



24 January 2012

International Ethics Standards Board for
Accountants (IESBA)
Jan Munro
Deputy Director

Email: janmunro@ifac.org

Ref.: ETH/PRJ/HBL/LFU/SHA

Dear Ms. Munro,

Re: FEE comments on IESBA Exposure Draft on Proposed Changes to the Code of Ethics for Professional Accountants related to Provisions Addressing a Breach of a Requirement of the Code

- (1) FEE (the Federation of European Accountants) is pleased to provide you with its comments on the IESBA Exposure Draft on Proposed Changes to the Code of Ethics for Professional Accountants related to Provisions Addressing a Breach of a Requirement of the Code ("the ED"). This letter includes our general comments on the ED below followed by our responses to the specific questions in the ED as follows:

General comments

- (2) In general, we support the proposals in the ED to include in the Code a general provision that will address the consequences of a breach of a requirement if a professional accountant identifies a breach of an independence provision of the Code but also a breach of any other provision of the Code.
- (3) Regarding the specific approach proposed, in particular to require the communication of *all* breaches, we would be concerned that where the IESBA Code does not reflect the materiality concept within the appropriate individual provisions, this may result in addressing immaterial matters.

- (4) Therefore, we believe that it would be appropriate to differentiate between significant breaches and those that are clearly trivial with the inclusion in the Code of de minimis exceptions.
- (5) For this, we propose that the threshold of being material to the financial statements be established to ensure that significant breaches are subject to the required communication and documentation but that those that are clearly trivial are not accorded the same treatment.
- (6) The approach in the ED, especially in relation to communication of a breach of a requirement of the Code, is not straightforward to “translate” into and apply appropriately in the context of smaller entities’ environments, served to a large extent by Small and Medium-sized Practitioners (SMPs). FEE would like to invite the IESBA to pay special attention to these issues in their finalisation of this ED.

Responses to specific questions

Question 1: Do respondents agree that the Code should contain provisions that require professional accountants to address the consequences of a breach of a requirement in the Code? If not why not?

- (7) We agree that the Code should contain provisions to address the consequences of a breach of a requirement of any provision of the Code. We are therefore in support of the proposed change to paragraph 100.10 of the Code to include such an overall provision.
- (8) We are fully supportive of the IESBA initiative to enhance the provisions to address the consequences of a breach of a requirement. We believe this is particularly important to address real life issues as breaches are, oftentimes unintentionally, bound to occur sooner or later. However, as we explain in our response to Question 3, we do have concerns as to the approach proposed, in that the IESBA decided to reject outright the inclusion of de minimis exceptions.
- (9) We do not agree with the view of some contributors that addressing a breach of a requirement of the IESBA Code is an implicit encouragement or even invitation to professional accountants to commit a breach. To the contrary, we believe it will enable professional accountants to better identify, communicate, correct and document breaches through the application of the necessary safeguards. Overall, the proposed changes to the Code will create an opportunity to better address the consequences of a breach.

Question 2: Do respondents agree with the overall approach proposed to deal with a breach of an independence requirement, including the proposal that the firm may continue with the audit engagement only if those charged with governance agree that action can be taken to satisfactorily address the consequences of the breach and such action is taken?

- (10) Subject to our comments on the matter addressed in Question 3, we agree with the overall approach proposed to deal with a breach of an independence requirement.

Question 3: Do respondents agree that a firm should be required to communicate all breaches of an independence requirement to those charged with governance? If not, why not and what should be the threshold for reporting?

- (11) We agree with the general approach to require that breaches of an independence requirement be communicated where the concept of materiality is built into the relevant individual provisions of the Code.
- (12) For instance, in relation to the provision of non-audit services, the Code includes various prohibitions that apply only if the impact of the relevant service is material to the financial statements of the audited client.

As an example, the provision in paragraph 290.211 of the Code stipulates that “acting in an advocacy role for an audit client in resolving a dispute or litigation when the amounts involved **are material to the financial statements** on which the firm will express an opinion would create advocacy and self-review threats so significant that no safeguards could reduce the threat to an acceptable level. Therefore, the firm shall not perform this type of service for an audit client”.

- (13) In this respect, and provided that trivial matters are discounted, we agree with the proposed requirement to communicate all breaches defined in the IESBA Code as being breaches.
- (14) However, where the IESBA Code does not reflect the materiality concept within the appropriate individual provisions, we have a concern with the proposal to require the communication of all breaches because this may result in addressing immaterial matters.
- (15) In particular, we have a concern regarding the individual provisions related to financial interests; for example having a direct financial interest in audit clients would always be considered a breach of a requirement of the Code without any regard to materiality (paragraph 290.104 of the current Code).
- (16) The SEC independence rules recognise that there may be situations where an accountant's independence becomes impaired unintentionally, such as where a family member makes an investment of which the covered person is not aware (paragraph (d) on Quality controls in the SEC rule 210.2-01) addresses those situations). However, this would not impact the audit firm's independence if certain quality control measures are put in place. We believe that the IESBA Code should contain a similar exception.

- (17) If the current concept of not providing for safeguards on any financial interests, no matter their significance is maintained, the proposed requirement to discuss with those charged with governance (paragraph 290.46 in the ED) and to document all the matters discussed (paragraph 290.50 in the ED) would be too burdensome. This could be in particular problematic for very large audits with many audit team members around the world.
- (18) We propose to ask for a threshold to be established to ensure that significant breaches are subject to such discussion and documentation but that those that are clearly trivial are not accorded the same treatment. These are the de minimis exceptions we refer to in paragraph 8 of this letter.

Question 4: Do respondents agree that the reasonable and informed third party test should be used in determining whether an action satisfactorily addresses the consequences of a breach of an independence requirement? If not, why not and what should the test be?

- (19) The conceptual framework in the Code already gives consideration to the reasonable and informed third party test (paragraphs 100.2 and 100.7 of the current Code). We agree that the reasonable and informed third party test should be used in determining whether an action satisfactorily addresses the consequences of a breach of an independence requirement.
- (20) In this context, we find that the wording of the third party test should be aligned to the wording in paragraph 100.7 of the current Code to make it clear that it is a thought process when exercising professional judgement.

Question 5: Do respondents agree that the matters that should be discussed with those charged with governance as proposed in section 290.46 are appropriate? If not, why not? Are there other matters that should be included, or matters that should be excluded?

- (21) Subject to our responses to Question 3, we agree that the matters that should be discussed with those charged with governance as proposed in section 290.46 are appropriate.

Question 6: Do respondents agree with the impact analysis as presented? Are there any other stakeholders, or other impacts on stakeholders, that should be considered and addressed by the IESBA?

- (22) As a general remark, we suggest enhancing the impact analysis by making it more succinct and shorten it into a single page thereby making it easier to read.
- (23) We note that the impact analysis appears to focus on costs. It would also be useful to include further potential benefits of the proposed revisions.

- (24) We also question whether the public perception would indeed mirror the statements anticipated on page 10 of the ED. For example, the public might believe that since all breaches have to be treated in the same way they are considered as being equally serious. The lack of differentiation between significant breaches and those that are clearly trivial may also potentially create a public perception that the profession is *often* in breach of its own Code without the public being in a position to appreciate that minor breaches do not necessarily equate to accountants being unethical.

Question 7: Would the proposal require firms to make significant changes to their systems or processes to enable them to properly implement the requirements? If so, does the proposed effective date provide sufficient time to make such changes?

- (25) In general terms, this question is directly related to the internal impacts on firms and as such we believe they are best placed to comment on this particular matter. However, we believe it is worth noting that for audit firms auditing Public Interest Entities (PIEs) in the European Union, there is already an existing obligation to annually confirm their independence. Therefore, the systems or processes to enable them to properly meet this obligation already need to be in place.

Question 8: Is the abbreviated version of the framework described in Section 290 for dealing with a breach of an independence requirement suitable for Section 291? If not, what do respondents believe Section 291 should contain?

- (26) We have no particular issues with the abbreviated version of the framework described in Section 290 as suitable for Section 291.

Drafting comments

- (27) We note that the terminology in the ED could be improved as it is not always clear. For instance, it is not fully clear what is meant by “eliminate” a relationship and “suspend” an interest in the proposed provision to “terminate, suspend or eliminate the interest or relationship that caused the breach” (proposed paragraph 290.40 in the ED), and moreover what is the difference between these three terms within this context. We suggest to change the wording so that it refers to “terminate (or suspend)” a relationship and “eliminate” an interest.
- (28) In paragraphs 290.42 and 290.44 of the ED the wording “... on the accounting records or amounts recorded in the financial statements...” ought to be amended to read “...on the accounting records or ~~amounts recorded in~~ on the financial statements...”, since the audit opinion is given on the financial statements as a whole as opposed to amounts recorded therein.

- (29) It would clarify the Code to highlight further the distinction (detailed in paragraph 290.49 of the ED) between breaches that occur prior to and after the issuance of the previous audit report. For instance, the specific paragraph 290.49 of the ED could be made more prominent by moving it upfront in the section to distinguish between these two different situations or by including it under a subheading which could be added.

For further information on this FEE¹ letter, please contact Hilde Blomme on +32 2 285 40 77 or via email at hilde.blomme@fee.be or Leyre Fuertes on +32 2 285 40 76 or via email at leyre.fuertes@fee.be from the FEE Secretariat.

Yours sincerely,



Philip Johnson
FEE President

¹ FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 45 professional institutes of accountants and auditors from 33 European countries, including all of the 27 European Union (EU) Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 700.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;
- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.

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