



Technical Director  
International Ethics Standards Board for Accountants  
International Federation of Accountants  
529 5<sup>th</sup> Avenue, 6<sup>th</sup> Floor  
New York 10017

March 24, 2016

**Re: IESBA Exposure Draft – Proposed Revisions Pertaining to Safeguards in the Code – Phase 1**

Dear Mr Siong

**Introduction**

We<sup>1</sup> appreciate and thank you for the opportunity to comment on the IESBA’s Exposure Draft “Proposed revisions pertaining to Safeguards in the Code – Phase 1”

**Principal comments**

Overall, we believe that the proposed changes to the code will provide appropriate and enhanced guidance for professional accountants and will help with an understanding of the Code and its intended application.

We do have some comments, however, and are responding to the proposals on an exception basis, as below. These comments largely relate to Question 1 posed by the Board.

**“Overall Assessment”**

We support the need to identify, evaluate and address threats to compliance with the fundamental principles and to re-evaluate threats if there are changes in the relevant facts and circumstances.

The proposal includes the concept of an “overall assessment” in the description of the Conceptual Framework in Part A of the Code paragraph R120.9.

We understand that this proposal is a response to the comment from IOSCO in its letter to the Board of 30 January 2015 (extract below for ease of reference) and which refers to the need for a “step back”.

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<sup>1</sup> This response is being filed on behalf of PricewaterhouseCoopers International Limited (PwCIL). References to “PwC”, “we” and “our” refer to PwCIL and its global network of member firms, each of which is a separate and independent legal entity.

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*..., in practice, on more than an infrequent basis, auditor oversight and securities regulators have encountered auditors who attempt to justify their actions by indicating compliance with the requirements without stepping back to determine if the facts and circumstances suggest that the fundamental principles may be violated though the requirements were achieved.*

*The fundamental principles are not simply background information but are overarching objectives that auditors must meet whereas the standards-specific requirements capture specific areas identified by the Board to which auditors must comply. We believe greater emphasis should be placed on the need for auditors to step back after complying with the standards-specific requirements to determine if, based on the facts and circumstances, the auditor is independent with respect to the fundamental principles which, pursuant to our suggestions above, could serve as and be called overall objectives.*

This comment was evidently made in the context of an audit of financial statements and the related independence requirements. However, R120.9 applies both to Professional Accountants in Professional Practice and those in Business.

Our concerns with the provision as drafted are as follows:

1. It is not clear whether the assessment is to be performed in relation to a specific threat or in terms of the overall relationship/engagement with the client/employer.
2. If the former, it is not evident what such an assessment achieves if the facts and circumstances have not changed subsequent to the initial process of identifying and addressing the threat.
3. It is not clear when this overall assessment is to be undertaken. This is particularly challenging in the case of those accountants “in business” who have an ongoing relationship with the employing organisation.
4. The additional documentation requirements are unclear.

Our understanding is that the provision is intended to be a requirement to “step back” and look at the “totality” of the facts and circumstances that may create threats to compliance with the fundamental principles, as may be appropriate, for example, in forming a conclusion at the end of an audit or in managing a conflict of interest.

We see this as particularly challenging to describe and apply when there is not a specific engagement or relationship to consider, such as will generally be the case for professional accountants in business and we recommend that the Board specifically re-considers, and clarifies, application by accountants in business. How, for example, will this assessment be replicated in revised Section B?

The concept of the “overall assessment” is also included in Section 300, Application of the conceptual framework by Professional Accountants in Professional Practice:

*When applying the conceptual framework, Section 120 requires that the professional accountant reviews judgments made and overall conclusions reached to determine that threats to compliance with the fundamental principles are eliminated, or reduced to an acceptable level*



*and that no further action is needed. The reasonable and informed third party test described in Section 120 is relevant to this assessment.*

This proposal is contained in Part C, 300.2 A12 as application material. This would apply in the context of all the relevant sections of Part C, such as that relating to managing conflicts of interest and may have most relevance in the context of applying the independence requirements. We assume that this will be further replicated in C1 (dealing with audits) in due course.

We agree that an overall assessment makes sense in the context of an audit or assurance engagement (or other engagement specific circumstance), but we remain concerned about the matters set out above (see items 1 to 4). Overall, we believe that greater clarity is needed (in all Parts of the Code) to address the points above, including the practicalities for the professional accountant as to when this assessment is to be undertaken, the focus of the assessment, and what might be expected in terms of documentation beyond the initial documentation of identifying and addressing threats to the fundamental principles.

In the context of the independence requirements, we believe that the need for an overall assessment or conclusion is largely covered by the ISA 220, as this requires the engagement partner to form a conclusion on independence requirements.

***Relevant Ethical Requirements***

*9. Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team.*

*10. If matters come to the engagement partner's attention through the firm's system of quality control or otherwise that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action.*

***Independence***

*11. The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement.*

We recognise that this Phase 1 ED does not address application in the context of independence but we feel that it is useful to make this comment now. As the Board reflects on the responses to this ED, we encourage the Board to work with the IAASB to ensure that there is alignment between the Code and the relevant ISA and to avoid any differences or unnecessary duplication.

We note that in 300.2 A1 the emphasis is on the “professional accountant” who is defined in the extant Code as an individual who is a member of an IFAC member body. This places the responsibility on an individual, whereas in practice it may be more appropriate for the “firm” or “an engagement team” to undertake the activities required in the code. Further, as structured, it has the possibility that a client engagement team comprising a number of



professional accountants would individually be required to comply with a requirement. This would be duplicative and unnecessary in our view.

### **Identifying threats**

Proposed paragraph 300.2A1 provides examples of facts and circumstances that might create threats to compliance with the fundamental principles. This Section 300 applies to all activities and services provided by the professional accountant in public practice.

The vast majority of the examples presented relate to facts and circumstances that create threats to independence and not to compliance with the fundamental principles.

We recommend that the Board re-consider this list of examples and focus more specifically on those that are threats to compliance with the fundamental principles (and not threats to independence). All the proposed examples relate to objectivity (and/or independence) and there is no obvious reference to threats to compliance with the other four principles. We believe that all the fundamental principles should be addressed in the examples.

The illustration could usefully be organised by fundamental principle, and then perhaps by type of threat to each. This would also help to address the point made by IOSCO regarding an overall focus on the fundamental principles. Examples include:

Objectivity - The interests of the professional accountant with respect to a particular matter and the interests of the client for whom the professional accountant provides a professional service related to that matter are in conflict.

Professional Competence - the professional accountant lacks the professional knowledge and skill required to ensure that a client or employer receives competent professional service.

The first of these clearly has the potential to create a self-interest threat. The second demonstrates the difficulty, at times, of establishing a clear link between the facts and circumstances and a threat to compliance with the fundamental principles (other than objectivity). None of the five threats seem relevant in terms of compliance with that fundamental principle.

Such a re-emphasis could also help many users of the Code whose predominant activity or service is not audit.

Furthermore, as proposed, by “generalising” a circumstance contained in the extant code we believe that the list suggests that such threats are created in a broader context. For example, in the extant code of “A member of the assurance team having a direct financial interest in the assurance client”, which is relevant in the context of C1, has been converted to “A professional accountant having a direct financial interest in a client”. A reading of this, even in the context of C1, could infer that interests of all the audit firm’s personnel need to be considered, rather than being limited to those who are addressed by the current Code, such as those on the audit team.



## **Evaluating threats**

We plan to comment on the proposed term “International Independence Standards” in our response to the Board’s ED on Structure of the Code.

Proposed 300.2 A6 contains a number of examples of environmental factors that may impact the level of a threat. We have the following observations:

- (a) The notion in the first bullet could usefully be mentioned in 300.2 A4 which addresses the client’s operating environment, such that “Leadership of the client entity promotes compliance with the fundamental principles”. This can impact the level of a threat to the professional accountant in public practice.
- (b) The fifth example is “*The engagement partner having authority for compliance with the fundamental principles, including decisions about the permissibility of services to an audit client*”. We do not see how this affects the level of a threat as it seems to focus on a process and further seems to place inappropriate responsibility in the hands of one individual. Having such “authority for compliance” is not clear and we suggest this needs clarification, if retained.
- (c) The last example could usefully extend to “concerns”, as a formal “complaint” may not always arise.

## **Addressing threats**

We have the same concerns regarding paragraph 300.2 A9 as we have with 300.2 A1 above, in that at least four of the six examples derive from the independence section of the Code. While we believe that these are effective safeguards, we recommend that the examples are reviewed in the light of the comments above and that the examples are mapped to such revised examples, focusing on addressing threats to compliance with the fundamental principles (and not threats to independence in the main).

## **Reasonable and Informed Third Party (Question 2)**

Paragraph 120.4 A1 introduces the concept of a “reasonable and informed third party”. While we concur with the underlying principle, we are concerned that the evaluation entails weighing what the accountant “knows or could reasonably be expected to know” at the time. A third party assessment with the benefit of hindsight might come to a different conclusion. This is particularly true given an uncertainty or expectation gap generated by the words “expected to know”. We believe that this goes beyond a judgement that the accountant can reasonably be expected to make.

Moreover, we note that the same principle adopted in the NOCLAR project is expressed differently - “*In determining the need for, and nature and extent of, further action, the professional accountant shall exercise professional judgment and take into account whether a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at the time, would be likely to conclude that the professional accountant has acted appropriately in the public interest.*”



We believe that the concepts should be consistent and recommend alignment with the NOCLAR wording.

**Contact**

If you would like to discuss any of the points raised in this letter, please contact either Jan McCahey (Tel +44 (0) 20 7212 2535 or email [jan.e.mccahey@uk.pwc.com](mailto:jan.e.mccahey@uk.pwc.com)) or Andrew Pinkney (Tel +44 (0) 20 7804 2852 or email [andrew.c.pinkney@uk.pwc.com](mailto:andrew.c.pinkney@uk.pwc.com)). We appreciate that it may be helpful to discuss some of these complex issues in person and would be very happy to do so.

Yours sincerely,

A handwritten signature in black ink that reads 'Jan McCahey' in a cursive, flowing script.

Jan McCahey  
Global Regulatory Leader