

**DATE:** February 18, 2011  
**TO:** Ethics Consultative Advisory Group  
**FROM:** Ken Dakdduk, Chair IESBA  
**SUBJECT:** Report from the IESBA

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## **Introduction**

This report summarizes the activities of the IESBA since the last Ethics CAG meeting in September 2010. The report also provides an update on each of the working projects of the IESBA.

## **Meetings**

The IESBA met in Singapore, Singapore on November 2-3, 2010 and New Delhi, India on February 6-8, 2011. The dates and locations of future IESBA meetings are as follows:

- June 15-17, 2011 (Warsaw, Poland)
- October 17-19, 2011 (New York, United States)
- February 20-22, 2012 (TBD)
- June 18-20, 2012 (TBD)
- October 15-17, 2012 (TBD)

## **Strategy and Work Plan 2011-2012**

At its February 2011 meeting, the IESBA approved its work plan for the period 2011-2012, which sets the direction and priorities for the IESBA. During this period the IESBA intends to build on the strong base established by the revised Code of Ethics for Professional Accountants issued in July 2009. The plan comprises three activities:

- Development of standards—additional guidance on conflicts of interest; guidance on responding to suspected fraud and illegal acts; review of the inadvertent violation provisions;
- Supporting adoption and implementation of the Code—issuance of additional staff Q&As as needed; understanding compliance issues faced by SMPs/SMEs; and
- Efforts to facilitate convergence of the Code with the standards of other jurisdictions.

## **Monitoring Group Report**

The IESBA discussed the recommendations of the Monitoring Group that have a direct bearing on the work of the board. Board members' comments included:

- It is important that the profession be sufficiently represented on the board.

- What matters most about the IESBA chair is the integrity of the individual rather than where they work.
- If there is a concern about board composition, unclear how increased transparency of board members' backgrounds, qualifications, and affiliations would help.
- Public interest matters are carefully and fully considered. Would be helpful to obtain from the Monitoring Group a better understanding of who would be seen as representing the public interest.

## **Inadvertent Violation**

At its November 2010 meeting, the IESBA approved a project proposal to reconsider the paragraphs in the Code that address an inadvertent violation of a provision of the Code. At its February 2011 meeting, the IESBA discussed Task Force proposals and provided input on preliminary wording for a new provision in the Code. The Task Force plans to present a revised document to the IESBA for approval as an exposure draft at its June 2011 meeting. Among the key tentative decisions reached by the board are:

- Guidance to deal with violations is needed; should apply for independence only.
- Should focus on addressing the impact of a violation, regardless of whether it was inadvertent; no need to use the term "inadvertent."
- Need to reduce the risk that the guidance will promote willful violations.
- Discussion with those charged with governance should be required. May be appropriate to require that all violations be reported, even insignificant violations.
- Specific documentation requirements should apply.

The matter is addressed in CAG Agenda Item C.

## **Responding to Suspected Fraud and Illegal Acts**

At its November 2010 meeting the IESBA approved a project proposal to develop guidance for professional accountants when they encounter a suspected fraud or illegal act. At its February 2011 meeting, the IESBA discussed Task Force proposals and provided input on the proposed direction. Among other things, the IESBA tentatively decided that :

- Breaching confidentiality by disclosing outside of the client or employing organization should not occur based on a highly subjective judgment of what is unethical/improper.
- Not all illegal acts should fall within the scope of the guidance, but focusing only on those that have a direct/indirect effect on financial reporting might be too limiting.
- The response should vary if an accountant is in public practice versus in business.
- External disclosure should be required if in the public interest and not contrary to law.
- Consideration may need to be given to whether protections are afforded the accountant and there is an appropriate authority to disclose information to.

The Task Force met after the IESBA meeting and reached tentative recommendations on several matters that will be discussed with the IESBA in June. Those matters are described in CAG Agenda Item D.

## **Conflicts of Interest**

At its November 2010 and February 2011 meetings, the IESBA discussed and commented on Task Force proposals for providing additional guidance for professional accountants when dealing with conflicts of interests. Key matters discussed included:

- Guidance would contain a description of a conflict, examples, a reasonable and informed third party test, a step for identifying/evaluating significance, and safeguards.
- The project scope should include guidance on ethical behavior in Section 320.
- May be appropriate to require disclosure and consent in all cases.
- Interest/relationship of network firms should be considered if a firm has reason to believe it creates a conflict.

The Task Force met after the IESBA's February meeting and reached tentative recommendations on several matters that will be discussed with the IESBA in June. Those matters are described in CAG Agenda Item E.

## **SME/SMP Working Group**

The IESBA was informed by respondents to its draft strategic work plan last year that SMEs and SMPs face unique and challenging issues in complying with the Code. The IESBA believes it is important to understand what those issues are and determine how it should respond. At its February 2011 meeting the IESBA approved the terms of reference of an IESBA SME/SMP Working Group. The Working Group's objective is to identify those issues, particularly with respect to SMPs serving SMEs, and recommend to the IESBA ways in which the board might address them.

The Working Group includes two members of IFAC's SMP Committee, an individual with the ICAEW, an accountant who works for a small company in the US, and a representative of FEE. The group is being led by an IESBA member with practice experience in the small and mid-size entities market. The group had a two-day meeting in January to establish its terms of reference.

The Working Group will be seeking input from those with different geographic and other perspectives. Its participation in IFAC's SMP forum in March in Istanbul will contribute to this objective and it may make targeted inquiries of individuals and organizations. It also will consider whether SMPs would benefit from guidance on performing non-assurance services for non-assurance clients.

The IESBA will receive an interim report on the group's findings at its June 2011 meeting and a final report along with the group's recommendations at its October 2011 meeting.

## **Impact Analysis**

The IESBA concluded, at its October 2009 meeting, that it would be useful for the two project task forces (Conflicts of Interest and Responding to Fraud and Illegal Acts) to perform an impact analysis so that a process for performing such an analysis can be developed and refined as necessary for efficient ongoing application.

The two Task Forces will present an impact analysis at the IESBA's June 2012 meeting.

## **Implementation and Adoption**

In December 2010, staff issued some non-authoritative questions and answers (Q&As) to support adoption and implementation of the Code. The Q&As are contained in Agenda Paper B-2 for the reference of CAG members.

## **Convergence**

At its November 2011 meeting, the IESBA discussed a stand-alone document identifying the independence requirements related to public interest entities. The IESBA provided input on changes to be made to the document, which would then be used to benchmark the Code requirements against the recommendations of select jurisdictions. At its February 2011 meeting, the IESBA received an update on the status of the benchmarking exercise. The IESBA will discuss a schedule of differences at its June 2011 meeting with the view to determining the extent to which the IESBA should focus its attention on these differences for possible future revisions to the Code.

The IESBA has also developed a one page high level summary of the conceptual framework approach and the prohibitions in the Code that apply to public interest entities. This summary is contained in Agenda Paper B-3 for the reference of CAG members.

## **Internal Audit**

The IESBA continues to closely follow the International Auditing and Assurance Standards Board (IAASB) project to revise ISA 610 *Using the Work of Internal Audit*. An IESBA member is a correspondent member of the IAASB's Task Force. At its February 2011 meeting, the IESBA discussed comments received by the IAASB on its exposure draft regarding the interaction of the definition of engagement team in the Code of Ethics and the provision of direct assistance by internal auditors. The IESBA agreed to consider the matter further, including whether a revision to the definition would be appropriate, at its June 2011 meeting.

## **Reviews and Compilations**

The IESBA has been closely following the IAASB project to revise International Standard on Review Engagements 2400 *Engagements to Review Financial Statements* and

International Standard on Related Services 4410 *Engagements to Compile Financial Statements*. An IESBA member is a correspondent member of the Task Force.

### **Definition of Professional Accountant**

At its February 2011 meeting the IESBA discussed a paper prepared by IFAC staff addressing the definition of a professional accountant. That term is currently defined in the Code of Ethics as “an individual who is a member of an IFAC member body.” IFAC staff has developed a proposed definition to address concerns that the existing definition does not recognize that professional accountants may not necessarily be members of IFAC member bodies. The IESBA agreed to form a small working group to consider the implications of the proposed definition on the Code.

### **IFAC Exposure Draft Public Interest Framework**

At its February 2011 meeting, the IESBA discussed the IFAC exposure draft containing a policy position paper “A Public Interest Framework for the Accountancy Profession.” The IESBA agreed that it would provide a verbal response to the Exposure Draft

### **EU Green Paper**

The IESBA responded to the EU Green Paper *Audit Policy: Lessons from the Crisis* in December 2010. At its February 2011 meeting, the IESBA received an overview of the responses to the EU Green Paper *Audit Policy: Lessons from the Crisis*. The IESBA agreed that it would closely monitor developments with the view to better informing the IESBA of issues it may wish to address as a result of comments on the Green Paper.