

Meeting: IESBA CAG
Meeting Location: New York
Meeting Date: September 9-10, 2014

Agenda Item

F

Structure of the Code

Objective of Agenda Item

1. To obtain CAG representatives' input on a draft Consultation Paper *Improving the Structure of the IESBA Code*, including examples of restructured extracts of the Code.

Project Status and Timeline

2. In February 2012, the IESBA agreed to consider how it might improve the structure of the Code to raise the visibility of the requirements and prohibitions in the Code, and to clarify who is responsible for meeting them (Responsibility). Also, various stakeholders have commented on issues associated with the structure, format and clarity of the Code. Some of these issues relate to the usability of the Code and may be impacting adoption and implementation.
3. The CAG discussed the initiative in April and September 2013, and March 2014.
4. At its April 2014 meeting, the IESBA approved the project proposal and established the Task Force.
5. At its July 2014 meeting, the IESBA considered a preliminary draft of the Consultation Paper.

March 2014 CAG Discussion

6. Below are extracts from the draft minutes of the March 2014 CAG meeting,¹ and an indication of how the Task Force or IESBA has responded to CAG Representatives' comment.

Matters Raised	Task Force/IESBA Response
DISTINGUISHING REQUIREMENTS	
<p>Ms. de Beer expressed support for restructuring the Code and making clear what the requirements are, as distinct from the guidance. She wondered whether the Board had considered issuing separate standards rather than a single Code as the concept of individual standards is familiar to users.</p>	<p>Mr. Thomson responded in the affirmative, noting that the Board had considered separate standards to help both those who are more interested in independence and those who are not concerned with independence. He noted that the Board was at the same time conscious of the need to maintain the Code as one package so that users do not ignore certain parts.</p>

¹ The minutes will be approved at the September 2014 IESBA CAG meeting.

Matters Raised	Task Force/IESBA Response
	<p>Apart from the independence provisions, the Task Force has explored the merits of individual standards for the other parts of the Code (Part C and non-independence parts of Part B) and concluded they are principles-based and would also benefit from the linkage to the fundamental principles being retained.</p>
RESPONSIBILITY	
<p>Mr. Dalkin highlighted the US GAO’s experience of providing examples in its code of ethics which then became de facto rules. He advised the Board to take this into consideration as it considers how to further improve the Code.</p>	<p>Point noted.</p>
<p>Mr. Koktvedgaard asked how the responsibility recommendations relate to ISQC 1.</p>	<p>Mr. Thomson replied that paragraph 290.12 already references ISQC 1 and the proposals reinforce the fact that a firm should have policies and procedures that enable relevant individuals to know their responsibilities.</p>
<p>Mr. Fukushima expressed support for categorizing the requirements into three groups: for the firm, for the engagement partner and for the engagement team. He acknowledged that there is variation in size of firms and engagement teams. However, he pointed out that ISQC 1² is clear in placing responsibilities on the firm, and that the International Standards on Auditing (ISAs) are clear in placing responsibilities on the engagement partner or engagement team. He felt that such an approach would increase usability and help with consistent application of the Code in practice.</p> <p>Mr. Thomson noted that the Task Force has discussed this matter and was moving towards clarifying that it is the firm that has the responsibility to identify the individuals who should take responsibility in the particular circumstances.</p>	<p>Point partially accepted.</p> <p>The Code is consistent with the ISAs/ISQC1 by assigning responsibility to the firm, the engagement team and the engagement partner as appropriate. The Task Force is aiming to clarify the circumstances where the Code uses the passive voice and is therefore unclear which of the three categories is responsible. In most instances, it is expected that “the firm” would be the most appropriate alternative to the passive voice, thereby allowing the firm to determine whether responsibility should fall to the engagement team, engagement partner or the firm itself.</p> <p>Relevant extracts from ISQC 1 and ISA 220³ are included in Appendix 1 to this agenda paper.</p>

² 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*

³ ISA 220, *Quality Control for an Audit of Financial Statements*

Matters Raised	Task Force/IESBA Response
<p>He nevertheless noted that the Task Force would take Mr. Fukushima's comments into consideration.</p>	
<p>Mr. Baumann reported that the PCAOB had issued a Concept Release on firms' supervisory responsibilities, and is continuing to look at this area. The PCAOB is not only looking at independence but more broadly at how a firm goes about documenting and implementing its supervisory responsibilities. He added that the PCAOB was moving down the path of having clearer delineation of how responsibility should be carried out. He was of the view that this should improve the quality of accountability and performance.</p>	<p>Point noted.</p>
<p>ELECTRONIC CODE AND REORGANIZING THE CODE</p>	
<p>Mr. Fukushima wondered who would benefit from an electronic Code as firms integrate the Code into their in-house systems and national standard setters integrate the Code into their ethics standards.</p> <p>Mr. Thomson noted that there are some professional accountants (PAs) who are still required to confirm that they are complying with international standards. Accordingly, it would be important to make the Code accessible and easy to navigate for them. He added that reorganization goes hand in hand with repackaging and that some people may be working from the Code. So increased usability may flow through from an e-Code.</p> <p>Mr. Kwok noted that an e-Code is not simply a digitization of the Code. It could, for example allow content to be searched according to a user's needs, such as what are the requirements applicable to audits of public interest entities (PIEs), or what are the requirements applicable to those in the chain of command. In addition, he suggested that an e-Code might allow for</p>	<p>The Board is of the view that the development of an electronic Code may facilitate the re-organization of the Code. The Board has agreed to develop in the short term an HTML version of the Code with enhanced navigation capabilities and hyperlinks to definitions. In the longer term, an enhanced electronic version of the Code would be integrated with a restructured Code.</p>

Matters Raised	Task Force/IESBA Response
explanations of Board deliberations to be attached to particular provisions.	
Ms. Blomme noted that some jurisdictions use the IESBA Code. In addition, the Code is used for cross-border audits in some jurisdictions.	Points noted.
PROJECT PROPOSAL	
Mr. Koktvedgaard noted that if the Board is to approve the Consultation Paper in July it would require a CAG conference call in June, which is not ideal given requests for CAG conference calls on other topics.	Point accepted. The Board now plans to approve the Consultation Paper at its October 2014 meeting.
EXAMPLES OF RESTRUCTURING	
Mr. Koktvedgaard wondered how the description of independence (paragraph 290.6) and PIEs (paragraph 290.25) are reflected in the examples, and how all of these articulate without seeing the front end.	Mr. Thomson replied that given that the entire Section 290 is being restructured, the focus at this stage is on presenting examples which illustrate the overarching principles. Neither paragraph 290.6 nor paragraph 290.25 has been selected for this purpose. It is proposed that the restructured Code would include a link, both in the paper and electronic versions, to a glossary to terms that are described in greater detail, within the Code, than in the definitions section.
Ms. Blomme suggested that cross references between requirements and guidance, similar to the approach taken in the ISAs, would be helpful.	Point accepted.
Mr. James asked when the CAG would be expected to provide input on final proposed illustrative examples. He felt that a conference call may not help. Ms. De Beer agreed with Mr. James, noting that this is a fundamental project and that it is important to obtain the buy-in of all stakeholders.	Mr. Thomson explained that work was already underway to restructure the Code to accelerate the process after the project proposal is approved and that the Consultation Paper will include examples of restructured sections for comment in due course. He added that the timing is driven by the need to move the initiative forward as quickly as possible, noting that the CAG would have the opportunity to consider the draft Consultation Paper in September.

Matters for CAG Consideration

A. DRAFT CONSULTATION PAPER

7. A draft of the Consultation Paper is presented as Agenda Item F-1.
8. At its July 2014 meeting, the IESBA expressed broad support for the Consultation Paper. A number of drafting suggestions were provided for consideration by the Task Force, which have now been addressed in the version set out in Agenda Item F-1.

Matters for CAG Consideration

1. Representatives are asked for input on the proposed Consultation Paper, including the illustrative examples, and for any comments or questions on the Board's approach to the project.

Material Presented – CAG Paper

Agenda Item F-1 Draft Consultation Paper

Appendix

EXTRACTS FROM ISQC 1

Relevant Ethical Requirements

20. The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. (Ref: Para. A7–A10)

Independence

21. The firm shall establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements (including network firm personnel) maintain independence where required by relevant ethical requirements. Such policies and procedures shall enable the firm to: (Ref: Para. A10)
- (a) Communicate its independence requirements to its personnel and, where applicable, others subject to them; and
 - (b) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement, where withdrawal is possible under applicable law or regulation.
22. Such policies and procedures shall require: (Ref: Para. A10)
- (a) Engagement partners to provide the firm with relevant information about client engagements, including the scope of services, to enable the firm to evaluate the overall impact, if any, on independence requirements;
 - (b) Personnel to promptly notify the firm of circumstances and relationships that create a threat to independence so that appropriate action can be taken; and
 - (c) The accumulation and communication of relevant information to appropriate personnel so that:
 - (i) The firm and its personnel can readily determine whether they satisfy independence requirements;
 - (ii) The firm can maintain and update its records relating to independence; and
 - (iii) The firm can take appropriate action regarding identified threats to independence that are not at an acceptable level.
23. The firm shall establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements, and to enable it to take appropriate actions to resolve such situations. The policies and procedures shall include requirements for: (Ref: Para. A10)
- (a) Personnel to promptly notify the firm of independence breaches of which they become aware;
 - (b) The firm to promptly communicate identified breaches of these policies and procedures to:
 - (i) The engagement partner who, with the firm, needs to address the breach; and

- (ii) Other relevant personnel in the firm and, where appropriate, the network, and those subject to the independence requirements who need to take appropriate action; and
 - (c) Prompt communication to the firm, if necessary, by the engagement partner and the other individuals referred to in subparagraph 23(b)(ii) of the actions taken to resolve the matter, so that the firm can determine whether it should take further action.
- 24. At least annually, the firm shall obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel required to be independent by relevant ethical requirements. (Ref: Para. A10–A11)
- 25. The firm shall establish policies and procedures: (Ref: Para. A10)
 - (a) Setting out criteria for determining the need for safeguards to reduce the familiarity threat to an acceptable level when using the same senior personnel on an assurance engagement over a long period of time; and
 - (b) Requiring, for audits of financial statements of listed entities, the rotation of the engagement partner and the individuals responsible for engagement quality control review, and, where applicable, others subject to rotation requirements, after a specified period in compliance with relevant ethical requirements. (Ref: Para. A12–A17)

EXTRACTS FROM ISA 220

Requirements

Leadership Responsibilities for Quality on Audits

- 8. The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. (Ref: Para. A3)

Relevant Ethical Requirements

- 9. Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. (Ref: Para. A4–A5)
- 10. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)

Independence

- 11. The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: (Ref: Para. A5)
 - (a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence;

- (b) Evaluate information on identified breaches, if any, of the firm's independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and
- (c) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action. (Ref: Para. A6–A7)