

**Minutes of the Meeting of the
Ethics Committee of the International Federation of Accountants
Held on September 20-21, 2004
In Helsinki, Finland**

	Members	Technical Advisors
<i>Present</i>	Marilyn Pendergast (Chair)	Lisa Snyder
	Frank Attwood	
	Christine Catasta	
	Mark Fong	
		Andrew Pinkney
	Richard George (Deputy-chair)	
	Akira Hattori	
	Thierry Karcher	Jean-Luc Doyle
	Neil Lerner	Tony Bromell
	Pekka Luoma	Jouko Ilola
	Wim P Moleveld	
	Russell Philp	Tiina-Liisa Sexton
	Jean Rothbarth	
	Hubert Graf Von Treuberg	Tim Volkmann
	David Winetroub	Peter Hughes
	Donald G Wray	John Babiak

IFAC Board Liaison

Jean-Francois Cats

IFAC Technical Staff

Present: Jim Sylph (Technical Director)
Jan Munro

Regrets David Devlin Heather Briers
Stephen Chan

1. Introduction and Administrative Matters

The chair opened the meeting and welcomed all those attending. The chair noted that David Devlin had sent his apologies and had given his proxy to Andrew Pinkney. The Committee approved the minutes of the May 2004 meeting.

2. Code Redraft

The Committee reviewed the proposed changes to the *Code of Ethics for Professional Accountants* to address the comments received on exposure and the Committee's comments at the previous meeting.

The Committee noted that:

- The preface had been restructured to refer to the role of IFAC and member bodies;
- The introduction to Section A had been expanded to provide more explanation on the application of the conceptual framework; and
- The proposed draft was less repetitive than the exposure draft.

The Committee discussed how the Code addressed how conflicts of interest could pose threats to the fundamental principles. While there were not a large number of comments received on exposure relating to conflicts of interest, it was noted that this is an area that creates challenges in practice and additional guidance in this area would be appropriate. The Committee agreed that it would be appropriate, as resources permit, to start a project in this area. The Committee directed staff to develop a project proposal to address conflicts of interest.

With respect to the Code, the Committee agreed that paragraph should 220.3 should be clarified to state that, depending on the circumstances giving rise to the conflict, one of three specific safeguards should ordinarily be applied to reduce the threat. All three safeguards would require obtaining consent to act.

The Committee discussed Section 110 that deals with integrity. The Committee noted that some respondents had expressed concern with how the section could be interpreted. The section states that a professional accountant should not be associated with reports and returns where they believe that the information contains a materiality false or misleading statement. It was noted that a professional accountant in public practice who issues a modified audit report on financial statements would, under auditing standards, be considered to be associated with the financial statements. The Committee agreed that the Code should contain a statement that a professional accountant would not be considered to be in breach of the integrity requirements when issuing a modified report.

The Committee approved the proposed changes to the Code (16 in favor, 0 against). The Committee agreed that in light of the changes to Section 290 (independence) it was appropriate to re-expose the whole Code to permit people to understand the changes to independence in context of the whole Code. The Committee noted that the re-exposure draft should solicit comment on only those new changes to Section 290 and should

clearly state that comment was not requested on the sections which had already been exposed.

The Committee considered the appropriate exposure period and concluded that, in light of the conforming nature of the changes to Section 290, a short exposure period would be appropriate. This would, subject to comments received, provide the Committee with the opportunity to approve the final Code at its February 2005 meeting.

3. Independence for Assurance Engagements

The Committee reviewed the proposed changes to Section 290 (Independence) to conform to the IAASB Assurance Framework and to the definitions contained in ISQC1 *Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements*.

The Chair reported that she, Jean Rothbarth and Jan Munro, had met with the IAASB to obtain their views on the proposal of the Ethics Committee Task Force to conform the Code to the new Assurance Framework. They had indicated that the Ethics Committee had not yet discussed the proposal of the Task Force. The intention was to focus the guidance in the Code on assertion-based engagements. This approach was proposed because the vast majority of assurance engagements performed by professional accountants in public practice are assertion-based engagements. The Task Force was also concerned that in direct-reporting engagements where the professional accountant directly evaluates or measures the subject matter the self-review threat created might be so significant that safeguards would not be available to reduce the threat to an acceptable level.

The IAASB discussed some of the differences between assertion-based and direct reporting engagements. It identified a number of engagements that would be considered to be direct-reporting engagements but for which it seemed clear that there was in fact an underlying assertion by management or some other reason to consider that the self-review threat could be reduced to an acceptable level by the application of appropriate safeguards. The IAASB suggested that the Ethics Committee may wish to include a statement in the Code that before accepting a direct reporting engagement the professional accountant in public practice should consider any self-review threat and, if such a threat exists, should apply safeguards to reduce the threat to an acceptable level.

At the May 2004 meeting, the Ethics Committee was concerned that the proposed changes to conform to the Assurance Framework were too complex and requested the Task Force to reconsider the draft and simplify the approach.

The Committee considered the draft presented by the Task Force and noted the following:

- Some of the introductory paragraphs had been re-ordered so that the description of independence is towards the beginning of the section;
- The revised draft contained a description of an assurance engagement, described the difference between subject matter and subject matter information and

- described the difference between an assertion-based engagement and a direct reporting engagement;
- The draft focused on assertion-based engagements stating that direct reporting engagements are not commonly performed by professional accountants in public practice; and
 - The draft dealt separately with financial statement audit engagements, other assertion-based engagements and restricted use reports.

The Committee agreed that it was appropriate that the Code focus primarily on assertion-based engagements since these were most common. The Committee expressed concern however, with the proposed draft, believing that it was still too complex.

The Committee discussed the proposed paragraphs that describe an assurance engagement, subject matter and subject matter information and distinguish between an assertion-based and a direct reporting engagement. The Committee concluded the paragraphs did not provide sufficient guidance to a professional accountant in public practice as to the various aspects of an assurance engagement and did not help the accountant to distinguish what was and what was not an assurance engagement. The Committee concluded that an accountant would need to consult the Framework for such guidance. Accordingly, the Committee agreed that these paragraphs should be removed from the Code.

The Committee discussed the distinction between assertion-based and direct reporting engagements. The Committee noted that it would be particularly useful to have examples of the different types of engagement that:

- Illustrated the difference between an assertion-based and a direct reporting engagement;
- Illustrated the difference between subject matter and subject matter information; and
- Described engagements where there were two different responsible parties.

The Committee felt that such examples would assist practitioners in applying the Framework and, had they been available to the Committee, would have assisted in the determination of appropriate independence requirements. The Committee concluded that it would be appropriate to write to the IAASB encouraging them to develop such examples.

The Committee discussed whether the Code should explicitly reference the engaging party and the intended user. After discussion, the majority of the Committee concluded that given the wide variety of assurance engagements it was not necessary to explicitly reference these parties in the Code, rather it was appropriately dealt with through the general requirement to identify threats to independence.

The Task Force discussed the paragraphs dealing with assertion-based and direct reporting engagements. Some members questioned whether it was necessary to separately deal with assertion-based and direct reporting engagements noting that this added to the complexity of the Code. It was also noted that requiring independence from the party responsible for the subject matter information in an assertion-based engagement and the party

responsible for the subject matter in a direct reporting engagement was confusing and would likely not be understood by users of the Code. After discussion the majority of the Committee concluded that the Code should not differentiate between assertion-based and direct reporting engagements, rather the Code should reference other assurance engagements that are not financial statement audit engagements. For these engagements, the assurance team and the firm would be required to be independent from the party responsible for the subject matter information.

The Committee discussed the Task Forces proposed changes to conform certain definitions to those contained in ISQC1 and to require rotation of the individual responsible for the engagement quality control review. The Committee agreed with the Task Force's proposal.

The Committee approved, for exposure, the changes to the Code [13 in favor, 3 opposed].

4. Project Proposals

The Committee discussed three project proposals which had been reviewed by the Planning Committee and were presented for the consideration and approval of the Committee.

Independence Re-visit

The existing independence requirements were issued in November 2001. Since that time there has been a loss of credibility in financial reporting and many jurisdictions have taken steps to address this loss in credibility. Some of these steps have related to auditor independence. In addition, IOSCO has indicated that the independence requirements should be reviewed.

The Committee approved the project which will gather information on implementation from member bodies and firms and will specifically consider:

- Clarity of prohibitions;
- Scope of services;
- Rotation; and
- Application to public interest entities.

Ethical Guidance for Members in Government

The Committee approved a project which would develop independence guidance for public accountants in government who perform assurance engagements and determine whether any additional guidance should be provided in Part C for professional accountants in government.

It was noted that because none of the Committee members work in government it would be important to recruit some task force members with this particular experience.

Ethical Guidance for Professional Accountants When Encountering Fraud or Illegal Acts

The Committee considered a project proposal to develop further guidance in the code for situations where a professional accountant encounters fraud or illegal acts. The

Committee concluded that a project should be undertaken but that it should be restricted to professional accountants in business because professional accountants in public practice face particular confidentiality requirements.

The Committee approved the project to address only public accountants in business.

5. Due Process

Planning Committee Terms of Reference

The Committee discussed the Planning Committee proposed terms of reference. Some Committee members questioned why a planning committee was needed and expressed concern that as drafted the terms of reference were taking away authority from the full Committee. The Deputy-Chair noted that was not the intent, rather the Planning Committee would do some of the preparatory work for the full Committee. For example, the Planning Committee reviewed the project proposals before they were brought to the full committee for discussion and approval. The chair noted that the establishment of such a committee is of support to chair because it provides the chair with a forum to develop ideas before bringing them to the full committee.

Due Process

The Committee discussed a draft description of due process that had been prepared by staff and reviewed by the Planning Committee. The Committee agreed with the Planning Committee's view that it was not necessary to have as extensive a due process document as that prepared by the IAASB. It also agreed that it was not necessary to expose the document. Subject to a few suggestions, the Committee approved the description and asked staff to post it on the web-site.

[Staff note: subsequent to the meeting the IFAC Board determined it would be desirable for the three IFAC PIACs to have the same due process description. Therefore, the document was not posted on the web-site and the matter will be discussed further at the February 2005 Ethics Committee meeting].

6. Communications with Those Charged with Governance

The Committee considered an extract of a draft of an IAASB exposure draft to revise ISA 260 *Communications with Those Charged with Governance*. The Committee noted several items that it asked staff to communicate to the IAASB:

- the proposed requirement to communicate all audit and non-audit fees charged to related entities was too broad, since this would include for, example, non-audit fees to an entity that has indirect control over the client;
- the need to communicate total fees is less important in small entities where there is little distinction between management and those charged with governance; and
- it might be difficult to know how to disclose the total fees that have been “contracted or bid for”.

7. Closing

The chair thanked the Finnish Institute for their hospitality and members, technical advisors and staff for their input, and closed the meeting.

The Committee collectively thanked Marilyn Pendergast for her outstanding contribution to the Committee first as a member and then as Chair of the Committee.

8. Future meeting date

February 14-15, 2005 – New York USA