

**Meeting:** IESBA CAG Meeting

**Meeting Location:** New York

**Meeting Date:** September 10, 2018

## Agenda Item

# C

### Non-assurance Services<sup>1</sup>

#### Objectives

1. To report back on the discussions about the IESBA's non-assurance services (NAS) initiative at the March 2018 CAG meeting.
2. To obtain Representatives' views on:
  - (a) Key issues raised by participants at the IESBA's global roundtables and the Working Group's (WG) assessments and proposals; and
  - (b) The NAS project proposal involving a review the NAS provisions in the [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) ("the revised and restructured Code" or "the Code").

#### Project Status and Timeline

3. In response to concerns from regulatory stakeholders and the Public Interest Oversight Board (PIOB), the IESBA included the NAS topic as a pre-commitment in the its proposed Strategy and Work Plan, 2019-2023, [Elevating Ethics in a Dynamic and Uncertain World](#).
4. Since the finalization of the revised and restructured Code, the IESBA has:
  - Established the NAS Working Group (WG) in December 2017 to respond to concerns about the independence provisions in the Code that apply when firms or network firms provide NAS to their audit clients, in particular with respect to permissibility.
  - Hosted three [global Non-assurance and Professional Skepticism Roundtables](#) in Washington DC, USA (June 11, 2018); Paris, France (June 15, 2018); and Tokyo, Japan (July 12, 2018) to obtain views about a way forward with respect to NAS. In response to calls for an additional event in Australia, the IESBA welcomed the support of the Australian Accounting Professional & Ethical Standards Board (APESB) and the New Zealand External Reporting Board (XRB) to host an additional roundtable in Melbourne, Australia on July 16, 2018.
  - Agreed to the release of a Briefing Note, [Non-assurance Services – Exploring Issues to Determine a Way Forward](#) to summarize the NAS issues that were identified in finalizing the revised and restructured Code in May 2018. The Briefing Note also includes the questions that

<sup>1</sup> NAS in this paper refers to the term "non-assurance services" as used in the Code. In some jurisdictions the term "non-audit" services is used in referring to matters similar to those being considered under this initiative. For example, the term "non-audit services" is used in the UK to cover any service that does not form part of the audit engagement (i.e., both "non-assurance" and "assurance services" other than an audit). The terms "non-audit services" and "non-assurance services" are not defined terms in the Code.

were discussed during the roundtables. An earlier draft of the Briefing Note was discussed with the CAG in March 2018 and the feedback from that discussion is incorporated in the final document.

5. Section III of **Agenda Item C-1** includes a summary of the feedback from the roundtables. Those roundtable discussions were lively and participants represented a wide range of stakeholder groups, including investors; public sector representatives; preparers; audit committee members/ those charged with governance (TCWG); national standard setters; firms and professional accountancy organizations.
6. The IESBA received a preliminary report-back on the Washington DC and Paris [roundtables](#) at its June meeting and was briefed on discussions with the IESBA-National Standard Setters (NSS) liaison group and the Forum of Firms.
7. The IESBA will consider at its September 2018 meeting, a full analysis of the feedback from the roundtables as well as the WG's assessments and recommendations, including a project proposal for NAS (see **Agenda Items C-1** and **C-2**).

#### Coordination with IAASB and Others

8. The WG notes that certain issues may require input from other IESBA Working Groups and the International Auditing and Assurance Standards Board (IAASB). For example, as further discussed in **Agenda Item C-1**, the WG considered issues referred to it by the Fees Working Group; and recommends that the NAS project include among other matters, a consideration of provisions that would require firms to re-evaluate threats to independence when the ratio of NAS fees to audit fees reach a particular threshold.
9. The WG is of the view that a NAS project should not deal with issues and questions that have been raised about whether the IESBA has a role to play in responding to broader concerns about audit quality and auditor independence that might arise from the multi-disciplinary consulting and advisory services provided by firms and network firms (i.e., firms' business model). Those matters have been referred to the IESBA Planning Committee for further consideration.

#### Report Back on March 2018 CAG Discussions

10. Below are extracts from the draft minutes of the March 2018 CAG meeting<sup>2</sup> and an indication of how the WG/IESBA has responded to CAG Representatives' comments.

Matters Raised	WG/ IESBA Response
MATERIALITY AND SIGNIFICANCE	
Mr. Baumann complimented the Board, noting that the initiative was timely and appropriate. Referring to materiality, he noted that the term is used in different ways in the Code and that his preference would be for it to be used in the same context as in the auditing standards (i.e., when	Point accepted.  During the meeting, Mr. Fleck acknowledged the comment, noting that there are broader issues relating to materiality, beyond NAS, that the Board

<sup>2</sup> The March 2018 CAG minutes will be approved during the September 2018 IESBA CAG meeting.

<p>referring to financial statements). He suggested that to avoid confusion, the term materiality should be not be used when referring to parts of a system or process, and that another term, for example, “significance” should instead be used. Mr. Hansen echoed Mr. Baumann’s remarks and agreed with his suggestion.</p>	<p>is planning to explore as part of a separate initiative on the topic of materiality.</p> <p>The project proposal in <b>Agenda Item C-2</b> covers materiality (see paragraphs 14-15). For a discussion of the feedback from roundtable participants on the topic and the WG’s assessments and recommendations, please see <b>Agenda Item C-1</b>, Section III, C and Section V, A.</p>
<p>Mr. Dalkin explained that to ensure consistent and appropriate application, the US Government Accountability Office (GAO) deemed it necessary to include an explicit presumption to emphasize that preparing financial statements is a significant NAS. He suggested that in some instances, a hybrid approach that involves both principles-based provisions and explicit prohibitions might be necessary to drive desired behaviors among auditors.</p>	<p>Point accepted.</p> <p>During the meeting, Mr. Fleck acknowledged the suggestion, and noted that in some circumstances (e.g., NAS and NOCLAR) the Code already follows such an approach. In the case of NAS, he explained that Working Group will need to consider the extent to which additional prohibitions might be required for clarity and additional specificity, for both public interest entities (PIEs) and non-PIEs.</p> <p>Appendix 2 to <b>Agenda Item C-1</b> highlights that the prohibitions relating to NAS are set out in Section 600.<sup>3</sup> With respect to providing accounting and bookkeeping services, including preparing financial statements, the Code includes two sets of prohibitions – one for audit clients that are PIEs, and another for those that are non-PIEs.<sup>4</sup> The Code also includes an exception to the PIE prohibition for accounting and bookkeeping services of <b>a routine or mechanical nature that are provided to divisions or related entities if the personnel providing the services are not audit team members</b> when specific conditions apply (see paragraph R601.7). Some roundtable participants believe that this exception</p>

<sup>3</sup> International Independence Standards, Part 4A – Independence for Audits and Review Engagements, Section 600, *Provision of Non-assurance Services to an Audit Client*

<sup>4</sup> For audit clients that are PIEs, paragraph R601.6 of the Code states that a firm or a network firm shall not provide to an audit client that is a PIE accounting and bookkeeping services **including preparing financial statements** on which the firm will express an opinion or financial information which forms the basis of such financial statements.

For audit clients that are not PIEs, paragraph R601.5 of the Code states that a firm or a network firm shall not provide to an audit client that is not a PIE accounting and bookkeeping services including **preparing financial statements** on which the firm will express an opinion or financial information which forms the basis of such financial statements, unless:

- (a) The services are of a routine or mechanical nature; and
- (b) The firm addresses any threats that are created by providing such services that are not at an acceptable level.

	weakens the Code and suggested that it be withdrawn (See Section III, B of <b>Agenda Item C-1</b> ). This matter will be considered as part of the NAS project.
PIE OR NON-PIE PROVISIONS	
Mr. Hansen and Ms. McGeachy-Colby questioned the need to revisit having different provisions in the Code for PIEs and non-PIEs. He noted that at a conceptual level it makes sense that the provisions should be the same, but that there are practical reasons why there should be more stringent provisions for PIEs as many small entities do not have the resources to prepare financial statements. However, he acknowledged that it is an issue when large private entities use their auditors for such NAS.	<p>Point accepted.</p> <p>During the meeting, Mr. Fleck responded that the philosophical question of the distinction between PIEs and non-PIEs has been raised at the IESBA. The SMP community would be very concerned if the distinction were eliminated. He agreed that there are some very large private entities, and that conceptually, there is consideration of owner-managed entities (OMEs) vs. non-OMEs. However, he noted that the concept of the OME is not globally recognized but that there would be a need to further reflect on it.</p> <p>The project proposal in <b>Agenda Item C-1</b> notes that the project will consider whether different approaches should be taken if the particular NAS is to be provided to different categories of entities (i.e., PIE versus non-PIE), taking into consideration specific suggestions made by roundtable participants (see paragraph 16). For a discussion of the feedback from roundtable participants about PIE versus non-PIE and the WG's assessments and recommendations, please see <b>Agenda Item C-1</b>, Section III, D and Section V, A.</p>
PRE-APPROVAL OF NAS BY TCWG	
Mr. Iluma noted that in many jurisdictions the role of TCWG is defined in the law or regulation of the specific jurisdiction. He questioned whether the IESBA's mandate extends to establishing requirements for TCWG; and whether any established requirements that might be added to the Code would be enforceable. He advised careful reflection about this matter.	<p>Point accepted.</p> <p>The project proposal in <b>Agenda Item C-1</b> notes that the consideration of whether to include pre-approval provisions in the Code will take into account the fact that the IESBA's remit cannot be extended to imposing obligations on TCWG (see paragraph 18).</p>
BENCHMARKING	

In relation to the Working Group's plans for comparing NAS provisions across G-20 jurisdictions, Mr. James questioned the Board's objective. He wondered whether it would be aspirational in nature, i.e., to understand and assess what is possible versus what is commonly achievable across jurisdictions. He added that the IESBA should consider whether there are actions that it might take to be clear and transparent about its planned approach in order to assuage concerns and lingering perceptions about the Code being a "lowest common denominator" (LCD). Ms. Elliott noted that while the OECD did not have any preconceived notions, there are risks to undertaking a benchmarking exercise in terms of going down to a LCD. She cautioned the IESBA against focusing solely on seeking alignment and also suggested that the Board consider reviewing OECD versus G-20 jurisdictions.

Mr. Fleck affirmed that it is not the IESBA's intent for the Code to go to a LCD. He emphasized that it is important to be clear that the IESBA is aiming for a globally operable Code at a higher level. He explained that as part of its fact finding, the Working Group is keen on understanding the extent to which the NAS provisions across the G-20 jurisdictions could be aligned or harmonized. He noted that the Working Group's preliminary work suggests that some of the different NAS provisions exist because of varying degrees of granularity in the provisions and variations in the definitions or descriptions of certain services. He added that from an aspirational point of view, where it is possible to align, the Board would do so. Hence, the Board would not necessarily take the easy option but there should be alignment where it makes sense to do so. In this regard, he noted that it would be important to hear stakeholders' views at the roundtables as to what would be in the public interest. He added that there is some pressure to reduce complexity.

Dr. Thomadakis added that four years ago, the IESBA learned about concerns about having an LCD Code and, in response, undertook to completely revise and restructure the Code to address many of the more substantive concerns. For example, he pointed to the NOCLAR standard as being the only one of its kind. Mr. Siong referred to several additional examples. Dr. Thomadakis then explained that in his view the Code is a principles-based Code that also includes specific guidance for dealing with certain issues. He also highlighted the strategic axis of raising bar globally in the proposed IESBA strategy and work plan 2019-2023. He then invited the CAG to point out specific areas in the Code that they believed contribute to perceptions of the Code being a LCD.

**Agenda Item C-1** includes a discussion of the benchmarking that the WG has performed to-date and its preliminary observations (see Section VI, B).

<p>Mr. Koktvedgaard commented that if there is a perception about LCD, the Board should address why it still exists. He explained that in his view, he saw value in the Board anchoring its decisions based on facts about the NAS provisions that are effective across jurisdictions (i.e., information about G-20 NAS provisions).</p>	<p>Point accepted.</p> <p>Mr. Fleck responded that the Board intends the Code to command respect, and that there is a need to reinforce the message that the IESBA is raising the bar.</p>
<p style="text-align: center;">OTHER MATTERS, INCLUDING BUSINESS MODEL</p>	
<p>Ms. Pettersson noted that the PIOB believes that the NAS initiative is very important and that the issues are sensitive. She was of the view that a possible way forward might involve a combination of different approaches – for example, having clearer and more explicit prohibitions, and having requirements for pre-approval by TCWG and for increased disclosures about NAS. She indicated that she looked forward to the project.</p>	<p>Point accepted.</p> <p>The project proposal in <b>Agenda Item C-2</b> involves a combination of different approaches.</p>
<p>Mr. Hansen noted that in the US, the Securities and Exchange Commission has emphasized that issuers have some responsibilities as well, and that they tend to be at fault in practice. Accordingly, he suggested that consideration be given to emphasizing management's responsibilities when a firm provides a NAS to an audit client.</p>	<p>Point accepted.</p> <p>During the meeting, Mr. Fleck acknowledged that joint responsibility is important. He added that in the UK, this is well understood among the FTSE 100. Beyond that group, appreciation of this notion tends to decrease.</p> <p>The NAS provisions in the Code:</p> <ul style="list-style-type: none"> <li>• Emphasizes that management is responsible for the preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework (paragraph 601.3 A2).</li> <li>• Prohibits firms and network firms from assuming a management responsibility for an audit client and includes clear guidance as to what constitutes a management responsibility (paragraphs R600.7 to 600.7 A3).</li> </ul>
<p>Mr. Hansen noted that this initiative was being approached on an engagement basis. He questioned whether the Working Group would be exploring broader issues about audit quality and auditor independence that might arise from the</p>	<p>Point noted.</p> <p>Mr. Fleck acknowledged the question, noting that it might lead to a consideration of whether the IESBA should develop a standard similar to the</p>

multi-disciplinary consulting and advisory services provided by firms and network firms (i.e., firms' business model). In particular, he wondered whether the way a firm positions itself and its overall tone or culture changes based on its business model.	<p>IAASB's ISQC 1<sup>5</sup> but for ethics. However, he explained that the NAS initiative is not intended to deal with issues or concerns relating to firms' provision of NAS to non-audit clients.</p> <p>The issues relating to business model extend beyond the remit of the NAS initiative and have been referred to the IESBA Planning Committee for further consideration (see <b>Agenda Item C-1</b> Section III, J and Section V, B).</p>
Mr. James noted that as part of the IAASB's Quality Control project (i.e., proposed revisions to ISQC 1), it is exploring "tone-at-the-top" and culture issues at the firm level. He questioned whether the IESBA should also be exploring these issues in the context of the Code.	<p>Point noted.</p> <p>Ms. Zietsman provided a high-level overview of the IAASB's Quality Control project, in particular the proposed revisions that are being considered for ISQC 1. She indicated that those proposed revisions will address, among other matters, issues relating to tone, culture and compensation and remuneration matters within the firm. The thrust of the proposed revisions goes to the choices that firms make but the overriding concern is audit quality.</p>
Ms. McGeachy-Colby questioned the need for considering revisions to the NAS section of the Code now, given the recent approval of the revised and restructured Code.	<p>Point taken into account.</p> <p>Mr. Fleck explained that there is a public interest need to address the incremental NAS issues relating to permissibility and that the WG did not anticipate having to revisit any of the restructuring or safeguard-related changes that have been made to the NAS provisions in the Code.</p>

## Matters for CAG Consideration

11. At its September 2018 meeting, the CAG will receive a presentation summarizing the feedback from the roundtables, the WG's assessments and recommendations, in particular, the rationale for the project proposal in **Agenda Item C-2**.
12. Representatives will be asked to:
  - (a) Note the report back in paragraph 10.
  - (b) Consider the matters for CAG consideration in **Agenda Item C-1** taking into account the feedback from the four global roundtables.

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<sup>5</sup> 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*

- (c) Provide input on the NAS project proposal in **Agenda Item C-2** in advance of its consideration by the IESBA for approval.

### **Material Presented**

Agenda Item C-1	NAS Issues Paper, Summary of Significant Matters Raised in Global Roundtables, Working Group Assessments and Proposals
Agenda Item C-2	NAS Project Proposal

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

[Ref. Material to Agenda Item C Non-assurance Services Roundtable Briefing Note](#)