

Benchmarking Initiative – Working Draft of Phase 1 Report as of November 22

Note to IESBA Meeting Participants: This draft has been updated to incorporate the Working Group’s progress to-date, including revisions to address the input provided by the IESBA and the IESBA CAG in September 2021. The document is subject to further refinements and includes placeholders for:

- The comparison of the Code and SEC/ PCAOB Rules on financial interest; and
- The comparison of the Code and the SEC/ PCAOB Rules on long association/ partner rotation.

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I. Introduction

Objective of the Benchmarking Initiative

1. The IESBA's benchmarking initiative compares the provisions of the IESBA's [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#), (the Code) with corresponding provisions in the laws and regulations of other jurisdictions that address auditor independence, including:
 - (a) The nature of the relationship between an auditor and an audit client, and
 - (b) The activities and services that may and may not be provided by an auditor to an audit client.
2. The comparison is intended to highlight the similarities and differences between the Code and the different jurisdictional-level independence rules and regulations. This initiative does not extend to making judgments as to the relative merits of the different approaches, rules or regulations.
3. The objective of this initiative is to promote awareness and adoption of the current version of the Code, especially the International Independence Standards (IIS).¹ It will also help the IESBA to identify any specific provisions of the IIS and the Code that it should review and, if appropriate, address as part of its future strategy and work plan.

About this Report

4. The report summarizes the outcome of Phase I of the IESBA Benchmarking Initiative. The initiative involved comparing the current IIS that are applicable to public interest entities (PIEs) with the independence requirements for entities subject to the US Securities and Exchange Commission (SEC/ the Commission) and the US Public Company Accounting Oversight Board (PCAOB) (collectively "SEC/PCAOB"). The comparison in this report (the "Report") focuses primarily on the independence requirements of the SEC and refers to the PCAOB independence requirements only where those requirements are more stringent than the SEC's framework.
5. This Report does not make qualitative comparisons between the provisions of the Code and the SEC/PCAOB requirements (such as whether one framework is more stringent or rigorous than the other) because:
 - a) The two frameworks are not directly comparable. As explained in Section II, they have different jurisdictional bases and adopt different conceptual approaches; and
 - b) Perceptions vary depending on the perspective of the reader – a standard-setting body adopting the Code might have a different focus from a regulator whose primary responsibility is enforcement.

¹ The current version of the Code (i.e., the 2021 edition) was released in October 2021. It includes all revisions that were approved by the IESBA as of December 2020 (including those that are not yet effective) namely:

- [Revised Part 4B](#), *Independence for Assurance Engagements Other than Audit and Review Engagements* which became effective in June 2021.
- The [revisions](#) arising from the Role and Mindset Expected of Professional Accountants project that will become effective in December 2021.
- The revisions relating to the objectivity of an engagement quality reviewer and appropriate reviewers that will become effective in December 2022.
- The Non-Assurance Service (NAS) and fee-related revisions to the Code that will become effective in December 2022.

The analysis in this Report therefore focuses on whether the provisions/rules address the same issues and achieve the same substantive outcomes.

6. This Report does not amend or override the Code, the text of which alone is authoritative, and does not constitute an authoritative or official pronouncement of the IESBA. Reading this Report is not a substitute for reading the Code. Readers are also cautioned to apply judgment in reading and interpreting this Report within the context of their jurisdiction.

Focus Areas and Topics

7. This Report reflects the IESBA Staff's understanding of the respective frameworks being compared. The IESBA Staff developed this Report based on input received from the IESBA's Benchmarking Working Group and the IESBA.
8. This Report deals with focus areas and topics that are greatest interest to IESBA, users of the Code and other stakeholders. These focus areas and topics include:
 - Overarching Principles and Approach (including non-compliance with laws and regulations)
 - Key Definitions
 - Fee-related Provisions
 - Permissibility of Non-Assurance Services (NAS)² to Audit Clients, Including Prohibited Services
 - Auditors' Communication with Those Charged With Governance (TCWG) about Independence Matters, Including Pre-approval of NAS and Disclosures about Fees
 - Financial Relationships
 - Business Relationships
 - Partner Rotation/Long Association
 - Gifts and Hospitality
9. The identification of the areas to be considered in this Report does not imply that those areas would be more important to auditor independence than other topics or standards not considered in this Report.

II. Overarching Principles

The Fundamental Principles and the Conceptual Framework

10. The Code establishes five fundamental principles with which all professional accountants and firms are required to comply in all circumstances. The Code also requires accountants to apply a specified conceptual framework to identify, evaluate and address threats to compliance with those

² Except where otherwise noted, NAS in this paper is used to refer to the term "non-assurance services" as used in the IESBA Code. In some jurisdictions the term "non-audit services" is used. For example, the term "non-audit services" is used in the US 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 IESBA Code.

fundamental principles. Applying the conceptual framework requires exercising professional judgement, having an inquiring mind, and using the reasonable and informed third party test.

11. Under the Code's conceptual framework, a professional accountant is required to identify whether any threat to compliance with the fundamental principles exists and, if so, to evaluate that threat to determine whether it is at an acceptable level.³ If the threat is not at an acceptable level, the conceptual framework requires the accountant to address that threat having regard to the facts and circumstances by either:
- a) Eliminating the circumstances, interests or relationships that are creating the threat;
 - b) Applying safeguards, where available and capable of being applied, to reduce the threat to an acceptable level; or
 - c) Declining or ending the specific professional activity [or engagement that gives rise to the threat.

The Code's (including the IIS') requirements and application material are collectively referred to as the Code's "provisions." The Code's provisions are interconnected by design—using a "building blocks" approach and drafting conventions that minimize duplication. Therefore, the provisions in Part 1 apply equally across all professional activities and are not repeated in Parts 2, 3 and 4, except for emphasis. This approach demonstrates the scalability of the Code's provisions and emphasizes the overarching principles-based provisions that apply to all accountants in all situations.

The Code notes that there are some situations in which threats can only be addressed by declining or ending the professional activity. This arises when the circumstances creating the threats cannot be eliminated and safeguards are not capable of being applied to reduce the threat to an acceptable level.⁴

Independence Provisions in the Code

12. In addition, the Code includes the IIS which require professional accountants to be independent when performing audit, review, and other assurance engagements. A professional accountant undertaking an assurance engagement is also required to apply the Code's conceptual framework to identify, evaluate, and address threats to independence. Applying safeguards is only one way that threats to independence may be addressed. The Code provides examples of safeguards that might be applied to reduce a threat to independence an acceptable level.
13. The Code's requirements are designated with the letter "R" and in most cases include the word "shall". Some requirements explicitly prohibit certain relationships between the auditor and the audit client, or the provision of particular activities or services to the audit client. The Code also includes application material which provides context that is relevant to a proper understanding of the requirement or provision to which it relates. While such application material does not itself impose a requirement, consideration of the material is necessary for the proper application of the

³ The Code's conceptual framework provides descriptions and definitions of key terms and concepts, including:

- Acceptable level – a level at which a professional accountant using the reasonable and informed third party test would likely conclude that the accountant complies with the fundamental principles (see paragraph 120.7A1).
- Reasonable and informed third party – a consideration by the professional accountant about whether the same conclusions would be reached by another party (see paragraph 120.7 A1).
- Safeguards – actions, individually or in combination, that the professional accountant takes that effectively reduces threats to compliance with the fundamental principles (and to independence) to an acceptable level (see paragraphs 120.10 A2).

⁴ See paragraph 120.10 A1

requirements of the Code, including the application of the conceptual framework. Application material is designated with the letter “A”.

14. The IIS includes additional requirements and application material that are applicable when a professional accountant is providing professional services to a “public interest entity” (PIE), a category that includes entities listed on a recognized stock exchange or other equivalent body. (see paragraph 41 below).

The SEC/PCAOB Rules

SEC Rules

15. The independence rules of the SEC must be complied with for audits required by US federal securities laws, including audits of the financial statements of issuers.⁵ Regulation S-X⁶ sets out the form and content of, and requirements for, financial statements required to be filed with the Commission, including the requirements for auditor independence.
16. [Rule 2-01 of Regulation S-X](#) requires auditors to be qualified and independent of their audit clients both in fact and in appearance. Accordingly, Rule 2-01 sets out restrictions, among others, on financial, employment, and business relationships between an accountant and an audit client and restrictions on an accountant providing certain non-audit services to an audit client.⁷
17. Rule 2-01(b)⁸ provides, as a general standard of auditor independence, that
“The [Security and Exchange] Commission will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant’s engagement. In determining whether an accountant is independent, the Commission will consider all relevant circumstances, including all relationships between the accountant and the audit client, and not just those relating to reports filed with the Commission.”
18. Rule 2-01(c)⁹ includes a non-exclusive list of specific rules and restrictions that are intended to reflect the general standard’s application to particular circumstances. However, in cases where Rule 2-01 (c) does not address specific situations or circumstances, accountants are required to consider the general standard to determine whether their independence is compromised.
19. To achieve this, Rule 2-01¹⁰ states that “the rule does not purport to, and the Commission could not, consider all circumstances that raise independence concerns, and these are subject to the

⁵ Based on Sarbanes Oxley Act of 2002, Section (2)(a)(7), the term “issuer” means an issuer (as defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c)), the securities of which are registered under section 12 of that Act (15 U.S.C. 78l), or that is required to file reports under section 15(d) (15 U.S.C. 78o(d)), or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933 (15 U.S.C. 77a et seq.), and that it has not withdrawn.

⁶ 17 C.F.R. Part 210

⁷ In considering Regulation S-X, regard has been given to the following independence related amendments, including in:

- [SEC Release \(2000\) - Revision of the Commission’s Auditor Independence Requirements](#)
- [SEC Release \(2003\) - Strengthening the Commission’s Requirements Regarding Auditor Independence](#)
- [SEC Release \(2019\) - Auditor Independence with Respect to Certain Loans or Debtor-Creditor Relationships](#)
- [SEC Release \(2020\) – Qualification of Accountants](#)

⁸ SEC Rule 2-01 of the Commission’s Regulation S-X, 17 C.F.R. § 210.2-01 (b)

⁹ SEC Rule 2-01 of the Commission’s Regulation S-X, 17 C.F.R. § 210.2-01 (c)

¹⁰ SEC Rule 2-01 of the Commission’s Regulation S-X, 17 C.F.R. § 210.2-01 Introductory note

general standard in §210.2-01(b). In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service:

- creates a mutual or conflicting interest between the accountant and the audit client;
- places the accountant in the position of auditing his or her own work;
- results in the accountant acting as management or an employee of the audit client; or
- places the accountant in a position of being an advocate for the audit client.”

PCAOB Rules

20. Audits of issuers (and broker-dealers) must also be performed in accordance with the requirements of the PCAOB, following their approval by the SEC. The PCAOB adopted ethics and independence standards and rules (i) issued by the PCAOB ([PCAOB rules](#)), and (ii) - on an interim basis - promulgated by other bodies, including the AICPA ([Interim Ethics and Independence Standards](#)). The Interim Ethics and Independence Standards consist of the
 - Ethics and independence standards in the AICPA's Code of Professional Conduct, and interpretations and rulings thereunder, in existence on April 16, 2003, to the extent not superseded or amended by the PCAOB, and
 - Independence Standards of the Independence Standards Board.
21. The PCAOB did not adopt the SEC independence rules, as those rules were already applicable to auditors of SEC issuers. Where SEC rules and PCAOB rules and Interim Ethics and Independence Standards are not equivalent, auditors of issuers (and broker-dealers) are required to comply with the more restrictive provision.¹¹ PCAOB Rule 3520 further provides that PCAOB registered firms and their associated persons must comply with both PCAOB and SEC independence criteria.
22. In preparing this Report, the IESBA Staff took an incremental approach and focused primarily on the SEC rules, then also considered those PCAOB rules that are more restrictive than the SEC Rules. The Report only includes reference to PCAOB's [Ethics and Independence Rules and Interim Standards](#), as well as other relevant PCAOB Standards and PCAOB [Rules of the Board](#) when, based on IESBA Staff's evaluation, those are incremental to the SEC rules.

The IESBA and SEC/PCAOB Frameworks Compared

Global Framework / Jurisdictional Framework

23. The Code and the SEC/PCAOB rules address fundamentally different contexts, which result in the different approaches that each has adopted:
 - (a) The Code applies to all professional accountants irrespective of the professional activity undertaken and the IIS apply to accountants performing audits, reviews or other assurance engagements for any entity. The SEC and PCAOB rules apply to auditors of issuers, as well as certain other entities where compliance with SEC Rule 2-01 and the PCAOB rules is required.

¹¹ In late 2020, the PCAOB made targeted conforming amendments to their independence rules to (i) avoid differences between the SEC and PCAOB independence rules; (ii) avoid duplicative requirements; and (iii) provide greater regulatory certainty.

- (b) The Code is prepared for adoption in any jurisdiction in the world and its application relies on national laws and regulations in that jurisdiction. The SEC and PCAOB rules are developed for application in accordance with the relevant US legislation and regulation.
- (c) The IESBA Code applies when professional activities/ services are provided to any entity, irrespective of their size, business and market specificities. As there is a higher expectation regarding the independence of firms auditing PIEs, the Code includes specific provisions addressing relationships with and services provided to those entities. The SEC/PCAOB rules address the relationships and provisions of services to audit clients having greater public interest relevance.

Application of the Conceptual Framework / General Independence Standard

- 24. Neither the Code nor the SEC framework is entirely “rules-based” or entirely “principles-based”. Both frameworks include strong overarching principles that are supported with specific requirements (a “hybrid approach”).
- 25. Under both the Code and the SEC rules, the determination of “independence” requires consideration of both independence in mind/in fact and independence in appearance:

Code (Independence in mind)	SEC (Independence in fact)	Code (Independence in appearance)	SEC (Independence in appearance)
<p>“Independence of mind - the state of mind that permits the <u>expression of a conclusion without being affected by influences that compromise professional judgment</u>, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.”</p>	<p>“The Commission will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, (...) capable of <u>exercising objective and impartial judgment on all issues</u> encompassed within the accountant's engagement.”</p>	<p>“Independence in appearance - the avoidance of facts and circumstances that are so significant that <u>a reasonable and informed third party would be likely to conclude that a firm's, or an audit team member's, integrity, objectivity or professional skepticism has been compromised.</u>”</p>	<p>“The Commission will not recognize an accountant as independent, with respect to an audit client, if (...) <u>a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues</u> encompassed within the accountant's engagement.”</p>

- 26. Under both frameworks, the “reasonable and informed third party” test / “reasonable investor with knowledge of all relevant facts and circumstances” test has a significant role in the assessment of a firm’s independence. In the Code, the “reasonable and informed third party test” is also a basis for evaluating whether a threat to independence is at an acceptable level. Similarly, when applying the general standard in the SEC rules in circumstances other than the ones addressed by Rule 2-01(c), the four principles in paragraph 19 should be applied when considering Rule 2-01(b) in determining whether the firm is independent.

27. Both frameworks set out similar fundamental objectives (or principles) by which an auditor's independence is assessed when applying the Code's conceptual framework or determining compliance with the SEC's general independence standard. The table below provides a comparison of the high-level concepts of the fundamental objectives (or principles) from each framework.¹²

<p><i>Concepts in IESBA's Conceptual Framework and Overarching Principles to Independence that are Analogous to SEC's General Standard</i></p>	<p><i>SEC's Rule 2-01 Introductory Note¹³</i></p> <p>"The rule does not purport to, and the Commission could not, consider all circumstances that raise independence concerns, and these are subject to the general standard in §210.2-01(b). In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service:"</p>
<p>A professional accountant shall not allow a conflict of interest to compromise professional or business judgment.¹⁴</p>	<ul style="list-style-type: none"> • creates a mutual or conflicting interest between the accountant and the audit client
<p>Self-interest threat - the threat that a financial or other interest will inappropriately influence a professional accountant's judgment or behavior.</p>	
<p>Familiarity threat - the threat that due to a long or close relationship with a client, or employing organization, a professional accountant will be too sympathetic to their interests or too accepting of their work.</p>	
<p>Intimidation threat - the threat that a professional accountant will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the accountant.</p>	

¹² The specific provisions supporting these objectives (or principles) are presented in the sections below.

¹³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (b)

¹⁴ Part III – Professional Accountant in Business, Section 310, Conflict of Interest, Paragraph R310.4. Based on the Code's building blocks approach, requirements and application material in Part III of the Code are also applicable in the context of the IIS.

<p>Self-review threat - the threat that a professional accountant will not appropriately evaluate the results of a previous judgment made; or an activity performed by the accountant, or by another individual within the accountant's firm or employing organization, on which the accountant will rely when forming a judgment as part of performing a current activity.</p>	<ul style="list-style-type: none"> places the accountant in the position of auditing his or her own work.
<p>A firm or a network firm shall not assume a management responsibility for an audit client.¹⁵</p>	<ul style="list-style-type: none"> results in the accountant acting as management or an employee of the audit client
<p>Advocacy threat - the threat that a professional accountant will promote a client's or employing organization's position to the point that the accountant's objectivity is compromised;</p>	<ul style="list-style-type: none"> places the accountant in a position of being an advocate for the audit client.

Evaluation of Threats

28. Although both frameworks set out similar fundamental objectives (or principles), the assessment and the application of those principles are different in the two independence frameworks.
29. The SEC's framework requires an auditor to determine whether the provision of a particular service or relationship would result in a breach/violation of the overarching principles and, if so, prohibits the provision of that service or relationship regardless of the materiality or significance of the breach/violation.
30. Under the Code, provided the relationship or provision of a specific service is not explicitly prohibited, the application of the conceptual framework requires the auditor to identify threats to compliance with the fundamental principles, to evaluate the level of a threat identified and then to determine whether any safeguards are available and capable of reducing that threat to an acceptable level. If appropriate safeguards are not available, the Code requires the auditor to end the specific professional activity.

Commentary

31. The two frameworks prescribe different processes for the determination of whether a relationship or service is prohibited.
 - a) The Code focuses on the possibility that a service or relationship might give rise to a threat – and then on whether that potential threat is at or can be reduced to an acceptable level. Only if the threat cannot be reduced to an acceptable level is the service or relationship prohibited.
 - b) By contrast, the SEC prohibits services or relationships that would involve a breach of the overarching principles. As a result, a firm's assessment focuses on whether any of the overarching principles will be breached.

¹⁵ Paragraph R410.13 of the Code

32. While the Code focuses on potential threats and then requires firms to put in place safeguards, the SEC rules do not permit safeguards to address situations where a service or relationship would otherwise breach the overarching principles. An all-encompassing comparative evaluation is, therefore, not possible as much will turn on the specific circumstances.

Assuming Management Responsibility

33. The Code prohibits firms assuming a management responsibility for an audit client.¹⁶ That prohibition applies to all aspects of the relationship between a firm and an audit client. The Code provides that management responsibility involves “controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, technological, physical and intangible resources.”¹⁷
34. The Code sets out criteria that firms are required to meet to demonstrate that the management of the audit client makes all judgments and decisions that are management’s proper responsibility, and that a designated competent employee will take ultimate responsibility for any actions arising from the activities. Under the Code, a firm will not be assuming management responsibility provided it complies with these criteria.¹⁸
35. As one of the overarching principles, the SEC rules includes a general prohibition from acting as management. They also prohibit a firm from acting as an employee of an audit client
36. In addition to this overarching prohibition, the SEC rules include a specific ban for the provision of any non-audit service that would constitute a management function, i.e., “acting, temporarily or permanently, as a director, officer, or employee of an audit client, or performing any decision-making, supervisory, or ongoing monitoring function for the audit client.”
37. The table below includes the relevant provisions of the Code and SEC rules:

Code’s revised provisions		SEC rules
R400.13	A firm or a network firm shall not assume a management responsibility for an audit client.	2-01 (b) ¹⁹ In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service (...) results in the accountant acting as management or an employee of the audit client; (...)
400.13 A1	Management responsibilities involve controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, technological, physical and intangible resources.	2-01 (c) (4) ²⁰ An accountant is not independent if, at any point during the audit and professional engagement period, the accountant provides the following non-audit services to an audit client
(...)		(vi) Management functions. Acting, temporarily or permanently, as a director, officer, or employee of an audit client, or performing any

¹⁶ Revised paragraph R400.13 of the Code

¹⁷ Revised paragraph 400.13 A1 of the Code

¹⁸ Revised paragraph R400.14 of the Code

¹⁹ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (b)²¹

Paragraph R523.3 of the Code

²¹ Paragraph R523.3 of the Code

<p>R400.14 When performing a professional activity for an audit client, the firm shall be satisfied that client management makes all judgments and decisions that are the proper responsibility of management. This includes ensuring that the client's management:</p> <p>(a) Designates an individual who possesses suitable skill, knowledge and experience to be responsible at all times for the client's decisions and to oversee the activities. Such an individual, preferably within senior management, would understand:</p> <p>(i) The objectives, nature and results of the activities; and</p> <p>(ii) The respective client and firm or network firm responsibilities.</p> <p>However, the individual is not required to possess the expertise to perform or re-perform the activities.</p> <p>(b) Provides oversight of the activities and evaluates the adequacy of the results of the activities performed for the client's purpose.</p> <p>(c) Accepts responsibility for the actions, if any, to be taken arising from the results of the activities.</p>	<p>decision-making, supervisory, or ongoing monitoring function for the audit client.</p>
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Commentary

38. Both frameworks prohibit a firm assuming management responsibility/acting as management for an audit client. However, the approaches in the Code and in the SEC rules differ.
- a) The Code focuses on whether the client's management is taking responsibility for those decisions relating to the services being provided that are properly the responsibility of management. Provided management does take such responsibility, the firm is permitted to provide the services concerned.
 - b) In contrast, the SEC rules prohibit the provision of services which the SEC regards as being the proper function of management. The prohibition applies irrespective of
 - i. The significance of the activity (and therefore prohibits matters that are routine or administrative),
 - ii. Any arrangements that might be in place to ensure that management takes responsibility for decisions relating to such services.
39. The SEC rules prohibit
- a) providing services or undertaking activities that would ordinarily be undertaken by an employee of an audit client.
 - b) activities such as acting, temporarily or permanently, as a director, officer, or employee of an audit client.
40. The Code prohibits²¹ a partner or an employee of an audit firm from serving as a director or an officer of an audit client. However, the Code does permit personnel to be loaned to an audit client for a short period of time, provided certain conditions are met.²²

Non-Compliance with Laws and Regulations

41. The Code *[and the SEC/PCAOB rules both]* require professional accountants, including the auditor, to comply with legislation that governs how professional accountants address actual or suspected non-compliance with laws and regulations.²³ Such legal or regulatory provisions typically apply to offenses such as terrorism, drug dealing, money- laundering, and dealing with the proceeds of crime; the required disclosure is to a designated authority.
42. Auditors might encounter actual or suspected non-compliance with laws and regulations other than those referred to in paragraph 41. The Code contains requirements and provides guidance on the approach to be taken by professional accountants in such circumstances.
43. The Code's approach focuses on non-compliance with laws and regulations:
- (i) that directly affect a client's financial statements or
 - (ii) where non-compliance might threaten a client's activities and continued operations.²⁴
44. In view of an auditor's responsibility to act in the public interest, the auditor's objectives are to comply with the fundamental principles of objectivity and professional behavior by alerting management or TCWG of the identified or suspected non-compliance so they can take action to

²¹ Paragraph R523.3 of the Code

²² Paragraph R525.4 of the Code

²³ Paragraph R360.6 of the Code

²⁴ Paragraph 360.3 of the Code

rectify or mitigate the consequences of the non-compliance or prevent it from occurring, and to take such other action as might be appropriate.²⁵

45. The Code provides that an auditor who encounters actual or suspected non-compliance should:
- Obtain an understanding of the relevant facts and circumstances²⁶;
 - Discuss the matter with the appropriate level of management and, where appropriate, TCWG²⁷ and advise them to take appropriate and timely actions²⁸;
 - Comply with applicable laws, regulations and professional standards²⁹;
 - Assess the appropriateness of the response of management and TCWG³⁰;
 - Determine whether further action is required in the public interest (including reporting the matter to an appropriate authority and/or withdrawing from the engagement)³¹, including considering whether a reasonable and informed third party would conclude that the accountant had acted appropriately in the public interest³²;

The Code provides that disclosure made in good faith to an appropriate authority is permitted and does not create a breach of the fundamental principles.³³

46. The Code also contains guidance on the considerations an auditor might have regard to when reporting actual or suspected non-compliance with laws and regulations to an appropriate authority.³⁴
47. The PCAOB auditing standards require an auditor to be aware of the possibility that illegal acts may have occurred. If specific information comes to the auditor's attention that provides evidence of the existence of possible illegal acts that could have a material indirect effect on the financial statements, the auditor is required to apply audit procedures specifically directed to ascertaining whether an illegal act has occurred.³⁵
48. Neither the SEC nor the PCAOB independence rules address the steps that might be taken by an auditor on becoming aware that an illegal act has occurred or is occurring.

Commentary

49. This is an area that is addressed in the Code, but it is not addressed explicitly in the SEC/PCAOB independence rules. However, the PCAOB auditing standards, (PCAOB AS 2405) addresses the auditor's responsibility with respect for illegal acts related to the audit of the financial statements.

[Note– this section is subject to further refinement to capture relevant aspects of PCAOB AS 2405]

²⁵ Paragraph 360.4 of the Code

²⁶ Paragraph 360.10 of the Code

²⁷ Paragraph R360.11 of the Code

²⁸ Paragraph R360.13 of the Code

²⁹ Paragraph R360.15 of the Code

³⁰ Paragraph R360.19 of the Code

³¹ Paragraphs R360.20 and 360.21 A1 of the Code

³² Paragraph R360.21 of the Code

³³ Paragraph R360.26 of the Code

³⁴ Paragraphs 260.20 A1 to 260.20 A3, and 360.25 A1 to A3 of the Code

³⁵ PCAOB AS 2405, paragraph 7

III. Key Definitions

50. A comparison of the key definitions is central to any benchmarking of the Code to the SEC/PCAOB rules, as substantive differences in those key definitions can materially affect the ambit and efficacy of the frameworks' substantive provisions.

Audit Client and Related Entities/ Affiliates

Audit Client

51. In the Code, the term 'audit client' is defined as any entity in respect of which a firm conducts an audit engagement, and the IIS apply to all firms and professional accountants undertaking such audit engagements.
52. The Code contains supplementary provisions that are applicable to audits of PIEs. A PIE is defined in the Code as:
- a) A listed entity; or
 - b) An entity:
 - i. Defined by regulation or legislation as a PIE; or
 - ii. For which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation might be promulgated by any relevant regulator, including an audit regulator.³⁶³⁷
53. In the context of the SEC rules, 'audit client' means the entity whose financial statements or other information is being audited, reviewed, or attested to and any affiliates of the audit client.³⁸
54. The SEC/PCAOB rules apply to audit firms and professional accountants that audit financial statements of 'issuers' among other entities. For purposes of this Benchmarking initiative, the term 'issuer' used in the SEC rules and 'listed entity' used in the PIE definition in the Code are equivalent. Although the Code applies to a wider group of entities than the SEC rules – by virtue of sub-paragraph (b) of the PIE definition - this Report compares the provisions of the Code relevant to auditors of PIEs with the requirements of the SEC rules.

Related Entities/ Affiliates

55. In the Code, the definition of an audit client includes its 'related entities.' Under the Code the related entities that are included in the definition of a PIE audit client that is a listed entity differ from the related entities if the audit client is an unlisted PIE.³⁹
56. Under the SEC rules, the definition of an audit client includes all 'affiliates'. It is therefore necessary to compare the definitions of 'related entities' in the Code with the definition of

³⁶ Please refer to the Glossary of the Code

³⁷ [Placeholder to highlight the forthcoming revisions to the definition of a PIE in which IESBA is planning to adopt in December 2021]

³⁸ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01(f) (6)

³⁹ Paragraph R400.20 of the Code provides that an audit client that is a listed entity includes all of its related entities. For all other entities, references to an audit client in this Part include related entities over which the client has direct or indirect control. When the audit team knows, or has reason to believe, that a relationship or circumstance involving any other related entity of the client is relevant to the evaluation of the firm's independence from the client, the audit team shall include that related entity when identifying, evaluating and addressing threats to independence

‘affiliates’ under the SEC rules to determine whether the application of the Code and the SEC rules to other entities within a group is equivalent in scope.

57. The table below summarizes the related entities of PIE listed audit clients under the Code and affiliates under the SEC rules:

Code - Related entities	SEC/PCAOB - Affiliates ⁴⁰
(a) An entity that has direct or indirect control over the client if the client is material to such entity;	(i) An entity that has control over the entity under audit, or over which the entity under audit has control, including the entity under audit's parents and subsidiaries;
(b) An entity with a direct financial interest in the client if that entity has significant influence over the client and the interest in the client is material to such entity;	(iv) An entity that has significant influence over the audit client, unless the audit client is not material to the entity; or
(c) An entity over which the client has direct or indirect control;	See point (i)
(d) An entity in which the client, or an entity related to the client under (c) above, has a direct financial interest that gives it significant influence over such entity and the interest is material to the client and its related entity in (c); and	(iii) An entity over which the audit client has significant influence, unless the entity is not material to the audit client;
(e) An entity which is under common control with the client (a “sister entity”) if the sister entity and the client are both material to the entity that controls both the client and sister entity.	(ii) An entity that is under common control with the entity under audit, including the entity under audit's parents and subsidiaries, when the entity and the entity under audit are each material to the controlling entity;
	(v) Each entity in the investment company complex as determined in paragraph (f)(14) of this section when the entity under audit is an investment company or investment adviser or sponsor, as those terms are defined in paragraphs (f)(14)(ii), (iii), and (iv) of this section.

58. Apart from the audit client, certain SEC rules apply only to “the entity under audit”, thereby excluding affiliates from scope of the requirement (see paragraph 227).

Commentary

59. There are two notable differences in the definitions in the two frameworks:
- The Code excludes entities that control an audit client if the audit client is immaterial to the controlling entity, whereas SEC rules include them; and

⁴⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01(f) (4)

- The Code includes relationships that result in significant influence only if that influence arises from a direct financial interest;⁴¹ the SEC rules apply irrespective of how that significant influence arises.⁴²

In both instances, the differences result in the SEC rules having a wider application.

60. The SEC rules define investment company complexes⁴³ and address which companies are included within an investment company complex and which are, therefore, considered affiliates of an audit client. Given its global context, the Code does not include specific provisions for investment company complexes. However, when adopting the recent changes to NAS and fee-related provisions of the Code, the IESBA considered the application of those revisions to investment company complexes, such as private equity complexes, and the Code revisions address the challenges arising from the complex structure of such entities.⁴⁴

Network Firms/ Associated Entities

61. Under the Code, firms and network firms are both required to be independent of their audit clients and the Code specifically states whether a specific provision applies not only to an audit firm, but also to any network firm.⁴⁵ In this Report, when referring to the use of 'firm' in the context of the Code, 'firm' includes network firms.
62. The SEC rules do not address specifically the position of network firms. However, the definition of an "accounting firm" includes⁴⁶ the accounting firm's "associated entities" and therefore the independence rules applicable to an accounting firm also apply to its "associated entities". In interpreting the rule, the SEC has regard to all the relevant facts and circumstances.⁴⁷

Commentary

63. As the SEC Staff's practice is to have regard to all the relevant facts and circumstances when applying its definition of an "accounting firm", it is not possible to provide a comprehensive list of all the types of entities that the SEC would regard as being within the definition of an accounting firm. However, both frameworks appear to have the same objective – namely to address the position of those firms which are required to be independent of an audit client.

Audit Team

64. The Code defines an "audit team" as
- All members of the engagement team for the audit engagement,
 - All others within a firm who can directly influence the outcome of the audit engagement,

⁴¹ See point (b) and (d) of the definition of related entities in the Glossary of the Code

⁴² SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (4) point (iii) and (iv)

⁴³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01(f)(14)

⁴⁴ Please refer to [Basis for Conclusions, Revisions to Fee-related Provisions of the Code](#), paragraphs 131 to 136

⁴⁵ Paragraphs 400.50 A1 to 400.54 A1 of the Code

⁴⁶ Based on SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (2) an "accounting firm" includes all of the organization's departments, divisions, parents, subsidiaries, and associated entities, including those located outside of the United States. An "accounting firm" also includes the organization's pension, retirement, investment, or similar plans.

⁴⁷ Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence – Frequently Asked Questions, [K. Definitions](#), Question 1

- All those within a network firm who can directly influence the outcome of the audit engagement.⁴⁸
65. The SEC rules define the “audit engagement team” as
- “All partners, principals, shareholders and professional employees participating in an audit, review, or attestation engagement of an audit client, including audit partners and all persons who consult with others on the audit engagement team during the audit, review, or attestation engagement regarding technical or industry-specific issues, transactions, or events”.*⁴⁹
66. When comparing the provisions of the Code and the SEC rules, it is relevant to note that the Code generally focuses on the audit team as the base, while the corresponding SEC rules apply to “covered persons” as well as to the members of the audit team (as defined). “Covered persons”⁵⁰ includes, but is not limited to, the partners, principals, shareholders, and employees of an accounting firm who form part of
- The “audit engagement team”;
 - The “chain of command”; and
 - Other partners, principals, shareholders, and managerial employees described in paragraph 67.

Commentary

67. The Code’s provisions apply to different individuals depending on the topic/area of the relationship. Where the Code’s provisions are relevant to the audit team only, the SEC rules are broader as the SEC rules apply to individuals who are not addressed in the Code’s audit team definition, namely:
- Any other partner, principal, shareholder, or managerial employee of the accounting firm who has provided ten or more hours of non-audit services to the audit client in the relevant time period, and
 - Any other partner, principal, or shareholder from an “office” of the accounting firm in which the lead audit engagement partner primarily practices in connection with the audit.
68. However, in the case of the prohibition on holding financial interests in the audit client⁵¹, the Code adopts a similar approach as SEC rules, and also includes other partners and managerial employees in the firm as persons to whom that prohibition applies.

Key Audit Partner/ Audit Partner

69. The Code⁵² and the SEC rules⁵³ adopt the same approach when defining a “key audit partner” (in the Code) and an “audit partner” (in the SEC rules). Whilst the individuals identified in the definition in each framework differ, both frameworks include the same categories of individuals, namely (a) the engagement partner/lead partner (b) the engagement quality reviewer (EQR), and

⁴⁸ Please refer to the Glossary to the Code

⁴⁹ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (7) (i)

⁵⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (11)

⁵¹ Paragraph R510.4 (c)-(d) of the Code

⁵² Please refer to the Glossary to the Code

⁵³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (7) (ii)

(c) other audit partners who make key decisions or judgments on significant matters with respect to the audit.

Commentary

70. The differences arise from the fact that SEC definition also includes:

- Other partners on the engagement team who maintain regular contact with management and the audit committee (whereas the Code only includes a partner who makes key decisions or judgments on significant matters); and
- Other audit engagement team partners who provide more than ten hours of audit, review, or attest services in connection with the annual or interim consolidated financial statements of the issuer or an investment company.

IV. Fees

Level of audit fees and total fees paid by an audit client

71. The 2021 fee-related revisions introduced new provisions to the IIS to address the threats to independence related to the audit payer model.⁵⁴ The Code approaches the issue of fees from the perspective that an inherent self-interest threat is created by fees of an audit firm being paid by an audit client. The Code does not seek to determine the level of fees that might be appropriate⁵⁵
72. Although the Code recognizes that the determination of audit fees is a business decision taking into account the facts and circumstances (including the requirements of professional and technical standards),⁵⁶ it emphasizes that the audit fee should be set on a standalone basis without regard to the level of fees for other services provided to an audit client.⁵⁷
73. Apart from level of fees, the Code explicitly addresses and includes requirements regarding the threats that might arise from the total amount of fees, including audit and other fees, paid by an audit client - such as the proportion of fees received from an audit client and a firm's dependency on fees received from an audit client.
74. Whilst the Code does not include any specific threshold or prohibition regarding the proportion of audit fees to non-audit fees, it does provide guidance on the evaluation of the level of threats created where a firm or network firm receives a large proportion of fees for the provision of services other than audit.⁵⁸
75. The Code provides guidance on the evaluation of the threats arising from fee-dependency at the firm, office or partner level.⁵⁹ Furthermore, if fees received from an audit client exceed 15 percent of the total fees of the firm, the Code requires the firm to determine – in line with the application of the conceptual framework – whether specific safeguards (pre-or a post issuance review by an external reviewer) could reduce the level of the threats to an acceptable level⁶⁰. If this level of

⁵⁴ Revised paragraph 410.3 A1

⁵⁵ Revised paragraphs 410.4 A1 to 410.4 A5

⁵⁶ Revised paragraph 410.5 A1

⁵⁷ Revised paragraphs R410.6 to R410.7

⁵⁸ Revised paragraphs 410.11 A1 to 410.11 A3

⁵⁹ Revised paragraphs 410.14 to 410.14 A7

⁶⁰ Revised paragraph R410.18

fee-dependency continues for more than five consecutive years, the Code requires the firm to cease to be the auditor and end the audit engagement.⁶¹

76. Complementing the specific provisions above, the 2021 fee-related revisions of the Code included new and enhanced requirements regarding disclosure of fee-related information to TCWG and to the public. (See paragraphs 90-91 below)
77. The SEC and PCAOB do not establish any independence rules to address any issues that might arise from the fees paid to the audit firm by the audit client. However, the SEC rules do require transparency of such fee-related information in the audit client's proxy statement. (See paragraph 92 below)

Commentary

78. While the Code includes detailed guidance and requirements in relation to the level of fees, the total amount of fees, and fee-dependency, the SEC and PCAOB ethics and independence rules do not address these issues.

Contingent Fees

Description

79. The Code defines contingent fees as fees that are calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed.⁶² A contingent fee charged through an intermediary is an example of an indirect contingent fee. A fee is not regarded as being contingent if established by a court or other public authority.
80. According to SEC rules, contingent fees are fees established for the sale of a product or the performance of any service pursuant to an arrangement under which no fee will be charged unless a specified finding or result is attained, or in which the amount of the fee is otherwise dependent upon the finding or result of such product or service. Under SEC's independence rules a fee is not a "contingent fee" if it is fixed by courts or other public authorities, or, in tax matters, if determined based on the results of judicial proceedings or the findings of governmental agencies.⁶³
81. Although the relevant PCAOB rules⁶⁴ and related definition of "contingent fee"⁶⁵ are modeled on the SEC's independence rules, the PCAOB rules differ in that the PCAOB rules do not include the SEC's exception for fees in tax matters if determined based on the results of judicial proceedings or the findings of government agencies.⁶⁶

Prohibitions

82. The Code expressly prohibits firms from charging, directly or indirectly, a contingent fee for an

⁶¹ Revised paragraph R410.21 provides an exception to this requirement if there is a compelling reason and the relevant profession or regulatory body concludes that it would be in the public interest if the firm continues the engagement, provided that all the conditions in paragraph

⁶² Revised paragraph 410.8 A1

⁶³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (10)

⁶⁴ Rule 3521. - Contingent Fees

⁶⁵ Rule 3501. Definitions of Terms Employed in Section 3, Part 5 of the Rules (c) (ii)

⁶⁶ As discussed in the Board's proposing release PCAOB , this exception may have been misinterpreted in the past and is largely redundant of the exception for fees fixed by courts or other public authorities. For these reasons, proposed Rule 3521 would eliminate this exception.

audit engagement⁶⁷ or other assurance engagement.⁶⁸ The Code also prohibits firms (or network firms) from charging, directly or indirectly, a contingent fee for a NAS provided to an audit client if:

- The fee is material or expected to be material to the firm expressing the opinion on the financial statements;
- The fee is charged by a network firm that participates in a significant part of the audit and the fee is material or expected to be material to that firm; or
- The outcome of the NAS, and therefore the amount of the fee, is dependent on a future or contemporary judgment related to the audit of a material amount in the financial statements.⁶⁹

83. The SEC rules state that a firm is not independent if, at any point during an audit or professional engagement period, it provides a service or product to an audit client for a contingent fee or a commission, or receives a contingent fee or commission from an audit client.⁷⁰ In addition, the PCAOB rules provide that a firm is not independent of an audit client if it receives a contingent fee or commission from that client "directly or indirectly".⁷¹

Commentary

84. Both frameworks prohibit firms from charging contingent fees for any audit or other assurance engagements.

85. While the SEC rules also prohibit a firm charging a contingent fee for any other service or product provided to an audit client, the Code:

- Prohibits charging contingent fees for a NAS provided to an audit client only if that fee is material;⁷²
- Require firms to apply the conceptual framework to identify, evaluate and address threats to independence that might be created by charging contingent fees for the provision of a NAS to an audit client.

86. In addition, the SEC rules restrict firms from providing services or products to an audit client for a commission. In contrast, the Code does not include a general prohibition on receiving such

⁶⁷ Revised paragraph R410.9

⁶⁸ Paragraph 905.7

⁶⁹ Revised paragraph R410.10

⁷⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (5)

⁷¹ The PCAOB rule's use of the term "indirectly" is meant to prevent arrangements for a fee from any person that is contingent on a finding or result attained by the audit client. The Board's determination to include such fees within the prohibition is based on the principle that, regardless of who pays the contingent fee, such a contingency gives an auditor a stake in the audit client attaining the finding or result. Accordingly, under Rule 3521, it does not matter who pays the contingent fee, if it is contingent on a finding or result attained by the audit client or otherwise related to the firm's services for the audit client. That is, while use of an intermediary to disguise an audit client's agreement to a contingent fee is certainly prohibited, the rule is not limited to circumstances in which a contingent fee may be traced (e.g., through an intermediary) to an agreement or payment by an audit client.

⁷² Paragraph 144 of the [Basis for Conclusions](#), *Revisions of Fee-related Provisions of the Code*, notes that:

- The changes arising from the NAS project (in particular the self-review threat prohibition) will significantly limit the extent of permissible NAS a firm could provide, especially to a PIE audit client.
- If the provision of a NAS is not prohibited by the revised NAS provisions and the contingent fee does not meet any criteria that would result in a prohibition according to paragraph R410.10, the conceptual framework will apply in addressing the self-interest threat created.

commissions if the criteria of a contingent fee is not met. However, the Code identifies that a self-interest threat to compliance with the principles of objectivity and professional competence and due care is created if the firm receives a commission relating to a client and requires the firm to apply the conceptual framework to reduce the level of such threat to an acceptable level.⁷³

Overdue Fees

87. The Code recognizes that firms generally obtain payment of fees for audit or services other than audit before an audit report is issued.⁷⁴ If a significant part of the fees due from an audit client remains unpaid for a long time, the Code requires the firm to determine
- Whether the overdue fees might be equivalent to a loan to the client, in which case the provisions of the Code governing loans to clients are applicable; and
 - Whether it is appropriate for the firm to be re-appointed or continue the audit engagement.⁷⁵
88. The SEC and PCAOB rules and guidance do not address overdue fees. However, in its response to a FAQ⁷⁶, the SEC Staff stated that “if audit and other professional services fees are owed to an accountant for an extended period of time and become material in relation to the fee expected to be charged for a current audit, there may be a question concerning the accountant’s independence with regard to the current audit because the accountant may appear to have a direct interest in the results of operations of the client.”

Commentary

89. Both frameworks recognize that fees for audit and other services provided to the audit client that remain unpaid for a long time, and are material, could impact the firm’s independence, and require a firm to assess the position and take appropriate action.

Transparency of Fee-related Information

90. The IESBA recognizes that transparency of fee-related information, including public disclosure, contributes to confidence in auditor independence. In some jurisdictions, national laws and regulations specify the information to be provided. Where no such laws or regulations exist, disclosure of fee-related information is the responsibility of the client management.⁷⁷ To address those circumstances, the Code requires audit firms to [discuss/communicate] the benefits to the client’s stakeholders of the client making such disclosures.⁷⁸
91. If the fee-related information is not disclosed by the client, the Code requires the firm to make information about audit fees, fees for services other than audit, and fee-dependency publicly available. The Code does not prescribe how that is to be achieved – it adopts a flexible approach recognizing that a firm will need to have regard to applicable laws and regulation.⁷⁹

⁷³ Paragraph 330.5 A1 of the Code

⁷⁴ Revised paragraph 410.12 A2

⁷⁵ Revised paragraph R410.13

⁷⁶ Office of the Chief Accountant: Application of the Commission’s Rules on Auditor Independence – Frequently Asked Questions, [A- General Standards of Independence](#), Question 2

⁷⁷ [Basis for Conclusions](#), Revisions to Fee-related Provisions

⁷⁸ Revised paragraph R410.30

⁷⁹ Revised paragraphs R410.31 to R410.32

92. The SEC requires an issuer to disclose in its proxy statement the aggregate fees billed for each of the last two fiscal years, grouped as audit fees, audit-related fees, tax fees and other fees paid by the audit client to the principal accountant.⁸⁰

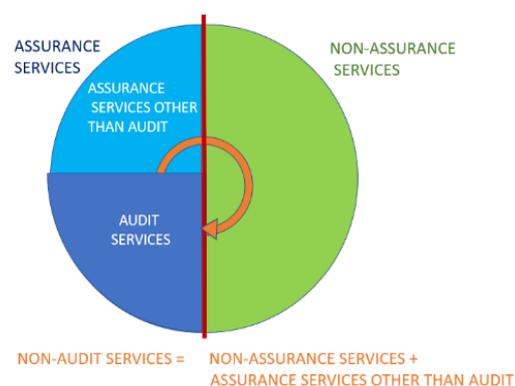
Commentary

93. Both the IESBA and the SEC attach importance to the public disclosure of information about fees paid to auditors for audit and other services.
94. However, given their different remits, the Code and the SEC rules establish different ways to achieve public disclosure. As a national regulator, the SEC has authority to establish requirements for the disclosure of fees by the audit client. In contrast, as the IESBA does not have legislative or regulatory authority in those jurisdictions that adopt the Code, the Code can only require a firm
- To promote the disclosure of fee-related information by an audit client, and
 - To publish that information in such manner as might be possible if an audit client refuses to disclose that information.

V. Provision of Non-Assurance/ Non-audit Services to Audit Clients

95. The Code and the SEC rules have the same overarching objective, namely, to ensure that the provision of additional services to audit clients does not compromise an audit firm's independence. In both frameworks, the approach taken is similar, in that both frameworks rely on strong overarching principles, complemented by a list of specific prohibited services.

PROFESSIONAL SERVICES OFFERED TO AN AUDIT CLIENT



96. Although the conceptual approach adopted by the two frameworks is similar, the relevant section of the Code⁸¹ applies only to the provision of non-assurance services to audit and review clients.⁸² The provision of assurance services other than audit and review, and audit-related services, are governed by the fundamental principles and the conceptual framework. The SEC rules⁸³ identify specific services that firms are prohibited from providing to audit clients (irrespective of whether they are non-assurance or non-audit services). All other services are subject to the SEC general standards and overarching principles.
97. This section compares the overarching principles relevant to the provision of non-audit/non-assurance services to an audit client and then, separately, compares the specific services prohibited under each framework. The role of TCWG in relation to the provision of NAS or non-audit services is considered in Section VII below.

⁸⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 240.14a-101 Schedule 14A. Information required in proxy statement – Item 9

⁸¹ Revised Section 600 of the Code

⁸² The provisions in the IIS apply to both audit and review engagements. The terms "audit," "audit team," "audit engagement," "audit client," and "audit report" apply equally to review, review team, review engagement, review client, and review engagement report. (See paragraph 400.2 in the Code)

⁸³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4)

Overarching Principles Relevant to the Provisions of NAS/ Non-audit Services to an Audit Client

98. Under the Code, when a firm is determining whether to provide a NAS to a PIE audit client the firm first considers:
- The laws and regulations in the specific jurisdiction relating to the provision of NAS.⁸⁴
 - Whether the provision will result in the firm assuming management responsibility.⁸⁵
 - Whether the provision of that service might create a self-review threat in relation to the audit of the financial statements on which the firm will express an opinion.⁸⁶
 - Whether any other threats identified (self-interest, familiarity, advocacy and/or intimidation) are at an acceptable level.⁸⁷
99. The SEC's approach with respect to services provided by auditors is largely founded on the core principles presented in paragraph 17-19, violations of which would impair the auditor's independence.

Commentary

100. The Code and the SEC rules are based on the application of the fundamental principles/overarching principles to the provision of NAS/ non-audit services to audit clients. Those principles are required to be complied with when firms provide services that are not mentioned specifically in the respective standards to audit clients.
101. As the Code is applicable at a global level and its application is subject to the national laws and regulations in each jurisdiction, the Code also requires consideration of whether national laws and regulations differ from or go beyond the Code's provisions.

Management responsibility

102. The approaches taken to the assumption of management responsibility in the Code and the SEC rules are considered in paragraph 38 above.

Prohibition on Self-review

103. Under both frameworks, the risk of the auditor being placed in a position of auditing his/her own work is a key consideration when determining whether an auditor can provide a specific service to an audit client.⁸⁸
104. The 2021 NAS-related revisions to the Code introduced a new, overarching requirement in the IIS that prohibits audit firms from providing a NAS to a PIE audit client if the provision of that service might create a self-review threat in relation to the audit of the financial statements on which the firm will express an opinion.
105. The use of "*might create*" in the Code's provision means that the provision of a NAS is prohibited once a firm identifies a risk that a self-review threat might be created – as opposed to where that firm concludes that a self-review threat will in fact be created - and is intended to reduce the risk that a firm might incorrectly conclude (a) that a proposed NAS will not create a self-review threat,

⁸⁴ Revised paragraph 600.6 A1 of the Code

⁸⁵ Revised paragraph 600.7 A1 of the Code

⁸⁶ Revised paragraph R600.8 of the Code

⁸⁷ Revised paragraph R600.14 of the Code

⁸⁸ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 Introductory note

or (b) that the outcome of the proposed NAS will not be subject to audit procedures, thereby circumventing the prohibition.

106. The Code does not include any specific prohibitions that apply where a firm provides assurance services to an audit client. The Code requires the firm to apply the conceptual framework and determine whether the self-review threat, and any other threats, created by the provision of the proposed assurance service to the audit client are at an acceptable level, and if not, to address such threats.
107. In line with the overarching principles, the SEC rules contain an absolute prohibition against accountants providing services to an audit client if that service places them in the position of auditing their own work.

Commentary

108. In practice, the approach of the two frameworks is the same. Under the IESBA Code any situation where a self-review threat might exist is prohibited for PIE audit clients. For entities subject to the SEC rules there is a fundamental principle that an auditor cannot be in a position (or be perceived to be in a position) of auditing his/her own work.

The Risk of Self-review Arising from the Provision of Advice and Recommendations

109. The Code acknowledges that provision of advice and recommendations, whether as a separate engagement or in the course of providing a specific NAS, might create a self-review threat and, as a general rule, prohibits the provision of advice and recommendations to a PIE audit client that might create a self-review threat.
110. As an exception to the application of the self-review threat prohibition, the Code allows the provision of advice and recommendations that might create a self-review threat if such NAS arise out of the normal course of an audit, provided that the other conditions in paragraph 62 above are complied with (i.e., it is not prohibited under local laws and regulations, does not involve the assumption of a management responsibility, and does not result in other threats to independence being at higher than an acceptable level).⁸⁹
111. The SEC's Rule 2-01 does not address the provision of advice and recommendations which could create a situation where an auditor might audit his or her own work or whether it would be permissible if it arose out of the normal course of an audit.
112. However, in addition to assessing the appropriateness of the service having regard to the general principles, the firm would be expected to consider all available SEC guidance (see paragraph 63 above). That would include, for example, an SEC release that recognizes that "obtaining an understanding of, assessing effectiveness of, and *recommending improvements* to the internal accounting and risk management controls is fundamental to the *audit process* and does not impair the accountant's independence"⁹⁰ (emphasis added).

Commentary

113. As an exception to the general self-review prohibition, the Code permits the provision of advice and recommendations arising out of the normal course of an audit. Although the SEC rules do not address this issue, SEC guidance and releases include examples of specific situations where providing advice and recommendation to an audit client does not impair the firm's independence.

⁸⁹ Revised paragraph R600.17 of the Code

⁹⁰ Release No. 33-8183 (January 28, 2003), *Strengthening the Commission's Requirements Regarding Auditor Independence*, Section II B 5.

Provision of Non-Assurance Services/ Non-Audit Services Involving Other Threats

114. Although the Code and the SEC rules have a similar approach in relation to the provision of NAS/non-audit services to an audit client, the Code does not include general prohibitions on the provision of services that would create threats other than a self-review threat. Accordingly, in the case of NAS that would give rise to other threats, the framework of the SEC rules could be more restrictive, as described in paragraph 31-32.

Advocating for an Audit Client

115. In 2021 IESBA introduced provisions prohibiting certain NAS that would create an advocacy threat but would not be prohibited on the basis that they give rise to a self-review threat, such as acting as an expert witness. In the case of PIE audit clients, the IESBA's view⁹¹ is that the introduction of the self-review threat prohibition and the additional restrictions on the provision of NAS that might create an advocacy threat will reduce the types of NAS in respect of which a firm may be permitted to apply safeguards to reduce threats to independence to an acceptable level.

Consideration of Materiality

116. Following the 2021 amendments to the NAS provisions of the Code, prohibitions on the provision of a NAS to a PIE audit client, including the “self-review threat” prohibition, apply regardless of the materiality of the outcome or results of the NAS on the financial statements on which the firm will express an opinion.⁹²

117. The SEC rules take the same approach to the relevance of materiality. In its response to a frequently asked question (FAQ) the SEC Staff stated that “*materiality is not a basis upon which to overcome the presumption in making a determination that “it is reasonable to conclude that the results of the services will not be subject to audit procedures.”*”⁹³

Provision of Services to Certain Related Entities

118. Under the Code,⁹⁴ a firm or a network firm may provide a NAS that would otherwise be prohibited to the following related entities of an audit client provided that specified conditions are satisfied, including in particular, that the NAS do not create a self-review threat is created:

- (a) An entity that has direct or indirect control over the client (i.e., parent entity);
- (b) An entity with a direct financial interest in the client if that entity has significant influence over the client and the interest in the client is material to such entity; or
- (c) An entity which is under common control with the client (i.e., a sister entity).

119. The SEC rules provide that the provision of “five specific services” (bookkeeping, internal audit outsourcing, valuation services, actuarial services, financial information system design and implementation) causes the auditor to lack independence, “*unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements*” (the “not subject to audit” exception).⁹⁵

⁹¹ [Basis for Conclusions, Revisions to Non-Assurance Service Provisions in the Code](#)

⁹² Revised paragraph 600.10 A2 of the Code

⁹³ Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence – Frequently Asked Questions, E - Non-audit Services [Question 3](#)

⁹⁴ See revised paragraph R600.26 of the Code.

⁹⁵ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (i) – (v)

120. The SEC and PCAOB rules do not explicitly exclude certain affiliates of audit clients from the scope of the restrictions of the provision of non-audit services to an audit client.⁹⁶ However, the SEC has recognized that an example of a situation where it would be reasonable to conclude that the results of a specific service would not be subject to audit procedures would be where an accounting firm provides a prohibited service to an affiliate of the audit client, but the accounting firm is not the auditor of the entity or entities that control the accounting firm's audit client or its affiliate.⁹⁷
121. Further, as part of an FAQ, the SEC Staff⁹⁸ noted that if separate entities under common control have autonomous financial and business operations, and the audit firm audits one of the entities, that audit firm might be able to apply the “not subject to audit” exception to entities that it does not audit. In that context, the SEC staff has not objected to the “not subject to audit” exception being applied in a private equity group context under similar circumstances. However, the SEC Staff added that the “not subject to audit” exception might not apply in other contexts, such as a traditional corporate entity or an investment company complex, depending on the particular facts and circumstances.
122. As the “not subject to audit” exception applies only to the “five specific services” listed in paragraph 85, the other non-audit services specifically addressed in the SEC⁹⁹ and PCAOB rules¹⁰⁰ - legal services, expert services unrelated to audit, management functions, corporate finance services, HR services and tax services – may not be provided to the affiliates of an audit client.

Commentary

123. Both frameworks provide an exception under its NAS/non-audit services prohibitions if the result of the service provided to certain related entities/affiliates will not be subject to audit procedures during an audit of the client's financial statements (and requirements regarding the other overarching principles are met). However, while the Code sets out the same exception to all prohibited NAS, the “not subject to audit exception” is applicable only to “five specific prohibited services” under the SEC framework.

VI. Provision Addressing Specific Non-Assurance/ Non-audit Services

Accounting and Bookkeeping Services

Overall approach

124. Both the Code and the SEC rules generally prohibit the provision of accounting and bookkeeping services by a firm to an audit client. Those prohibitions are based on the fact that provision of such services would place the firm in a position of auditing its own work and, if the service involved the preparation and fair presentation of the financial statements, the firm would be assuming

⁹⁶ PCAOB rules generally do not explicitly exclude affiliates of audit clients from the scope of the restrictions of the provision of non-audit services to an audit client (or its personnel) either. See PCAOB rule 3523 that includes exceptions based on materiality and if service is provided to an affiliate of audit client that is audited by another firm.

⁹⁷ Release No. 33-8183 (January 28, 2003), *Strengthening the Commission's Requirements Regarding Auditor Independence*, Footnote 51

⁹⁸ Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence – Frequently Asked Questions, E. Non-Audit Service [Question 5](#)

⁹⁹ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (vi) – (X)

¹⁰⁰ PCAOB Rules 3522 and 3523

management responsibility. In either case, the provision of the service would impair the auditor's independence.

Exception to Prepare Statutory Financial Statements for a Related Entity/Affiliate

125. As an exception to the general prohibition, the Code allows a firm to prepare the statutory financial statements for controlled related entities of an audit client where a local regulator requires the issuance of financial statements that are prepared in accordance with the applicable local legislation or regulation¹⁰¹ provided that:
- The audit report on the group financial statements of the public interest entity has been issued;
 - The firm does not assume management responsibility and applies the conceptual framework to identify, evaluate and address threats to independence;
 - The firm does not prepare the accounting records underlying the statutory financial statements of the related entity and those financial statements are based on client approved information; and
 - The statutory financial statements of the related entity will not form the basis of future group financial statements of that public interest entity.¹⁰²
126. The SEC adopts a similar approach where accountants are asked to prepare statutory financial statements for foreign companies provided those financial statements are not filed with the Commission¹⁰³. The SEC's release stated¹⁰⁴ that "an accountant's independence would be impaired where the accountant prepared the statutory financial statements if those statements form the basis of the financial statements that are filed with us. Under these circumstances, an accountant or accounting firm who has prepared the statutory financial statements of an audit client is put in the position of auditing its own work when auditing the resultant U.S. GAAP financial statements."

Valuation Services

127. Valuation services in the Code are defined as services that involve making assumptions with regard to future developments, the application of appropriate methodologies and techniques and the combination of both to compute a certain value, or range of values, for an asset, a liability or for the whole or part of an entity.¹⁰⁵
128. The Code¹⁰⁶ prohibits valuation services that might create self-review threat. However, if a valuation service does not create a self-review threat but might create an advocacy threat, a firm may provide the service to an audit client, provided that safeguards are applied to reduce the

¹⁰¹ Preparation of such statutory financial statements would not constitute the assumption of management responsibility because the firm would be required to use client-approved and client-prepared accounting records in preparing those statutory financial statements

¹⁰² Revised paragraph R601.7 of the Code

¹⁰³ SEC Release No. 33-8183 (January 28, 2003), *Strengthening the Commission's Requirements Regarding Auditor Independence*, Section II B 1.

¹⁰⁴ SEC Release No. 33-8183 (January 28, 2003), *Strengthening the Commission's Requirements Regarding Auditor Independence*, Section II B 1.

¹⁰⁵ Revised paragraph 603.2 A1 of the Code

¹⁰⁶ Revised paragraph 603.5 of the Code

advocacy threat to an acceptable level and other applicable provisions in the Code are complied with.

129. The SEC prohibits the provision of the following valuation-related services to an audit client:
- Any appraisal service, valuation service, or any service involving a fairness opinion or contribution-in-kind report for an audit client, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements.¹⁰⁷
 - Any actuarially-oriented advisory service involving the determination of amounts recorded in the financial statements and related accounts for the audit client other than assisting a client in understanding the methods, models, assumptions, and inputs used in computing an amount unless it is reasonable to conclude that the results of such services will not be subject to audit procedures during an audit of the audit client's financial statements.¹⁰⁸
130. Appraisal and valuation services include any process that involves valuing assets, both tangible and intangible, or liabilities – such as in-process research and development, financial instruments, assets and liabilities acquired in a merger, and real estate. Fairness opinions and contribution-in-kind reports are opinions and reports in which the firm provides its opinion on the adequacy of consideration in a transaction.¹⁰⁹
131. Valuation services to assist an audit client with tax reporting obligations or for tax planning purposes where the results of the valuation have no effect on the accounting records or the financial statements is considered in paragraphs 121 to 124 below.

Commentary

132. The objectives of the prohibitions in the Code and in the SEC rules appear to be the same, namely, to prohibit a firm from undertaking a valuation procedure, the outcome of which will affect the accounting records or the financial statements on which the firm will express an opinion and thereby result in the firm auditing its own work.
133. In relation to valuation services that give rise to advocacy threat – despite the conceptually different approaches described in paragraphs 31-32 – the Code's "self-review threat prohibition" significantly limits the types of valuation services which a firm may provide, with the application of safeguards to reduce any threats to independence. Consequently, the outcome under the Code is not substantively different from that under the SEC rules.

Administrative Services

134. The Code permits the provision of administrative services that involve firms assisting audit clients with routine or mechanical tasks within the normal course of operations unless a self-review threat might be created.¹¹⁰ The Code's approach is based on the fact that the definition of administrative

¹⁰⁷ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (iii)

¹⁰⁸ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01(c) (4) (iv)

¹⁰⁹ SEC Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 3.

¹¹⁰ Revised paragraph 602.2 A2 provides the following examples of administrative services:

- Word processing or document formatting.
- Preparing administrative or statutory forms for client approval.
- Submitting such forms as instructed by the client.
- Monitoring statutory filing dates and advising an audit client of those dates.

services requires the services to be clerical in nature and to require little to no professional judgment.¹¹¹

135. The SEC and PCAOB rules do not address the provision of administrative services to an audit client. However, the SEC rules prohibit a firm from acting as an employee of an audit client (see paragraph 38). The firm would therefore need to be satisfied that the provision of the administrative services would not place the firm in a position of acting as an employee of its audit client.

Tax Services

General

136. Tax gives rise to a broad range of services that are often interrelated in practice and might be combined with other types of services, such as corporate finance services, provided by a firm to an audit client. In accordance with this breadth, the Code does not define “tax services”¹¹² and does not contain any general provisions addressing the prohibition or permissibility of providing tax services to an audit client. Consequently, following the approach in the conceptual framework, if a tax service is not explicitly prohibited by the Code, a firm is permitted to deliver that service, provided that the general requirements of the Code are complied with.
137. The Code does, however, explicitly prohibit the provision of the following tax services by a firm to a PIE audit client:
- Calculations of current/deferred taxes for the purpose of preparing accounting entries that support such balances
 - Tax advice that depends on a particular accounting treatment/financial statement presentation with respect to which there is reasonable doubt as to its appropriateness,
 - Acting as an advocate before a tribunal or court to resolve a tax matter,
 - Valuation for tax purposes if it might create a self-review threat,
 - Tax advisory and tax planning services if it might create a self-review threat, and
 - Assistance in the resolution of tax disputes if it might create a self-review threat.
138. The SEC rules are silent in relation to the provision of tax services. However, an SEC release explains that: “the Commission reiterates its long-standing position that an accounting firm can provide tax services to its audit clients without impairing the firm's independence. Accordingly, accountants may continue to provide tax services such as tax compliance, tax planning, and tax advice to audit clients, subject to the normal audit committee pre-approval requirements under 2-01(c)(7)”. The SEC’s release also adds that: “nevertheless, merely labeling a service as a “tax service” will not necessarily eliminate its potential to impair independence under Rule 2-01(b). Audit committees and accountants should understand that providing certain tax services to an audit client would, as described below, or could, in certain circumstances, impair the independence of the accountant.”¹¹³

¹¹¹ Revised paragraph 602.2 A1 of the Code

¹¹² Revised paragraph 604.2 A1 of the Code

¹¹³ SEC Release No. 33-8183 (January 28, 2003), *Strengthening the Commission's Requirements Regarding Auditor Independence*, Section II B 11.¹¹⁴ PCAOB Rule 3522. Tax Transactions. These rules apply to audits of issuers and broker-dealers.

139. The PCAOB has developed standards addressing the provision of tax services to audit clients which supplement the application of the SEC's general independence standards. PCAOB Rules 3522¹¹⁴ and 3523¹¹⁵ are designed to address potential ethics and independence problems posed by firms' involvement in two areas
- Advice on tax positions that might be abusive (confidential transactions and aggressive tax position transactions), and
 - Tax compliance and planning services for certain senior officers, i.e., those in a financial reporting oversight role.¹¹⁶

Aggressive Tax Positions and Confidential Transactions

140. The 2021 NAS-related revisions to the Code prohibit firms from providing a tax service or recommending a transaction to an audit client if the service or transaction relates to marketing, planning, or opining in favor of a tax treatment that was initially recommended, directly or indirectly, by the firm or network firm, and a significant purpose of the tax treatment or transaction is tax avoidance unless the firm is confident that the proposed treatment has a basis in applicable tax law or regulation that is likely to prevail.¹¹⁷
141. PCAOB Rule 3522¹¹⁸ provides that “the registered public accounting firm is not independent of its audit client if the firm, or any affiliate of the firm, during the audit and professional engagement period, provides any non-audit service to the audit client related to marketing, planning, or opining in favor of the tax treatment of, a transaction -
- Confidential Transactions¹¹⁹ - that is a confidential transaction; or
 - Aggressive Tax Position Transactions - that was initially recommended, directly or indirectly, by the registered public accounting firm and a significant purpose of which is tax avoidance, unless the proposed tax treatment is at least more likely than not to be allowable under applicable tax laws”.

Commentary

142. Whilst both frameworks prohibit the provision of aggressive tax advice and transactions¹²⁰, the Code does not include a prohibition on the provision of a confidential transaction to an audit client.

Specific Tax Services Provided to an Audit Client

Tax Return Preparation

¹¹⁴ PCAOB Rule 3522. Tax Transactions. These rules apply to audits of issuers and broker-dealers.

¹¹⁵ PCAOB Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles. These rules apply to audits of issuers.

¹¹⁶ To the extent that auditors' provision of other tax services is consistent with the SEC's independence requirements, the PCAOB rules would not prohibit accounting firms from providing those services to their audit clients, subject to the SEC's requirements and PCAOB Rule 3524 relating to audit committee pre-approval of such services

¹¹⁷ Revised paragraph R604.4 of the Code

¹¹⁸ PCAOB Rule 3522. Tax Transactions

¹¹⁹ Based on PCAOB Rule 3501 (c)(i) (1), a “confidential transaction” is a transaction that is offered to a taxpayer under conditions of confidentiality and for which the taxpayer has paid an advisor a fee.

¹²⁰ Note: the IESBA's prohibition is applicable to all audit clients, not only to PIEs or listed entities.

143. Provided that the general provisions of the Code applicable to services provided to PIE audit clients are met, including the “self-review threat prohibition”, the Code does not prohibit the provision of tax return preparation services to an audit client because:
- Tax return preparation services are based on historical information and principally involve analysis and presentation of such historical information under existing tax law, including precedents and established practice; and
 - Tax returns are subject to whatever review or approval process the tax authority considers appropriate.¹²¹
144. The PCAOB’s position¹²² is that “as a general matter, routine tax return preparation and tax compliance services have not raised independence concerns. In the case of most tax compliance services, the auditor does not prepare tax returns until after management has calculated and allocated its tax liability and the auditor has audited the income tax accounts to obtain reasonable assurance that they are fairly stated and are accompanied by appropriate disclosure. Also, in preparing a tax return, the auditor is not acting as an advocate for its client”.

Tax Calculations

145. The Code and the SEC rules do not contain general provisions governing the provision of tax calculations to audit clients.
146. The Code does, however, explicitly prohibit the provision of calculations of current and deferred tax liabilities (or assets) to an audit client for the purpose of preparing accounting entries that support such balances because such calculations create a self-review threat.¹²³

Commentary

147. Whilst the SEC rules do not prohibit a firm from undertaking tax calculations for audit clients, the prohibition on the provision of accounting and bookkeeping services and the application of the SEC’s principle that a firm is prohibited from auditing its own work and acting as management would result in the same outcome as that under the Code.

Tax Advisory and Tax Planning

148. The Code does not contain a general prohibition on the provision of tax advisory or tax planning services to an audit client unless the purpose of the tax advice is tax avoidance (see paragraphs 106 to 108 above).¹²⁴
149. However, the Code prohibits tax advisory and tax planning services:
- That would result in a firm assuming a management responsibility for an audit client.
 - Where the effectiveness of the tax advice depends on a particular accounting treatment or presentation in the financial statements, and the audit team has doubt as to the

¹²¹ Revised paragraph 604.6 A1 of the Code

¹²² PCAOB Release No. 2004-015 (December 14, 2004)

¹²³ Revised paragraphs 604.8 A1 and R604.10 of the Code

¹²⁴ This approach is based on the fact that tax advisory and tax planning services comprise a broad range of services, including advising the audit client how to structure its affairs in a tax-efficient manner or advising on the application of a tax law or regulation (Revised paragraph 604.11 A1 of the Code)

appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework.¹²⁵

- That might create a self-review threat.¹²⁶

150. If provision of the service will not create a self-review threat, but might create an advocacy threat, a firm may provide the service if safeguards can be applied to reduce any advocacy threat to an acceptable level.¹²⁷
151. The PCAOB¹²⁸ has stated that the provision of tax advisory or tax planning services to audit clients would not be prohibited provided that
- a) The audit client makes the decisions relating to, and takes responsibility for, both the tax work and the presentation of tax related accounts and other matters in the financial statements, and
 - b) The firm does not provide non-audit services relating to aggressive tax strategies that are prohibited (see paragraphs 106 to 108 above).

This conclusion was based on research showing that tax planning in connection with routine and even non-routine business transactions initiated by the audit client had not given rise to auditor independence concerns.

152. Although the SEC rules do not contain specific prohibitions in this area, an SEC release¹²⁹ states that “merely labeling a service as a “tax service” will not necessarily eliminate its potential to impair independence under Rule 2-01(b). Audit committees and accountants should understand that providing certain tax services to an audit client would, as described below, or could, in certain circumstances, impair the independence of the accountant.”.

Commentary

153. Unlike the Code, the SEC rules do not allow the application of any safeguards if the provision of tax advisory and tax planning services would place the auditor in an advocacy role. Despite the conceptually different approaches described in paragraphs 31-32, the combination of the “self-review threat prohibition” and the explicit prohibitions on services that create an advocacy threat significantly limit the types of services which a firm may be permitted to provide under the Code by applying safeguards to reduce any threats to independence. Consequently, the outcome under the Code is not substantively different from the outcome under the SEC rules.

Tax services Involving Valuations

154. The provision of tax services which involve valuations can arise in a range of circumstances, including (i) merger and acquisition transactions, (ii) group restructurings and corporate reorganizations, (iii) transfer pricing studies, and (iv) stock-based compensation arrangements.¹³⁰ Such services might create a self-review threat and an advocacy threat.¹³¹

¹²⁵ Revised paragraph R604.13 of the Code

¹²⁶ Revised paragraph R604.15 of the Code

¹²⁷ Revised paragraph 604.15 A1 of the Code

¹²⁸ PCAOB Release No. 2004-015 (December 14, 2004)

¹²⁹ SEC Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 11.

¹³⁰ Revised paragraph 604.16 A1 of the Code

¹³¹ Revised paragraph 604.17 A1 of the Code

155. The Code prohibits the provision of tax services involving valuations to an audit client if they might create a self-review threat.¹³² No such prohibition exists if such services create only an advocacy threat; the Code permits a firm to apply safeguards, if available, to reduce the advocacy threat to an acceptable level.¹³³
156. The SEC's release states¹³⁴ that the "rules do not prohibit an accounting firm from providing such services [*appraisal or valuation services, fairness opinions, or contribution-in-kind reports*] for non-financial reporting (e.g., transfer pricing studies, cost segregation studies, and other tax-only valuations) purpose."

Commentary

157. The provision of the tax services involving valuations to an audit client when such service might create a self-review threat is explicitly prohibited under the Code. The SEC rules do not prohibit tax services that involve valuations. However, before providing such a service, the auditor is required to consider the general independence standards and principles. If a firm concludes that a service would result in the firm auditing its own work, it would not be permissible under the SEC rules. In the case of services that give rise only to advocacy threats please refer to paragraph 99.

Assistance in the Resolution of Tax Disputes

158. A firm might be asked to assist an audit client in the resolution of a tax dispute, for example, where a tax authority has notified an audit client that arguments on a particular issue have been rejected and the tax authority or the client refers the matter for determination in a formal proceeding before a tribunal or court.¹³⁵
159. Under the Code, a firm is prohibited from assisting an audit client in the resolution of tax disputes if the provision of that assistance might create a self-review threat.¹³⁶ No such prohibition exists if such services create only an advocacy threat; the Code permits a firm to apply safeguards, if available, to reduce the advocacy threat to an acceptable level.¹³⁷
160. The Code specifically prohibits a firm from acting for a PIE audit client as an advocate before a tribunal or court.¹³⁸ However, a firm may act in an advisory role in relation to the matter that is being heard before a tribunal or court by, for example, responding to specific requests for information, providing factual accounts or testimony about the work performed, or assisting the client in analyzing the tax issues related to the matter.¹³⁹
161. The SEC rules do not include specific prohibitions regarding the provision of assistance in tax disputes. However, the SEC's release¹⁴⁰ sets out that "merely labeling a service as a "tax service" will not necessarily eliminate its potential to impair independence under Rule 2-01(b). Audit committees and accountants should understand that providing certain tax services to an audit

¹³² Revised paragraph R604.19 of the Code

¹³³ Revised paragraph 604.19 A1 of the Code

¹³⁴ SEC Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 3.

¹³⁵ Revised paragraph 604.20 A1 of the Code

¹³⁶ Revised paragraph R604.24 of the Code

¹³⁷ Revised paragraph 604.24 A1 of the Code

¹³⁸ Revised paragraph R604.26 of the Code

¹³⁹ Revised paragraph 604.27 A1 of the Code

¹⁴⁰ SEC Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 11

client would, as described below, or could, in certain circumstances, impair the independence of the accountant. Specifically, accountants would impair their independence by representing an audit client before a tax court, district court, or federal court of claims.”

Commentary

162. Both the Code and the SEC rules prohibit firms from representing an audit client in tax matters before a tribunal or court. However, unlike the Code, the SEC rules do not allow firms to act in an advisory role in relation to a tax matter that is being heard before a tribunal or court.

Tax Services for Persons in Financial Reporting Oversight Roles

163. PCAOB Rule 3523¹⁴¹ prohibits a firm, with limited exceptions¹⁴², from providing a tax service to a person in a financial reporting oversight role at an issuer audit client, or an immediate family member of such person. The PCAOB Rule addresses concern that performing tax services for certain individuals involved in the financial reporting processes of an audit client creates an appearance of a mutual interest between the auditor and those individuals.¹⁴³

Commentary

164. The Code does not include an equivalent provision. However, based on the application of the conceptual framework a firm would be expected to consider whether the provision of tax services to a person in a financial reporting oversight role at an audit client might give rise to a familiarity threat or compromise the firm’s judgment.

Internal Audit Services

165. The provision of internal audit services to an audit client might

- result in a firm (or network firm) assuming a management responsibility (see paragraph 38). The Code provides examples of internal audit activities that are prohibited because they would result in a firm assuming management responsibility.¹⁴⁴
- create a self-review threat in relation to the audit of the financial statements on which the firm will express an opinion.¹⁴⁵ The Code prohibits firms from providing internal audit services to

¹⁴¹ PCAOB Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

¹⁴² The PCAOB rule is not applicable to a person in a financial reporting role if:

- a) the person is in a financial reporting oversight role at the issuer audit client only because he or she serves as a member of the board of directors or similar management or governing body of the audit client;
- b) the person is in a financial reporting oversight role at the issuer audit client only because of the person’s relationship to an affiliate of the entity being audited
 - (1) whose financial statements are not material to the consolidated financial statements of the entity being audited; or
 - (2) whose financial statements are audited by an auditor other than the firm or an associated person of the firm; or
- c) the person was not in a financial reporting oversight role at the issuer audit client before a hiring, promotion, or other change in employment event and the tax services are
 - (1) provided pursuant to an engagement in process before the hiring, promotion, or other change in employment event; and
 - (2) completed on or before 180 days after the hiring or promotion event.

¹⁴³ PCAOB Release No. 2005-014 July 26, 2005

¹⁴⁴ Revised 605.3 A2 of the Code

¹⁴⁵ Revised 605.4 A1 of the Code

a PIE audit client if the provision of such services might create a self-review threat.¹⁴⁶

As internal audit services might involve matters that are operational in nature, they do not necessarily relate to matters that will be subject to consideration in relation to the audit of the financial statements and therefore create a self-review threat.¹⁴⁷

166. However, the Code includes examples of services that would create a self-review threat, namely services that relate to (i) the internal controls over financial reporting, (ii) financial accounting systems that generate information for the client's accounting records or financial statements on which the firm will express an opinion, or (iii) amounts or disclosures that relate to the financial statements on which the firm will express an opinion.¹⁴⁸
167. Similar to the Code's approach, the SEC rules prohibit providing any internal audit services outsourced by an audit client that relates to the audit client's internal accounting controls, financial systems, or financial statements, for an audit client, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements.¹⁴⁹
168. Both the Code¹⁵⁰ and the SEC's releases¹⁵¹ recognize that firms should be able to provide advice and recommendations in relation to matters that they identify in the course of an audit relating to the audit client's internal controls (see also paragraphs 76 to 80).

Commentary

169. Overall, the frameworks of the Code and the SEC intend to prohibit the provisions of the same type of internal audit services to an audit client.

Information Technology (IT) System Services

170. The provision of IT system services to an audit client might (i) result in a firm assuming management responsibility or (ii) create a self-review threat if there is a risk that the results of the services will affect the audit of the financial statements on which the firm will express an opinion.¹⁵²

¹⁴⁶ Revised R605.6 of the Code

¹⁴⁷ Revised 605.2 A2 of the Code

¹⁴⁸ Revised 605.6 A1 of the Code

¹⁴⁹ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (v)

¹⁵⁰ Revised R600.17 of the Code

¹⁵¹ Despite the above-mentioned prohibition, the SEC's release includes that "during the conduct of the audit in accordance with generally accepted auditing standards ("GAAS") or when providing attest services related to internal controls, the auditor evaluates the company's internal controls and, as a result, may make recommendations for improvements to the controls. Doing so is a part of the accountant's responsibilities under GAAS or applicable attestation standards and, therefore, does not constitute an internal audit outsourcing engagement" Furthermore, the SEC's release added that "along those lines, this prohibition on "outsourcing" does not preclude engaging the accountant to perform nonrecurring evaluations of discrete items or other programs that are not in substance the outsourcing of the internal audit function. For example, the company may engage the accountant, subject to the audit committee pre-approval requirements, to conduct "agreed-upon procedures" engagements related to the company's internal controls, since management takes responsibility for the scope and assertions in those engagements. The prohibition also does not preclude the accountant from performing operational internal audits unrelated to the internal accounting controls, financial systems, or financial statements. (No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 5)

¹⁵² Revised 606.4 A1 of the Code

171. The Code prohibits the provision of IT systems services to a PIE audit client if those services might create a self-review threat.¹⁵³ Examples of services that might create a self-review threat include those involving designing or implementing IT systems that:
- a) Form part of the internal control over financial reporting; or
 - b) Generate information for the client's accounting records or financial statements on which the firm will express an opinion.¹⁵⁴
172. Similarly, in its 2003 Adopting Release, the SEC stated that “designing, implementing, or operating systems affecting the financial statements may place the accountant in a management role, or result in the accountant auditing his or her own work or attesting to the effectiveness of internal control systems designed or implemented by that accountant”.¹⁵⁵
173. Consequently, the SEC rules prohibit a firm from providing “any service [*related to the financial information systems design and implementation*] unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client's financial statements, including:
- (A) Directly or indirectly operating, or supervising the operation of, the audit client's information system or managing the audit client's local area network; or
 - (B) Designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant to the audit client's financial statements or other financial information systems taken as a whole”.¹⁵⁶
174. Like the Code, the SEC's release also stated that “such rules do not preclude an accounting firm from working on hardware or software systems that are unrelated to the audit client's financial statements or accounting records as long as those services are pre-approved by the audit committee”.¹⁵⁷
175. The SEC's release further stated that “this prohibition does not preclude the accountant from evaluating the internal controls of a system as it is being designed, implemented or operated either as part of an audit or attest service and making recommendations to management. Likewise, the accountant would not be precluded from making recommendations on internal control matters to management or other service providers in conjunction with the design and installation of a system by another service provider”.¹⁵⁸
176. The SEC's release is, therefore, in line with the Code's approach of not prohibiting the provision of advice and recommendations that arise out of the normal course of an audit as described in paragraph 75 above.

Commentary

177. Overall, the Code and the SEC address the same concerns in substantially the same manner.

¹⁵³ Revised R606.6 of the Code

¹⁵⁴ Revised 606.6 A1 of the Code

¹⁵⁵ Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 2

¹⁵⁶ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (ii)

¹⁵⁷ Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 2

¹⁵⁸ Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 2

Litigation Support Services

178. Litigation support services include, for example, (i) assisting with document management and retrieval; (ii) acting as a witness, including an expert witness; (iii) calculating estimated damages or other amounts that might become receivable or payable as the result of litigation or other legal dispute; or (iv) forensic or investigative services.¹⁵⁹
179. Providing litigation support services to an audit client might create a self-review threat or an advocacy threat. The Code prohibits the provision of litigation support services to a PIE audit client if it might create a self-review threat¹⁶⁰. The provision of advice in connection with a legal proceeding the outcome of which might affect the quantification of a provision or other amount in the financial statements on which the firm will express an opinion is an example of a service that creates a self-review threat.¹⁶¹
180. Litigation support services might also create advocacy threats. The Code does not explicitly prohibit the provision of litigation services that might create an advocacy threat – other than acting as an expert witness - provided that the firm ensures that the level of such threat is at an acceptable level.¹⁶²
181. The Code addresses the position where a firm, or an individual within a firm, acts as a witness for an audit client. The Code distinguishes between giving evidence to a tribunal or court as a witness of fact or as an expert witness.¹⁶³
182. Under the Code¹⁶⁴, a firm is permitted to act for an audit client as an expert witness, if it is:
- (a) Appointed by a tribunal or court to act as an expert witness in a matter involving a client; or
 - (b) Engaged to advise or act as an expert witness in relation to a class action (or an equivalent group representative action) provided that:
 - (i) The firm's audit clients constitute less than 20% of the members of the class or group (in number and in value);
 - (ii) No audit client is designated to lead the class or group; and
 - (iii) No audit client is authorized by the class or group to determine the nature and scope of the services to be provided by the firm or the terms on which such services are to be provided.
183. The SEC rules prohibit the provision of an expert opinion or other expert service for an audit client, for the purpose of advocating an audit client's interests in litigation or in a regulatory or administrative proceeding or investigation. A firm is also prohibited from providing such services to an audit client's legal representative.¹⁶⁵ An SEC's release explains¹⁶⁶ that although all services provided by an accountant might be perceived to be expert services, this prohibition only applies to services that involve advocacy in proceedings and investigations and does not apply to other permitted non-audit services, such as tax services.

¹⁵⁹ Revised 607.2 A1 of the Code

¹⁶⁰ Revised R607.6 of the Code

¹⁶¹ Revised 607.6 A1 of the Code

¹⁶² Revised 607.6 A2 of the Code

¹⁶³ Revised 607.7 A1 of the Code

¹⁶⁴ Revised 607.7 A3 and R607.9 of the Code

¹⁶⁵ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (x)

¹⁶⁶ Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Footnote 97;

184. Like the Code, the SEC rules make it clear that a firm's independence is not impaired if a firm provides factual accounts, including in testimony, of work performed or explains the positions taken or conclusions reached during the performance of any permitted service provided by the accountant for the audit client.¹⁶⁷ However, the SEC rules do not provide an exception if the witness is appointed by the court or engaged in relation to a class action, as in the case of the Code.
185. An SEC's release also stated that the SEC rules "do not preclude an audit committee or, at its direction, its legal counsel, from engaging the firm to perform internal investigations or fact-finding engagements. These types of engagements might include, among others, forensic or other fact-finding work that results in the issuance of a report to the audit client".¹⁶⁸

Commentary

186. The SEC's restrictions in relation to litigation support services are broader than the Code's prohibitions as they
- prohibit the provision of any kind of expert services for the purpose of advocating an audit client's interest.¹⁶⁹
 - do not permit the provision of litigation services to affiliates of an audit client. In contrast, the Code allows the provision of prohibited litigation support services to related entities provided certain conditions are met (see paragraph 88 above).

Legal Services

187. Legal services are defined in the Code as those services for which the individual providing the services must either:
- Have the required legal training to practice law; or
 - Be admitted to practice law before the courts of the jurisdiction in which such services are to be provided.¹⁷⁰
188. The Code does not contain a general prohibition on the provision of legal services to an audit client. In the case of PIE audit clients, the Code prohibits:
- Provision of legal advice if it might create a self-review threat.¹⁷¹
 - A partner or employee of the firm or the network firm serving as General Counsel of an audit client¹⁷²

¹⁶⁷ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (x)

¹⁶⁸ Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II. B 10

¹⁶⁹ In situations involving advocacy, the provision of expert services by the accountant makes the accountant part of the "team" that has been assembled to advance or defend the client's interests. The appearance of advocacy created by providing such expert services is sufficient to deem the accountant's independence impaired. The prohibition on providing "expert" services included in this rule covers engagements that are intended to result in the accounting firm's specialized knowledge, experience and expertise being used to support the audit client's positions in various adversarial proceedings. (Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II. B 10)

¹⁷⁰ Revised 608.2 A1 of the Code

¹⁷¹ Revised R608.7 of the Code

¹⁷² Revised R608.9 of the Code

- Acting in an advocacy role for an audit client in resolving a dispute or litigation before a tribunal or court¹⁷³

189. The SEC rules prohibit the provision of any service to an audit client that, under circumstances in which the service is provided, could be provided only by someone licensed, admitted, or otherwise qualified to practice law in the jurisdiction in which the service is provided.^{174,175}

Commentary

190. The Code focuses only on specific types of legal services and does not establish a general prohibition on the provision of legal services by firms to their audit clients. The Code also permits the provision of prohibited legal services to related entities of an audit client provided that certain conditions are met (see paragraph 88 above).

191. By contrast, the SEC rules prohibit the provision of legal services to an audit client or to any affiliate of that audit client.

Recruiting Services

192. The provision of recruiting services to an audit client (i) might result in a firm assuming management responsibility and (ii) might create a self-interest, familiarity or intimidation threat.¹⁷⁶

193. The Code restricts firms from providing the following recruiting services to an audit client:

- Acting as a negotiator on the client's behalf, and¹⁷⁷
- Services that relate to:¹⁷⁸
 - (a) Searching for or seeking out candidates;
 - (b) Undertaking reference checks of prospective candidates;
 - (c) Recommending the person to be appointed; or
 - (d) Advising on the terms of employment, remuneration or related benefits of a particular candidate,

with respect to the following positions:

- (i) A director or officer of the entity; or
- (ii) A member of senior management in a position to exert significant influence over the preparation of the client's accounting records or the financial statements on which the firm will express an opinion.

¹⁷³ Revised R608.11 of the Code

¹⁷⁴ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (ix)

¹⁷⁵ The SEC stated that: "We believe that a lawyer's core professional obligation is to advance clients' interests. Rules of professional conduct in the U.S. require the lawyer to "represent a client zealously and diligently within the bounds of the law." The lawyer must "take whatever lawful and ethical measures are required to vindicate a client's cause or endeavor. . . . In the exercise of professional judgment, a lawyer should always act in a manner consistent with the best interests of the client." We have long maintained that an individual cannot be both a zealous legal advocate for management or the client company, and maintain the objectivity and impartiality that are necessary for an audit." (Release No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II. B 9)

¹⁷⁶ Revised R609.3 and 609.4 A1 of the Code

¹⁷⁷ Revised R609.5 of the Code

¹⁷⁸ Revised R609.6 of the Code

194. However, the Code acknowledges that provision of the following services to an audit client does not usually create a threat to a firm's independence:
- Reviewing the professional qualifications of a number of applicants and providing advice on their suitability for the position.
 - Interviewing candidates and advising on a candidate's competence for financial accounting, administrative or control positions.
195. The SEC rules prohibit the following human resources services:¹⁷⁹
- Searching for or seeking out prospective candidates for managerial, executive, or director positions;
 - Engaging in psychological testing, or other formal testing or evaluation programs;
 - Undertaking reference checks of prospective candidates for an executive or director position;
 - Acting as a negotiator on the audit client's behalf, such as determining position, status or title, compensation, fringe benefits, or other conditions of employment; or
 - Recommending, or advising the audit client to hire, a specific candidate for a specific job (except that an accounting firm may, upon request by the audit client, interview candidates and advise the audit client on the candidate's competence for financial accounting, administrative, or control positions).¹⁸⁰
196. The SEC's release explains that "assisting management in human resource selection or development places the accountant in the position of having an interest in the success of the employees that the accountant has selected, tested, or evaluated. Accordingly, observers may perceive that an accountant would be reluctant to suggest the possibility that those employees failed to perform their jobs appropriately, or at least reasonable investors might perceive the accountant to be reluctant, because doing so would require the accountant to acknowledge shortcomings in its human resource service. The accountant also might have other incentives not to report such employees' ineffectiveness, including that the accountant would identify and be identified with the recruited employees."¹⁸¹

Commentary

197. The prohibitions regarding recruiting/ human resources services in the SEC rules and in the Code mainly cover the same types of services, with a few minor differences; for example:
- The SEC rules prohibit firms from engaging in psychological testing, or other formal testing or evaluation programs for the audit client. In contrast, these services are not explicitly prohibited under the Code's provisions.
 - While the SEC rules prohibit a firm from recommending or advising an audit client to hire a specific candidate for any kind of job, the equivalent Code prohibition applies only in respect of such services only in relation to the director, officers, or specific members of senior management.

¹⁷⁹ Although the Code's provision construe "recruiting services", while the SEC/PCAOB rules "human resources services", the IESBA Staff is of the view that the determination of these services is the same in the two frameworks.

¹⁸⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (viii)

¹⁸¹ No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 7

Corporate Finance Services

198. The Code provides that the provision of corporate finance services¹⁸² by a firm to an audit client might result in the firm assuming management responsibility, and might create a self-review threat.¹⁸³
199. As a result, the Code prohibits firms from providing to an audit client:
- Corporate finance services that involve promoting, dealing in, or underwriting the shares, debt or other financial instruments issued by the audit client or providing advice on investment in such shares, debt or other financial instruments;¹⁸⁴
 - Advice in relation to corporate finance services where:
 - (a) The effectiveness of such advice depends on a particular accounting treatment or presentation in the financial statements on which the firm will express an opinion; and
 - (b) The audit team has doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework;¹⁸⁵
 - Corporate finance services, if the provision of such services might create a self-review threat.¹⁸⁶
200. Apart from the risk of assuming management responsibility and the self-review threat, the Code also states that the provision of corporate finance services might create an advocacy threat. The Code does not prohibit services that only create an advocacy threat provided that the firm applies safeguards to address such threats.¹⁸⁷
201. The SEC rules address explicitly: (i) broker-dealer, (ii) investment adviser, and (iii) investment banking services, and prohibit firms from:
- Acting as a broker-dealer (registered or unregistered), promoter, or underwriter, on behalf of an audit client,
 - Making investment decisions on behalf of the audit client or otherwise having discretionary authority over an audit client's investments,
 - Executing a transaction to buy or sell an audit client's investment, or
 - Having custody of assets of the audit client, such as taking temporary possession of securities purchased by the audit client.^{188, 189}
202. The SEC's approach is based on a view that "selling – directly or indirectly – an audit client's securities is incompatible with the accountant's responsibility of assuring the public that the company's financial condition is fairly presented. When an accountant, in any capacity, recommends to anyone (including non-audit clients) that they buy or sell the securities of an audit

¹⁸² Revised 610.2 A1 of the Code

¹⁸³ Revised 610.3 A1 of the Code

¹⁸⁴ Revised R610.5 of the Code

¹⁸⁵ Revised R610.6 of the Code

¹⁸⁶ Revised R610.6 of the Code

¹⁸⁷ Revised 610.3 A1 and 610.8 A1 of the Code

¹⁸⁸ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (4) (viii)

¹⁸⁹ PCAOB interim standard, ET Section 101.5 sets out specific group of services such as investment - advisory or management services and corporate finance – consulting or advisory services that would impair the firm's independence. The specific list of services is in line with the SEC's relevant prohibitions, however PCAOB interim standard also includes the situation when the firm commits the client to the terms of a transaction or consummate a transaction on behalf of the client.

client or an affiliate of the audit client, the accountant has an interest in whether those recommendations were correct. That interest could affect the audit of the client whose securities, or whose affiliate's securities, were recommended.”¹⁹⁰

203. Furthermore, “broker-dealers often give advice and recommendations on investments and investment strategies. The value of that advice is measured principally by the performance of a customer's securities portfolio. When the customer is an audit client, the accountant has an interest in the value of the audit client's securities portfolio, even as the accountant must determine whether management has properly valued the portfolio as part of an audit. Thus, the accountant would be placed in a position of auditing his or her own work. Furthermore, the accountant is placed in a position of acting as an advocate on behalf of the client.”¹⁹¹

Commentary

204. Both frameworks prohibit corporate finance services that
- involve promoting, dealing in, or underwriting the shares, debt or other financial instruments issued by the audit client – including acting as a broker-dealer – or providing advice on investment, and
 - services that might create a self-review threat or would put the firm in a position of auditing its own work.
205. In relation to corporate finance services that give rise to an advocacy threat the Code does not include a general prohibition, while the overarching principles in the SEC rules restrict firms from providing any corporate finance services that place the accountant in a position of being an advocate for the audit client, such as responding to requests for information from a counterparty to the transaction or drafting transaction-related documentation. Despite the conceptually different approaches between the two frameworks as described in paragraphs 31-32, the combination of the “self-review threat prohibition” and the explicit prohibitions on certain services that create an advocacy threat limit the types of services which a firm may be permitted to provide under the Code, with the application of safeguards to reduce any threats to independence.
206. In relation to other types of corporate finance services, the Code relies on the application of general principles, while the SEC rules prohibit a number of specific services.¹⁹² For example, the SEC prohibits having custody of assets of the audit client. While the Code does not include such a prohibition, firms have to apply the conceptual framework to determine whether such service is permissible or not under the particular circumstances.

VII. Communication with Those Charged with Governance (TCWG)

Communication of Independence Matters

207. Transparency and auditor communication of independence related matters to TCWG or to the audit committee play an important role in the oversight of the financial reporting process and

¹⁹⁰ No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 8

¹⁹¹ No. 33-8183 (January 28, 2003), Strengthening the Commission's Requirements Regarding Auditor Independence, Section II B 8

¹⁹² Revised 610.2 A1 of the Code

auditor independence under both frameworks. Although, the definition of TCWG in the Code¹⁹³ is broader than the audit committee definition in the SEC¹⁹⁴ and PCAOB¹⁹⁵ rules, for the purposes of this benchmarking initiative which relates only to PIE audit clients, the definitions of TCWG and audit committees are intended to cover the individuals performing the same function.¹⁹⁶

Firm Communications Requirements Under the Code

208. The provisions of the Code in relation to communication with TCWG build on the requirements of the IAASB's International Standard on Auditing 260 (Revised), *Communication with Those Charged with Governance*. ISA 260 (Revised) requires¹⁹⁷ an auditor of a listed entity to confirm to TCWG that the engagement team and others in the firm, as appropriate, the firm and, when applicable, network firms, have complied with relevant ethical requirements regarding independence. In addition, an auditor is required to disclose:

- All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, might reasonably be thought to bear on independence. This includes the total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity;¹⁹⁸ and
- The safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level.

209. When the disclosure is not specifically required by professional standards or laws or regulations, the Code encourages regular communication between a firm and TCWG of all audit clients – including PIEs and non-PIEs - regarding relationships and other matters that might, in the firm's opinion, reasonably bear on independence. Such communication is intended to enable TCWG to:

- (a) Consider the firm's judgments in identifying and evaluating threats;

¹⁹³ Based on the Code's Glossary TCWG are the person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance might include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

¹⁹⁴ Based on SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (f) (17) in the context of his section audit committee defined under 3(a)(58) of the Securities Exchange Act of 1934 (15 U.S.C.8c(a)(58)) as it means:

- (A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer; and
- (B) if no such committee exists with respect to an issuer, the entire board of directors of the issuer.

¹⁹⁵ PCAOB Rule 3501 the term "audit committee" means a committee (or equivalent body) established by and among the board of directors of an entity for the purpose of overseeing the accounting and financial reporting processes of the entity and audits of the financial statements of the entity; if no such committee exists with respect to the entity, the entire board of directors of the entity. For audits of non-issuers, if no such committee or board of directors (or equivalent body) exists with respect to the entity, "audit committee" means the person(s) who oversee(s) the accounting and financial reporting processes of the entity and audits of the financial statements of the entity.

¹⁹⁶ Based on the Code's termination TCWG also include organizations or persons overseeing the strategic directions related to accountability and not only the processes themselves.

¹⁹⁷ Paragraph 17 (a) of ISA 260

¹⁹⁸ These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor

- (b) Consider how threats have been addressed, including the appropriateness of safeguards when they are available and capable of being applied; and
- (c) Take appropriate action.

210. The revised NAS and fee-related provisions revisions to the Code have introduced more detailed and specific requirements¹⁹⁹ regarding auditor communication with TCWG about NAS and fee-related matters. The main purpose of the enhanced provisions is to provide a basis for a meaningful, two-way discussion with TCWG about NAS and fee-related matters, which will assist TCWG in assessing the firm's independence.

Firm Communications Requirements Under the PCAOB Standards

211. The PCAOB rules²⁰⁰ requires a firm to confirm to the audit committee annually in writing that, as of the date of the communication, it is independent in compliance with PCAOB rule 3520²⁰¹. In addition, prior to accepting an initial engagement and at least annually, a firm is required to
- Describe in writing, to the audit committee, all relationships between the firm or any affiliates of the firm and the audit client or persons in financial reporting oversight roles, as of the date of the communication, which might reasonably be thought to bear on independence; and
 - Discuss with the audit committee the potential effects of the relationships described above on the firm's independence.
212. The PCAOB rules require the firm to document the substance of its discussions with the audit committee.

Commentary

213. Both frameworks require audit firms to inform TCWG or the audit committee about any relationships and other matters that might, in the firm's opinion, reasonably bear on independence and so enable TCWG and the audit committee to assess the firm's independence. The PCAOB rules also specify the timing, form and manner in which the communication is to be documented.
214. The Code contains detailed guidance regarding communication of fee-related information to enable TCWG to consider whether any independence considerations arise from the scale or nature of such fees. The SEC and PCAOB rules²⁰² do not address in general the communication of fee-related matters to audit committees.

Approval of Provision of NAS/Non-audit Services to an Audit Client

Code's Provisions

215. The 2021 NAS-related revisions introduced enhanced communication and approval requirements to be complied with by firms prior to provision of NAS to an audit client. Unless otherwise

¹⁹⁹ See revised paragraphs 410.22 A1 to R410.28 for communication requirements relating to fees and paragraphs 600.19 A1 to R600.24 for communication requirements about NAS.

²⁰⁰ PCAOB Rule 3526. Communication with Audit Committees Concerning Independence

²⁰¹ PCAOB Rule 3520 requires the firm and its associated persons to be independent of the firm's audit client throughout the audit and professional engagement period.

²⁰² In connection with seeking audit committee pre- approval of certain tax services PCAOB Rule 3524 requires the communication to the audit committee of the fee structure for the engagement, and any compensation arrangement or other agreement (such as a referral agreement, a referral fee or fee-sharing arrangement,) between the firm and any person (other than the audit client) with respect to the promoting, marketing, or recommending of a transaction covered by the service.

addressed by a pre-determined process agreed between the firm and TCWG²⁰³, the firm is required to:

- (a) Inform TCWG of the PIE that the firm has determined that the provision of the NAS is not prohibited and will not create a threat to the firm's independence, or that any identified threat is at an acceptable level or, if not, will be eliminated or reduced to an acceptable level.
- (b) Provide TCWG of the PIE with information to enable them to make an informed assessment about the impact of the provision of the NAS on the firm's independence.
- (c) Obtain concurrence from TCWG of the PIE before providing a NAS to an audit client.²⁰⁴

216. The new requirement covers NAS that are to be provided to (i) the PIE; (ii) any entity that controls that PIE, directly or indirectly; or (iii) any entity that is controlled directly or indirectly by that PIE.

217. The Code also addresses the situation where a firm is prohibited from providing information about a proposed NAS to TCWG of the PIE, or where the provision of such information would result in disclosure of sensitive or confidential information.^{205 206}

218. Under the Code, having considered any matters raised by TCWG of the audit client or by the proposed recipient of the proposed service, a firm is required to decline the NAS or end the audit engagement if:

- (a) The firm or the network firm is not permitted to provide any information to TCWG of the PIE; or
- (b) TCWG of the PIE disagree with the firm's conclusion that the provision of the service will not create a threat to the firm's independence from the client or that any identified threat is at an acceptable level or, if not, will be eliminated or reduced to an acceptable level.²⁰⁷

SEC and PCAOB rules

219. Before a firm is engaged by an issuer or its subsidiaries, or by a registered investment company to provide an audit or non-audit service, the SEC rules require that the engagement is:

- (a) Approved by the issuer's or registered investment company's audit committee; or

²⁰³ Based on the [Basis for Conclusions](#) to Revisions to NAS Provisions of the Code, the IESBA considered whether there should be any constraints on the matters that may be addressed in any process agreed by a firm and TCWG of a PIE. It concluded that it was for TCWG to determine what was acceptable to enable them to discharge their governance responsibilities. Examples of arrangements that could be addressed in any such process include:

- To pre-approve specific categories of NAS for specified related entities where TCWG are satisfied that any threats to independence would be at an acceptable level;
- To allocate responsibilities and any required reporting between TCWG of multiple PIEs within the same group; and
- To provide monetary limits for delegated authority for specific approvals within preapproved categories.

²⁰⁴ Revised paragraphs R600.21 and R600.22

²⁰⁵ In such instances, the firm may provide the proposed NAS if:

- a) The firm provides such information as it is able without breaching its legal or professional obligations;
- b) The firm informs TCWG of the PIE that the provision of the NAS will not create a threat to the firm's independence, or that any identified threat is at an acceptable level; and
- c) TCWG do not disagree with the firm's conclusion about the impact of the proposed NAS on the firm's independence .

²⁰⁶ Revised paragraph R600.23

²⁰⁷ Revised paragraph R00.24

- (b) Entered into pursuant to pre-approval policies and procedures established by the audit committee of the issuer²⁰⁸ or registered investment company, provided the (i) policies and procedures are detailed as to the particular service, (ii) the audit committee is informed of each service, and (iii) such policies and procedures do not include delegation of the audit committee's responsibilities to management.²⁰⁹
220. With respect to the provision of services other than audit, review or attest services, the SEC rules provide de-minimis exceptions from the pre-approval requirement if:
- (a) The aggregate amount of all such services provided constitutes no more than five percent of the total amount of revenues paid by the audit client to the firm during the fiscal year in which the services are provided;
 - (b) Such services were not recognized by the issuer at the time of the engagement to be non-audit services; and
 - (c) Such services are promptly brought to the attention of the audit committee of the issuer or registered investment company and approved prior to the completion of the audit by the audit committee or by one or more members of the audit committee who are members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee.²¹⁰
221. The SEC rules also require a firm to obtain pre-approval from the registered investment company's audit committee where the firm proposes to provide non-audit services to the investment company's investment adviser (not including a sub-adviser whose role is primarily portfolio management and is sub-contracted or overseen by another investment adviser) and any entity controlling, controlled by, or under common control with the investment adviser that provides ongoing services to the registered investment company.^{211 212,}
222. The PCAOB rules set out specific requirements in relation of pre-approval of tax services²¹³ and non-audit services related to internal control over financial reporting²¹⁴. The rules require additional information to be provided to the audit committee about the scope of the service, and on the potential effects of the services on the independence of the firm.

Commentary

223. Both frameworks require a firm to obtain concurrence or approval from TCWG/ the audit committee before a NAS/ non-audit services may be provided to an audit client. Such

²⁰⁸ The SEC rules requires the issuer to disclose the audit committee's pre-approval policies and procedures in the company's proxy statement. Additionally, to the extent that the audit committee has applied the de minimis exception discussed previously, the issuer must disclose the percentage of the total fees paid to the independent accountant where the de minimis exception was used. This information should be provided by category.(SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 240.14a-101 Schedule 14A. Information required in proxy statement – Item 9)

²⁰⁹ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (7) (i) (A)-(B)

²¹⁰ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (7) (i) (C)

²¹¹ Recognizing the investment companies' complex structures, in such cases, the SEC rules limit the audit committee pre-approval responsibility to those services provided directly to the investment company and those services provided to an entity in the investment company complex where the nature of the services provided have a direct impact on the operations or financial reporting of the investment company.

²¹² SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (7) (ii)

²¹³ Rule 3524. - Audit Committee Pre-approval of Certain Tax Services

²¹⁴ Rule 3525.- Audit Committee Pre-approval of Non-audit Services Related to Internal Control Over Financial Reporting

concurrence or approval must be obtained for each proposed NAS individually or under a general, predetermined policy agreed between the firm and TCWG/ the audit committee.

224. Arising from the different conceptual approaches, there are some differences between the approach taken by the two frameworks:
- (a) The SEC rules require the audit committee to actually approve the service, while the Code requires TCWG to concur with the firm’s assessments of any impact on independence and with the provision of the proposed service.²¹⁵
 - (b) The SEC rules requires the firm to seek approval before providing any audit or non-audit service. The Code requirements are applicable only to the provision of NAS.
 - (c) The Code requires pre-approval to be obtained for the provision of NAS to the PIE, and any subsidiaries or parent entities of that PIE. Whilst the SEC rules require pre-approval from the audit committee of the issuer if the service is to be provided to the issuer or its subsidiaries, pre-approval is not required for the provision of a service to a parent of the issuer.
 - (d) The SEC rules specifically address the pre-approval of services provided to investment company complexes. The Code does not.
 - (e) The SEC rules provide a de minimis exception to the pre-approval requirements for the provision of services other than audit, review or attest services provided that the audit committee approves the service prior to completion of the audit. The Code does not include a de minimis threshold because the IESBA concluded that the Code’s provisions regarding breaches²¹⁶ are appropriate to address inadvertent breaches arising from the application of the requirements for firm communication with TCWG about NAS-related matters.
 - (f) The Code’s provisions address a situation where the provision of information in relation to the NAS would result in disclosure of sensitive or confidential information or it would be prohibited under national laws and regulation.²¹⁷ Such provisions are not required where a framework - such the SEC/PCAOB rules - has legal or regulatory standing in a particular jurisdiction.

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[Placeholder for section on comparison of financial Interest]
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VIII. Business Relationships

225. The Code prohibits a firm, a network firm or an audit team member from having a close business relationship with an audit client or its management unless any financial interest is immaterial, and the business relationship is insignificant to the client or its management and the firm, the network firm or the audit team member, as applicable.²¹⁸ The Code does not prohibit a close business

²¹⁵ Under the corporate governance structures of some jurisdictions TCWG may not have the authority to pre-approve NAS. To allow for those situations, the Code uses the term “concurrence” TCWG, instead of “approval”.

²¹⁶ Paragraphs R400.80 to R400.89

²¹⁷ The IESBA acknowledged that the IESBA does not have authority to establish requirements for TCWG, nor can it: (i) require firms or network firms to share information that is otherwise not permitted by local law or regulation; or (ii) require firms or network firms to share information that is sensitive or confidential. ([Basis for Conclusions](#) to Revisions to NAS Provisions of the Code)

²¹⁸ Paragraph R520.4 of the Code

relationship between an audit client or its management and the immediate family of an audit team member. However, it identifies the risk that such circumstances might create a self-interest or intimidation threat and requires the firm to apply the conceptual framework.²¹⁹

226. The Code provides the following examples of a close business relationship arising from a commercial relationship or common financial interest:

- Having a financial interest in a joint venture with either the client or a controlling owner, director or officer or other individual who performs senior managerial activities for that client.
- Arrangements to combine one or more services or products of the firm or a network firm with one or more services or products of the client and to market the package with reference to both parties.
- Distribution or marketing arrangements under which the firm or a network firm distributes or markets the client's products or services, or the client distributes or markets the firm or a network firm's products or services.²²⁰

227. The Code also prohibits a firm from having a business relationship through holding an interest in common with the audit client. The Code restricts a firm, a network firm, an audit team member, or any of that individual's immediate family from having a business relationship involving the holding of an interest in a closely-held entity when an audit client or a director or officer of the client, or any group thereof, also holds an interest in that entity, unless:

- a) The business relationship is insignificant to the firm, the network firm, or the individual as applicable, and the client;
- b) The financial interest is immaterial to the investor or group of investors; and
- c) The financial interest does not give the investor, or group of investors, the ability to control the closely-held entity.²²¹

228. The Code provides that the purchase of goods and services from an audit client by a firm, a network firm, an audit team member, or any of that individual's immediate family does not usually create a threat to independence if the transaction is in the normal course of business and at arm's length.²²²

229. The SEC rules prohibit a firm or any covered person in the firm from having any direct or material indirect business relationship with

- a) an audit client, or
- b) with persons associated with the audit client in a decision-making capacity, such as
 - an audit client's officers or directors that have the ability to affect decision-making at the entity under audit or
 - beneficial owners (known through reasonable inquiry) of the audit client's equity securities where such beneficial owner has significant influence over the entity under audit.²²³

²¹⁹ Paragraph 520.4 A1 of the Code

²²⁰ Paragraph 520.3 A2 of the Code

²²¹ Paragraph R520.5 of the Code

²²² Paragraph 520.6 A1 of the Code

²²³ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (3)

230. SEC Staff FAQ²²⁴ highlighted joint ventures, limited partnerships, investments in supplier or customer companies, certain leasing interest and sales by the accountant of items other than professional services as examples of business relationships that may impair an accountant's independence. In its response to the FAQ, the SEC has recognized “that certain situations, including those in which accountants and their audit clients have joined together in a profit-sharing venture, create a unity of interest between the accountant and client. In such cases, both the revenue accruing to each party and the existence of the relationship itself create a situation in which to some degree the auditor's interest is wedded to that of its client.”
231. The SEC's prohibition does not apply to a relationship in which the firm or covered person in the firm provides professional services to an audit client or is a consumer in the ordinary course of business.²²⁵

Commentary

232. Both frameworks include prohibitions regarding business relationships between the firm or audit team members²²⁶ and the audit client or the management / persons associated with the audit client in a decision-making capacity. However, the approaches of the Code and the SEC rules differ in certain regards:
- The SEC rules prohibit any direct and material indirect business relationships. In contrast, the Code only restricts close business relationships where the financial interest is material and the business relationship is significant.
 - The restriction under the Code only includes the audit client and management, whereas the SEC restriction also captures beneficial owners with significant influence.
233. Although the SEC rules do not specifically address business relationships created by financial interest held in common with the audit client or its management, the application of the SEC's principles, especially the prohibition of relationships that would create a mutual interest between the auditor and the audit client, would result in the same outcome, irrespective whether the business relationship is material or not. Furthermore, the SEC's prohibition²²⁷ regarding common investment with the client also restricts such business relationships between the firm and the audit client (see paragraphs XX above).
234. Both the SEC rules and the Code provide an exception to business relationship prohibitions in relation to the purchase of goods and services from an audit client by a firm, an audit team member/covered persons in the normal course of business.

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[Placeholder for section on comparison of partner rotation/long association]
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IX. Gifts and Hospitality

235. The Code prohibits a firm, a network firm or an audit team member from accepting gifts and hospitality from an audit client, unless the value is trivial and inconsequential.

²²⁴ Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence – Frequently Asked Questions, [D. Business relationships](#)

²²⁵ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (3)

²²⁶ Please see comparison of “audit team” and “covered persons” definitions in Section III of this document

²²⁷ SEC Rule 2-01 of the Commission's Regulation S-X, 17 C.F.R. § 210.2-01 (c) (1) (i) (E) (1) (i)

236. Based on the Code's provisions, a firm cannot accept or offer, or encourage others to accept or offer, any inducement²²⁸ that the firm concludes is made, or considers a reasonable and informed third party would be likely to conclude is made, with the intent to improperly influence the behavior²²⁹ of the recipient or of another individual.²³⁰
237. If a firm concludes that there is no actual or perceived intent to improperly influence the behavior of the recipient or of another individual, the conceptual framework still applies. However, if such an inducement is trivial and inconsequential, any threats created will be at an acceptable level.²³¹
238. The SEC rules and guidance do not explicitly address the firm or audit team members offering or accepting gifts, hospitality, or other inducements. However, in its response to a FAQ the SEC Staff ²³² noted that the " [SEC] staff would consider all relevant facts and circumstances associated with the giving or acceptance of gifts or entertainment from an audit client in assessing whether the accountant will—or will not—be deemed independent under the general standard. The nature and frequency of the activities may reflect a close personal relationship that could be independence impairing."

Commentary

239. Both frameworks recognize that giving or accepting gifts and other inducements to or from an audit client could impact the firm's independence. However, the Code includes more specific guidance and general prohibitions in this regard.

²²⁸ The Glossary to the Code defines inducement as an object, situation, or action that is used as a means to influence another individual's behavior, but not necessarily with the intent to improperly influence that individual's behavior. Inducements can range from minor acts of hospitality between business colleagues (for professional accountants in business), or between professional accountants and existing or prospective clients (for professional accountants in public practice), to acts that result in non-compliance with laws and regulations. An inducement can take many different forms, for example: Gifts, Hospitality, Entertainment, Political or charitable donations, Appeals to friendship and loyalty, Employment or other commercial opportunities, Preferential treatment, rights or privileges.

²²⁹ An inducement is considered as improperly influencing an individual's behavior if it causes the individual to act in an unethical manner. Such improper influence can be directed either towards the recipient or towards another individual who has some relationship with the recipient. The fundamental principles are an appropriate frame of reference for a professional accountant in considering what constitutes unethical behavior on the part of the accountant and, if necessary, by analogy, other individuals.

²³⁰ Paragraphs R340.7 and R340.8 of the Code

²³¹ Paragraphs 340.11 A1 and A2 of the Code

²³² Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence – Frequently Asked Questions, A. General standard of independence, [Question 3](#)