

# Agenda Item 4



**Meeting Location:** Conrad Ballroom, Conrad Hotel, Dublin, Ireland

**Meeting Date:** February 20-22, 2012

## Revised IESBA Strategy

### Objective of Agenda Item

1. To discuss and approve a revision to the IESBA strategy.

### Overview

The Planning Committee is recommending that the IESBA undertake the activities described in this memo in view of ongoing regulatory scrutiny of the auditing profession and related standard setting proposals in Europe and the US, as well as recent events involving certain publicly reported financial accounting irregularities that may have ethics implications. The activities will better position the IESBA as a leading international standard setter of ethics rules for the accounting profession, and further its objective of international convergence of national rules with those of the Code, the Planning Committee recommends that the actions described herein be taken.

### Background

The 2008 global financial crisis prompted increased scrutiny by regulators, policy makers, and legislators of the financial reporting system, including the auditing profession. That scrutiny has resulted in certain proposed changes to improve the independence of auditors. The pace of change is occurring at a record pace. For example, the European Commission (EC) proposed changes to its auditor independence rules in 2010. Last year it issued proposed legislation that contains many significant changes. Among them are principally *mandatory firm rotation* and a complete *prohibition of non-assurance services* by auditors to their audit clients.

In the UK, the House of Lords, a chamber of the UK Parliament that shares law making with the House of Commons, published in 2011 a report on the role and future of the external audit. Its consideration of the auditing profession continues and the UK's Auditing Practices Board has been actively considering how it might strengthen its auditor independence rules.

In the US, the Public Company Accounting Oversight Board issued a concept release in 2011 to explore ways to improve auditor objectivity, independence, and skepticism. The concept release focused on mandatory firm rotation as the way to achieve that objective. The Times of India recently reported that the Indian government is planning a review of the audit and financial services sector to guard against corporate frauds and irregularities. Included among its plans is prohibiting audit firms from providing certain non-audit services to their audit clients.

In addition, reports of corporate accounting irregularities, most recently at Olympus Corp., continue to appear in the financial press. The Planning Committee believes it is important for the board to understand the facts involved in those situations in order to assess their ethical implications and determine whether the Code could be strengthened to promote greater protection of the public interest by professional accountants in business.

### **Recommendation**

The measures under consideration by regulators and others have global implications. None have been considered by the IESBA as part of its due process procedures. The Planning Committee believes that for the IESBA to properly exercise its authority as a global standard-setter of ethics rules for accountants, it must have a position on those measures. It also must seek to understand the factors within a reporting entity that may have contributed to corporate accounting irregularities and determine whether improvements to the Code could be made to promote behavior by professional accountants in business that will reduce the likelihood of such occurrences.

The board's Strategy and Work Plan for 2011/ 2012 states

“... events and circumstances may require us to amend our [work] plan, and for this reason it will be kept under constant review.”

The Planning Committee believes that the events described above are the types of events and circumstances encompassed by that statement. Accordingly, the Planning Committee recommends that the IESBA consider the independence-related measures being debated by the EC and PCAOB. Doing so will enable the IESBA to demonstrate leadership for member bodies of IFAC who are entitled to look to the IESBA to take the lead in determining whether and how the Code should be revised in light of these activities. Thus, the objective should be to determine what the board's position is regarding each of the significant measures that are within its purview, whether changes to the Code are warranted, and, if so, engage in due process and deliberation to bring about those changes. Likewise, the board must take the lead in assessing the ethical implications of recent corporate accounting irregularities and determine whether the Code could be strengthened to promote greater protection of the public interest by professional accountants in business.

The Planning Committee believes this action is consistent with the IESBA's Terms of Reference, which state:

The IESBA's objective is to serve the public interest by setting high-quality ethics standards for professional accountants and by facilitating the convergence of

international and national ethics standards, thereby enhancing the quality and consistency of services provided by professional accountants throughout the world and strengthening public confidence in the global accounting profession.

### **Matter to Address**

*Non-assurance services* - When considering the EC's proposal to ban all non-assurance services, the board should consider whether the Code's position on non-assurance services remains appropriate, including the use of materiality. If certain non-assurance services are permitted, the board might consider whether they should be subject to pre-approval by those charged with governance, restricted in size in relation to the audit fee, or publicly disclosed.

*Rotation* - When considering firm rotation, the board should include consideration of the time period for rotation and whether rotation should apply for all public interest entities or only certain entities (for example, by type of industry, listed entities, or entities of a certain size). The board also should consider whether the Code's position on key audit partner rotation remains appropriate, including whether the requirement to rotate off of the audit engagement after serving seven years as a key audit partner and then observe a two-year time out period continues to be appropriate.

*Professional accountants in business* - The board should perform research to understand the facts surrounding recent corporate accounting irregularities. The results of the research will help inform the Board's Strategy and Work Plan for 2013 and 2014.

### **Resources**

In order for the IESBA to undertake these actions, at a minimum the board will need a fourth meeting this year and likely in one or more subsequent years. The chair intends to discuss the board's resource needs, such as for the new task forces and a research group, with the IFAC Board of Directors at its March meeting.

### **Material Presented**

Agenda Paper 4                      This Agenda Paper

### **Action Requested**

1. IESBA members are asked to discuss and provide input on the Planning Committee's recommendation.