



Federation of European Accountants

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Brussels, 14 April 2016

**Subject: FEE comments on the IESBA Exposure Draft: *Proposed Revisions Pertaining to Safeguards in the Code – Phase 1***

Dear Sir or Madam,

The Federation of European Accountants (the Federation) is pleased to provide you with its comments on the IESBA Exposure Draft *Proposed Revisions Pertaining to Safeguards in the Code – Phase 1* (the ED).

In our comments to the IESBA *Consultation Paper on the Proposed Strategy and Work Plan 2014-2018* dated 20 February 2014, we made the following remarks:

- importance of a pause in both ethics and independence standard setting
- time for IESBA to focus on adoption and implementation of the Code
- further relentless amendments to the Code cannot be justified

We regret that these points have not been followed by IESBA, but understand that other stakeholders see this project on safeguards as strategic.

The Federation's responses to the questions set out in the ED can be found in the appendix to this letter.

## General comments

As a first remark, these comments should be understood as preliminary. The Federation would like to assess Phase 2 of this project, as well as the outcome of the other EDs currently under consultation, before expressing any final opinion on the overall impact of the proposed changes to the Code. The rationale behind having two phases in this project is not clear. For some matters, such as small- and medium-sized practices (SMPs) and non-audit services, it would have been very useful to discuss them in Phase 1 rather than leaving it for Phase 2 as they should be assessed in conjunction with the proposed amendments. In addition, the overlap of this ED with the one on the structure of the Code makes it difficult to evaluate the potential impact of both projects on the clarity of the Code. We would have favoured a step-by-step approach, first allowing time for restructuring and then evaluation of the safeguards approach.

Generally speaking, the Federation thinks that by adding further requirements the Code becomes rules-based, leading invariably to a tick-box approach. This change does not meet the needs of practice and can result in problems of application by professional accountants. Nevertheless, the Federation would like to express its full support to the increased prominence of the requirement to apply the conceptual framework.

The imposition of the “third party test” is intended to provide a basis for establishing a framework to ensure the objective and rigorous assessment for determining the need for, as well as the nature and extent of, further action. It should be emphasised that what is deemed to be a “reasonable and informed third party” is subjective and the reference to a “hypothetical person” only reinforces this approach without any benefit for the user.

Regarding the “acceptable level”, the Federation considers that the proposed amendment introduces a different concept, making it unnecessarily more stringent, in replacing “to conclude that compliance with the fundamental principles is not compromised” with “to conclude that the professional accountant complies with the fundamental principles”. Although we understand the reasoning of shifting to an affirmative approach, this amendment does not bring added value as it is not very instructive on how professional accountants would achieve the intended result. The application of “acceptable level” by professional accountants is a well-established practice and therefore the Federation does not see a need for change.

The proposed description of safeguards has to be assessed in conjunction with the other amendments introduced in this regard. Introducing the concept of effectiveness in the definition of safeguard is unnecessary as, by definition, the elimination of threats must always be effective.

We have strong concerns in relation to the removal of certain conditions, policies, and procedures as safeguards. This adds confusion to the process and makes it more difficult for SMPs to consider how to apply the safeguards approach. The confusion comes from the fact that, in conjunction with the safeguards, another category has been implicitly created with these proposed amendments, namely ‘other’ elements that can be considered, but that should not be considered as safeguards anymore.

Overall, we believe that IESBA is proposing a very strict concept of safeguard, disregarding important practical implications.

We would also call for your attention to the proposed terminology harmonisation between materiality and significance: these two should not be mixed because some concepts are directly linked to audit (e.g. materiality) while others are not (e.g. significance).

We appreciate the opportunity to provide input and hope that IESBA finds our comments helpful when amending the Code.

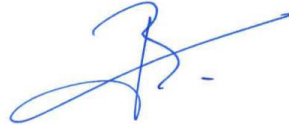
For further information on this FEE letter, please contact Noémi Robert on +32 2 893 33 80 or via email at [noemi.robert@fee.be](mailto:noemi.robert@fee.be) or Tiago Mateus on +32 2 893 3376 or via email at [tiago.mateus@fee.be](mailto:tiago.mateus@fee.be).

Kind regards,

On behalf of the Federation of European Accountants,

A handwritten signature in black ink, appearing to be 'Petr Kriz', with a stylized, cursive script.

Petr Kriz  
President

A handwritten signature in blue ink, appearing to be 'Olivier Boutellis-Taft', with a stylized, cursive script.

Olivier Boutellis-Taft  
Chief Executive

## Annex

### Request for specific comments

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#### Proposed Revisions to the Conceptual Framework

1. *Do respondents support the Board's proposed revisions to the extant Code pertaining to the conceptual framework, including the proposed requirements and application material related to:*
  - a) *Identifying threats;*
  - b) *Evaluating threats;*
  - c) *Addressing threats;*
  - d) *Re-evaluating threats; and*
  - e) *The overall assessment.**If not, why not?*

Although it may add some clarity, IESBA should carefully assess the introduction of new requirements, namely the re-evaluation of threats and the overall assessment, as they are already implicit. Regarding the re-evaluation of threats, it is unclear if it is intended to be a new requirement or a simple thought process that has to be present at all times. New facts and circumstances are already being taken into consideration. When they arise, the professional accountant has to assess whether a new threat was created and, if it has been, repeat the whole process.

Generally speaking, by adding further requirements, the Code becomes rules-based, leading invariably to a tick-box approach. This change does not meet the needs of practice and can result in problems of application by professional accountants.

Furthermore, there are inconsistencies between the thought process described in sections 120 and 300, namely regarding the identification and evaluation of threats. For further details, please refer to our response to question 5.

In addition, the new definition of safeguards together with the new category of circumstances makes it more difficult for practitioners to document properly and in a logical manner the threats, the safeguards, and the related conclusion.

Apart from the independence requirements, the Code is rather vague in terms of documentation requirements. IESBA could consider introducing new requirements in order to help practitioners realise that the documentation aspect is important in some respects, especially for regulators. More guidance on documentation would help practitioners demonstrate the considerations they gave to the threats and safeguards approach for a particular situation. This might be a better approach than removing safeguards from the list that could be taken into account, but are no longer regarded as safeguards.

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#### Proposed Revised Descriptions of “Reasonable and Informed Third Party” and “Acceptable Level”

2. *Do respondents support the proposed revisions aimed at clarifying the concepts of (a) “reasonable and informed third party;” and (b) “acceptable level” in the Code. If not, why not?*

The imposition of the “third party test” is intended to provide a basis for establishing a framework to ensure the objective and rigorous assessment for determining the need for, as well as the nature and extent of, further action. It should be emphasised that what is deemed to be a “reasonable and informed third party” is subjective and the reference to a “hypothetical person” only reinforces this approach without any benefit for the user.

Regarding the “acceptable level”, the Federation considers that the proposed amendment introduces a different concept, making it unnecessarily more stringent, in replacing “to conclude that compliance with the fundamental principles is not compromised” with “to conclude that the professional accountant complies with the fundamental principles”. Although we understand the reasoning of shifting to an affirmative approach, this amendment does not bring added value as it is not very instructive on how professional accountants would achieve the intended result. The application of “acceptable level” by professional accountants is a well-established practice and therefore the Federation does not see a need for change.

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### Proposed Revised Description of Safeguards

3. *Do respondents support the proposed description of “safeguards?” If not, why not?*

As mentioned in the general comments, the proposed description of safeguards has to be assessed in conjunction with the other amendments introduced in this regard. Introducing the concept of “effectiveness” in the definition of safeguard is unnecessary as, by definition, the elimination of threats must always be effective.

We have strong concerns in relation to the removal of certain conditions, policies, and procedures as safeguards, as it will add confusion to the process and impact their application by SMPs. In particular, with respect to the assessment of threats to independence, so far the current model has been considered as very practical in terms of documentation. The proposed draft seems unclear and leaves uncertainty as to how practitioners should consider the ‘old’ safeguards – i.e. the circumstances that are part of a new category of items to be considered – in terms of documentation.

A cost-benefit analysis will be necessary at the end of the project when both phases’ outcomes will be consolidated. IESBA should consider that reducing the availability of safeguards could lead to increased costs in business, namely for SMPs, for which external review may in some cases be the only available option.

In addition, the proposed R120.7, “Declining or discontinuing the specific professional activity or service involved” should not be at the same level as the remaining actions/measures because it should be regarded as last resort, and in some jurisdictions it is not even possible.

Overall, we believe that IESBA is proposing a very strict concept of safeguard, disregarding important practical implications.

4. *Do respondents agree with the IESBA’s conclusions that “safeguards created by the profession or legislation,” “safeguards in the work environment,” and “safeguards implemented by the entity” in the extant Code:*

f) *Do not meet the proposed description of safeguards in this ED?*

g) *Are better characterized as “conditions, policies and procedures that affect the professional accountant’s identification and potentially the evaluation of threats as discussed in paragraphs 26–28 of this Explanatory Memorandum?”*

*If not, why not?*

We agree with the revised definition of safeguards as “conditions, policies and procedures that affect the professional accountant’s identification and potentially the evaluation of threats” as discussed in paragraphs 26–28 of the *Explanatory Memorandum*. However, this revised definition should not be used to review the entire threats and safeguards approach. We have strong concerns in relation to the removal of certain conditions, policies, and procedures as safeguards, as it adds confusion to the process and makes it more difficult for SMPs to consider how to apply the safeguards approach. The confusion comes from the fact that another category has been implicitly created with the proposed amendments in conjunction with the safeguards, namely other elements than can be considered, but that should not be considered as safeguards anymore.

The Federation believes that this approach can be misleading for supervisory authorities as they will also have to deal with this new undefined category.

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## Proposals for Professional Accountants in Public Practice

5. *Do respondents agree with the IESBA’s approach to the revisions in proposed Section 300 for professional accountants in public practice? If not, why not and what suggestions for an alternative approach do respondents have that they believe would be more appropriate?*

The Federation would like to stress that the approach taken in Section 300 is not consistent with the one retained in Section 120, namely regarding the identification and evaluation of threats; we strongly advise that IESBA align the two sections. In this regard, the guidance provided in 300.2 A2 is more helpful and should be retained. Nevertheless, the process is still very complex and difficult to read. We refer to our response to question 1.

On the other hand, the scope of proposed 300.2 A5 could be broader. The reference to parts C1 and C2 of the Code give the impression that circumstances where no safeguards could reduce the threat to an acceptable level are only likely to arise in assurance engagements; we therefore suggest adding reference to other services.

## Request for general comments

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**In addition to the request for specific comments above, the IESBA is also seeking comments on the matters set out below:**

- a) *Small and Medium Practices (SMPs) – The IESBA invites comments regarding the impact of the proposed changes for SMPs.*

As IESBA acknowledges in the Explanatory Memorandum of the ED, SMPs face unique challenges in employing safeguards due to their resources, including the number of partners.

Therefore, it would have been very useful to discuss these challenges in Phase 1 rather than leaving it for a second moment (Phase 2), as this matter should be assessed in conjunction with the proposed amendments.

We think that a cost-benefit analysis is required in this regard as IESBA should consider that reducing the availability of safeguards, sometimes limited to external review in the case of SMPs, could lead to increased costs in business.

- b) *Developing Nations—Recognizing that many developing nations have adopted or are in the process of adopting the Code, the IESBA invites respondents from these nations to comment on the proposals, and in particular, on any foreseeable difficulties in applying them in their environment.*

The Federation has no comment on this specific question.

- c) *Translations—Recognizing that many respondents may intend to translate the final pronouncement for adoption in their environments, the IESBA welcomes comment on potential translation issues respondents may note in reviewing the proposals.*

As stated in the general comments, the Federation would first like to assess Phase 2 of this project before expressing its final opinion on the overall impact of the proposed changes to the Code.