

February 4, 2015

IFAC Small and Medium Practices (SMP) Committee Response to the International Ethics Standards Board for Accountants (IESBA) Consultation Paper: *Improving the Structure of the Code of Ethics for Professional Accountants*

INTRODUCTION

The SMP Committee is pleased to respond to the IESBA (the Board) on this Consultation Paper (CP).

The SMP Committee is charged with identifying and representing the needs of its constituents and, where applicable, to give consideration to relevant issues pertaining to small-and medium-sized entities (SMEs). The constituents of the SMP Committee are small-and medium-sized practices (SMPs) who provide accounting, assurance and business advisory services principally, but not exclusively, to clients who are SMEs. Members of the SMP Committee have substantial experience within the accounting profession, especially in dealing with issues pertaining to SMEs, and are drawn from IFAC member bodies representing 18 countries from all regions of the world.

GENERAL COMMENTS

The SMP Committee has been grateful for the opportunity to provide previous comments on the Structure of the Code project in advance of the IESBA Board's meetings. In our response to the IESBA Consultation Paper: *Proposed Strategy and Work Plan, 2014-2018*¹ we expressed our agreement for a project to improve the usability of the structure of the *Code of Ethics for Professional Accountants* (the Code).

We continue to support the approach taken by the IESBA and the general direction of the project. We agree with the proposal to clearly separate the requirements from guidance, as it will enhance the users understanding of the specific prohibitions. The CP asks for views on the possibility of creating separate standards on specific topics and rebranding the Code as the International Standards on Ethics. In our opinion, this would be a completely separate way to restructure the Code, a more onerous undertaking and a move away from a principles-based to a more rules based version of the Code. We recognize that there could be some merit in exploring the option for specific areas of the Code to be separate standards, for example auditor independence, but we do not believe it should be applied to the entire code.

We welcome the reference in the CP to the results from the [SMP Quick Poll](#)² which found that the biggest barrier faced by SMPs in fully adhering to the Code was due to understanding its requirements. As highlighted in our comment letters in both July and October 2014, we strongly encourage the IESBA to consider how it can best elicit feedback and comments on its proposals from a large number of SMPs.

¹ See <http://www.ifac.org/publications-resources/smp-committee-response-iesba-consultation-paper-proposed-strategy-and-work-pl>

² Note. In 2014 the SMP Quick Poll was rebranded as the IFAC Global SMP Survey. A [press release](#) covering the initial 2014 results was released on January 22, 2015.



Due to their often limited resources, these stakeholders are often not able to easily respond and engage with the standard setting consultation process. Despite this, these SMPs are some of the main users of the Code and therefore it is important their opinions are canvassed and their input considered by the Board. We look forward to seeing how successful the IESBA is in this wider engagement and would be willing to work closer with the respective Task Force on this matter as the project develops.

In our view, the IESBA should adopt the “think small first” principle in its approach to standard setting. This is important at the early stages of a project to ensure the end product is useable by the full range of firms – from sole practitioners to practices with many partners. For example, we agree that it may be appropriate to assign the responsibility to the firm in certain instances, but we highlight the fact that for many small practitioners a firm represents just one individual.

We also believe that the Board should give further consideration to the cost of implementation of the restructuring on individual jurisdictions and how it will impact codes which are based on the Code, but slightly modified.

SPECIFIC COMMENTS

We have outlined our responses to each question (*in italics*) in the CP below.

1. Do you believe that the approach outlined in this Consultation Paper, as reflected in the Illustrative Examples, would be likely to achieve IESBA’s objective of making the Code more understandable? If not, why not and what other approaches might be taken?

In principle we agree that the outlined approach to restructuring would be likely to achieve IESBA’s objective of making the Code more understandable. As the Code currently mixes rules (requirements and prohibitions) with application guidance, the separation should help. Cross-referencing the requirements to the related application guidance as proposed is also essential to mitigate the risk that some users could be drawn more to the requirements, without the benefit of the separate application material and guidance and therefore have a quite different interpretation from what is intended.

We note that in its clarity project the IAASB had decided not to use the present tense at all when referring to an auditor’s actions. We would also support the IESBA adopting this stance (as outlined in paragraph 15), as we believe that the use of present tense is a particularly important issue in achieving clarity of meaning as to what is required and what is not. The Illustrative Examples indicate the difficulties in achieving this if material from the extant Code is merely rearranged. In particular, we note instances of repetition and in certain areas believe that further guidance would be beneficial to assist practical application, for example in regard to the issue of independence.

2. Do you believe that the approach outlined in this Consultation Paper, as reflected in the Illustrative Examples would be likely to make the Code more capable of being adopted into laws and regulations, effectively implemented and consistently applied? If not, why not and what other approaches might be taken?



In comparison with the existing code the structure outlined in the Illustrative Examples may be helpful in terms of consistency in implementation and overall we support the approach on this basis.

In our opinion, there is a risk attached when the Code is adopted locally. In jurisdictions where a State regulator has developed its own code, it is very often not quite in alignment with the Code adopted by professional bodies, although the sentiments are the same. Adoption of the Code will be easier to align where the application material is separated out. However, there is a risk that such alignment may simply be of the requirements and the application material would not make it, in full or in part, into local legislation. If the restructuring of the Code goes ahead, the IESBA will need to make clear that the requirements do not stand alone and the complete code is adopted.

In jurisdictions where it is solely a matter for the professional accountancy organization to adopt and supervise its member's adherence to the Code, it should be fairly easy to adopt. However, there is the risk that the professional bodies may challenge the cost/ benefit of changing the structure in line with the Code, which may result in it not being consistently applied. In principle, this could be managed through IFAC's Statements of Membership Obligations (SMOs), which are the basis of IFAC Member Body Compliance Program. In essence, SMO 4 requires the adoption and implementation of ethical standards no less stringent than the Code.

We note that the restructure may have an impact on the take up of the Code, but there are many other factors impacting adoption into law and regulation, which will be taken into account by legislators in their individual decisions whether to reflect specific provisions of the Code in their national laws.

3. Do you have any comments on the suggestions as to the numbering and ordering of the content of the Code (including reversing the order of extant Part B and Part C), as set out in paragraph 20 of the Consultation Paper?

We have no issues with the proposed numbering and ordering of the content of the Code and agree that reversing the order of extant Part B and Part C is logical.

It would have been useful if the CP or one of the Illustrative Examples could have indicated how the Board is proposing to more clearly differentiate the provisions applicable to public interest entities (PIEs) from those applicable to other entities, especially in respect to auditor independence. Since not all SMPs have PIEs amongst their clients, this differentiation would be helpful both to those who are unaffected by more precise or more stringent requirements as well as those who may take on new clients that are PIEs. We believe that many professional accountants in private practice throughout the world would find a clear overview of these differences helpful.

4. Do you believe that issuing the provisions in the Code as separate standards or rebranding the Code, for example as International Standards on Ethics, would achieve benefits such as improving the visibility or enforceability of the Code?

In our view, issuing the provisions in the Code as separate standards and rebranding the Code, for example as International Standards on Ethics, are two very different restructuring possibilities.



Developing the provisions in the Code to constitute a series of truly separate standards would likely necessitate the addition of considerable further material to provide clarification in some areas, and would be far more onerous than the “simpler” approach suggested in the Illustrative Examples.

We do not consider that rebranding the Code without developing a full set of such standards could have a significant impact on improving its visibility and enforceability. However, we would expect that clarifying ethical requirements and providing guidance material thereto would improve both professional accountants’ understanding of the actions ethical behavior in accordance with the Code demands on their part, and that of those responsible for enforceability.

We also believe that rebranding the Code would be contradictory to the basis of the Code as a conceptual framework and as a measure alone will not change ethical behavior. The CP itself notes that IESBA is mindful of the conceptual framework approach, which addresses threats to compliance with the fundamental principles rather than simply complying with rules (paragraph 12). In our opinion, the Code should remain as principles-based ethical behavior over prescription. This is also important to allow the Code to work in conjunction with various national requirements. If the Board decides to simply rebrand the Code, it is important that any expectations of the impact are carefully managed.

5. Do you believe that the suggestions as to use of language, as reflected in the Illustrative Examples, are helpful? If not, why not?

A robust definition of each key term used in the Code is essential for proper application by professional accountants. To the extent that the understanding of a particular term or terms is critical to the application of requirements of a particular standard it would be useful to include the definition(s). We otherwise agree with the matters listed in paragraph 23. The use of too colloquial terms/ vocabulary could also potentially devalue the perception of the profession by the public in general.

6. Do you consider it is necessary to clarify responsibility in the Code? If so, do you consider that the illustrative approach to responsibility is an appropriate means to enhance the usability and enforceability of the Code? If not, what other approach would you recommend?

We wholly agree with IESBA that a global code should be sufficiently flexible to accommodate different circumstances that firms need to take into account when they prescribe responsibilities (paragraph 27). The circumstances in SMPs are often very different to those in the largest firms. The Code needs to be clear as to the respective responsibilities of firms on the one hand and the individual professional accountants on the other, but it does not necessarily need to ensure that firm’s go as far as assigning the firm’s responsibilities to a particular individual. The key issue is that the particular ethical requirement is adhered to, not who is and who is not, assigned the responsibility.

We generally see some merit for larger firms establishing who is to assume responsibilities in this area, although it will often not make sense in respect of small firms, who may have other effective but less formal ways of ensuring ethical behavior. In addition, we believe this proposal may require further consideration on whether it is required within the Code or within quality control standards. However, we



recognize that paragraph 20 in ISQC 1³ establishes an overall requirement for firms undertaking audit, review and other assurance and related services to establish policies and procedures to provide the firm with reasonable assurance that the firm and its personnel comply with relevant ethical requirements. To the extent that parts of the Code apply to firms whose activities do not fall within the scope of ISQC 1, it might make sense for the Code to include a similar provision.

Should the IESBA, contrary to our comments, decide to require the explicit allocation of responsibilities within a firm, we also recommend that consideration is given to whether any such provision should include an exception for SMPs of a certain size. This could, for example, be based on a similar provision in the UK APB Ethical Standard 1 (Revised) *Integrity, Objectivity and Independence*⁴ which states:

“26. In audit firms with three or fewer partners who are ‘responsible individuals’⁵ it may not be practicable for an Ethics Partner to be designated. In these circumstances all partners will regularly discuss ethical issues amongst themselves, so ensuring that they act in a consistent manner and observe the principles set out in APB Ethical Standards. In the case of a sole practitioner, advice on matters where a difficult and objective judgment needs to be made is obtained through the ethics helpline of the auditor’s professional body, or through discussion with a practitioner from another firm. In all cases, it is important that such discussions are documented”.

7. Do you find the examples of responsible individuals illustrated in paragraph 33 useful?

We note that in the example included in paragraph 33 the policies that enable identification of responsible individuals may differ depending on the size, structure and organization of a firm. If IESBA extends the Code as suggested, which as noted above, the SMPC is not convinced is necessary in respect of all firms - guidance would be needed to explain factors that may influence decisions on firm’s responsibilities. From an SMP perspective, and in light of our response to question 6, it would be essential to add guidance to address how for example, the smallest firm or a sole practitioner might be expected to evidence compliance.

We have some concerns with the terms used in the example in paragraph 33. The term “senior individuals” would need to be explained as it could suggest that a firm or principal could designate responsibility to someone who is not a professional accountant and perhaps does not fully understand the profession or the Code and may look at matters in a more commercial as opposed to ethical light. Similarly, any other individual who is a responsible individual in relation to a particular matter needs clarification.

³ ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

⁴ <https://www.frc.org.uk/Our-Work/Codes-Standards/Audit-and-assurance/Standards-and-guidance/Standards-and-guidance-for-auditors/Ethical-standards-for-auditors.aspx>

⁵ The UK APB *Ethical Standard 1 (Revised) Integrity, Objectivity and Independence* defines ‘responsible individual’ as a partner or employee of the audit firm who is responsible for audit work and designated as such under the audit regulations of a Recognized Supervisory Body.



8. Do you have any comments on the suggestions for an electronic version of the Code, including which aspects might be particularly helpful in practice?

We believe that an electronic Code is a very helpful step forward and welcome the improvements available with its development.

We understand that in the majority of jurisdictions SMPs use a local translation of the Code, which has been tailored to their national jurisdiction. The Code on the IESBA website may therefore not be the prime source used by practitioners. In addition, some accountants may not have the means to use an electronic Code yet, so a paper based Code is still needed.

We see no reason why both versions cannot be the official version as they are effectively the same Code, just presented differently.

9. Do you have any comments on the indicative timeline described in Section VIII of this Paper?

At present, we believe the timetable indicated is not unreasonable, but may be ambitious given the need to adhere to due process. In addition, if the IESBA decide to develop a set of Standards on Ethics, beyond the topic of independence, it would likely need longer than has been proposed to restructure the current code based on this approach.

We also remind the Board of the importance of clearly communicating proposed changes to the Code as SMPs have less human, financial and technological resources to read, understand and effectively apply the Code.

10. Do you have any other comments on the matters set out in the Consultation Paper?

We believe that the needs of the SMP community should be at the forefront as IESBA takes this project forward. We would be very willing to provide further input and work with the relevant Task Force as this project develops.

CONCLUDING COMMENTS

We hope the IESBA finds this letter helpful in moving forward with the project to restructure the Code. In turn, we are committed to helping the Board in whatever way we can to build upon the results of this Consultation Paper. Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,

A handwritten signature in black ink, appearing to read 'Giancarlo Attolini', is written over a horizontal line. The signature is fluid and cursive.

Giancarlo Attolini
Chair, SMP Committee