

**Meeting:** IESBA CAG

**Meeting Location:** Paris, France

**Meeting Date:** March 7, 2016

## Agenda Item D-1

### Report Back – Structure of the Code Phase 1

#### Objectives of Agenda Item

1. To note the report-back on the September 2015 CAG discussion.
2. To encourage CAG member organizations to respond to the Exposure Draft, [\*Improving the Structure of the Code of Ethics for Professional Accountants – Phase 1\*](#) (ED-1).

#### Project Status and Timeline

3. Appendix 1 to this paper provides a history of previous discussions with the CAG on this topic, including links to relevant CAG documentation.
4. ED-1 was approved at the November/December 2015 IESBA meeting and issued in the latter part of December 2015. The IESBA views this project as strategically important, and therefore a high priority. ED-1 sets out the first concrete application of the proposed new Structure format, which the IESBA hopes will lead to greater usability and understandability of the Code, and hence more consistent application and improved enforcement.
5. The timing of the sections of the extant Code that have been exposed in ED-1 takes into account the expected approval dates for various sections of the Code which are currently under revision or development. The IESBA is mindful of the need for appropriate alignment of the timing of the work on the Structure of the Code project with the timing of other projects currently in progress. In conjunction with the release of ED-1, the IESBA released [\*IESBA Update: Restructuring the Code of Ethics for Professional Accountants\*](#) to explain how it plans to coordinate the restructuring work with the various other work streams. This publication, which is provided for information as **Agenda Item D-1.1**, includes a forward timetable for Phases 1 and 2 of the Structure of the Code project as well as for other ongoing projects.
6. ED-1 is open for comment through **April 18, 2016**. **CAG Member Organizations are strongly encouraged to respond to ED-1 and to submit their comments to the IESBA by the comment deadline.** Feedback from the formal responses to ED-1 will be considered by the Structure Task Force and the IESBA in Q2 2016. A summary of the responses to ED-1 will be presented to the CAG at its September 2016 meeting.
7. ED-1 includes an Explanatory Memorandum with questions for respondents and a summary of the IESBA's deliberations in developing the proposed restructured Code. This Explanatory Memorandum is included as pages 4-12 of ED-1 and forms part of the CAG reference materials. The ED has also been circulated to the Representatives in PDF format as well as via hyperlink.

## September 2015 CAG Discussion

8. Below are extracts from the draft minutes of the September 2015 CAG meeting,<sup>1</sup> and an indication of how the Task Force or IESBA has responded to CAG Representatives' comments.

Matters Raised	Task Force/IESBA Response
GENERAL COMMENTS	
Mr. Hansen wondered whether the project was a clarification project.	Mr. Thomson responded that the IESBA had undertaken a clarity project previously. He noted that the current project was more than just relocating paragraphs. He explained that part of the Task Force's mandate is to enhance the understandability of the Code. He acknowledged, however, that there is a risk of unintended changes in meaning of the Code in doing so. To mitigate this risk, the TF has taken steps such as developing mapping tables.
Referring to the matter of code vs. standards, Mr. Ahmed commented that from a prudential perspective the concern is not to spend too much time debating this matter. Rather, when discussing core principles in the prudential sector, there is a need to consider the assessment methodology. In relation to the matter of whether to use the terms "purpose," "objective" or "goal," he was of the view that there should not be a debate about which concept is at a higher level. Instead, there needs to be consideration of what the objective and application guidance should be.	Mr. Thomson responded that the Task Force had discussed the matter and had endeavored to draw out the best of both worlds, i.e., by focusing on compliance with the fundamental principles.
Noting that not everyone will navigate the Code in the same manner, Ms. Molyneux felt that the issue is whether to retain the focus on fundamental principles vs. requirements. She was of the view that stakeholders should be made aware that there are requirements that support compliance with the fundamental principles. In this regard, she noted that the OECD had taken an approach of keeping each principle with the requirements. Mr. Koltvedgaard observed that an e-Code could assist in this respect.	Mr. Thomson indicated that the Task Force had already started exploring ideas along those lines, for example, links that could take a user of the Code from the requirements back to the fundamental principles. He added that the Task Force had also been working on a guide to the Code. He highlighted that the Task Force's key concern is to build an appropriate linkage between the fundamental principles and the detailed requirements.

<sup>1</sup> The draft September 2015 CAG minutes will be approved at March 2016 IESBA CAG meeting.

Matters Raised	Task Force/IESBA Response
<p>Mr. Dalkin shared his experience on INTOSAI. He noted that while application material with respect to the International Standards on Auditing (ISAs) has a specific meaning, views within the INTOSAI working group charged with revising INTOSAI's Code of Ethics have been divided on the matter of whether application material is optional. He wondered whether the IESBA had encountered a similar challenge. Ms. Elliott noted that the IIA had faced such a challenge in terms of determining what is mandatory and what is optional. She felt that this is a real issue as there are varying interpretations around the world. Ms. Miller noted that one of the reasons for the challenge at the IIA is that professional standards used to be referred to as "strong recommendations." However, the IIA had now moved away from the concept of a strong recommendation as it was too close to a requirement. So, there is now simply reference to mandatory provisions and guidance.</p>	<p>Mr. Thomson noted that the Board was aware of the issue. He added that application material is more than optional as a professional accountant must comply with the requirement and should consider the application material in doing so. He indicated that there is a need to clearly communicate what appropriate weight to attribute to application material.</p> <p><u>Update from December 2015 Exposure Draft</u></p> <p>Paragraph 8 of the proposed Guide to the Code states the following: "In addition to requirements, the Code contains application material that provides context relevant to a proper understanding of the Code. In particular, the application material is intended to help the professional accountant to understand how to apply the conceptual framework to a particular set of circumstances or a specific requirement. While such application material does not of itself impose a requirement, consideration of the material is necessary to the proper application of the requirements of the Code, including application of the conceptual framework. The entire text of Part A and the relevant Section is required to understand and properly apply that Section. ..."</p>
<p>Referring to Mr. Hansen's earlier question about the project's objective, Mr. James noted the need to be clear about such objective. He felt that there was an opportunity for the Board to address areas of ambiguity in the Code and to make the Code stronger. He further inquired as to whether there were set criteria to determine if the Task Force will address an issue or if the Board will address it in the future.</p>	<p>Mr. Thomson responded that the Task Force was endeavoring to add clarity to the Code where possible while at the same time building a list of matters for further Board attention. He noted that the Task Force needed to be careful in not tackling every issue that might exist. However, with respect to safeguards, as these are integral to the Code the Board had agreed to undertake a review of safeguards now.</p> <p>Dr. Thomadakis cautioned that there would be a risk that the Structure project would never end if the Task Force were to attempt to address every matter. He also highlighted that the project is not only about repackaging the Code but also about making it easier to use. Mr. Siong reminded Representatives that an overriding principle for the project is not to introduce substantive changes to the Code.</p>

Matters Raised	Task Force/IESBA Response
Mr. Ahmed agreed, noting that to benefit from the project truly, its scope must be properly ring-fenced.	Support noted.
Referring to Mr. Siong's comment about no substantive changes to the Code, Ms. Lang wondered whether the Board knows how the Code is being used in practice to make such a judgment.	Mr. Thomson noted that the Board reads the application material as it is written.
Ms. Lang commented that there should then be a need to know the impact of the proposed changes.	Mr. Thomson responded that the Board has undertaken more research consultation and outreach on this project than on other projects. The common theme from all this work has consistently been support from stakeholders for the proposed approach to restructuring the Code. Accordingly, the Board was comfortable with the project's approach. He noted that stakeholders would have the opportunity to comment on any perceived changes in meaning when the ED is issued.
Mr. Hansen commented that the unique benefit of the project is in clarifying the requirements, noting that these should be unequivocal.	Point taken into account.
Mr. Van der Ende noted that he saw a parallel with the Basel Committee on Banking Supervision in terms of how to deal with emerging issues. He noted that if these are issues that have a broader impact around the world, the Public Interest Activity Committees (PIACs) operating under the auspices of IFAC could explore whether these should be addressed and who should be involved in doing so. The CAGs should then be asked for their input on how best to deal with these issues.	Dr. Thomadakis expressed appreciation for this comment, noting that this is a broader strategic issue for the PIACs. In relation to the IESBA, he noted that the Board had already established an Emerging Issues and Outreach Committee (EIOC) charged with identifying emerging issues. He noted that the CAG itself can assist in this regard.
Ms. Singh suggested that the Board maintain a running list of issues for future consideration.	Mr. Thomson indicated that the Task Force had already been tracking such matters.
NAVIGABILITY	
Mr. Thomson noted that the proposed revised Preface is consistent with the extant Code and	–

Matters Raised	Task Force/IESBA Response
<p>may or may not be adopted by local jurisdictions. He indicated that the Task Force had added a Guide to the Code which was targeted at infrequent users in order to describe the purpose of the Code, how it is structured, and how to use it. He noted that the Guide to the Code also contains an appendix on dealing with ethical dilemmas, <sup>2</sup> including guidance addressing circumstances where application of the Code would result in a disproportionate outcome. He explained that the guidance on ethical dilemmas was currently located in Part A of the Code. However, the Task Force felt that it would be better located as an appendix to the Guide to avoid any user viewing the guidance as reason for not complying with the Code.</p> <p>Representatives had no comments.</p>	
<p>REQUIREMENTS AND APPLICATION MATERIAL</p>	
<p>Mr. Thomson noted that the Task Force was proposing to change the heading “Guidance” back to “Application Material.” He explained that The Task Force felt that the term “guidance” could be interpreted by users to mean that the material to which it refers is optional whereas the term “application material” conveyed more the sense that the material is integral to applying the requirements. Accordingly, explanatory material had been added to the Guide to the Code to indicate that while application material does not impose any additional obligations, it must be considered in applying the requirements.</p> <p>Representatives had no comments.</p>	<p>–</p>
<p>CROSS-REFERENCES</p>	
<p>Mr. Thomson noted that cross-references to the conceptual framework are heavily used in the DRC. Therefore, some sections of the Code have</p>	<p>–</p>

<sup>2</sup> The guidance on ethical dilemmas was subsequently relocated to the body of the Guide in the December 2015 [Exposure Draft](#).

Matters Raised	Task Force/IESBA Response
<p>been organized as subsections to reduce the extent of such cross-referencing. He also indicated that the section on objectivity mentions independence and that the Task Force was proposing to add a specific reference to objectivity at the beginning of the sections addressing independence.</p> <p>The following matters were raised:</p>	
<p>Ms. Miller wondered how independence links to objectivity, noting that she saw independence more from an application perspective, such as not holding financial interests in an audit client.</p>	<p>Mr. Thomson noted that independence represents a way for stakeholders to assess a particular situation and draw comfort as to whether the professional accountant is objective.</p>
<p>Mr. Koltvedgaard inquired to whom the Code was addressed.</p>	<p>Mr. Thomson indicated that the Code is intended for stakeholders to whom it is relevant, including national standards setters, professional accountants and firms as well as regulators and others.</p>
<p>Mr. James noted that IOSCO members have been concerned about a number of instances where a firm complied with the requirements but did not go the extra step of standing back and considering the broader fundamental principles. He wondered whether this point was coming across sufficiently strongly in the proposals.</p>	<p>Mr. Thomson responded that the Task Force was addressing this matter structurally with, among other changes, cross references to the conceptual framework. Also, the Safeguards Task Force was exploring the merits of introducing a new requirement for professional accountants to step back by performing an overall assessment to determine whether, after application of appropriate safeguards, the threats to compliance with the fundamental principles are eliminated or reduced to an acceptable level.</p>
<p>Ms. Molyneux wondered whether regulators had identified specific areas of difficulty with respect to enforceability of the Code. She felt that a code is not as strong as standards with respect to compliance and enforcement.</p>	<p>Mr. Thomson indicated that the Board had indeed heard from regulators in relation to the clarity of the requirements, compliance with the fundamental principles, and the clarity, appropriateness and effectiveness of safeguards. The Task Force had therefore endeavored to create appropriate linkages with the fundamental principles, including introducing a more structured approach in terms of a broad requirement to comply with the fundamental principles and apply the conceptual framework. He noted that rules that are too “black and white” have their own problems. He indicated that the Task Force</p>

Matters Raised	Task Force/IESBA Response
	believed that its combined approach of the overarching requirement to comply with the fundamental principles, supported by detailed requirements, was a robust approach.
Mr. Hansen noted that the Code contains a number of prohibitions. To mitigate the risk that professional accountants rationalize not complying with them, he suggested that it should be made clear that such prohibitions are not subject to the conceptual framework.	Mr. Thomson noted that the Task Force was endeavoring to address such a concern through the use of unequivocal wording, including the use of the word “shall” to mean a requirement.
SPECIFIC REFERENCES TO NETWORK FIRMS	
Mr. Thomson noted that the extant Code uses the term “firm” to mean both a firm and a network firm. He indicated that this has resulted in some areas within the Code, particularly in relation to the assessment of materiality and significance, that are not as clear as they could be. Accordingly, the Task Force was proposing to make clear in the DRC when network firms are specifically intended to be covered.  Representatives had no comments.	–
RELOCATION OF CERTAIN MATERIAL TO SUBSECTIONS	
Mr. Thomson noted that some material within the extant Code would be relocated to assist navigability. In particular, the Task Force was proposing a subsection dealing with documentation, including material of general application and cross references to discussion of documentation for particular matters. He indicated that it is outside the scope of the project to address what should or should not be documented. However, the Task Force can propose wording clarifications where warranted.  Representatives had no comments.	–

Matters Raised	Task Force/IESBA Response
LABELLING AND TERMINOLOGY	
<p>Mr. Thomson noted that there had been a question at the IESBA as to whether the various parts of the Code should be labelled A, B and C as in the extant Code or given numeric references. He indicated that the Task Force was proposing to retain the alpha references to avoid confusion with parts that contain section numbers that would begin with a number different from a numbered Part. The Task Force had also clarified the scope of the term PAIB by including particulars in the Guide to the Code. In addition, the Task Force was proposing that the term “may” be used when a professional accountant is permitted to take an action, and the term “might” when describing situations that could occur.</p> <p>Representatives had no comments.</p>	<p>–</p>
MATTERS FOR BOARD ATTENTION	
<p>Mr. Thomson explained that the Task Force had created a list of matters for Board attention. These represent potential issues outside of the scope of the project that may need to be addressed in future. He then outlined the items on the list.</p> <p>Representatives had no comments.</p>	<p>–</p>

### Matters for Consideration

9. Representatives are asked to note the report back.

### Material Presented

Agenda Item D-1.1 December 2015 IESBA Update, *Restructuring the Code of Ethics For Professional Accountants*

### Material Presented –FOR IESBA CAG REFERENCE PURPOSES ONLY

Structure Exposure Draft Phase 1: *Improving the Structure of the Code of Ethics for Professional Accountants—Phase 1* <http://www.ifac.org/publications-resources/exposure-draft-improving-structure-code-ethics-professional-accountants-phase>



## Appendix

### Project History

#### Project: Structure of the Code

##### Summary

	CAG Meeting	IESBA Meeting
Project commencement	March 2014 September 2014	March 2014 June 2014 September 2014 December 2014
Development of proposed international pronouncement for Phase I (up to exposure)	March 2015 September 2015	April 2015 June/July 2015 September 2015 November/December 2015
Phase I Exposure	December 2015 – April 18, 2016	

##### CAG Discussions: Detailed References

<b>Project Commencement</b>	<p><u>March 2014</u></p> <p>See IESBA CAG meeting material <a href="#">here</a> (see Agenda Items F and F-1, F-2, F-3, F-4 and F-5) and final CAG <a href="#">meeting minutes</a> (see section F).</p> <p><u>September 2014</u></p> <p>See IESBA CAG meeting material <a href="#">here</a> (see Agenda Items F and F-1) and final CAG <a href="#">meeting minutes</a> (see section F).</p>
<b>Development of proposed international pronouncement (up to exposure)</b>	<p><u>March 2015</u></p> <p>See IESBA CAG meeting material here (see Agenda Items C and C-1) and final CAG <a href="#">meeting minutes</a> (see C section).</p> <p><u>September 2015</u></p> <p>See IESBA CAG meeting material <a href="#">here</a> (see Agenda Items D and D-1) and CAG meeting minutes at Agenda Item A (see Section D).</p>