ELEMENTS OF SSQC 1

RELEVANT ETHICAL REQUIREMENTS

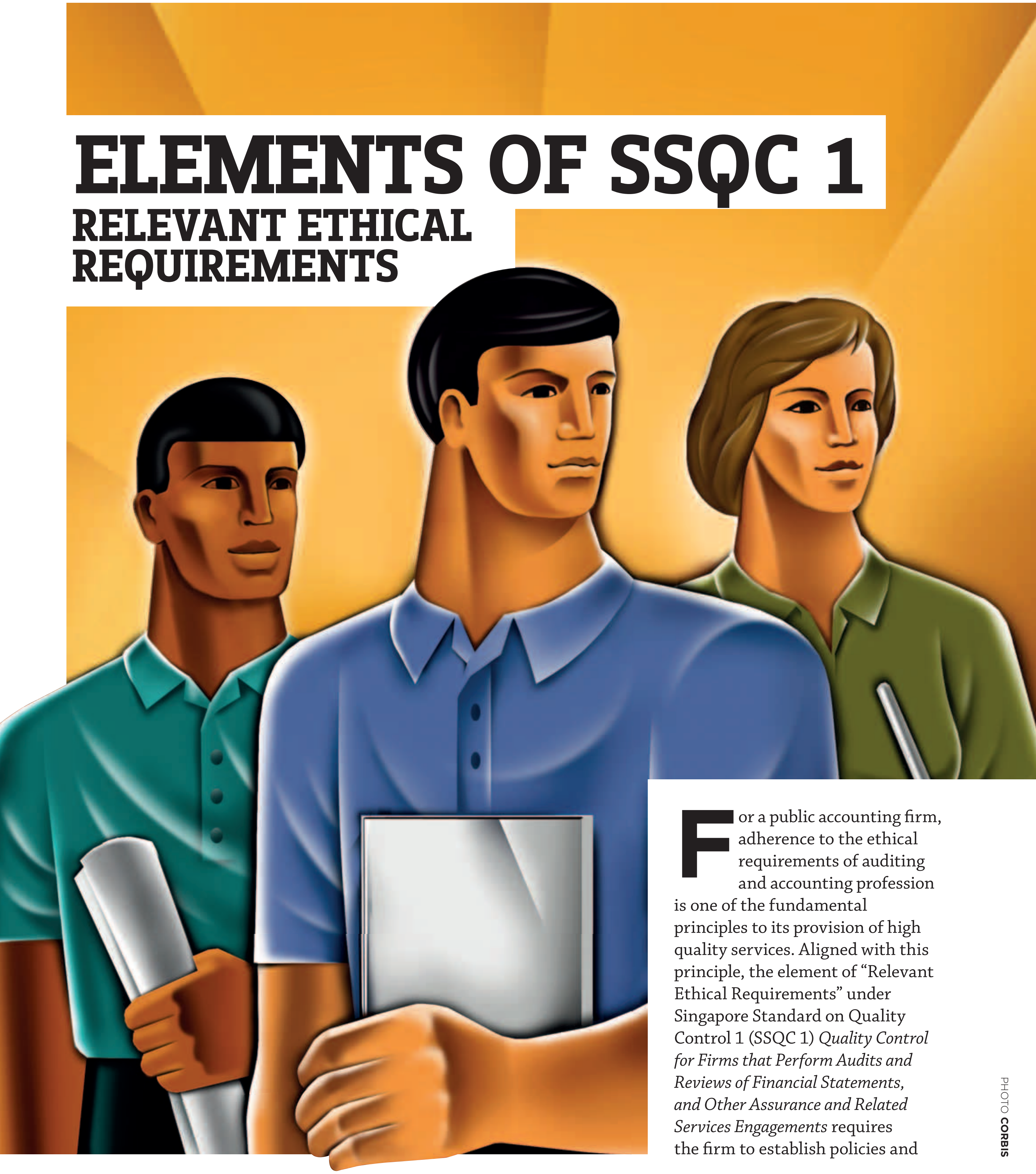

PHOTO CORBIS

For a public accounting firm, adherence to the ethical requirements of auditing and accounting profession is one of the fundamental principles to its provision of high quality services. Aligned with this principle, the element of "Relevant Ethical Requirements" under Singapore Standard on Quality Control 1 (SSQC 1) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* requires the firm to establish policies and procedures to provide the firm with reasonable assurance that the firm and its personnel comply with the requirements on ethics, in particular, the Code of Professional Conduct and Ethics under the Fourth Schedule of Accountants (Public Accountants) Rules (the Code).

A public accounting firm should make every effort to ensure that it meets all relevant ethical requirements at all times. Regular communication of the ethical requirements to the firm's personnel is pivotal to achieve this objective. For instance, the firm could discuss matters relating to compliance or non-compliance with the ethical requirements at internal management meetings on a periodic basis. Such discussions will demonstrate to the firm's personnel that the commitment to comply with the ethical requirements is highly important.

Other than the regular communication, the firm should evaluate its personnel's commitment to ethical requirements when conducting the performance review for career advancement or compensation. This criterion should be emphasised to instil the right ethical values and behaviours among the firm's personnel.

There are three core components in Relevant Ethical Requirements: Independence, Conflict of Interest, and Confidentiality and Other Ethical Requirements.

1 INDEPENDENCE

The objective of this component is to ensure that a public accounting firm's personnel, who include all partners and staff, are independent of its clients. One of the important aspects of the component is the communication to the firm's personnel of the independence requirement. This communication can be achieved through the firm's orientation or training programmes for new staff. The firm can also arrange refresher courses for its existing staff to ensure they understand the relevant independence requirements and keep abreast of the changes in these requirements, if any.

IT IS CRUCIAL FOR A PUBLIC ACCOUNTING FIRM TO ESTABLISH A CORPORATE CULTURE THAT FOSTERS HIGH ETHICAL STANDARDS WHICH WILL PROMOTE THE IMMERSION OF ALL PERSONNEL OF THE FIRM INTO SUCH A CULTURE.

In assessing threats to independence, the firm should identify and eliminate the threats that could compromise its independence. Upon evaluation of the identified threats, the firm should address each by applying appropriate safeguards to eliminate or reduce them to an acceptable level. If the threats cannot be eliminated or reduced to an acceptable level, the firm should exercise discretion and choose to withdraw from the client relationship or the specific engagement.

In evaluating the impact on independence before accepting an engagement, the engagement partner should provide the firm with necessary information pertaining to the scope of services and identities of the prospective client's directors, shareholders and other related parties. When assessing acceptance or continuance of client relationships and specific engagements, the firm should perform comprehensive independence checks to ensure its compliance.

The threats to independence can be categorised as arising from self-interest, self-review, advocacy, familiarity and intimidation. The safeguards to eliminate or reduce such threats may include the following:

- Replacing a member of the engagement team;
- Ceasing or altering the type of service performed for the engagement;
- Ceasing or changing the nature of personal or business relationships with the client; and
- Divesting financial or ownership interest in the client or its related entities

For a public accounting firm, it is not uncommon to face threats to independence. For example, if the firm's client fails to settle its overdue fee with the firm, a self-interest threat may be present. In such a situation, it is the firm's responsibility to resolve the unpaid fee before commencing its engagement for the following year. This threat could be mitigated through communicating with the client and following up on collection, before proceeding with the following year's engagement with the same client.

A familiarity threat may arise when the same engagement partner or the engagement quality control reviewer (EQCR) serves a listed company's assurance engagement over a long period of time. To eliminate this threat, the engagement partner and EQCR should be rotated after serving this client for a predetermined period, normally five years in Singapore. Smaller firms with a limited number of partners could engage another public accountant, who is not associated with the engagement team, as a reviewer. The review performed by a suitably qualified external party should suffice to reduce the familiarity threat to an acceptable level.

To facilitate compliance with independence requirements, the firm should designate a personnel or a group of personnel for oversight of such requirements. The designated personnel should possess sufficient authority, knowledge and experience on independence-related issues, and is tasked with the responsibility to monitor compliance with independence requirements by the firm's personnel, including the firm's partners and all professional staff. This provides firm-wide control on compliance with independence requirements through the provision of guidance and addressing instances of non-compliance by implementing corrective and followup actions.

The aforementioned designated personnel should also maintain a listing of the firm's clients and its related entities, such as subsidiaries and associated companies, from which the firm is required to be independent. All professional staff of the firm should be granted access to view (but not modify) the listing to self-monitor their independence and notify the firm whenever a specific circumstance or relationship poses a threat to independence.

All personnel of the firm, including partners, are required to submit written independence confirmations at least annually, and for new staff, at the time of joining. The confirmation may be in paper or electronic format, and should expressly state that the personnel understand and comply with the independence requirements which should be in accordance with the Code. This is a firm-level independence confirmation. At the engagement level, all personnel assigned with an assurance engagement should also provide an independence confirmation to the engagement partner before the commencement of the work and promptly notify the engagement partner if there is any threat to independence.

If a firm belongs to a network, it should be noted that independence requirements extend to every firm in the network. The firm operating within a network should apply the same requirements to other firms within the network, and communicate with each other on independence requirements on a periodic basis.

2 CONFLICT OF INTEREST

The objective of this component is to ensure that a public accounting firm's personnel do not have a conflict of interest with its clients. If there is any conflict of interest with the prospective client, the firm should have safeguards in place to

PHOTO CORBIS

eliminate or reduce the conflict to an acceptable level. For example, if the firm is engaged by a client to provide tax compliance service and financial statement audit service, a conflict of interest may arise. The firm could apply appropriate safeguards to eliminate or reduce this potential conflict of interest by using separate engagement teams with different engagement partners to perform the respective engagements, or establishing separate entities to provide the respective services; the latter safeguard would be more relevant under such circumstances.

If the firm cannot resolve the conflict of interest, it should choose to withdraw from the client relationship or the engagement. The firm should also designate a personnel or a group of personnel to identify and assess any conflict of interest. The designated personnel is responsible for identifying circumstances that could lead to a conflict of interest between the firm and a client, or between two of its clients. If a situation is identified that could pose a conflict of interest, the designated personnel should determine the most appropriate measures to address the issue, as well as document its resolution.

3 CONFIDENTIALITY AND OTHER ETHICAL REQUIREMENTS

The final component deals with confidentiality of a public accounting firm's client information and compliance with other ethical requirements. The firm's personnel should protect and maintain confidentiality of its client's information which should only be used or disclosed for the purpose of the engagement which the firm undertakes, unless there is a legal obligation to disclose it to certain third parties. Under no other circumstances should the firm disclose its client's information to unauthorised third parties. All partners and personnel are required to sign a declaration of confidentiality confirming their understanding of the requirements and obligations, upon joining the firm. For non-compliance, the firm should take disciplinary action against the errant parties.

The firm's personnel should be prudent when dealing with confidential client information in public areas. For example, professional care must be taken to ensure that unused draft client reports are properly disposed of. In addition, the firm should restrict access to confidential information pertaining to the engagement to only the engagement team members. Physical control may be achieved through hard copies being maintained and controlled by filing clerks, and computer access control may be achieved through password requirements as well as encryption of electronic files. Non-engagement team members who need to access the engagement's information are required to submit the access request with reasons to the designated engagement team member, normally the engagement manager or partner, for approval.

IF A FIRM BELONGS TO A NETWORK, IT SHOULD BE NOTED THAT INDEPENDENCE REQUIREMENTS EXTEND TO EVERY FIRM IN THE NETWORK. THE FIRM OPERATING WITHIN A NETWORK SHOULD APPLY THE SAME REQUIREMENTS TO OTHER FIRMS WITHIN THE NETWORK, AND COMMUNICATE WITH EACH OTHER ON INDEPENDENCE REQUIREMENTS ON A PERIODIC BASIS.

In addition to confidentiality requirements, the firm should also ensure that its personnel comply with the ethical requirements prescribed in the Code, which include integrity, objectivity, professional competence and due care, as well as professional behaviour and any additional regulatory requirements relating to ethics for the auditing and accounting profession.

CONCLUSION

Last but not least, it is crucial for a public accounting firm to establish a corporate culture that fosters high ethical standards which will promote the immersion of all personnel of the firm into such a culture. With this, the firm's personnel can comply with the relevant ethical requirements thereby exercising their professional judgements objectively, with a reasonable level of scepticism, in drawing conclusions on the engagement report. CPA

By Jason Pang, Quality Assurance Manager, ICPAS