates it is confusing under the present header. If IESBA decides to retain the text, it may be more appropriate for it to be placed in the preface to the Code.

- 2. Do you support the inclusion of the concept of determination to act appropriately in difficult situations and its position in Subsection 111?**

While we agree in essence with the proposed changes, how it will be operationalized is likely to cause concern for many PAs and SMPs. A more robust mechanism (similarly raised in Question 1 above) involving threshold/ severity, work effort etc., to guide the PA to act appropriately may be needed, especially when doing so can create potential adverse personal or organizational consequences.

Aside from the Code, a supportive eco-system (such as the option of obtaining advice from an appropriately knowledgeable and experienced individual through a telephone hotline or via e-mail) is also required to guide the PA to act appropriately in difficult situations. Additional support could therefore be expected to be provided, for example by PAOs in order to help their member navigate such difficult dilemmas or situations. Recently, the IFAC Professional Accountants in Business (PAIB) Committee shared some [examples](#) of how some PAOs are undertaking various ethical activities to better support their members.

There is concern that “*having the determination to act appropriately*” (para. 111.1 A2) will cause translation issues and it may imply that the intent is more important than the actual action. The Board must also recognize that “having the determination to act” is one thing; the PA will still need to have the fortitude or “backbone” to carry out the action.

**3. Do you support the proposal to require a professional accountant to behave in a manner that is consistent with the profession’s responsibility to act in the public interest in paragraphs 110.1 A1 (e) and R115.1?**

The SMPC does not support the current proposal, as it significantly widens the type and scope of assignment and the number of parties (users of output) where PA might be challenged or possibly even sued, contractual law notwithstanding. Hence, it is important for the expectation under the context of public interest to be defined. As suggested above, at most a PA could be expected not to act in such a way as would be contrary to his or her understanding of the public interest in the specific circumstances (i.e., the PA’s action(s) would involve consideration of the public interest).

Guidance material covering a trigger for action, the extent of the work effort for further investigation and critical evaluation and how the PA can address those situations satisfactorily (such as to discuss with clients or TCWG or the withholding of work to-date etc.) would be helpful.

In our view, the term “public interest” is likely to be subject to various different interpretations, not least where cultural differences come into play. The Board may want to reconsider the need for a project on the meaning of public interest in the global context. In our view, such project will need to be a collaborative effort of IESBA and other standard setters such as IAASB and possibly, PIOB and other regulators with a global remit. As mentioned in the IESBA Strategy Survey of April 2017, the Code currently does not expand upon individual public interest obligations and therefore, contains very little application material relating to a PA’s public interest responsibilities. The lack of a clear definition and common understanding of public interest remains an issue as the interpretation of acting in the public interest can be highly subjective. For example, the degree of public interest in the work performed by the profession is not uniform. It can vary based on the type of engagement performed e.g. audit as compared to compilation engagements. The level of staff (e.g. in a practice, a partner compared to junior staff member) is also a factor. While there is a widespread recognition of the collective contribution of SMEs to the global economy, and hence the sector’s high level of public interest, the public interest element in any one small practitioner’s client base is expected to vary.

**4. *Notwithstanding that the IESBA has a separate Working Group that is exploring the implications of developments in technology, are there any additional matters relating to the impact of technology beyond the proposals in paragraphs 110.1 A1(b)(iii), 113.1 A2 and 120.12 A2 that you consider should be addressed specifically as part of the Role and Mindset project?***

The SMPC recognizes the significant impact technology developments are having on the accountancy profession and the need to reinforce the value of PAs' professional judgment, knowledge and expertise. However, as the Technology Working Group is not due to present its Phase 1 final report and recommendations for the Board's consideration until December 2019, we question the timing of the proposals to include reminders in Part 1 of the Code of the potential impact of technology on compliance with the Code. The Board agreed that including examples involving technology would be premature given the Technology Working Group's ongoing work and we believe this should be the same approach for these other changes and that all the proposals should therefore be deferred.

Any changes in the Code will need to be translated and in certain jurisdictions, other due process will also be required before the Code can be adopted. Unless the changes are critical, non-substantive amendments should be avoided where possible. The SMPC believes that the Board needs to be more sensitive to balancing the burden arising from the changes to the Code and the likely benefits to the public interest.

Para R112.1 states that a PA shall comply with the principle of objectivity, which requires an accountant to exercise professional or business judgment without being compromised by (c) undue influence of, or undue reliance on individuals, organizations, technology or other factors. In Para R220.4, it has been added that when preparing or presenting information, a PA shall: (e) avoid undue reliance on individuals, organizations or technology. The SMPC is concerned about the inclusion of "undue reliance" and how such undue reliance could happen in practice. For a person in a senior management capacity, it is inevitable that there will be a certain extent of reliance on individuals, systems or infrastructure. The question arises about when that reliance crosses the line to become undue reliance. For clarity of application, there should be examples to illustrate undue reliance on individuals, organizations or even on technology, where warranted.

We recommend the Board consider revising para 113.1 A2 to state that the skill sets have to be appropriate to the role or work performed by the PA. At present, it just includes "relevant" which could be too vague as a term. It should be tailored to ensure the PA can comply with the competence requirements applicable to his or her individual work areas.

**5. *Do you agree with the concept of an inquiring mind as set out in the proposals in Section 120?***

The SMPC is supportive of the IESBA's decision to reserve the term "professional skepticism" for audit and assurance activities. The Committee is also supportive of the Board exploring concepts other than professional skepticism (such as inquiring mind) to capture the behavior expected of all PAs but is not convinced it should add a standalone requirement in the way currently proposed outside of the fundamental principles.

The Committee agrees (and this has been our consistent position) that all PAs must bring certain level of diligence to their work (and this must be proportionate to their level of seniority, experience etc.) and is supportive of the Board exploring concepts other than professional skepticism to capture the behavior of all PAs. However, as noted in our earlier submission, some members consider that the current Code is already

sufficiently robust and do not believe there is a need for a stand-alone requirement outside of the fundamental principles. If there is a need to reinforce the Code, there may be merit for the IESBA to consider approaching this project by highlighting through guidance material (this could be outside the Code) the characteristics which should be expected of PAs that captures the essence of an “inquiring mind”- while acting in compliance with the Code’s fundamental principles. The notion is akin to not turning a blind eye when involved in a professional activity and/ or acting in a professional capacity in tandem with the actions of others.

We noted that the application material covering inquiring mind has been partly taken from the existing content dealing with “professional judgement”; this may cause inadvertent confusion because of the overlap between the terms.

We understand the rationale for the new description of professional judgment in the glossary of the Code to be appropriate for application to all PAs. However, we are concerned that the description is not more closely aligned with the definition in the IAASB standards as it introduces different concepts such as “skill”, “interests and relationships” etc. The Explanatory Memorandum does not cover whether the IAASB supports the direction of this proposal. In addition, it may raise the question of whether it is now different to “business judgement” which is referred to with professional judgment each time (professional or business judgment).

**6. Do you support the approach to addressing bias? If so, do you agree with the list of examples of bias set out in paragraph 120.12 A2? Should any examples be omitted or new ones added?**

We generally support the addition of bias and the list of examples of different types of bias. However, we are concerned that the list could become a checklist for regulators.

We strongly support the need for the Board to continue to liaise with the IAASB to ensure there is appropriate alignment with the IAASB’s text relating to bias in ISA 220 (Revised)<sup>1</sup>.

There is a general statement about mitigating bias (120.12 A3), but it may be worth exploring more specifically what accountants can do to reduce bias and its link to professional judgement. Guidance material could be useful in this context.

**7. Are there any other aspects about organizational culture in addition to the role of leadership that you consider should be addressed in the proposals?**

We agree that the internal culture of an employer can significantly impact whether PAs comply with the Code and act ethically. Hence, we agree that the role of leadership in the firm or company in setting, demonstrating and encouraging an ethical culture is fundamental. However, as indicated in our response to question 1, we are concerned that the new application material (120.13 A1 and A2) refers to “ethical values” without further explanation of what these are intended to entail.

We do not consider there are other aspects about organizational culture, which should be addressed in the proposals. The challenge for PAs may not be limited to what is included in the Code. The SMPC believes that it will need the entire eco-system to work together in a way that can provide the impetus for a PA to

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<sup>1</sup> International Standard on Auditing 220 (Revised), *Quality Management for an Audit of Financial Statements*

comply with the Code and act ethically and in certain instances, with the appropriate resolve despite possible adverse personal consequences.

#### **CONCLUDING COMMENTS**

We hope the IESBA finds this letter helpful in informing the Board's deliberations on your role and mindset expectations project. Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,

A handwritten signature in blue ink that reads "Monica Foerster".

Monica Foerster  
Chair, SMP Committee