



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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Agenda Item

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Board International Ethics Standards Board for Accountants

Meeting Location: Marriott Marble Arch, London, UK

Meeting Date: December 10-12, 2008

Drafting Conventions

Objective of Agenda Item

To commence the review of comments received on exposure (by deliberating the change from “should to shall,” the departure clause, and the deletion of the term “clearly insignificant”). In subsequent meetings we will address the remaining points, such as effective date and specific comments on individual paragraphs.

Background

In July 2008, the IESBA issued an exposure draft proposing revisions to improve the drafting conventions of the Code. The explanatory memorandum stressed that the IESBA was seeking comments only on the proposed changes to the Code that were the result of the drafting conventions project.

The exposure period was three months and ended on October 15, 2008.

To date, comments have been received from the following:

Member Bodies of IFAC	21
Firms	7
Regulators and Oversight Authorities	2
Others	15
Total Responses	45

At the time of writing, the IOSCO letter is outstanding. If this letter is received before the IESBA meeting, it will be posted separately.

The Task Force met on November 4-5, 2008 to address comments received on questions 1-4 in the exposure draft.

The CAG meets on November 24, 2008 and the contents of this agenda paper will be discussed with the CAG members. The Task Force meets on November 25, 2008 to

discuss and respond to CAG member comments. The Task Force’s response will be reported at this IESBA meeting.

This agenda paper provides an overview of comments received on questions 1-4 in the exposure draft, followed by the Task Force’s proposal to address the comments received. Responses to question 5 and other comments on the exposure draft will be addressed at a subsequent meeting.

All of the comment letters received have been posted on the IFAC website and may be downloaded at <http://www.ifac.org/Guidance/EXD-Details.php?EDID=0116>.

Discussion

ED Question 1 The IESBA is of the view that identifying a requirement by the use of the word “shall” clarifies the Code and appropriately brings the language in line with that adopted by the IAASB. Do you agree? If you do not agree please provide an explanation.

ED Responses

The majority of respondents were supportive of the approach proposed in the ED.

	Member Bodies	Firms	Others
Supportive	AICPA, IDW, FARS, MIA, SAICA, ICPAS, NIVRA, ICAEW, Wpk, ICAS, JICPA, HKCIPA, CICPA, ICPAC, CNCC, ICAA/CPA Aus/ NIA	BDO, EYG, RSM, KPMG,	Shum, AIA, APESB, CARB, RM, IIA, Basel, IRBA
Supportive but is of the view that some additional paragraphs should use shall			CEBS
Supportive but questions whether shall is appropriate in a few specific paragraphs	CSOEC, FEE	GTI, CIMA, CICA	
Supportive but must be clear that principles prevail			CARB
Supportive but of view that shall ought to be used only for requirements			APB
Supportive if certain revisions, including 100.11 are made		DTT	
Supportive of change to shall		PwC	

but not the way implemented			
Concerned that change suggests an absolute requirement rather than a course to be followed in normal circumstances			LSCA

Illustrative arguments in favor of the approach are:

- We support the drafting convention change from “should” to “shall” in the Code as we believe it enables an overall strengthening of the Code and furthers efforts towards convergence. The use of “should” implies a greater degree of discretion than the use of “shall”. Accordingly, the use of “shall” enhances the clarity and understandability of the Code as it removes a degree of discretion that we do not believe was intended by the Code (EYG); and
- The Joint Accounting Bodies agree that identifying a requirement by the use of the word “shall” clarifies the Code, and appropriately brings it into line with the language adopted by IAASB. We believe that the Code still presents as a principles-based document utilising a conceptual framework, which does not diminish the accountant’s need to exercise professional judgement. (ICAA/ CPA Aus/ NIA).

Some respondents expressed general support for the change from “should” to “shall” but were of the view that either some additional paragraphs should use the term “shall” (for example, paragraph 100.5, which states “a professional accountant is required to comply with the following...”)(Basel). Others expressed general support for the change but questioned whether “shall” was appropriate in a few specific paragraphs (for example, 320.2, which states that a professional accountant who has responsibility for the preparation or approval of general purposes financial statements shall ensure the financial statements are presented in accordance with the applicable financial reporting standards – the professional accountant that prepares the financial statements may not have ultimate authority to approve them)(APESB)

One respondent (APB) expressed support for the approach but was of the view that:

- All requirements should contain the word “shall” – for example 130.1 which states “the principle of professional competence and due care *imposes the following obligations on all professional accountants* to maintain professional knowledge”” should be re-written to state “the professional accountant *shall maintain* professional knowledge...”;
- Only requirements should contain the word shall – for example, 290.101, which states “Paragraphs 290.102 to 290.126 contain references to the materiality of a financial interest, loan, or guarantee, or the significance of a business relationship. For the purpose of determining whether such an interest is material to an individual, the combined net worth of the individual and the individual’s immediate family members shall be taken into account.”;
- The word “shall” should be eliminated where a generic threats and safeguards approach is required – the repetition of phrases such as “the significance of the

- threat shall be evaluated...” leads to a large number of instances where the word ‘shall’ is used but there are no specific additional requirements or prohibitions; and
- The requirements should be more apparent - It is not very clear in the text where a requirement is included, since the word ‘shall’ often appears at the end of a paragraph after associated explanatory text and there is often more than one requirement in each paragraph.

One respondent (DTT) expressed support for the change provided certain other revisions to the Code, including paragraph 100.11, were made. This is discussed in more detail below under Question 3(b).

One respondent (PwC) was supportive of the move to shall but was concerned with the way the change had been implemented. The respondent stated that:

- We do not believe, however, that the Board has satisfactorily addressed the consequences that flow from its wholesale change to “shall,” nor do we believe the ED, as it currently stands, is clear, unequivocal, and capable of straightforward implementation;
- The use of “shall” throughout the Code has fundamentally changed the Code's nature. The result is essentially a “rule book,” given the definition of “shall” in paragraph 100.4, instead of a principles-based Code. The ED’s adoption of so many “requirements” eliminates in many areas the accountant’s ability to apply appropriate professional judgment;
- By using the word “shall,” the ED implies that any violation of any requirement will, by definition, in the context of Section 290, impair the auditor’s independence, render the firm unable to sign the assurance opinion, and thereby force the firm to resign; and
- We believe that the change to a more rules-based approach makes clarity even more important....Specifically, for each requirement it should be clear what the triggering event is, who is responsible for forming conclusions and taking action, and what actions are to be taken and when.

To address these matters, the respondent recommended:

- Restructuring [the Code] to include the fundamental principles, requirements, and guidance. The mandatory “shall” should be reserved only for the principles and requirements; guidance (including examples), in contrast, would use “should” or “may.”; and
- Modifying the Code to permit and require the professional accountant to exercise professional judgment in determining how to comply with the fundamental principles and the various specific provisions of the Code.

While expressing support for the move from “should” to “shall,” several (11) respondents expressed concern that the Code was moving away from a principles-based approach. Illustrative comments include:

- We are concerned, therefore, that the proposed changes give the impression of moving the Code further away from the threats and safeguards approach towards a legalistic, rules-based standard. We believe the robustness of the principles-

- based approach is being undermined by the proliferation of detailed underlying rules (FEE) and
- However, we would like to remind IESBA to be mindful and to strike a balance between on one hand having a principles-based approach to the Code, and on the other hand, placing too many requirements with a “shall” in the Code, as it has been reported that the tone of the Code has changed. We believe that there is a need to ensure that a balance is made in order that the Code is robust. (HKICPA)

Task Force Proposal

The Task Force notes that the majority of respondents were supportive of the position proposed in the exposure draft.

When the exposure draft was prepared, the IESBA was of the view that some existing provisions of the Code, while not using the word “shall,” were clearly requirements (e.g. ¶100.5 “professional accountant is required...”) and, therefore, did not propose any changes to clarify these provisions. The Task Force has considered this matter in light of the comments received and for the sake of consistency recommends that all requirements be identified by use of the word “shall.”

The Task Force considered the comments expressing concern that the Code was moving away from a principles-based approach. The Task Force noted that this matter has been raised by respondents in the past, principally on exposure of IT1 and IT2. The IESBA, and CAG, discussed the issue at that time and concluded that there is no conflict between a principles-based approach and absolute restrictions or prohibitions, provided that such restrictions or prohibitions flow directly from the application of the principles. The Task Force is not, therefore, proposing any changes in response to these comments. The Task Force will, however, carefully review the Code to examine each use of the word “shall” to determine whether there are instances where the requirement may have inadvertently been changed. If there are any such instances, the Task Force will raise these matters at a subsequent IESBA meeting (likely the February 2009 meeting).

The Task Force considered the comment that the use of the word “shall” should be eliminated where a generic threats and safeguards approach is required because this leads to a large number of instances where the word “shall” is used but there are no specific additional requirements. The Task Force is of the view that the repetition is important because in each case the professional accountant is required to evaluate the significance of the threats and apply safeguards as necessary.

The Task Force considered the comments from the respondent who, while supporting the move to shall, was concerned with the way the change had been implemented. The Task Force noted that this was an isolated comment and that part of the respondent’s concern seemed to relate to the exception paragraph, which is discussed in question 3. In addition the issue of separately presenting the objective, requirements to achieve that objective, and guidance is discussed in question 2.

IESBA Question

IESBA members are asked to consider the comments received regarding the identification of requirements by the use of shall and determine whether they agree with the Task Force’s proposal.

ED Question 2 The IESBA is of the view that separately presenting the objective to be achieved, the requirements designed to achieve that objective, and the application guidance as in the ISAs would not further improve the clarity of the Code. Do you agree? If you do not agree, please provide an explanation and an example of the separate presentation that you recommend.

ED Responses

The majority of respondents were supportive of the approach proposed in the ED.

	Member Bodies	Firms	Others
Supportive	AICPA, ICPAS, JICPA, SAICA, CICAP, MIA, WpK, ICAEW, HKICPA, CNCC, CSOEC, CIMA, IDW, CICA, FARS, ICAS, ICAA/ CPA Aus/ NIA, ICPAC, ICPAS,	GTI, BDO, EYG, RSM, KPMG, DTT,	MS, AIA, CARB, FEE, IRBA
Supportive but notes that distinction between overriding principle and requirement is not always clear			CCAB
Agree in principle but should demonstrate why position is appropriate			Basel
Supportive of approach for short term but more could be done to highlight requirements			APB
While same format as ISAs may not be appropriate structure should not be dismissed	ACCA		
Disagree	NIVRA	PwC	VSCPA

Illustrative arguments in favor of the approach are:

- Whilst the revised structure of ISAs may better suit standards that deal with procedures basically performed by professional accountants, we do not believe that such a structure would suit a principles-based Code primarily dealing with professional behaviour. We, therefore, agree that the clarity of the Code would not be improved if the IESBA were to adopt the structure used for ISAs (WpK); and
- We agree that these additional drafting conventions implemented by the IAASB would not further improve the clarity of the Code. In fact it would likely make the Code lengthier, which could make it more difficult to apply (AICPA).

Illustrative arguments against the approach are:

- Separation of, in particular, requirements and guidance would make the requirements clearer and would make the Code more readable. We believe that it would also contribute to a more uniform implementation of the Code into national regulation. It is also logical and desirable that regulation forming part of the same structure has a consistent look and feel (NIVRA); and
- We believe the ED would be significantly improved, as well as consistent with the ISAs, if it were restructured to include the fundamental principles, requirements and guidance. The mandatory “shall” should be reserved only for the principles and requirements; guidance (including examples), in contrast, would use “should” or “may.” A redraft along these lines would also ensure that “requirements” are limited and clearly differentiated (PwC).

In addition, one respondent (APB) indicated support for the structure in the short term but stated that more needs to be done to help users identify the requirements in the IFAC Code. This could be achieved by highlighting the requirements as follows:

- use bold type for relevant sentences or
- underline the word ‘shall’ wherever it is used, or
- use a numbering convention to indicate requirements.

Task Force Proposal

The Task Force considered the responses to the question and noted that the majority of respondents were supportive of the approach. The Task Force was not persuaded that the suggested alternative approach would result in a Code that was clearer in all cases. In addition, the Task Force was of the view that some of the proposed solutions for a change in structure could be seen as weakening the Code. The Task Force is not, therefore, proposing any changes to the structure.

IESBA Question

IESBA members are asked to consider the comments received regarding the structure of the Code and determine whether they agree with the Task Force’s proposal.

ED Question 3a Do you agree that the Code should contain a provision that permits any exception to compliance with a requirement set out in the Code? If you do not agree, please provide an explanation.

ED Responses

The majority of respondents supported the inclusion of a provision that permits an exception, though a significant minority disagreed with the inclusion of the exception clause. In addition, several of those who supported an exception disagreed with how the exception was drafted – their concerns in this regard are addressed under question 3(b).

	Member Bodies	Firms	Others
Supportive	FARS, MIA, IDW, SAICA, HKICPA, AICPA, ICPAS, CSOEC, JICPA, NIVRA, WpK, ACCA, CIMA, ICPAC, ICAEW, ICAS, CICA	RSM, GTI, DTT, PwC	RM, MS, IIA, FEE, NASBA, CCAB, APB
Support but may not implement in jurisdiction because may lead to abuse	CICPA		
Not supportive	CNCC, ICAA/CPA Aus/ NIA	BDO, KPMG, EYG	VSCPA, AIA, CEBS, APESB, IRBA , CARB, Basel

Illustrative supportive comments are:

- However, there may be exceptional circumstances where compliance is impossible, and those circumstances are not deemed to compromise compliance with the fundamental principles. Moreover, it is impossible to anticipate all such circumstances. Given that such exceptional circumstances could happen, a provision that permits departure from compliance should be contained in the Code to allow a response in such cases (JICPA);
- In a principles-based Code there may be situations, albeit rare, where compliance with a specific requirement may result in a failure to adhere to the fundamental

- principles. Consequently, we believe that an exception concept is needed that, with appropriate safeguards in place, would allow to override a single provision if such override would better serve the public interest (WpK);
- Given that the Code cannot anticipate all possible circumstances, we recommend that a new provision be added to Section A of the Code (in lieu of proposed 100.11) which explains that it may be necessary in certain circumstances for the professional accountant and firm to apply professional judgement and to take a course of action even though it may not be in strict accordance with the letter of the Code (PwC); and
 - This provides the auditor and the client the ability to consider the need for a temporary departure of the requirements within a defined framework. In these limited and exceptional situations, the professional accountant and the audit or review client could consider whether an informed third party aware of the facts and circumstances would reasonably conclude that the departure does not impair the accountants' independence. We assume that the circumstances would be rare and that the accountant would resign or the departure corrected or cured in a timely manner (GTI).

Illustrative comments from those who disagreed with the paragraph are:

- Creating an overarching exception to all requirements as part of the Code, despite the setting of various conditions, could be seen to undermine the obligation which a 'shall' requirement is supposed to signify (CEBS);
- There does not appear to be any conceptual basis as to why such an exemption is required. It is our view that draft paragraph 100.11 seriously compromises the integrity of the Code and may lead to undesirable departures from the requirements and spirit of the Code (APESB);
- We have serious concerns that providing this departure provision in the Code is an introduction for potential abuse of compliance with the Code. Such provision would weaken the Code and is inconsistent with the conceptual framework. With the exception of environments which are extremely remote, having scarce resources, we cannot envisage circumstances which would support departure from compliance with the Code. The examples provided for application of Paragraph 100.11 do not provide adequate rationale to allow a firm to continue as the auditor for their client. The examples appear to be a rationale to protect the commercial needs of an individual firm or accountant. (BDO); and
- Would weaken the Code. . . We presume that the proposed exception to compliance with the Code has been drafted principally with regard to section 290 of the Code and not to other sections of the Code which generally contain few absolute prohibitions for which an exception might ever need to be contemplated. As stated earlier, we are concerned that the proposed exception to compliance with the Code will be seen to weaken the Code as it relates to auditors' independence. (KPMG).

Task Force Proposal

The Task Force considered the comments received. The Task Force noted that the majority of respondents supported the inclusion of an exception paragraph. The Task

Force noted that many of those that did not support the paragraph were concerned that it might weaken the Code. The Task Force is of the view that a paragraph is necessary and that concerns about it weakening the Code could be addressed through some changes to the drafting of the paragraph, as discussed under question 3(b) below.

IESBA Question

IESBA members are asked to consider the comments received regarding the need for an exception paragraph in the Code and determine whether they believe the Task Force proposal is appropriate.

ED Question 3b If you believe that the Code should contain a provision that permits an exception to compliance, are the conditions under which the exception would apply appropriate? Should there be additional or fewer conditions and, if so, what are they?

ED Responses

Responses to this question were very diverse. Five respondents (SAICA, MIA, ICPAS, FARS, AIA) expressed support for the exception as drafted. Other respondents felt that some of the conditions were not necessary or that there should be additional conditions. There was also comment regarding the positioning of the paragraph.

For reference, ¶100.11 in the ED stated:

In exceptional and unforeseen circumstances that are outside the control of the professional accountant, the firm or employing organization, and the client, the application of a specific requirement in the Code may result in an outcome that a reasonable and informed third party would not regard as being in the interest of the users of the output of the professional services. In such circumstances, the professional accountant may judge it necessary to depart temporarily from that specific requirement. Such a departure would be acceptable only if all of the following conditions are met:

- The professional accountant discusses the matter with those charged with governance; the discussion shall include the nature of the exceptional and unforeseen circumstance, the fact that the circumstance is outside the control of the relevant parties, why in the professional accountant's judgment it is necessary to depart temporarily from a specific requirement in the Code, and any safeguards that will be applied;
- The professional accountant documents the matters discussed with those charged with governance;
- The nature of the departure and the reasons for the departure are appropriately disclosed to the users of the output of the professional services; and
- The professional accountant complies with the requirements of the Code at the earliest date that compliance can be achieved.

The professional accountant may wish to discuss the matter with the relevant regulatory authority. If the accountant has such a discussion, the substance of that discussion shall be documented.

The following key comments were made:

Position of paragraph

- As drafted it only envisages an exception applying to audit work – it should therefore be moved to Section 290 (CARB, CIMA)
- Exception could be included in the preface (GTI)

Unforeseen Circumstances

- It is not necessary for the circumstances to be unforeseen (HKICPA, ACCA, WpK, IDW, FEE, CSOEC, DTT, AIA, PwC)

Outside Control of Professional Accountant, Firm or Employing Organization and Client

- Critical test is whether the exception is in the public interest therefore the “outside of control” test is not necessary (HKICPA)
- Outside control of client – would seem to unfairly punish an audit client that makes a business decision to acquire an entity to which its auditor is rendering a nonaudit service (AICPA) – [please also see discussion below on mergers]
- Events that are within the control of the relevant parties should qualify for the exception (JICPA)
- Such circumstances will be so rare that they give the professional accountant and the firm insufficient latitude to use their judgement in applying and complying with the fundamental principles in all circumstances in which it may be warranted. A better test would be whether a reasonable and informed third party would conclude that the fundamental principles have not been compromised (PwC, GTI)

Disclosure to Users of Output of Professional Services

- Unnecessary as the accountant has to have agreement of those charged with governance (HKICPA)
- Unnecessary given other conditions and would undermine the credibility and stature of the audit report (AICPA, FEE, PwC, DTT, GTI, JICPA)
- Uncertain whether the need to disclose the nature of the departure and the reasons for it to the users of the output of the professional services will necessarily be in the public interest (APB)
- Disclosure of the nature of the departure and the reasons for the departure could, in certain cases, be interpreted by the wider public as constituting a statement that a professional accountant has not complied with the Code of Ethics, which would not be the case, nor would it be in the public interest (IDW, FEE, WpK)
- It is unclear who would be the “users” and, in the case of a PIE, it may be impossible for the accountant to identify all of the users (IRBA)

- It may not be possible to provide appropriate disclosure to all of the users in every instance and we would suggest “users” be modified to “known users” or something similar (CICA).

Discussion with Relevant Regulatory Authority

- Should be mandatory (VSCPA)
- Should be mandatory and the regulatory body should be made aware of all the relevant facts and circumstances (IRBA)
- If the applicable regulator or the IFAC member body has established a process, whether formal or informal, for professional accountants to discuss conclusions reached with respect to independence issues, the professional accountant shall take the steps necessary to comply with such process, determine that the regulator or IFAC member body has no objection to the conclusions reached, and document the matters discussed (GTI, AICPA, PwC)

Task Force Proposal

The Task Force considered the responses to the question in determining what changes to the paragraph are appropriate.

Position of paragraph

The Task Force considered the purpose of the paragraph in the ED, which was to provide the accountant with guidance in dealing with unforeseen circumstances where the application of a specific requirement may result in an outcome that a reasonable and informed third party would not regard as being in the interest of the users of the output of the accountant’s services. The Task Force considered whether it would ever be appropriate to depart from a specific requirement such that compliance with one of the fundamental principles was compromised. The Task Force was unable to think of a circumstance where it would be appropriate for an accountant not to comply with the following fundamental principles:

- Integrity;
- Objectivity;
- Professional competence and due care;
- Confidentiality; and
- Professional behavior.

The Task Force is of the view that the paragraph is necessary mainly to address situations where the application of a specific independence requirement may produce a result that is not in the public interest and agreed that the paragraph would be most operational and most intuitive if viewed in the context of auditor independence. The Task Force, therefore, proposes that the paragraph be moved to section 290 (with an equivalent paragraph in section 291).

Scope of paragraph

The Task Force considered the comments of those who expressed concern that the paragraph in the exposure draft would be seen by some as weakening the Code. The Task Force concluded that a reasonable and informed third party would conclude that

application of a specific requirement was not appropriate only in circumstances where independence was not compromised – for example, because the accountant was able to apply alternative safeguards. The Task Force, therefore, concluded that before the accountant could take an action that was other than an action specifically required by a provision in the Code, the accountant would have to conclude that independence would not be compromised by taking the alternative action.

Unforeseen circumstances outside control of the relevant parties

In considering the exposure draft requirements that the circumstances be unforeseen and outside the control of the relevant parties, the Task Force concluded that these requirements were not necessary given the new proposed requirement that the accountant has to conclude that independence is not compromised. The Task Force, therefore, proposes that these requirements be deleted.

Disclosure to users of service

Several respondents expressed concern with the requirement in the exposure draft that “the nature of the departure and the reasons for the departure” be appropriately disclosed to the users of the output of the professional services. Respondents noted that, in the case of an audit report, this could be confusing and undermine the credibility of the report. The Task Force concluded that, in light of its recommendation that a “departure” be acceptable only if the professional accountant concludes that independence would not be compromised, such disclosure is not appropriate.

Discussion with relevant regulatory authority

The Task Force considered the comments from those who felt the discussion with a relevant regulatory authority should be mandatory, and reflected on the concern that the paragraph could be seen as weakening the Code. The Task Force concluded that, in the case of a public interest entity, the matter should be discussed with a relevant regulator and, if no such regulator was available, the matter should be discussed with a member body. In the case of an audit client that is not a public interest entity the matter should be discussed with the relevant member body. The Task Force recognizes that this proposed requirement does mean when there is neither a regulator nor a member body with whom to discuss the matter, a departure is not a possible.

Proposed re-drafted paragraph

In light of the above, the Task Force proposes that the paragraph be re-drafted as follows:

In exceptional circumstances, the application of a specific requirement in this section may result in an outcome that a reasonable and informed third party would not regard as being in the public interest. In such circumstances, the professional accountant may determine it is necessary to take an action, including applying safeguards, other than as specifically required in this section. Before taking the action, the professional accountant shall conclude that independence would not be compromised and:

- The professional accountant shall discuss the matter with those charged with governance; and

- In the case of an audit client that is a public interest entity, the professional accountant shall discuss the matter with the relevant regulator, which may be an audit regulator, and, where a relevant regulator is not available, with the relevant member body; or
- In the case of an audit client that is not a public interest entity, the professional accountant shall discuss the matter with the relevant member body.

The professional accountant shall document the substance of the discussions and the basis of the professional accountant's conclusion that independence would not be compromised.

IESBA Question

IESBA members are asked to consider the comments received regarding the content of the exception paragraph and determine whether they agree with the Task Force's proposed re-draft and re-positioning.

***ED Question 3(c)** If you believe that the Code should not contain a provision that permits an exception, please explain how you would deal with the types of exceptional and unforeseen situations that may be covered by paragraph 100.11.*

ED Responses

- We believe the relevant regulatory authority should apply judgment and address exceptional situations based on the facts and circumstances surrounding the situation (Basel)
- We believe that there is adequate guidance provided in paragraphs 100.1 – 100.10 and paragraphs 100.12 to 100.23, which make the proposed paragraph 100.11 unnecessary (IRBA)
- We would be supportive of a reasonable compliance transition period for problematic situations involving non-audit services for new clients or for entities acquired by existing audit clients... This would, however, need to be subject to the service being completed or terminated within a reasonable (say ninety days) period of time (KPMG) [Point is repeated below under 3(d)].

Task Force Proposal

In light of the comments received, as discussed above, the Task Force is of the view the Code should contain an exception paragraph and that it should be in sections 290 and 291.

ED Question 3(d) *Are there any other circumstances where you believe a departure from a requirement in the Code would be acceptable?*

ED Responses

- While we are contrary to a provision that permits an exception, we believe that business combinations is one situation that may give rise to instances where the strict adherence to the Code may be disadvantageous to the client and/or users (EYG, IDW, DTT, IRBA, BDO, PwC)
- We would be supportive of a reasonable compliance transition period for problematic situations involving non-audit services for new clients or for entities acquired by existing audit clients...This would, however, need to be subject to the service being completed or terminated within a reasonable (say ninety days) period of time (KPMG)
- Where an audit team member accepts gifts or hospitality that is other than trivial or inconsequential. In such a case, a violation of the Code occurs and the team member may not have inadvertently accepted the gift. The provision would seem to suggest that the auditor must resign, since there is no mention of the possibility to apply safeguards, including the possible safeguard of removing the individual from the audit team and having his or her work reviewed. (PwC, DTT)

Task Force Proposal

The Task Force considered the comments received and believes that it would be prudent to develop a provision that helps the accountant to deal with independence issues that might arise from a client's business acquisition. The Task Force intends to better understand business acquisition scenarios to assess matters such as (a) the extent to which such transactions become known to the accountant prior to consummation, (b) how that knowledge is typically gained, (c) how much time the accountant typically has to address potential independence issues that might arise from the transaction and whether that time is sufficient to take action to avoid independence violations of the Code, and (d) the types of safeguards that firms typically apply in such situations.

IESBA Question

IESBA members are asked to consider the comments received regarding additional circumstances where a departure would be acceptable and determine whether they believe the Code should address any of these matters, in particular business acquisitions.

ED Question 4 *The IESBA is of the view that the proposed modification to focus the application of the conceptual framework throughout the Code, and the related documentation requirements in Sections 290 and 291, on threats that are not at an acceptable level will result in a more efficient and effective application of the framework approach. Do you agree?*

ED Responses

The majority of respondents were supportive of the proposal. A few expressed the view that the documentation requirement should be strengthened.

	Member Bodies	Firms	Others
Supportive	AICPA, IDW, MIA, WpK, SAICA, FARS, ICPAS, CIMA, JICPA, HKICPA, ICAA/CPA Aus/ NIA, ICPAC, ICPAS, CICPA, CICA, NIVRA, ICAEW, ICAS	BDO, GTI, KPMG, EYG, DTT, RSM, PwC	RM, MS. VSCPA, AIA, CARB, CCAB,, LSCA, FEE
Supportive but documentation requirements need to be strengthened	ACCA, CNCC, CSOEC		APB, CEBS, Basel

Illustrative supportive comments are:

- We believe that the existing use of the terms “clearly insignificant” and “acceptable level” within the Code has the potential to create unnecessary ambiguity for accountants when applying the conceptual framework (RSM); and
- [The proposed change] will result in a more efficient and effective application of the framework approach (NIVRA).

Comments on documentation:

- There is a large degree of subjectivity required when assessing whether or not the threats are at an ‘acceptable level’, and so we believe that it is still necessary to document independence conclusions and related discussions in any situation where the threat is not trivial and inconsequential (ACCA)
- It would seem that documentation is only necessary where the auditor believes that a safeguard is needed. However, it would seem more robust to us if the auditor had to document the whole assessment, not just when safeguards are applied. And if this is what is intended it should be clearer in the paragraph (CEBS, Basel)
- Delete the phrase “even though documentation is not a determinant of whether a firm is independent” (CEBS, Basel)

- The accountant should document that analysis of the threats and how he accountant concluded the threats were at an acceptable level (CNCC, CSOEC)
- The documentation should include
 - all threats identified, other than those which are trivial and inconsequential, and the process used in identifying them;
 - safeguards adopted and the reasons why they are considered to be effective;
 - conclusions from any review by an engagement quality control reviewer or an independent partner;
 - the audit engagement partner's overall assessment of threats and safeguards; and
 - matters communicated with those charged with governance regarding auditor independence issues. (APB)

Task Force Proposal

The Task Force has considered the responses to this question and proposes changes to the independence requirements to address the comments.

¶290.29 in the ED read:

“Even though documentation is not, in itself, a determinant of whether a firm is independent, conclusions regarding compliance with independence requirements, and any relevant discussions that support those conclusions, shall be documented. Documentation of independence conclusions and related discussions prepared to meet the requirements of international standards on auditing will meet this requirement. When threats to independence are identified that require the application of safeguards, the documentation shall also describe the nature of those threats and the safeguards applied to eliminate them or reduce them to an acceptable level.”

The Task Force proposes that it be changed to two paragraphs that read as follows:

“Documentation provides evidence of the professional accountant’s judgments in forming conclusions regarding compliance with independence requirements; it is not a determinant of whether a firm is independent.

The professional accountant shall document conclusions regarding compliance with independence requirements, and the substance of any relevant discussions that support those conclusions. When threats are identified that require the professional accountant to determine whether safeguards are necessary to reduce them to an acceptable level, the professional accountant shall also document the nature of those threats and safeguards, if any, applied.”

IESBA Question

IESBA members are asked to consider the comments received and determine whether they agree with the Task Force’s proposed change.

Effective Date

IESBA members will be asked to consider comments regarding the effective date at a subsequent meeting.

Material Presented

Agenda Paper 3	This Agenda Paper
Agenda Paper 3-A	Detailed cut and paste of comments
Agenda Paper 3-B	Exposure Draft

Action Requested

1. IESBA members are asked to consider the questions contained in the agenda paper.

Appendix

As at November 11, 2008 the following comment letters had been received. The content of these comment letters is included in the detailed cut and paste of comments which is included in Agenda Paper 3-A.

Legend

AAT	Association of Accounting Technicians
ACCA	Association of Chartered Certified Accountants
AIA	Association of International Accountants
AICPA	American Institute of Certified Public Accountants
APB	Auditing Practices Board (UK)
APESB	Accounting Professional and Ethical Standards Board – Australia
Basel	Basel Committee on Banking Supervision
BDO	BDO Global Coordination B. V.
CARB	Chartered Accountants Regulatory Board – Ireland
CCAB	The Consultative Committee of Accountancy Bodies
CEBS	Committee of European Banking Supervisors
CICA	Canadian Institute of Chartered Accountants
CICPA	Chinese Institute of Certified Public Accountants
CIMA	Chartered Institute of Management Accountants
CNCC	Compagnie Nationale des Commissaires aux Comptes
CSOEC	Conseil Supérieur de l'Ordre des Experts-Comptables
DTT	Deloitte Touche Tohmatsu
EYG	Ernst & Young Global Limited
FARS	The Institute for the Accountancy Profession in Sweden
FEE	Federation des Experts Comptables Europeens
GTI	Grant Thornton International
HKICPA	Hong Kong Institute of Chartered Accountants
ICAA/CPA Aus/ NIA	The Institute of Chartered Accountants in Australia/ CPA Australia/ National Institute of Accountants in Australia
ICAEW	The Institute of Chartered Accountants in England and Wales
ICAS	Institute of Chartered Accountants of Scotland
ICPAC	The Institute of Certified Public Accountants of Cyprus
ICPAS	Institute of Public Accountants in Singapore
IDW	Institut der Wirtschaftsprüfer (Germany)
IIA	Institute of Internal Auditors
IRBA	Independent Regulatory Board for Auditors
JICPA	Japanese Institute of Certified Public Accountants
JM	Joseph Maresca
KICPA	Korean Institute of Certified Public Accountants
KPMG	KPMG
LSCA	London Society of Chartered Accountants
NASBA	National Association of State Boards of Accountancy
MIA	Malaysian Institute of Accountants
MS	Mark Shum

NIVRA	Koninklijk Nederlands Instituut van Registeraccountants (Royal NIVRA)
PwC	PricewaterhouseCoopers
RM	Ramachandran Mahadevan
RSM	RSM International
SAICA	South African Institute of Chartered Accountants
VSCPA	Virginia Society of Certified Public Accountants
Wpk	Wirtschaftsprueferkammer

Outstanding comment letter

IOSCO	International Organization of Securities Commissions
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