

Revision of Part C¹ – Applicability and Issues and Task Force Proposals Pertaining to Restructuring

How the Project Serves the Public Interest

A significant proportion of the world's professional accountants are professional accountants in business (PAIBs), accountants who do not work in public accounting practices. PAIBs are a very diverse constituency and work as employees or consultants in commerce, industry, financial services, education, and the public and not-for-profit sectors. Many are in a position of strategic or functional leadership, or are otherwise well-placed to collaborate with colleagues in other disciplines to help their organizations toward long-term sustainable success.

All organizations require relevant and reliable information in order to conduct their affairs. In addition, other stakeholders (such as investors, suppliers, customers, creditors and government agencies) require relevant and reliable information to assess an organization's financial situation and to oversee accountability. Such information enables the stakeholder to make reliable and informed decisions regarding the organization.

A PAIB may be offered an inducement with the intention of influencing the behavior of the PAIB or obtaining an advantage from the PAIB that would not have been attained without the inducement. Such actions might violate the legitimate objectives of the PAIB's employing organization and could result in the PAIB failing to comply with the fundamental principles of the Code.

In addition, while the focus of Part C of the Code is on PAIBs, the guidance within Part C might be applicable to professional accountants in public practice (PAPPs) in certain circumstances, notably as relates to intra-firm relationships and relationships with external parties that are not clients.

It is not in the public interest for a PAIB to offer, solicit or accept inducements that could result in non-compliance with the fundamental principles of the Code. Conversely, it is in the public interest to provide guidance to clarify that Part C might be applicable to PAPPs in certain situations.

Introduction

1. This paper:
 - (a) Addresses matters pertaining to the applicability of the requirements and application material in extant Part C (restructured Part 2) to PAPPs; and
 - (b) Discusses issues and Task Force's proposals regarding the restructuring of extant Part C Phase 1.

Issues and Task Force Proposals

Applicability of the Provisions in Extant Part C to PAPPs

Revisions to Explanatory Paragraph

2. At its March 2016 meeting, the Board agreed with the Task Force's conclusion that it is possible for PAPPs to find themselves in ethically problematic circumstances and situations that do not involve

¹ Extant Part C, *Professional Accountants in Business* (restructured Part 2– *Professional Accountants in Business*)

clients, such as intra-firm conflicts or situations involving external parties that are not clients, and hence face some of the same issues and ethical dilemmas as PAIBs. At its June 2016 meeting, the IESBA considered and generally agreed to the Task Force's proposal to include an "explanatory paragraph" in the Code to explain the applicability of the requirements and application material set out in extant Part C (restructured Part 2) to PAPPs. The IESBA also asked that some refinements be made to address the matters below.

Accountants' Relationship with the Employing Organization

3. Some members felt that the phrase "pursuant to the accountant's employment or ownership relationship with the employing organization, for example a firm" needed to be reconsidered to better define the PAPPs relationship with his or her employing organization. A member also noted that if the PAPP is a partner of a firm, and hence not an employee, he or she cannot be in a relationship with an employing organization.
4. The Task Force is of the view that no amendments are needed to the phrase, as it is sufficiently broad to cover both intra-firm dilemmas, such as a senior partner placing undue pressure on a PAPP, and ethical dilemmas relating to external third parties that are not clients, such as vendors. The Task Force also believes that, as relates to PAPPs, the employing organization is the firm, and therefore, the term "employing organization" can be replaced with "firm". The Task Force is of the view that irrespective of whether PAPPs are partners (i.e. owners) or employees of an organization, they should have to consider the relevance of all the requirements and application material the Code, including those set out in extant Part C. Accordingly, the Task Force proposes to also retain the words "ownership relationship."

Signposting / Examples

5. There was a suggestion that a summary of the ethical issues on which a PAPP might consider referring to guidance in extant Part C could be provided. It was also suggested that the "explanatory paragraph" indicate the manner in which ethical duties are discharged in situations where the PAPP is not providing services to clients as this will dictate whether extant Part C might be relevant.
6. The Task Force continues to be of the view that signposting to specific sections in extant Part C is not needed because all the requirements and application material in extant Part C should be considered by a PAPP. The Task Force believes that signposting might result in a PAPP inadvertently overlooking a requirement or application material that might be relevant.
7. However, the Task Force believes that the objective of the paragraph would be enhanced by adding an example to the proposed wording. Rather than referring to different sections in Part C of the extant Code (restructured Part 2), the Task Force suggests adding an example that explains a situation where the PAPP might face an ethical dilemma that is not client-related. The revised text below includes the Task Force's proposed example. This example was developed based on the input provided by IESBA members during the IESBA March 2016 meeting.²

² Examples from IESBA March 2016 meeting Agenda Paper 7-D:

- PAPPs may be inappropriately pressured by superiors to compromise audit quality by working within unrealistic time budgets.
- A division of a firm is pressured by another division of the firm to retain an untrustworthy client, solely to protect the larger fee income of the latter division.

Feedback on Structure ED-1

8. In developing refinements, the Task Force also considered input from some respondents to the December 2015 Exposure Draft, *Improving the Structure of the Code of Ethics for Professional Accountants – Phase 1* (Structure ED-1) relevant to this topic.³ One of those respondents suggested that the IESBA consider repositioning the following sentence that was presented in paragraph 4 of the Guide to the proposed restructured Code to the body of the Code itself to ensure it is not overlooked:

“Professional accountants in public practice might also find [extant] Part C [i.e., restructured Part B] relevant to their particular circumstances.”

Task Force’s Recommendation

9. The Task Force agrees with the respondent’s recommendation and is of the view that it achieves the same objective as the recommendation set out in the June 2016 IESBA agenda materials, namely that the “explanatory paragraph” should be appropriately located within the restructured Code to ensure that it is not overlooked by users. At its June 2016 meeting, the IESBA generally agreed with the Task Force proposed placement of the following explanatory paragraph (marked to show changes since the June 2016 IESBA discussion) below be included in restructured Parts 1 and 3, proposed Sections 120⁴ and 300⁵ respectively (see **Agenda Item 3-H** for proposed placement):

R120.X When facing an ethical issue, a professional accountant in public practice shall consider the context within which the issue has occurred. Where the accountant is performing professional activities pursuant to the accountant’s employment or ownership relationship with the ~~firm employing organization, for example a firm~~, there might be guidance in Part ~~2-C~~ that is applicable to those circumstances. If so, t~~The~~ accountant shall comply with ~~consult~~ relevant provisions and comply with them.

120.X A1 For example, where a professional accountant in public practice is faced with pressure from an engagement partner to perform a task without sufficient skills or training, or with unrealistic deadlines, the requirements and application material guidance is set out in Section 260 might be relevant.

Matters for IESBA Consideration

1. IESBA members are asked for views on the proposed revisions to the “explanatory paragraph”.

- A firm’s internal accounting staff might be pressured to massage the firm’s results so that profit shares for partners are distorted towards one individual or group of partners.

³ The IESBA did not deal with issues related to the applicability of Part C to PAPPs in its Structure ED-1. However, the following proposals are relevant to the issue:

- The sentence in paragraph 100.3 (“Professional accountants in public practice may also find Part C relevant to their particular circumstances”) of the extant Code has been repositioned to the Guide;
- The Explanatory Memorandum to ED-1 noted that the order of Parts B and C of the extant Code would be reversed, with “Part C” retitled to be proposed “Part B”.

As noted at **Agenda Item 3-A**, the Structure Task Force has retitled Part B to Part 2 in response to feedback from respondents to Structure ED-1.

⁴ Proposed Section 120, *The Conceptual Framework*

⁵ Proposed Section 300, *Professional Accountants in Public Practice*

Finalizing the “Explanatory Paragraph”

10. At the June 2016 National Standard Setters (NSS) Liaison Group meeting, it was noted in some jurisdictions, the section of the Code that applies to PAIBs,⁶ has not been adopted within their local Code. Accordingly, only the requirements and application material in Parts A⁷ (restructured Part 1) and B⁸ (restructured 3-4) of the IESBA Code are relevant. During its June 2016 Board meeting, IESBA members acknowledged that the Italian institute incorporated the provisions for PAIBs into their local code, and that the Japanese Institute is in the process of converging and plans to consider the inclusion of provisions for PAIBs in its local Code.
11. The Task Force accepts that the inclusion of the explanatory paragraph in the Code might be an issue for some jurisdictions. However, it believes that its proposal for PAPPs to consider the applicability and relevance of the material set out in **Agenda Item 4-B**, will enhance the Code and make it more robust by setting the same ethical standards on all professional accountants, and thus justify the additional requirements.
12. There is still an open question about whether the text for the “explanatory paragraph” set out in paragraph 9 should be exposed for public comment. The proposed explanatory paragraph essentially means a change of meaning to the extant Code⁹ since it imposes an obligation for all PAPPs to also consider the requirements and application material set out in **Agenda Item 4-B** (i.e., the provisions for PAIBs). Therefore it is the view of the Task Force that the proposed explanatory paragraph should be exposed for public comment.

Matter for IESBA Consideration

2. Do IESBA members believe that there is a need to expose the “explanatory paragraph” that explains the applicability of the provisions set out in **Agenda Item 4-B** to PAPPs?
3. If yes, should this paragraph be exposed as part of Structure ED-2, or as part of the Part C Phase 2 exposure draft, taking into account the different timelines for each exposure drafts?

Issues Pertaining to Restructuring

13. The close-off document for Part C Phase 1 (close-off document) has been written under the format and drafting conventions of the extant Code. Restructured drafts of the close-off document were presented to the Board at its March 2016 and June 2016 meetings. As noted in Agenda Item 3, it is planned that the final restructured text will be included in Structure ED-2.
14. The Task Force has proposed further revisions since June 2016 draft to:
 - Address the comments raised by IESBA members at their June 2016 meeting;
 - Include conforming amendments arising from Safeguards ED-1 (see paragraphs shaded in gray); and
 - Adhere to the updated drafting guidelines set out in **Agenda Item 3-J**.

⁶ For example, in France, the French Institute adopted only extant Parts A and B. Consequently, the requirements in extant Part C are not applicable to PAPPs.

⁷ Part A, *General Application of the Code*

⁸ Part B, *Professional Accountants in Public Practice*

⁹ See paragraph 100.3 of extant Code (presented as paragraph 4 of the Guide in Structure ED-1).

Clarification of the term PAIB¹⁰

15. A member expressed a view that the proposed wording in bullet point “B” of the clarification of the term PAIB should not focus on the legal relationship between a PAPP and their firm, but more on the nature of the role that is being performed that might require the PAPP to consider guidance in extant Part C.
16. The Task Force feels that Part C could also be applicable to a PAPP’s relations with colleagues within the PAPP’s firm, hence rewording the bullet point to just consider the functional relationship between the PAPP and the role that they are performing could narrow the scope of situations in which a PAPP would consider the guidance in Part C. Hence no changes have been made to the footnote in this regard.
17. The member’s view however has been considered in revisions to the “explanatory paragraph” clarifying the applicability of Part C to PAPPs.

Revised Restructuring of Extant Paragraph 310.4

18. At the June 2016 meeting, a member commented that beginning the second sentence in the proposed revised paragraph with the word “when” could imply that the guidance in the sentence was a requirement on the professional accountant. After considering some editorial suggestions, the Task Force is of the view that the addition of the word “such” into the second sentence would clarify that the provisions within this sentence are applicable only if the professional accountant were to seek guidance from outside the employing organization.

Revised Restructuring of Extant Paragraph 320.3

19. Also, a member expressed a concern over the proposed restructured text, indicating that it could be interpreted to mean that a professional accountant should not use discretion at all. The member was of the view that the material needed to clarify that the professional accountant is able to exercise discretion, but not with the intention to mislead and that use of discretion is one of several methods that a professional account could use to mislead. It was noted that the focus of the extant material in the close-off document is to specifically deal with the misuse of discretion with the intention to mislead. The Task Force was cautioned against revisiting issues that were previously approved within the close-off document.
20. The Task Force has reviewed the restructured text and considers it to be appropriate and in line with the extant material in the close-off document.

Glossary Definition of PAIB

21. The Part C Task Force considered how the glossary definition of a PAIB could be enhanced to align it to the definition of a PAIB in extant 300.3.¹¹ The Task Force considered that the glossary definition needed to accommodate all types of relationships that a PAIB might have with the employing

¹⁰ As per the initial restructuring guidelines, the clarification of the term PAIB was presented as a footnote in the restructured paragraph 200.1. Revised redrafting guidelines do not permit the use of footnotes and hence the clarification to be presented within the body of the restructured text.

¹¹ Extract from 300.3: A professional accountant in business may be an employee, contractor, partner, director (executive or non-executive), owner-manager, or volunteer of an employing organization.

organization. When enhancements to paragraph 300.3 were being considered as part of Part C Phase 1, the Task Force considered the various types of relationships that a PAIB could have with the employing organization and drafted the paragraph accordingly.

22. The Task Force is thus of the view that alignment could be achieved by expanding the glossary definition to include additional types of relationships, detailed in paragraph 300.3, that a PAIB could have with an employing organization. On reviewing the extant glossary definition, the Task Force also feels that the guidance could be streamlined by removing commerce and service as sectors as these would be covered under industry.
23. The Task Force's proposed changes to the glossary definition to achieve alignment are shown in mark-up below:

A professional accountant that is an employee or contractor, partner, director (executive or non-executive) owner-manager or volunteer or engaged in an executive or non-executive capacity operating in such areas as ~~commerce~~, industry, ~~service~~, the public sector, education, the not for profit sector, regulatory ~~bodies~~ or professional bodies, ~~or an accountant contracted by such entities.~~¹²

Conforming Amendments Arising out of the Safeguards Project

24. As part of the conforming amendments arising out of the Safeguards project, the Part C and Safeguards Task Forces are of the view that it would be helpful to provide an example of an advocacy threat. The Task Forces acknowledged that the "close-off" document did not include an examples of an advocacy threat, but was of the view that this was more apparent in the restructure material. Accordingly, the Task Forces propose the inclusion of the following example in paragraph 200.5 A1 (c):

"A professional accountant, in order to obtain favorable financing, includes in, or excludes critical information from a prospectus."

25. Also, within paragraph 200.5 A2, the Task Forces agreed that one of the examples of a familiarity threat¹³ would be more suitably presented as an example of a self-interest threat.

Matter for IESBA Consideration

4. IESBA members are asked for their views about the proposed revisions made to restructure close-off document, in particular the conforming changes arising from safeguards (i.e., the paragraphs shaded in gray).
5. Do IESBA members agree to the revised glossary definition for PAIBs set out in paragraph 21 above?
6. Do IESBA members agree to include the example of advocacy threats in paragraph 200.5 A1 (c)?

¹² Marked to show changes to proposed restructured definition in **Agenda Item 3-B**.

¹³ A professional accountant accepting a gift or special treatment, unless the value is trivial and inconsequential.