



Proposed Revisions Pertaining to Safeguards in the Code - Phase 2

ICAEW welcomes the opportunity to comment on the *Proposed Revisions Pertaining to Safeguards in the Code - Phase 2 and Related Conforming Amendments* published by IESBA on 24 January 2017, a copy of which is available from this [link](#).

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OVERALL

1. While we have not encountered significant issues with our members understanding the notion of the conceptual framework, we remain supportive of this project to enhance discussion in the IESBA Code of Ethics (the Code), the general approach taken, and its co-ordination with the structure and other projects.
2. We note the Board's recognition in a number of places in the Explanatory Memorandum (EM) of the issues that SMPs face with implementing safeguards, so it is a little disappointing that the enhanced discussion in the Code fails to address that. We comment further on this in our response to question 3.
3. We set out our responses to the questions asked in the consultation paper below, and have included comments on the wording in specific paragraphs under the most relevant heading.

REQUEST FOR SPECIFIC COMMENTS

Section 600, Provision of Non-Assurance Services to an Audit Client

Q1: Do respondents support the proposals in Section 600? If not, why not?

In particular, do respondents agree with the proposal to extend the scope of the prohibition on recruiting services as described in paragraph 25(h) above to all audit client entities? If not, please explain why.

4. Except as noted below, we support the proposals.
5. We are not persuaded of the necessity of the proposed extension of the recruitment services prohibition that is currently applicable only to PIE audits, to all audits. IESBA offers no evidence in the EM of an independence problem arising with the provision of recruitment services to non-PIE audit clients, only an assertion that no safeguards could be thought of, so the threats and safeguards approach is to be overridden. This is not an evidence-based approach to regulation and the logic undermines the general approach with non-PIE audit clients: apply the conceptual framework and allow the action to fit the many variations in individual circumstances.
6. R600.8a refers to designating an individual to be responsible for management decisions. This could be read to require the same person to be responsible for every decision – we assume that is not what is meant as organisations operate in a variety of ways.
7. R601.8 includes an exception cross reference to 601.6: we believe it should refer to 601.7.
8. In 603.3A2 we believe that the last part of the last sentence should state 'the application material....applies.'
9. In 604.5A1, the statement that 'Providing tax return preparation services does not usually create a threat' is slightly more sweeping than the equivalent comment in the existing 290.179, which includes an important caveat.
10. We note that the discussion in the area from 600.7 onwards is generally around ensuring that the auditor does not assume a management responsibility. However, the title is 'Avoiding management responsibilities'. 'Avoiding' is acquiring a negative connotation in some countries (in the context of tax avoidance) so we would prefer the title to be 'Not assuming management responsibilities'. The same comment also applies to 950.5.

Section 950, Provision of Non-Assurance Services to an Assurance Client

Q2: Do respondents support the proposals in Section 950? If not, why not?

11. Apart from a detailed comment on 950.5, referred to in paragraph 10 above, we support the proposals.

Examples of Safeguards

Q3: Do respondents have suggestions for other actions that might be safeguards in the NAS and other sections of the Code that would meet the revised description of a safeguard?

12. It seems to be rather late in the process of examining safeguards, to be asking about additional safeguards. Perhaps going forward, this sort of question might usefully be posed at an earlier stage in a project process.
13. Specific safeguards will tend either towards exclusion of relevant individuals from the assignment, or some form of independent review of the work done. For SMPs, the former is often unavailable and the latter will involve review by someone external to the firm. We think some discussion could be had on whether different forms of independent review might be appropriate depending on the 'level' of threat. For example:
 - a) would an independent review always need to be a pre-sign-off 'hot' review;
 - b) could it in some circumstances be restricted to no more than a consultation on the specific issue, rather than something wider, which is perhaps implied by 'review';
 - c) could it be addressed, where the 'level' of threat is at a relatively low level (but above not needing addressing at all) by a post-sign-off 'cold' review.
14. One of the principal threats in respect of potential conflict of interest situations is that a conflict could give rise to a failure to be able to provide genuinely objective advice. If the level of the threat is not so overwhelming as to require refusal or termination – perhaps being restricted to one specific aspect of the engagement, one possible action to mitigate this might be to advise the client(s) to seek alternative, independent advice.

Conforming Amendments Arising from the Safeguards Project

Q4: Do respondents agree with proposed conforming amendments set out in:

- (a) Chapter 2 of this document.
- (b) The grey text in Chapters 2–5 of Structure ED-2.

15. We support the general approach to conforming amendments, but have a number of detailed comments, set out below.
16. In 310.8A2, 'Separating confidential information' appears to be more of an action that could apply (thus featuring in 310.8A3) rather than a factor in this paragraph.
17. In 320.6A3 we believe that a more relevant factor in evaluating the level of threats created by appointments would be whether the tender or any other document or law, would prevent the prospective accountant contacting the previous accountant.
18. 340.4A2 specifically refers to the 'reasonable and informed third party' ('RITP') test, whereas elsewhere this is taken as read given the discussion in s120. It is unclear why this inconsistency is needed.
19. In section 410 paras 14 and 18, we assume the second paragraph referred to in 14 is the same paragraph as is referred to in 18, as they seem remarkably similar.

20. 511.4A1 and 2 suggests that an action to deal with a loan to the firm might be to have a reviewing professional from a network firm. This would only work if the network firm were not dependent on the firm in question, as may be the case in some circumstances.

Other matters

Q5: Respondents are asked for any comments on any other matters that are relevant to Phase 2 of the Safeguards project.

Safeguards

21. We note from the EM that the Board is replacing discussion on the 'significance' of a threat with discussion around the 'level' of a threat. While this ties in with the definition of 'acceptable level' we believe that the concept of significance is (or could be) well understood by professional accountants. 'Level' has a variety of meanings and we wonder if it will translate well into other languages.
22. We endorse the Board's re-assertion that the RITP is a concept rather than a specific person. It is important not to over-engineer the description of the attributes of the RITP to give a misleading impression that a specific person should be chosen. The description of the RITP in paragraph 120.5A1 of the compilation document includes the comment that the RITP 'does not need to be an accountant'. Given that the RITP is a hypothetical person, including a description of what that person need or not be (rather than the knowledge and perspective they would apply) seems to be confusing and potentially misleading. This could be taken to imply that the Board would prefer the RITP to be an accountant, while not insisting on it. We do not believe this is intended and would invite the Board to reconsider whether these words are helpful.
23. We note from the 'Basis of Agreement in principle' document that the Board re-confirmed its intention to describe 'acceptable level' in an affirmative manner, notwithstanding concerns from some, including ourselves. We are not sure this has been thought through: given that ethics is by its nature a behavioural concept built around a mind-set, rather than merely measurable actions, we fail to see how any RITP could make a conclusion of positive compliance with the fundamental principles.

Other points

24. We note that there are a number of inconsistencies within the current code that the safeguards (and structure) revisions have made more obvious. While acknowledging that these are likely to be outside of the remit of the safeguards and structure projects, we invite the Board to consider them at their earliest convenience. These include:
- a) Inconsistent usage of 'listed entity' (for example in the definition of 'audit client') and 'public interest entity' (where, for example, differential treatment is highlighted throughout the new NAS section). From the interaction of these usages, there may be audit clients that are not PIEs, audit clients that are PIEs but not listed, and audit clients that are listed and thus PIEs. In fact in the UK there are, using the definitions issued by the Financial Reporting Council, also audit clients that are listed non-PIEs - but the Code does not yet allow for this.
 - b) Inconsistent treatment across the code of 'materiality' and 'significance'. In our view 'materiality' should only be used where a narrow quantitative test is intended. A 'significance' test would embrace a wider assessment of factors likely to lead to influence and should generally be preferred in a principles-based code.

REQUEST FOR GENERAL COMMENTS

25. We have no comments on the general issues referred to in the consultation paper other than to endorse the references in the EM to the unique challenges faced by SMPs in employing some safeguards. We have commented further on this in our response to question 3.