

Meeting: IESBA CAG
Meeting Location: New York
Meeting Date: March 10, 2014

Agenda Item

C

Non-Assurance Services (NAS)

Objective of Agenda Item

1. To obtain CAG Representatives' views on proposed changes to the subsections within Section 290¹ of the Code addressing management responsibilities² and the preparation of accounting records and financial statements.³

Project Status and Timeline

2. The IESBA approved the project proposal at its September 2013 meeting.⁴ The project is focused on:
 - a) Clarifying the NAS provisions in the Code concerning management responsibilities;
 - b) Clarifying the phrase "routine or mechanical" as it pertains to the provision of accounting and bookkeeping services; and
 - c) Examining the "emergency exception" provisions related to bookkeeping and taxation services.
3. The Task Force presented a first draft of proposed changes to the Board at the December 2013 IESBA meeting. The Task Force met in January 2014 to consider the feedback from the Board. The Task Force will present a revised draft of the proposed changes at the April 2014 IESBA meeting.
4. The Task Force anticipates Board approval of the changes for exposure at the July 2014 IESBA meeting.

September 2013 CAG Discussion

5. The CAG considered the project proposal at its September 2013 meeting. Below are extracts from the draft minutes of the September 2013 CAG meeting,⁵ and an indication of how the Task Force or IESBA has responded to date to CAG Representatives' comments:

¹ Section 290, *Independence – Audit and Review Engagements*

² Paragraphs 290.162 – 290.166

³ Paragraphs 290.167 – 290.173

⁴ The project proposal can be accessed at: <http://www.ifac.org/sites/default/files/meetings/files/Agenda%20Item%208-A%20-%20Revised%20NAS%20Project%20Proposal.pdf>.

⁵ The minutes will be approved at the March 2014 IESBA CAG meeting.

Representatives' Comments	Task Force/IESBA Response
<p>Mr. Hansen expressed support for moving forward with the project. He noted that he was on an American Institute of Certified Public Accountants (AICPA) attest Task Force that revised aspects of the AICPA's Code and that the task proved challenging. He was of the view that a significant part of the problem resides in the small- and medium-sized entity (SME) market, for example, whether a bank reconciliation is an internal control activity or a management responsibility, and whether or not a cash to accrual basis conversion is a non-attest service. In respect of the latter, he noted that the AICPA had concluded that this type of service is not an assurance service but a management responsibility.</p>	<p>Ms. Sapet noted that all these matters could be considered by the Task Force with respect to whether useful guidance could be developed. She cautioned, however, that care would be needed regarding the level of detail to build into the Code as it would be important for the Code to focus on principles.</p>
<p>In relation to communication with those charged with governance (TCWG), Mr. Ratnayake noted that practice can be inconsistent. He noted that in some countries, some within TCWG are interested in financial reporting matters whereas others are close to management. So the communication itself can give rise to good outcomes in some cases but not in others.</p>	<p>Ms. Sapet noted that as the Code is for professional accountants, it is difficult for it to place an obligation on TCWG. She also noted that the IESBA had discussed the topic of communication with TCWG at some length in the Breaches project. However, the Task Force had not yet determined if there would be merit in TCWG being involved in approving NAS.</p>
<p>Mr. Bluhme noted that the IFAC Small and Medium Practices (SMP) Committee was supportive of the topics included in the project proposal and that these were identified in the IFAC SMP Committee's recent survey of SMPs. However, he was of the view that the proposed timeline appeared aggressive.</p>	<p>Support noted.</p> <p>The Task Force has reconsidered the timeline and anticipates Board approval of the exposure draft at the July 2014 IESBA meeting.</p>
<p>Ms. Blomme noted that in the context of the audit reform discussions in the European Union (EU), the European Commission proposals are much more restrictive than the Code, but the EU Parliament in its discussions has been taking a view very close to the Code. She was of the view that this simply demonstrated that there is significant room for interpretation, especially related to the provision of tax service, and taking management responsibilities. She observed, however, that the outcome of the project may not arrive in time for the</p>	<p>Ms. Sapet acknowledged the short timeline for the project but noted the importance of moving timeously given the narrow scope of the project and Ms. Blomme's comments about the IESBA's deliverables not arriving in time for the EU discussions.</p>

Representatives' Comments	Task Force/IESBA Response
EU discussions.	
<p>Mr. Hansen expressed support for a principles-based approach to the Code. At the same time, he noted that practitioners often ask whether specific services are permissible. Accordingly, he was of the view that application often moves to a rules-based approach from a practice perspective and he hoped the Task Force could be open to that.</p>	<p>Ms. Sapet noted that the Task Force is aiming to develop guidance recognizing that there is room for improvement in the Code. She highlighted as an example the fact that some safeguards in the Code are difficult for professional accountants to implement. She emphasized, however, that the Task Force will not focus on rules. Nevertheless, she agreed that clarity was needed with respect to implementation. Mr. Holmquist felt that Mr. Hansen's observation was somewhat contradictory as the Code is actually a mix of principles and rules. He highlighted the Board's view that a rules-based Code would not be the way to go, not only because of the wide variation in legal frameworks around the world, but also because research has demonstrated that the greater the focus on rules, the less thinking professional accountants do. He noted that the reality is that the Code is principles-based but specific in certain areas.</p>
<p>Mr. Ratnayake commented that the areas of internal audit and valuation services, and to some extent taxation services, are ones that can potentially give rise to conflicts relative to audit engagements. He was of the view that the fact that some jurisdictions have more restrictive provisions in these areas would warrant the Board's consideration.</p>	<p>Ms. Sapet noted that the Task Force is aware that some jurisdictions are more restrictive than the Code in the areas of internal audit and valuation services.</p> <p>The Task Force undertook a survey of 26 jurisdictions in March 2013 regarding national ethical requirements pertaining to NAS, including internal audit, valuation and taxation services. The responses from the survey did not provide clear cut directions or majority views on how jurisdictions address these services. The Task Force also discussed the balance between the benefits and risks to audit quality and the public interest concerning valuation, taxation and internal audit services. On the basis of this analysis, the Task Force concluded that there is no case for reviewing the Code's positions on taxation, valuation and internal audit services at this time as the Code's threats and safeguards approach continues to be appropriate.</p>
Ms. Lang noted difficulty in fully understanding the	Ms. Sapet noted that the Task Force had discussed

Representatives' Comments	Task Force/IESBA Response
<p>objective of the NAS paper. She wondered whether it would be more logical to complete the paper before undertaking changes to the Code if the objective of the paper were to establish support for the IESBA's position on NAS in the Code.</p>	<p>this matter and that the NAS paper will be finalized and issued before the IESBA considers whether there is a need to do more on the Code. With respect to the three areas included in the scope of the project proposal, she noted that there was real data supporting a review of these areas.</p>
<p>In relation to the NAS paper, Mr. Baumann noted that the larger firms have been acquiring a number of different businesses outside of audit in recent years, for example, cyber security. He wondered whether the project should look at new and emerging services and whether these are appropriately addressed in the Code.</p> <p>Mr. Holmquist commented that he had become aware of the fact that in the US, the publication of the amount of fees firms earn from NAS provided to their clients has led to a reduction of NAS fees as a percentage of audit fees. Mr. Baumann noted that the comment is generally accurate, consistent with a general decline in NAS fees as a percentage of audit fees, although there has been a modest reversal in this trend recently. He noted, however, that in the US, firms have been acquiring a variety of businesses and that the PCAOB was monitoring this development closely.</p>	<p>Ms. Sapet noted that the Task Force will consider in the paper new areas or services that professional accountants may provide in the future.</p>

Matters for CAG Consideration

A. EMERGENCY EXCEPTIONS

6. Pursuant to the project proposal, the Task Force examined the emergency exception provisions as they applied to bookkeeping (290.174) and taxation services (290.186), and considered the appropriateness of the exception provisions for continued inclusion in the Code. For information, these provisions are included in Agenda Item C-1.
7. At the December 2013 IESBA meeting, the Task Force recommended that the emergency provisions be deleted from the Code on the following grounds:
 - a) A situation in which an emergency provision should be allowable should be so rare and extraordinary that it should not be addressed by the Code, nor should the determination to use the provision be made by the auditor and the client. Rather, such determination should be made by a local regulator;

- b) Removing the emergency provisions would strengthen the Code by removing the potential for misuse of the provision due to subjective terms such as “emergency” and “unusual situations” included in the extant guidance; and
- c) The Code would be strengthened by the fact that if a regulator did allow an emergency provision within a jurisdiction due to a rare and extraordinary event, the firm would have to implement the provisions addressing breaches of the Code, which would address threats to independence during the performance of prohibited services in the emergency exception period.

8. The Board generally agreed with the recommendation of the Task Force.

Matter for CAG Consideration

1. Do Representatives support the recommendation to remove the emergency exceptions from the Code?

B. MANAGEMENT RESPONSIBILITIES

9. Pursuant to the project proposal, the Task Force reviewed the subsection entitled *Management Responsibilities* of Section 290 in order to propose clarifying edits. Agenda Items C-2 and C-3 are mark-up and clean versions, respectively, of the proposed revised subsection.
10. The first change proposed at the December 2013 IESBA meeting relates to the order of the first three paragraphs of the guidance. The Task Force proposed that these follow that of the guidance for internal audit services to provide a more logical order. Thus, the first paragraph of the topic (paragraph 290.162) should continue to contain a description of a management responsibility. The second paragraph (paragraph 290.163) should state the threats associated with assuming a management responsibility. Thus, paragraph 290.165 of the extant Code would be moved to 290.163. The third paragraph of the topic (paragraph 290.164) should include examples of activities that would generally be considered a management responsibility. This order is consistent with other guidance in the Code and provides a logical order of guidance for professional accountants. The Board generally agreed with the proposal.
11. The Task Force proposes clarifying paragraph 290.162 to further describe a management responsibility. In particular, the first sentence has been deleted so that the paragraph clearly provides a concise description of a management responsibility.
12. Also within paragraph 290.162, the Task Force proposes that the term “significant” be deleted in the following sentence: “Management responsibilities involve controlling, planning, leading and directing an entity, including making ~~significant~~ decisions regarding the acquisition, deployment and control of human, financial, physical, technological and intangible resources.” The Task Force agreed that all decisions concerning management responsibilities should be made by the client. If the term “significant” is included in the sentence, there may be ambiguity concerning appropriate decisions of the auditor.
13. The Task Force proposes adding further examples to paragraph 290.164 to further clarify what may be considered to be a management responsibility. Also the sentence stating that advice and certain recommendations may be provided to the client was moved from extant paragraph 290.164 to the

proposed paragraph 290.164 to provide further explanatory language concerning what may not be considered to be a management responsibility.

14. The Task Force noted that extant paragraph 290.164 includes activities that are of an administrative nature in support of management, such as monitoring dates for filing statutory returns. When this paragraph is located under the “management responsibilities” sub-heading, it appears as if the professional accountant may assume “some” management responsibilities. This may cause confusion to users of the Code. Due to language that can be possibly construed as being contradictory and due to the fact that extant paragraph 290.164 contains examples of actual non-assurance services and not guidance concerning the notion of accepting a management responsibility, the Task Force proposes that this paragraph stand alone within the Code with its own sub-heading entitled “Administrative Services.” The Board was in general agreement with this recommendation.
15. The Task Force proposes to amend extant paragraph 290.166 to ensure that the requirement of the firm to be satisfied that a member of management accepts responsibility for the actions of the service is more robust and is more clearly defined. This requirement has been made clearer and more robust by expanding on what is meant by management accepting responsibilities for NAS. In particular, the Task Force proposes to require that the firm be satisfied that the client’s management makes all judgments and decisions that are the proper responsibility of management. This includes ensuring that the client’s management:
 - a) Provides oversight of the service, and evaluates the adequacy and results of the services performed;
 - b) Accepts responsibility for the actions to be taken arising from the results of the service; and,
 - c) Designates an individual, preferably within senior management who possesses suitable skill, knowledge and experience to be responsible at all times for the client’s decisions and to oversee and acknowledge responsibility for the services. A suitable individual would understand the objectives, nature and results of the services and the respective client and firm responsibilities. However, the individual is not required to possess the expertise to perform or re-perform the services.
16. The Board was in general agreement with the proposed provisions.

Matter for CAG Consideration

2. Representatives are asked to provide feedback on the proposed changes to the subsection *Management Responsibilities* of Section 290 of the Code.

C. ROUTINE OR MECHANICAL

17. Pursuant to the project proposal, the Task Force reviewed the subsection entitled *Preparing Accounting Records and Financial Statements* of Section 290 in order to propose clarifying changes. Agenda Items C-4 and C-5 contain the proposed changes in mark-up and clean versions respectively.
18. The proposed changes state that activities that are routine or mechanical “require little to no professional judgment from the professional accountant,” as judgments should be made by management. The proposed change to paragraph 290.171 also reminds the professional

accountant that the performance of such services is subject to the provisions on management responsibilities in proposed paragraph 290.165. This change provides clarity in defining the characteristics of routine or mechanical activities and provides robust guidance requiring the firm to ensure that client management properly accepts all management responsibilities for the services.

19. The Task Force proposes to further amend paragraph 290.171 to provide clear and detailed examples of services that would be considered routine or mechanical. To provide additional clarity, the proposed changes also provide examples of services that would not be considered routine or mechanical.

Matter for CAG Consideration

3. Representatives are asked to provide feedback on the proposed changes to the subsection *Preparing Accounting Records and Financial Statements* of the Section 290 of the Code.

Material Presented – CAG Paper

Agenda Item C-1	Emergency Exception Paragraphs
Agenda Item C-2	Management Responsibilities (Mark-Up)
Agenda Item C-3	Management Responsibilities (Clean)
Agenda Item C-4	Preparing Accounting Records and Financial Statements (Mark-Up)
Agenda Item C-5	Preparing Accounting Records and Financial Statements (Clean)