



香港會計師公會

HONG KONG SOCIETY OF ACCOUNTANTS

(Incorporated by the Professional Accountants Ordinance, Cap. 50)

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**To: HKSA members
All other interested parties**

Exposure Draft of Proposed HKSA Code of Ethics

Comments to be received by 15 December 2002

***Issued by the Council,
Hong Kong Society of Accountants***

The Hong Kong Society of Accountants' Council (Council) has issued an Exposure Draft of proposed HKSA Code of Ethics which is based on the IFAC Code of Ethics for Professional Accountants.

--- A copy of the Exposure Draft is attached. The Exposure Draft can also be found on-line at: <http://www.hksa.org.hk/professionaltechnical/ethics/exposedraft/>.

The Council invites comments from any interested party on all aspects of the Exposure Draft. Comments should be supported by specific reasoning and should be submitted in written form.

In issuing the Exposure Draft for consultation, the Council is aware that the IFAC Ethics Committee has a plan to restate the IFAC Code of Ethics for Professional Accountants on a principles basis in its entirety in line with that adopted for section 8 on independence and to expand Part C on the ethical requirements for employed professional accountants. The Council will review and issue further consultation on any proposed changes that may be made to the IFAC Code of Ethics for Professional Accountants in due course with the aim of attaining convergence of our standards with current international standards at all times.

Comments are requested to be received by **15 December 2002** and may be sent by mail, fax or e-mail to:

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Comments will be acknowledged and may be made available for public review unless otherwise requested by the contributor.

(October 2002)



Exposure Draft of Proposed HKSA Code of Ethics

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Preface

1. Introduction

- 1.1 The Council has approved an Exposure Draft of proposed HKSA Code of Ethics for review by members. Comments on all aspects of the proposed HKSA Code of Ethics are encouraged.
- 1.2 The proposed HKSA Code of Ethics is closely modelled on the IFAC Code of Ethics for Professional Accountants which was last updated in November 2001 with a new section on “independence”.

2. Adoption of the IFAC Code of Ethics for Professional Accountants

- 2.1 Recent corporate failures have provided increased interest and scrutiny regarding ethics matters, underlying the importance of encouraging global adoption of the independence provisions set forth in the IFAC Code. The Council shares the IFAC Board’s belief that early adoption of the IFAC Code by member bodies is essential to providing appropriate safeguards to maintain independence both in fact and in appearance and to meet the expectations of investors and the business community. As a result, the Council gave a mandate last year to the Ethics Committee to adopt the IFAC Code in Hong Kong. The adoption of the IFAC Code is a key step by the HKSA in achieving the convergence of local standards with international standards.
- 2.2 The Ethics Committee has started the adoption process by firstly completed a mapping exercise between the IFAC Code and the existing HKSA Statements of Professional Ethics (PES). The results of the mapping exercise reveal that the IFAC Code covers all of the requirements of the existing HKSA PES. On the other hand, the HKSA has also issued a number of ethical guidance to members because of local circumstances, some of which are not found in the IFAC Code and therefore there is a need for the HKSA to keep these local ethical guidance.
- 2.3 After the conclusion of mapping exercise, the Ethics Committee has agreed that the IFAC Code should be adopted as the basis for the HKSA Code of Ethics.
- 2.4 The key changes to the existing ethical requirements introduced by the proposed HKSA Code of Ethics are highlighted below.

- a. Section 8 – Conceptual framework on independence

The proposed HKSA Code of Ethics sets out a conceptual framework on independence that focuses on the factors that pose a threat to independence for all assurance engagements and the safeguards that auditors should put in place to preserve their independence.

The proposed HKSA Code of Ethics identifies five categories of threats to independence – self-interest, self-review, advocacy, familiarity and intimidation threats. Each has its own level and nature of risks attached that need to be balanced against possible safeguards. The proposed HKSA Code of Ethics also identifies three categories of safeguards to mitigate threats.

In addition, the proposed HKSA Code of Ethics provides in the Appendix to this section examples of situations on how the conceptual approach to independence is to be applied to specific circumstances and relationships. A discussion of “provision of non-assurance services to assurance clients” is set out in sections 8.155 to 8.202 of the proposed HKSA Code of Ethics, dealing separately with ten categories of non-audit services, including preparation of accounting records and financial statements, tax services, valuation services, internal audit services, IT systems services, litigation support services, legal services, corporate finance, provision of staff assignment and recruiting senior management.

There is no specific banning based on types of services, but rather, based on the principles set out in the proposed HKSA Code of Ethics, a firm should not accept an appointment where the threat to independence is so significant that no safeguard could reduce the threat to an acceptable level. There are specific examples that this will be so including specific types of legal, corporate finance and valuation services, and accounting records and financial statement preparation for listed audit clients.

b. Section 14 – Advertising and solicitation

The proposed HKSA Code of Ethics has further liberalised the practice promotion rules by removing the restrictions of cold calling, direct mailing, distribution of leaflets, promotional gifts and other items, and making references to fees or scale charges in promotional material, provided that they comply with the requirements in this section.

- 2.5 The Council has also approved a draft of proposed Preface to the Ethical Requirements of the Hong Kong Society of Accountants – Statement of Policy of Council for review by members, which sets out the authority of the proposed HKSA Code of Ethics. This is attached at **Annex 1**.

3. Specific questions

Members are requested to comment on all aspects of the proposed HKSA Code of Ethics, but it would also help if members would indicate their views (with reasons) on a number of specific issues as set out below.

- 3.1 Do you agree with the move to a conceptual framework that requires the identification and evaluation of threats to independence and the application of safeguards to reduce any threats created to an acceptable level?
- 3.2 Do you consider the inclusion in the Appendix to section 8 of examples of specific circumstances and relationships that may create threats to independence of assistance in assessing independence?
- 3.3 Do you agree with the further liberalisation of the practice promotion rules by removing the restrictions of cold calling, direct mailing, distribution of leaflets, promotional gifts and other items, and making references to fees or scale charges in promotional material, provided that they comply with the requirements in section 14 “Advertising and Solicitation”?

4. Future withdrawals of the HKSA Professional Ethics Statements

4.1 On the finalisation of the proposed HKSA Code of Ethics, the following HKSA Professional Ethics Statements will be withdrawn:

- 1.200 Explanatory foreword
- 1.201 General
- 1.202 Descriptions
- 1.203 Integrity, objectivity and independence
- 1.204A Confidentiality
- 1.205 Practice promotion
- 1.207 Changes in a professional appointment
- 1.208 Fees
- 1.209 Management consulting services
- 1.210 Ethics in tax practice
- 1.212 Clients' monies
- 1.291 The ethical responsibilities of members in business

4.2 The following HKSA Professional Ethics Statements will be kept and updated as they provide additional guidance:

- 1.203 Integrity, objectivity and independence in insolvency (Supp.)
- 1.204B Unlawful acts or defaults by clients of members
- 1.290C Unlawful acts or defaults by or on behalf of a members' employer
- 1.290D Financial and accounting responsibilities of directors
- 1.292 Corporate finance advice

4.3 A sample of the proposed revised Section 1.2 "Professional Ethics" of Members' Handbook Volume I is at **Annex 2**.

Annex 1

**PROPOSED PREFACE TO THE ETHICAL REQUIREMENTS OF
THE HONG KONG SOCIETY OF ACCOUNTANTS (HKSA)**

STATEMENT OF POLICY OF COUNCIL

This Preface was approved by the Council of the HKSA for publication on [Day, Month, Year].

1. The HKSA as a member of the International Federation of Accountants (IFAC) is committed to the IFAC's broad objective of developing and enhancing a coordinated worldwide accountancy profession with harmonized standards. In working towards this objective, IFAC develops guidance on ethics for professional accountants. IFAC believes that issuing such guidance will improve the degree of uniformity of professional ethics throughout the world.
2. As a condition of its membership, the HKSA is obliged to support the work of IFAC by informing its members of every pronouncement developed by IFAC, and to work towards implementation, when and to the extent possible under local circumstances, of those pronouncements.
3. The HKSA has determined to adopt the IFAC Code of Ethics for Professional Accountants as the basis for the HKSA Code of Ethics which is the Ethical Requirements in Hong Kong.
4. Where the Council of the HKSA deems it necessary, additional Ethical Requirements may be developed on matters of relevance in Hong Kong not covered by an IFAC pronouncement.
5. Members and Registered Students of the HKSA are required to comply with the Ethical Requirements issued by the HKSA. Apparent failure to do so will result in an investigation into their conduct by the HKSA in accordance with sections 33 to 41 of the Professional Accountants Ordinance.
6. It is not practical to establish the Ethical Requirements which apply to all situations and circumstances that Members and Registered Students of the HKSA may encounter. Therefore, Members and Registered Students of the HKSA should consider the Ethical Requirements as the basic principles which they should follow in performing their work.
7. In addition to the Ethical Requirements, the HKSA also issues Additional Guidance of a more general nature for the benefit of Members and Registered Students of the HKSA. Failure to follow such Guidance does not of itself necessarily constitute misconduct, but means that a Member or Registered Student of the HKSA concerned may be at risk of having to justify his/her actions in answer to a complaint to the HKSA.

Annex 2

**HONG KONG SOCIETY OF ACCOUNTANTS
MEMBERS' HANDBOOK
CONTENTS OF VOLUME I**

(Extract)

	<i>Issue/ Review date</i>
1.2 PROFESSIONAL ETHICS	
Preface to The Ethical Requirements of The Hong Kong Society of Accountants – Statement of Policy of Council	[]
1.20 HKSA Code of Ethics	[]
Additional Guidance	
1.203 Integrity, objectivity and independence in insolvency (Supp.)	8/94
1.204B Unlawful acts or defaults by clients of members	8/94
1.290C Unlawful acts or defaults by or on behalf of a member's employer	10/91
1.290D Financial and accounting responsibilities of directors	9/92
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**EXPOSURE DRAFT OF
PROPOSED HKSA CODE OF ETHICS
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EXPLANATORY FOREWORD

The Council of the Hong Kong Society of Accountants (HKSA) has determined that the Code of Ethics is mandatory for all Members and Registered Students of the HKSA to observe in respect of the performance of professional services after [date to be inserted after exposure].

DEFINITIONS

In the Code of Ethics the following expressions have the following meanings assigned to them:

Advertising	The communication to the public of information as to the services or skills provided by professional accountants in public practice with a view to procuring professional business.
Audit client	An entity in respect of which a firm conducts an audit engagement. When the audit client is a listed entity, audit client will always include its related entities.
Audit engagement	An assurance engagement to provide a high level of assurance that financial statements are free of material misstatement, such as an engagement in accordance with Statements of Auditing Standards (SASs) issued by the HKSA or International Standards on Auditing. This includes a Statutory Audit which is an audit required by legislation or other regulation.
Assurance client	An entity in respect of which a firm conducts an assurance engagement.
Assurance engagement	<p>An engagement conducted to provide:</p> <ul style="list-style-type: none">(a) a high level of assurance that the subject matter conforms in all material respects with identified suitable criteria; or(b) a moderate level of assurance that the subject matter is plausible in the circumstances. <p>This would include an engagement in accordance with Standards on Assurance Engagements (SAEs) issued by the HKSA or International Standard on Assurance Engagements or in accordance with specific standards for assurance engagements issued by the HKSA or the International Auditing and Assurance Standards Board such as an audit or review of financial statements in accordance with SASs or International Standards on Auditing.</p>
Assurance team	<ul style="list-style-type: none">(a) All professionals participating in the assurance engagement;(b) All others within a firm who can directly influence the outcome of the assurance engagement, including:<ul style="list-style-type: none">• those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the assurance engagement partner in connection with the performance of the assurance engagement. For the purposes of an audit engagement this includes those at all successively senior levels above the lead engagement partner through the firm's chief executive;• those who provide consultation regarding technical or industry specific issues, transactions or events for the assurance engagement; and• those who provide quality control for the assurance engagement;and(c) For the purposes of an audit client, all those within a network firm who can directly influence the outcome of the audit engagement.

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Client account	Any bank account which is used solely for the banking of clients' monies.
Clients' monies	Any monies — including documents of title to money e.g., bills of exchange, promissory notes, and documents of title which can be converted into money e.g., bearer bonds — received by a professional accountant in public practice to be held or paid out on the instruction of the person from whom or on whose behalf they are received.
Close family	A parent, non-dependent child or sibling.
Direct financial interest	A financial interest: <ul style="list-style-type: none">• owned directly by and under the control of an individual or entity (including those managed on a discretionary basis by others); or• beneficially owned through a collective investment vehicle, estate, trust or other intermediary over which the individual or entity has control.
Directors and officers	Those charged with the governance of an entity, regardless of their title, which may vary from country to country.
Employed professional accountant	A professional accountant employed in industry, commerce, the public sector or education.
Existing accountant	A professional accountant in public practice currently holding an audit appointment or carrying out accounting, taxation, consulting or similar professional services for a client.
Financial interest	An interest in an equity or other security, debenture, loan or other debt instrument of an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.
Firm	(a) A sole practitioner, partnership or corporation of professional accountants; (b) An entity that controls such parties; and (c) An entity controlled by such parties.
Immediate family	A spouse (or equivalent) or dependent.
Independence	Independence is: <ul style="list-style-type: none">(a) Independence of mind – the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism; and(b) Independence in appearance – the avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.

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Indirect financial interest	A financial interest beneficially owned through a collective investment vehicle, estate, trust or other intermediary over which the individual or entity has no control.
Lead engagement partner	In connection with an audit, the partner responsible for signing the report on the consolidated financial statements of the audit client, and, where relevant, the partner responsible for signing the report in respect of any entity whose financial statements form part of the consolidated financial statements and on which a separate stand-alone report is issued. When no consolidated financial statements are prepared, the lead engagement partner would be the partner responsible for signing the report on the financial statements.
Listed entity	An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.
Network firm	An entity under common control, ownership or management with the firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as being part of the firm nationally or internationally.
Objectivity	A combination of impartiality, intellectual honesty and a freedom from conflicts of interest.
Office	A distinct sub-group, whether organized on geographical or practice lines.
Practice	A sole practitioner, a partnership or a corporation of professional accountants which offers professional services to the public.
Professional accountant	Those persons, whether they be in public practice (including a sole practitioner, partnership or corporate body), industry, commerce, the public sector or education, who are members of the HKSA.
Professional accountant in public practice	Each partner or person occupying a position similar to that of a partner, and each employee in a practice providing professional services to a client irrespective of their functional classification (e.g. audit, tax or consulting) and professional accountants in a practice having managerial responsibilities. This term is also used to refer to a firm of professional accountants in public practice.
Professional services	Any service requiring accountancy or related skills performed by a professional accountant including accounting, auditing, taxation, management consulting and financial management services.
Publicity	The communication to the public of facts about a professional accountant which are not designed for the deliberate promotion of that professional accountant.
Receiving accountant	A professional accountant in public practice to whom the existing accountant or client of the existing accountant has referred audit, accounting, taxation, consulting or similar appointments, or who is consulted in order to meet the needs of the client.
Related entity	An entity that has any of the following relationships with the client:

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- (a) An entity that has direct or indirect control over the client provided the client is material to such entity;
- (b) An entity with a direct financial interest in the client provided that such entity has significant influence over the client and the interest in the client is material to such entity;
- (c) An entity over which the client has direct or indirect control;
- (d) An entity in which the client, or an entity related to the client under (c) above, has a direct financial interest that gives it significant influence over such entity and the interest is material to the client and its related entity in (c); and
- (e) An entity which is under common control with the client (hereinafter a “sister entity”) provided the sister entity and the client are both material to the entity that controls both the client and sister entity.

Solicitation

The approach to a potential client for the purpose of offering professional services.

INTRODUCTION

1. The Code of Ethics is established on the basis that unless a limitation is specifically stated, the objectives and fundamental principles are equally valid for all professional accountants, whether they be in public practice, industry, commerce, the public sector or education.
2. A profession is distinguished by certain characteristics including:
 - Mastery of a particular intellectual skill, acquired by training and education;
 - Adherence by its members to a common code of values and conduct established by its administering body, including maintaining an outlook which is essentially objective; and
 - Acceptance of a duty to society as a whole (usually in return for restrictions in use of a title or in the granting of a qualification).
3. Members' duty to their profession and to society may at times seem to conflict with their immediate self interest or their duty of loyalty to their employer.
4. Against this background the HKSA has laid down ethical requirements for its members to ensure the highest quality of performance and to maintain public confidence in the profession.

THE PUBLIC INTEREST

5. A distinguishing mark of a profession is acceptance of its responsibility to the public. The accountancy profession's public consists of clients, credit grantors, governments, employers, employees, investors, the business and financial community, and others who rely on the objectivity and integrity of professional accountants to maintain the orderly functioning of commerce. This reliance imposes a public interest responsibility on the accountancy profession. The public interest is defined as the collective well-being of the community of people and institutions the professional accountant serves.
6. A professional accountant's responsibility is not exclusively to satisfy the needs of an individual client or employer. The standards of the accountancy profession are heavily determined by the public interest, for example:
 - Independent auditors help to maintain the integrity and efficiency of the financial statements presented to financial institutions in partial support for loans and to stockholders for obtaining capital;
 - Financial executives serve in various financial management capacities in organizations and contribute to the efficient and effective use of the organization's resources;
 - Internal auditors provide assurance about a sound internal control system which enhances the reliability of the external financial information of the employer;
 - Tax experts help to establish confidence and efficiency in, and the fair application of, the tax system; and
 - Management consultants have a responsibility toward the public interest in advocating sound management decision making.
7. Professional accountants have an important role in society. Investors, creditors, employers and other sectors of the business community, as well as the government and the public at large rely on professional accountants for sound financial accounting and reporting, effective financial management and competent advice on a variety of business and taxation matters. The attitude and behavior of professional accountants in providing such services have an impact on the economic well-being of their community.
8. Professional accountants can remain in this advantageous position only by continuing to provide the public with these unique services at a level which demonstrates that the public confidence is firmly founded. It is in the best interest of the accountancy profession to make known to users of the services provided by professional accountants that they are executed at the highest level of performance and in accordance with ethical requirements that strive to ensure such performance.
9. In formulating the Code of Ethics, the HKSA has considered the public service and user expectations of the ethical standards of professional accountants and taken their views into account. The purpose of doing so is to address or explain any existing "expectation gap" between the standards expected and those prescribed.

OBJECTIVES

10. The Code of Ethics recognizes that the objectives of the accountancy profession are to work to the highest standards of professionalism, to attain the highest levels of performance and generally to meet the public interest requirement set out above. These objectives require four basic needs to be met:
- *Credibility*
In the whole of society there is a need for credibility in information and information systems.
 - *Professionalism*
There is a need for individuals who can be clearly identified by clients, employers and other interested parties as professional persons in the accountancy field.
 - *Quality of Services*
There is a need for assurance that all services obtained from a professional accountant are carried out to the highest standards of performance.
 - *Confidence*
Users of the services of professional accountants should be able to feel confident that there exists a framework of professional ethics which governs the provision of those services.

FUNDAMENTAL PRINCIPLES

11. In order to achieve the objectives of the accountancy profession, professional accountants have to observe a number of prerequisites or fundamental principles.
12. The fundamental principles are:
 - *Integrity*
A professional accountant should be straightforward and honest in performing professional services.
 - *Objectivity*
A professional accountant should be fair and should not allow prejudice or bias, conflict of interest or influence of others to override objectivity.
 - *Professional Competence and Due Care*
A professional accountant should perform professional services with due care, competence and diligence and has a continuing duty to maintain professional knowledge and skill at a level required to ensure that a client or employer receives the advantage of competent professional service based on up-to-date developments in practice, legislation and techniques.
 - *Confidentiality*
A professional accountant should respect the confidentiality of information acquired during the course of performing professional services and should not use or disclose any such information without proper and specific authority or unless there is a legal or professional right or duty to disclose.
 - *Professional Behavior*
A professional accountant should act in a manner consistent with the good reputation of the profession and refrain from any conduct which might bring discredit to the profession. The obligation to refrain from any conduct which might bring discredit to the profession requires the professional accountant to recognise his or her responsibilities to clients, third parties, other members of the accountancy profession, staff, employers, and the general public.
 - *Technical Standards*
A professional accountant should carry out professional services in accordance with the relevant technical and professional standards. Professional accountants have a duty to carry out with care and skill, the instructions of the client or employer insofar as they are compatible with the requirements of integrity, objectivity and, in the case of professional accountants in public practice, independence (see Section 8 below). In addition, they should conform with the technical and professional standards promulgated by:
 - The HKSA;
 - IFAC (e.g., International Standards on Auditing);
 - International Accounting Standards Board;
 - Other regulatory body; and
 - Relevant legislation.

THE CODE OF ETHICS

13. The objectives as well as the fundamental principles are of a general nature and are not intended to be used to solve a professional accountant's ethical problems in a specific case. However, the Code of Ethics provides some guidance as to the application in practice of the objectives and the fundamental principles with regard to a number of typical situations occurring in the accountancy profession.
14. The Code of Ethics set out below is divided into three parts:
 - Part A applies to all professional accountants unless otherwise specified.
 - Part B applies only to those professional accountants in public practice.
 - Part C applies to employed professional accountants, and may also apply, in appropriate circumstances, to accountants employed in public practice.

PART A — APPLICABLE TO ALL PROFESSIONAL ACCOUNTANTS

SECTION 1

Integrity and Objectivity

- 1.1 Integrity implies not merely honesty but fair dealing and truthfulness. The principle of objectivity imposes the obligation on all professional accountants to be fair, intellectually honest and free of conflicts of interest.
- 1.2 Professional accountants serve in many different capacities and should demonstrate their objectivity in varying circumstances. Professional accountants in public practice undertake assurance engagements, and render tax and other management advisory services. Other professional accountants prepare financial statements as a subordinate of others, perform internal auditing services, and serve in financial management capacities in industry, commerce, the public sector and education. They also educate and train those who aspire to admission into the profession. Regardless of service or capacity, professional accountants should protect the integrity of their professional services, and maintain objectivity in their judgment.
- 1.3 In selecting the situations and practices to be specifically dealt with in ethics requirements relating to objectivity, adequate consideration should be given to the following factors:
 - (a) Professional accountants are exposed to situations which involve the possibility of pressures being exerted on them. These pressures may impair their objectivity.
 - (b) It is impracticable to define and prescribe all such situations where these possible pressures exist. Reasonableness should prevail in establishing standards for identifying relationships that are likely to, or appear to, impair a professional accountant's objectivity.
 - (c) Relationships should be avoided which allow prejudice, bias or influences of others to override objectivity.
 - (d) Professional accountants have an obligation to ensure that personnel engaged on professional services adhere to the principle of objectivity.
 - (e) Professional accountants should neither accept nor offer gifts or entertainment which might reasonably be believed to have a significant and improper influence on their professional judgment or those with whom they deal. What constitutes an excessive gift or offer of entertainment varies from country to country but professional accountants should avoid circumstances which would bring their professional standing into disrepute.

SECTION 2

Resolution of Ethical Conflicts

- 2.1 From time to time professional accountants encounter situations which give rise to conflicts of interest. Such conflicts may arise in a wide variety of ways, ranging from the relatively trivial dilemma to the extreme case of fraud and similar illegal activities. It is not possible to attempt to itemize a comprehensive check list of potential cases where conflicts of interest might occur. The professional accountant should be constantly conscious of and be alert to factors which give rise to conflicts of interest. It should be noted that an honest difference of opinion between a professional accountant and another party is not in itself an ethical issue. However, the facts and circumstances of each case need investigation by the parties concerned.
- 2.2 It is recognized, however, that there can be particular factors which occur when the responsibilities of a professional accountant may conflict with internal or external demands of one type or another. Hence:
- There may be the danger of pressure from an overbearing supervisor, manager, director or partner; or when there are family or personal relationships which can give rise to the possibility of pressures being exerted upon them. Indeed, relationships or interests which could adversely influence, impair or threaten a professional accountant's integrity should be discouraged.
 - A professional accountant may be asked to act contrary to technical and/or professional standards.
 - A question of divided loyalty as between the professional accountant's superior and the required professional standards of conduct could occur.
 - Conflict could arise when misleading information is published which may be to the advantage of the employer or client and which may or may not benefit the professional accountant as a result of such publication.
- 2.3 In applying standards of ethical conduct professional accountants may encounter problems in identifying unethical behavior or in resolving an ethical conflict. When faced with significant ethical issues, professional accountants should follow the established policies of the employing organization to seek a resolution of such conflict. If those policies do not resolve the ethical conflict, the following should be considered:
- Review the conflict problem with the immediate superior. If the problem is not resolved with the immediate superior and the professional accountant determines to go to the next higher managerial level, the immediate superior should be notified of the decision. If it appears that the superior is involved in the conflict problem, the professional accountant should raise the issue with the next higher level of management. When the immediate superior is the Chief Executive Officer (or equivalent) the next higher reviewing level may be the Executive Committee, Board of Directors, Non-Executive Directors, Trustees, Partners' Management Committee or Shareholders.
 - Seek counseling and advice on a confidential basis with an independent advisor or the HKSA to obtain an understanding of possible courses of action.
 - If the ethical conflict still exists after fully exhausting all levels of internal review, the professional accountant as a last resort may have no other recourse on significant matters (e.g., fraud) than to resign and to submit an information memorandum to an appropriate representative of that organization.

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- 2.4 Furthermore, local laws or regulations may require certain serious matters to be reported to an external body such as an enforcement or supervisory authority.
- 2.5 Any professional accountant in a senior position should endeavor to ensure that policies are established within his or her employing organization to seek resolution of conflicts.

SECTION 3

Professional Competence

- 3.1 Professional accountants should not portray themselves as having expertise or experience they do not possess.
- 3.2 Professional competence may be divided into two separate phases:
- (a) Attainment of professional competence

The attainment of professional competence requires initially a high standard of general education followed by specific education, training and examination in professionally relevant subjects, and whether prescribed or not, a period of work experience. This should be the normal pattern of development for a professional accountant.
 - (b) Maintenance of professional competence
 - (i) The maintenance of professional competence requires a continuing awareness of developments in the accountancy profession including relevant local and international pronouncements on accounting, auditing and other relevant regulations and statutory requirements.
 - (ii) A professional accountant should adopt a program designed to ensure quality control in the performance of professional services consistent with appropriate local and international pronouncements.

SECTION 4

Confidentiality

- 4.1 Professional accountants have an obligation to respect the confidentiality of information about a client's or employer's affairs acquired in the course of professional services. The duty of confidentiality continues even after the end of the relationship between the professional accountant and the client or employer.
- 4.2 Confidentiality should always be observed by a professional accountant unless specific authority has been given to disclose information or there is a legal or professional duty to disclose.
- 4.3 Professional accountants have an obligation to ensure that staff under their control and persons from whom advice and assistance is obtained respect the principle of confidentiality.
- 4.4 Confidentiality is not only a matter of disclosure of information. It also requires that a professional accountant acquiring information in the course of performing professional services does neither use nor appear to use that information for personal advantage or for the advantage of a third party.
- 4.5 A professional accountant has access to much confidential information about a client's or employer's affairs not otherwise disclosed to the public. Therefore, the professional accountant should be relied upon not to make unauthorized disclosures to other persons. This does not apply to disclosure of such information in order properly to discharge the professional accountant's responsibility according to the profession's standards.
- 4.6 It is in the interest of the public and the profession that the profession's standards relating to confidentiality be defined and guidance given on the nature and extent of the duty of confidentiality and the circumstances in which disclosure of information acquired during the course of providing professional services shall be permitted or required.
- 4.7 The following are examples of the points which should be considered in determining whether confidential information may be disclosed:
 - (a) When disclosure is authorized. When authorization to disclose is given by the client or the employer the interests of all the parties including those third parties whose interests might be affected should be considered.
 - (b) When disclosure is required by law. Examples of when a professional accountant is required by law to disclose confidential information are:
 - (i) To produce documents or to give evidence in the course of legal proceedings; and
 - (ii) To disclose to the appropriate public authorities infringements of the law which come to light.
 - (c) When there is a professional duty or right to disclose:
 - (i) To comply with technical standards and ethics requirements; such disclosure is not contrary to this section;
 - (ii) To protect the professional interests of a professional accountant in legal proceedings;
 - (iii) To comply with the practice review of the HKSA ; and
 - (iv) To respond to an inquiry or investigation by the HKSA or a regulatory body.

4.8 When the professional accountant has determined that confidential information can be disclosed, the following points should be considered:

- Whether or not all the relevant facts are known and substantiated, to the extent it is practicable to do so; when the situation involves unsubstantiated fact or opinion, professional judgment should be used in determining the type of disclosure to be made, if any;
- What type of communication is expected and the addressee; in particular, the professional accountant should be satisfied that the parties to whom the communication is addressed are appropriate recipients and have the responsibility to act on it; and
- Whether or not the professional accountant would incur any legal liability having made a communication and the consequences thereof.

In all such situations, the professional accountants should consider the need to consult legal counsel.

SECTION 5

Tax Practice

- 5.1 A professional accountant rendering professional tax services is entitled to put forward the best position in favor of a client, or an employer, provided the service is rendered with professional competence, does not in any way impair integrity and objectivity, and is in the opinion of the professional accountant consistent with the law. Doubt may be resolved in favor of the client or the employer if there is reasonable support for the position.
- 5.2 A professional accountant should not hold out to a client or an employer the assurance that the tax return prepared and the tax advice offered are beyond challenge. Instead, the professional accountant should ensure that the client or the employer is aware of the limitations attaching to tax advice and services so that it does not misinterpret an expression of opinion as an assertion of fact.
- 5.3 A professional accountant who undertakes or assists in the preparation of a tax return should advise the client or the employer that the responsibility for the content of the return rests primarily with the client or employer. The professional accountant should take the necessary steps to ensure that the tax return is properly prepared on the basis of the information received.
- 5.4 Tax advice or opinions of material consequence given to a client or an employer should be recorded, either in the form of a letter or in a memorandum for the files.
- 5.5 A professional accountant should not be associated with any return or communication in which there is reason to believe that it:
- (a) Contains a false or misleading statement;
 - (b) Contains statements or information furnished recklessly or without any real knowledge of whether they are true or false; or
 - (c) Omits or obscures information required to be submitted and such omission or obscurity would mislead the revenue authorities.
- 5.6 A professional accountant may prepare tax returns involving the use of estimates if such use is generally acceptable or if it is impractical under the circumstances to obtain exact data. When estimates are used, they should be presented as such in a manner so as to avoid the implication of greater accuracy than exists. The professional accountant should be satisfied that estimated amounts are reasonable under the circumstances.
- 5.7 In preparing a tax return, a professional accountant ordinarily may rely on information furnished by the client or employer provided that the information appears reasonable. Although the examination or review of documents or other evidence in support of the information is not required, the professional accountant should encourage, when appropriate, such supporting data to be provided.

In addition, the professional accountant:

- (a) Should make use of the client's returns for prior years whenever feasible;
- (b) Is required to make reasonable inquiries when the information presented appears to be incorrect or incomplete; and
- (c) Is encouraged to make reference to the books and records of the business operations.

- 5.8 When a professional accountant learns of a material error or omission in a tax return of a prior year (with which the professional accountant may or may not have been associated), or of the failure to file a required tax return, the professional accountant has a number of responsibilities:
- (a) Promptly advise the client or employer of the error or omission and recommend that disclosure be made to the revenue authorities. Normally, the professional accountant is not obligated to inform the revenue authorities, nor may this be done without permission.
 - (b) If the client or the employer does not correct the error the professional accountant:
 - (i) Should inform the client or the employer that it is not possible to act for it in connection with that return or other related information submitted to the authorities; and
 - (ii) Should consider whether continued association with the client or employer in any capacity is consistent with professional responsibilities.
 - (c) If the professional accountant concludes that a professional relationship with the client or employer can be continued, all reasonable steps should be taken to ensure that the error is not repeated in subsequent tax returns.
 - (d) Professional or statutory requirements in Hong Kong may also make it necessary for the professional accountant to inform the revenue authorities that there is no longer any association with the return or other information involved and that acting for the client or employer has ceased. In these circumstances, the professional accountant should advise the client or employer of the position before informing the authorities and should give no further information to the authorities without the consent of the client or employer unless required to do so by law.

SECTION 6

Cross Border Activities

- 6.1 When considering the application of ethical requirements in cross border activities a number of situations may arise. Whether a professional accountant is a member of the HKSA only or is also a member of the profession in the country where the services are performed should not affect the manner of dealing with each situation.
- 6.2 A professional accountant may reside in another country or may be temporarily visiting that country to perform professional services. In all circumstances, the professional accountant should carry out professional services in accordance with the relevant technical standards and ethical requirements. The particular technical standards which should be followed are not dealt within this section. In all other respects, however, the professional accountant should be guided by the ethical requirements set out below.
- 6.3 When a professional accountant performs services outside Hong Kong and differences on specific matters exist between ethical requirements of the two jurisdictions the following provisions should be applied:
- (a) When the ethical requirements of the country in which the services are being performed are less strict than the Code of Ethics, then the Code of Ethics should be applied.
 - (b) When the ethical requirements of the country in which the services are being performed are stricter than the Code of Ethics, then the ethical requirements in the country where the services are being performed should be applied.

SECTION 7

Publicity

- 7.1 In the marketing and promotion of themselves and their work, professional accountants should:
- (a) Not use means which brings the profession into disrepute;
 - (b) Not make exaggerated claims for the services they are able to offer, the qualifications they possess, or experience they have gained; and
 - (c) Not denigrate the work of other professional accountants.

PART B — APPLICABLE TO PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE

SECTION 8

Independence for Assurance Engagements

- 8.1 It is in the public interest and, therefore, required by the Code of Ethics, that members of assurance teams, firms and, when applicable, network firms be independent of assurance clients.
- 8.2 Assurance engagements are intended to enhance the credibility of information about a subject matter by evaluating whether the subject matter conforms in all material respects with suitable criteria. The SAEs issued by the HKSA and International Standard on Assurance Engagements issued by the International Auditing and Assurance Standards Board describe the objectives and elements of assurance engagements to provide either a high or a moderate level of assurance. The HKSA and the International Auditing and Assurance Standards Board have also issued specific standards for certain assurance engagements. For example, SASs and International Standards on Auditing provide specific standards for audit (high level assurance) and review (moderate level assurance) of financial statements.

Paragraphs 8.3 through 8.6 are taken from SAE 100 “Framework for assurance engagements intended to provide either a high or moderate level of assurance” and the International Standard on Assurance Engagements and describe the nature of an assurance engagement. These paragraphs are presented here only to describe the nature of an assurance engagement. To obtain a full understanding of the objectives and elements of an assurance engagement it is necessary to refer to the full text contained in SAE 100 and the International Standard on Assurance Engagements.

- 8.3 Whether a particular engagement is an assurance engagement will depend upon whether it exhibits all the following elements:
- (a) A three party relationship involving:
 - (i) A professional accountant;
 - (ii) A responsible party; and
 - (iii) An intended user;
 - (b) A subject matter;
 - (c) Suitable criteria;
 - (d) An engagement process; and
 - (e) A conclusion.

The responsible party and the intended user will often be from separate organizations but need not be. A responsible party and an intended user may both be within the same organization. For example, a governing body may seek assurance about information provided by a component of that organization. The relationship between the responsible party and the intended user needs to be viewed within the context of a specific engagement.

- 8.4 There is a broad range of engagements to provide a high or moderate level of assurance. Such engagements may include:
- Engagements to report on a broad range of subject matters covering financial and non-financial information;

- Attest and direct reporting engagements;
 - Engagements to report internally and externally; and
 - Engagements in the private and public sector.
- 8.5 The subject matter of an assurance engagement may take many forms, such as the following:
- Data (for example, historical or prospective financial information, statistical information, performance indicators);
 - Systems and processes (for example, internal controls); or
 - Behavior (for example, corporate governance, compliance with regulation, human resource practices).
- 8.6 Not all engagements performed by professional accountants are assurance engagements. Other engagements frequently performed by professional accountants that are not assurance engagements include:
- Agreed-upon procedures;
 - Compilation of financial or other information;
 - Preparation of tax returns when no conclusion is expressed, and tax consulting;
 - Management consulting; and
 - Other advisory services.
- 8.7 This section of the Code of Ethics (this section) provides a framework, built on principles, for identifying, evaluating and responding to threats to independence. The framework establishes principles that members of assurance teams, firms and network firms should use to identify threats to independence, evaluate the significance of those threats, and, if the threats are other than clearly insignificant, identify and apply safeguards to eliminate the threats or reduce them to an acceptable level. Judgment is needed to determine which safeguards are to be applied. Some safeguards may eliminate the threat while others may reduce the threat to an acceptable level. This section requires members of assurance teams, firms and network firms to apply the principles to the particular circumstances under consideration. The examples presented are intended to illustrate the application of the principles in this section and are not intended to be, nor should they be interpreted as, an exhaustive list of all circumstances that may create threats to independence. Consequently, it is not sufficient for a member of an assurance team, a firm or a network firm merely to comply with the examples presented, rather they should apply the principles in this section to the particular circumstances they face.

A Conceptual Approach to Independence

8.8 Independence requires:

(a) Independence of mind:

The state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

(b) Independence in appearance:

The avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.

- 8.9 The use of the word “independence” on its own may create misunderstandings. Standing alone, the word may lead observers to suppose that a person exercising professional judgment ought to be free from all economic, financial and other relationships. This is impossible, as every member of society has relationships with others. Therefore, the significance of economic, financial and other relationships should also be evaluated in the light of what a reasonable and informed third party having knowledge of all relevant information would reasonably conclude to be unacceptable.
- 8.10 Many different circumstances, or combination of circumstances, may be relevant and accordingly it is impossible to define every situation that creates threats to independence and specify the appropriate mitigating action that should be taken. In addition, the nature of assurance engagements may differ and consequently different threats may exist, requiring the application of different safeguards. A conceptual framework that requires firms and members of assurance teams to identify, evaluate and address threats to independence, rather than merely comply with a set of specific rules which may be arbitrary, is, therefore, in the public interest.
- 8.11 This section is based on such a conceptual approach, one that takes into account threats to independence, accepted safeguards and the public interest. Under this approach, firms and members of assurance teams have an obligation to identify and evaluate circumstances and relationships that create threats to independence and to take appropriate action to eliminate these threats or to reduce them to an acceptable level by the application of safeguards. In addition to identifying and evaluating relationships between the firm, network firms, members of the assurance team and the assurance client, consideration should be given to whether relationships between individuals outside of the assurance team and the assurance client create threats to independence.
- 8.12 This section provides a framework of principles that members of assurance teams, firms and network firms should use to identify threats to independence, evaluate the significance of those threats, and, if the threats are other than clearly insignificant, identify and apply safeguards to eliminate the threats or reduce them to an acceptable level, such that independence of mind and independence in appearance are not compromised.
- 8.13 The principles in this section apply to all assurance engagements. The nature of the threats to independence and the applicable safeguards necessary to eliminate the threats or reduce them to an acceptable level differ depending on the characteristics of the individual engagement: whether the assurance engagement is an audit engagement or another type of engagement; and in the case of an assurance engagement that is not an audit engagement, the purpose, subject matter and intended users of the report. A firm should, therefore, evaluate the relevant circumstances, the nature of the assurance engagement and the threats to independence in deciding whether it is appropriate to accept or continue an engagement, as well as the nature of the safeguards required and whether a particular individual should be a member of the assurance team.
- 8.14 Audit engagements provide assurance to a wide range of potential users; consequently, in addition to independence of mind, independence in appearance is of particular significance. Accordingly, for audit clients, the members of the assurance team, the firm and network firms are required to be independent of the audit client. Similar considerations in the case of assurance engagements provided to non-audit assurance clients require the members of the assurance team and the firm to be independent of the non-audit assurance client. In the case of these engagements, consideration should be given to any threats that the firm has reason to believe may be created by network firm interests and relationships.

8.15 In the case of an assurance report to a non-audit assurance client expressly restricted for use by identified users, the users of the report are considered to be knowledgeable as to the purpose, subject matter and limitations of the report through their participation in establishing the nature and scope of the firm’s instructions to deliver the services, including the criteria by which the subject matter are to be evaluated. This knowledge and enhanced ability of the firm to communicate about safeguards with all users of the report increase the effectiveness of safeguards to independence in appearance. These circumstances may be taken into account by the firm in evaluating the threats to independence and considering the applicable safeguards necessary to eliminate the threats or reduce them to an acceptable level. At a minimum, it will be necessary to apply the provisions of this section in evaluating the independence of members of the assurance team and their immediate and close family. Further, if the firm had a material financial interest, whether direct or indirect, in the assurance client, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. Limited consideration of any threats created by network firm interests and relationships may be sufficient.

8.16 Accordingly:

- For assurance engagements provided to an audit client, the members of the assurance team, the firm and network firms are required to be independent of the client;
- For assurance engagements provided to clients that are not audit clients, when the report is not expressly restricted for use by identified users, the members of the assurance team and the firm are required to be independent of the client; and
- For assurance engagements provided to clients that are not audit clients, when the assurance report is expressly restricted for use by identified users, the members of the assurance team are required to be independent of the client. In addition, the firm should not have a material direct or indirect financial interest in the client.

These independence requirements for assurance engagements are illustrated as follows:

Client	Type of Assurance Engagement		
	Audit	Non-audit – not restricted use	Non-audit – restricted use
Audit client	Assurance team, firm and network firms		
Non-audit assurance client		Assurance team and firm	Assurance team and firm has no material financial interest

8.17 The threats and safeguards identified in this section are generally discussed in the context of interests or relationships between the firm, network firms, a member of the assurance team and the assurance client. In the case of a listed audit client, the firm and any network firms are required to consider the interests and relationships that involve that client’s related entities. Ideally those entities and the interests and relationships should be identified in advance. For all other assurance clients, when the assurance team has reason to believe that a related entity of such an assurance client is relevant to the evaluation of the firm’s independence of the client, the assurance team should consider that related entity when evaluating independence and applying appropriate safeguards.

8.18 The evaluation of threats to independence and subsequent action should be supported by evidence obtained before accepting the engagement and while it is being performed. The obligation to make such an evaluation and take action arises when a firm, a network firm or a

member of the assurance team knows, or could reasonably be expected to know, of circumstances or relationships that might compromise independence. There may be occasions when the firm, a network firm or an individual inadvertently violates this section. If such an inadvertent violation occurs, it would generally not compromise independence with respect to an assurance client provided the firm has appropriate quality control policies and procedures in place to promote independence and, once discovered, the violation is corrected promptly and any necessary safeguards are applied.

- 8.19 Throughout this section, reference is made to significant and clearly insignificant threats in the evaluation of independence. In considering the significance of any particular matter, qualitative as well as quantitative factors should be taken into account. A matter should be considered clearly insignificant only if it is deemed to be both trivial and inconsequential.

Objective and Structure of this Section

- 8.20 The objective of this section is to assist firms and members of assurance teams in:
- (a) Identifying threats to independence;
 - (b) Evaluating whether these threats are clearly insignificant; and
 - (c) In cases when the threats are not clearly insignificant, identifying and applying appropriate safeguards to eliminate or reduce the threats to an acceptable level.

In situations when no safeguards are available to reduce the threat to an acceptable level, the only possible actions are to eliminate the activities or interest creating the threat, or to refuse to accept or continue the assurance engagement.

- 8.21 This section outlines the threats to independence (paragraphs 8.24 through 8.29). It then analyzes safeguards capable of eliminating these threats or reducing them to an acceptable level (paragraphs 8.30 through 8.43). The appendix to this section (paragraphs 8.100 through 8.202) sets out some examples of how this conceptual approach to independence is to be applied to specific circumstances and relationships. The examples discuss threats to independence that may be created by specific circumstances and relationships. Professional judgment is used to determine the appropriate safeguards to eliminate threats to independence or to reduce them to an acceptable level. In certain examples, the threats to independence are so significant that the only possible actions are to eliminate the activities or interest creating the threat, or to refuse to accept or continue the assurance engagement. In other examples, the threat can be eliminated or reduced to an acceptable level by the application of safeguards. The examples are not intended to be all-inclusive.
- 8.22 When threats to independence that are not clearly insignificant are identified, and the firm decides to accept or continue the assurance engagement, the decision should be documented. The documentation should include a description of the threats identified and the safeguards applied to eliminate or reduce the threats to an acceptable level.
- 8.23 The evaluation of the significance of any threats to independence and the safeguards necessary to reduce any threats to an acceptable level, takes into account the public interest. Certain entities may be of significant public interest because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. Examples of such entities might include listed companies, credit institutions, insurance companies, and pension funds. Because of the strong public interest in the financial statements of listed entities, certain paragraphs in this section deal with additional matters that are relevant to the audit of listed entities. Consideration should be given to the application of the principles set out in this section in relation to the audit of listed entities to other audit clients that may be of significant public interest.

Threats to Independence

8.24 Independence is potentially affected by self-interest, self-review, advocacy, familiarity and intimidation threats.

8.25 “Self-Interest Threat” occurs when a firm or a member of the assurance team could benefit from a financial interest in, or other self-interest conflict with, an assurance client.

Examples of circumstances that may create this threat include, but are not limited to:

- (a) A direct financial interest or material indirect financial interest in an assurance client;
- (b) A loan or guarantee to or from an assurance client or any of its directors or officers;
- (c) Undue dependence on total fees from an assurance client;
- (d) Concern about the possibility of losing the engagement;
- (e) Having a close business relationship with an assurance client;
- (f) Potential employment with an assurance client; and
- (g) Contingent fees relating to assurance engagements.

8.26 “Self-Review Threat” occurs when (1) any product or judgment of a previous assurance engagement or non-assurance engagement needs to be re-evaluated in reaching conclusions on the assurance engagement or (2) when a member of the assurance team was previously a director or officer of the assurance client, or was an employee in a position to exert direct and significant influence over the subject matter of the assurance engagement.

Examples of circumstances that may create this threat include, but are not limited to:

- (a) A member of the assurance team being, or having recently been, a director or officer of the assurance client;
- (b) A member of the assurance team being, or having recently been, an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement;
- (c) Performing services for an assurance client that directly affect the subject matter of the assurance engagement; and
- (d) Preparation of original data used to generate financial statements or preparation of other records that are the subject matter of the assurance engagement.

8.27 “Advocacy Threat” occurs when a firm, or a member of the assurance team, promotes, or may be perceived to promote, an assurance client’s position or opinion to the point that objectivity may, or may be perceived to be, compromised. Such may be the case if a firm or a member of the assurance team were to subordinate their judgment to that of the client.

Examples of circumstances that may create this threat include, but are not limited to:

- (a) Dealing in, or being a promoter of, shares or other securities in an assurance client; and
- (b) Acting as an advocate on behalf of an assurance client in litigation or in resolving disputes with third parties.

8.28 “Familiarity Threat” occurs when, by virtue of a close relationship with an assurance client, its directors, officers or employees, a firm or a member of the assurance team becomes too sympathetic to the client’s interests.

Examples of circumstances that may create this threat include, but are not limited to:

- (a) A member of the assurance team having an immediate family member or close family member who is a director or officer of the assurance client;
- (b) A member of the assurance team having an immediate family member or close family member who, as an employee of the assurance client, is in a position to exert direct and significant influence over the subject matter of the assurance engagement;
- (c) A former partner of the firm being a director, officer of the assurance client or an employee in a position to exert direct and significant influence over the subject matter of the assurance engagement;
- (d) Long association of a senior member of the assurance team with the assurance client; and
- (e) Acceptance of gifts or hospitality, unless the value is clearly insignificant, from the assurance client, its directors, officers or employees.

- 8.29 “Intimidation Threat” occurs when a member of the assurance team may be deterred from acting objectively and exercising professional skepticism by threats, actual or perceived, from the directors, officers or employees of an assurance client.

Examples of circumstances that may create this threat include, but are not limited to:

- (a) Threat of replacement over a disagreement with the application of an accounting principle; and
- (b) Pressure to reduce inappropriately the extent of work performed in order to reduce fees.

Safeguards

- 8.30 The firm and members of the assurance team have a responsibility to remain independent by taking into account the context in which they practise, the threats to independence and the safeguards available to eliminate the threats or reduce them to an acceptable level.

- 8.31 When threats are identified, other than those that are clearly insignificant, appropriate safeguards should be identified and applied to eliminate the threats or reduce them to an acceptable level. This decision should be documented. The nature of the safeguards to be applied will vary depending upon the circumstances. Consideration should always be given to what a reasonable and informed third party having knowledge of all relevant information, including safeguards applied, would reasonably conclude to be unacceptable. The consideration will be affected by matters such as the significance of the threat, the nature of the assurance engagement, the intended users of the assurance report and the structure of the firm.

- 8.32 Safeguards fall into three broad categories:

- (a) Safeguards created by the profession, legislation or regulation;
- (b) Safeguards within the assurance client; and
- (c) Safeguards within the firm’s own systems and procedures.

The firm and the members of the assurance team should select appropriate safeguards to eliminate or reduce threats to independence, other than those that are clearly insignificant, to an acceptable level.

- 8.33 Safeguards created by the profession, legislation or regulation, include the following:

- (a) Educational, training and experience requirements for entry into the profession;
- (b) Continuing education requirements;

- (c) Professional standards and monitoring and disciplinary processes;
 - (d) External review of a firm's quality control system; and
 - (e) Legislation governing the independence requirements of the firm.
- 8.34 Safeguards within the assurance client, include the following:
- (a) When the assurance client's management appoints the firm, persons other than management ratify or approve the appointment;
 - (b) The assurance client has competent employees to make managerial decisions;
 - (c) Policies and procedures that emphasize the assurance client's commitment to fair financial reporting;
 - (d) Internal procedures that ensure objective choices in commissioning non-assurance engagements; and
 - (e) A corporate governance structure, such as an audit committee, that provides appropriate oversight and communications regarding a firm's services.
- 8.35 Audit committees can have an important corporate governance role when they are independent of client management and can assist the Board of Directors in satisfying themselves that a firm is independent in carrying out its audit role. There should be regular communications between the firm and the audit committee (or other governance body if there is no audit committee) of listed entities regarding relationships and other matters that might, in the firm's opinion, reasonably be thought to bear on independence.
- 8.36 Firms should establish policies and procedures relating to independence communications with audit committees, or others charged with governance. In the case of the audit of listed entities, the firm should communicate orally and in writing at least annually, all relationships and other matters between the firm, network firms and the audit client that in the firm's professional judgment may reasonably be thought to bear on independence. Matters to be communicated will vary in each circumstance and should be decided by the firm, but should generally address the relevant matters set out in this section.
- 8.37 Safeguards within the firm's own systems and procedures may include firm-wide safeguards such as the following:
- (a) Firm leadership that stresses the importance of independence and the expectation that members of assurance teams will act in the public interest;
 - (b) Policies and procedures to implement and monitor quality control of assurance engagements;
 - (c) Documented independence policies regarding the identification of threats to independence, the evaluation of the significance of these threats and the identification and application of safeguards to eliminate or reduce the threats, other than those that are clearly insignificant, to an acceptable level;
 - (d) Internal policies and procedures to monitor compliance with firm policies and procedures as they relate to independence;
 - (e) Policies and procedures that will enable the identification of interests or relationships between the firm or members of the assurance team and assurance clients;
 - (f) Policies and procedures to monitor and, if necessary, manage the reliance on revenue received from a single assurance client;
 - (g) Using different partners and teams with separate reporting lines for the provision of non-assurance services to an assurance client;

- (h) Policies and procedures to prohibit individuals who are not members of the assurance team from influencing the outcome of the assurance engagement;
 - (i) Timely communication of a firm's policies and procedures, and any changes thereto, to all partners and professional staff, including appropriate training and education thereon;
 - (j) Designating a member of senior management as responsible for overseeing the adequate functioning of the safeguarding system;
 - (k) Means of advising partners and professional staff of those assurance clients and related entities from which they must be independent;
 - (l) A disciplinary mechanism to promote compliance with policies and procedures; and
 - (m) Policies and procedures to empower staff to communicate to senior levels within the firm any issue of independence and objectivity that concerns them; this includes informing staff of the procedures open to them.
- 8.38 Safeguards within the firm's own systems and procedures may include engagement specific safeguards such as the following:
- (a) Involving an additional professional accountant to review the work done or otherwise advise as necessary. This individual could be someone from outside the firm or network firm, or someone within the firm or network firm who was not otherwise associated with the assurance team;
 - (b) Consulting a third party, such as a committee of independent directors, a professional regulatory body or another professional accountant;
 - (c) Rotation of senior personnel;
 - (d) Discussing independence issues with the audit committee or others charged with governance;
 - (e) Disclosing to the audit committee, or others charged with governance, the nature of services provided and extent of fees charged;
 - (f) Policies and procedures to ensure members of the assurance team do not make, or assume responsibility for, management decisions for the assurance client;
 - (g) Involving another firm to perform or re-perform part of the assurance engagement;
 - (h) Involving another firm to re-perform the non-assurance service to the extent necessary to enable it to take responsibility for that service; and
 - (i) Removing an individual from the assurance team, when that individual's financial interests or relationships create a threat to independence.
- 8.39 When the safeguards available, such as those described above, are insufficient to eliminate the threats to independence or to reduce them to an acceptable level, or when a firm chooses not to eliminate the activities or interests creating the threat, the only course of action available will be the refusal to perform, or withdrawal from, the assurance engagement.

Engagement Period

- 8.40 The members of the assurance team and the firm should be independent of the assurance client during the period of the assurance engagement. The period of the engagement starts when the assurance team begins to perform assurance services and ends when the assurance report is issued, except when the assurance engagement is of a recurring nature. If the assurance engagement is expected to recur, the period of the assurance engagement ends with the notification by either party that the professional relationship has terminated or the issuance of the final assurance report, whichever is later.

8.41 In the case of an audit engagement, the engagement period includes the period covered by the financial statements reported on by the firm. When an entity becomes an audit client during or after the period covered by the financial statements that the firm will report on, the firm should consider whether any threats to independence may be created by:

- Financial or business relationships with the audit client during or after the period covered by the financial statements, but prior to the acceptance of the audit engagement; or
- Previous services provided to the audit client.

Similarly, in the case of an assurance engagement that is not an audit engagement, the firm should consider whether any financial or business relationships or previous services may create threats to independence.

8.42 If non-assurance services were provided to the audit client during or after the period covered by the financial statements but before the commencement of professional services in connection with the audit and those services would be prohibited during the period of the audit engagement, consideration should be given to the threats to independence, if any, arising from those services. If the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Discussing independence issues related to the provision of the non-assurance services with those charged with governance of the client, such as the audit committee;
- Obtaining the audit client's acknowledgement of responsibility for the results of the non-assurance services;
- Precluding personnel who provided the non-assurance services from participating in the audit engagement; and
- Engaging another firm to review the results of the non-assurance services or having another firm re-perform the non-assurance services to the extent necessary to enable it to take responsibility for those services.

8.43 Non-assurance services provided to a non-listed audit client will not impair the firm's independence when the client becomes a listed entity provided:

- The previous non-assurance services were permissible under this section for non-listed audit clients;
- The services will be terminated within a reasonable period of time of the client becoming a listed entity, if they are impermissible under this section for listed audit clients; and
- The firm has implemented appropriate safeguards to eliminate any threats to independence arising from the previous services or reduce them to an acceptable level.

APPENDIX TO SECTION 8

Application of Principles to Specific Situations

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a. Introduction

- 8.100 The following examples describe specific circumstances and relationships that may create threats to independence. The examples describe the potential threats created and the safeguards that may be appropriate to eliminate the threats or reduce them to an acceptable level in each circumstance. The examples are not all-inclusive. In practice, the firm, network firms and the members of the assurance team will be required to assess the implications of similar, but different, circumstances and relationships and to determine whether safeguards, including the safeguards in paragraphs 8.33 through 8.38 can be applied to satisfactorily address the threats to independence. Paragraphs 8.1 through 8.43 of this section provide conceptual guidance to assist in this process.
- 8.101 Some of the examples deal with audit clients while others deal with assurance clients that are not audit clients. The examples illustrate how safeguards should be applied to fulfill the requirement for the members of the assurance team, the firm and network firms to be independent of an audit client, and for the members of the assurance team and the firm to be independent of an assurance client that is not an audit client. The examples do not include assurance reports to a non-audit assurance client expressly restricted for use by identified users. As stated in paragraph 8.15 for such engagements, members of the assurance team and their immediate and close family are required to be independent of the assurance client. Further, the firm should not have a material financial interest, direct or indirect, in the assurance client.

b. Financial Interests

- 8.102 A financial interest in an assurance client may create a self-interest threat. In evaluating the significance of the threat, and the appropriate safeguards to be applied to eliminate the threat or reduce it to an acceptable level, it is necessary to examine the nature of the financial interest. This includes an evaluation of the role of the person holding the financial interest, the materiality of the financial interest and the type of financial interest (direct or indirect).
- 8.103 When evaluating the type of financial interest, consideration should be given to the fact that financial interests range from those where the individual has no control over the investment vehicle or the financial interest held (e.g., a mutual fund, unit trust or similar intermediary vehicle) to those where the individual has control over the financial interest (e.g., as a trustee) or is able to influence investment decisions. In evaluating the significance of any threat to independence, it is important to consider the degree of control or influence that can be exercised over the intermediary, the financial interest held, or its investment strategy. When control exists, the financial interest should be considered direct. Conversely, when the holder of the financial interest has no ability to exercise such control the financial interest should be considered indirect.

Examples Applicable to all Assurance Clients

- 8.104 If a member of the assurance team, or their immediate family member, has a direct financial interest, or a material indirect financial interest, in the assurance client, the self-interest threat created would be so significant the only safeguards available to eliminate the threat or reduce it to an acceptable level would be to:
- Dispose of the direct financial interest prior to the individual becoming a member of the assurance team;

- Dispose of the indirect financial interest in total or dispose of a sufficient amount of it so that the remaining interest is no longer material prior to the individual becoming a member of the assurance team; or
- Remove the member of the assurance team from the assurance engagement.

8.105 If a member of the assurance team, or their immediate family member receives, by way of, for example, an inheritance, gift or, as a result of a merger, a direct financial interest or a material indirect financial interest in the assurance client, a self-interest threat would be created. The following safeguards should be applied to eliminate the threat or reduce it to an acceptable level:

- Disposing of the financial interest at the earliest practical date; or
- Removing the member of the assurance team from the assurance engagement.

During the period prior to disposal of the financial interest or the removal of the individual from the assurance team, consideration should be given to whether additional safeguards are necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Discussing the matter with those charged with governance, such as the audit committee; or
- Involving an additional professional accountant to review the work done, or otherwise advise as necessary.

8.106 When a member of the assurance team knows that his or her close family member has a direct financial interest or a material indirect financial interest in the assurance client, a self-interest threat may be created. In evaluating the significance of any threat, consideration should be given to the nature of the relationship between the member of the assurance team and the close family member and the materiality of the financial interest. Once the significance of the threat has been evaluated, safeguards should be considered and applied as necessary. Such safeguards might include:

- The close family member disposing of all or a sufficient portion of the financial interest at the earliest practical date;
- Discussing the matter with those charged with governance, such as the audit committee;
- Involving an additional professional accountant who did not take part in the assurance engagement to review the work done by the member of the assurance team with the close family relationship or otherwise advise as necessary; or
- Removing the individual from the assurance engagement.

8.107 When a firm or a member of the assurance team holds a direct financial interest or a material indirect financial interest in the assurance client as a trustee, a self-interest threat may be created by the possible influence of the trust over the assurance client. Accordingly, such an interest should only be held when:

- The member of the assurance team, an immediate family member of the member of the assurance team, and the firm are not beneficiaries of the trust;
- The interest held by the trust in the assurance client is not material to the trust;
- The trust is not able to exercise significant influence over the assurance client; and
- The member of the assurance team or the firm does not have significant influence over any investment decision involving a financial interest in the assurance client.

8.108 Consideration should be given to whether a self-interest threat may be created by the financial interests of individuals outside of the assurance team and their immediate and close family members. Such individuals would include:

- Partners, and their immediate family members, who are not members of the assurance team;
- Partners and managerial employees who provide non-assurance services to the assurance client; and
- Individuals who have a close personal relationship with a member of the assurance team.

Whether the interests held by such individuals may create a self-interest threat will depend upon factors such as:

- The firm's organizational, operating and reporting structure; and
- The nature of the relationship between the individual and the member of the assurance team.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Where appropriate, policies to restrict people from holding such interests;
- Discussing the matter with those charged with governance, such as the audit committee; or
- Involving an additional professional accountant who did not take part in the assurance engagement to review the work done or otherwise advise as necessary.

8.109 An inadvertent violation of this section as it relates to a financial interest in an assurance client would not impair the independence of the firm, the network firm or a member of the assurance team when:

- (a) The firm, and the network firm, has established policies and procedures that require all professionals to report promptly to the firm any breaches resulting from the purchase, inheritance or other acquisition of a financial interest in the assurance client;
- (b) The firm, and the network firm, promptly notifies the professional that the financial interest should be disposed of; and
- (c) The disposal occurs at the earliest practical date after identification of the issue, or the professional is removed from the assurance team.

8.110 When an inadvertent violation of this section relating to a financial interest in an assurance client has occurred, the firm should consider whether any safeguards should be applied. Such safeguards might include:

- Involving an additional professional accountant who did not take part in the assurance engagement to review the work done by the member of the assurance team; or
- Excluding the individual from any substantive decision-making concerning the assurance engagement.

Examples Applicable to Audit Clients

8.111 If a firm, or a network firm, has a direct financial interest in an audit client of the firm the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. Consequently, disposal of the financial interest would be the only action appropriate to permit the firm to perform the engagement.

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- 8.112 If a firm, or a network firm, has a material indirect financial interest in an audit client of the firm a self-interest threat is also created. The only actions appropriate to permit the firm to perform the engagement would be for the firm, or the network firm, either to dispose of the indirect interest in total or to dispose of a sufficient amount of it so that the remaining interest is no longer material.
- 8.113 If a firm, or a network firm, has a material financial interest in an entity that has a controlling interest in an audit client, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. The only actions appropriate to permit the firm to perform the engagement would be for the firm, or the network firm, either to dispose of the financial interest in total or to dispose of a sufficient amount of it so that the remaining interest is no longer material.
- 8.114 If the retirement benefit plan of a firm, or network firm, has a financial interest in an audit client a self-interest threat may be created. Accordingly, the significance of any such threat created should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level.
- 8.115 If other partners, including partners who do not perform assurance engagements, or their immediate family, in the office in which the lead engagement partner practises in connection with the audit hold a direct financial interest or a material indirect financial interest in that audit client, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. Accordingly, such partners or their immediate family should not hold any such financial interests in such an audit client.
- 8.116 The office in which the lead engagement partner practises in connection with the audit is not necessarily the office to which that partner is assigned. Accordingly, when the lead engagement partner is located in a different office from that of the other members of the assurance team, judgment should be used to determine in which office the partner practises in connection with that audit.
- 8.117 If other partners and managerial employees who provide non-assurance services to the audit client, except those whose involvement is clearly insignificant, or their immediate family, hold a direct financial interest or a material indirect financial interest in the audit client, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. Accordingly, such personnel or their immediate family should not hold any such financial interests in such an audit client.
- 8.118 A financial interest in an audit client that is held by an immediate family member of (a) a partner located in the office in which the lead engagement partner practises in connection with the audit, or (b) a partner or managerial employee who provides non-assurance services to the audit client is not considered to create an unacceptable threat provided it is received as a result of their employment rights (e.g., pension rights or share options) and, where necessary, appropriate safeguards are applied to reduce any threat to independence to an acceptable level.
- 8.119 A self-interest threat may be created if the firm, or the network firm, or a member of the assurance team has an interest in an entity and an audit client, or a director, officer or controlling owner thereof also has an investment in that entity. Independence is not compromised with respect to the audit client if the respective interests of the firm, the network firm, or member of the assurance team, and the audit client, or director, officer or controlling owner thereof are both immaterial and the audit client cannot exercise significant influence over the entity. If an interest is material, to either the firm, the network firm or the audit client, and the audit client can exercise significant influence over the entity, no safeguards are available to reduce the threat to an acceptable level and the firm, the network

firm, should either dispose of the interest or decline the audit engagement. Any member of the assurance team with such a material interest should either:

- Dispose of the interest;
- Dispose of a sufficient amount of the interest so that the remaining interest is no longer material; or
- Withdraw from the audit.

Examples Applicable to Non-Audit Assurance Clients

- 8.120 If a firm has a direct financial interest in an assurance client that is not an audit client the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. Consequently, disposal of the financial interest would be the only action appropriate to permit the firm to perform the engagement.
- 8.121 If a firm has a material indirect financial interest in an assurance client that is not an audit client a self-interest threat is also created. The only action appropriate to permit the firm to perform the engagement would be for the firm to either dispose of the indirect interest in total or to dispose of a sufficient amount of it so that the remaining interest is no longer material.
- 8.122 If a firm has a material financial interest in an entity that has a controlling interest in an assurance client that is not an audit client, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level. The only action appropriate to permit the firm to perform the engagement would be for the firm either to dispose of the financial interest in total or to dispose of a sufficient amount of it so that the remaining interest is no longer material.
- 8.123 When a restricted use report for an assurance engagement that is not an audit engagement is issued, exceptions to the provisions in paragraphs 8.104 through 8.108 and 8.120 through 8.122 are set out in 8.15.

c. Loans and Guarantees

- 8.124 A loan from, or a guarantee thereof by, an assurance client that is a bank or a similar institution, to the firm would not create a threat to independence provided the loan is made under normal lending procedures, terms and requirements and the loan is immaterial to both the firm and the assurance client. If the loan is material to the assurance client or the firm it may be possible, through the application of safeguards, to reduce the self-interest threat created to an acceptable level. Such safeguards might include involving an additional professional accountant from outside the firm, or network firm, to review the work performed.
- 8.125 A loan from, or a guarantee thereof by, an assurance client that is a bank or a similar institution, to a member of the assurance team or their immediate family would not create a threat to independence provided the loan is made under normal lending procedures, terms and requirements. Examples of such loans include home mortgages, bank overdrafts, car loans and credit card balances.
- 8.126 Similarly, deposits made by, or brokerage accounts of, a firm or a member of the assurance team with an assurance client that is a bank, broker or similar institution would not create a threat to independence provided the deposit or account is held under normal commercial terms.
- 8.127 If the firm, or a member of the assurance team, makes a loan to an assurance client, that is not a bank or similar institution, or guarantees such an assurance client's borrowing, the self-

interest threat created would be so significant no safeguard could reduce the threat to an acceptable level, unless the loan or guarantee is immaterial to both the firm or the member of the assurance team and the assurance client.

- 8.128 Similarly, if the firm or a member of the assurance team accepts a loan from, or has borrowing guaranteed by, an assurance client that is not a bank or similar institution, the self-interest threat created would be so significant no safeguard could reduce the threat to an acceptable level, unless the loan or guarantee is immaterial to both the firm or the member of the assurance team and the assurance client.
- 8.129 The examples in paragraphs 8.124 through 8.128 relate to loans and guarantees between the firm and an assurance client. In the case of an audit engagement, the provisions should be applied to the firm, all network firms and the audit client.

d. Close Business Relationships with Assurance Clients

- 8.130 A close business relationship between a firm or a member of the assurance team and the assurance client or its management, or between the firm, a network firm and an audit client, will involve a commercial or common financial interest and may create self-interest and intimidation threats. The following are examples of such relationships:
- (a) Having a material financial interest in a joint venture with the assurance client or a controlling owner, director, officer or other individual who performs senior managerial functions for that client;
 - (b) Arrangements to combine one or more services or products of the firm with one or more services or products of the assurance client and to market the package with reference to both parties; and
 - (c) Distribution or marketing arrangements under which the firm acts as a distributor or marketer of the assurance client's products or services, or the assurance client acts as the distributor or marketer of the products or services of the firm.

In the case of an audit client, unless the financial interest is immaterial and the relationship is clearly insignificant to the firm, the network firm and the audit client, no safeguards could reduce the threat to an acceptable level. In the case of an assurance client that is not an audit client, unless the financial interest is immaterial and the relationship is clearly insignificant to the firm and the assurance client, no safeguards could reduce the threat to an acceptable level. Consequently, in both these circumstances the only possible courses of action are to:

- Terminate the business relationship;
- Reduce the magnitude of the relationship so that the financial interest is immaterial and the relationship is clearly insignificant; or
- Refuse to perform the assurance engagement.

Unless any such financial interest is immaterial and the relationship is clearly insignificant to the member of the assurance team, the only appropriate safeguard would be to remove the individual from the assurance team.

- 8.131 In the case of an audit client, business relationships involving an interest held by the firm, a network firm or a member of the assurance team or their immediate family in a closely held entity when the audit client or a director or officer of the audit client, or any group thereof, also has an interest in that entity, do not create threats to independence provided:
- The relationship is clearly insignificant to the firm, the network firm and the audit client;
 - The interest held is immaterial to the investor, or group of investors; and

- The interest does not give the investor, or group of investors, the ability to control the closely held entity.

8.132 The purchase of goods and services from an assurance client by the firm (or from an audit client by a network firm) or a member of the assurance team would not generally create a threat to independence providing the transaction is in the normal course of business and on an arm's length basis. However, such transactions may be of a nature or magnitude so as to create a self-interest threat. If the threat created is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Eliminating or reducing the magnitude of the transaction;
- Removing the individual from the assurance team; or
- Discussing the issue with those charged with governance, such as the audit committee.

e. Family and Personal Relationships

8.133 Family and personal relationships between a member of the assurance team and a director, an officer or certain employees, depending on their role, of the assurance client, may create self-interest, familiarity or intimidation threats. It is impracticable to attempt to describe in detail the significance of the threats that such relationships may create. The significance will depend upon a number of factors including the individual's responsibilities on the assurance engagement, the closeness of the relationship and the role of the family member or other individual within the assurance client. Consequently, there is a wide spectrum of circumstances that will need to be evaluated and safeguards to be applied to reduce the threat to an acceptable level.

8.134 When an immediate family member of a member of the assurance team is a director, an officer or an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement, or was in such a position during any period covered by the engagement, the threats to independence can only be reduced to an acceptable level by removing the individual from the assurance team. The closeness of the relationship is such that no other safeguard could reduce the threat to independence to an acceptable level. If application of this safeguard is not used, the only course of action is to withdraw from the assurance engagement. For example, in the case of an audit of financial statements, if the spouse of a member of the assurance team is an employee in a position to exert direct and significant influence on the preparation of the audit client's accounting records or financial statements, the threat to independence could only be reduced to an acceptable level by removing the individual from the assurance team.

8.135 When a close family member of a member of the assurance team is a director, an officer, or an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement, threats to independence may be created. The significance of the threats will depend on factors such as:

- The position the close family member holds with the client; and
- The role of the professional on the assurance team.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Removing the individual from the assurance team;

- Where possible, structuring the responsibilities of the assurance team so that the professional does not deal with matters that are within the responsibility of the close family member; or
 - Policies and procedures to empower staff to communicate to senior levels within the firm any issue of independence and objectivity that concerns them.
- 8.136 In addition, self-interest, familiarity or intimidation threats may be created when a person who is other than an immediate or close family member of a member of the assurance team has a close relationship with the member of the assurance team and is a director, an officer or an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement. Therefore, members of the assurance team are responsible for identifying any such persons and for consulting in accordance with firm procedures. The evaluation of the significance of any threat created and the safeguards appropriate to eliminate the threat or reduce it to an acceptable level will include considering matters such as the closeness of the relationship and the role of the individual within the assurance client.
- 8.137 Consideration should be given to whether self-interest, familiarity or intimidation threats may be created by a personal or family relationship between a partner or employee of the firm who is not a member of the assurance team and a director, an officer or an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement. Therefore partners and employees of the firm are responsible for identifying any such relationships and for consulting in accordance with firm procedures. The evaluation of the significance of any threat created and the safeguards appropriate to eliminate the threat or reduce it to an acceptable level will include considering matters such as the closeness of the relationship, the interaction of the firm professional with the assurance team, the position held within the firm, and the role of the individual within the assurance client.
- 8.138 An inadvertent violation of this section as it relates to family and personal relationships would not impair the independence of a firm or a member of the assurance team when:
- (a) The firm has established policies and procedures that require all professionals to report promptly to the firm any breaches resulting from changes in the employment status of their immediate or close family members or other personal relationships that create threats to independence;
 - (b) Either the responsibilities of the assurance team are re-structured so that the professional does not deal with matters that are within the responsibility of the person with whom he or she is related or has a personal relationship, or, if this is not possible, the firm promptly removes the professional from the assurance engagement; and
 - (c) Additional care is given to reviewing the work of the professional.
- 8.139 When an inadvertent violation of this section relating to family and personal relationships has occurred, the firm should consider whether any safeguards should be applied. Such safeguards might include:
- Involving an additional professional accountant who did not take part in the assurance engagement to review the work done by the member of the assurance team; or
 - Excluding the individual from any substantive decision-making concerning the assurance engagement.

f. Employment with Assurance Clients

8.140 A firm or a member of the assurance team's independence may be threatened if a director, an officer or an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement has been a member of the assurance team or partner of the firm. Such circumstances may create self-interest, familiarity and intimidation threats particularly when significant connections remain between the individual and his or her former firm. Similarly, a member of the assurance team's independence may be threatened when an individual participates in the assurance engagement knowing, or having reason to believe, that he or she is to, or may, join the assurance client some time in the future.

8.141 If a member of the assurance team, partner or former partner of the firm has joined the assurance client, the significance of the self-interest, familiarity or intimidation threats created will depend upon the following factors:

- The position the individual has taken at the assurance client;
- The amount of any involvement the individual will have with the assurance team;
- The length of time that has passed since the individual was a member of the assurance team or firm; and
- The former position of the individual within the assurance team or firm.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Considering the appropriateness or necessity of modifying the assurance plan for the assurance engagement;
- Assigning an assurance team to the subsequent assurance engagement that is of sufficient experience in relation to the individual who has joined the assurance client;
- Involving an additional professional accountant who was not a member of the assurance team to review the work done or otherwise advise as necessary; or
- Quality control review of the assurance engagement.

In all cases, all of the following safeguards are necessary to reduce the threat to an acceptable level:

- The individual concerned is not entitled to any benefits or payments from the firm unless these are made in accordance with fixed pre-determined arrangements. In addition, any amount owed to the individual should not be of such significance to threaten the firm's independence; and
- The individual does not continue to participate or appear to participate in the firm's business or professional activities.

8.142 A self-interest threat is created when a member of the assurance team participates in the assurance engagement while knowing, or having reason to believe, that he or she is to, or may, join the assurance client some time in the future. This threat can be reduced to an acceptable level by the application of all of the following safeguards:

- Policies and procedures to require the individual to notify the firm when entering serious employment negotiations with the assurance client; and
- Removal of the individual from the assurance engagement.

In addition, consideration should be given to performing an independent review of any significant judgments made by that individual while on the engagement.

g. Recent Service with Assurance Clients

- 8.143 To have a former officer, director or employee of the assurance client serve as a member of the assurance team may create self-interest, self-review and familiarity threats. This would be particularly true when a member of the assurance team has to report on, for example, subject matter he or she had prepared or elements of the financial statements he or she had valued while with the assurance client.
- 8.144 If, during the period covered by the assurance report, a member of the assurance team had served as an officer or director of the assurance client, or had been an employee in a position to exert direct and significant influence over the subject matter of the assurance engagement, the threat created would be so significant no safeguard could reduce the threat to an acceptable level. Consequently, such individuals should not be assigned to the assurance team.
- 8.145 If, prior to the period covered by the assurance report, a member of the assurance team had served as an officer or director of the assurance client, or had been an employee in a position to exert direct and significant influence over the subject matter of the assurance engagement, this may create self-interest, self-review and familiarity threats. For example, such threats would be created if a decision made or work performed by the individual in the prior period, while employed by the assurance client, is to be evaluated in the current period as part of the current assurance engagement. The significance of the threats will depend upon factors such as:
- The position the individual held with the assurance client;
 - The length of time that has passed since the individual left the assurance client; and
 - The role the individual plays on the assurance team.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Involving an additional professional accountant to review the work done by the individual as part of the assurance team or otherwise advise as necessary; or
- Discussing the issue with those charged with governance, such as the audit committee.

h. Serving as an Officer or Director on the Board of Assurance Clients

- 8.146 If a partner or employee of the firm serves as an officer or as a director on the board of an assurance client the self-review and self-interest threats created would be so significant no safeguard could reduce the threats to an acceptable level. In the case of an audit engagement, if a partner or employee of a network firm were to serve as an officer or as a director on the board of an audit client the threats created would be so significant no safeguard could reduce the threats to an acceptable level. Consequently, if such an individual were to accept such a position the only course of action is to refuse to perform, or to withdraw from the assurance engagement.
- 8.147 The position of Company Secretary has different implications in different jurisdictions. The duties may range from administrative duties such as personnel management and the maintenance of company records and registers, to duties as diverse as ensuring that the company complies with regulations or providing advice on corporate governance matters.

Generally this position is seen to imply a close degree of association with the entity and may create self-review and advocacy threats.

- 8.148 If a partner or employee of the firm or a network firm serves as Company Secretary for an audit client the self-review and advocacy threats created would generally be so significant, no safeguard could reduce the threat to an acceptable level unless the duties and functions undertaken are limited to those of a routine and formal administrative nature such as the preparation of minutes and maintenance of statutory returns, and are permitted by law.
- 8.149 Routine administrative services to support a company secretarial function or advisory work in relation to company secretarial administration matters is generally not perceived to impair independence, provided client management makes all relevant decisions.

i. Long Association of Senior Personnel with Assurance Clients

General Comments

- 8.150 Using the same senior personnel on an assurance engagement over a long period of time may create a familiarity threat. The significance of the threat will depend upon factors such as:
- The length of time that the individual has been a member of the assurance team;
 - The role of the individual on the assurance team;
 - The structure of the firm; and
 - The nature of the assurance engagement.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied to reduce the threat to an acceptable level. Such safeguards might include:

- Rotating the senior personnel off the assurance team;
- Involving an additional professional accountant who was not a member of the assurance team to review the work done by the senior personnel or otherwise advise as necessary; or
- Independent internal quality reviews.

Audit Clients that Are Listed Entities

- 8.151 Using the same lead engagement partner on an audit over a prolonged period may create a familiarity threat. This threat is particularly relevant in the context of the audit of listed entities and safeguards should be applied in such situations to reduce such threat to an acceptable level. Accordingly for the audit of listed entities:
- (a) The lead engagement partner should be rotated after a pre-defined period, normally no more than seven years; and
 - (b) A partner rotating after a pre-defined period should not resume the lead engagement partner role until a further period of time, normally two years, has elapsed.
- 8.152 When an audit client becomes a listed entity the length of time the lead engagement partner has served the audit client in that capacity should be considered in determining when the partner should be rotated. However, the partner may continue to serve as the lead engagement partner for two additional years before rotating off the engagement.

8.153 While the lead engagement partner should be rotated after such a pre-defined period, some degree of flexibility over timing of rotation may be necessary in certain circumstances. Examples of such circumstances include:

- Situations when the lead engagement partner's continuity is especially important to the audit client, for example, when there will be major changes to the audit client's structure that would otherwise coincide with the rotation of the lead engagement partner; and
- Situations when, due to the size of the firm, rotation is not possible or does not constitute an appropriate safeguard.

In all such circumstances when the lead engagement partner is not rotated after such a pre-defined period equivalent safeguards should be applied to reduce any threats to an acceptable level.

8.154 When a firm has only a few audit partners with the necessary knowledge and experience to serve as lead engagement partner on an audit client that is a listed entity, rotation of the lead partner may not be an appropriate safeguard. In these circumstances the firm should apply other safeguards to reduce the threat to an acceptable level. Such safeguards would include involving an additional professional accountant who was not otherwise associated with the assurance team to review the work done or otherwise advise as necessary. This individual could be someone from outside the firm or someone within the firm who was not otherwise associated with the assurance team.

j. Provision of Non-Assurance Services to Assurance Clients

8.155 Firms have traditionally provided to their assurance clients a range of non-assurance services that are consistent with their skills and expertise. Assurance clients value the benefits that derive from having these firms, who have a good understanding of the business, bring their knowledge and skill to bear in other areas. Furthermore, the provision of such non-assurance services will often result in the assurance team obtaining information regarding the assurance client's business and operations that is helpful in relation to the assurance engagement. The greater the knowledge of the assurance client's business, the better the assurance team will understand the assurance client's procedures and controls, and the business and financial risks that it faces. The provision of non-assurance services may, however, create threats to the independence of the firm, a network firm or the members of the assurance team, particularly with respect to perceived threats to independence. Consequently, it is necessary to evaluate the significance of any threat created by the provision of such services. In some cases it may be possible to eliminate or reduce the threat created by application of safeguards. In other cases no safeguards are available to reduce the threat to an acceptable level.

8.156 The following activities would generally create self-interest or self-review threats that are so significant that only avoidance of the activity or refusal to perform the assurance engagement would reduce the threats to an acceptable level:

- Authorizing, executing or consummating a transaction, or otherwise exercising authority on behalf of the assurance client, or having the authority to do so;
- Determining which recommendation of the firm should be implemented; and
- Reporting, in a management role, to those charged with governance.

8.157 The examples set out in paragraphs 8.163 through 8.202 are addressed in the context of the provision of non-assurance services to an assurance client. The potential threats to independence will most frequently arise when a non-assurance service is provided to an audit client. The financial statements of an entity provide financial information about a broad range of transactions and events that have affected the entity. The subject matter of other assurance services, however, may be limited in nature. Threats to independence, however, may also

arise when a firm provides a non-assurance service related to the subject matter of a non-audit assurance engagement. In such cases, consideration should be given to the significance of the firm's involvement with the subject matter of the non-audit assurance engagement, whether any self-review threats are created and whether any threats to independence could be reduced to an acceptable level by application of safeguards, or whether the non-assurance engagement should be declined. When the non-assurance service is not related to the subject matter of the non-audit assurance engagement, the threats to independence will generally be clearly insignificant.

8.158 The following activities may also create self-review or self-interest threats:

- Having custody of an assurance client's assets;
- Supervising assurance client employees in the performance of their normal recurring activities; and
- Preparing source documents or originating data, in electronic or other form, evidencing the occurrence of a transaction (for example, purchase orders, payroll time records, and customer orders).

The significance of any threat created should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level. Such safeguards might include:

- Making arrangements so that personnel providing such services do not participate in the assurance engagement;
- Involving an additional professional accountant to advise on the potential impact of the activities on the independence of the firm and the assurance team; or
- Other relevant safeguards set out in local regulations.

8.159 New developments in business, the evolution of financial markets, rapid changes in information technology, and the consequences for management and control, make it impossible to draw up an all-inclusive list of all situations when providing non-assurance services to an assurance client might create threats to independence and of the different safeguards that might eliminate these threats or reduce them to an acceptable level. In general, however, a firm may provide services beyond the assurance engagement provided any threats to independence have been reduced to an acceptable level.

8.160 The following safeguards may be particularly relevant in reducing to an acceptable level threats created by the provision of non-assurance services to assurance clients:

- Policies and procedures to prohibit professional staff from making management decisions for the assurance client, or assuming responsibility for such decisions;
- Discussing independence issues related to the provision of non-assurance services with those charged with governance, such as the audit committee;
- Policies within the assurance client regarding the oversight responsibility for provision of non-assurance services by the firm;
- Involving an additional professional accountant to advise on the potential impact of the non-assurance engagement on the independence of the member of the assurance team and the firm;
- Involving an additional professional accountant outside of the firm to provide assurance on a discrete aspect of the assurance engagement;
- Obtaining the assurance client's acknowledgement of responsibility for the results of the work performed by the firm;

- Disclosing to those charged with governance, such as the audit committee, the nature and extent of fees charged; or
 - Making arrangements so that personnel providing non-assurance services do not participate in the assurance engagement.
- 8.161 Before the firm accepts an engagement to provide a non-assurance service to an assurance client, consideration should be given to whether the provision of such a service would create a threat to independence. In situations when a threat created is other than clearly insignificant, the non-assurance engagement should be declined unless appropriate safeguards can be applied to eliminate the threat or reduce it to an acceptable level.
- 8.162 The provision of certain non-assurance services to audit clients may create threats to independence so significant that no safeguard could eliminate the threat or reduce it to an acceptable level. However, the provision of such services to a related entity, division or discrete financial statement item of such clients may be permissible when any threats to the firm's independence have been reduced to an acceptable level by arrangements for that related entity, division or discrete financial statement item to be audited by another firm or when another firm re-performs the non-assurance service to the extent necessary to enable it to take responsibility for that service.

Preparing Accounting Records and Financial Statements

- 8.163 Assisting an audit client in matters such as preparing accounting records or financial statements may create a self-review threat when the financial statements are subsequently audited by the firm.
- 8.164 It is the responsibility of client management to ensure that accounting records are kept and financial statements are prepared, although they may request the firm to provide assistance. If firm, or network firm, personnel providing such assistance make management decisions, the self-review threat created could not be reduced to an acceptable level by any safeguards. Consequently, personnel should not make such decisions. Examples of such managerial decisions include the following:
- Determining or changing journal entries, or the classifications for accounts or transaction or other accounting records without obtaining the approval of the audit client;
 - Authorizing or approving transactions; and
 - Preparing source documents or originating data (including decisions on valuation assumptions), or making changes to such documents or data.
- 8.165 The audit process involves extensive dialogue between the firm and management of the audit client. During this process, management requests and receives significant input regarding such matters as accounting principles and financial statement disclosure, the appropriateness of controls and the methods used in determining the stated amounts of assets and liabilities. Technical assistance of this nature and advice on accounting principles for audit clients are an appropriate means to promote the fair presentation of the financial statements. The provision of such advice does not generally threaten the firm's independence. Similarly, the audit process may involve assisting an audit client in resolving account reconciliation problems, analyzing and accumulating information for regulatory reporting, assisting in the preparation of consolidated financial statements (including the translation of local statutory accounts to comply with group accounting policies and the transition to a different reporting framework such as International Accounting Standards), drafting disclosure items, proposing adjusting journal entries and providing assistance and advice in the preparation of local statutory accounts of subsidiary entities. These services are considered to be a normal part of the audit process and do not, under normal circumstances, threaten independence.

General Comments

- 8.166 The examples in paragraphs 8.167 through 8.170 indicate that self-review threats may be created if the firm is involved in the preparation of accounting records or financial statements and those financial statements are subsequently the subject matter of an audit engagement of the firm. This notion may be equally applicable in situations when the subject matter of the assurance engagement is not financial statements. For example, a self-review threat would be created if the firm developed and prepared prospective financial information and subsequently provided assurance on this prospective financial information. Consequently, the firm should evaluate the significance of any self-review threat created by the provision of such services. If the self-review threat is other than clearly insignificant safeguards should be considered and applied as necessary to reduce the threat to an acceptable level.

Audit Clients that are not Listed Entities

- 8.167 The firm, or a network firm, may provide an audit client that is not a listed entity with accounting and bookkeeping services, including payroll services, of a routine or mechanical nature, provided any self-review threat created is reduced to an acceptable level. Examples of such services include:

- Recording transactions for which the audit client has determined or approved the appropriate account classification;
- Posting coded transactions to the audit client's general ledger;
- Preparing financial statements based on information in the trial balance; and
- Posting audit client approved entries to the trial balance.

The significance of any threat created should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Making arrangements so such services are not performed by a member of the assurance team;
- Implementing policies and procedures to prohibit the individual providing such services from making any managerial decisions on behalf of the audit client;
- Requiring the source data for the accounting entries to be originated by the audit client;
- Requiring the underlying assumptions to be originated and approved by the audit client; or
- Obtaining audit client approval for any proposed journal entries or other changes affecting the financial statements.

Audit Clients that are Listed Entities

- 8.168 The provision of accounting and bookkeeping services, including payroll services and the preparation of financial statements or financial information which forms the basis of the financial statements on which the audit report is provided, on behalf of an audit client that is a listed entity, may impair the independence of the firm or network firm, or at least give the appearance of impairing independence. Accordingly, no safeguard other than the prohibition of such services, except in emergency situations and when the services fall within the statutory audit mandate, could reduce the threat created to an acceptable level. Therefore, a firm or a network firm should not, with the limited exceptions below, provide such services to listed entities which are audit clients.

- 8.169 The provision of accounting and bookkeeping services of a routine or mechanical nature to divisions or subsidiaries of listed audit clients would not be seen as impairing independence with respect to the audit client provided that the following conditions are met:
- The services do not involve the exercise of judgment;
 - The divisions or subsidiaries for which the service is provided are collectively immaterial to the audit client, or the services provided are collectively immaterial to the division or subsidiary; and
 - The fees to the firm, or network firm, from such services are collectively clearly insignificant.

If such services are provided, all of the following safeguards should be applied:

- The firm, or network firm, should not assume any managerial role nor make any managerial decisions;
- The listed audit client should accept responsibility for the results of the work; and
- Personnel providing the services should not participate in the audit.

Emergency Situations

- 8.170 The provision of accounting and bookkeeping services to audit clients in emergency or other unusual situations, when it is impractical for the audit client to make other arrangements, would not be considered to pose an unacceptable threat to independence provided:
- The firm, or network firm, does not assume any managerial role or make any managerial decisions;
 - The audit client accepts responsibility for the results of the work; and
 - Personnel providing the services are not members of the assurance team.

Valuation Services

- 8.171 A valuation comprises the making of assumptions with regard to future developments, the application of certain methodologies and techniques, and the combination of both in order to compute a certain value, or range of values, for an asset, a liability or for a business as a whole.
- 8.172 A self-review threat may be created when a firm or network firms performs a valuation for an audit client that is to be incorporated into the client's financial statements.
- 8.173 If the valuation service involves the valuation of matters material to the financial statements and the valuation involves a significant degree of subjectivity, the self-review threat created could not be reduced to an acceptable level by the application of any safeguard. Accordingly, such valuation services should not be provided or, alternatively, the only course of action would be to withdraw from the audit engagement.
- 8.174 Performing valuation services that are neither separately, nor in the aggregate, material to the financial statements, or that do not involve a significant degree of subjectivity, may create a self-review threat that could be reduced to an acceptable level by the application of safeguards. Such safeguards might include:
- Involving an additional professional accountant who was not a member of the assurance team to review the work done or otherwise advise as necessary;
 - Confirming with the audit client their understanding of the underlying assumptions of the valuation and the methodology to be used and obtaining approval for their use;

- Obtaining the audit client's acknowledgement of responsibility for the results of the work performed by the firm; and
- Making arrangements so that personnel providing such services do not participate in the audit engagement.

In determining whether the above safeguards would be effective, consideration should be given to the following matters:

- The extent of the audit client's knowledge, experience and ability to evaluate the issues concerned, and the extent of their involvement in determining and approving significant matters of judgment;
- The degree to which established methodologies and professional guidelines are applied when performing a particular valuation service;
- For valuations involving standard or established methodologies, the degree of subjectivity inherent in the item concerned;
- The reliability and extent of the underlying data;
- The degree of dependence on future events of a nature which could create significant volatility inherent in the amounts involved; and
- The extent and clarity of the disclosures in the financial statements.

8.175 When a firm, or a network firm, performs a valuation service for an audit client for the purposes of making a filing or return to a tax authority, computing an amount of tax due by the assurance client, or for the purpose of tax planning, this would not create a significant threat to independence because such valuations are generally subject to external review, for example by a tax authority.

8.176 When the firm performs a valuation that forms part of the subject matter of an assurance engagement that is not an audit engagement, the firm should consider any self-review threats. If the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level.

Provision of Taxation Services to Audit Clients

8.177 In Hong Kong, the firm may be asked to provide taxation services to an audit client. Taxation services comprise a broad range of services, including compliance, planning, provision of formal taxation opinions and assistance in the resolution of tax disputes. Such assignments are generally not seen to create threats to independence.

Provision of Internal Audit Services to Audit Clients

8.178 A self-review threat may be created when a firm, or network firm, provides internal audit services to an audit client. Internal audit services may comprise an extension of the firm's audit service beyond requirements of generally accepted auditing standards, assistance in the performance of a client's internal audit activities or outsourcing of the activities. In evaluating any threats to independence, the nature of the service will need to be considered. For this purpose, internal audit services do not include operational internal audit services unrelated to the internal accounting controls, financial systems or financial statements.

8.179 Services involving an extension of the procedures required to conduct an audit in accordance with SASs or International Standards on Auditing would not be considered to impair independence with respect to an audit client provided that the firm's or network firm's

personnel do not act or appear to act in a capacity equivalent to a member of audit client management.

- 8.180 When the firm, or a network firm, provides assistance in the performance of a client's internal audit activities or undertakes the outsourcing of some of the activities, any self-review threat created may be reduced to an acceptable level by ensuring that there is a clear separation between the management and control of the internal audit by audit client management and the internal audit activities themselves.
- 8.181 Performing a significant portion of the audit client's internal audit activities may create a self-review threat and a firm, or network firm, should consider the threats and proceed with caution before taking on such activities. Appropriate safeguards should be put in place and the firm, or network firm, should, in particular, ensure that the audit client acknowledges its responsibilities for establishing, maintaining and monitoring the system of internal controls.
- 8.182 Safeguards that should be applied in all circumstances to reduce any threats created to an acceptable level include ensuring that:
- (a) The audit client is responsible for internal audit activities and acknowledges its responsibility for establishing, maintaining and monitoring the system of internal controls;
 - (b) The audit client designates a competent employee, preferably within senior management, to be responsible for internal audit activities;
 - (c) The audit client, the audit committee or supervisory body approves the scope, risk and frequency of internal audit work;
 - (d) The audit client is responsible for evaluating and determining which recommendations of the firm should be implemented;
 - (e) The audit client evaluates the adequacy of the internal audit procedures performed and the findings resulting from the performance of those procedures by, among other things, obtaining and acting on reports from the firm; and
 - (f) The findings and recommendations resulting from the internal audit activities are reported appropriately to the audit committee or supervisory body.
- 8.183 Consideration should also be given to whether such non-assurance services should be provided only by personnel not involved in the audit engagement and with different reporting lines within the firm.

Provision of IT Systems Services to Audit Clients

- 8.184 The provision of services by a firm or network firm to an audit client that involve the design and implementation of financial information technology systems that are used to generate information forming part of a client's financial statements may create a self-review threat.
- 8.185 The self-review threat is likely to be too significant to allow the provision of such services to an audit client unless appropriate safeguards are put in place ensuring that:
- (a) The audit client acknowledges its responsibility for establishing and monitoring a system of internal controls;
 - (b) The audit client designates a competent employee, preferably within senior management, with the responsibility to make all management decisions with respect to the design and implementation of the hardware or software system;
 - (c) The audit client makes all management decisions with respect to the design and implementation process;

- (d) The audit client evaluates the adequacy and results of the design and implementation of the system; and
 - (e) The audit client is responsible for the operation of the system (hardware or software) and the data used or generated by the system.
- 8.186 Consideration should also be given to whether such non-assurance services should be provided only by personnel not involved in the audit engagement and with different reporting lines within the firm.
- 8.187 The provision of services by a firm or network firm to an audit client which involve either the design or the implementation of financial information technology systems that are used to generate information forming part of a client's financial statements may also create a self-review threat. The significance of the threat, if any, should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level.
- 8.188 The provision of services in connection with the assessment, design and implementation of internal accounting controls and risk management controls are not considered to create a threat to independence provided that firm or network firm personnel do not perform management functions.

Temporary Staff Assignments to Audit Clients

- 8.189 The lending of staff by a firm, or network firm, to an audit client may create a self-review threat when the individual is in a position to influence the preparation of a client's accounts or financial statements. In practice, such assistance may be given (particularly in emergency situations) but only on the understanding that the firm's or network firm's personnel will not be involved in:
- (a) Making management decisions;
 - (b) Approving or signing agreements or other similar documents; or
 - (c) Exercising discretionary authority to commit the client.

Each situation should be carefully analyzed to identify whether any threats are created and whether appropriate safeguards should be implemented. Safeguards that should be applied in all circumstances to reduce any threats to an acceptable level include:

- The staff providing the assistance should not be given audit responsibility for any function or activity that they performed or supervised during their temporary staff assignment; and
- The audit client should acknowledge its responsibility for directing and supervising the activities of firm, or network firm, personnel.

Provision of Litigation Support Services to Audit Clients

- 8.190 Litigation support services may include such activities as acting as an expert witness, calculating estimated damages or other amounts that might become receivable or payable as the result of litigation or other legal dispute, and assistance with document management and retrieval in relation to a dispute or litigation.

8.191 A self-review threat may be created when the litigation support services provided to an audit client include the estimation of the possible outcome and thereby affects the amounts or disclosures to be reflected in the financial statements. The significance of any threat created will depend upon factors such as:

- The materiality of the amounts involved;
- The degree of subjectivity inherent in the matter concerned; and
- The nature of the engagement.

The firm, or network firm, should evaluate the significance of any threat created and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level. Such safeguards might include:

- Policies and procedures to prohibit individuals assisting the audit client from making managerial decisions on behalf of the client;
- Using professionals who are not members of the assurance team to perform the service; or
- The involvement of others, such as independent experts.

8.192 If the role undertaken by the firm or network firm involved making managerial decisions on behalf of the audit client, the threats created could not be reduced to an acceptable level by the application of any safeguard. Therefore, the firm or network firm should not perform this type of service for an audit client.

Provision of Legal Services to Audit Clients

8.193 Legal services are defined as any services for which the person providing the services must either be admitted to practice before the Courts of the jurisdiction in which such services are to be provided, or have the required legal training to practise law. Legal services encompass a wide and diversified range of areas including both corporate and commercial services to clients, such as contract support, litigation, mergers and acquisition advice and support and the provision of assistance to clients' internal legal departments. The provision of legal services by a firm, or network firm, to an entity that is an audit client may create both self-review and advocacy threats.

8.194 Threats to independence need to be considered depending on the nature of the service to be provided, whether the service provider is separate from the assurance team and the materiality of any matter in relation to the entities' financial statements. The safeguards set out in paragraph 8.160 may be appropriate in reducing any threats to independence to an acceptable level. In circumstances when the threat to independence cannot be reduced to an acceptable level the only available action is to decline to provide such services or withdraw from the audit engagement.

8.195 The provision of legal services to an audit client which involve matters that would not be expected to have a material effect on the financial statements are not considered to create an unacceptable threat to independence.

8.196 There is a distinction between advocacy and advice. Legal services to support an audit client in the execution of a transaction (e.g., contract support, legal advice, legal due diligence and restructuring) may create self-review threats; however, safeguards may be available to reduce these threats to an acceptable level. Such a service would not generally impair independence, provided that:

- Members of the assurance team are not involved in providing the service; and

- In relation to the advice provided, the audit client makes the ultimate decision or, in relation to the transactions, the service involves the execution of what has been decided by the audit client.
- 8.197 Acting for an audit client in the resolution of a dispute or litigation in such circumstances when the amounts involved are material in relation to the financial statements of the audit client would create advocacy and self-review threats so significant no safeguard could reduce the threat to an acceptable level. Therefore, the firm should not perform this type of service for an audit client.
- 8.198 When a firm is asked to act in an advocacy role for an audit client in the resolution of a dispute or litigation in circumstances when the amounts involved are not material to the financial statements of the audit client, the firm should evaluate the significance of any advocacy and self-review threats created and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to eliminate the threat or reduce it to an acceptable level. Such safeguards might include:
- Policies and procedures to prohibit individuals assisting the audit client from making managerial decisions on behalf of the client; or
 - Using professionals who are not members of the assurance team to perform the service.
- 8.199 The appointment of a partner or an employee of the firm or network firm as General Counsel for legal affairs to an audit client would create self-review and advocacy threats that are so significant that no safeguards could reduce the threats to an acceptable level. The position of General Counsel is generally a senior management position with broad responsibility for the legal affairs of a company and consequently, no member of the firm or network firm should accept such an appointment for an audit client.

Recruiting Senior Management

- 8.200 The recruitment of senior management for an assurance client, such as those in a position to affect the subject of the assurance engagement, may create current or future self-interest, familiarity and intimidation threats. The significance of the threat will depend upon factors such as:
- The role of the person to be recruited; and
 - The nature of the assistance sought.

The firm could generally provide such services as reviewing the professional qualifications of a number of applicants and provide advice on their suitability for the post. In addition, the firm could generally produce a short-list of candidates for interview, provided it has been drawn up using criteria specified by the assurance client.

The significance of the threat created should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. In all cases, the firm should not make management decisions and the decision as to whom to hire should be left to the client.

Corporate Finance and Similar Activities

- 8.201 The provision of corporate finance services, advice or assistance to an assurance client may create advocacy and self-review threats. In the case of certain corporate finance services, the independence threats created would be so significant no safeguards could be applied to reduce the threats to an acceptable level. For example, promoting, dealing in, or underwriting of an assurance client's shares is not compatible with providing assurance services. Moreover,

committing the assurance client to the terms of a transaction or consummating a transaction on behalf of the client would create a threat to independence so significant no safeguard could reduce the threat to an acceptable level. In the case of an audit client the provision of those corporate finance services referred to above by a firm or a network firm would create a threat to independence so significant no safeguard could reduce the threat to an acceptable level.

8.202 Other corporate finance services may create advocacy or self-review threats; however, safeguards may be available to reduce these threats to an acceptable level. Examples of such services include assisting a client in developing corporate strategies, assisting in identifying or introducing a client to possible sources of capital that meet the client specifications or criteria, and providing structuring advice and assisting a client in analyzing the accounting effects of proposed transactions. Safeguards that should be considered include:

- Policies and procedures to prohibit individuals assisting the assurance client from making managerial decisions on behalf of the client;
- Using professionals who are not members of the assurance team to provide the services; and
- Ensuring the firm does not commit the assurance client to the terms of any transaction or consummate a transaction on behalf of the client.

k. Fees and Pricing

Fees - Relative Size

8.203 When the total fees generated by an assurance client represent a large proportion of a firm's total fees, the dependence on that client or client group and concern about the possibility of losing the client may create a self-interest threat. The significance of the threat will depend upon factors such as:

- The structure of the firm; and
- Whether the firm is well established or newly created.

The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Discussing the extent and nature of fees charged with the audit committee, or others charged with governance;
- Taking steps to reduce dependency on the client;
- External quality control reviews; and
- Consulting a third party, such as a professional regulatory body or another professional accountant.

8.204 A self-interest threat may also be created when the fees generated by the assurance client represent a large proportion of the revenue of an individual partner. The significance of the threat should be evaluated and, if the threat is other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threat to an acceptable level. Such safeguards might include:

- Policies and procedures to monitor and implement quality control of assurance engagements; and
- Involving an additional professional accountant who was not a member of the assurance team to review the work done or otherwise advise as necessary.

Fees - Overdue

8.205 A self-interest threat may be created if fees due from an assurance client for professional services remain unpaid for a long time, especially if a significant part is not paid before the issue of the assurance report for the following year. Generally the payment of such fees should be required before the report is issued. The following safeguards may be applicable:

- Discussing the level of outstanding fees with the audit committee, or others charged with governance; and
- Involving an additional professional accountant who did not take part in the assurance engagement to provide advice or review the work performed.

The firm should also consider whether the overdue fees might be regarded as being equivalent to a loan to the client and whether, because of the significance of the overdue fees, it is appropriate for the firm to be re-appointed.

Pricing

8.206 When a firm obtains an assurance engagement at a significantly lower fee level than that charged by the predecessor firm, or quoted by other firms, the self-interest threat created will not be reduced to an acceptable level unless:

- The firm is able to demonstrate that appropriate time and qualified staff are assigned to the task; and
- All applicable assurance standards, guidelines and quality control procedures are being complied with.

Contingent Fees

8.207 Contingent fees are fees calculated on a predetermined basis relating to the outcome or result of a transaction or the result of the work performed. For the purposes of this section, fees are not regarded as being contingent if a court or other public authority has established them.

8.208 A contingent fee charged by a firm in respect of an assurance engagement creates self-interest and advocacy threats that cannot be reduced to an acceptable level by the application of any safeguard. Accordingly, a firm should not enter into any fee arrangement for an assurance engagement under which the amount of the fee is contingent on the result of the assurance work or on items that are the subject matter of the assurance engagement.

8.209 A contingent fee charged by a firm in respect of a non-assurance service provided to an assurance client may also create self-interest and advocacy threats. If the amount of the fee for a non-assurance engagement was agreed to, or contemplated, during an assurance engagement and was contingent on the result of that assurance engagement, the threats could not be reduced to an acceptable level by the application of any safeguard. Accordingly, the only acceptable action is not to accept such arrangements. For other types of contingent fee arrangements, the significance of the threats created will depend on factors such as:

- The range of possible fee amounts;
- The degree of variability;
- The basis on which the fee is to be determined;
- Whether the outcome or result of the transaction is to be reviewed by an independent third party; and

- The effect of the event or transaction on the assurance engagement.

The significance of the threats should be evaluated and, if the threats are other than clearly insignificant, safeguards should be considered and applied as necessary to reduce the threats to an acceptable level. Such safeguards might include:

- Disclosing to the audit committee, or others charged with governance, the extent of nature and extent of fees charged;
- Review or determination of the final fee by an unrelated third party; or
- Quality and control policies and procedures.

l. Gifts and Hospitality

- 8.210 Accepting gifts or hospitality from an assurance client may create self-interest and familiarity threats. When a firm or a member of the assurance team accepts gifts or hospitality, unless the value is clearly insignificant, the threats to independence cannot be reduced to an acceptable level by the application of any safeguard. Consequently, a firm or a member of the assurance team should not accept such gifts or hospitality.

m. Actual or Threatened Litigation

- 8.211 When litigation takes place, or appears likely, between the firm or a member of the assurance team and the assurance client, a self-interest or intimidation threat may be created. The relationship between client management and the members of the assurance team must be characterized by complete candor and full disclosure regarding all aspects of a client's business operations. The firm and the client's management may be placed in adversarial positions by litigation, affecting management's willingness to make complete disclosures and the firm may face a self-interest threat. The significance of the threat created will depend upon such factors as:

- The materiality of the litigation;
- The nature of the assurance engagement; and
- Whether the litigation relates to a prior assurance engagement.

Once the significance of the threat has been evaluated the following safeguards should be applied, if necessary, to reduce the threats to an acceptable level:

- Disclosing to the audit committee, or others charged with governance, the extent and nature of the litigation;
- If the litigation involves a member of the assurance team, removing that individual from the assurance team; or
- Involving an additional professional accountant in the firm who was not a member of the assurance team to review the work done or otherwise advise as necessary.

If such safeguards do not reduce the threat to an appropriate level, the only appropriate action is to withdraw from, or refuse to accept, the assurance engagement.

SECTION 9

Professional Competence and Responsibilities Regarding the Use of Non-Accountants

- 9.1 Professional accountants in public practice should refrain from agreeing to perform professional services which they are not competent to carry out unless competent advice and assistance is obtained so as to enable them to satisfactorily perform such services. If a professional accountant does not have the competence to perform a specific part of the professional service, technical advice may be sought from experts such as other professional accountants, lawyers, actuaries, engineers, geologists, valuers.
- 9.2 In such situations, although the professional accountant is relying on the technical competence of the expert, the knowledge of the ethical requirements cannot be automatically assumed. Since the ultimate responsibility for the professional service rests with the professional accountant, the professional accountant should see that the requirements of ethical behavior are followed.
- 9.3 When using the services of experts who are not professional accountants, the professional accountant must take steps to see that such experts are aware of ethical requirements. Primary attention should be paid to the Fundamental Principles in paragraph 12 of the Code of Ethics. These principles would extend to any assignment in which such experts would participate.
- 9.4 The degree of supervision and the amount of guidance that will be needed will depend upon the individuals involved and the nature of the engagement. Examples of such guidance and supervision might include:
- Asking individuals to read the appropriate ethical codes;
 - Requiring written confirmation of understanding of the ethical requirements; and
 - Providing consultation when potential conflicts arise.
- 9.5 The professional accountant should also be alert to specific independence requirements or other risks unique to the engagement. Such situations will require special attention and guidance/supervision to see that ethical requirements are met. For example, Section 8 of the Code of Ethics requires all professionals participating in the assurance engagement to be independent of the assurance client.
- 9.6 If at any time the professional accountant is not satisfied that proper ethical behavior can be respected or assured, the engagement should not be accepted; or, if the engagement has commenced, it should be terminated.

SECTION 10

Fees and Commissions

- 10.1 Professional accountants in public practice who undertake professional services for a client, assume the responsibility to perform such services with integrity and objectivity and in accordance with the appropriate technical standards. That responsibility is discharged by applying the professional skill and knowledge which professional accountants in public practice have acquired through training and experience. For the services rendered, the professional accountant in public practice is entitled to remuneration.

Professional Fees

- 10.2 Professional fees should be a fair reflection of the value of the professional services performed for the client, taking into account:
- (a) The skill and knowledge required for the type of professional services involved;
 - (b) The level of training and experience of the persons necessarily engaged in performing the professional services;
 - (c) The time necessarily occupied by each person engaged in performing the professional services; and
 - (d) The degree of responsibility that performing those services entails.
- 10.3 Professional fees should normally be computed on the basis of appropriate rates per hour or per day for the time of each person engaged in performing professional services. These rates should be based on the fundamental premise that the organization and conduct of the professional accountant in public practice and the services provided to clients are well planned, controlled and managed. They should take into account the factors set out in paragraph 10.2 and are influenced by the local legal, social and economic conditions. It is for each professional accountant in public practice to determine the appropriate rates.
- 10.4 A professional accountant in public practice should not make a representation that specific professional services in current or future periods will be performed for either a stated fee, estimated fee, or fee range if it is likely at the time of the representation that such fees will be substantially increased and the prospective client is not advised of that likelihood.
- 10.5 When performing professional services for a client it may be necessary or expedient to charge a pre-arranged fee, in which event the professional accountant in public practice should estimate a fee taking into account the matters referred to in paragraphs 10.2 through 10.4.
- 10.6 It is not improper for a professional accountant in public practice to charge a client a lower fee than has previously been charged for similar services, provided the fee has been calculated in accordance with the factors referred to in paragraphs 10.2 through 10.4.

Commentary

The fact that a professional accountant in public practice secures work by quoting a fee lower than another is not improper. However, professional accountants in public practice who obtain work at fees significantly lower than those charged by an existing accountant, or quoted by others, should be aware that there is a risk of a perception that the quality of work could be impaired.

Accordingly, when deciding on a fee to be quoted to a client for the performance of professional services, a professional accountant should be satisfied that, as a result of the fee quoted:

- The quality of work will not be impaired and that due care will be applied to comply with all professional standards and quality control procedures in the performance of those services; and
- The client will not be misled as to the precise scope of services that a quoted fee is intended to cover and the basis on which future fees will be charged.

10.7 As stated in paragraph 8.208:

An assurance engagement should not be performed for a fee that is contingent on the result of the assurance work or on items that are the subject matter of the assurance engagement. Paragraph 8.209 provides guidance on threats that may be created if a non-assurance engagement is provided to an assurance client for a contingent fee, and the safeguards that may reduce the threats to an acceptable level.

Commentary

Fees should not be regarded as being contingent if fixed by a court or other public authority. Fees charged on a percentage or similar basis, except when authorized by statute as generally accepted practice for certain professional services, should be regarded as contingent fees.

10.8 The foregoing paragraphs relate to fees as distinct from reimbursement of expenses. Out-of-pocket expenses, in particular travelling expenses, attributable directly to the professional services performed for a particular client would normally be charged to that client in addition to the professional fees.

10.9 It is in the best interests of both the client and the professional accountant in public practice that the basis on which fees are computed and any billing arrangements are clearly defined, preferably in writing, before the commencement of the engagement to help in avoiding misunderstandings with respect to fees. (For further guidance, refer to SAS 140 “Engagement letters” or International Standard on Auditing 210 “Terms of Audit Engagements”.)

Commissions

10.10 A professional accountant in public practice should not give any commission, fee or reward to a third party, unless the third party is either his or her employee or another professional accountant, in return for the introduction of a client.

10.11 Where a professional accountant in public practice becomes aware that any commission, fee or reward, may be earned by the practice or anyone in it or by a network firm for the introduction of a client, or as a result of advice given to a client, the client should be informed in writing:

- (a) that commission is likely to result and, when the fact is known, that such commission, fee or reward will be received; and
- (b) as soon as practicable, of its amount and terms.

10.12 A professional accountant in public practice may enter into an arrangement for the purchase of the whole or part of an accounting practice requiring payments to individuals formerly engaged in the practice or payments to their heirs or estates. Such payments are not regarded as commissions for the purpose of paragraph 10.10.

SECTION 11

Activities Incompatible with the Practice of Public Accountancy

- 11.1 A professional accountant in public practice should not concurrently engage in any business, occupation or activity which impairs or might impair integrity, objectivity or independence, or the good reputation of the profession and therefore would be incompatible with the rendering of professional services.
- 11.2 The rendering of two or more types of professional services concurrently does not by itself impair integrity, objectivity or independence.
- 11.3 The simultaneous engagement in another business, occupation or activity unrelated to professional services which has the effect of not allowing the professional accountant in public practice properly to conduct a professional practice in accordance with the fundamental ethical principles of the accountancy profession should be regarded as inconsistent with the practice of public accountancy.

SECTION 12

Clients' Monies

- 12.1 A professional accountant in public practice should not hold clients' monies if there is reason to believe that they were obtained from, or are to be used for, illegal activities.
- 12.2 A professional accountant in public practice entrusted with monies belonging to others should:
- (a) Keep such monies separately from personal or firm monies;
 - (b) Use such monies only for the purpose for which they are intended; and
 - (c) At all times, be ready to account for those monies to any persons entitled to such accounting.
- 12.3 A professional accountant in public practice should maintain one or more bank accounts for clients' monies. Such bank accounts may include a general client account into which the monies of a number of clients may be paid.
- 12.4 Clients' monies received by a professional accountant in public practice should be deposited without delay to the credit of a client account, or — if in the form of documents of title to money and documents of title which can be converted into money — be safeguarded against unauthorized use.
- 12.5 Monies may only be drawn from the client account on the instructions of the client.
- 12.6 Fees due from a client may be drawn from client's monies provided the client, after being notified of the amount of such fees, has agreed to such withdrawal.
- 12.7 Payments from a client account shall not exceed the balance standing to the credit of the client.
- 12.8 When it seems likely that the client's monies remain on client account for a significant period of time, the professional accountant in public practice should, with the concurrence of the client, place such monies in an interest bearing account within a reasonable time.
- 12.9 All interest earned on clients' monies should be credited to the client account.
- 12.10 Professional accountants in public practice should keep such books of account as will enable them, at any time, to establish clearly their dealings with clients' monies in general and the monies of each individual client in particular. A statement of account should be provided to the client at least once a year.

SECTION 13

Relations with Other Professional Accountants in Public Practice

Accepting New Assignments

- 13.1 The extension of the operations of a business undertaking frequently results in the formation of branches or subsidiary companies at locations where an existing accountant does not practise. In these circumstances, the client or the existing accountant in consultation with the client may request a receiving accountant practising at those locations to perform such professional services as necessary to complete the assignment.
- 13.2 Referral of business may also arise in the area of special services or special tasks. The scope of the services offered by professional accountants in public practice continues to expand and the depth of knowledge which is needed to serve the public often calls for special skills. Since it is impracticable for any one professional accountant in public practice to acquire special expertise or experience in all fields of accountancy, some professional accountants in public practice have decided that it is neither appropriate nor desirable to develop within their firms the complete range of special skills which may be required.
- 13.3 Professional accountants in public practice should only undertake such services which they can expect to complete with professional competence. It is essential therefore for the profession in general and in the interests of their clients that professional accountants in public practice be encouraged to obtain advice when appropriate from those who are competent to provide it.
- 13.4 An existing accountant without a particular skill may however be reluctant to refer a client to another professional accountant in public practice who may possess that skill, because of the fear of losing existing business to the other professional accountant in public practice. As a result, clients may be deprived of the benefit of advice which they are entitled to receive.
- 13.5 The wishes of the client should be paramount in the choice of professional advisers, whether or not special skills are involved. Accordingly, a professional accountant in public practice should not attempt to restrict in any way the client's freedom of choice in obtaining special advice, and when appropriate should encourage a client to do so.
- 13.6 The services or advice of a professional accountant in public practice having special skills may be sought in one or other of the following ways:
- (a) By the client;
 - (i) After prior discussion and consultation with the existing accountant;
 - (ii) On the specific request or recommendation of the existing accountant; and
 - (iii) Without reference to the existing accountant; or
 - (b) By the existing accountant with due observance of the duty of confidentiality.
- 13.7 When a professional accountant in public practice is asked to provide services or advice, inquiries should be made as to whether the prospective client has an existing accountant. In cases where there is an existing accountant who will continue to provide professional services, the procedures set out in paragraphs 13.8–13.14 should be observed. If the appointment will result in another professional accountant in public practice being superseded, the procedures set out in paragraphs 13.15–13.26 should be followed.

- 13.8 The receiving accountant should limit the services provided to the specific assignment received by referral from the existing accountant or the client unless otherwise requested by the client. The receiving accountant also has the duty to take reasonable steps to support the existing accountant's current relationship with the client and should not express any criticism of the professional services of the existing accountant without giving the latter an opportunity to provide all relevant information.
- 13.9 A receiving accountant who is asked by the client to undertake an assignment of a type which is clearly distinct from that being carried out by the existing accountant or from that initially received by referral from the existing accountant or from the client, should regard this as a separate request to provide services or advice. Before accepting any appointments of this nature, the receiving accountant should advise the client of the professional obligation to communicate with the existing accountant and should immediately do so preferably in writing, advising of the approach made by the client and the general nature of the request as well as seeking all relevant information, if any, necessary to perform the assignment.
- 13.10 Circumstances sometimes arise when the client insists that the existing accountant should not be informed. In this case, the receiving accountant should decide whether the client's reasons are valid. In the absence of special circumstances a mere disinclination by the client for communication with the existing accountant would not be a satisfactory reason.
- 13.11 The receiving accountant should:
- (a) Comply with the instructions received from the existing accountant or the client to the extent that they do not conflict with relevant legal or other requirements; and
 - (b) Ensure, insofar as it is practicable to do so, that the existing accountant is kept informed of the general nature of the professional services being performed.
- 13.12 When there are two or more other professional accountants in public practice performing professional services for the client concerned it may be appropriate to notify only the relevant professional accountant in public practice depending on the specific services being performed.
- 13.13 When appropriate the existing accountant, in addition to issuing instructions concerning referred business, should maintain contact with the receiving accountants and cooperate with them in all reasonable requests for assistance.
- 13.14 When the opinion of a professional accountant, other than the existing accountant, is sought on the application of accounting, auditing, reporting or other standards or principles to specific circumstances or transactions, the professional accountant should be alert to the possibility of the opinion creating undue pressure on the judgment and objectivity of the accountant. An opinion given without full and proper facts can cause difficulty to the receiving accountant if the opinion is challenged or the receiving accountant is subsequently appointed by the company. Accordingly, the professional accountant should seek to minimize the risk of giving inappropriate guidance by ensuring that he or she has access to all relevant information. When there is a request for an opinion in the above circumstances there is a requirement for communication with the existing accountant. It is important that the existing accountant, with the permission of the client, provides the receiving accountant with all requested relevant information about the client. With the permission of the client, the receiving accountant should also provide a copy of the final report to the existing accountant. If the client does not agree to these communications, then the engagement should ordinarily not be performed.

Superseding Another Professional Accountant in Public Practice

- 13.15 The proprietors of a business have an indisputable right to choose their professional advisers and to change to others should they so desire. While it is essential that the legitimate interests of the proprietors are protected, it is also important that a professional accountant in public practice who is asked to replace another professional accountant in public practice has the opportunity to ascertain if there are any professional reasons why the appointment should not be accepted. This cannot effectively be done without direct communication with the existing accountant. In the absence of a specific request, the existing accountant should not volunteer information about the client's affairs.
- 13.16 Communication enables a professional accountant in public practice to ascertain whether the circumstances in which a change in appointment is proposed are such that the appointment can properly be accepted and also whether there is a wish to undertake the engagement. In addition, such communication helps to preserve the harmonious relationships which should exist between all professional accountants in public practice on whom clients rely for professional advice and assistance.
- 13.17 The extent to which an existing accountant can discuss the affairs of the client with the proposed professional accountant in public practice depend on:
- (a) Whether the client's permission to do so has been obtained; and/or
 - (b) The legal or ethical requirements relating to such disclosure.
- 13.18 The proposed professional accountant in public practice should treat in the strictest confidence and give due weight to any information provided by the existing accountant.
- 13.19 The information provided by the existing accountant may indicate, for example, that the ostensible reasons given by the client for the change are not in accordance with the facts. It may disclose that the proposal to make a change in professional accountants in public practice was made because the existing accountants stood their ground and properly carried out the duties as professional accountants in public practice despite opposition or evasion on an occasion on which important differences of principles or practice have arisen with the client.
- 13.20 Communication between the parties therefore serves:
- (a) To protect a professional accountant in public practice from accepting an appointment in circumstances where all the pertinent facts are not known.
 - (b) To protect the minority proprietors of a business who may not be fully informed of the circumstances in which the change is proposed.
 - (c) To protect the interests of the existing accountant when the proposed change arises from, or is an attempt to interfere with, the conscientious exercise of the existing accountant's duty to act as an independent professional.
- 13.21 Before accepting an appointment involving recurring professional services hitherto carried out by another professional accountant in public practice, the proposed professional accountant in public practice should:
- (a) Ascertain if the prospective client has advised the existing accountant of the proposed change and has given permission, preferably in writing, to discuss the client's affairs fully and freely with the proposed professional accountant in public practice.
 - (b) When satisfied with the reply received from prospective client, request permission to communicate with the existing accountant. If such permission is refused or the permission referred to in (a) above is not given, the proposed professional accountant in public practice should, in the absence of exceptional circumstances of which there is full

knowledge, and unless there is satisfaction as to necessary facts by other means, decline the appointment.

- (c) On receipt of permission, ask the existing accountant, preferably in writing:
 - (i) To provide information on any professional reasons which should be known before deciding whether or not to accept the appointment and, if there are such matters; and
 - (ii) To provide all the necessary details to be able to come to a decision.
- 13.22 The existing accountant, on receipt of the communication referred to in paragraph 13.21 (c) should forthwith:
- (a) Reply, preferably in writing, advising whether there are any professional reasons why the proposed professional accountant in public practice should not accept the appointment.
 - (b) If there are any such reasons or other matters which should be disclosed, ensure that the client has given permission to give details of this information to the proposed professional accountant in public practice. If permission is not granted, the existing accountant should report that fact to the proposed professional accountant in public practice.
 - (c) On receipt of permission from the client, disclose all information needed by the proposed professional accountant in public practice to be able to decide whether or not to accept the appointment, and discuss freely with the proposed professional accountant in public practice all matters relevant to the appointment of which the latter should be aware.
- 13.23 If the proposed professional accountant in public practice does not receive, within a reasonable time, a reply from the existing accountant and there is no reason to believe that there are any exceptional circumstances surrounding the proposed change, the proposed professional accountant in public practice should endeavor to communicate with the existing accountant by some other means. If unable to obtain a satisfactory outcome in this way, the proposed professional accountant in public practice should send a further letter, stating that there is an assumption that there is no professional reason why the appointment should not be accepted and that there is an intention to do so.
- 13.24 The fact that there may be fees owing to the existing accountant is not a professional reason why another professional accountant in public practice should not accept the appointment.
- 13.25 The existing accountant should promptly transfer to the new professional accountant in public practice all books and papers of the client which are or may be held after the change in appointment has been effected and should advise the client accordingly, unless the professional accountant in public practice has a legal right to withhold them.
- 13.26 Certain organizations, either because of legislative requirements or otherwise, call for submissions or tenders, e.g., competitive bids, in relation to professional services offered by accountants in public practice. In reply to a public advertisement or an unsolicited request to make a submission or submit a tender, a professional accountant in public practice should, if the appointment may result in the replacement of another professional accountant in public practice, state in the submission or tender that before acceptance the opportunity to contact the other professional accountant in public practice is required so that inquiries may be made as to whether there are any professional reasons why the appointment should not be accepted. If the submission or tender is successful, the existing accountant should then be contacted.

SECTION 14

Advertising and Solicitation

- 14.1 Advertising and solicitation by professional accountants in public practice are permitted subject to the requirements set out in paragraphs 14.2 to 14.7 below.
- 14.2 Such advertising and solicitation should be aimed at informing the public in an objective manner and should be decent, honest, truthful and in good taste. Solicitation by the use of coercion or harassment is prohibited.
- 14.3 If reference is made in promotional material to fees, the basis on which fees are calculated, or to hourly or other charging rates, the greatest care should be taken to ensure that such reference does not mislead as to the precise range of services and time commitment that the reference is intended to cover. A professional accountant in public practice should not make comparisons in such material between their fees and the fees of others, whether professional accountants in public practice or not.
- 14.4 The danger of giving a misleading impression is particularly pronounced when constraints of space limit the amount of information which can be given. For this reason it will seldom be appropriate to include information about fees in short advertisements.
- 14.5 A professional accountant in public practice may offer a free consultation at which levels of fees will be discussed.
- 14.6 Examples of activities which may be considered not to meet the criteria in paragraph 14.2 include those that:
- (a) Create false, deceptive or unjustified expectations of favorable results;
 - (b) Imply the ability to influence any court, tribunal, regulatory agency or similar body or official;
 - (c) Consist of self-laudatory statements that are not based on verifiable facts;
 - (d) Make comparisons with other professional accountants in public practice;
 - (e) Contain testimonials or endorsements;
 - (f) Contain any other representations that would be likely to cause a reasonable person to misunderstand or be deceived;
 - (g) Make unjustified claims to be an expert or specialist in a particular field of accountancy; and
 - (h) Include in promotional material references to fees, in respect of audit and assurance engagements requiring the expression of an opinion, that they are at certain amount and above.
- 14.7 A professional accountant in public practice should not seek to obtain an advantage by advertising in newspapers or magazines published or distributed outside Hong Kong where advertising is prohibited.

PART C — APPLICABLE TO EMPLOYED PROFESSIONAL ACCOUNTANTS

The following sections contain guidance which is particularly relevant to professional accountants working in industry, commerce, the public sector or education. Professional accountants employed in public practice should be aware they may find that the principles set out below are also of application to their particular circumstances. If professional accountants employed in public practice are in doubt as to the applicability of any particular guidance, they should seek assistance from the HKSA.

SECTION 15

Conflict of Loyalties

- 15.1 Employed professional accountants owe a duty of loyalty to their employer as well as to their profession and there may be times when the two are in conflict. An employee's normal priority should be to support his or her organization's legitimate and ethical objectives and the rules and procedures drawn up in support of them. However, an employee cannot legitimately be required to:
- (a) Break the law;
 - (b) Breach the rules and standards of their profession;
 - (c) Lie to or mislead (including misleading by keeping silent) those acting as auditors to the employer; or
 - (d) Put their name to or otherwise be associated with a statement which materially misrepresents the facts.
- 15.2 Differences in view about the correct judgment on accounting or ethical matters should normally be raised and resolved within the employee's organization, initially with the employee's immediate superior and possibly thereafter, where disagreement about a significant ethical issue remains, with higher levels of management or non executive directors.
- 15.3 If employed accountants cannot resolve any material issue involving a conflict between their employers and their professional requirements they may, after exhausting all other relevant possibilities, have no other recourse but to consider resignation. Employees should state their reasons for doing so to the employer but their duty of confidentiality normally precludes them from communicating the issue to others (unless legally or professionally required to do so).
- 15.4 For further guidance as to the considerations involved see Section 2—Resolution of Ethical Conflicts.

SECTION 16

Support for Professional Colleagues

- 16.1 A professional accountant, particularly one having authority over others, should give due weight for the need for them to develop and hold their own judgment in accounting matters and should deal with differences of opinion in a professional way.

SECTION 17

Professional Competence

- 17.1 A professional accountant employed in industry, commerce, the public sector or education may be asked to undertake significant tasks for which he or she has not had sufficient specific training or experience. When undertaking such work the professional accountant should not mislead the employer as to the degree of expertise or experience he or she possesses, and where appropriate expert advice and assistance should be sought.

SECTION 18

Presentation of Information

- 18.1 A professional accountant is expected to present financial information fully, honestly and professionally and so that it will be understood in its context.
- 18.2 Financial and non-financial information should be maintained in a manner that describes clearly the true nature of business transactions, assets or liabilities and classifies and records entries in a timely and proper manner, and professional accountants should do everything that is within their powers to ensure that this is the case.