

# MEMBERS' HANDBOOK

## Update No. 192

(Issued 16 December 2016)

| <u>Document Reference and Title</u>                                   | <u>Instructions</u>  | <u>Explanations</u>    |
|---|--|------------------------|
| <b><u>VOLUME I</u></b>  |  |                        |
| <a href="#">Contents of Volume I</a>                                  | Discard existing page i & replace with revised page i.   | Revised contents pages |
| <b>PROFESSIONAL ETHICS</b>  |  |                        |
| <a href="#">Code of Ethics for Professional Accountants (Revised)</a> | Replace the cover page, pages 2, 4, 37, 47, 59-78, 81-84, 92-98 and 202-206 with revised cover page, pages 2, 4, 37, 47, 59-78, 81-84, 92-98 and 202-206. Insert pages 207-234 after page 206. | - Notes                |

### Notes:

1. In September 2016, the Institute's Ethics Committee approved the issuance of *Responding to Non-Compliance with Laws and Regulations* (NOCLAR) for application in Hong Kong, following the International Ethics Standards Board for Accountants' equivalent standard.
2. NOCLAR is effective on 15 July 2017 and applies to all categories of professional accountants, including auditors, other professional accountants in public practice and professional accountants in business. Early adoption is permitted.
3. NOCLAR sets out the response framework to guide professional accountants in deciding how best to act in the public interest when they become aware of non-compliance or suspected non-compliance with laws and regulations during the course of their work. In particular:
  - it provides a clear pathway for professional accountants to disclose potential non-compliance situations to appropriate public authorities in certain situations without being constrained by the ethical duty of confidentiality;
  - it places renewed emphasis on the role of senior-level accountants in business in promoting a culture of compliance with laws and regulations and prevention of non-compliance within their organizations;
  - it addresses breaches of laws and regulations that deal with matters such as fraud, corruption and bribery, money laundering, tax payments, financial products and services, environmental protection, and public health and safety.

4. As a result of NOCLAR, consequential amendments are made to Part A, Part B and Part D of the Code of Ethics for Professional Accountants (the Code).
5. NOCLAR and its consequential amendments to other parts of the Code are set out in Appendix 3 of the Code and will be incorporated into the main body of the Code after being effective.
6. The main body of the Code has also been updated to incorporate amendments that were effective on 15 April 2016 that address certain non-assurance services provided to audit and assurance clients. Those amendments were previously set out in Appendix 3 of the Code.



## MEMBERS' HANDBOOK CONTENTS OF VOLUME I

(Updated to December 2016)

|                            |   | <i>Issue/Review<br/>date</i> |
|----------------------------|---|------------------------------|
| <b>1.1</b>                 | <b>PROFESSIONAL ACCOUNTANTS ORDINANCE, BY-LAWS, RULES,<br/>GUIDELINES</b>   |                              |
| CAP.50                     | <a href="#">Professional Accountants Ordinance</a> .....  | 3/14                         |
| CAP.50A                    | <a href="#">Professional Accountants By-laws</a> .....  | 3/14                         |
| 1.101                      | <a href="#">Disciplinary Committee Proceedings Rules</a> .....  | 10/06                        |
| 1.101A                     | <a href="#">Guidelines for the Chairman and the Committee on Administering the<br/>Disciplinary Committee Proceedings Rules</a> .....                               | 11/15                        |
| 1.102<br>(Oct 2016)        | <a href="#">Corporate Practices (Registration) Rules</a> .....  | 10/16                        |
| 1.102 (sch.)<br>(Mar 2014) | <a href="#">Schedule to the Corporate Practices (Registration) Rules</a><br><a href="#">"Corporate Practices (Model Articles of Association)"</a> .....             | 3/14                         |
| 1.103                      | <a href="#">Corporate Practices (Professional Indemnity) Rules</a> .....  | 10/16                        |
| <b>1.2</b>                 | <b>PROFESSIONAL ETHICS</b>  |                              |
| COE<br>(Revised)           | <a href="#">Code of Ethics for Professional Accountants</a> .....   | 12/16                        |
| <b>1.3</b>                 | <b>GENERAL GUIDANCE</b>   |                              |
| 1.300                      | <a href="#">Explanatory Foreword</a> .....  | 9/04                         |
| 1.301                      | <a href="#">Books and Papers - Ownership, Disclosure and Lien</a> .....   | 9/04                         |
| 1.302                      | <a href="#">Formation of Companies by Accountants</a> .....   | 4/85                         |
| 1.303                      | <a href="#">Restrictions on Appointments as Secretaries and Directors of Audit Clients</a> ...  | 5/15                         |
| 1.304                      | <a href="#">Arrangements to Cover the Incapacity or Death of a Sole Practitioner</a> .....  | 9/04                         |
| 1.305                      | <a href="#">Direct Professional Access</a> .....  | 9/04                         |
| 1.306                      | <a href="#">Guidance on Reasonable Steps to be Taken for PII Purposes</a> .....   | 8/96                         |
| 1.307                      | <a href="#">Production of Audit Working Papers to the Securities and Futures<br/>Commission<br/>under section 179 of the Securities and Futures Ordinance</a> ..... | 9/04                         |
| <b>1.4</b>                 | <b>PRACTICE REVIEW</b>  |                              |
| 1.400                      | <a href="#">Explanatory Foreword</a> .....  | 3/06                         |
| 1.401                      | <a href="#">Review Procedures and Conduct of Members</a> .....  | 3/06                         |

COE  
Revised July 2015 December 2016

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Effective on 1 January 2011  
(including subsequent amendments as indicated)

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# Code of Ethics for Professional Accountants



Hong Kong Institute of  
**Certified Public Accountants**  
香港會計師公會

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|  |         |
|--|---------|
| <b>DEFINITIONS</b> .....   | 186-191 |
| <b>EFFECTIVE DATE</b> .....  | 192-193 |
| APPENDIX 1: Sample Code of Conduct under the Prevention of Bribery Ordinance .....     | 194-200 |
| APPENDIX 2: Comparison with the IESBA Code of Ethics for Professional Accountants..... | 201     |
| APPENDIX 3: Amendments to the Code of Ethics for Professional Accountants .....        | 202-234 |

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**SECTION 290**  
**INDEPENDENCE—AUDIT AND REVIEW ENGAGEMENTS**  
**CONTENTS**

|   | Paragraph |
|---|-----------|
| Structure of Section .....  | 290.1     |
| A Conceptual Framework Approach to Independence .....   | 290.4     |
| Networks and Network Firms .....  | 290.13    |
| Public Interest Entities .....  | 290.25    |
| Related Entities .....  | 290.27    |
| Those Charged with Governance .....   | 290.28    |
| Documentation .....   | 290.29    |
| Engagement Period .....   | 290.30    |
| Mergers and Acquisitions .....  | 290.33    |
| Breach of a Provision of this Section .....   | 290.39    |
| Application of the Conceptual Framework Approach to Independence .....                          | 290.100   |
| Financial Interests .....   | 290.102   |
| Loans and Guarantees .....  | 290.117   |
| Business Relationships .....  | 290.123   |
| Family and Personal Relationships .....   | 290.126   |
| Employment with an Audit Client .....   | 290.132   |
| Temporary Staff Assignments .....   | 290.140   |
| Recent Service with an Audit Client .....   | 290.141   |
| Serving as a Director or Officer of an Audit Client .....                                       | 290.144   |
| Long Association of Senior Personnel (Including Partner Rotation)<br>with an Audit Client ..... | 290.148   |
| Provision of Non-assurance Services to Audit Clients .....                                      | 290.154   |
| Management Responsibilities .....   | 290.159   |
| Administrative Services .....   | 290.163   |
| Preparing Accounting Records and Financial Statements .....                                     | 290.164   |
| Valuation Services .....  | 290.171   |
| Taxation Services .....   | 290.177   |
| Internal Audit Services .....   | 290.190   |
| IT Systems Services .....   | 290.196   |
| Litigation Support Services .....   | 290.202   |
| Legal Services .....  | 290.204   |
| Recruiting Services .....   | 290.209   |
| Corporate Finance Services .....  | 290.211   |
| Fees .....  | 290.215   |
| Fees—Relative Size .....  | 290.215   |
| Fees—Overdue .....  | 290.218   |
| Contingent Fees .....   | 290.219   |
| Compensation and Evaluation Policies .....  | 290.223   |
| Gifts and Hospitality .....   | 290.225   |
| Actual or Threatened Litigation .....   | 290.226   |
| Reports that Include a Restriction on Use and Distribution .....                                | 290.500   |

## Application of the Conceptual Framework Approach to Independence

- 290.100 Paragraphs 290.102 to 290.226 describe specific circumstances and relationships that create or may create threats to independence. The paragraphs describe the potential threats and the types of safeguards that may be appropriate to eliminate the threats or reduce them to an acceptable level and identify certain situations where no safeguards could reduce the threats to an acceptable level. The paragraphs do not describe all of the circumstances and relationships that create or may create a threat to independence. The firm and the members of the audit team shall evaluate the implications of similar, but different, circumstances and relationships and determine whether safeguards, including the safeguards in paragraphs 200.12 to 200.15, can be applied when necessary to eliminate the threats to independence or reduce them to an acceptable level.
- 290.101 Paragraphs 290.102 to 290.125 contain references to the materiality of a financial interest, loan, or guarantee, or the significance of a business relationship. For the purpose of determining whether such an interest is material to an individual, the combined net worth of the individual and the individual's immediate family members may be taken into account.

### Financial Interests

- 290.102 Holding a financial interest in an audit client may create a self-interest threat. The existence and significance of any threat created depends on: (a) the role of the person holding the financial interest, (b) whether the financial interest is direct or indirect, and (c) the materiality of the financial interest.
- 290.103 Financial interests may be held through an intermediary (e.g. a collective investment vehicle, estate or trust). The determination of whether such financial interests are direct or indirect will depend upon whether the beneficial owner has control over the investment vehicle or the ability to influence its investment decisions. When control over the investment vehicle or the ability to influence investment decisions exists, this Code defines that financial interest to be a direct financial interest. Conversely, when the beneficial owner of the financial interest has no control over the investment vehicle or ability to influence its investment decisions, this Code defines that financial interest to be an indirect financial interest.
- 290.104 If a member of the audit team, a member of that individual's immediate family, or a firm has a direct financial interest or a material indirect financial interest in the audit client, the self-interest threat created would be so significant that no safeguards could reduce the threat to an acceptable level. Therefore, none of the following shall have a direct financial interest or a material indirect financial interest in the client: a member of the audit team; a member of that individual's immediate family; or the firm.
- 290.105 When a member of the audit team has a close family member who the audit team member knows has a direct financial interest or a material indirect financial interest in the audit client, a self-interest threat is created. The significance of the threat will depend on factors such as:
- The nature of the relationship between the member of the audit team and the close family member; and
  - The materiality of the financial interest to the close family member.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- The close family member disposing, as soon as practicable, of all of the financial interest or disposing of a sufficient portion of an indirect financial interest so that the remaining interest is no longer material;
- Having a professional accountant review the work of the member of the audit team; or
- Removing the individual from the audit team.



- 290.158 A non-assurance service provided to an audit client does not compromise the firm's independence when the client becomes a public interest entity if:
- (a) The previous non-assurance service complies with the provisions of this section that relate to audit clients that are not public interest entities;
  - (b) Services that are not permitted under this section for audit clients that are public interest entities are terminated before or as soon as practicable after the client becomes a public interest entity; and
  - (c) The firm applies safeguards when necessary to eliminate or reduce to an acceptable level any threats to independence arising from the service.

*Management Responsibilities*

290.159 Management responsibilities involve controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, technological, physical and intangible resources.

290.160 Determining whether an activity is a management responsibility depends on the circumstances and requires the exercise of judgment. Examples of activities that would be considered a management responsibility include:

- Setting policies and strategic direction.
- Hiring or dismissing employees.
- Directing and taking responsibility for the actions of employees in relation to the employees' work for the entity.
- Authorizing transactions.
- Controlling or managing of bank accounts or investments.
- Deciding which recommendations of the firm or other third parties to implement.
- Reporting to those charged with governance on behalf of management.
- Taking responsibility for the preparation and fair presentation of financial statements in accordance with the applicable financial reporting framework.
- Taking responsibility for designing, implementing, monitoring or maintaining internal controls.

290.161 A firm shall not assume a management responsibility for an audit client. The threats created would be so significant that no safeguards could reduce the threats to an acceptable level. For example, deciding which recommendations of the firm to implement will create self-review and self-interest threats. Further, assuming a management responsibility creates a familiarity threat because the firm becomes too closely aligned with the views and interests of management. Subject to compliance with paragraph 290.162, providing advice and recommendations to assist management in discharging its responsibilities is not assuming a management responsibility.

290.162 To avoid the risk of assuming a management responsibility when providing non-assurance services to an audit client, the firm shall be satisfied that client management makes all judgments and decisions that are the responsibility of management. This includes ensuring that the client's management:

- Designates an individual who possesses suitable skill, knowledge and experience to be responsible at all times for the client's decisions and to oversee the services. Such an individual, preferably within senior management, would understand the objectives, nature and results of the services and the respective client and firm responsibilities.

However, the individual is not required to possess the expertise to perform or re-perform the services;

- Provides oversight of the services and evaluates the adequacy of the results of the services performed for the client's purpose; and
- Accepts responsibility for the actions, if any, to be taken arising from the results of the services.

### *Administrative Services*

290.163 Administrative services involve assisting clients with their routine or mechanical tasks within the normal course of operations. Such services require little to no professional judgment and are clerical in nature. Examples of administrative services include word processing services, preparing administrative or statutory forms for client approval, submitting such forms as instructed by the client, monitoring statutory filing dates, and advising an audit client of those dates. Providing such services does not generally create a threat to independence. However, the significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level.

### *Preparing Accounting Records and Financial Statements*

#### General Provisions

290.164 Management is responsible for the preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework. These responsibilities include:

- Determining accounting policies and the accounting treatment within those policies.
- Preparing or changing 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).
- Originating or changing journal entries, or determining or approving the account classifications of transactions.

290.165 Providing an audit client with accounting and bookkeeping services, such as preparing accounting records or financial statements, creates a self-review threat when the firm subsequently audits the financial statements.

290.166 The audit process, however, necessitates dialogue between the firm and management of the audit client, which may involve:

- The application of accounting standards or policies and financial statement disclosure requirements;
- The appropriateness of financial and accounting control and the methods used in determining the stated amounts of assets and liabilities; or
- Proposing adjusting journal entries.

These activities are considered to be a normal part of the audit process and do not, generally, create threats to independence so long as the client is responsible for making decisions in the preparation of the accounting records and financial statements.

290.167 Similarly, the client may request technical assistance from the firm on matters such as resolving account reconciliation problems or analyzing and accumulating information for regulatory reporting. In addition, the client may request technical advice on accounting issues such as the conversion of existing financial statements from one financial reporting framework to another (for example, to comply with group accounting policies or to transition to a different financial reporting framework such as International Financial Reporting

Standards). Such services do not, generally, create threats to independence provided the firm does not assume a management responsibility for the client.

### Audit Clients that are Not Public Interest Entities

290.168 The firm may provide services related to the preparation of accounting records and financial statements to an audit client that is not a public interest entity where the services are of a routine or mechanical nature, so long as any self-review threat created is reduced to an acceptable level. Services that are routine or mechanical in nature require little to no professional judgement from the professional accountant. Some examples of such services are:

- Preparing payroll calculations or reports based on client-originated data for approval and payment by the client.
- Recording recurring transactions for which amounts are easily determinable from source documents or originating data, such as a utility bill where the client has determined or approved the appropriate account classification.
- Recording a transaction for which the client has already determined the amount to be recorded, even though the transaction involves a significant degree of subjectivity.
- Calculating depreciation on fixed assets when the client determines the accounting policy and estimates of useful life and residual values.
- Posting client-approved entries to the trial balance.
- Preparing financial statements based on information in the client-approved trial balance and preparing the related notes based on client-approved records.

In all cases, the significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Arranging for such services to be performed by an individual who is not a member of the audit team; or
- If such services are performed by a member of the audit team, using a partner or senior staff member with appropriate expertise who is not a member of the audit team to review the work performed.

### Audit Clients that are Public Interest Entities

290.169 A firm shall not provide to an audit client that is a public interest entity accounting and bookkeeping services, including payroll services, or prepare financial statements on which the firm will express an opinion or financial information which forms the basis of the financial statements.

290.170 Despite paragraph 290.169, a firm may provide accounting and bookkeeping services, including payroll services and the preparation of financial statements or other financial information, of a routine or mechanical nature for divisions or related entities of an audit client that is a public interest entity if the personnel providing the services are not members of the audit team and:

- (a) The divisions or related entities for which the service is provided are collectively immaterial to the financial statements on which the firm will express an opinion; or
- (b) The services relate to matters that are collectively immaterial to the financial statements of the division or related entity.

## Valuation Services

### General Provisions

- 290.171 A valuation comprises the making of assumptions with regard to future developments, the application of appropriate methodologies and techniques, and the combination of both to compute a certain value, or range of values, for an asset, a liability or for a business as a whole.
- 290.172 Performing valuation services for an audit client may create a self-review threat. The existence and significance of any threat will depend on factors such as:
- Whether the valuation will have a material effect on the financial statements.
  - The extent of the client's involvement in determining and approving the valuation methodology and other significant matters of judgment.
  - The availability of established methodologies and professional guidelines.
  - For valuations involving standard or established methodologies, the degree of subjectivity inherent in the item.
  - The reliability and extent of the underlying data.
  - The degree of dependence on future events of a nature that could create significant volatility inherent in the amounts involved.
  - The extent and clarity of the disclosures in the financial statements.
- The significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:
- Having a professional who was not involved in providing the valuation service review the audit or valuation work performed; or
  - Making arrangements so that personnel providing such services do not participate in the audit engagement.
- 290.173 Certain valuations do not involve a significant degree of subjectivity. This is likely the case where the underlying assumptions are either established by law or regulation, or are widely accepted and when the techniques and methodologies to be used are based on generally accepted standards or prescribed by law or regulation. In such circumstances, the results of a valuation performed by two or more parties are not likely to be materially different.
- 290.174 If a firm is requested to perform a valuation to assist an audit client with its tax reporting obligations or for tax planning purposes and the results of the valuation will not have a direct effect on the financial statements, the provisions included in paragraph 290.186 apply.

### Audit Clients that are Not Public Interest Entities

- 290.175 In the case of an audit client that is not a public interest entity, if the valuation service has a material effect on the financial statements on which the firm will express an opinion and the valuation involves a significant degree of subjectivity, no safeguards could reduce the self-review threat to an acceptable level. Accordingly a firm shall not provide such a valuation service to an audit client.

### Audit Clients that are Public Interest Entities

- 290.176 A firm shall not provide valuation services to an audit client that is a public interest entity if the valuations would have a material effect, separately or in the aggregate, on the financial statements on which the firm will express an opinion.

## *Taxation Services*

290.177 Taxation services comprise a broad range of services, including:

- Tax return preparation;
- Tax calculations for the purpose of preparing the accounting entries;
- Tax planning and other tax advisory services; and
- Assistance in the resolution of tax disputes.

While taxation services provided by a firm to an audit client are addressed separately under each of these broad headings; in practice, these activities are often interrelated.

290.178 Performing certain tax services creates self-review and advocacy threats. The existence and significance of any threats will depend on factors such as:

- The system by which the tax authorities assess and administer the tax in question and the role of the firm in that process;
- The complexity of the relevant tax regime and the degree of judgment necessary in applying it;
- The particular characteristics of the engagement; and
- The level of tax expertise of the client's employees.

## **Tax Return Preparation**

290.179 Tax return preparation services involve assisting clients with their tax reporting obligations by drafting and completing information, including the amount of tax due (usually on standardized forms) required to be submitted to the applicable tax authorities. Such services also include advising on the tax return treatment of past transactions and responding on behalf of the audit client to the tax authorities' requests for additional information and analysis (including providing explanations of and technical support for the approach being taken). Tax return preparation services are generally based on historical information and principally involve analysis and presentation of such historical information under existing tax law, including precedents and established practice. Further, the tax returns are subject to whatever review or approval process the tax authority deems appropriate. Accordingly, providing such services does not generally create a threat to independence if management takes responsibility for the returns including any significant judgments made.

## **Tax Calculations for the Purpose of Preparing Accounting Entries**

### **Audit Clients that are Not Public Interest Entities**

290.180 Preparing calculations of current and deferred tax liabilities (or assets) for an audit client for the purpose of preparing accounting entries that will be subsequently audited by the firm creates a self-review threat. The significance of the threat will depend on:

- (a) The complexity of the relevant tax law and regulation and the degree of judgment necessary in applying them;
- (b) The level of tax expertise of the client's personnel; and
- (c) The materiality of the amounts to the financial statements.

Safeguards shall be applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to perform the service;
- If the service is performed by a member of the audit team, using a partner or senior staff member with appropriate expertise who is not a member of the audit team to review the tax calculations; or

- Obtaining advice on the service from an external tax professional.

### Audit Clients that are Public Interest Entities

290.181 In the case of an audit client that is a public interest entity, a firm shall not prepare tax calculations of current and deferred tax liabilities (or assets) for the purpose of preparing accounting entries that are material to the financial statements on which the firm will express an opinion.

### Tax Planning and Other Tax Advisory Services

290.182 Tax planning or other tax advisory services comprise a broad range of services, such as advising the client how to structure its affairs in a tax efficient manner or advising on the application of a new tax law or regulation.

290.183 A self-review threat may be created where the advice will affect matters to be reflected in the financial statements. The existence and significance of any threat will depend on factors such as:

- The degree of subjectivity involved in determining the appropriate treatment for the tax advice in the financial statements;
- The extent to which the outcome of the tax advice will have a material effect on the financial statements;
- Whether the effectiveness of the tax advice depends on the accounting treatment or presentation in the financial statements and there is doubt as to the appropriateness of the accounting treatment or presentation under the relevant financial reporting framework;
- The level of tax expertise of the client's employees;
- The extent to which the advice is supported by tax law or regulation, other precedent or established practice; and
- Whether the tax treatment is supported by a private ruling or has otherwise been cleared by the tax authority before the preparation of the financial statements.

For example, providing tax planning and other tax advisory services where the advice is clearly supported by tax authority or other precedent, by established practice or has a basis in tax law that is likely to prevail does not generally create a threat to independence.

290.184 The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to perform the service;
- Having a tax professional, who was not involved in providing the tax service, advise the audit team on the service and review the financial statement treatment;
- Obtaining advice on the service from an external tax professional; or
- Obtaining pre-clearance or advice from the tax authorities.

290.185 Where the effectiveness of the tax advice depends on a particular accounting treatment or presentation in the financial statements and:

- (a) The audit team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework; and
- (b) The outcome or consequences of the tax advice will have a material effect on the financial statements on which the firm will express an opinion;

The self-review threat would be so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, a firm shall not provide such tax advice to an audit client.

290.186 In providing tax services to an audit client, a firm may be requested to perform a valuation to assist the client with its tax reporting obligations or for tax planning purposes. Where the result of the valuation will have a direct effect on the financial statements, the provisions included in paragraphs 290.171 to 290.176 relating to valuation services are applicable. Where the valuation is performed for tax purposes only and the result of the valuation will not have a direct effect on the financial statements (i.e. the financial statements are only affected through accounting entries related to tax), this would not generally create threats to independence if such effect on the financial statements is immaterial or if the valuation is subject to external review by a tax authority or similar regulatory authority. If the valuation is not subject to such an external review and the effect is material to the financial statements, the existence and significance of any threat created will depend upon factors such as:

- The extent to which the valuation methodology is supported by tax law or regulation, other precedent or established practice and the degree of subjectivity inherent in the valuation.
- The reliability and extent of the underlying data.

The significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to perform the service;
- Having a professional review the audit work or the result of the tax service; or
- Obtaining pre-clearance or advice from the tax authorities.

### Assistance in the Resolution of Tax Disputes

290.187 An advocacy or self-review threat may be created when the firm represents an audit client in the resolution of a tax dispute once the tax authorities have notified the client that they have rejected the client's arguments on a particular issue and either the tax authority or the client is referring the matter for determination in a formal proceeding, for example before a tribunal or court. The existence and significance of any threat will depend on factors such as:

- Whether the firm has provided the advice which is the subject of the tax dispute;
- The extent to which the outcome of the dispute will have a material effect on the financial statements on which the firm will express an opinion;
- The extent to which the matter is supported by tax law or regulation, other precedent, or established practice;
- Whether the proceedings are conducted in public; and
- The role management plays in the resolution of the dispute.

The significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to perform the service;
- Having a tax professional, who was not involved in providing the tax service, advise the audit team on the services and review the financial statement treatment; or
- Obtaining advice on the service from an external tax professional.

290.188 Where the taxation services involve acting as an advocate for an audit client before a public tribunal or court in the resolution of a tax matter and the amounts involved are material to the financial statements on which the firm will express an opinion, the advocacy threat created would be so significant that no safeguards could eliminate or reduce the threat to an acceptable level. Therefore, the firm shall not perform this type of service for an audit

client. What constitutes a “public tribunal or court” shall be determined according to how tax proceedings are heard in the particular jurisdiction.

- 290.189 The firm is not, however, precluded from having a continuing advisory role (for example, responding to specific requests for information, providing factual accounts or testimony about the work performed or assisting the client in analyzing the tax issues) for the audit client in relation to the matter that is being heard before a public tribunal or court.

### *Internal Audit Services*

#### General Provisions

- 290.190 The scope and objectives of internal audit activities vary widely and depend on the size and structure of the entity and the requirements of management and those charged with governance. Internal audit activities may include:

- Monitoring of internal control – reviewing controls, monitoring their operation and recommending improvements thereto;
- Examination of financial and operating information – reviewing the means used to identify, measure, classify and report financial and operating information, and specific inquiry into individual items including detailed testing of transactions, balances and procedures;
- Review of the economy, efficiency and effectiveness of operating activities including non-financial activities of an entity; and
- Review of compliance with laws, regulations and other external requirements, and with management policies and directives and other internal requirements.

- 290.191 Internal audit services involve assisting the audit client in the performance of its internal audit activities. The provision of internal audit services to an audit client creates a self-review threat to independence if the firm uses the internal audit work in the course of a subsequent external audit. Performing a significant part of the client’s internal audit activities increases the possibility that firm personnel providing internal audit services will assume a management responsibility. If the firm’s personnel assume a management responsibility when providing internal audit services to an audit client, the threat created would be so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, a firm’s personnel shall not assume a management responsibility when providing internal audit services to an audit client.

- 290.192 Examples of internal audit services that involve assuming management responsibilities include:

- (a) Setting internal audit policies or the strategic direction of internal audit activities;
- (b) Directing and taking responsibility for the actions of the entity’s internal audit employees;
- (c) Deciding which recommendations resulting from internal audit activities shall be implemented;
- (d) Reporting the results of the internal audit activities to those charged with governance on behalf of management;
- (e) Performing procedures that form part of the internal control, such as reviewing and approving changes to employee data access privileges;
- (f) Taking responsibility for designing, implementing and maintaining internal control; and
- (g) Performing outsourced internal audit services, comprising all or a substantial portion of the internal audit function, where the firm is responsible for determining the scope of the internal audit work and may have responsibility for one or more of the matters noted in (a)–(f).



- 290.193 To avoid assuming a management responsibility, the firm shall only provide internal audit services to an audit client if it is satisfied that:
- (a) The client designates an appropriate and competent resource, preferably within senior management, to be responsible at all times for internal audit activities and to acknowledge responsibility for designing, implementing, and maintaining internal control;
  - (b) The client's management or those charged with governance reviews, assesses and approves the scope, risk and frequency of the internal audit services;
  - (c) The client's management evaluates the adequacy of the internal audit services and the findings resulting from their performance;
  - (d) The client's management evaluates and determines which recommendations resulting from internal audit services to implement and manages the implementation process; and
  - (e) The client's management reports to those charged with governance the significant findings and recommendations resulting from the internal audit services.

290.194 When a firm uses the work of an internal audit function, Hong Kong Standards on Auditing require the performance of procedures to evaluate the adequacy of that work. When a firm accepts an engagement to provide internal audit services to an audit client, and the results of those services will be used in conducting the external audit, a self-review threat is created because of the possibility that the audit team will use the results of the internal audit service without appropriately evaluating those results or exercising the same level of professional skepticism as would be exercised when the internal audit work is performed by individuals who are not members of the firm. The significance of the threat will depend on factors such as:

- The materiality of the related financial statement amounts;
- The risk of misstatement of the assertions related to those financial statement amounts; and
- The degree of reliance that will be placed on the internal audit service.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. An example of such a safeguard is using professionals who are not members of the audit team to perform the internal audit service.

### Audit Clients that are Public Interest Entities

- 290.195 In the case of an audit client that is a public interest entity, a firm shall not provide internal audit services that relate to:
- (a) A significant part of the internal controls over financial reporting;
  - (b) Financial accounting systems that generate information that is, separately or in the aggregate, significant to the client's accounting records or financial statements on which the firm will express an opinion; or
  - (c) Amounts or disclosures that are, separately or in the aggregate, material to the financial statements on which the firm will express an opinion.

### *IT Systems Services*

#### General Provisions

290.196 Services related to information technology ("IT") systems include the design or implementation of hardware or software systems. The systems may aggregate source data, form part of the internal control over financial reporting or generate information that affects the accounting records or financial statements, or the systems may be unrelated to the

audit client's accounting records, the internal control over financial reporting or financial statements. Providing systems services may create a self-review threat depending on the nature of the services and the IT systems.

- 290.197 The following IT systems services are deemed not to create a threat to independence as long as the firm's personnel do not assume a management responsibility:
- (a) Design or implementation of IT systems that are unrelated to internal control over financial reporting;
  - (b) Design or implementation of IT systems that do not generate information forming a significant part of the accounting records or financial statements;
  - (c) Implementation of "off-the-shelf" accounting or financial information reporting software that was not developed by the firm if the customization required to meet the client's needs is not significant; and
  - (d) Evaluating and making recommendations with respect to a system designed, implemented or operated by another service provider or the client.

### Audit Clients that are Not Public Interest Entities

- 290.198 Providing services to an audit client that is not a public interest entity involving the design or implementation of IT systems that (a) form a significant part of the internal control over financial reporting or (b) generate information that is significant to the client's accounting records or financial statements on which the firm will express an opinion creates a self-review threat.
- 290.199 The self-review threat is too significant to permit such services unless appropriate safeguards are put in place ensuring that:
- (a) The client acknowledges its responsibility for establishing and monitoring a system of internal controls;
  - (b) The client assigns the responsibility to make all management decisions with respect to the design and implementation of the hardware or software system to a competent employee, preferably within senior management;
  - (c) The client makes all management decisions with respect to the design and implementation process;
  - (d) The client evaluates the adequacy and results of the design and implementation of the system; and
  - (e) The client is responsible for operating the system (hardware or software) and for the data it uses or generates.
- 290.200 Depending on the degree of reliance that will be placed on the particular IT systems as part of the audit, a determination shall be made as to whether to provide such non-assurance services only with personnel who are not members of the audit team and who have different reporting lines within the firm. The significance of any remaining threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. An example of such a safeguard is having a professional accountant review the audit or non-assurance work.

### Audit Clients that are Public Interest Entities

- 290.201 In the case of an audit client that is a public interest entity, a firm shall not provide services involving the design or implementation of IT systems that (a) form a significant part of the internal control over financial reporting or (b) generate information that is significant to the client's accounting records or financial statements on which the firm will express an opinion.

### *Litigation Support Services*

- 290.202 Litigation support services may include activities such 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. These services may create a self-review or advocacy threat.
- 290.203 If the firm provides a litigation support service to an audit client and the service involves estimating damages or other amounts that affect the financial statements on which the firm will express an opinion, the valuation service provisions included in paragraphs 290.171 to 290.176 shall be followed. In the case of other litigation support services, the significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level.

### *Legal Services*

- 290.204 For the purpose of this section, legal services are defined as any services for which the person providing the services must either be admitted to practice law before the courts of the jurisdiction in which such services are to be provided or have the required legal training to practice law. Such legal services may include, depending on the jurisdiction, a wide and diversified range of areas including both corporate and commercial services to clients, such as contract support, litigation, mergers and acquisition legal advice and support and assistance to clients' internal legal departments. Providing legal services to an entity that is an audit client may create both self-review and advocacy threats.
- 290.205 Legal services that support an audit client in executing a transaction (e.g., contract support, legal advice, legal due diligence and restructuring) may create self-review threats. The existence and significance of any threat will depend on factors such as:
- The nature of the service;
  - Whether the service is provided by a member of the audit team; and
  - The materiality of any matter in relation to the client's financial statements.
- The significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:
- Using professionals who are not members of the audit team to perform the service; or
  - Having a professional who was not involved in providing the legal services provide advice to the audit team on the service and review any financial statement treatment.
- 290.206 Acting in an advocacy role for an audit client in resolving a dispute or litigation when the amounts involved are material to the financial statements on which the firm will express an opinion would create advocacy and self-review threats so significant that no safeguards could reduce the threat to an acceptable level. Therefore, the firm shall not perform this type of service for an audit client.
- 290.207 When a firm is asked to act in an advocacy role for an audit client in resolving a dispute or litigation when the amounts involved are not material to the financial statements on which the firm will express an opinion, the firm shall evaluate the significance of any advocacy and self-review threats created and apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:
- Using professionals who are not members of the audit team to perform the service; or
  - Having a professional who was not involved in providing the legal services advise the audit team on the service and review any financial statement treatment.
- 290.208 The appointment of a partner or an employee of the firm as General Counsel for legal affairs of 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 shall accept such an appointment for an audit client.

### *Recruiting Services*

#### General Provisions

290.209 Providing recruiting services to an audit client may create self-interest, familiarity or intimidation threats. The existence and significance of any threat will depend on factors such as:

- The nature of the requested assistance; and
- The role of the person to be recruited.

The significance of any threat created shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. In all cases, the firm shall not assume management responsibilities, including acting as a negotiator on the client's behalf, and the hiring decision shall be left to the client.

The firm may generally provide such services as reviewing the professional qualifications of a number of applicants and providing advice on their suitability for the post. In addition, the firm may interview candidates and advise on a candidate's competence for financial accounting, administrative or control positions.

#### Audit Clients that are Public Interest Entities

290.210 A firm shall not provide the following recruiting services to an audit client that is a public interest entity with respect to a director or officer of the entity or senior management in a position to exert significant influence over the preparation of the client's accounting records or the financial statements on which the firm will express an opinion:

- Searching for or seeking out candidates for such positions; and
- Undertaking reference checks of prospective candidates for such positions.

### *Corporate Finance Services*

290.211 Providing corporate finance services such as:

- Assisting an audit client in developing corporate strategies;
- Identifying possible targets for the audit client to acquire;
- Advising on disposal transactions;
- Assisting finance raising transactions; and
- Providing structuring advice,

may create advocacy and self-review threats. The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to provide the services; or
- Having a professional who was not involved in providing the corporate finance service advise the audit team on the service and review the accounting treatment and any financial statement treatment.

290.212 Providing a corporate finance service, for example advice on the structuring of a corporate finance transaction or on financing arrangements that will directly affect amounts that will be reported in the financial statements on which the firm will provide an opinion may create a self-review threat. The existence and significance of any threat will depend on factors such as:

- The degree of subjectivity involved in determining the appropriate treatment for the outcome or consequences of the corporate finance advice in the financial statements;
- The extent to which the outcome of the corporate finance advice will directly affect amounts recorded in the financial statements and the extent to which the amounts are material to the financial statements; and
- Whether the effectiveness of the corporate finance advice depends on a particular accounting treatment or presentation in the financial statements and there is doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework.

The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Using professionals who are not members of the audit team to perform the service; or
- Having a professional who was not involved in providing the corporate finance service to the client advise the audit team on the service and review the accounting treatment and any financial statement treatment.

290.213 Where the effectiveness of corporate finance advice depends on a particular accounting treatment or presentation in the financial statements and:

- (a) The audit team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework; and
- (b) The outcome or consequences of the corporate finance advice will have a material effect on the financial statements on which the firm will express an opinion;

The self-review threat would be so significant that no safeguards could reduce the threat to an acceptable level, in which case the corporate finance advice shall not be provided.

290.214 Providing corporate finance services involving promoting, dealing in, or underwriting an audit client's shares would create an advocacy or self-review threat that is so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, a firm shall not provide such services to an audit client.

## **Fees**

### *Fees—Relative Size*

290.215 When the total fees from an audit client represent a large proportion of the total fees of the firm expressing the audit opinion, the dependence on that client and concern about losing the client creates a self-interest or intimidation threat. The significance of the threat will depend on factors such as:

- The operating structure of the firm;
- Whether the firm is well established or new; and
- The significance of the client qualitatively and/or quantitatively to the firm.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Reducing the dependency on the client;
- External quality control reviews; or
- Consulting a third party, such as a professional regulatory body or a professional accountant, on key audit judgments.

290.216 A self-interest or intimidation threat is also created when the fees generated from an audit client represent a large proportion of the revenue from an individual partner's clients or a large proportion of the revenue of an individual office of the firm. The significance of the threat will depend upon factors such as:

- The significance of the client qualitatively and/or quantitatively to the partner or office; and
- The extent to which the remuneration of the partner, or the partners in the office, is dependent upon the fees generated from the client.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Reducing the dependency on the audit client;
- Having a professional accountant review the work or otherwise advise as necessary; or
- Regular independent internal or external quality reviews of the engagement.

### Audit Clients that are Public Interest Entities

290.217 Where an audit client is a public interest entity and, for two consecutive years, the total fees from the client and its related entities (subject to the considerations in paragraph 290.27) represent more than 15% of the total fees received by the firm expressing the opinion on the financial statements of the client, the firm shall disclose to those charged with governance of the audit client the fact that the total of such fees represents more than 15% of the total fees received by the firm, and discuss which of the safeguards below it will apply to reduce the threat to an acceptable level, and apply the selected safeguard:

- Prior to the issuance of the audit opinion on the second year's financial statements, a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, performs an engagement quality control review of that engagement or a professional regulatory body performs a review of that engagement that is equivalent to an engagement quality control review ("a pre-issuance review"); or
- After the audit opinion on the second year's financial statements has been issued, and before the issuance of the audit opinion on the third year's financial statements, a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, or a professional regulatory body performs a review of the second year's audit that is equivalent to an engagement quality control review ("a post-issuance review").

When the total fees significantly exceed 15%, the firm shall determine whether the significance of the threat is such that a post-issuance review would not reduce the threat to an acceptable level and, therefore, a pre-issuance review is required. In such circumstances a pre-issuance review shall be performed.

Thereafter, when the fees continue to exceed 15% each year, the disclosure to and discussion with those charged with governance shall occur and one of the above safeguards shall be applied. If the fees significantly exceed 15%, the firm shall determine whether the significance of the threat is such that a post-issuance review would not reduce the threat to an acceptable level and, therefore, a pre-issuance review is required. In such circumstances a pre-issuance review shall be performed.

### *Fees—Overdue*

290.218 A self-interest threat may be created if fees due from an audit client remain unpaid for a long time, especially if a significant part is not paid before the issue of the audit report for the following year. Generally the firm is expected to require payment of such fees before

such audit report is issued. If fees remain unpaid after the report has been issued, the existence and significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. An example of such a safeguard is having an additional professional accountant who did not take part in the audit engagement provide advice or review the work performed. The firm shall determine 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 or continue the audit engagement.

### *Contingent Fees*

- 290.219 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed by the firm. For the purposes of this section, a fee is not regarded as being contingent if established by a court or other public authority.
- 290.220 A contingent fee charged directly or indirectly, for example through an intermediary, by a firm in respect of an audit engagement creates a self-interest threat that is so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, a firm shall not enter into any such fee arrangement.
- 290.221 A contingent fee charged directly or indirectly, for example through an intermediary, by a firm in respect of a non-assurance service provided to an audit client may also create a self-interest threat. The threat created would be so significant that no safeguards could reduce the threat to an acceptable level if:
- (a) The fee is charged by the firm expressing the opinion on the financial statements and the fee is material or expected to be material to that firm;
  - (b) The fee is charged by a network firm that participates in a significant part of the audit and the fee is material or expected to be material to that firm; or
  - (c) The outcome of the non-assurance service, and therefore the amount of the fee, is dependent on a future or contemporary judgment related to the audit of a material amount in the financial statements.

Accordingly, such arrangements shall not be accepted.

- 290.222 For other contingent fee arrangements charged by a firm for a non-assurance service to an audit client, the existence and significance of any threats will depend on factors such as:
- The range of possible fee amounts;
  - Whether an appropriate authority determines the outcome of the matter upon which the contingent fee will be determined;
  - The nature of the service; and
  - The effect of the event or transaction on the financial statements.

The significance of any threats shall be evaluated and safeguards applied when necessary to eliminate the threats or reduce them to an acceptable level. Examples of such safeguards include:

- Having a professional accountant review the relevant audit work or otherwise advise as necessary; or
- Using professionals who are not members of the audit team to perform the non-assurance service.

### **Compensation and Evaluation Policies**

- 290.223 A self-interest threat is created when a member of the audit team is evaluated on or compensated for selling non-assurance services to that audit client. The significance of the threat will depend on:

- The proportion of the individual's compensation or performance evaluation that is based on the sale of such services;
- The role of the individual on the audit team; and
- Whether promotion decisions are influenced by the sale of such services.

The significance of the threat shall be evaluated and, if the threat is not at an acceptable level, the firm shall either revise the compensation plan or evaluation process for that individual or apply safeguards to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Removing such members from the audit team; or
- Having a professional accountant review the work of the member of the audit team.

290.224 A key audit partner shall not be evaluated on or compensated based on that partner's success in selling non-assurance services to the partner's audit client. This is not intended to prohibit normal profit-sharing arrangements between partners of a firm.

### **Gifts and Hospitality**

290.225 Accepting gifts or hospitality from an audit client may create self-interest and familiarity threats. If a firm or a member of the audit team accepts gifts or hospitality, unless the value is trivial and inconsequential, the threats created would be so significant that no safeguards could reduce the threats to an acceptable level. Consequently, a firm or a member of the audit team shall not accept such gifts or hospitality.

### **Actual or Threatened Litigation**

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

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

The significance of the threats shall be evaluated and safeguards applied when necessary to eliminate the threats or reduce them to an acceptable level. Examples of such safeguards include:

- If the litigation involves a member of the audit team, removing that individual from the audit team; or
- Having a professional review the work performed.

If such safeguards do not reduce the threats to an acceptable level, the only appropriate action is to withdraw from, or decline, the audit engagement.

**Paragraphs 290.227 to 290.499 are intentionally left blank.**

## **Reports that Include a Restriction on Use and Distribution**

### *Introduction*

290.500 The independence requirements in Section 290 apply to all audit engagements. However, in certain circumstances involving audit engagements where the report includes a restriction on use and distribution, and provided the conditions described in 290.501 to 290.502 are met, the independence requirements in this section may be modified as provided in paragraphs 290.505 to 290.514. These paragraphs are only applicable to an audit



engagement on special purpose financial statements (a) that is intended to provide a conclusion in positive or negative form that the financial statements are prepared in all material respects, in accordance with the applicable financial reporting framework, including, in the case of a fair presentation framework, that the financial statements give a true and fair view or are presented fairly, in all material respects, in accordance with the applicable financial reporting framework, and (b) where the audit report includes a restriction on use and distribution. The modifications are not permitted in the case of an audit of financial statements required by law or regulation.

- 290.501 The modifications to the requirements of Section 290 are permitted if the intended users of the report (a) are knowledgeable as to the purpose and limitations of the report, and (b) explicitly agree to the application of the modified independence requirements. Knowledge as to the purpose and limitations of the report may be obtained by the intended users through their participation, either directly or indirectly through their representative who has the authority to act for the intended users, in establishing the nature and scope of the engagement. Such participation enhances the ability of the firm to communicate with intended users about independence matters, including the circumstances that are relevant to the evaluation of the threats to independence and the applicable safeguards necessary to eliminate the threats or reduce them to an acceptable level, and to obtain their agreement to the modified independence requirements that are to be applied.
- 290.502 The firm shall communicate (for example, in an engagement letter) with the intended users regarding the independence requirements that are to be applied with respect to the provision of the audit engagement. Where the intended users are a class of users (for example, lenders in a syndicated loan arrangement) who are not specifically identifiable by name at the time the engagement terms are established, such users shall subsequently be made aware of the independence requirements agreed to by the representative (for example, by the representative making the firm's engagement letter available to all users).
- 290.503 If the firm also issues an audit report that does not include a restriction on use and distribution for the same client, the provisions of paragraphs 290.500 to 290.514 do not change the requirement to apply the provisions of paragraphs 290.1 to 290.226 to that audit engagement.
- 290.504 The modifications to the requirements of Section 290 that are permitted in the circumstances set out above are described in paragraphs 290.505 to 290.514. Compliance in all other respects with the provisions of Section 290 is required.

### *Public Interest Entities*

- 290.505 When the conditions set out in paragraphs 290.500 to 290.502 are met, it is not necessary to apply the additional requirements in paragraphs 290.100 to 290.226 that apply to audit engagements for public interest entities.

### *Related Entities*

- 290.506 When the conditions set out in paragraphs 290.500 to 290.502 are met, references to audit client do not include its related entities. However, when the audit team knows or has reason to believe that a relationship or circumstance involving a related entity of the client is relevant to the evaluation of the firm's independence of the client, the audit team shall include that related entity when identifying and evaluating threats to independence and applying appropriate safeguards.

### *Networks and Network Firms*

- 290.507 When the conditions set out in paragraphs 290.500 to 290.502 are met, reference to the firm does not include network firms. However, when the firm knows or has reason to believe that threats are created by any interests and relationships of a network firm, they shall be included in the evaluation of threats to independence.

*Financial Interests, Loans and Guarantees, Close Business Relationships and Family and Personal Relationships*

- 290.508 When the conditions set out in paragraphs 290.500 to 290.502 are met, the relevant provisions set out in paragraphs 290.102 to 290.143 apply only to the members of the engagement team, their immediate family members and close family members.
- 290.509 In addition, a determination shall be made as to whether threats to independence are created by interests and relationships, as described in paragraphs 290.102 to 290.143, between the audit client and the following members of the audit team:
- (a) Those who provide consultation regarding technical or industry specific issues, transactions or events; and
  - (b) Those who provide quality control for the engagement, including those who perform the engagement quality control review.

An evaluation shall be made of the significance of any threats that the engagement team has reason to believe are created by interests and relationships between the audit client and others within the firm who can directly influence the outcome of the audit engagement, including those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the audit engagement partner in connection with the performance of the audit engagement (including those at all successively senior levels above the engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent)).

- 290.510 An evaluation shall also be made of the significance of any threats that the engagement team has reason to believe are created by financial interests in the audit client held by individuals, as described in paragraphs 290.108 to 290.111 and paragraphs 290.113 to 290.115.
- 290.511 Where a threat to independence is not at an acceptable level, safeguards shall be applied to eliminate the threat or reduce it to an acceptable level.
- 290.512 In applying the provisions set out in paragraphs 290.106 and 290.115 to interests of the firm, if the firm has a material financial interest, whether direct or indirect, in the audit client, the self-interest threat created would be so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, the firm shall not have such a financial interest.

*Employment with an Audit Client*

- 290.513 An evaluation shall be made of the significance of any threats from any employment relationships as described in paragraphs 290.132 to 290.136. Where a threat exists that is not at an acceptable level, safeguards shall be applied to eliminate the threat or reduce it to an acceptable level. Examples of safeguards that might be appropriate include those set out in paragraph 290.134.

*Provision of Non-Assurance Services*

- 290.514 If the firm conducts an engagement to issue a restricted use and distribution report for an audit client and provides a non-assurance service to the audit client, the provisions of paragraphs 290.154 to 290.226 shall be complied with, subject to paragraphs 290.504 to 290.507.

**SECTION 291**  
**INDEPENDENCE—OTHER ASSURANCE ENGAGEMENTS**  
**CONTENTS**

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|  | Paragraph |
|--|-----------|
| Structure of Section .....   | 291.1     |
| A Conceptual Framework Approach to Independence .....                  | 291.4     |
| Assurance Engagements .....  | 291.12    |
| Assertion-Based Assurance Engagements .....                            | 291.17    |
| Direct Reporting Assurance Engagements .....                           | 291.20    |
| Reports that Include a Restriction on Use and Distribution .....       | 291.21    |
| Multiple Responsible Parties .....                                     | 291.28    |
| Documentation .....  | 291.29    |
| Engagement Period .....  | 291.30    |
| Breach of a Provision of this Section .....                            | 291.33    |
| Application of the Conceptual Framework Approach to Independence ..... | 291.100   |
| Financial Interests .....  | 291.104   |
| Loans and Guarantees .....   | 291.112   |
| Business Relationships .....   | 291.118   |
| Family and Personal Relationships .....                                | 291.120   |
| Employment with Assurance Clients .....                                | 291.126   |
| Recent Service with an Assurance Client .....                          | 291.130   |
| Serving as a Director or Officer of an Assurance Client .....          | 291.133   |
| Long Association of Senior Personnel with an Assurance Client .....    | 291.137   |
| Provision of Non-assurance Services to an Assurance Client .....       | 291.138   |
| Management Responsibilities .....                                      | 291.141   |
| Other Considerations .....   | 291.145   |
| Fees .....   | 291.148   |
| Fees—Relative Size .....   | 291.148   |
| Fees—Overdue .....   | 291.150   |
| Contingent Fees .....  | 291.151   |
| Gifts and Hospitality .....  | 291.155   |
| Actual or Threatened Litigation .....                                  | 291.156   |

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## Structure of Section

- 291.1 This section addresses independence requirements for assurance engagements that are not audit or review engagements. Independence requirements for audit and review engagements are addressed in Section 290. If the assurance client is also an audit or review client, the requirements in Section 290 also apply to the firm, network firms and members of the audit or review team. In certain circumstances involving assurance engagements where the assurance report includes a restriction on use and distribution and provided certain conditions are met, the independence requirements in this section may be modified as provided in 291.21 to 291.27.
- 291.2 Assurance engagements are designed to enhance intended users' degree of confidence about the outcome of the evaluation or measurement of a subject matter against criteria. The Hong Kong Framework for Assurance Engagements (the Assurance Framework) describes the elements and objectives of an assurance engagement and identifies engagements to which Hong Kong Standards on Assurance Engagements (HKSAEs) apply. For a description of the elements and objectives of an assurance engagement, refer to the Assurance Framework.
- 291.3 Compliance with the fundamental principle of objectivity requires being independent of assurance clients. In the case of assurance engagements, it is in the public interest and, therefore, required by this Code of Ethics, that members of assurance teams and firms be independent of assurance clients and that any threats that the firm has reason to believe are created by a network firm's interests and relationships be evaluated. In addition, when the assurance team knows or has reason to believe that a relationship or circumstance involving a related entity of the assurance client is relevant to the evaluation of the firm's independence from the client, the assurance team shall include that related entity when identifying and evaluating threats to independence and applying appropriate safeguards.

## A Conceptual Framework Approach to Independence

- 291.4 The objective of this section is to assist firms and members of assurance teams in applying the conceptual framework approach described below to achieving and maintaining independence.
- 291.5 Independence comprises:
- (a) *Independence of Mind*
- The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby 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 would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism has been compromised.
- 291.6 The conceptual framework approach shall be applied by professional accountants to:
- (a) Identify threats to independence;
- (b) Evaluate the significance of the threats identified; and
- (c) Apply safeguards when necessary to eliminate the threats or reduce them to an acceptable level.

When the professional accountant determines that appropriate safeguards are not available or cannot be applied to eliminate the threats or reduce them to an acceptable level, the professional accountant shall eliminate the circumstance or relationship creating the threats or decline or terminate the assurance engagement.

and (b) explicitly agree to the application of the modified independence requirements. Knowledge as to the purpose, subject matter information, and limitations of the report may be obtained by the intended users through their participation, either directly or indirectly through their representative who has the authority to act for the intended users, in establishing the nature and scope of the engagement. Such participation enhances the ability of the firm to communicate with intended users about independence matters, including the circumstances that are relevant to the evaluation of the threats to independence and the applicable safeguards necessary to eliminate the threats or reduce them to an acceptable level, and to obtain their agreement to the modified independence requirements that are to be applied.

- 291.22 The firm shall communicate (for example, in an engagement letter) with the intended users regarding the independence requirements that are to be applied with respect to the provision of the assurance engagement. Where the intended users are a class of users (for example, lenders in a syndicated loan arrangement) who are not specifically identifiable by name at the time the engagement terms are established, such users shall subsequently be made aware of the independence requirements agreed to by the representative (for example, by the representative making the firm's engagement letter available to all users).
- 291.23 If the firm also issues an assurance report that does not include a restriction on use and distribution for the same client, the provisions of paragraphs 291.25 to 291.27 do not change the requirement to apply the provisions of paragraphs 291.1 to 291.156 to that assurance engagement. If the firm also issues an audit report, whether or not it includes a restriction on use and distribution, for the same client, the provisions of Section 290 shall apply to that audit engagement.
- 291.24 The modifications to the requirements of Section 291 that are permitted in the circumstances set out above are described in paragraphs 291.25 to 291.27. Compliance in all other respects with the provisions of Section 291 is required.
- 291.25 When the conditions set out in paragraphs 291.21 and 291.22 are met, the relevant provisions set out in paragraphs 291.104 to 291.132 apply to all members of the engagement team, and their immediate and close family members. In addition, a determination shall be made as to whether threats to independence are created by interests and relationships between the assurance client and the following other members of the assurance team:
- Those who provide consultation regarding technical or industry specific issues, transactions or events; and
  - Those who provide quality control for the engagement, including those who perform the engagement quality control review.

An evaluation shall also be made, by reference to the provisions set out in paragraphs 291.104 to 291.132, of any threats that the engagement team has reason to believe are created by interests and relationships between the assurance client and others within the firm who can directly influence the outcome of the assurance engagement, including those who recommend the compensation, or who provide direct supervisory, management or other oversight, of the assurance engagement partner in connection with the performance of the assurance engagement.

- 291.26 Even though the conditions set out in paragraphs 291.21 to 291.22 are met, 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 that no safeguards could reduce the threat to an acceptable level. Accordingly, the firm shall not have such a financial interest. In addition, the firm shall comply with the other applicable provisions of this section described in paragraphs 291.112 to 291.156.
- 291.27 An evaluation shall also be made of any threats that the firm has reason to believe are created by network firm interests and relationships.

## Multiple Responsible Parties

291.28 In some assurance engagements, whether assertion-based or direct reporting, there might be several responsible parties. In determining whether it is necessary to apply the provisions in this section to each responsible party in such engagements, the firm may take into account whether an interest or relationship between the firm, or a member of the assurance team, and a particular responsible party would create a threat to independence that is not trivial and inconsequential in the context of the subject matter information. This will take into account factors such as:

- The materiality of the subject matter information (or of the subject matter) for which the particular responsible party is responsible; and
- The degree of public interest associated with the engagement.

If the firm determines that the threat to independence created by any such interest or relationship with a particular responsible party would be trivial and inconsequential, it may not be necessary to apply all of the provisions of this section to that responsible party.

## Documentation

291.29 Documentation provides evidence of the professional accountant's judgments in forming conclusions regarding compliance with independence requirements. The absence of documentation is not a determinant of whether a firm considered a particular matter nor whether it is independent.

The professional accountant shall document conclusions regarding compliance with independence requirements, and the substance of any relevant discussions that support those conclusions. Accordingly:

- (a) When safeguards are required to reduce a threat to an acceptable level, the professional accountant shall document the nature of the threat and the safeguards in place or applied that reduce the threat to an acceptable level; and
- (b) When a threat required significant analysis to determine whether safeguards were necessary and the professional accountant concluded that they were not because the threat was already at an acceptable level, the professional accountant shall document the nature of the threat and the rationale for the conclusion.

## Engagement Period

291.30 Independence from the assurance client is required both during the engagement period and the period covered by the subject matter information. The engagement period starts when the assurance team begins to perform assurance services with respect to the particular engagement. The engagement period ends when the assurance report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has terminated or the issuance of the final assurance report.

291.31 When an entity becomes an assurance client during or after the period covered by the subject matter information on which the firm will express a conclusion, the firm shall determine whether any threats to independence are created by:

- (a) Financial or business relationships with the assurance client during or after the period covered by the subject matter information but before accepting the assurance engagement; or
- (b) Previous services provided to the assurance client.

291.32 If a non-assurance service was provided to the assurance client during or after the period covered by the subject matter information but before the assurance team begins to perform assurance services and the service would not be permitted during the period of the assurance engagement, the firm shall evaluate any threat to independence created by the service. If any threat is not at an acceptable level, the assurance engagement shall only be accepted if

safeguards are applied to eliminate any threats or reduce them to an acceptable level. Examples of such safeguards include:

- Not including personnel who provided the non-assurance service as members of the assurance team;
- Having a professional accountant review the assurance and non-assurance work as appropriate; or
- Engaging another firm to evaluate the results of the non-assurance service or having another firm re-perform the non-assurance service to the extent necessary to enable it to take responsibility for the service.

However, if the non-assurance service has not been completed and it is not practical to complete or terminate the service before the commencement of professional services in connection with the assurance engagement, the firm shall only accept the assurance engagement if it is satisfied:

- (a) The non-assurance service will be completed within a short period of time; or
- (b) The client has arrangements in place to transition the service to another provider within a short period of time.

During the service period, safeguards shall be applied when necessary. In addition, the matter shall be discussed with those charged with governance.

### **Breach of a Provision of this Section**

- 291.33 When a breach of a provision of this section is identified, the firm shall terminate, suspend or eliminate the interest or relationship that caused the breach, and shall evaluate the significance of that breach and its impact on the firm's objectivity and ability to issue an assurance report. The firm shall determine whether action can be taken that satisfactorily addresses the consequences of the breach. In making this determination, the firm shall exercise professional judgment and take into account whether a reasonable and informed third party, weighing the significance of the breach, the action to be taken and all the specific facts and circumstances available to the professional accountant at that time, would be likely to conclude that the firm's objectivity would be compromised such that the firm is unable to issue an assurance report.
- 291.34 If the firm determines that action cannot be taken to satisfactorily address the consequences of the breach, the firm shall, as soon as possible, inform the party that engaged the firm or those charged with governance, as appropriate, and take the steps necessary to terminate the assurance engagement in compliance with any applicable legal or regulatory requirements relevant to terminating the assurance engagement.
- 291.35 If the firm determines that action can be taken to satisfactorily address the consequences of the breach, the firm shall discuss the breach and the action it has taken or proposes to take with the party that engaged the firm or those charged with governance, as appropriate. The firm shall discuss the breach and the proposed action on a timely basis, taking into account the circumstances of the engagement and the breach.
- 291.36 If the party that engaged the firm or those charged with governance, as appropriate, do not concur that the action satisfactorily addresses the consequences of the breach, the firm shall take the steps necessary to terminate the assurance engagement in compliance with any applicable legal or regulatory requirements relevant to terminating the assurance engagement.
- 291.37 The firm shall document the breach, the actions taken, key decisions made and all the matters discussed with the party that engaged the firm or those charged with governance. When the firm continues with the assurance engagement, the matters to be documented shall also include the conclusion that, in the firm's professional judgment, objectivity has not been compromised and the rationale for why the action taken satisfactorily addressed the consequences of the breach such that the firm could issue an assurance report.

**Paragraphs 291.38 to 291.99 are intentionally left blank.****Application of the Conceptual Framework Approach to Independence**

- 291.100 Paragraphs 291.104 to 291.156 describe specific circumstances and relationships that create or may create threats to independence. The paragraphs describe the potential threats and the types of safeguards that may be appropriate to eliminate the threats or reduce them to an acceptable level and identify certain situations where no safeguards could reduce the threats to an acceptable level. The paragraphs do not describe all of the circumstances and relationships that create or may create a threat to independence. The firm and the members of the assurance team shall evaluate the implications of similar, but different, circumstances and relationships and determine whether safeguards, including the safeguards in paragraphs 200.11 to 200.14 can be applied when necessary to eliminate the threats to independence or reduce them to an acceptable level.
- 291.101 The paragraphs demonstrate how the conceptual framework approach applies to assurance engagements and are to be read in conjunction with paragraph 291.28 which explains that, in the majority of assurance engagements, there is one responsible party and that responsible party is the assurance client. However, in some assurance engagements there are two or more responsible parties. In such circumstances, an evaluation shall be made of any threats the firm has reason to believe are created by interests and relationships between a member of the assurance team, the firm, a network firm and the party responsible for the subject matter. For assurance reports that include a restriction on use and distribution, the paragraphs are to be read in the context of paragraphs 291.21 to 291.27.
- 291.102 Interpretation 2005-01 provides further guidance on applying the independence requirements contained in this section to assurance engagements.
- 291.103 Paragraphs 291.104 to 291.119 contain references to the materiality of a financial interest, loan, or guarantee, or the significance of a business relationship. For the purpose of determining whether such an interest is material to an individual, the combined net worth of the individual and the individual's immediate family members may be taken into account.

**Financial Interests**

- 291.104 Holding a financial interest in an assurance client may create a self-interest threat. The existence and significance of any threat created depends on: (a) the role of the person holding the financial interest, (b) whether the financial interest is direct or indirect, and (c) the materiality of the financial interest.
- 291.105 Financial interests may be held through an intermediary (e.g. a collective investment vehicle, estate or trust). The determination of whether such financial interests are direct or indirect will depend upon whether the beneficial owner has control over the investment vehicle or the ability to influence its investment decisions. When control over the investment vehicle or the ability to influence investment decisions exists, this Code defines that financial interest to be a direct financial interest. Conversely, when the beneficial owner of the financial interest has no control over the investment vehicle or ability to influence its investment decisions, this Code defines that financial interest to be an indirect financial interest.
- 291.106 If a member of the assurance team, a member of that individual's immediate family, or a firm has a direct financial interest or a material indirect financial interest in the assurance client, the self-interest threat created would be so significant that no safeguards could reduce the threat to an acceptable level. Therefore, none of the following shall have a direct financial interest or a material indirect financial interest in the client: a member of the assurance team; a member of that individual's immediate family member; or the firm.



- 291.139 When specific guidance on a particular non-assurance service is not included in this section, the conceptual framework shall be applied when evaluating the particular circumstances.
- 291.140 Before the firm accepts an engagement to provide a non-assurance service to an assurance client, a determination shall be made as to whether providing such a service would create a threat to independence. In evaluating the significance of any threat created by a particular non-assurance service, consideration shall be given to any threat that the assurance team has reason to believe is created by providing other related non-assurance services. If a threat is created that cannot be reduced to an acceptable level by the application of safeguards the non-assurance service shall not be provided.

### *Management Responsibilities*

- 291.141 Management responsibilities involve controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, technological, physical and intangible resources.
- 291.142 Determining whether an activity is a management responsibility depends on the circumstances and requires the exercise of judgment. Examples of activities that would be considered a management responsibility include:
- Setting policies and strategic direction.
  - Hiring or dismissing employees.
  - Directing and taking responsibility for the actions of employees in relation to the employees' work for the entity.
  - Authorizing transactions.
  - Control or management of bank accounts or investments.
  - Deciding which recommendations of the firm or other third parties to implement.
  - Reporting to those charged with governance on behalf of management.
  - Taking responsibility for designing, implementing, monitoring or maintaining internal controls.
- 291.143 In providing assurance services to an assurance client, a firm shall not assume a management responsibility as part of the assurance service. If the firm were to assume a management responsibility as part of the assurance service, the threats created would be so significant that no safeguards could reduce the threats to an acceptable level. If the firm assumes a management responsibility as part of any other services provided to the assurance client, the firm shall ensure that the responsibility is not related to the subject matter or subject matter information of the assurance engagement provided by the firm.
- 291.144 When providing services that are related to the subject matter or subject matter information of an assurance engagement provided by the firm, the firm shall be satisfied that client management makes all judgments and decisions relating to the subject matter or subject matter information of the assurance engagement that are the responsibility of management. This includes ensuring that the client's management:
- Designates an individual who possesses suitable skill, knowledge and experience to be responsible at all times for the client's decisions and to oversee the services. Such an individual, preferably within senior management, would understand the objectives, nature and results of the services and the respective client and firm responsibilities. However, the individual is not required to possess the expertise to perform or re-perform the services;
  - Provides oversight of the services and evaluates the adequacy of the results of the services performed for the client's purpose; and

- Accepts responsibility for the actions, if any, to be taken arising from the results of the services.

### *Other Considerations*

- 291.145 Threats to independence may be created when a firm provides a non-assurance service related to the subject matter information of an assurance engagement. In such cases, an evaluation of the significance of the firm's involvement with the subject matter information of the engagement shall be made, and a determination shall be made of whether any self-review threats that are not at an acceptable level can be reduced to an acceptable level by the application of safeguards.
- 291.146 A self-review threat may be created if the firm is involved in the preparation of subject matter information which is subsequently the subject matter information of an assurance engagement. For example, a self-review threat would be created if the firm developed and prepared prospective financial information and subsequently provided assurance on this information. Consequently, the firm shall evaluate the significance of any self-review threat created by the provision of such services and apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level.
- 291.147 When a firm performs a valuation that forms part of the subject matter information of an assurance engagement, the firm shall evaluate the significance of any self-review threat and apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level.

## **Fees**

### *Fees—Relative Size*

- 291.148 When the total fees from an assurance client represent a large proportion of the total fees of the firm expressing the conclusion, the dependence on that client and concern about losing the client creates a self-interest or intimidation threat. The significance of the threat will depend on factors such as:

- The operating structure of the firm;
- Whether the firm is well established or new; and
- The significance of the client qualitatively and/or quantitatively to the firm.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Reducing the dependency on the client;
- External quality control reviews; or
- Consulting a third party, such as a professional regulatory body or a professional accountant, on key assurance judgments.

- 291.149 A self-interest or intimidation threat is also created when the fees generated from an assurance client represent a large proportion of the revenue from an individual partner's clients. The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. An example of such a safeguard is having an additional professional accountant who was not a member of the assurance team review the work or otherwise advise as necessary.

### *Fees—Overdue*

- 291.150 A self-interest threat may be created if fees due from an assurance client remain unpaid for a long time, especially if a significant part is not paid before the issue of the assurance report, if any, for the following period. Generally the firm is expected to require payment of

such fees before any such report is issued. If fees remain unpaid after the report has been issued, the existence and significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. An example of such a safeguard is having another professional accountant who did not take part in the assurance engagement provide advice or review the work performed. The firm shall determine 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 or continue the assurance engagement.

### *Contingent Fees*

- 291.151 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed by the firm. For the purposes of this section, fees are not regarded as being contingent if established by a court or other public authority.
- 291.152 A contingent fee charged directly or indirectly, for example through an intermediary, by a firm in respect of an assurance engagement creates a self-interest threat that is so significant that no safeguards could reduce the threat to an acceptable level. Accordingly, a firm shall not enter into any such fee arrangement.
- 291.153 A contingent fee charged directly or indirectly, for example through an intermediary, by a firm in respect of a non-assurance service provided to an assurance client may also create a self-interest threat. If the outcome of the non-assurance service, and therefore, the amount of the fee, is dependent on a future or contemporary judgment related to a matter that is material to the subject matter information of the assurance engagement, no safeguards could reduce the threat to an acceptable level. Accordingly, such arrangements shall not be accepted.
- 291.154 For other contingent fee arrangements charged by a firm for a non-assurance service to an assurance client, the existence and significance of any threats will depend on factors such as:
- The range of possible fee amounts;
  - Whether an appropriate authority determines the outcome of the matter upon which the contingent fee will be determined;
  - The nature of the service; and
  - The effect of the event or transaction on the subject matter information.

The significance of any threats shall be evaluated and safeguards applied when necessary to eliminate the threats or reduce them to an acceptable level. Examples of such safeguards include:

- Having a professional accountant review the relevant assurance work or otherwise advise as necessary; or
- Using professionals who are not members of the assurance team to perform the non-assurance service.

### **Gifts and Hospitality**

- 291.155 Accepting gifts or hospitality from an assurance client may create self-interest and familiarity threats. If a firm or a member of the assurance team accepts gifts or hospitality, unless the value is trivial and inconsequential, the threats created would be so significant that no safeguards could reduce the threats to an acceptable level. Consequently, a firm or a member of the assurance team shall not accept such gifts or hospitality.

### **Actual or Threatened Litigation**

- 291.156 When litigation takes place, or appears likely, between the firm or a member of the assurance team and the assurance client, self-interest and intimidation threats are 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. When the firm and the client's management are placed in adversarial positions by actual or threatened litigation, affecting management's willingness to make complete disclosures self-interest and intimidation threats are created. The significance of the threats created will depend on such factors as:

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

The significance of the threats shall be evaluated and safeguards applied when necessary to eliminate the threats or reduce them to an acceptable level. Examples of such safeguards include:

- If the litigation involves a member of the assurance team, removing that individual from the assurance team; or
- Having a professional review the work performed.

If such safeguards do not reduce the threats to an acceptable level, the only appropriate action is to withdraw from, or decline, the assurance engagement.

### **Interpretation 2005-01 (Revised June 2010 to conform to changes resulting from the IESBA's project to improve the clarity of the Code)**

#### *Application of Section 291 to Assurance Engagements that are Not Financial Statement Audit Engagements*

This interpretation provides guidance on the application of the independence requirements contained in Section 291 to assurance engagements that are not financial statement audit engagements.

This interpretation focuses on the application issues that are particular to assurance engagements that are not financial statement audit engagements. There are other matters noted in Section 291 that are relevant in the consideration of independence requirements for all assurance engagements. For example, paragraph 291.3 states that an evaluation shall be made of any threats the firm has reason to believe are created by a network firm's interests and relationships. It also states that 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 shall include the related entity when evaluating threats to independence and when necessary applying safeguards. These matters are not specifically addressed in this interpretation.

As explained in the Hong Kong Framework for Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants, in an assurance engagement, the professional accountant in public practice expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria.

#### *Assertion-Based Assurance Engagements*

In an assertion-based assurance engagement, the evaluation or measurement of the subject matter is performed by the responsible party, and the subject matter information is in the form of an assertion by the responsible party that is made available to the intended users.

In an assertion-based assurance engagement independence is required from the responsible party, which is responsible for the subject matter information and may be responsible for the subject matter.

In those assertion-based assurance engagements where the responsible party is responsible for the subject matter information but not the subject matter, independence is required from the responsible party. In addition, an evaluation shall be made of any threats the firm has reason to believe are created by interests and relationships between a member of the assurance team, the firm, a network firm and the party responsible for the subject matter.

### *Direct Reporting Assurance Engagements*

In a direct reporting assurance engagement, the professional accountant in public practice either directly performs the evaluation or measurement of the subject matter, or obtains a representation from the responsible party that has performed the evaluation or measurement that is not available to the intended users. The subject matter information is provided to the intended users in the assurance report.

In a direct reporting assurance engagement independence is required from the responsible party, which is responsible for the subject matter.

### *Multiple Responsible Parties*

In both assertion-based assurance engagements and direct reporting assurance engagements there may be several responsible parties. For example, a public accountant in public practice may be asked to provide assurance on the monthly circulation statistics of a number of independently owned newspapers. The assignment could be an assertion based assurance engagement where each newspaper measures its circulation and the statistics are presented in an assertion that is available to the intended users. Alternatively, the assignment could be a direct reporting assurance engagement, where there is no assertion and there may or may not be a written representation from the newspapers.

In such engagements, when determining whether it is necessary to apply the provisions in Section 291 to each responsible party, the firm may take into account whether an interest or relationship between the firm, or a member of the assurance team, and a particular responsible party would create a threat to independence that is not trivial and inconsequential in the context of the subject matter information. This will take into account:

- The materiality of the subject matter information (or the subject matter) for which the particular responsible party is responsible; and
- The degree of public interest that is associated with the engagement.

If the firm determines that the threat to independence created by any such relationships with a particular responsible party would be trivial and inconsequential it may not be necessary to apply all of the provisions of this section to that responsible party.

### *Example*

The following example has been developed to demonstrate the application of Section 291. It is assumed that the client is not also a financial statement audit client of the firm, or a network firm.

A firm is engaged to provide assurance on the total proven oil reserves of 10 independent companies. Each company has conducted geographical and engineering surveys to determine their reserves (subject matter). There are established criteria to determine when a reserve may be considered to be proven which the professional accountant in public practice determines to be suitable criteria for the engagement.

The proven reserves for each company as at 31 December 20X0 were as follows:

|           | <b>Proven oil reserves<br/>thousands of barrels</b> |
|-----------|---|
| Company 1 | 5,200   |
| Company 2 | 725   |
| Company 3 | 3,260   |
| Company 4 | 15,000  |

|              |                |
|--------------|----------------|
| Company 5    | 6,700          |
| Company 6    | 39,126         |
| Company 7    | 345            |
| Company 8    | 175            |
| Company 9    | 24,135         |
| Company 10   | 9,635          |
| <b>Total</b> | <b>104,301</b> |

The engagement could be structured in differing ways:

### Assertion-Based Engagements

- A1 Each company measures its reserves and provides an assertion to the firm and to intended users.
- A2 An entity other than the companies measures the reserves and provides an assertion to the firm and to intended users.

### Direct Reporting Engagements

- D1 Each company measures the reserves and provides the firm with a written representation that measures its reserves against the established criteria for measuring proven reserves. The representation is not available to the intended users.
- D2 The firm directly measures the reserves of some of the companies.

### Application of Approach

- A1 Each company measures its reserves and provides an assertion to the firm and to intended users.

There are several responsible parties in this engagement (companies 1-10). When determining whether it is necessary to apply the independence provisions to all of the companies, the firm may take into account whether an interest or relationship with a particular company would create a threat to independence that is not at an acceptable level. This will take into account factors such as:

- The materiality of the company's proven reserves in relation to the total reserves to be reported on; and
- The degree of public interest associated with the engagement. (Paragraph 291.28.)

For example Company 8 accounts for 0.17% of the total reserves, therefore a business relationship or interest with Company 8 would create less of a threat than a similar relationship with Company 6, which accounts for approximately 37.5% of the reserves.

Having determined those companies to which the independence requirements apply, the assurance team and the firm are required to be independent of those responsible parties that would be considered to be the assurance client (paragraph 291.28).

- A2 An entity other than the companies measures the reserves and provides an assertion to the firm and to intended users.

The firm shall be independent of the entity that measures the reserves and provides an assertion to the firm and to intended users (paragraph 291.19). That entity is not responsible for the subject matter and so an evaluation shall be made of any threats the firm has reason to believe are created by interests/relationships with the party responsible for the subject matter (paragraph 291.19). There are several parties responsible for the subject matter in this engagement (Companies 1-10). As discussed

in example A1 above, the firm may take into account whether an interest or relationship with a particular company would create a threat to independence that is not at an acceptable level.

- D1 Each company provides the firm with a representation that measures its reserves against the established criteria for measuring proven reserves. The representation is not available to the intended users.

There are several responsible parties in this engagement (Companies 1-10). When determining whether it is necessary to apply the independence provisions to all of the companies, the firm may take into account whether an interest or relationship with a particular company would create a threat to independence that is not at an acceptable level. This will take into account factors such as:

- The materiality of the company's proven reserves in relation to the total reserves to be reported on; and
- The degree of public interest associated with the engagement. (Paragraph 291.28).

For example, Company 8 accounts for 0.17% of the reserves, therefore a business relationship or interest with Company 8 would create less of a threat than a similar relationship with Company 6 that accounts for approximately 37.5% of the reserves.

Having determined those companies to which the independence requirements apply, the assurance team and the firm shall be independent of those responsible parties that would be considered to be the assurance client (paragraph 291.28).

- D2 The firm directly measures the reserves of some of the companies.

The application is the same as in example D1.

## APPENDIX 3

### Amendments to the Code of Ethics for Professional Accountants

*The following sets out amendments required for this Code of Ethics for Professional Accountants. The amendments set out below will be incorporated into the text of this Code after being effective and relevant content in this appendix will be deleted.*

#### Changes to the Code of Ethics for Professional Accountants — Responding to Non-Compliance with Laws and Regulations

*(The changes will be effective on 15 July 2017. Early adoption is permitted)*

Sections 225 and 360 are added to the Code.

#### SECTION 225

##### Responding to Non-Compliance with Laws and Regulations

###### Purpose

- 225.1 A professional accountant in public practice may encounter or be made aware of non-compliance or suspected non-compliance with laws and regulations in the course of providing a professional service to a client. The purpose of this section is to set out the professional accountant's responsibilities when encountering such non-compliance or suspected non-compliance, and guide the professional accountant in assessing the implications of the matter and the possible courses of action when responding to it. This section applies regardless of the nature of the client, including whether or not it is a public interest entity.
- 225.2 Non-compliance with laws and regulations ("non-compliance") comprises acts of omission or commission, intentional or unintentional, committed by a client, or by those charged with governance, by management or by other individuals working for or under the direction of a client which are contrary to the prevailing laws or regulations.
- 225.3 In some jurisdictions, there are legal or regulatory provisions governing how professional accountants should address non-compliance or suspected non-compliance which may differ from or go beyond this section. When encountering such non-compliance or suspected non-compliance, the professional accountant has a responsibility to obtain an understanding of those provisions and comply with them, including any requirement to report the matter to an appropriate authority and any prohibition on alerting the client prior to making any disclosure, for example, pursuant to anti-money laundering legislation.
- 225.4 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. When responding to non-compliance or suspected non-compliance, the objectives of the professional accountant are:
- (a) To comply with the fundamental principles of integrity and professional behavior;
  - (b) By alerting management or, where appropriate, those charged with governance of the client, to seek to:
    - (i) Enable them to rectify, remediate or mitigate the consequences of the identified or suspected non-compliance; or
    - (ii) Deter the commission of the non-compliance where it has not yet occurred; and
  - (c) To take such further action as appropriate in the public interest.



## Scope

- 225.5 This section sets out the approach to be taken by a professional accountant who encounters or is made aware of non-compliance or suspected non-compliance with:
- (a) Laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the client's financial statements; and
  - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the client's financial statements, but compliance with which may be fundamental to the operating aspects of the client's business, to its ability to continue its business, or to avoid material penalties.
- 225.6 Examples of laws and regulations which this section addresses include those that deal with:
- Fraud, corruption and bribery.
  - Money laundering, terrorist financing and proceeds of crime.
  - Securities markets and trading.
  - Banking and other financial products and services.
  - Data protection.
  - Tax and pension liabilities and payments.
  - Environmental protection.
  - Public health and safety.
- 225.7 Non-compliance may result in fines, litigation or other consequences for the client that may have a material effect on its financial statements. Importantly, such non-compliance may have wider public interest implications in terms of potentially substantial harm to investors, creditors, employees or the general public. For the purposes of this section, an act that causes substantial harm is one that results in serious adverse consequences to any of these parties in financial or non-financial terms. Examples include the perpetration of a fraud resulting in significant financial losses to investors, and breaches of environmental laws and regulations endangering the health or safety of employees or the public.
- 225.8 A professional accountant who encounters or is made aware of matters that are clearly inconsequential, judged by their nature and their impact, financial or otherwise, on the client, its stakeholders and the general public, is not required to comply with this section with respect to such matters.
- 225.9 This section does not address:
- (a) Personal misconduct unrelated to the business activities of the client; and
  - (b) Non-compliance other than by the client or those charged with governance, management or other individuals working for or under the direction of the client. This includes, for example, circumstances where a professional accountant has been engaged by a client to perform a due diligence assignment on a third party entity and the identified or suspected non-compliance has been committed by that third party.

The professional accountant may nevertheless find the guidance in this section helpful in considering how to respond in these situations.

## Responsibilities of the Client's Management and Those Charged with Governance

- 225.10 It is the responsibility of the client's management, with the oversight of those charged with governance, to ensure that the client's business activities are conducted in accordance with

laws and regulations. It is also the responsibility of management and those charged with governance to identify and address any non-compliance by the client, by an individual charged with governance of the entity, by a member of management, or by other individuals working for or under the direction of the client.

## **Responsibilities of Professional Accountants in Public Practice**

- 225.11 Where a professional accountant becomes aware of a matter to which this section applies, the steps that the professional accountant takes to comply with this section shall be taken on a timely basis, having regard to the professional accountant's understanding of the nature of the matter and the potential harm to the interests of the entity, investors, creditors, employees or the general public.

## **Audits of Financial Statements**

### *Obtaining an Understanding of the Matter*

- 225.12 If a professional accountant engaged to perform an audit of financial statements becomes aware of information concerning an instance of non-compliance or suspected non-compliance, whether in the course of performing the engagement or through information provided by other parties, the professional accountant shall obtain an understanding of the matter, including the nature of the act and the circumstances in which it has occurred or may occur.
- 225.13 The professional accountant is expected to apply knowledge, professional judgment and expertise, but is not expected to have a level of knowledge of laws and regulations that is greater than that which is required to undertake the engagement. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. Depending on the nature and significance of the matter, the professional accountant may consult on a confidential basis with others within the firm, a network firm or a professional body, or with legal counsel.
- 225.14 If the professional accountant identifies or suspects that non-compliance has occurred or may occur, the professional accountant shall discuss the matter with the appropriate level of management and, where appropriate, those charged with governance.
- 225.15 Such discussion serves to clarify the professional accountant's understanding of the facts and circumstances relevant to the matter and its potential consequences. The discussion also may prompt management or those charged with governance to investigate the matter.
- 225.16 The appropriate level of management with whom to discuss the matter is a question of professional judgment. Relevant factors to consider include:
- The nature and circumstances of the matter.
  - The individuals actually or potentially involved.
  - The likelihood of collusion.
  - The potential consequences of the matter.
  - Whether that level of management is able to investigate the matter and take appropriate action.
- 225.17 The appropriate level of management is generally at least one level above the person or persons involved or potentially involved in the matter. If the professional accountant believes that management is involved in the non-compliance or suspected non-compliance, the professional accountant shall discuss the matter with those charged with governance. The professional accountant may also consider discussing the matter with internal auditors, where applicable. In the context of a group, the appropriate level may be management at an entity that controls the client.

*Addressing the Matter*

- 225.18 In discussing the non-compliance or suspected non-compliance with management and, where appropriate, those charged with governance, the professional accountant shall advise them to take appropriate and timely actions, if they have not already done so, to:
- (a) Rectify, remediate or mitigate the consequences of the non-compliance;
  - (b) Deter the commission of the non-compliance where it has not yet occurred; or
  - (c) Disclose the matter to an appropriate authority where required by law or regulation or where considered necessary in the public interest.
- 225.19 The professional accountant shall consider whether the client's management and those charged with governance understand their legal or regulatory responsibilities with respect to the non-compliance or suspected non-compliance. If not, the professional accountant may suggest appropriate sources of information or recommend that they obtain legal advice.
- 225.20 The professional accountant shall comply with applicable:
- (a) Laws and regulations, including legal or regulatory provisions governing the reporting of non-compliance or suspected non-compliance to an appropriate authority. In this regard, some laws and regulations may stipulate a period within which reports are to be made; and
  - (b) Requirements under auditing standards, including those relating to:
    - Identifying and responding to non-compliance, including fraud.
    - Communicating with those charged with governance.
    - Considering the implications of the non-compliance or suspected non-compliance for the auditor's report.

*Communication with Respect to Groups*

- 225.21 A professional accountant may:
- (a) For purposes of an audit of group financial statements, be requested by the group engagement team to perform work on financial information related to a component of the group; or
  - (b) Be engaged to perform an audit of a component's financial statements for purposes other than the group audit, for example, a statutory audit.

Where the professional accountant becomes aware of non-compliance or suspected non-compliance in relation to the component in either situation, the professional accountant shall, in addition to responding to the matter in accordance with the provisions of this section, communicate it to the group engagement partner unless prohibited from doing so by law or regulation. This is to enable the group engagement partner to be informed about the matter and to determine, in the context of the group audit, whether and, if so, how it should be addressed in accordance with the provisions in this section.

- 225.22 Where the group engagement partner becomes aware of non-compliance or suspected non-compliance in the course of an audit of group financial statements, including as a result of being informed of such a matter in accordance with paragraph 225.21, the group engagement partner shall, in addition to responding to the matter in the context of the group audit in accordance with the provisions of this section, consider whether the matter may be relevant to one or more components:
- (a) Whose financial information is subject to work for purposes of the audit of the group financial statements; or
  - (b) Whose financial statements are subject to audit for purposes other than the group audit, for example, a statutory audit.

If so, the group engagement partner shall take steps to have the non-compliance or suspected non-compliance communicated to those performing work at components where the matter may be relevant, unless prohibited from doing so by law or regulation. If necessary in relation to subparagraph (b), appropriate inquiries shall be made (either of management or from publicly available information) as to whether the relevant component(s) is subject to audit and, if so, to ascertain to the extent practicable the identity of the auditor. The communication is to enable those responsible for work at such components to be informed about the matter and to determine whether and, if so, how it should be addressed in accordance with the provisions in this section.

*Determining Whether Further Action Is Needed*

- 225.23 The professional accountant shall assess the appropriateness of the response of management and, where applicable, those charged with governance.
- 225.24 Relevant factors to consider in assessing the appropriateness of the response of management and, where applicable, those charged with governance include whether:
- The response is timely.
  - The non-compliance or suspected non-compliance has been adequately investigated.
  - Action has been, or is being, taken to rectify, remediate or mitigate the consequences of any non-compliance.
  - Action has been, or is being, taken to deter the commission of any non-compliance where it has not yet occurred.
  - Appropriate steps have been, or are being, taken to reduce the risk of re-occurrence, for example, additional controls or training.
  - The non-compliance or suspected non-compliance has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.
- 225.25 In light of the response of management and, where applicable, those charged with governance, the professional accountant shall determine if further action is needed in the public interest.
- 225.26 The determination of whether further action is needed, and the nature and extent of it, will depend on various factors, including:
- The legal and regulatory framework.
  - The urgency of the matter.
  - The pervasiveness of the matter throughout the client.
  - Whether the professional accountant continues to have confidence in the integrity of management and, where applicable, those charged with governance.
  - Whether the non-compliance or suspected non-compliance is likely to recur.
  - Whether there is credible evidence of actual or potential substantial harm to the interests of the entity, investors, creditors, employees or the general public.
- 225.27 Examples of circumstances that may cause the professional accountant no longer to have confidence in the integrity of management and, where applicable, those charged with governance include situations where:
- The professional accountant suspects or has evidence of their involvement or intended involvement in any non-compliance.
  - The professional accountant is aware that they have knowledge of such non-compliance and, contrary to legal or regulatory requirements, have not reported, or

authorized the reporting of, the matter to an appropriate authority within a reasonable period.

- 225.28 In determining the need for, and nature and extent of, further action, the professional accountant shall exercise professional judgment and take into account whether a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at the time, would be likely to conclude that the professional accountant has acted appropriately in the public interest.
- 225.29 Further action by the professional accountant may include:
- Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
  - Withdrawing from the engagement and the professional relationship where permitted by law or regulation.
- 225.30 Where the professional accountant determines that withdrawing from the engagement and the professional relationship would be appropriate, doing so would not be a substitute for taking other actions that may be needed to achieve the professional accountant's objectives under this section. In some jurisdictions, however, there may be limitations as to the further actions available to the professional accountant and withdrawal may be the only available course of action.
- 225.31 Where the professional accountant has withdrawn from the professional relationship pursuant to paragraphs 225.25 and 225.29, the professional accountant shall, on request by the proposed successor accountant, provide all such facts and other information concerning the identified or suspected non-compliance that, in the predecessor accountant's opinion, the proposed successor accountant needs to be aware of before deciding whether to accept the audit appointment. The predecessor accountant shall do so despite paragraph 210.14, unless prohibited by law or regulation. If the proposed successor accountant is unable to communicate with the predecessor accountant, the proposed successor accountant shall take reasonable steps to obtain information about the circumstances of the change of appointment by other means, such as through inquiries of third parties or background investigations of management or those charged with governance.
- 225.32 As consideration of the matter may involve complex analysis and judgments, the professional accountant may consider consulting internally, obtaining legal advice to understand the professional accountant's options and the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or professional body.

### Determining Whether to Disclose the Matter to an Appropriate Authority

- 225.33 Disclosure of the matter to an appropriate authority would be precluded if doing so would be contrary to law or regulation. Otherwise, the purpose of making disclosure is to enable an appropriate authority to cause the matter to be investigated and action to be taken in the public interest.
- 225.34 The determination of whether to make such a disclosure depends in particular on the nature and extent of the actual or potential harm that is or may be caused by the matter to investors, creditors, employees or the general public. For example, the professional accountant may determine that disclosure of the matter to an appropriate authority is an appropriate course of action if:
- The entity is engaged in bribery (for example, of local or foreign government officials for purposes of securing large contracts).
  - The entity is regulated and the matter is of such significance as to threaten its license to operate.

- The entity is listed on a securities exchange and the matter could result in adverse consequences to the fair and orderly market in the entity's securities or pose a systemic risk to the financial markets.
- Products that are harmful to public health or safety would likely be sold by the entity.
- The entity is promoting a scheme to its clients to assist them in evading taxes.

The determination of whether to make such a disclosure will also depend on external factors such as:

- Whether there is an appropriate authority that is able to receive the information, and cause the matter to be investigated and action to be taken. The appropriate authority will depend on the nature of the matter, for example, a securities regulator in the case of fraudulent financial reporting or an environmental protection agency in the case of a breach of environmental laws and regulations.
- Whether there exists robust and credible protection from civil, criminal or professional liability or retaliation afforded by legislation or regulation, such as under whistle-blowing legislation or regulation.
- Whether there are actual or potential threats to the physical safety of the professional accountant or other individuals.

225.35 If the professional accountant determines that disclosure of the non-compliance or suspected non-compliance to an appropriate authority is an appropriate course of action in the circumstances, this will not be considered a breach of the duty of confidentiality under Section 140 of this Code. When making such disclosure, the professional accountant shall act in good faith and exercise caution when making statements and assertions. The professional accountant shall also consider whether it is appropriate to inform the client of the professional accountant's intentions before disclosing the matter.

225.36 In exceptional circumstances, the professional accountant may become aware of actual or intended conduct that the professional accountant has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. Having considered whether it would be appropriate to discuss the matter with management or those charged with governance of the entity, the professional accountant shall exercise professional judgment and may immediately disclose the matter to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach of law or regulation. Such disclosure will not be considered a breach of the duty of confidentiality under Section 140 of this Code.

### *Documentation*

225.37 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the professional accountant shall, in addition to complying with the documentation requirements under applicable auditing standards, document:

- How management and, where applicable, those charged with governance have responded to the matter.
- The courses of action the professional accountant considered, the judgments made and the decisions that were taken, having regard to the reasonable and informed third party perspective.
- How the professional accountant is satisfied that the professional accountant has fulfilled the responsibility set out in paragraph 225.25.

225.38 International Standards on Auditing (ISAs), for example, require a professional accountant performing an audit of financial statements to:

- Prepare documentation sufficient to enable an understanding of significant matters arising during the audit, the conclusions reached, and significant professional judgments made in reaching those conclusions;

- Document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place; and
- Document identified or suspected non-compliance, and the results of discussion with management and, where applicable, those charged with governance and other parties outside the entity.

### **Professional Services Other than Audits of Financial Statements**

#### ***Obtaining an Understanding of the Matter and Addressing It with Management and Those Charged with Governance***

- 225.39 If a professional accountant engaged to provide a professional service other than an audit of financial statements becomes aware of information concerning an instance of non-compliance or suspected non-compliance, the professional accountant shall seek to obtain an understanding of the matter, including the nature of the act and the circumstances in which it has occurred or may be about to occur.
- 225.40 The professional accountant is expected to apply knowledge, professional judgment and expertise, but is not expected to have a level of understanding of laws and regulations beyond that which is required for the professional service for which the accountant was engaged. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. Depending on the nature and significance of the matter, the professional accountant may consult on a confidential basis with others within the firm, a network firm or a professional body, or with legal counsel.
- 225.41 If the professional accountant identifies or suspects that non-compliance has occurred or may occur, the professional accountant shall discuss the matter with the appropriate level of management and, if the professional accountant has access to them and where appropriate, those charged with governance.
- 225.42 Such discussion serves to clarify the professional accountant's understanding of the facts and circumstances relevant to the matter and its potential consequences. The discussion also may prompt management or those charged with governance to investigate the matter.
- 225.43 The appropriate level of management with whom to discuss the matter is a question of professional judgment. Relevant factors to consider include:
- The nature and circumstances of the matter.
  - The individuals actually or potentially involved.
  - The likelihood of collusion.
  - The potential consequences of the matter.
  - Whether that level of management is able to investigate the matter and take appropriate action.

#### ***Communicating the Matter to the Entity's External Auditor***

- 225.44 If the professional accountant is performing a non-audit service for an audit client of the firm, or a component of an audit client of the firm, the professional accountant shall communicate the non-compliance or suspected non-compliance within the firm, unless prohibited from doing so by law or regulation. The communication shall be made in accordance with the firm's protocols or procedures or, in the absence of such protocols and procedures, directly to the audit engagement partner.
- 225.45 If the professional accountant is performing a non-audit service for an audit client of a network firm, or a component of an audit client of a network firm, the professional accountant shall consider whether to communicate the non-compliance or suspected non-compliance to the network firm. Where the communication is made, it shall be made in

accordance with the network's protocols or procedures or, in the absence of such protocols and procedures, directly to the audit engagement partner.

225.46 If the professional accountant is performing a non-audit service for a client that is not:

- (a) An audit client of the firm or a network firm; or
- (b) A component of an audit client of the firm or a network firm,

the professional accountant shall consider whether to communicate the non-compliance or suspected non-compliance to the firm that is the client's external auditor, if any.

225.47 Factors relevant to considering the communication in accordance with paragraphs 225.45 and 225.46 include:

- Whether doing so would be contrary to law or regulation.
- Whether there are restrictions about disclosure imposed by a regulatory agency or prosecutor in an ongoing investigation into the non-compliance or suspected non-compliance.
- Whether the purpose of the engagement is to investigate potential non-compliance within the entity to enable it to take appropriate action.
- Whether management or those charged with governance have already informed the entity's external auditor about the matter.
- The likely materiality of the matter to the audit of the client's financial statements or, where the matter relates to a component of a group, its likely materiality to the audit of the group financial statements.

225.48 In all cases, the communication is to enable the audit engagement partner to be informed about the non-compliance or suspected non-compliance and to determine whether and, if so, how it should be addressed in accordance with the provisions of this section.

### *Considering Whether Further Action Is Needed*

225.49 The professional accountant shall also consider whether further action is needed in the public interest.

225.50 Whether further action is needed, and the nature and extent of it, will depend on factors such as:

- The legal and regulatory framework.
- The appropriateness and timeliness of the response of management and, where applicable, those charged with governance.
- The urgency of the matter.
- The involvement of management or those charged with governance in the matter.
- The likelihood of substantial harm to the interests of the client, investors, creditors, employees or the general public.

225.51 Further action by the professional accountant may include:

- Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
- Withdrawing from the engagement and the professional relationship where permitted by law or regulation.

225.52 In considering whether to disclose to an appropriate authority, relevant factors to take into account include:

- Whether doing so would be contrary to law or regulation.



- Whether there are restrictions about disclosure imposed by a regulatory agency or prosecutor in an ongoing investigation into the non-compliance or suspected non-compliance.
  - Whether the purpose of the engagement is to investigate potential non-compliance within the entity to enable it to take appropriate action.
- 225.53 If the professional accountant determines that disclosure of the non-compliance or suspected non-compliance to an appropriate authority is an appropriate course of action in the circumstances, this will not be considered a breach of the duty of confidentiality under Section 140 of this Code. When making such disclosure, the professional accountant shall act in good faith and exercise caution when making statements and assertions. The professional accountant shall also consider whether it is appropriate to inform the client of the professional accountant's intentions before disclosing the matter.
- 225.54 In exceptional circumstances, the professional accountant may become aware of actual or intended conduct that the professional accountant has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. Having considered whether it would be appropriate to discuss the matter with management or those charged with governance of the entity, the professional accountant shall exercise professional judgment and may immediately disclose the matter to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach of law or regulation. Such disclosure will not be considered a breach of the duty of confidentiality under Section 140 of this Code.
- 225.55 The professional accountant may consider consulting internally, obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or professional body.

### *Documentation*

- 225.56 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the professional accountant is encouraged to document:
- The matter.
  - The results of discussion with management and, where applicable, those charged with governance and other parties.
  - How management and, where applicable, those charged with governance have responded to the matter.
  - The courses of action the professional accountant considered, the judgments made and the decisions that were taken.
  - How the professional accountant is satisfied that the professional accountant has fulfilled the responsibility set out in paragraph 225.49.

## SECTION 360

### Responding to Non-Compliance with Laws and Regulations

#### Purpose

- 360.1 A professional accountant in business may encounter or be made aware of non-compliance or suspected non-compliance with laws and regulations in the course of carrying out professional activities. The purpose of this section is to set out the professional accountant's responsibilities when encountering such non-compliance or suspected non-compliance, and guide the professional accountant in assessing the implications of the matter and the possible courses of action when responding to it. This section applies regardless of the nature of the employing organization, including whether or not it is a public interest entity.
- 360.2 Non-compliance with laws and regulations ("non-compliance") comprises acts of omission or commission, intentional or unintentional, committed by the professional accountant's employing organization or by those charged with governance, by management, or by other individuals working for or under the direction of the employing organization which are contrary to the prevailing laws or regulations.
- 360.3 In some jurisdictions, there are legal or regulatory provisions governing how professional accountants should address non-compliance or suspected non-compliance which may differ from or go beyond this section. When encountering such non-compliance or suspected non-compliance, the professional accountant has a responsibility to obtain an understanding of those provisions and comply with them, including any requirement to report the matter to an appropriate authority and any prohibition on alerting the relevant party prior to making any disclosure, for example, pursuant to anti-money laundering legislation.
- 360.4 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. When responding to non-compliance or suspected non-compliance, the objectives of the professional accountant are:
- (a) To comply with the fundamental principles of integrity and professional behavior;
  - (b) By alerting management or, where appropriate, those charged with governance of the employing organization, to seek to:
    - (i) Enable them to rectify, remediate or mitigate the consequences of the identified or suspected non-compliance; or
    - (ii) Deter the commission of the non-compliance where it has not yet occurred; and
  - (c) To take such further action as appropriate in the public interest.

#### Scope

- 360.5 This section sets out the approach to be taken by a professional accountant who encounters or is made aware of non-compliance or suspected non-compliance with:
- (a) Laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the employing organization's financial statements; and
  - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the employing organization's financial statements, but compliance with which may be fundamental to the operating aspects of the employing organization's business, to its ability to continue its business, or to avoid material penalties.

- 360.6 Examples of laws and regulations which this section addresses include those that deal with:
- Fraud, corruption and bribery.
  - Money laundering, terrorist financing and proceeds of crime.
  - Securities markets and trading.
  - Banking and other financial products and services.
  - Data protection.
  - Tax and pension liabilities and payments.
  - Environmental protection.
  - Public health and safety.
- 360.7 Non-compliance may result in fines, litigation or other consequences for the employing organization that may have a material effect on its financial statements. Importantly, such non-compliance may have wider public interest implications in terms of potentially substantial harm to investors, creditors, employees or the general public. For the purposes of this section, an act that causes substantial harm is one that results in serious adverse consequences to any of these parties in financial or non-financial terms. Examples include the perpetration of a fraud resulting in significant financial losses to investors, and breaches of environmental laws and regulations endangering the health or safety of employees or the public.
- 360.8 A professional accountant who encounters or is made aware of matters that are clearly inconsequential, judged by their nature and their impact, financial or otherwise, on the employing organization, its stakeholders and the general public, is not required to comply with this section with respect to such matters.
- 360.9 This section does not address:
- (a) Personal misconduct unrelated to the business activities of the employing organization; and
  - (b) Non-compliance other than by the employing organization or those charged with governance, management, or other individuals working for or under the direction of the employing organization.

The professional accountant may nevertheless find the guidance in this section helpful in considering how to respond in these situations.

### **Responsibilities of the Employing Organization’s Management and Those Charged with Governance**

- 360.10 It is the responsibility of the employing organization’s management, with the oversight of those charged with governance, to ensure that the employing organization’s business activities are conducted in accordance with laws and regulations. It is also the responsibility of management and those charged with governance to identify and address any non-compliance by the employing organization or by an individual charged with governance of the entity, by a member of management, or by other individuals working for or under the direction of the employing organization.

### **Responsibilities of Professional Accountants in Business**

- 360.11 Many employing organizations have established protocols and procedures (for example, an ethics policy or internal whistle-blowing mechanism) regarding how non-compliance or suspected non-compliance by the employing organization should be raised internally. Such protocols and procedures may allow for matters to be reported anonymously through designated channels. If these protocols and procedures exist within the professional

accountant's employing organization, the professional accountant shall consider them in determining how to respond to such non-compliance.

- 360.12 Where a professional accountant becomes aware of a matter to which this section applies, the steps that the professional accountant takes to comply with this section shall be taken on a timely basis, having regard to the professional accountant's understanding of the nature of the matter and the potential harm to the interests of the employing organization, investors, creditors, employees or the general public.

### Responsibilities of Senior Professional Accountants in Business

- 360.13 Senior professional accountants in business ("senior professional accountants") are directors, officers or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organization's human, financial, technological, physical and intangible resources. Because of their roles, positions and spheres of influence within the employing organization, there is a greater expectation for them to take whatever action is appropriate in the public interest to respond to non-compliance or suspected non-compliance than other professional accountants within the employing organization.

#### *Obtaining an Understanding of the Matter*

- 360.14 If, in the course of carrying out professional activities, a senior professional accountant becomes aware of information concerning an instance of non-compliance or suspected non-compliance, the professional accountant shall obtain an understanding of the matter, including:
- (a) The nature of the act and the circumstances in which it has occurred or may occur;
  - (b) The application of the relevant laws and regulations to the circumstances; and
  - (c) The potential consequences to the employing organization, investors, creditors, employees or the wider public.
- 360.15 A senior professional accountant is expected to apply knowledge, professional judgment and expertise, but is not expected to have a level of understanding of laws and regulations beyond that which is required for the professional accountant's role within the employing organization. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. Depending on the nature and significance of the matter, the professional accountant may cause, or take appropriate steps to cause, the matter to be investigated internally. The professional accountant may also consult on a confidential basis with others within the employing organization or a professional body, or with legal counsel.

#### *Addressing the Matter*

- 360.16 If the senior professional accountant identifies or suspects that non-compliance has occurred or may occur, the professional accountant shall, subject to paragraph 360.11, discuss the matter with the professional accountant's immediate superior, if any, to enable a determination to be made as to how the matter should be addressed. If the professional accountant's immediate superior appears to be involved in the matter, the professional accountant shall discuss the matter with the next higher level of authority within the employing organization.
- 360.17 The senior professional accountant shall also take appropriate steps to:
- (a) Have the matter communicated to those charged with governance to obtain their concurrence regarding appropriate actions to take to respond to the matter and to enable them to fulfill their responsibilities;
  - (b) Comply with applicable laws and regulations, including legal or regulatory provisions governing the reporting of non-compliance or suspected non-compliance to an appropriate authority;

- (c) Have the consequences of the non-compliance or suspected non-compliance rectified, remediated or mitigated;
- (d) Reduce the risk of re-occurrence; and
- (e) Seek to deter the commission of the non-compliance if it has not yet occurred.

360.18 In addition to responding to the matter in accordance with the provisions of this section, the senior professional accountant shall determine whether disclosure of the matter to the employing organization's external auditor, if any, is needed pursuant to the professional accountant's duty or legal obligation to provide all information necessary to enable the auditor to perform the audit.

*Determining Whether Further Action Is Needed*

360.19 The senior professional accountant shall assess the appropriateness of the response of the professional accountant's superiors, if any, and those charged with governance.

360.20 Relevant factors to consider in assessing the appropriateness of the response of the senior professional accountant's superiors, if any, and those charged with governance include whether:

- The response is timely.
- They have taken or authorized appropriate action to seek to rectify, remediate or mitigate the consequences of the non-compliance, or to avert the non-compliance if it has not yet occurred.
- The matter has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.

360.21 In light of the response of the senior professional accountant's superiors, if any, and those charged with governance, the professional accountant shall determine if further action is needed in the public interest.

360.22 The determination of whether further action is needed, and the nature and extent of it, will depend on various factors, including:

- The legal and regulatory framework.
- The urgency of the matter.
- The pervasiveness of the matter throughout the employing organization.
- Whether the senior professional accountant continues to have confidence in the integrity of the professional accountant's superiors and those charged with governance.
- Whether the non-compliance or suspected non-compliance is likely to recur.
- Whether there is credible evidence of actual or potential substantial harm to the interests of the employing organization, investors, creditors, employees or the general public.

360.23 Examples of circumstances that may cause the senior professional accountant no longer to have confidence in the integrity of the professional accountant's superiors and those charged with governance include situations where:

- The professional accountant suspects or has evidence of their involvement or intended involvement in any non-compliance.
- Contrary to legal or regulatory requirements, they have not reported the matter, or authorized the matter to be reported, to an appropriate authority within a reasonable period.

360.24 In determining the need for, and nature and extent of any further action needed, the senior professional accountant shall exercise professional judgment and take into account whether

a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at the time, would be likely to conclude that the professional accountant has acted appropriately in the public interest.

- 360.25 Further action by the professional accountant may include:
- Informing the management of the parent entity of the matter if the employing organization is a member of a group.
  - Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
  - Resigning from the employing organization.
- 360.26 Where the senior professional accountant determines that resigning from the employing organization would be appropriate, doing so would not be a substitute for taking other actions that may be needed to achieve the professional accountant's objectives under this section. In some jurisdictions, however, there may be limitations as to the further actions available to the professional accountant and resignation may be the only available course of action.
- 360.27 As consideration of the matter may involve complex analysis and judgments, the senior professional accountant may consider consulting internally, obtaining legal advice to understand the professional accountant's options and the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or professional body.

### Determining Whether to Disclose the Matter to an Appropriate Authority

- 360.28 Disclosure of the matter to an appropriate authority would be precluded if doing so would be contrary to law or regulation. Otherwise, the purpose of making disclosure is to enable an appropriate authority to cause the matter to be investigated and action to be taken in the public interest.
- 360.29 The determination of whether to make such a disclosure depends in particular on the nature and extent of the actual or potential harm that is or may be caused by the matter to investors, creditors, employees or the general public. For example, the senior professional accountant may determine that disclosure of the matter to an appropriate authority is an appropriate course of action if:
- The employing organization is engaged in bribery (for example, of local or foreign government officials for purposes of securing large contracts).
  - The employing organization is a regulated entity and the matter is of such significance as to threaten its license to operate.
  - The employing organization is listed on a securities exchange and the matter could result in adverse consequences to the fair and orderly market in the employing organization's securities or pose a systemic risk to the financial markets.
  - Products that are harmful to public health or safety would likely be sold by the employing organization.
  - The employing organization is promoting a scheme to its clients to assist them in evading taxes.

The determination of whether to make such a disclosure will also depend on external factors such as:

- Whether there is an appropriate authority that is able to receive the information, and cause the matter to be investigated and action to be taken. The appropriate authority will depend upon the nature of the matter, for example, a securities regulator in the case of fraudulent financial reporting or an environmental protection agency in the case of a breach of environmental laws and regulations.

- Whether there exists robust and credible protection from civil, criminal or professional liability or retaliation afforded by legislation or regulation, such as under whistle-blowing legislation or regulation.
  - Whether there are actual or potential threats to the physical safety of the professional accountant or other individuals.
- 360.30 If the senior professional accountant determines that disclosure of the matter to an appropriate authority is an appropriate course of action in the circumstances, this will not be considered a breach of the duty of confidentiality under Section 140 of this Code. When making such disclosure, the professional accountant shall act in good faith and exercise caution when making statements and assertions.
- 360.31 In exceptional circumstances, the senior professional accountant may become aware of actual or intended conduct that the professional accountant has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. Having considered whether it would be appropriate to discuss the matter with management or those charged with governance of the entity, the professional accountant shall exercise professional judgment and may immediately disclose the matter to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach of law or regulation. Such disclosure will not be considered a breach of the duty of confidentiality under Section 140 of this Code.

### *Documentation*

- 360.32 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the senior professional accountant is encouraged to have the following matters documented:
- The matter.
  - The results of discussions with the professional accountant's superiors, if any, and those charged with governance and other parties.
  - How the professional accountant's superiors, if any, and those charged with governance have responded to the matter.
  - The courses of action the professional accountant considered, the judgments made and the decisions that were taken.
  - How the professional accountant is satisfied that the professional accountant has fulfilled the responsibility set out in paragraph 360.21.

### **Responsibilities of Professional Accountants Other than Senior Professional Accountants in Business**

- 360.33 If, in the course of carrying out professional activities, a professional accountant becomes aware of information concerning an instance of non-compliance or suspected non-compliance, the professional accountant shall seek to obtain an understanding of the matter, including the nature of the act and the circumstances in which it has occurred or may occur.
- 360.34 The professional accountant is expected to apply knowledge, professional judgment and expertise, but is not expected to have a level of understanding of laws and regulations beyond that which is required for the professional accountant's role within the employing organization. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. Depending on the nature and significance of the matter, the professional accountant may consult on a confidential basis with others within the employing organization or a professional body, or with legal counsel.
- 360.35 If the professional accountant identifies or suspects that non-compliance has occurred or may occur, the professional accountant shall, subject to paragraph 360.11, inform an immediate superior to enable the superior to take appropriate action. If the professional

accountant's immediate superior appears to be involved in the matter, the professional accountant shall inform the next higher level of authority within the employing organization.

- 360.36 In exceptional circumstances, the professional accountant may decide that disclosure of the matter to an appropriate authority is an appropriate course of action. If the professional accountant does so pursuant to paragraph 360.29, this will not be considered a breach of the duty of confidentiality under Section 140 of this Code. When making such disclosure, the professional accountant shall act in good faith and exercise caution when making statements and assertions.

### *Documentation*

360.37 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the professional accountant is encouraged to have the following matters documented:

- The matter.
- The results of discussions with the professional accountant's superior, management and, where applicable, those charged with governance and other parties.
- How the professional accountant's superior has responded to the matter.
- The courses of action the professional accountant considered, the judgments made and the decisions that were taken.

Consequential and conforming changes to other sections of the Code are set out below.

## **SECTION 100**

### **Introduction and Fundamental Principles**

...

#### *Fundamental Principles*

*[Bullet point (e) in extant paragraph 100.5 will be replaced by bullet point (e) below.]*

...

- (e) Professional Behavior – to comply with relevant laws and regulations and avoid any conduct that discredits the profession.

...

#### *Conflicts of Interest*

...

#### **Ethical Conflict Resolution**

...

*[Extant paragraph 100.23 and 100.24 will be replaced by paragraphs 100.23 and 100.24 below.]*

100.23 If a significant conflict cannot be resolved, a professional accountant may consider obtaining professional advice from the relevant professional body or from legal advisors. The professional accountant generally can obtain guidance on ethical issues without breaching the fundamental principle of confidentiality if the matter is discussed with the relevant professional body on an anonymous basis or with a legal advisor under the protection of legal privilege.

100.24 If, after exhausting all relevant possibilities, the ethical conflict remains unresolved, a professional accountant shall, unless prohibited by law, refuse to remain associated with



the matter creating the conflict. The professional accountant shall determine whether, in the circumstances, it is appropriate to withdraw from the engagement team or specific assignment, or to resign altogether from the engagement, the firm or the employing organization.

*[Paragraph 100.26 below will be added after extant paragraph 100.25.]*

100.26 In some cases, all of those charged with governance are involved in managing the entity, for example, a small business where a single owner manages the entity and no one else has a governance role. In these cases, if matters are communicated with person(s) with management responsibilities, and those person(s) also have governance responsibilities, the matters need not be communicated again with those same person(s) in their governance role. The professional accountant or firm shall nonetheless be satisfied that communication with person(s) with management responsibilities adequately informs all of those with whom the professional accountant or firm would otherwise communicate in their governance capacity.

## SECTION 140

### Confidentiality

*[Extant paragraph 140.7 will be replaced by paragraph 140.7 below.]*

140.7 As a fundamental principle, confidentiality serves the public interest because it facilitates the free flow of information from the professional accountant's client or employing organization to the professional accountant. Nevertheless, the following are circumstances where professional accountants are or may be required to disclose confidential information or when such disclosure may be appropriate:

- (a) Disclosure is permitted by law and is authorized by the client or the employer;
- (b) Disclosure is required by law, for example:
  - (i) Production of documents or other provision of evidence in the course of legal proceedings; or
  - (ii) Disclosure to the appropriate public authorities of infringements of the law that come to light; and
- (c) There is a professional duty or right to disclose, when not prohibited by law:
  - (i) To comply with the quality review of a member body or professional body;
  - (ii) To respond to an inquiry or investigation by a member body or regulatory body;
  - (iii) To protect the professional interests of a professional accountant in legal proceedings; or
  - (iv) To comply with technical and professional standards, including ethical requirements.

**SECTION 150****Professional Behavior**

*[Extant paragraph 150.1 will be replaced by paragraph 150.1 below.]*

- 150.1 The principle of professional behavior imposes an obligation on all professional accountants to comply with relevant laws and regulations and avoid any conduct that the professional accountant knows or should know may discredit the profession. This includes conduct that a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at that time, would be likely to conclude adversely affects the good reputation of the profession.

**SECTION 210****Professional Appointment**

*[Paragraphs 210.1 to 210.4 together with the heading below will replace extant paragraphs 210.1 to 210.5 and the heading above extant paragraph 210.1.]*

*Client Acceptance and Continuance*

- 210.1 Before accepting a new client relationship, a professional accountant in public practice shall determine whether acceptance would create any threats to compliance with the fundamental principles. Potential threats to integrity or professional behavior may be created from, for example, issues associated with the client (its owners, management or activities) that, if known, could threaten compliance with the fundamental principles. These include, for example, client involvement in illegal activities (such as money laundering), dishonesty, questionable financial reporting practices or other unethical behavior.
- 210.2 A professional accountant in public practice shall evaluate the significance of any threats and apply safeguards when necessary to eliminate them or reduce them to an acceptable level.
- Examples of such safeguards include:
- Obtaining knowledge and understanding of the client, its owners, managers and those responsible for its governance and business activities; or
  - Securing the client's commitment to address the questionable issues, for example, through improving corporate governance practices or internal controls.
- 210.3 Where it is not possible to reduce the threats to an acceptable level, the professional accountant in public practice shall decline to enter into the client relationship.
- 210.4 Potential threats to compliance with the fundamental principles may have been created after acceptance that would have caused the professional accountant to decline the engagement had that information been available earlier. A professional accountant in public practice shall, therefore, periodically review whether to continue with a recurring client engagement. For example, a threat to compliance with the fundamental principles may be created by a client's unethical behavior such as improper earnings management or balance sheet valuations. If a professional accountant in public practice identifies a threat to compliance with the fundamental principles, the professional accountant shall evaluate the significance of the threats and apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level. Where it is not possible to reduce the threat to an acceptable level, the professional accountant in public practice shall consider terminating the client relationship where termination is not prohibited by law or regulation.

*[Extant paragraphs 210.6 to 210.9 will be renumbered paragraphs 210.5 to 210.8 respectively.]*

*[Extant paragraphs 210.10 and 210.11 will be replaced by paragraph 210.9 below.]*

210.9 A professional accountant in public practice shall evaluate the significance of any threats. Safeguards shall be applied when necessary to eliminate any threats or reduce them to an acceptable level. Examples of such safeguards include:

- When replying to requests to submit tenders, stating in the tender that, before accepting the engagement, contact with the existing or predecessor accountant will be requested so that inquiries may be made as to whether there are any professional or other reasons why the appointment should not be accepted;
- Asking the predecessor accountant to provide known information on any facts or circumstances that, in the predecessor accountant's opinion, the proposed successor accountant needs to be aware of before deciding whether to accept the engagement. For example, the apparent reasons for the change in appointment may not fully reflect the facts and may indicate disagreements with the predecessor accountant that may influence the decision to accept the appointment; or
- Obtaining necessary information from other sources.

*[Extant paragraph 210.12 will be renumbered paragraph 210.11.]*

*[Extant paragraphs 210.13 and 210.14 will be replaced by paragraphs 210.12 and 210.13 below.]*

210.12 An existing or predecessor accountant is bound by confidentiality. Whether that professional accountant is permitted or required to discuss the affairs of a client with a proposed accountant will depend on the nature of the engagement and on:

- (a) Whether the client's permission to do so has been obtained; or
- (b) The legal or ethical requirements relating to such communications and disclosure, which may vary by jurisdiction.

Circumstances where the professional accountant is or may be required to disclose confidential information or where such disclosure may otherwise be appropriate are set out in Section 140 of Part A of this Code.

210.13 A professional accountant in public practice will generally need to obtain the client's permission, preferably in writing, to initiate discussion with an existing or predecessor accountant. Once that permission is obtained, the existing or predecessor accountant shall comply with relevant laws and regulations governing such requests. Where the existing or predecessor accountant provides information, it shall be provided honestly and unambiguously. If the proposed accountant is unable to communicate with the existing or predecessor accountant, the proposed accountant shall take reasonable steps to obtain information about any possible threats by other means, such as through inquiries of third parties or background investigations of senior management or those charged with governance of the client.

*[Paragraph 210.14 below will be added after paragraph 210.13.]*

210.14 In the case of an audit of financial statements, a professional accountant shall request the predecessor accountant to provide known information regarding any facts or other information that, in the predecessor accountant's opinion, the proposed successor accountant needs to be aware of before deciding whether to accept the engagement. Except for the circumstances involving identified or suspected non-compliance with laws and regulations set out in paragraph 225.31:

- (a) If the client consents to the predecessor accountant disclosing any such facts or other information, the predecessor accountant shall provide the information honestly and unambiguously; and
- (b) If the client fails or refuses to grant the predecessor accountant permission to discuss the client's affairs with the proposed successor accountant, the predecessor accountant shall disclose this fact to the proposed successor accountant, who shall

carefully consider such failure or refusal when determining whether or not to accept the appointment.

## **SECTION 270**

### **Custody of Client Assets**

...

*[Extant paragraph 270.3 will be replaced by paragraph 270.3 below.]*

270.3 As part of client and engagement acceptance procedures for services that may involve the holding of client assets, a professional accountant in public practice shall make appropriate inquiries about the source of such assets and consider legal and regulatory obligations. For example, if the assets were derived from illegal activities, such as money laundering, a threat to compliance with the fundamental principles would be created. In such situations, the professional accountant shall comply with the provisions of section 225.

## **SECTION 410**

### **Unlawful Acts or Defaults by Clients of Members**

*[The extant first and second introduction paragraphs will be replaced by the paragraphs below.]*

*This section should be read in conjunction with Section 140 "Confidentiality" and Section 225 "Responding to Non-Compliance with Laws and Regulations".*

Occasions sometimes arise where a member, in carrying out his professional duties, acquires knowledge indicating that a client or an officer or employee of the client may have been guilty of some default or unlawful act. This may put him in a difficult situation of conflicting duties, aggravated sometimes by allegations that he himself is implicated in some way in those unlawful acts, or has some legal responsibility arising from those acts. Section 225 of the Code sets out the response framework for members in practice when members encounter or are made aware of suspected or actual non-compliance with laws and regulations in the course of providing professional services to clients. This section gives additional guidance to members concerning certain areas of difficulty, which involve both professional conduct and legal considerations. However, it is for general guidance only and in any particular case reference should also be made to any relevant legislation. Although various examples are given of the duties of members, they are examples only.

...

### **General Principles**

#### *Introduction*

...

*[Extant paragraphs 410.2 and 410.3 will be replaced by paragraphs 410.2 and 410.3 below.]*

410.2 Section 225 of the Code sets out the response framework for members in practice to respond to suspected or actual non-compliance with laws and regulations committed by clients that have a direct effect on the client's financial statements or the operation of the client's business. This section provides additional local guidance to assist members in responding to situations when, in one way or another, their clients or officers or employees of their clients come under suspicion by the authorities (whether justified or not) of having committed some criminal offences, or members themselves have information that their clients have in one way or another become so implicated. The guidance given in the Guidelines is not intended to be exhaustive. There will arise from time to time situations of

conflicting duties not covered by these Guidelines. Members should therefore use their own judgement in all cases and would be well advised to seek legal or other professional advice if in doubt.

- 410.3 A practising member, acting in any professional capacity, has access to much information of a private nature. It is essential that he should normally treat such information as available to him for the purpose only of carrying out the professional duties for which he has been engaged. To divulge information about a client's affairs would normally be a breach of professional confidence unless the response framework set out in section 225 of the Code prescribes otherwise. Accordingly, the duty of confidentiality is not absolute. Where, for example, members acquire information in the course of an audit showing that actual or suspected defaults and unlawful acts have taken place, members may be duty-bound to make such disclosures and statements in their reports as would ensure that their functions and duties as auditors are properly discharged. Likewise members may have duties to make reports as auditors under the Banking Ordinance 1986 or to make disclosures to the relevant authorities under the Drug Trafficking (Recovery of Proceeds) Ordinance both of which require the disclosure of confidential information. Even if there is no law or regulation that requires members to disclose the defaults and unlawful acts, members should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

### Disclosure of Information by His Client to a Member

...

*[Extant paragraphs 410.8 and 410.10 will be replaced by paragraphs 410.8 and 410.10 below.]*

- 410.8 It is an implied term of a member's contract with his client that the member will not, as a general rule, disclose to other persons information about his client's affairs acquired during and as a result of their professional relationship, against his client's wishes.
- 410.10 However, the confidentiality is by no means absolute. There will be circumstances where a member is *required by law or statute* to disclose to others knowledge of defaults or criminal acts acquired in the course of such confidential relationship. Even if there is no law or regulation that requires the member to disclose suspected or actual non-compliance matters, members should follow the response framework set out in section 225 of the Code to respond to such non-compliance situations and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

### Obligation to Disclose

...

*[Extant paragraphs 410.13 and 410.14 will be replaced by paragraphs 410.13 and 410.14 below.]*

- 410.13 Where a member is approached by the police, the Inland Revenue Department, the Independent Commission Against Corruption ('ICAC') or other authority in the course of making enquiries concerning the affairs of a client or former client, the member should act with caution. He should first ascertain whether or not the person requesting information has a statutory right to demand it. Generally speaking, a member will not be acting contrary to law if he refuses to impart information to persons who have no statutory right to demand it; on the other hand, he might well be acting in breach of his duty of confidence to his client if he volunteers the information. It is advisable for members to seek legal advice to clarify the legal aspects of their positions if in doubt. Nevertheless, if a member has encountered or is aware of any suspected or actual non-compliance with laws and regulations in the course of providing professional services to his client that is related to the enquiry made by the authority, he should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

- 410.14 If a notice is served on a client requiring production of documents which are in the possession of the member but are the property of the client the member should read the notice carefully to see if he is under compulsion of law to produce the documents. If he is, then the question of the client's permission is not relevant and the member must comply with the notice. If there is doubt in the matter - where, for example, the notice does not sufficiently identify the documents or class of documents to be produced - then the member should not produce the document unconditionally. One way of resolving a dispute of this nature is to have the documents put separately and sealed, pending the taking of legal advice.

*[Paragraph 410.17 together with the heading below will replace the extant paragraph 410.17 and the heading above the extant paragraph 410.17.]*

#### Disclosure for the Protection of the Member's Own Interest

- 410.17 [Not used]

...

#### Past accounts later found to be defective

...

*[Extant paragraph 410.31 will be replaced by paragraph 410.31 below.]*

- 410.31 If the client refuses to act in accordance with the member's advice to make an immediate disclosure, the member should inform his client that he can no longer act for him in tax matters and that it will be necessary for the member to inform the Inland Revenue Department that, since he prepared or reported upon the accounts concerned or the returns or computations based thereon, he has acquired information which indicates that those accounts or documents cannot be relied upon and that he has ceased to act for the client in tax matters. The member should then so inform the Inland Revenue Department. Under sections 51(4) and 51B of the Inland Revenue Ordinance, the Inland Revenue Department may require members to furnish relevant information as may be required, and may obtain search warrants for the purpose of obtaining such information. Should such action be taken by the Inland Revenue Department, the member would be under no obligation to obtain the client's consent before releasing such information. Even if the Inland Revenue Department does not invoke section 51(4) and 51B of the Inland Revenue Ordinance, members should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

#### Accounts currently being prepared or audited

...

*[Extant paragraphs 410.33 and 410.34 will be replaced by paragraphs 410.33 and 410.34 below.]*

- 410.33 If the client dispenses with the member's services or if the member resigns before he has completed his work and reported on the accounts, there is no further legal duty rests on the member towards the Inland Revenue Department unless the Inland Revenue Department invokes section 51(4) or 51B of the Inland Revenue Ordinance. However, members are reminded that under section 225.30 of the Code, withdrawing from an engagement or a professional relationship in response to non-compliance with laws and regulations would not discharge the members' professional duty under the Code as withdrawing from an engagement or a professional relationship is not a substitute for taking other appropriate actions, e.g. disclosing the matter to an appropriate authority.
- 410.34 Where, however, the member's services are not dispensed with, his position in relation to the Inland Revenue Department after he has completed his professional duties as accountant or auditor is as follows:

- (a) the member should not without the client's authority send the accounts to the Inland Revenue Department (see paragraph 410.28).
- (b) if the member is not requested to undertake the taxation work (that is to say, to act on the client's behalf in dealing with the Inland Revenue Department) he has no responsibility towards the Inland Revenue Department. In the event of his receiving any enquiry from the Inland Revenue Department he should normally do no more than state that he is not dealing with taxation matters and that all enquiries should be addressed to the client. If the enquiry indicates that accounts bearing the member's name have been submitted he should normally state that he cannot add to his report thereon. The position is the same whether or not the member has acted for the client in taxation matters in previous years.
- (c) on the other hand, if the client requests the member to undertake the taxation work he should always make it clear to the client that he can do so only on the basis of full disclosure of all relevant information. If the client will not agree, the member should state that he cannot act for him in taxation matters and in that case the position regarding any enquiries the member may receive from the Inland Revenue Department is the same as in b above.

In any cases, the Inland Revenue Department may invoke section 51(4) or 51B of the Inland Revenue Ordinance to obtain relevant information from members. Members also have a professional duty to follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

...

### Taxation Frauds and Negligence not Involving Accounts

*[Extant paragraph 410.37 will be replaced by paragraph 410.37 below.]*

410.37 Paragraphs 410.28 to 410.36 above relate to taxation frauds and negligence through the medium of defective accounts. A member may, however, acquire knowledge indicating that a client has been guilty of taxation frauds or negligence by means which do not affect the client's accounts, for example, the submission of incorrect returns of private income. The member should advise his client to make a complete disclosure to the Inland Revenue Department. If the client refuses to do so, the member's position will depend upon whether or not the matter is within the scope of the duties he has undertaken for the client:

- (a) if it relates to taxation matters on which the member has not acted for the client (for example, omission of private income where the member has dealt only with the tax computations of business profits and not with the client's tax returns), the member has no legal duty to make any disclosure to the Inland Revenue Department. He could lawfully continue to act for the client as hitherto. He may prefer to terminate the association.
- (b) if it relates to taxation matters on which the member has acted for the client, then the member should inform the client that he can no longer act for him and that it will be necessary for the member to inform the Inland Revenue Department that he must dissociate himself from the returns (or other information involved) for the years in question and that he has ceased to act for the client on taxation matters. The member should then so inform the Inland Revenue Department.

In the case of either a or b above, the Inland Revenue Department may invoke section 51(4) or 51B of the Inland Revenue Ordinance to obtain further details as may be relevant. Members also have the professional duty to follow the response framework in section 225 of the Code and determine whether further action is needed, which may include disclosing such taxation frauds and negligence to an appropriate authority.

## General Professional Duty to Give Guidance

*[Extant paragraphs 410.38 and 410.41 will be replaced by paragraphs 410.38 and 410.41 below.]*

- 410.38 A member should regard himself as having a professional obligation to urge upon a client, in the client's own interests, the importance of making a full disclosure and authorising the member to proceed, where necessary, with "back duty" negotiations.
- 410.41 All these are matters which the member should regard as his professional duty to impress upon the client. If nevertheless his advice is not accepted, it is important that the member's subsequent conduct should, from both the legal and professional standpoints, be correct.

## Statutory Provisions Relating to Disclosure of Information

...

*[Extant paragraph 410.44 will be replaced by paragraph 410.44 below.]*

- 410.44 As indicated in paragraphs 410.31 and 410.37b above, a member should inform the Inland Revenue Department when he subsequently learns that accounts prepared by him, or returns or computations based thereon, are defective and cannot be relied upon, and where such is the fact, that he has ceased to act for the client in taxation matters. Where a member has taken over the practice of another accountant, he may receive a request from the Inland Revenue Department for his co-operation by way of providing information relating to his clients, the object being to enable the Department to make a general review to decide whether there are any clients whose affairs appear to need further investigation. The member should not normally disclose information without client's consent unless he is compelled by law or he determines that such disclosure is needed in the public interest according to section 225 of the Code.

...

## Members' Working Papers

...

*[Extant paragraphs 410.47 to 410.49 will be replaced by paragraphs 410.47 to 410.49 below.]*

- 410.47 The Council wishes to emphasise that it is entirely for the member to decide whether to make his working papers available to the Inland Revenue Department. He should not normally do so without the consent of his client unless such disclosure is required by law or regulation or when the member determines that it is needed in the public interest in accordance with section 225 of the Code. The following paragraphs provide guidance about disclosure of the working papers listed in paragraph 410.46:
- (a) with regard to the analyses, schedules and correspondence referred to in paragraph 410.46 (a), (b) and (c), the Council would see no objection to the production of relevant working papers to the Inland Revenue Department in appropriate cases if they are likely to be significant as factual evidence supporting the accountant's report and the statements submitted therewith;
  - (b) the correspondence and notes referred to in paragraph 410.46 (d) and (e) may well be of a highly confidential nature. Members should normally not produce such working papers to the Inland Revenue Department without client's consent unless it is required by law or regulation or when members determines that it is needed in the public interest in accordance with section 225 of the Code. Members are advised to seek legal advice if in doubt as to his rights and duty to disclose.



### *Other Taxes and Duties*

- 410.48 Taxes and duties other than property, salaries, profits and interest taxes with which members or their clients may be concerned include at the date of publication of this section:
- (a) Stamp, Estate, Betting, Entertainment and Hotel Accommodation Duties.
  - (b) Business Registration Fees.

The general considerations regarding taxation frauds and negligence mentioned in paragraphs 410.23 to 410.26 above broadly apply to the above mentioned fees and duties; and where a practising member is acting as an agent for a client for the purpose of any of them similar considerations to those set out in paragraphs 410.29 to 410.41 above arise. With regard to requirements to disclose information or to produce documents, reference should be made in each case to the relevant statutory provisions, which vary in their terms as between one tax or duty and another, and whether such disclosure is needed in the public interest in accordance with section 225 of the Code.

### **Special Areas**

#### *Special Points in Connection with Companies*

- 410.49 In considering the advice given in this section it is important to bear in mind that in the case of a company governed by the Companies Ordinance the auditor's client is the company and not the directors. Where, however, the directors have so acted as to result in the company defrauding the Inland Revenue Department or committing other offences, references in this section to the "client" should be regarded in the first instance as referring to the directors of the company: for example, where it is necessary for the member to advise a client to make a full disclosure to the Inland Revenue Department the advice should be given to the directors.

...

#### **Past Accounts**

*[Bullet point (c) in extant paragraph 410.54 will be replaced by bullet point (c) below.]*

...

- (c) Third parties. The auditor ought not to allow anyone to continue to rely upon accounts on which he has reported, but now finds to be false, if there is any possibility of the third party acting to his detriment through reliance on the false accounts. An auditor might be held to be guilty of fraud (though the point is not covered by any authority) or held to be civilly liable in negligence (see the ICAEW statement "Accountants' Liability to Third Parties - The Hedley Byrne Decision") if he knew that the accounts had been submitted to a third party as an inducement to the third party to act thereon and he failed to inform the third party on discovering the falsity of the accounts before the third party had acted to his detriment. And in the case of a listed company an auditor should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include informing the relevant Stock Exchanges of what he had discovered. It is advised that, before making any such communication, he should seek legal advice about his duty and rights in the particular circumstances of the case, as to the method of any communication he decides to make and as to the terms in which the communication should be made.

## Removal of the Auditor

*[Extant paragraph 410.55 will be replaced by paragraph 410.55 below.]*

410.55 The distinction between the directors and the shareholders will sometimes have little or no relevance, either because the directors hold a controlling interest or because all the shareholders are directors. When in these circumstances the directors fail to comply with the auditor's advice they are likely to wish to prevent the auditor from completing his audit and making a report containing qualifications. They could achieve this by calling a general meeting at which the sole business would be the removal of the auditor, no accounts being placed before the meeting. If this procedure is followed, the auditor may wish to exercise his right under section 411 of the Companies Ordinance to attend the meeting and be heard. The auditor may also consider exercising the rights under section 422(3) of the Companies Ordinance by giving the company a statement that sets out in reasonable length the circumstances surrounding the proposed removal and may request the company to comply with the requirements specified in section 422(5) of the Companies Ordinance in relation to the statement. If he has been acting for the company in relation to taxation matters, and he receives any enquiries from the Inland Revenue Department he should follow the guidance in paragraphs 410.23 to 410.48 when responding to the Inland Revenue Department.

## Companies in Liquidation

...

*[Extant paragraph 410.57 will be replaced by paragraph 410.57 below.]*

410.57 The auditor of a company which is in liquidation may be approached by the police for assistance in enquiries which may lead to a director or other individual being prosecuted. Under this circumstance, the auditor's appropriate course is to make available to the liquidator all relevant information, leaving with the liquidator the responsibility of deciding whether under section 277 of Companies (Winding Up and Miscellaneous Provisions) Ordinance the liquidator has a duty to make a report to the Secretary for Justice. If such a report is made by the liquidator then the auditor is, by subsection (4), one of the persons having a statutory duty to give assistance to the Secretary for Justice, so that in these circumstances his duty of confidence is overridden by the statutory provisions. However, if the auditor has encountered or is aware of any suspected or actual non-compliance with laws and regulations of the clients which is related to the enquiry made by the police, the auditor should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the matter to the police, without referring to the liquidator.

## *Special Points In Connection with Sole Traders and Partnerships*

...

*[Extant paragraph 410.61 will be replaced by paragraph 410.61 below.]*

410.61 Where a member is acting for a client in taxation matters he may receive from the Inland Revenue Department questions designed to ascertain whether all receipts have been properly accounted for, or whether disallowable expenditure is included in amounts charged in the accounts, or whether stock has been valued on proper and consistent principles. A member should not undertake responsibility for replies to such questions unless he is satisfied from his examination of the books and records that all relevant information is available to him. Where he is not so satisfied his proper course is to obtain answers from his client and pass them on as such to the Inland Revenue Department.

## Responsibilities of a Member who Discovers During his Work that His Client is Committing or Has Committed an Offence under the Prevention of Bribery Ordinance

*[Extant paragraph 410.68 will be replaced by paragraph 410.68 below.]*

410.68 Although in the absence of compulsion by due process of law, a member is not at liberty and is generally under no legal obligation to disclose to the ICAC information acquired during the performance of his duties, he should, in the event of his discovering a corruption offence, follow the response framework set out in section 225 of the Code.

...

## Other Matters

### *Member's Relationship with a successor*

*[Extant paragraphs 410.79 to 410.83 will be replaced by paragraphs 410.79 to 410.83 below.]*

410.79 It is the duty of any member of the Institute, before accepting nomination for appointment as auditor for a company, partnership or individual, to communicate with the previous auditor. In this connection attention is drawn to section 440 "Changes in a Professional Appointment" wherein the Council makes it clear that it is essential for a member who is proposed for appointment as auditor to have an opportunity of knowing all the reasons for the change, that this requirement can only be fulfilled by direct communication with the holder of the existing appointment and that a member should not accept the appointment if he is refused permission to make this communication.

410.80 Where a member resigns his appointment or indicates to his client that he will not accept reappointment, or where the client terminates the appointment, the question arises whether the member should inform his prospective successor of the reasons for the change where they relate to fraud on the Inland Revenue Department or other unlawful acts or defaults. Members are advised as follows:

- (a) the initiative in the matter of communication rests with the prospective successor; the retiring member should not volunteer information in the absence of any communication;
- (b) the prospective successor should seek the permission of the client to make this communication and should not accept the appointment if permission to make the communication is refused;
- (c) subject to what is said in the next sub-paragraph, when a member receives a communication from a prospective successor he should inform the prospective successor of at least the general nature of the reason for the change; and to the extent that it seems necessary in order to put the prospective successor adequately on his guard he should be informed of the facts constituting that reason;
- (d) the legal position of the retiring member depends not upon whether the prospective successor has received the client's permission to communicate with the retiring members but upon whether the retiring member has been authorised by the client to discuss the client's affairs with the prospective successor. The retiring member could obtain this authorisation either by having made it a term of his contract with his client that he should be entitled to comply with Code of Ethics issued by the Institute regarding these communications or by informing his client when the prospective successor communicates with him and getting express permission to tell the prospective successor the reasons for his retirement. If he has this authorisation then provided he says what he honestly believes to be true he can state the reasons for his retirement without any fear of an action for either breach of contract or defamation. If he does not have this authorisation the Council is advised that he would nevertheless have a strong measure of protection against an action for defamation in

that his communication would be the subject of qualified privilege, which means that he would not be liable to pay damages for defamatory statements, even though untrue, if they were made without malice: and provided he stated only what he sincerely believed to be true the chances of his being held malicious are remote. Moreover although in making a communication without authorisation a retiring member might technically be in breach of contract and although there could be circumstances in which the resulting damages were substantial, the likelihood of an action being brought against him is small and in most cases the damages awarded in such an action would be nominal;

- (e) where a member, in the course of an audit of financial statements, has unconfirmed suspicion or actual knowledge that the audit client has defrauded the Inland Revenue Department or been guilty of some other unlawful act or default and as a result, has withdrawn from the professional relationship with the client, he should provide all such facts and other information to a prospective successor who communicates with him without the need to obtain client's consent. (See paragraph 225.31 of the Code);
- (f) the prospective successor should treat in the strictest confidence any information given to him by the retiring member. After due consideration of the information it is for the prospective successor to decide whether as a matter of professional conduct or as one of personal inclination he can properly accept the appointment. If he does so, the advice given in this section would then be applicable to him.

410.81 The consideration arising on a change of auditor apply to a large extent also where a member is invited to undertake other recurring professional work in place of another accountant, except that section 410.80(e) above does not apply to non-audit engagement.

#### *Prosecution of a Client or Former Client*

410.82 It follows from paragraphs 410.8 to 410.18 above that it would depend upon the nature of the offence and other circumstances connected with it whether or not a member would be acting in breach of his contractual duty of confidence or contrary to proper professional standards if he were, except under legal compulsion or with his client's consent, to assist the police, Inland Revenue Department, ICAC or other authority by giving information about his client's affairs for the purposes of enquiries leading towards a prosecution of the client for an offence other than treason. If he is requested to give information he should comply if the person requesting the information has a statutory right to demand it. In any other cases, the member should follow the response framework set out in section 225 of the Code and determine whether further action is needed, which may include disclosing the information to an appropriate authority.

410.83 A member should not normally appear in Court as a witness for the government in a case against a client or former client, unless he is served with a subpoena or other lawful summons to do so, in which case he must of course answer truthfully any questions that the Court allows to be put to him even though this involves disclosure of facts of which he obtained knowledge in his confidential professional capacity. Moreover he cannot lawfully refuse to produce in Court any documents in his ownership or possession which the Court may direct him to produce. If the persons in charge of the prosecution have indicated that they will call upon the member to produce certain documents in Court, the member would be wise to have the documents with him but the power to order their production in Court rests with the Court.

## SECTION 411

### Unlawful Acts or Defaults by or on Behalf of a Member's Employer

*[The extant first introduction paragraph will be replaced by the paragraph below.]*

*This section should be read in conjunction with Section 140 "Confidentiality" and Section 360 "Responding to Non-Compliance with Laws and Regulations"*

...

#### Part 1 – Introduction

...

*[Extant paragraph 411.2 will be replaced by paragraph 411.2 below.]*

411.2 If a member acquires knowledge indicating that his employer or someone acting on behalf of his employer may have been guilty of some default or unlawful act he should normally raise the matter with management internally at an appropriate level. If his concerns are not satisfactorily resolved, he should report the matter to non-executive directors and those charged with governance where these exist. Where this is not possible or fails to resolve the matter a member may wish to consider making a report to a third party. Members in business should refer to section 360 of the Code, which sets out the response framework when members encounter non-compliance with laws and regulations during the course of their work. Local guidance is provided below on reporting suspected defaults or unlawful acts to third parties outside the organisation for which the member works.

#### Part 2 - Relations between a Member and His Employer

...

##### *Disclosure to Third Parties of Defaults or Unlawful Acts*

*[Extant paragraph 411.4 will be replaced by paragraph 411.4 below.]*

411.4 An employed member has a general duty to his employer to act with good faith and fidelity, including a duty to keep confidential information obtained as a result of this employment. If no such express term appears in his contract of employment it will be implied by law.

...

*[Extant paragraph 411.6 will be replaced by paragraph 411.6 below.]*

411.6 There are, however, circumstances in which, in spite of any duty of confidentiality, a member may be obliged to disclose. Even if not obliged to disclose, he may determine that such disclosure is justified in the public interest (see section 360) or required for the protection of the member's own interest. Guidance on whether a member should disclose the matter to a third party is set out in the paragraphs below.

...

*[Extant paragraphs 411.9 and 411.10 will be replaced by paragraphs 411.9 and 411.10 below. Extant headings above paragraphs 411.9 and 411.10 will be deleted. ]*

411.9 [Not used]

411.10 [Not used]

...

##### *Disclosure to Non-governmental Bodies*

*[Extant paragraphs 411.14 and 411.15 will be replaced by paragraphs 411.14 and 411.15 below.]*

411.14 Members are sometimes approached by recognised but non-governmental bodies seeking information concerning suspected acts of misconduct not amounting to a crime or civil wrong. Some non-governmental bodies enjoy statutory powers to require persons to supply information for that purpose, in which case the member should comply. In other cases, however, the member should follow the response framework in section 360 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

*Prosecution of an Employer or Former Employer*

411.15 Where a member is approached by the police, the Inland Revenue Department, or other public authority making enquiries which may lead to the prosecution of an employer or former employer for an offence, the member should comply if the person requesting for information has such a legal right. In other cases, however, the member should follow the response framework in section 360 of the Code and determine whether further action is needed, which may include disclosing the matter to an appropriate authority.

**SECTION 430**

**Ethics in Tax Practice**

...

**Development of the Fundamental Principles**

...

*[Extant paragraph 430.6 will be replaced by paragraph 430.6 below.]*

- 430.6 A member must not associate himself with any return or communication which he has reason to believe:
- (a) contains a false or misleading statement;
  - (b) contains statements or information furnished by the client 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 Inland Revenue Department.

If any of the above situations prevails, the member's responsibility is to resign from acting as the client's tax representative. Having resigned the member should:

- (a) inform the Inland Revenue Department that he has withdrawn his services.
- (b) act according to paragraphs 225.39 – 225.56 of the Code, including consider whether disclosing the matter to the external auditor and / or the Inland Revenue Department.

...

*[Extant paragraph 430.9 will be replaced by paragraph 430.9 below.]*

- 430.9 The member's responsibility when he learns of a material error or omission in a client's tax return of a prior year (with which he may or may not have been associated), or of the failure of a client to file a required tax return, is as follows:
- (a) He should promptly advise his client of the error or omission and recommend that the client make disclosure to the Inland Revenue Department.

- (b) If the client does not correct the error:
  - (i) the member should inform the client that he cannot act for him in connection with that return or other related information submitted to the authorities;
  - (ii) the member should consider whether continued association with the client in any capacity is consistent with his professional responsibilities;
  - (iii) and if the member concludes that he can continue with his professional relationships with the client, he should take all reasonable steps to assure himself that the error is not repeated in subsequent tax returns.
- (c) If because of the error or omission, the member ceases to act for the client, in these circumstances, the member should advise the client of the position before informing the authorities of his having ceased to act.
- (d) He should consider, under paragraphs 225.39 – 225.56 of the Code, whether disclosing the matter to the external auditor and / or the Inland Revenue Department is appropriate.

## **SECTION 431**

### **Corporate Finance Advice**

#### **Introduction**

...

*[Extant paragraph 431.3 will be replaced by paragraph 431.3 below.]*

431.3 Failure to follow such guidance may constitute misconduct, and a member concerned may be at risk of having to justify his actions in answer to a complaint to the Institute. In addition, matters discussed in this section may have legal implications and a member who is in doubt as to his position should consider obtaining legal advice.

...

#### **Documents for Client and Public Use/Confidentiality**

*[Extant paragraph 431.24 will be replaced by paragraph 431.24 below.]*

431.24 Information acquired in the course of professional work should not be disclosed except where consent has been obtained from the client, employer or other proper source, or where there is a public duty to disclose or where there is a legal or professional right or duty to disclose (see Section 140 "Confidentiality" and Section 225 "Responding to Non-Compliance with Laws and Regulations").

## **SECTION 440**

### **Changes in a Professional Appointment**

...

#### **Guidelines**

##### *General*

*[Extant paragraph 440.11 will be replaced by paragraph 440.11 below.]*

440.11 Although the guidance which follows takes as its basis the replacement of an auditor of a company, that basis is adopted as but one example of a change in a professional

appointment. It follows that the considerations arising on a change of auditor generally also apply, in appropriate fashion, when a member is invited to undertake advisory work of a recurring nature (including the provision of services such as, e.g. accountancy and taxation) in place of another accountant, except for paragraph 440.23 which applies only to audit engagement. They apply whether the client is a company or any other corporate body, an individual, a partnership or any other kind of association, and a member invited to accept nomination or appointment as auditor of a body other than a company should be guided by the same considerations as those indicated in relation to a company. In the case of an audit client they apply in respect of non-audit work as they do to audit work. The reasons for communication as set out in this guidance are equally applicable in all cases.

...

### *Audit Appointments*

...

*[Extant paragraph 440.18 will be replaced by paragraph 440.18 below.]*

440.18 The initiative in the matter of communication rests with the member. The existing auditor should not volunteer information in the absence of such communication and of authority from the client (See paragraph 440.23 for circumstance where client's consent is not needed).

...

*[Extant paragraph 440.23 will be replaced by paragraph 440.23 below.]*

440.23 If the existing auditor has withdrawn from the professional relationship pursuant to paragraphs 225.25 and 225.29 of the Code, he should, on request by the proposed new auditor, provide all facts and other information concerning the identified or suspected non-compliance with laws and regulations to the proposed new auditor without the need to obtain client's consent, unless prohibited by law or regulation. See paragraph 225.31 of the Code for further guidance.

## **SECTION 441**

### **Changes of Auditors of a Listed Issuer of The Stock Exchange of Hong Kong**

*[Extant paragraph 441.25 will be deleted.]*

*[Extant paragraph 441.26 will be renumbered paragraph 441.25.]*