

### Proposed Changes to the *Code of Ethics for Professional Accountants* Addressing Conflicts of Interest

#### Clean Version

*Paragraphs 100.17-100.18 and their heading below would be inserted before the heading Ethical Conflict Resolution and extant paragraphs 100.17-100.22 would be renumbered as paragraphs 100.19-100.24.*

#### *Conflicts of Interest*

100.17 A professional accountant may be faced with a conflict of interest when undertaking a professional activity<sup>1</sup>. A conflict of interest creates a threat to objectivity and may create threats to the other fundamental principles. Such threats may be created when:

- The professional accountant provides a professional service related to a particular matter for two or more parties whose interests with respect to that matter are in conflict; or
- The interests of the professional accountant with respect to a particular matter and the interests of a party for whom the professional accountant undertakes a professional activity related to that matter are in conflict.

100.18 Parts B and C of this Code discuss conflicts of interest for professional accountants in public practice and professional accountants in business, respectively.

#### SECTION 220

#### Conflicts of Interest

*Paragraphs 220.1-220.6 would be deleted and replaced with the following paragraphs 220.1-220.10:*

220.1 A professional accountant in public practice may be faced with a conflict of interest when performing a professional service<sup>2</sup>. A conflict of interest creates a threat to objectivity and may create threats to the other fundamental principles. Such threats may be created when:

- The professional accountant provides a professional service related to a particular matter for two or more clients whose interests with respect to that matter are in conflict; or
- 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.

A professional accountant shall not allow a conflict of interest to compromise professional or business judgment.

When the professional service is an assurance service the professional accountant in public practice shall also comply with the independence requirements of Sections 290 and 291 as appropriate.

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<sup>1</sup> **New Definition:** Professional Activity: An activity requiring accountancy or related skills undertaken by a professional accountant, including accounting, auditing, taxation, management consulting, and financial management.

<sup>2</sup> **Revised Definition:** Professional Services: Professional activities performed for clients.

220.2 Examples of situations in which conflicts of interest may arise include:

- Providing a transaction advisory service to a client seeking to acquire an audit client of the firm, where the firm has confidential information that may be relevant to the transaction;
- Advising two clients at the same time who are competing to acquire the same company where the advice might be relevant to the parties' competitive positions;
- Providing services to both a vendor and a purchaser in relation to the same transaction;
- Preparing valuations of assets for two parties who are in an adversarial position with respect to the assets;
- Representing two clients who are in a legal dispute with each other, such as during divorce proceedings or the dissolution of a partnership;
- Providing an assurance report for a licensor on royalties due under a licence agreement when at the same time operating the accounts payable system for the licensee;
- Recommending a client to invest in a business in which a family member of the professional accountant in public practice has a financial interest;
- Advising a client on its competitive position while having a joint venture or similar interest with a major competitor of the client;
- Advising a client on the acquisition of a business which the firm is also interested in acquiring;
- Advising a client on the purchase of a product or service while having a royalty or commission agreement with one of the potential vendors.

220.3 When identifying and evaluating the interests and relationships that might create a conflict of interest and implementing safeguards, when necessary, to eliminate or reduce any threat to compliance with the fundamental principles to an acceptable level, a professional accountant in public practice 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 compliance with the fundamental principles is not compromised.

220.4 When addressing conflicts of interest including making disclosures or sharing information within the firm or network and seeking guidance of third parties, the professional accountant in public practice shall remain alert to the fundamental principle of confidentiality.

220.5 If safeguards cannot eliminate the threat to objectivity and any threat to compliance with other fundamental principles created by a conflict of interest or reduce it to an acceptable level, the professional accountant in public practice shall decline to perform or shall discontinue professional services that would result in the conflict of interest; or terminate certain relationships or dispose of certain interests to eliminate the conflict.

220.6 Before accepting a new client relationship, engagement, or business relationship, a professional accountant in public practice shall take reasonable steps to identify circumstances that might create a conflict of interest including identification of:

- The nature of the relationships between the parties involved and the nature of any relevant interests; and
- The nature of the service and its implication for relevant parties.

The nature of the services and the relevant relationships may change during the course of the engagement. This is particularly true when a professional accountant is asked to conduct an engagement in a situation that may become adversarial, even though the parties who engage the professional accountant may not initially be involved in a dispute. The professional accountant shall remain alert to such changes for the purpose of identifying circumstances that might create a conflict of interest.

220.7 For the purpose of identifying relationships that might create a conflict of interest, having an effective conflict identification process assists a professional accountant in public practice to identify potential conflicts prior to accepting an engagement and throughout an engagement. This includes matters notified by external parties, for example clients or potential clients. The earlier a potential conflict is identified, the greater the likelihood of the professional accountant being able to apply safeguards, when necessary, to eliminate the threat to objectivity and any threat to compliance with other fundamental principles or reduce it to an acceptable level. The process to identify potential conflicts of interest will depend on such factors as:

- The nature of the professional services provided;
- The size of the firm;
- The size and nature of the client base; and
- The structure of the firm, for example the number and geographic location of offices.

If the firm is a member of a network, conflict identification shall extend to any conflicts of interest that the professional accountant knows or has reason to believe may exist or might arise due to interests and relationships of a network firm, having made enquiries as appropriate. The extent of enquiries will depend on such factors as the nature of the professional services provided, the clients served by the network and the geographic locations of all relevant parties.

220.8 If a conflict of interest is identified, the professional accountant in public practice shall evaluate:

- The significance of relevant interests or relationships; and
- The significance of the conflict of interest created by performing the professional service or services. In general, the more direct the connection between the professional service and the matter on which the parties' interests are in conflict, the more significant the conflict of interest will be.

220.9 The professional accountant in public practice shall apply safeguards, when necessary, to eliminate or reduce the threats to compliance with the fundamental principles created by the conflict of interest to an acceptable level. Examples of safeguards include:

- Implementing mechanisms to prevent unauthorized disclosure of confidential information when performing professional services for two or more clients with conflicting interests. This could include:

- when performing professional services for two or more clients with conflicting interests, using separate engagement teams who are provided with clear policies and procedures on maintaining security and confidentiality;
- creating separate areas of practice for specialty functions within the firm, which may act as a barrier to the passing of confidential client information from one practice area to another within a firm;
- establishing policies and procedures to limit access to client files, the use of confidentiality agreements signed by employees and partners of the firm and/or the physical and electronic separation of confidential information;
- Regular review of the application of safeguards by a senior individual not involved with the client engagement or engagements;
- Having a professional accountant who is not involved in providing the service or otherwise affected by the conflict, review the work performed to assess whether the key judgments and conclusions are appropriate; and
- Consulting with third parties, such as a professional body, legal counsel or another professional accountant.

220.10 In addition, depending on the circumstances giving rise to the conflict, it is generally necessary to disclose the nature of the conflict and the related safeguards, if any, to all clients affected by the conflict and to obtain their consent to the professional accountant performing the professional services.

Disclosure and consent may take different forms, for example:

- General disclosure to potential clients of circumstances where the professional accountant, in keeping with common commercial practice, does not provide services exclusively for any one client (for example, in a particular service in a particular market sector) in order for the client to provide general consent accordingly. Such disclosure might, for example, be made in the professional accountant's standard terms and conditions for the engagement.
- Specific disclosure to all affected clients of the circumstances of the particular conflict together with any planned safeguards, sufficient to enable the client to make an informed decision with respect to the matter and to provide explicit consent accordingly.
- In certain circumstances consent may be implied by the client's conduct where the professional accountant is able to conclude that clients know the circumstances at the outset and have accepted the conflict of interest if they do not raise an objection to the existence of the conflict.

The professional accountant shall determine whether the significance of the conflict of interest is such that specific disclosure and explicit consent is necessary.

220.11 Where a professional accountant in public practice has requested explicit consent from a client in respect of a matter where the respective interests are in conflict and that consent has been refused by the client or withdrawn, the professional accountant shall decline to perform or shall discontinue professional services that could result in the conflict of interest; or terminate certain relationships or dispose of certain interests to eliminate the conflict.

220.12 When disclosure is verbal, or consent is verbal or implied, the professional accountant in public practice is encouraged to document the nature of the circumstances giving rise to the conflict of interest, the safeguards in place or applied to reduce the threats to an acceptable level and the consent obtained.

220.13 In certain circumstances, making specific disclosure for the purpose of obtaining explicit consent would result in a breach of confidentiality. Examples of such circumstances may include:

- Performing a transaction-related service for a client in connection with a hostile takeover of another client of the firm;
- Performing a forensic investigation for a client in connection with a suspected fraudulent act where the firm has confidential information obtained through having performed a professional service for another client who might be involved in the fraud.

The firm shall not accept or continue an engagement under such circumstances unless the following conditions are met:

- The firm does not act in an advocacy role for one client where this requires the firm to assume an adversarial position against the other client;
- Specific mechanisms are in place to prevent disclosure of confidential information between the engagement teams serving the two clients; and
- The firm is satisfied, that 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 it is appropriate for the firm to accept or continue the engagement because a restriction on the firm's ability to provide the service would produce a disproportionate adverse outcome for the clients or other relevant third parties.

The professional accountant shall document the nature of the circumstances, including the role that the professional accountant is to undertake, the specific mechanisms in place to prevent disclosure of information between the engagement teams serving the two clients and the rationale for the conclusion that it is appropriate to accept the engagement.

## **SECTION 310**

### **Conflicts of Interest**

310.1 A professional accountant in business may be faced with a conflict of interest when undertaking a professional activity. A conflict of interest creates a threat to objectivity and may create threats to the other fundamental principles. Such threats may be created when:

- The professional accountant undertakes a professional activity related to a particular matter for two or more parties whose interests with respect to that matter are in conflict; or
- The interests of the professional accountant with respect to a particular matter and the interests of a party for whom the professional accountant undertakes a professional activity related to that matter are in conflict.

A party may include an employing organization, a vendor, a customer, a lender, a shareholder, or another party.

A professional accountant shall not allow a conflict of interest to compromise professional or business judgment.

310.2 Examples of situations in which conflicts of interest may arise include:

- Serving in a management or governance position for two employing organizations and acquiring confidential information from one employing organization that could be used by the professional accountant to the advantage or disadvantage of the other employing organization;
- Undertaking a professional activity for each of two parties in a partnership employing the professional accountant to assist them to dissolve their partnership;
- Preparing financial information for certain members of management of the entity employing the professional accountant who are seeking to undertake a management buy-out;
- Being responsible for selecting a vendor for the accountant's employing organization when an immediate family member of the professional accountant could benefit financially from the transaction; and
- Serving in a governance capacity in an employing organization that is approving certain investments for the company where one of those specific investments will increase the value of the personal investment portfolio of the professional accountant or an immediate family member.

310.3 When identifying and evaluating the interests and relationships that might create a conflict of interest and implementing safeguards, when necessary, to eliminate or reduce any threat to compliance with the fundamental principles to an acceptable level, a professional accountant in business shall exercise professional judgment and be alert to all interests and relationships that 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, might compromise compliance with the fundamental principles.

310.4 When addressing a conflict of interest, a professional accountant in business is encouraged to seek guidance from within the employing organization or from others, such as a professional body, legal counsel or another professional accountant. When making disclosures or sharing

information within the employing organization and seeking guidance of third parties, the professional accountant shall remain alert to the fundamental principle of confidentiality.

310.5 If safeguards cannot eliminate the threat or reduce it to an acceptable level, a professional accountant in business shall decline to undertake or discontinue the professional activity or terminate the interest or relationship that creates the conflict of interest.

310.6 In identifying whether a conflict of interest exists or may be created, a professional accountant in business shall take reasonable steps to identify:

- the nature of the relationships between the parties involved and the nature of any relevant interests and;
- the nature of the activity and its implication for relevant parties.

The nature of the activities and the relevant relationships may change over time. The professional accountant shall remain alert to such changes for the purposes of identifying circumstances that might create a conflict of interest.

310.7 If a conflict of interest is identified, a professional accountant in business shall evaluate:

- the significance of relevant interests or relationships; and
- the significance of the conflict of interest created by undertaking the professional activity or activities. In general, the more direct the connection between the professional activity and the matter on which the parties' interests are in conflict, the more significant the conflict of interest will be.

310.8 The professional accountant in business shall apply safeguards when necessary to eliminate or reduce the threats to compliance with the fundamental principles created by the conflict of interest to an acceptable level. Depending on the circumstances giving rise to the conflict of interest, application of one or more of the following safeguards may be appropriate:

- Restructuring or segregating certain responsibilities and duties;
- Obtaining appropriate oversight, for example acting under the supervision of an executive or non-executive director;
- Withdrawing from the decision making process related to the matter giving rise to the conflict of interest;
- Consulting with third parties, such as a professional body, legal counsel or another professional accountant.

310.9 Depending upon the circumstances giving rise to the conflict of interest, it is generally necessary to disclose the nature of the conflict to the relevant parties, including to the appropriate levels within the employing organization, and obtain their consent for the professional accountant in business to undertake the professional activity. In certain circumstances, consent may be implied by a party's conduct where the professional accountant is able to conclude that parties know the circumstances at the outset and have accepted the conflict of interest if they do not raise an objection to the existence of the conflict.

310.10 When disclosure is verbal, or consent is verbal or implied, the professional accountant in business is encouraged to document the nature of the circumstances giving rise to the conflict of

interest, the safeguards in place or applied to reduce the threats to an acceptable level and the consent obtained.

- 310.11 A professional accountant in business may encounter other threats to compliance with the fundamental principles. This may occur, for example, when preparing or reporting financial information as a result of undue pressure from others within the employing organization or financial, business or personal relationships that close or immediate family members of the professional accountant have with the employing organization. Guidance on managing such threats is covered by Sections 320 and 340 of the Code.

## SECTION 320

### Preparation and Reporting of Information

- 320.1 Professional accountants in business are often involved in the preparation and reporting of information that may either be made public or used by others inside or outside the employing organization. Such information may include financial or management information, for example, forecasts and budgets, financial statements, management's discussion and analysis, and the management letter of representation provided to the auditors during the audit of the entity's financial statements. A professional accountant in business shall prepare or present such information fairly, honestly and in accordance with relevant professional standards so that the information will be understood in its context.
- 320.2 A professional accountant in business who has responsibility for the preparation or approval of the general purpose financial statements of an employing organization shall be satisfied that those financial statements are presented in accordance with the applicable financial reporting standards.
- 320.3 A professional accountant in business shall take reasonable steps to maintain information for which the professional accountant in business is responsible in a manner that:
- (a) Describes clearly the true nature of business transactions, assets, or liabilities;
  - (b) Classifies and records information in a timely and proper manner; and
  - (c) Represents the facts accurately and completely in all material respects.
- 320.4 Threats to compliance with the fundamental principles, for example, self-interest or intimidation threats to integrity, objectivity or professional competence and due care, are created where a professional accountant in business is pressured (either externally or by the possibility of personal gain) to prepare or report information in a misleading way or to become associated with misleading information through the actions of others.

*Paragraph 320.5 as amended would become 320.5 and 320.6*

- 320.5 The significance of such threats will depend on factors such as the source of the pressure and the corporate culture within the employing organization. The professional accountant in business shall be alert to the principle of integrity, which imposes an obligation on all professional accountants to be straightforward and honest in all professional and business relationships. Where the threats arise from compensation and incentive arrangements the guidance in section 340 is relevant.



320.6 The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate them threat or reduce it to an acceptable level. Such safeguards include consultation with superiors within the employing organization, the audit committee or those charged with governance of the organization, or with a relevant professional body.

*Paragraph 320.6 as amended would become 320.7*

320.7 Where it is not possible to reduce the threat to an acceptable level, a professional accountant in business shall refuse to be or remain associated with information the professional accountant determines is misleading. A professional accountant in business may have been unknowingly associated with misleading information. Upon becoming aware of this, the professional accountant in business shall take steps to be disassociated from that information. In determining whether there is a requirement to report the circumstances outside the organization, the professional accountant in business may consider obtaining legal advice. In addition, the professional accountant may consider whether to resign.

## **SECTION 340**

*The heading would be amended as follows:*

### **Financial Interests, Compensation and Incentives Linked to Financial Reporting and Decision Making**

340.1 Professional accountants in business may have financial interests, including those arising from compensation or incentive arrangements, or may know of financial interests of immediate or close family members, that, in certain circumstances, may create threats to compliance with the fundamental principles. For example, self-interest threats to objectivity or confidentiality may be created through the existence of the motive and opportunity to manipulate price sensitive information in order to gain financially. Examples of circumstances that may create self-interest threats include situations where the professional accountant in business or an immediate or close family member:

- Holds a direct or indirect financial interest in the employing organization and the value of that financial interest could be directly affected by decisions made by the professional accountant in business;
- Is eligible for a profit related bonus and the value of that bonus could be directly affected by decisions made by the professional accountant in business;
- Holds, directly or indirectly, deferred bonus share entitlements or share options in the employing organization, the value of which could be directly affected by decisions made by the professional accountant in business;
- Otherwise participates in compensation arrangements which provide incentives to achieve performance targets or to support efforts to maximize the value of the employing organization's shares, for example through participation in long term incentive plans which are linked to certain performance conditions being met.

*Paragraph 340.2 as amended would become 340.4. Paragraph 340.3 would be deleted. They would be replaced with the following paragraphs 340.2-340.3:*

- 340.2 Self-interest threats arising from compensation or incentive arrangements may be further compounded by pressure from superiors or peers in the employing organization who participate in the same arrangements. For example, such arrangements often entitle participants to be awarded shares in the employing organization at little or no cost to the employee provided certain performance criteria are met. In some cases, the value of the shares awarded may be significantly greater than the base salary of the professional accountant in business.
- 340.3 A professional accountant in business shall not manipulate information nor use confidential information for personal gain or for the financial gain of others. The more senior the position that the professional accountant in business holds, the greater the ability and opportunity to influence financial reporting and decision making and the greater the pressure there might be from superiors and peers to manipulate information. In such situations, the professional accountant in business shall be particularly alert to the principle of integrity, which imposes an obligation on all professional accountants to be straightforward and honest in all professional and business relationships.
- 340.4 The significance of any threat created by financial interests, shall be evaluated and safeguards applied, when necessary, to eliminate the threat or reduce it to an acceptable level. In evaluating the significance of any threat and, when necessary, determining the appropriate safeguards to be applied, a professional accountant in business shall evaluate the nature of the interest. This includes evaluating the significance of the interest. What constitutes a significant interest will depend on personal circumstances. Examples of such safeguards include:
- Policies and procedures for a committee independent of management to determine the level or form of remuneration of senior management.
  - Disclosure of all relevant interests, and of any plans to exercise entitlements or trade in relevant shares, to those charged with the governance of the employing organization, in accordance with any internal policies.
  - Consultation, where appropriate, with superiors within the employing organization.
  - Consultation, where appropriate, with those charged with the governance of the employing organization or relevant professional bodies.
  - Internal and external audit procedures.
  - Up-to-date education on ethical issues and on the legal restrictions and other regulations around potential insider trading.