

Note for Quebec CPAs

ONLY THE PROVISIONS ENCLOSED IN BOXES ARE COVERED BY THE DYNAMIC REFERENCE IN SECTION 36.4 OF THE *CODE OF ETHICS OF CHARTERED PROFESSIONAL ACCOUNTANTS* (CQLR c. C-48.1, r.6). THE “GUIDANCE” IS PROVIDED FOR INFORMATION PURPOSES ONLY.

204 Independence

DEFINITIONS:

For the purposes of Rules 204.1 to 204.10 and the related Guidance:

“accounting role” means a role in which a person is in a position to or does exercise more than minimal influence over:

- (a) the contents of the client’s accounting records related to the financial statements subject to audit or review by the member or firm; or
- (b) anyone who prepares such financial statements.

“assurance client” means an entity in respect of which a member or firm has been engaged to perform an assurance engagement. In the application of Rule 204.4(1) to (12) “assurance client” includes its related entities, and the reference to an assurance client, a client or an entity that is an assurance client shall be read as including all related entities of the assurance client, client or entity as the case may be.

“assurance engagement” means an assurance engagement as contemplated in the CPA Canada Handbook – Assurance. For the purpose of Rule 204.4, “assurance engagement” also includes a specified auditing procedures engagement as contemplated by the CPA Canada Handbook – Assurance.

“audit client” means an entity in respect of which a member or firm has been engaged to perform an audit of the financial statements. In the application of Rule 204.4(1) to (12) “audit client” includes its related entities, and the reference to an assurance client, a client or an entity that is an audit client shall be read as including all related entities of the assurance client, client or entity as the case may be.

“audit committee” means the audit committee of the entity, or if there is no audit committee, another governance body which has the duties and responsibilities normally granted to an audit committee, or those charged with governance of the entity.

“audit engagement” means an engagement to audit financial statements as contemplated in the CPA Canada Handbook – Assurance.

“audit partner” means a person who is a partner in a firm or a person who has equivalent responsibility, who is a member of the engagement team, other than a specialist or technical partner or equivalent who consults with others on the engagement team regarding technical or industry-specific issues, transactions or events.

“clearly insignificant” means trivial and inconsequential.

“close family member” means a parent, child or sibling who is not an immediate family member.

“direct financial interest” means a financial interest:

- (a) owned directly by and under the control of an individual or entity (including those managed

- on a discretionary basis by others);
- (b) beneficially owned through a collective investment vehicle, estate, trust or other intermediary over which the individual or entity has control or ability to influence investment decisions ;
- (c) owned through an investment club or by a private mutual fund in which the individual participates in the investment decisions.

“engagement period” means the period that starts at the earlier of the date when the member or firm signs the engagement letter or commences procedures in respect of the engagement and ends when the assurance report is issued, except when the engagement is of a recurring nature, in which case the engagement period ends with

- (a) notification by either the client or the firm that the professional relationship has terminated or the issuance of the final assurance report, whichever is later, or
- (b) in the case of an audit engagement for a reporting issuer or listed entity, notification by either the client or the firm to the relevant Securities Commission that the audit client is no longer an audit client of the firm.

“engagement quality control reviewer”, often referred to as reviewing, concurring or second partner, means the audit partner or other person in the firm who, prior to issuance of the audit report, provides an objective evaluation of the significant judgments made and conclusions reached by the members of the engagement team in formulating the report on the engagement.

“engagement team” means:

- (a) each member of the firm performing the assurance engagement;
- (b) all other members of the firm who can directly influence the outcome of the assurance engagement, including:
 - (i) those who recommend the compensation of, or who provide direct supervisory, management or other oversight of, the assurance engagement partner in connection with the performance of the assurance engagement. For the purposes of an audit engagement this includes those at all successively senior levels above the lead engagement partner through to the firm’s chief executive officer;
 - (ii) those who provide consultation regarding technical or industry-specific issues, transactions or events for the assurance engagement; and
 - (iii) those who provide quality control for the assurance engagement;
- and
- (c) in the case of an audit client, all persons in a network firm who can directly influence the outcome of the audit engagement.

“financial interest” includes a direct or indirect ownership interest in an equity or other security, debenture, loan or other debt instrument of an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.

“financial reporting oversight role” means a role in which a person is in a position to or does exercise influence over:

- (a) the contents of the financial statements subject to audit or review by the member or firm; or
- (b) anyone who prepares the financial statements.

“firm” means a sole practitioner, partnership, [provinces add professional corporation or incorporated professional where appropriate] or association of members who carries or carry on the practice of public accounting, or carries or carry on related activities as defined by the [Board/Council]. A related business or practice, as defined by [insert appropriate bylaw reference], is considered to be part of the firm.

“fund manager” means, with respect to a mutual fund, an entity that is responsible for investing the mutual fund’s assets, managing its portfolio trading and providing it with administrative and other services, pursuant to a management contract.

“immediate family member” means a spouse (or equivalent) or dependant.

“indirect financial interest” means a financial interest beneficially owned through a collective investment vehicle such as a mutual fund, estate, trust or other intermediary over which the beneficial owner has no control or ability to influence investment decisions.

“key audit partner” means

- (a) an audit partner who is the lead engagement partner,
- (b) the engagement quality control reviewer, and
- (c) any other audit partner on the engagement team who makes important decisions or judgments on significant matters with respect to the audit or review engagement.

“lead engagement partner” means the partner or other person who is responsible for the engagement and its performance, for the report that is issued on behalf of the firm and who, where required, has the appropriate authority from a professional, legal or regulatory body.

“legal service” means any service that may only be provided by a person licensed, admitted, or otherwise qualified to practice law in the jurisdiction in which the service is provided. If the same service could be provided in Canada by a person who is not a lawyer, such a service is not a legal service for the purposes of this rule.

“listed entity” means an entity whose shares, debt or other securities are quoted on, listed on or marketed through a recognized stock exchange or other equivalent body, whether within or outside of Canada, other than an entity that has, in respect of a particular fiscal year, market capitalization and total assets that are each less than \$10,000,000. An entity that becomes a listed entity by virtue of the market capitalization or total assets becoming \$10,000,000 or more in respect of a particular fiscal year shall be considered to be a listed entity thenceforward unless and until the entity ceases to have its shares or debt quoted, listed or marketed in connection with a recognized stock exchange or the entity has remained under the market capitalization or total assets threshold for a period of two years.

In the case of a period in which an entity makes a public offering:

- (a) the term “market capitalization” shall be read as referring to the market price of all outstanding listed securities and publicly traded debt measured using the closing price on the day of the public offering; and
- (b) the term “total assets” shall be read as referring to the amount of total assets presented on the most recent financial statements prepared in accordance with generally accepted accounting principles included in the public offering document.

“market capitalization” in respect of a particular fiscal year means the average market price of all outstanding listed securities and publicly traded debt of the entity measured at the end of each of the first, second and third quarters of the prior fiscal year and the year-end of the second prior fiscal year.

“member of a firm” or **“member of the firm”**, as the case may be, means a person, whether or not a member of a provincial CPA body,, who is:

- (a) a sole practitioner;
- (b) a partner, professional employee or [candidate or student] of the firm;
- (c) an individual engaged under contract by the firm to provide services that might otherwise be

provided by a partner or professional employee of the firm, but does not include an external expert possessing skills, knowledge and experience in a field other than accounting or auditing whose work in that field is used to assist the member or firm in obtaining sufficient appropriate evidence ;

- (d) an individual who provides to the firm services which are referred to in Rule 204.1 and includes any corporate or other entity through which the individual contracts to provide such services; or*
- (e) a retired partner of the firm who retains a close association with the firm.*

“mutual fund” means a mutual fund that is a reporting issuer under the applicable Canadian provincial or territorial securities legislation.

“mutual fund complex” means:

- (a) a mutual fund that has the same fund manager as a client;*
- (b) a mutual fund that has a fund manager that is controlled by the fund manager of a client; and*
- (c) a mutual fund that has a fund manager that is under common control with the fund manager of a client.*

“network firm” means an entity that is, or that a reasonable observer would conclude to be, part of a larger structure of co-operating entities that shares;

- (a) common quality control policies and procedures that are designed, implemented and monitored across the larger structure;*
- (b) common business strategy that involves agreement to achieve common strategic objectives;*
- (c) the use of a common brand name, including the use of common initials and the use of the common brand name as part of, or along with, a firm name when a partner of the firm signs an audit or review engagement report; or*
- (d) professional resources, such as*
 - (i) common systems that enable the exchange of information such as client data, billing or time records;*
 - (ii) partners and staff;*
 - (iii) technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;*
 - (iv) audit methodology or audit manuals; or*
 - (v) training courses and facilities,*
where such professional resources are significant.

“office” means a distinct sub-group of a firm, whether organized on geographical or practice lines.

“related entity” means any one of the following:

- (a) in the case of an engagement to audit the financial statements of a client that is a reporting issuer or listed entity*
 - (i) an entity over which the client has control,*
 - (ii) an entity that has control over the client, provided that the client is material to such entity,*
 - (iii) an entity that has significant influence over the client, provided that the client is material to such entity,*
 - (iv) an entity which is under common control with the client, provided that such entity and the client are both material to the controlling entity, or*
 - (v) an entity over which a client has significant influence, provided that the entity is material to the client;*
- (b) in the case of an engagement to audit or review the financial statements of a client that is not a reporting issuer or listed entity*

- (i) *an entity over which the client has control, or*
- (ii) *any of the following entities where the engagement team knows or has reason to believe that the existence of an activity, interest or relationship involving the member or firm and that other entity is relevant to the evaluation of the independence of the member or firm with respect to the audit or review of the financial statements of the client:*
 - (A) *an entity that has control over the client, provided that the client is material to such entity,*
 - (B) *an entity that has significant influence over the client, provided that the client is material to such entity,*
 - (C) *an entity which is under common control with the client, provided that such entity and the client are both material to the controlling entity, or*
 - (D) *an entity over which a client has significant influence, provided that the entity is material to the client; and*
- (c) *in the case of an assurance engagement that is not an engagement to audit or review the financial statements of a client, any of the following entities where the engagement team knows or has reason to believe that the existence of an activity, interest or relationship involving the member or firm and that other entity is relevant to the evaluation of the independence of the member or firm with respect to the assurance engagement:*
 - (i) *an entity over which the client has control,*
 - (ii) *an entity that has control over the client, provided that the client is material to such entity,*
 - (iii) *an entity that has significant influence over the client, provided that the client is material to such entity,*
 - (iv) *an entity which is under common control with the client, provided that such entity and the client are both material to the controlling entity, or*
 - (v) *an entity over which a client has significant influence, provided that the entity is material to the client.*

“reporting issuer” means an entity that is defined as a reporting issuer under the applicable Canadian provincial or territorial securities legislation, other than an entity that has, in respect of a particular fiscal year, market capitalization and total assets that are each less than \$10,000,000. An entity that becomes a reporting issuer by virtue of the market capitalization or total assets becoming \$10,000,000 or more in respect of a particular fiscal year shall be considered to be a reporting issuer thenceforward unless and until the entity ceases to have its shares or debt quoted, listed or marketed in connection with a recognized stock exchange or the entity has remained under the market capitalization or total assets threshold for a period of two years.

In the case of a period in which an entity makes a public offering:

- (a) *the term “market capitalization” shall be read as referring to the market price of all outstanding listed securities and publicly traded debt measured using the closing price on the day of the public offering; and*
- (b) *the term “total assets” shall be read as referring to the amount of total assets presented on the most recent financial statements prepared in accordance with generally accepted accounting principles included in the public offering document.*

In the case of a reporting issuer that does not have listed securities or publicly traded debt, the definition of reporting issuer shall be read without reference to market capitalization.

“review client” means an entity in respect of which a member or firm conducts a review engagement. In the application of Rule 204.4(1) to (12) “review client” includes its related entities, and the reference to an assurance client, a client or an entity that is a review client shall be read as including all related entities of the assurance client, client or entity, as the case may be.

“review engagement” means an engagement to review financial statements as contemplated in the CPA Canada Handbook – Assurance.

“specified auditing procedures engagement” means an engagement to perform specified auditing procedures as contemplated in the CPA Canada Handbook – Assurance.

“total assets” in respect of a particular fiscal year means the amount of total assets presented on the third quarter of the prior fiscal year’s financial statements prepared in accordance with generally accepted accounting principles that are filed with a relevant securities regulator or stock exchange. In the case of an entity that is not required to file quarterly financial statements, total assets in respect of a particular fiscal year means the amount of total assets presented on the annual financial statements of the second previous fiscal year prepared in accordance with generally accepted accounting principles that are filed with a relevant securities regulator or stock exchange.

GUIDANCE - Rule 204 Definitions

“clearly insignificant”

Throughout this Rule and Guidance, reference is made to “significant” and “clearly insignificant”. In considering the significance of any particular matter, qualitative as well as quantitative factors should be taken into account. A matter should be considered clearly insignificant only if it is both trivial and inconsequential.

“firm”

The definition of “firm” refers to related activities as defined by the [Board/Council]. A related activity includes a related business or practice that is cross-referenced with a practice of public accounting or with any other business or practice which is cross-referenced with a practice of public accounting in accordance with By-law [number of appropriate By-law].

“key audit partner”

A key audit partner does not include those “specialty” and “technical” partners who consult with others on the engagement team regarding technical or industry-specific issues, transactions or events, including tax matters. In addition, the provisions of Rules 204.4(20)(b) and 204.4(38) do not apply to those partners who, subsequent to the issuance of the audit report, provide quality control for the engagement. Such partners typically have a low level of involvement with senior management as well as a relatively low level responsibility for overall presentation in the financial statements.

A transitional provision has been introduced in relation to the adoption, in 2014, of the term “key audit partner”. This transitional provision will permit a person who was not required to rotate under the previous requirements to serve up to an additional two years in a key audit partner role before rotation is required.

“member of a firm” - retired partner

A retired partner who retains a close association with the firm from which the partner has retired is considered to be a member of the firm for the purposes of Rules 204.1 to 204.10 and the related Guidance. Retired partners may have varying degrees of involvement with the firm. When a retired partner continues to provide administrative or client service for or on behalf of the firm, the partner may be closely associated with the firm. The following factors may indicate that the partner retains a close association with the firm:

- the nature and extent of the retired partner’s client and administrative activities within the firm may be more than clearly insignificant and transitional;

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- the retired partner holds a direct or indirect financial interest in the firm, including share-based retirement income that may fluctuate with the firm's income; and
- the retired partner is held out to be a member of the firm through, for example, having a separate, identified office on the firm's premises, acting as its spokesperson or representative, using a firm business card or having a listing in the firm's telephone directory for other than a predetermined period of time following retirement.

When evaluating whether a retired partner has a close association with the firm, consideration should be given to how a reasonable observer would regard the association.

“network firm”

The references to “firms” and “network firms” in Rules 204.1 to 204.10 and this Guidance should be read as referring to those entities themselves and not to the persons who are partners or employees thereof.

Rules 204.1 to 204.4 and their Guidance bring the independence of a network firm into consideration when evaluating the independence of a member or firm for an assurance engagement. It is the member's or firm's responsibility to determine whether the network firm and its members have any interests or relationships or provide any services that would create threats to independence.

A firm may participate in a larger structure with other firms and entities to enhance its ability to provide professional services. Whether the agreements and relationships among the firms and entities that are part of such a larger structure are such that any of the firms or entities is a network firm depends on the particular facts and circumstances. The geographic location of the firms and entities, either within or outside of Canada, is irrelevant as to whether such a larger structure exists. Whether the firms and entities are legally separate from each other is not determinative, in and of itself, of whether such a larger structure exists.

Another firm or entity will not be considered to be network firm simply by virtue of the existence of one of the following arrangements between that other firm or entity and the firm itself:

- the sharing of costs that are immaterial to the firm that is performing the particular engagement;
- an association with the other firm or entity to provide a service or develop a product on a joint basis;
- co-operation to facilitate the referral of work or solely to respond jointly to a request for a proposal for the provision of a professional service;
- references on stationery or in promotional materials to an association with other firms or entities that does not constitute a larger structure of co-operating firms or entities as described in the definition of network firm; or
- the use of a common name when an agreement in relation to the sale of a component of a firm or entity provides that each of the transacting firms or entities may use the existing name for a limited period of time.

The definition of a network firm refers to co-operating entities that share significant professional resources. Shared professional resources may be considered to be significant where there is an exchange of people or information, such as where staff is drawn from a shared pool, or a common technical department is created within a larger structure to provide participating firms or entities with technical advice that they are required to follow. Shared professional resources will not be considered to be significant when they are limited to common audit methodology or audit manuals or a shared training endeavour, with no exchange of personnel or client or market information. Similarly, the sharing of costs limited only to the development of such common audit methodology, audit manuals or a shared training endeavour will not be considered to give rise to a network firm relationship.

“related entity”

For the purposes of Rules 204.1 to 204.10 “related entity” is a defined term that is dependent on the nature of the assurance engagement, the nature of the client and the relationship between the client and the other entity. The circumstances in which another entity is defined to be a related entity of an assurance client are outlined below:

Definition reference	Test	Reporting issuer or listed entity client	Audit or review client that is not a reporting issuer or listed entity	Non-audit, non-review assurance client
(a)(i) (b)(i) (c)(i)	The entity is controlled by the client.	Related	Related	Conditional*
(a)(ii)&(iii) (b)(ii)(A)&(B) (c)(ii)&(iii)	The entity has either control or significant influence over the client and the client is material to the entity.	Related	Conditional*	Conditional*
(a)(iv) (b)(ii)(C) (c)(iv)	The entity and the client are both controlled by a second entity and both the client and the first entity are material to the controlling second entity.	Related	Conditional*	Conditional*
(a)(v) (b)(ii)(D) (c)(v)	The entity is subject to significant influence by the client and the entity is material to the client.	Related	Conditional*	Conditional*

*An entity referred to in paragraphs (b)(ii)(A) to (D) and (c)(i) to (v) of the definition of “related entity”, as applicable, is a related entity if the engagement team knows or has reason to believe that an activity, interest or relationship involving the other entity is relevant to the evaluation of independence of the member or firm with respect to the assurance engagement. This condition is not intended to require the engagement team to undertake a search for such possible activities, interests or relationships with such entities.

In determining whether significant influence exists members should follow the guidance established in the *CPA Canada Handbook – Accounting*. Ideally, the client’s related entities and the interests and relationships that involve the related entities should be identified in advance.

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RULES:

Effective date and transitional provisions

A. Effective date

Rules 204.1 to 204.10 shall take effect:

- (a) for an assurance engagement in respect of a particular reporting period of a client, for the first reporting period commencing after December 15, 2014; and
- (b) for any other assurance engagement and an engagement to issue a report of the results of applying specified auditing procedures where the engagement is commenced after December 15, 2014,

subject to the following transitional provisions, as may be applicable.

B. Provision of litigation support services

The litigation services referred to in 204.4(29)(a) do not include a service that has not been completed before July 1, 2014 where:

- (a) there exists on June 30, 2014 a binding contract for the member or firm to provide the service; and
- (b) the provision of the service by the member or firm would not have contravened the provisions of Rule 204.1 as it read prior to July 1, 2014.

C. Key audit partner rotation

Notwithstanding the requirements of 204.4(20), where the application of the definition of “key audit partner” which takes effect pursuant to the effective date established by A. above has the effect of requiring the rotation of a person who would not have been subject to rotation based on the definition of “audit partner” in effect immediately prior to that effective date, that person may continue to participate in the audit of the financial statements of the particular client up to and including the second fiscal year of the client commencing after December 15, 2014.

D. Rule 204.6 - Breach of a provision of Rule 204.3 or 204.4

Rule 204.6 shall take effect:

- (a) for audit or review engagements for fiscal periods beginning after December 15, 2016; and
- (b) for any other assurance engagement and an engagement to issue a report of the results of applying specified auditing procedures where the engagement is commenced after December 15, 2016.

E. Rule 204.4(36.1)- Contingent Fees

Rule 204.4(36.1) shall take effect:

- (a) for audit or review engagements for fiscal periods beginning after December 15, 2016; and
- (b) for any other assurance engagement and an engagement to issue a report of the results of applying specified auditing procedures where the engagement is commenced after December 15, 2016.

GUIDANCE

- 1 Paragraph D above refers to an effective date of December 15, 2016 for Rule 204.6. – Breach of a provision of Rule 204.3 or 204.4. Until that Rule is effective, members and firms should continue to refer to the following pre-existing guidance in the CPA Code related to inadvertent breaches.

- **Guidance to Rule 204.1 to 204.3, paragraph 27;**

- 27 The ongoing evaluation and disposition of threats to independence should be supported by evidence obtained both before accepting an engagement and while it is being performed. The obligation to make such evaluation and take action arises when a member of a firm or network firm knows, or should reasonably be expected to know, of circumstances or relationships that might impair independence. There may be occasions when a member, a firm or a network firm is inadvertently in breach of a provision of this Rule. If such an inadvertent breach occurs, it would generally not impair independence for the purposes of Rules 204.1 to 204.10, provided the firm had appropriate quality control policies and procedures in place to promote independence and, once discovered, the breach was corrected promptly and any necessary safeguards were applied. An inadvertent breach would include a situation where the member did not know of the circumstances that created the breach.

• **Guidance to Rule 204.4(1) to (6), paragraph 11;**

- 11 An inadvertent breach of the provisions of Rules 204.4(1) to (6) and 204.4(10) to (12), would not impair the independence of the member of the firm or the firm when:
- the firm has established policies and procedures that require a network firm and all members of the firm to report promptly any breaches resulting from the purchase, inheritance or other acquisition of a financial interest in the assurance client;
 - the firm promptly notifies the network firm or the member of the firm that the financial interest should be disposed of; and
 - the disposal occurs at the earliest practical date after identification of the issue, but no later than 30 days after the person has both the knowledge of the financial interest and the right or ability to dispose of it, or the person is removed from the engagement team.

and

• **Guidance to Rule 204.4(14) and (15), paragraphs 7 and 8**

- 7 An inadvertent breach of the provisions of Rules 204.4(14) or (15) as they relate to family and personal relationships would not impair the independence of the member of the firm, or the firm, when:
- the firm has established policies and procedures that require all members of the firm to report promptly to the firm any breaches resulting from changes in the employment status of their immediate or close family members or other personal relationships that create a threat to independence;
 - either the responsibilities of the engagement team are restructured so that the person on the engagement team does not deal with matters that are within the responsibility of the person with whom he or she is related or has a personal relationship, or, if that is not possible, the firm promptly removes that person from the engagement team; and
 - additional care is given to reviewing the work of the particular person on the engagement team.
- 8 When an inadvertent breach of the provisions of Rules 204.4(14) or (15) relating to family and personal relationships has occurred, the firm should consider whether, and if so which, safeguards should be applied. Such safeguards might include:
- involving another member of the firm who is not, and never was, on the engagement team to review the work done by the person on the engagement team; or

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- excluding that person from any substantive decision-making concerning the assurance engagement.

Members, [candidates and students] are reminded that Rule 204.7 requires a member, [candidate or student] who has a relationship that is precluded by this Rule to advise in writing a designated partner of the firm of the relationship. Inadvertent breaches are also discussed in paragraph 27 of the Guidance to Rules 204.1 to 204.3.

- 2 Paragraph E above refers to an effective date of December 15, 2016 for Rule 204.4(36.1) – Independence - Contingent Fees. Members and firms should continue to refer to the provisions of Rules 215.1 and 215.2 and their related Guidance.

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RULES:

204.1 Assurance and Specified Auditing Procedures Engagements

A member or firm who engages or participates in an engagement:

- (a) to issue a written communication under the terms of an assurance engagement; or*
- (b) to issue a report on the results of applying specified auditing procedures;*

shall be and remain independent such that the member, firm and members of the firm shall be and remain free of any influence, interest or relationship which, in respect of the engagement, impairs the professional judgment or objectivity of the member, firm or a member of the firm or which, in the view of a reasonable observer, would impair the professional judgment or objectivity of the member, firm or a member of the firm.

204.2 Compliance with Rule 204.1

A member or firm who is required to be independent pursuant to Rule 204.1 shall, in respect of the particular engagement, comply with the provisions of Rules 204.3 and 204.4.

204.3 Identification of Threats and Safeguards

A member or firm who is required to be independent pursuant to Rule 204.1 shall, in respect of the particular engagement, identify threats to independence, evaluate the significance of those threats and, if the threats are other than clearly insignificant, identify and apply safeguards to reduce the threats to an acceptable level. Where safeguards are not available to reduce the threat or threats to an acceptable level, the member or firm shall eliminate the activity, interest or relationship creating the threat or threats, or refuse to accept or continue the engagement.

GUIDANCE - Rules 204.1 to 204.3

INTRODUCTION

- 1 It is a fundamental principle of the practice of Chartered Professional Accountancy that a member who provides assurance services shall do so with unimpaired professional judgment and objectivity, and shall be seen to be doing so by a reasonable observer. This principle is the foundation for public confidence in the reports of assurance providers.
- 2 The confidence that professional judgment has been exercised depends on the unbiased and objective state of mind of the reporting accountant, both in fact and appearance. Independence is the condition of mind and circumstance that would reasonably be expected to result in the application by a member of unbiased judgment and objective consideration in arriving at opinions or decisions in support of the member's report. A member or firm is not considered to be independent if the member or firm does not comply with the provisions of Rules 204.1 to 204.4.
- 3 Rule 204.1 provides that a member or firm who engages or participates in an engagement:
 - to issue a written communication under the terms of any assurance engagement; or
 - to issue a report on the results of applying specified auditing procedures;must be independent of the client. Independence requires the avoidance of situations which impair the professional judgment or objectivity of the member, firm or a member of the firm or which, in the view of a reasonable observer, would impair that professional judgment or objectivity.
- 4 Rule 204.2 provides that a member or firm, who is required to be independent pursuant to Rule 204.1 in respect of a particular engagement, must comply with Rules 204.3 and 204.4.

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- 5 Rule 204.3 provides that a member or firm must identify and evaluate threats to independence and, if they are not clearly insignificant, identify and apply safeguards to reduce them to an acceptable level. Where safeguards are not available to reduce the threats to an acceptable level the member or firm must eliminate the activity, interest or relationship creating the threats, or refuse to accept or continue the engagement.

Rule 204.4 describes circumstances and activities which members and firms must avoid when performing assurance and specified auditing procedure engagements because adequate safeguards will not exist that will, in the view of a reasonable observer, eliminate the threat or reduce it to an acceptable level, as required by Rule 204.3. The requirements to avoid these circumstances and activities are referred to as “prohibitions.”
- 6 Rule 204.5 requires the member or firm to document compliance with Rules 204.3, 204.4(24)(b), 204.4(34)(b), 204.4(35) and 204.4(40).
- 7 Rule 204.7 provides that a member or [candidate/student] must disclose breaches of the CPA Code to a designated partner in the firm. It also provides that, when a member or [candidate/student] has been assigned to an engagement team, the member or [candidate/student] must disclose to a designated partner any interest, relationship or activity that would preclude the member or [candidate/student] from being on the engagement team.
- 8 Rule 204.8 provides that a firm must ensure that members of the firm comply with Rule 204.4. The Rule provides that a firm may not permit any member of the firm to have a relationship with or an interest in an assurance client, or provide a service to an assurance client, which is precluded by Rule 204.
- 9 This Guidance describes a conceptual framework of principles that members and firms should use to identify threats to independence and evaluate their significance. If the threats are other than clearly insignificant, the member or firm should identify available safeguards. Some safeguards may already exist within the structure of the firm or the client, while others may be created by the action of the member, firm or client. Safeguards should be identified and, where applicable, applied to eliminate the threats or reduce them to an acceptable level. Members should exercise professional judgment to determine which safeguards to apply and whether the safeguards will permit the member or firm to accept or continue the engagement.
- 10 The effectiveness of safeguards largely depends on the culture of the particular firm. Therefore, the [Board/Council] encourages leaders of firms to stress the importance of compliance with Rule 204 and emphasize the expectation that members of the firm will act in the public interest. In doing so, firms should create and monitor effective policies and procedures designed to preserve the independence of the firm and its partners and employees when required by Rule 204.
- 11 The specific circumstances and examples presented herein are intended to illustrate the application of the principles; they are not, nor should they be interpreted as, an exhaustive list of all circumstances that may create a threat to independence. Consequently, it is not sufficient for a member or a firm merely to comply with the specific circumstances and examples presented. Rule 204.3 requires that they apply the principles to any particular circumstance encountered, whether or not the examples used in the Guidance, or the prohibitions set out in Rule 204.4, reflect those circumstances.
- 12 Specific circumstances and relationships that may create threats to independence are described together with safeguards that may be appropriate to eliminate the threats or

reduce them to an acceptable level in each circumstance. While the specific circumstances and examples relate to the audit or review of financial statements and other assurance engagements, they also apply to engagements to issue a report on the results of applying specified auditing procedures as required by Rule 204.1(b).

- 13** This Guidance sets out how, in the [Board's/Council's] opinion, a reasonable observer might view certain situations in the application of Rule 204.1 to 204.10. The reasonable observer is a hypothetical individual who has knowledge of the facts which the member knew or ought to have known, including the safeguards applied, and who applies judgment objectively, with integrity and due care. Members should also refer to the Preamble to the CPA Code, which provides the rationale for establishing the reasonable observer principle.
- 14** Members are reminded that for the purposes of Rules 204.1 to 204.10, independence includes both independence of mind and independence in appearance. As stated in Rule 204.1, independence requires the absence of any influence, interest or relationship which would impair the professional judgment or objectivity of the member or a member of the firm or which, in the view of a reasonable observer, would impair the professional judgment or objectivity of the member or a member of the firm. Frequently it is appearance of independence, or lack thereof, that poses the greatest challenge. In all situations, members should reflect on the wording of the Rule and Guidance to ensure compliance with the spirit and intent of the Rule and Guidance.
- 15** If, after considering the Rules and this Guidance, members are uncertain as to their correct application, they are encouraged to discuss the matter with partners, professional colleagues or [CPA Province/ Institute] staff. Members may also request the view of [name of appropriate committee].
- 16** Members should also be cognizant of any relevant Canadian or foreign legislation that may preclude a member from accepting or continuing an engagement. Members are cautioned that legislation under which corporations and other enterprises are incorporated or governed may impose differing requirements in respect of independence. Members should satisfy both the requirements of any governing legislation and the CPA Code.

THE FRAMEWORK

- 17** The objective of this Guidance is to assist members and firms in:
- identifying and evaluating threats to independence; and
 - identifying and applying appropriate safeguards to eliminate or reduce the threat or threats to an acceptable level in instances where their cumulative effect is not clearly insignificant.

This Guidance also describes those situations referred to in Rule 204.4 where safeguards are not available to reduce a threat or threats to an acceptable level, and the only possible actions are to eliminate the activity, interest or relationship creating them, or to refuse to accept or continue the assurance engagement.

- 18** The use of the word “independence” on its own may create misunderstandings. Standing alone, the word may suggest that a person exercising professional judgment ought to be free from all economic, financial and other relationships. This is impossible, as everyone has relationships with others. Therefore, members should evaluate the significance of economic, financial and other relationships in the light of what a reasonable observer would conclude to be acceptable in maintaining independence.

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- 19 In making this evaluation, many different circumstances may be relevant. Accordingly, it is impossible to define every situation that creates a threat to independence and specify the appropriate mitigating action. In addition, because of differences in the size and structure of firms, the nature of assurance engagements and client entities different threats may exist, that require the application of different safeguards. A conceptual framework that requires members and firms to identify, evaluate and address threats to independence, rather than merely comply with a set of specific and perhaps arbitrary rules, is, therefore, in the public interest.
- 20 Based on such an approach, this Guidance describes a conceptual framework of principles for compliance with Rules 204.1 to 204.10. Members, firms and network firms should use this conceptual framework to identify threats to independence, to evaluate their significance and, if they are other than clearly insignificant, to identify and apply safeguards to eliminate them or reduce them to an acceptable level, so that independence in fact and appearance are not impaired. In addition, consideration should be given to whether relationships between members of the firm who are not on the engagement team and the assurance client may also create threats to independence. Where safeguards are not available to reduce threats to an acceptable level, the member, firm or network firm should eliminate the activity, interest or relationship creating the threats, or the member or firm should refuse to accept or continue the particular engagement.
- 21 Rule 204.1 requires members and firms to be independent in fact and in appearance. The requirement to comply with the specific prohibitions set out in Rule 204.4 does not relieve a firm from complying with Rules 204.1 and 204.3 and the need to apply the conceptual framework and determine on a principles-based approach whether or not the firm is independent with respect to all assurance engagements, including audit and review engagements.
- 22 Rule 204.1 and, therefore, the principles in this Guidance apply to all assurance engagements and engagements to issue a report on the results of applying specified auditing procedures. The nature of the threats to independence and the applicable safeguards necessary to eliminate them or reduce them to an acceptable level will differ depending on the particulars of the engagement. Differences in threats and safeguards will arise, for example, if the engagement is an audit or review engagement or another type of assurance engagement; and, in the case of an assurance engagement that is not an audit or review engagement, in the purpose, subject matter and intended users of the report. Members and firms should, therefore, evaluate the relevant circumstances, the nature of the engagement and the entity, the threats to independence and the adequacy of available safeguards in deciding whether it is appropriate to accept or continue an engagement, and whether a particular person should be on the engagement team.
- 23 For audit clients and review clients, the persons on the engagement team, the firm and network firms should be independent of the client. In the case of an assurance engagement where the client is neither an audit nor a review client, those on the engagement team and the firm should be independent of the client. In addition, in the case of an engagement that is not an audit or review engagement, consideration should be given to any threats the firm has reason to believe may be created by the interests and relationships of network firms.

EXTENT OF APPLICATION OF REQUIREMENT FOR INDEPENDENCE FOR DIFFERENT TYPES OF ENGAGEMENTS

- 24 An engagement to report on the results of applying specified auditing procedures is not an assurance engagement as contemplated in the *CPA Canada Handbook – Assurance*. However, for the purposes of Rules 204.1 to 204.10 and this Guidance, the principles contained herein applicable to an assurance engagement, other than an audit or review engagement, also apply to an engagement to report on the results of applying specified auditing procedures. In so applying those principles, the reference to an assurance client is to be read as a reference to a client where the engagement is to report on the results of applying specified auditing procedures.
- 25 In the case of an assurance report to an assurance client that is not an audit client or a review client where the report is intended only for the use of identified users, as contemplated by the *CPA Canada Handbook – Assurance*, the users of the report are considered to be knowledgeable as to the purpose, subject matter and limitations of the report. Users gain such knowledge through their participation in establishing the nature and scope of the member's or firm's engagement, including the criteria by which the particular subject matter is to be evaluated. The member's or firm's knowledge and enhanced ability to communicate about safeguards with all the report's users increase the effectiveness of safeguards to independence in appearance. Therefore, the member or firm may take these circumstances into account when evaluating the threats to independence and considering the applicable safeguards necessary to eliminate them or reduce them to an acceptable level. With respect to network firms, limited consideration of any threats created by their interests and relationships may be sufficient.
- 26 The effect of Rules 204.1 to 204.8 is that:
- for an assurance engagement for a client that is an audit or review client, those on the engagement team, the firm and network firms are required to be independent of the client;
 - for an assurance engagement for a client that is not an audit or review client, when the assurance report is not intended only for the use of identified users, those on the engagement team and the firm are required to be independent of the client; and
 - for an assurance engagement for a client that is not an audit or review client, when the assurance report is intended only for the use of identified users, those on the engagement team are required to be independent of the client. In addition, the firm should not have a material direct or indirect financial interest in the client.

EVALUATING THREATS AND SAFEGUARDS

- 27 The ongoing evaluation and disposition of threats to independence should be supported by evidence obtained both before accepting an engagement and while it is being performed. The obligation to make such evaluation and take action arises when a member of a firm or network firm knows, or should reasonably be expected to know, of circumstances or relationships that might impair independence.
- 28 Rule 204.4 describes activities, interests or relationships that create threats to independence that are so significant that there are no safeguards available to reduce them to an acceptable level and, accordingly, prohibits the provision of assurance services, as specified, in conjunction with such activities, interests or relationships. Rules 204.1 to 204.7 and this Guidance also describe the threats to independence and analyze safeguards that may be capable of eliminating them or reducing them to an acceptable level. They conclude with

some examples of how the conceptual framework to independence is to be applied to specific circumstances and relationships and the relevant threats and safeguards. The examples are not all inclusive. Professional judgment should be used to determine whether appropriate safeguards exist to eliminate all threats to independence or to reduce their cumulative effect to an acceptable level. In some examples, it may be possible to eliminate the threat or reduce it to an acceptable level by the application of safeguards. In some other examples, the threat or threats to independence will be so significant that the only possible actions are to eliminate the activity, interest or relationship creating the threat or threats, or to refuse to accept or continue the engagement

- 29 When a member or firm identifies a threat to independence that is not clearly insignificant, and the member or firm decides to apply appropriate safeguards and accepts or continues the assurance engagement, the decision should be documented in accordance with Rule 204.5. The documentation should include the following information:
- a description of the nature of the engagement;
 - the threat identified;
 - the safeguard or safeguards identified and applied to eliminate the threat or reduce it to an acceptable level; and
 - an explanation of how, in the member or firm's professional judgment, the safeguards eliminate the threat or reduce it to an acceptable level.

THREATS TO INDEPENDENCE

- 30 Independence is potentially affected by self-interest, self-review, advocacy, familiarity and intimidation threats. The mere existence of such threats does not *per se* mean that the performance of a prospective engagement is precluded. The undertaking or continuation of an engagement is only precluded where safeguards are not available to eliminate or reduce the threats to an acceptable level or where Rule 204.4 provides a specific prohibition.

Self-Interest Threats

- 31 A self-interest threat occurs when a firm or a person on the engagement team could benefit from a financial interest in, or other self-interest conflict with, an assurance client. Examples of circumstances that may create a self-interest threat include, but are not limited to:
- a direct financial interest or material indirect financial interest in an assurance client;
 - a loan or guarantee to or from an assurance client or any of its directors or officers;
 - dependence by a firm, office or member on total fees from an assurance client;
 - undue concern about the possibility of losing the engagement;
 - evaluating performance or providing compensation for selling non-audit services to an assurance client;
 - having a close business relationship with an assurance client; and
 - potential employment with an assurance client.

Self-Review Threats

- 32 A self-review threat occurs when any product or judgment from a previous engagement needs to be evaluated in reaching a conclusion on the particular assurance engagement, or when a person on the engagement team was previously an officer or director of the client, or was in a position to exert significant influence over the subject matter of the assurance engagement. Examples of circumstances that may create a self-review threat include, but are not limited to:
- a person on the engagement team being, or having recently been, an officer or director of the client;
 - a person on the engagement team being, or having recently been, an employee of the assurance client in a position to exert significant influence over the subject matter of the

- assurance engagement, or another person having the duties or responsibilities normally associated with such an employee;
- a member or firm performing services for an assurance client that directly affect the subject matter of the engagement; and
- a member or firm preparing original data used to generate financial statements or preparing other records that are the subject matter of the engagement.

Advocacy Threats

- 33** An advocacy threat occurs when a firm, or a person on the engagement team, promotes, or may be perceived to promote, an assurance client's position or opinion to the point that objectivity may be, or may be perceived to be, impaired. Such would be the case if a person on the engagement team were to subordinate his or her judgment to that of the client, or the firm were to do so. Examples of circumstances that may create an advocacy threat include, but are not limited to:
- dealing in, or being a promoter of, shares or other securities of an assurance client; and
 - acting as an advocate for or on behalf of an assurance client in litigation or in resolving disputes with third parties.

Familiarity Threats

- 34** A familiarity threat occurs when, by virtue of a close relationship with an assurance client, its directors, officers or employees, a firm or a person on the engagement team becomes too sympathetic to the client's interests. Examples of circumstances that may create a familiarity threat include, but are not limited to:
- a person on the engagement team having an immediate or close family member who is an officer or director of the assurance client;
 - a person on the engagement team having an immediate or close family member who is in a position to exert significant influence over the subject matter of the assurance engagement;
 - a former partner of the firm being an officer or director of the assurance client or in a position to exert significant influence over the subject matter of the assurance engagement;
 - the long association of a senior person on the engagement team with the assurance client; and
 - the acceptance of gifts or hospitality from the assurance client, its directors, officers or employees, unless the value thereof is clearly insignificant.

Intimidation Threats

- 35** An intimidation threat occurs when a person on the engagement team may be deterred from acting objectively and exercising professional skepticism by threats, actual or perceived, from the directors, officers or employees of an assurance client. Examples of circumstances that may create an intimidation threat include, but are not limited to:
- the threat of being replaced due to a disagreement with the application of an accounting principle; and
 - the application of pressure to inappropriately reduce the extent of work performed in order to reduce or limit fees.

SAFEGUARDS

- 36** Members and firms have an ongoing responsibility to comply with Rules 204.1 to 204.7 by taking into account the context in which they practise, the threats to independence and the safeguards which may be available to eliminate the threats or reduce them to an acceptable level. Safeguards fall into three broad categories:
- safeguards created by the profession, legislation or regulation;

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- safeguards within the assurance client; and
 - safeguards within the firm's own systems and procedures.
- 37** Safeguards created by the profession, legislation or regulation include the following:
- education, training and practical experience requirements for entry into the profession;
 - continuing education programs;
 - professional standards;
 - external practice inspection;
 - disciplinary processes;
 - members' practice advisory services;
 - participation by members of the public in oversight and governance of the profession; and
 - legislation governing the independence requirements of the firm and its members.
- 38** Safeguards within the assurance client may include the following:
- employees of the client who are competent to make management decisions;
 - policies and procedures that emphasize the client's commitment to fair financial reporting;
 - internal procedures that ensure objective choices in commissioning non-assurance engagements; and
 - an audit committee that provides appropriate oversight and communications regarding a firm's services.
- However, it is not possible to rely solely on safeguards within the assurance client to reduce threats to an acceptable level.
- 39** Where an audit committee does not exist, as is set out in the definition of "audit committee", references in the CPA Code to an audit committee should be interpreted to refer to another governance body which has the duties and responsibilities normally granted to an audit committee or to those charged with governance for the entity. In some cases, this role may be filled by client management personnel. The *CPA Canada Handbook – Assurance* requires members and firms to determine the appropriate person or persons within the entity's governance structure with whom to communicate and establishes requirements for communication on matters relating to independence with such a person or persons.
- 40** Safeguards within the firm's own systems and procedures may include firm-wide safeguards such as the following:
- firm leadership that stresses the importance of independence and the expectation that persons on engagement teams will act in the public interest;
 - policies and procedures to implement and monitor quality control of assurance engagements;
 - documented independence policies regarding the identification of threats to independence, the evaluation of their significance and the identification and application of appropriate safeguards to eliminate or reduce the threats, other than those that are clearly insignificant, to an acceptable level;
 - internal policies and procedures, including annual reporting by members of the firm, to monitor compliance with firm policies and procedures as they relate to independence;
 - policies and procedures that will enable the identification of interests or relationships between the firm or those on the engagement team and assurance clients;
 - policies and procedures to monitor and manage the reliance on revenue received from a single assurance client;
 - internal performance measures that do not put excessive pressure on partners to

generate non-assurance revenue from their assurance clients and do not over emphasize budgeted hours;

- using different partners and teams with separate reporting lines for the provision of non-assurance services to an assurance client;
- policies and procedures to prohibit members of the firm who are not on the engagement team from influencing the outcome of the assurance engagement;
- timely communication of a firm's policies and procedures, and any changes thereto, to all members of the firm, including appropriate training and education thereon;
- designating a member of the firm's senior management as responsible for overseeing the adequate functioning of the safeguarding system;
- means of advising all members of the firm of those clients and related entities from which they should be independent;
- an internal disciplinary mechanism to promote compliance with firm policies and procedures; or
- policies and procedures that empower members of the firm to communicate, without fear of retribution, to senior levels within the firm any issue of independence and objectivity that may concern them.

41 Safeguards within the firm's own systems and procedures may include engagement-specific safeguards such as the following:

- involving another person to review the work done or advise as necessary. This person could be someone from outside the firm or network firm, or someone from within who was not otherwise associated with the engagement team. The person should be independent of the assurance client and will not, by reason of the review performed or advice given, be considered to be on the engagement team;
- consulting a third party, such as a committee of independent directors, a professional regulatory body or a professional colleague;
- rotating senior personnel on the engagement team;
- discussing independence issues with the audit committee;
- disclosing to the audit committee, the nature of services provided and extent of fees charged;
- policies and procedures designed to ensure that persons on the engagement team do not make, or assume responsibility for, management decisions for the client;
- involving another firm to perform or re-perform part of the assurance engagement;
- involving another firm to re-perform the non-assurance service; or
- removing a person from the engagement team, when that person's financial interests, relationships or activities create a threat to independence.

PRACTITIONERS WITH SMALL OR OWNER-MANAGED CLIENTS

42 The size and structure of the firm and the nature of the assurance client and the engagement will affect the type and degree of the threats to independence and, consequently, the types of safeguards appropriate to eliminate such threats or reduce them to an acceptable level. For example, it is understood that not all the safeguards noted in paragraphs 39 to 42 of the Guidance to Rules 204.1 to 204.3 will be available to the sole practitioner or small firm or within smaller clients such as owner-managed entities. Smaller clients often rely on members to provide a broad range of accounting and business services. Independence will not be impaired provided such services are not specifically prohibited by Rule 204.4 and provided safeguards are applied to reduce any threat to an acceptable level. In many circumstances, explaining the result of the service and obtaining client approval and acceptance for the result of the service will be an appropriate safeguard for such smaller entities. Similarly, such clients often have a long-standing relationship with an individual who is a sole practitioner or partner from a firm. Independence will not be impaired provided safeguards are applied to

reduce any familiarity threat to an acceptable level. In most circumstances, periodic external practice inspection and, where appropriate, consultation will reduce any threat to independence to an acceptable level.

APPLICATION OF THE FRAMEWORK

- 43** Rule 204 and its related Guidance describe the application of the framework to specific circumstances and relationships that may create threats to independence. The provisions describe potential threats created and safeguards that may be appropriate to eliminate the threats or reduce them to an acceptable level. The circumstances that are described are not intended to be comprehensive or all-inclusive. In practice, when independence is required, members and firms should assess the implications of all circumstances and relationships and, where required, assess those of network firms, to determine whether there are threats to independence that are other than clearly insignificant and, if they exist, whether safeguards can be applied to satisfactorily address them. In situations where safeguards are not available to reduce a threat or threats to an acceptable level, the only possible actions are to eliminate the activity, interest or relationship creating the threats, or to refuse to accept or continue the assurance engagement.

Rebuttable presumption – not subject to audit procedures

- 44** Rules 204.4(24) to (28) set out non-audit services that may not be provided during either the period covered by the financial statements subject to audit or during the engagement period to an audit client that is a reporting issuer or listed entity unless it is reasonable to conclude that the results of any such service will not be subject to audit procedures during the audit of the client's financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of such services will be subject to audit procedures. Materiality is not an appropriate basis upon which to overcome this presumption. For example, determining whether a subsidiary, division or other unit of the consolidated entity is material is a matter of audit judgment. Therefore, the determination of whether to apply detailed audit procedures to a unit of a consolidated entity is, in itself, an audit procedure.

Other specific threats

- 45** Rule 204.3 sets out the general requirement to identify and evaluate threats and either apply safeguards or decline an engagement. Rule 204.4 sets out prohibitions in relation to specific circumstances and relationships. There are also some circumstances and relationships that have been specifically identified as creating threats to independence and, accordingly, require an evaluation of their significance and the application of appropriate safeguards. Paragraphs 46 to 50 discuss those specific circumstances and relationships.

Provision of non-assurance services to an assurance client

- 46** Firms have traditionally provided to their clients a range of non-assurance services that are consistent with their skills and expertise. The provision of such a non-assurance service is not subject to the requirements of Rule 204.1 and, accordingly, does not require independence on the part of a member or firm. However, the provision of such a non-assurance service may create a self-interest, self-review or advocacy threat that impacts the independence of the member or firm with respect to the provision of an assurance or specified auditing procedures service for which independence is required by Rule 204.1. Consequently, before a firm accepts an engagement to provide a non-assurance service, it should evaluate the significance of any threat to independence, in relation to an existing assurance service, that may be created by providing the non-assurance service. When such a threat is other than clearly insignificant, the non-assurance engagement should be declined unless appropriate safeguards can be applied to eliminate the threat or threats or reduce them to an acceptable level. Specific circumstances in which adequate safeguards do not exist to eliminate or reduce such a threat to independence to an acceptable level are set out

in Rules 204.4(22) to (34) as prohibitions.

- 47** Subject to the specific prohibitions set out in Rules 204.4(22) to (34), a firm or a member of a firm may provide a non-assurance service to an assurance client or related entity, provided that any threats to independence have been reduced to an acceptable level by safeguards, such as:
- policies and procedures to prohibit members of the firm from making management decisions for the client, or assuming responsibility for such decisions;
 - discussing independence issues related to the provision of non-assurance services with the audit committee;
 - policies within the assurance client regarding the oversight responsibility for provision of non-assurance services by the firm;
 - involving another member of the firm who is not on the engagement team to advise on any impact of the non-assurance service on the independence of the persons on the engagement team and the firm;
 - involving a professional accountant from outside of the firm to provide assurance on a discrete aspect of the assurance engagement;
 - obtaining the client's acknowledgement of responsibility for the results of the non-assurance service performed by the firm;
 - disclosing to the audit committee the nature of the non-assurance service and extent of fees charged; or
 - arranging that the members of the firm providing the non-assurance service do not participate on the assurance engagement team.

48 *Intentionally left blank.*

Actual or threatened litigation

- 49** Actual, threatened or prospective litigation between a firm or a member of an engagement team and the assurance client or a shareholder or creditor of the client may create a self-interest or intimidation threat. The relationship between client management and persons on the engagement team should be characterized by complete candour and full disclosure regarding all aspects of the client's business operations and all matters relevant to the client's financial statements. The firm and the client's management may be placed in adversarial positions by actual, threatened or prospective litigation, which could impair complete candour and full disclosure, and in this, or other ways, the firm may face a self-interest or intimidation threat. The significance of the threat will depend upon such factors as:
- the materiality of the litigation;
 - the nature of the assurance engagement;
 - the stage of the litigation; and
 - whether the litigation relates to a prior assurance engagement.

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

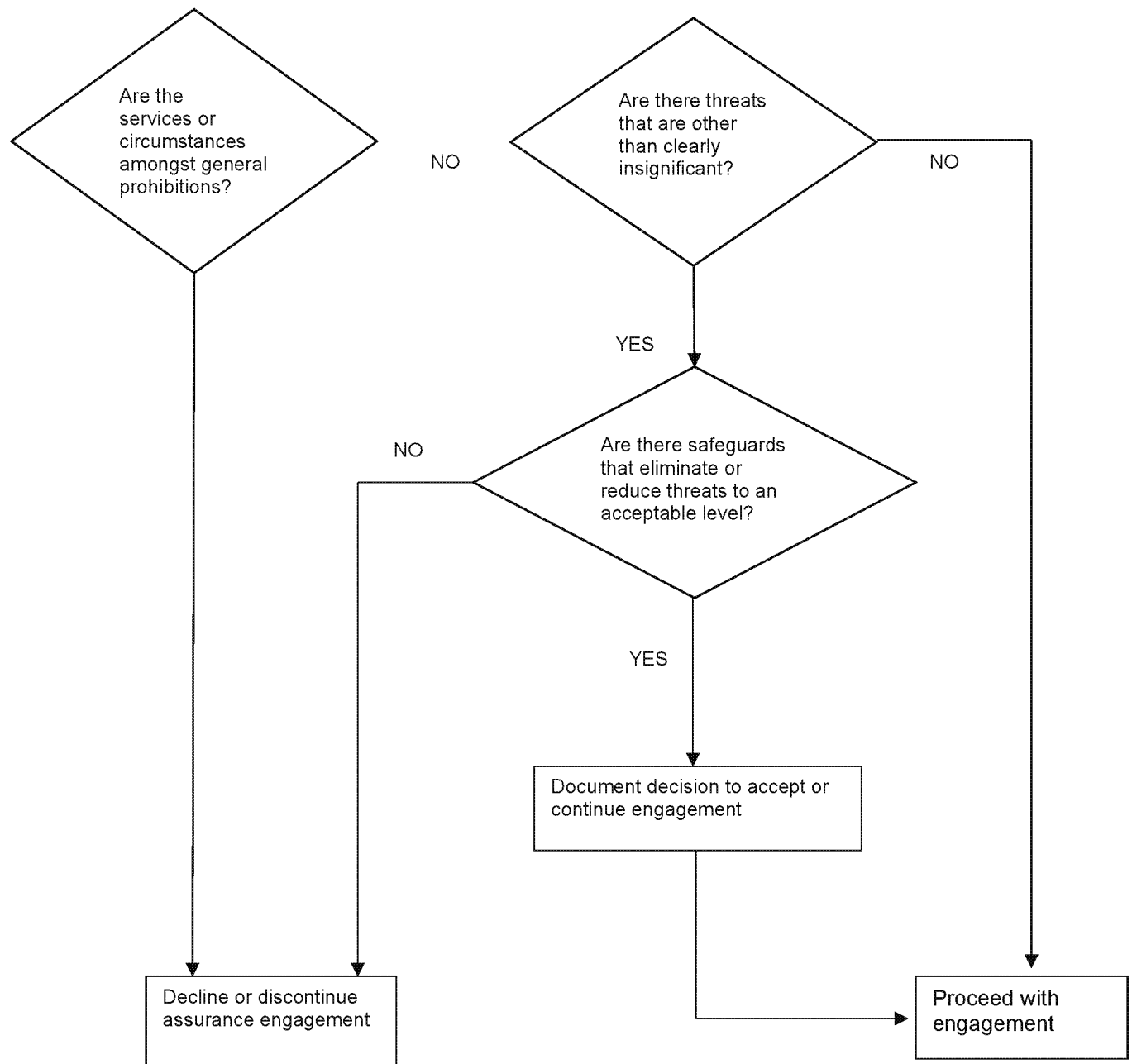
- disclosing to the audit committee the extent and nature of the litigation;
- removing from the engagement team any person involved in the litigation; or
- involving an additional member of the firm who is not part of the engagement team to review the work done or advise as necessary.

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

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- 50** Members are cautioned that actual litigation often results in a conflict of interest between the client and the member or firm which will preclude the member or firm from continuing to provide professional services to the client. Threatened or prospective litigation can have the same result. When faced with threatened, prospective or actual litigation, members and firms should refer to Rule 210 and the related Guidance, and consult with their legal counsel, to determine whether they can continue to provide professional services to the client and, if so, whether there are particular arrangements which should be made with the client.

OVERVIEW OF INDEPENDENCE STANDARD FOR ASSURANCE ENGAGEMENT — FLOWCHART



204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Financial interests

- (1)(a) A member, [candidate or student] shall not participate on the engagement team for an assurance client if the member, [candidate or student], or an immediate family member of the member, [candidate or student], holds a direct financial interest or a material indirect financial interest in the client.
- (b) A member, [candidate or student] shall not participate on the engagement team for an assurance client if the member, [candidate or student], or an immediate family member of the member, [candidate or student], holds, as trustee, a direct financial interest or a material indirect financial interest in the client.
- (1.1) Notwithstanding Rules 204.4(1)(a) and (b), if the assurance client is a co-operative, credit union or caisse populaire; a social club, such as a golf club or curling club; or a similar organization, the financial interest in the assurance client held, either personally or as a trustee, by a member, [candidate or student] or an immediate or close family member of the member, [candidate or student] shall not preclude the member, [candidate or student] from participating on the engagement team provided that:
- (a) such a financial interest is restricted to the minimum amount that is a prerequisite of membership;
 - (b) the assets of the organization cannot by virtue of the organization's by-laws be distributed to the individual members of the organization other than as patronage dividends or in circumstances of forced liquidation or expropriation, unless there is a written undertaking with the organization to forfeit entitlement to such distributed assets; and
 - (c) the member, [candidate or student] or immediate or close family member:
 - (i) does not serve on the governing body or as an officer of the organization;
 - (ii) does not have the right or responsibility to exercise significant influence over the financial or accounting policies of the organization or any of its associates;
 - (iii) does not exercise any right derived from membership to vote at meetings of the organization; and
 - (iv) cannot dispose of the financial interest for gain.
- (2)(a) A member or firm shall not perform an assurance engagement for an entity if the member or firm holds a direct financial interest or material indirect financial interest in the entity.
- (b) A member or firm shall not perform an audit or review engagement for an entity if the member, firm or a network firm, has a direct financial interest or a material indirect financial interest in the entity.
- (2.1) Notwithstanding Rules 204.4(2)(a) and (b), if an assurance client is a co-operative, credit union or caisse populaire; a social club, such as a golf club or curling club; or a similar organization, the financial interest in the entity held by a member or firm, or in the case of an audit or review engagement, a member, firm or a network firm, shall not preclude the member or firm from performing an assurance or audit or review engagement, as the case may be, for the entity provided that:
- (a) such a financial interest is restricted to the minimum amount that is a prerequisite of membership;
 - (b) the assets of the organization cannot by virtue of the organization's by-laws be distributed to the individual members of the organization other than as patronage dividends or in circumstances of forced liquidation or expropriation, unless there is a written undertaking with the organization to forfeit entitlement to such distributed assets; and

- (c) *the member, firm or network firm, as the case may be:*
 - (i) *does not serve on the governing body or as an officer of the organization;*
 - (ii) *does not have the right or responsibility to exercise significant influence over the financial or accounting policies of the organization or any of its associates;*
 - (iii) *does not exercise any right derived from membership to vote at meetings of the organization; and*
 - (iv) *cannot dispose of the financial interest for gain.*
- (3) *A member or firm shall not perform an audit or review engagement for an entity if a pension or other retirement plan of the firm or network firm has a direct financial interest or a material indirect financial interest in the entity.*
- (4) *A member who is a partner of a firm and who holds, or whose immediate family member holds, a direct financial interest or a material indirect financial interest in an audit or review client shall not practise in the same office as the lead engagement partner for the client, unless, in the case of a financial interest held by an immediate family member, the financial interest is received as a result of employment and*
 - (a) *the immediate family member does not have the right to dispose of the financial interest or, in the case of a share option, the right to exercise the option; or*
 - (b) *where such rights are obtained, the financial interest is disposed of as soon as is practicable.*
- (5)(a) *A member who is a partner or managerial employee of a firm and who holds a direct financial interest or a material indirect financial interest in an audit or review client shall not provide a non-assurance service to the client, unless the non-assurance service is clearly insignificant.*
- (b) *A member who is a partner or managerial employee of a firm whose immediate family member holds a direct financial interest or a material indirect financial interest in an audit or review client shall not provide a non-assurance service to the client, unless*
 - (i) *the non-assurance service is clearly insignificant; or*
 - (ii) *the financial interest is received as a result of employment and*
 - (A) *the immediate family member does not have the right to dispose of the financial interest or, in the case of a share option, the right to exercise the option; or*
 - (B) *where such rights are obtained, the financial interest is disposed of as soon as is practicable.*
- (6)(a) *A member or firm shall not perform an audit or review engagement for an entity (the first entity) if the firm or a network firm has a financial interest in a second entity, and the member or firm knows that the first entity or a director, officer or controlling owner of the first entity also has a financial interest in the second entity, unless the respective financial interests of the firm or network firm and the first entity, the director, officer or controlling owner of the first entity are immaterial and the first entity cannot exercise significant influence over the second entity.*
- (b) *A member, [candidate or student] shall not participate on the engagement team for an audit or review client if the member or student or an immediate family member of the member, [candidate or student] has a financial interest in an entity and the member, [candidate or student] knows that the client or a director, officer or controlling owner of the client also has a financial interest in the entity, unless the respective financial interests of the member, [candidate or student], or immediate family member, and the client, the director, officer or controlling owner of the client are immaterial and the client cannot exercise significant influence over the entity.*

GUIDANCE - Rule 204.4(1) to (6)

- 1 A financial interest in an assurance client may create a self-interest threat. In evaluating the significance of the threat, and the appropriate safeguards to be applied to eliminate the threat or reduce it to an acceptable level, it is necessary to examine the nature of the financial interest. This includes an evaluation of the role of the person holding the financial interest, whether that interest is material and whether it is direct or indirect.
- 2 Financial interests may be held through an intermediary such as 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 such control or ability exists, that financial interest is a direct financial interest. Conversely, when such control or ability does not exist, such a financial interest is an indirect financial interest.
- 3 In the application of Rules 204.4(1) to (12) to an assurance, audit or review client the reference to an assurance, audit or review client, a client or an entity includes related entities, as defined, of the assurance, audit or review client, client or entity, as the case may be.

Assurance clients

- 4 A reasonable observer will not view a member or [candidate or student] who holds a direct financial interest or material indirect financial interest as a trustee differently than someone who holds the interest beneficially. Accordingly Rule 204.4(1) applies to members, [candidates, students] and immediate family members of members, [candidates or students] who hold a direct financial interest or material indirect financial interest in the capacity of a trustee.
- 5 When a person on an engagement team, or any of the person's immediate family members, receives, for example, by way of gift or inheritance, a direct financial interest or a material indirect financial interest in an assurance client, or a related entity, one of the following actions should be taken to comply with Rule 204.4(1):
 - dispose of the financial interest at the earliest practical date but no later than 30 days after the person has knowledge of the financial interest and the right or ability to dispose of it; or
 - remove the person from the engagement team.

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

- discussing the matter with the audit committee; or
- involving another member of the firm who is not, and has not been, on the engagement team to review the work done by the person, or advise as necessary.

Members, [candidates and students] are reminded that Rule 204.6 requires a member, [candidate or student] who has an interest that is precluded by this Rule to advise in writing a designated partner of the firm of the interest. When a financial interest in an assurance client or related entity is acquired as a result of a merger or acquisition, the provisions of Rule 204.4(40) apply.

- 6 When a person on an engagement team knows that a close family member has a direct financial interest or a material indirect financial interest in the assurance client, or a related

entity, a self-interest threat may exist. In evaluating the significance of any such threat, consideration should be given to the nature of the relationship between the person on the engagement team and the close family member and the materiality of the financial interest. Once the significance of the threat has been evaluated, safeguards should be applied. Such safeguards might include:

- the close family member disposing of all or a sufficient portion of the financial interest at the earliest practical date;
- discussing the matter with the audit committee;
- involving another member of the firm who is not, and never was, on the engagement team to review the work done by the particular person on the engagement team or advise as necessary; or
- removing the person from the engagement team.

7 Consideration should be given to whether a self-interest threat may exist because of the financial interests of individuals other than those on the engagement team and their immediate and close family members. Such individuals would include:

- a member of the firm who provides a non-assurance service to the assurance client;
- a member of the firm who has a close personal relationship with a person on the engagement team;
- a spouse or dependant of an immediate or close family member of a person on the engagement team; and
- an individual for whom a member of the engagement team holds power of attorney.

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

- the firm's organizational, operating and reporting structure;
- the nature of the relationship between the individual and the person on the engagement team; and
- in the case of a power of attorney, the degree of decision making power granted by the power of attorney.

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

- where appropriate, policies to prohibit such individuals from holding such interests;
- discussing the matter with the audit committee; or
- involving another member of the firm who is not, and never was, on the engagement team to review the work done by the particular individual or advise as necessary.

8 The specific prohibitions of Rule 204.4 do not preclude a firm from accepting an assurance engagement with an entity if one or more partners of the firm who do not participate on the engagement team, and who do not practice in the same office as the lead engagement partner, have a financial interest in the entity. However, Rule 204.1 requires the firm to be independent in fact and appearance and requires the firm to identify threats to independence arising from such circumstances, evaluate the significance of the threats and, if they are other than clearly insignificant, apply safeguards to reduce the threats to an acceptable level. If adequate safeguards are not available the firm should not accept the engagement.

Assurance clients that are not audit or review clients

9 With respect to an assurance report for an assurance client that is not an audit client or a review client where the report is intended only for the use of identified users, as contemplated by the *CPA Canada Handbook – Assurance*, members are referred to the

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provisions in paragraph 26 of the Guidance to Rules 204.1 to 204.3.

Audit or review clients

- 10** Rule 204.4(4) refers to the office in which the lead engagement partner practices in connection with an audit or review engagement. Such an office is not necessarily the office to which that partner is ordinarily assigned. Accordingly, for the purposes of Rule 204.4(4) and this Guidance, when the lead engagement partner is located in a different office from others on the engagement team, professional judgment should be exercised to determine in which office the partner practices in connection with the audit or review engagement.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Loans and guarantees**

- (10)(a) *A member or firm shall not perform an assurance engagement for a client if the firm, or a network firm in the case of an audit or review client, has a loan from or has a loan guaranteed by the client, except when the client is a bank or similar financial institution and the loan or guarantee is immaterial to the firm, the network firm, and the client, and the loan or guarantee is made under normal commercial terms and conditions and is in good standing.*
- (b) *A member or firm shall not perform an assurance engagement for a client that is not a bank or similar financial institution if the firm, or a network firm in the case of an audit or review client, has a loan to the client.*
- (c) *A member or firm shall not perform an assurance engagement for a client if the firm, or a network firm in the case of an audit or review client, guarantees a loan of the client.*
- (11)(a) *A member or firm shall not perform an assurance engagement for a client if the firm, or a network firm in the case of an audit or review client, has a loan from or has a loan guaranteed by:*
- (ii) an officer or director of the assurance client; or*
 - (iii) a shareholder of the assurance client who owns more than 10% of the equity securities of the client, unless the shareholder is a bank or similar financial institution and the loan or guarantee is made under normal commercial terms and conditions.*
- (b) *A member or firm shall not perform an assurance engagement for a client if the firm, or a network firm in the case of an audit or review client, has a loan to or guarantees a loan of:*
- (i) an officer or director of the assurance client; or*
 - (ii) a shareholder of the assurance client who owns more than 10% of the equity securities of the client.*
- (12)(a) *A member, [candidate or student] shall not participate on the engagement team for an assurance client where the member, [candidate or student] has a loan from or has a loan guaranteed by:*
- (i) such a client, except a client that is a bank or similar financial institution where the loan or guarantee is made under normal commercial terms and conditions and the loan is in good standing;*
 - (ii) an officer or director of the client; or*
 - (iii) a shareholder of the client who owns more than 10% of the equity securities of the client, unless the shareholder is a bank or similar financial institution and the loan or guarantee is made under normal commercial terms and conditions.*
- (b) *A member, [candidate or student] shall not participate on the engagement team for an assurance client where the member, [candidate or student] has a loan to or guarantees the borrowing of:*
- (i) such a client that is not a bank or similar financial institution;*
 - (ii) an officer or director of the client; or*
 - (iii) a shareholder of the client who owns more than 10% of the equity securities of the client.*

GUIDANCE - Rule 204.4(10) to (12)

- 1** A loan from, or a loan guaranteed by, an assurance client that is a bank or a similar financial institution to a person on the engagement team or his or her immediate family member would not create a threat to independence provided the loan or guarantee is made under normal commercial terms and conditions and is in good standing. Examples of such loans include home mortgages, bank overdrafts, car loans and credit card balances.
- 2** Similarly, deposits or brokerage accounts of a firm or a person on the engagement team with an assurance client that is a bank, broker or similar financial institution would not create a threat to independence provided the deposit or brokerage account was held under normal commercial terms and conditions.
- 3** Rules 204.4(10) and (11) relate to loans and guarantees between a firm and an assurance client. In the case of an assurance client that is an audit or review client, the provisions of Rules 204.4(10) and (11) also apply to network firms. In all cases the provisions of Rule 204.4(10), (11) and (12) should be read as applying also to related entities of the client.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Close business relationships

- (13)(a) *A member or firm shall not perform an audit or review engagement for an entity if the firm, or a network firm, has a close business relationship with the entity, a related entity or the management of either, unless the close business relationship is limited to a financial interest that is immaterial and the relationship is clearly insignificant to the firm or network firm and either entity or its management, as the case may be.*
- (b) *A member or firm shall not perform an assurance engagement that is not an audit or review engagement if the firm has a close business relationship with the assurance client, a related entity or the management of either unless the close business relationship is limited to a financial interest that is immaterial and the relationship is clearly insignificant to the firm and the client, the related entity or the management of either, as the case may be.*
- (c) *A member, [candidate or student] who has, or whose immediate family member has a close business relationship with an assurance client, a related entity or the management of either shall not participate on the engagement team for the client unless the close business relationship is limited to a financial interest that is immaterial and the relationship is clearly insignificant to the member, [candidate, student] or immediate family member and the client, the related entity or the management of either, as the case may be.*

GUIDANCE - Rule 204.4(13)

- 1 A close business relationship between a firm, a network firm or a person on the engagement team and the assurance client or its management, involving a common commercial or financial interest may create a self-interest or an intimidation threat. Members and firms should also consider whether such threats may be created by close business relationships with a related entity or its management. The following are examples of such relationships:
- (a) having a material financial interest in a joint venture with the client or a controlling owner, director, officer or other individual who performs senior management functions for that client;
 - (b) arrangements to combine one or more services or products of the firm with one or more services or products of the client and to market the package with reference to both parties; and
 - (c) arrangements under which either the firm or the client acts as a distributor or marketer of the other's products or services.
- A close business relationship does not include the relationship created by the professional engagement between the client and the member, the firm, or the network firm as the case may be.
- 2 In the case of an audit or review client, a business relationship involving an interest held by a firm, a network firm or a person on the engagement team or any of that person's immediate family members in a closely held entity in which the client or a director or officer of the client, or any group thereof, also has an interest, does not create threats to independence provided:
- the relationship is clearly insignificant to the firm, the network firm and the client;
 - the interest held is immaterial to the investor, or group of investors; and
 - the interest does not give the investor, or group of investors, the ability to control the closely held entity.
- 3 The purchase of goods or services from an assurance client by a firm (and, in the case of an

audit client, by a network firm) or a person on the engagement team will not generally create a threat to independence, provided the transaction is conducted in the normal course of the client's business and on an arm's length basis. However, such a transaction may be of a nature or magnitude such that it does create a self-interest threat. If the threat so created is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level. Such safeguards might include:

- reducing the magnitude of or eliminating the transaction;
- removing the individual involved from the engagement team; or
- discussing the issue with the audit committee.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Family and personal relationships

- (14) A member, [candidate or student] shall not participate on the engagement team for an assurance client if the member's, [candidate's or student's] immediate family member is an officer or director of the client or a related entity or is in a position to exert significant influence over the subject matter of the engagement, or was in such a position during the period covered by the assurance report or the engagement period.
- (15) A member, [candidate or student] shall not participate on the engagement team for an audit client that is a reporting issuer or listed entity if the member's, [candidate's or student's] immediate or close family member has an accounting role or a financial reporting oversight role, or had such a position during the period covered by the financial statements subject to audit by the member or firm or the engagement period.

GUIDANCE - Rule 204.4(14) and (15)

- 1 Family and personal relationships between a person on an engagement team and a director, officer or certain employees, depending on their role, of the assurance client or a related entity may create a self-interest, familiarity or intimidation threat. The significance of such a relationship will depend on a number of factors, including the person's responsibilities on the assurance engagement, the closeness of the relationship and the role of the family member or other individual within the assurance client or related entity. Consequently, there are many circumstances that involve a threat to independence that will require evaluation.
- 2 A person has an accounting role when the person is in a position to or does exercise more than minimal influence over the contents of the client's accounting records related to the financial statements that are subject to audit or review by the member or firm or over anyone who prepares such financial statements.
- 3 A person has a financial reporting oversight role when the person is in a position to or does exercise influence over the financial statements that are subject to audit or review by the member or firm or over anyone who prepares such accounting records or financial statements.

An individual holding one of the following titles will generally be considered to be in a financial reporting oversight role: a member of the board of directors or similar management or governing body, president, chief executive officer, chief operating officer, chief financial officer, controller, director of internal audit, director of financial reporting, treasurer, and, depending upon the particular facts and circumstances, the general counsel.

When the financial statements of an audit or review client are consolidated, a financial reporting oversight role can extend beyond the client to its subsidiaries or investees. In determining whether an individual is in a financial reporting oversight role for the audit or review client, consideration should be given to the position of the individual, the extent of the individual's involvement in the financial reporting process of the client and the impact of the individual's role on the financial statements subject to audit or review by the member or firm.

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

- the position the close family member holds; and
- the role of the particular person on the engagement team.

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

- removing the particular person from the engagement team;
- where possible, restructuring the engagement team's responsibilities so that the particular person does not deal with matters that are within the responsibility of the close family member; or
- policies and procedures to empower staff to communicate, without fear of retribution, to senior levels within the firm any issue of independence and objectivity that may concern them.

5 A self-interest, familiarity or intimidation threat may exist when:

- an officer or director or person in a position to exert significant influence over the subject matter of the assurance engagement, who is not an immediate or close family member of a person on the engagement team, has a close relationship with a person on the engagement team; or
- a director, officer or employee in a financial reporting oversight role with respect to an audit or review client, who is not an immediate or close family member of a person on the engagement team, has a close relationship with a person on the engagement team.

Those on the engagement team should identify such individuals, and evaluate the relationship and consult with others in the firm in accordance with its policies and procedures. The evaluation of the significance of any threat and the availability of safeguards appropriate to eliminate it or reduce it to an acceptable level will include considering matters such as the closeness of the relationship and the role of the individual.

6 Consideration should be given to whether a self-interest, familiarity or intimidation threat exists because of a personal or family relationship between a member of the firm who is not part of the engagement team and:

- (a) an officer or director of the assurance client or a related entity, or person in a position to exert significant influence over the subject matter of the assurance engagement; or
- (b) an officer or director of the assurance client or a related entity, or person in a financial reporting oversight role with respect to the financial statements subject to audit or review by the member or firm.

Members of the firm should identify and evaluate the relationship and consult with others in the firm in accordance with its policies and procedures. The evaluation of the significance of any threat and the availability of safeguards appropriate to eliminate it or reduce it to an acceptable level will include considering matters such as the closeness of the relationship, the interaction of the member of the firm with the engagement team, the position held within the firm, and the role of the individual.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Employment or service with a reporting issuer or listed entity audit client**

- (16) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if:
- (a) a person who participated in an audit capacity in an audit of the financial statements of the entity performed by the member or firm is an officer or director of the entity or is in a financial reporting oversight role unless a period of one year has elapsed from the date that the financial statements were filed with the relevant securities regulator or stock exchange; or
 - (b) a person who was the firm's chief executive officer is an officer or director of the entity or is in a financial reporting oversight role, unless a period of one year has elapsed from the date that the individual was the chief executive officer of the firm.

Recent service with or for an assurance client

- (17)(a) A member, [candidate or student] shall not participate on the engagement team for an assurance client if the member, [candidate or student] served as an officer or director of the client or a related entity or was in a position to exert significant influence over the subject matter of the engagement during the period covered by the assurance report or the engagement period.

Temporary loan of staff to an audit or review client

- (17)(b) A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member or firm has loaned a member of the firm or a network firm to the entity or a related entity, unless:
- (i) the loan of any such person or persons is made for only a short period of time;
 - (ii) the loan of any such person or persons is not made on a recurring basis;
 - (iii) the loan of any such person or persons does not result in the person or persons making a management decision or performing a management function or providing any non-assurance services that would otherwise be prohibited by Rules 204.4(22) to (34); and
 - (iv) management of the entity or related entity directs and supervises the work performed by the person or persons.

GUIDANCE - Rule 204.4(16) and (17)

- 1 The independence of a firm or a person on the engagement team may be threatened if an officer or director of the assurance client or a related entity, or a person in a position to exert influence over the subject matter of the assurance engagement has been a member of the engagement team or a partner of the firm. Such circumstances may create a self-interest, familiarity or intimidation threat, particularly when a significant connection remains between the individual and his or her former firm.
- 2 The significance of a threat so created will depend upon the following factors:
 - the position the individual has taken at the client and whether the position involves significant influence over the subject matter of the assurance engagement or the financial statements subject to audit or review by the member or firm;
 - the amount of any involvement the individual will have with the engagement team;
 - the length of time since the individual was on the engagement team or with the firm; and
 - the former position of the individual within the engagement team or firm.

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

- modifying the plan for the assurance engagement;
- assigning an engagement team to the subsequent assurance engagement that is of sufficient seniority and experience in relation to the individual who has joined the assurance client;
- involving another member of the firm who is not, and never was, on the engagement team to review the work done or advise as necessary; or
- performing an additional quality control review of the assurance engagement by the firm.

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

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

- 3 A self-interest threat exists when a person on the engagement team participates in the assurance engagement while knowing, or having reason to believe, that he or she will or may join the client. In all such cases the following safeguards should be applied:

- having firm policies and procedures that require those on the engagement team to notify the firm when entering employment negotiations with the assurance client; and
- removing the person from the engagement team.

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

The effect of the safeguards described above is that members and students who initiate or entertain discussions with respect to a potential role with an assurance client would be precluded from being on the engagement team for that assurance engagement until such discussions have been concluded and acceptance of such a role has been declined.

- 4 For the purposes of Rule 204.4(16)(a), other than a key audit partner, the following persons are not considered to have participated in an audit capacity in an earlier audit.

- a person who is employed by the reporting issuer or listed entity due to an emergency or other unusual situation provided that the entity's audit committee has determined that the employment of such person is in the interest of the shareholders;
- a person who provided ten or fewer hours of assurance services in the earlier audit;
- a person who recommended the compensation of, or who provided direct supervisory, management or oversight of, the lead engagement partner in connection with the performance of the earlier audit, including those at all successively senior levels above the lead engagement partner through to the firm's chief executive; and
- a person who provided quality control for the audit engagement.

- 5 An individual may have fully complied with Rule 204.4(16)(a) and (b) in accepting employment with an entity, and subsequently thereto, the entity merged with or was acquired by another entity resulting in that individual having a financial reporting oversight role of a combined entity which is audited by the firm in which the individual was previously an

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employee or a partner. In such a circumstance, unless the employment offer was accepted in contemplation of the merger or acquisition, the individual or the entity could not be expected to know that the employment decision could result in a threat to independence. In all such cases the safeguard of informing the audit committee should be applied.

- 6 For the purposes of Rule 204.4(16)(a) audit procedures are deemed to have commenced for the current audit engagement period on the day after the financial statements for the previous period are filed with the relevant securities regulator or stock exchange.
- 7 For the purposes of Rule 204.4(16)(b), chief executive officer means a person in a position having the usual responsibility and authority of a chief executive officer regardless of the title applied to the person.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Serving as an officer or director of an assurance client**

(18)(a) *A member or firm shall not perform an assurance engagement for an entity if a member or an employee of the firm serves as an officer or director of the entity or a related entity, except for serving as company secretary when the practice is specifically permitted under local law, professional rules or practice, and the duties and functions undertaken are limited to those of a routine and formal administrative nature.*

Serving as an officer or director of an audit or review client

(18)(b) *A member or firm shall not perform an audit or review engagement for an entity that is not a reporting issuer or listed entity if a member or an employee of the firm or of a network firm serves as an officer or director of the entity or a related entity except for serving as company secretary when the practice is specifically permitted under local law, professional rules or practice, and the duties and functions undertaken are limited to those of a routine and formal administrative nature.*

Serving as an officer or director of a reporting issuer or listed entity audit client

(19) *A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if a member or an employee of the firm or of a network firm serves as an officer or a director of the reporting issuer or listed entity or a related entity.*

GUIDANCE - Rule 204.4(18) and (19)

- 1 A self-interest, self-review or familiarity threat may exist when a former officer or director of an assurance client or related entity or a person who has been in a financial reporting oversight role becomes a part of the engagement team for that assurance client.
- 2 If, prior to the period covered by an assurance report, a person on the engagement team served as an officer or director of the assurance client or a related entity, or had been in a position to exert significant influence over the subject matter of the assurance engagement, a self-interest, self-review or familiarity threat may exist. For example, such a threat will exist if a decision made or work performed by that individual in the prior period, while employed by the client, is to be evaluated in the current period as part of the assurance engagement. The significance of the threat will depend upon factors such as:
 - the position the individual held;
 - the length of time since the individual left the position; and
 - the role of the individual on the engagement team.

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

- involving another member of the firm who is not, and never was, on the engagement team to review the work of the particular person or advise as necessary; or
- discussing the issue with the audit committee.

Company secretary

- 3 The position of company secretary has different implications in different jurisdictions. The duties of company secretary may range from administrative duties such as personnel management and the maintenance of company records and registers, to duties as diverse as ensuring that the company complies with regulations or providing advice on corporate governance matters. Generally this position is seen to imply a close degree of association

with the entity and may create self-review and advocacy threats.

- 4** If a partner or employee of a firm serves as company secretary for an assurance client or related entity, the self-review and advocacy threats created would generally be so significant that safeguards are unlikely to be available to reduce the threats to an acceptable level. Similarly, if a partner or employee of a firm or network firm serves as company secretary for an audit or review client that is not reporting issuer or listed entity or a related entity, the self-review and advocacy threats created would generally be so significant that safeguards are unlikely to be available to reduce the threats to an acceptable level. However, when the practice of acting as company secretary is specifically permitted under local law, professional rules or practice, the duties and functions undertaken should be limited to those of a routine and formal administrative nature such as the preparation of minutes and maintenance of statutory returns.
- 5** Routine administrative services to support a company secretarial function or advisory work in relation to company secretarial administration matters is generally not perceived to impair independence, provided client management makes all relevant decisions.

Religious organizations

- 6** A threat to independence is ordinarily not created when a person on the engagement team, or any of the person's immediate or close family members, belongs to a religious organization that is an assurance client provided the person on the engagement team, or the immediate or close family member:

 - does not serve on the religious organization's governing body; and
 - does not have the right or responsibility to exercise significant influence over the financial or accounting policies of the religious organization or any of its associates.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Long association of senior personnel with a reporting issuer or listed entity audit client**

(20)(a) *A member shall not continue as the lead engagement partner or the engagement quality control reviewer with respect to the audit of the financial statements of a reporting issuer or listed entity for more than seven years in total, and shall not thereafter participate in an audit of the financial statements of the reporting issuer or listed entity until a further five years have elapsed.*

In the case of an audit engagement of a reporting issuer that is a mutual fund, the lead engagement partner and the engagement quality control reviewer shall not thereafter participate in an audit of the financial statements of the reporting issuer or another reporting issuer that is in the same mutual fund complex as the reporting issuer until a further five years have elapsed.

(b) *A member, who is a key audit partner with respect to the audit of the financial statements of a reporting issuer or listed entity, other than a lead engagement partner or engagement quality control reviewer, shall not continue in such role for more than seven years in total and shall not thereafter participate in an audit of the financial statements of the reporting issuer or listed entity until a further two years have elapsed.*

In the case of an audit engagement of a reporting issuer that is a mutual fund, such an audit partner shall not thereafter participate in an audit of the financial statements of the reporting issuer or another reporting issuer that is in the same mutual fund complex as the reporting issuer until a further two years have elapsed.

(c) *Notwithstanding paragraph (b), when an audit client becomes a reporting issuer or listed entity, a key audit partner who has served in that capacity for five or more years at the time the client becomes a reporting issuer or listed entity may continue in that capacity for two more years before being replaced as a key audit partner.*

GUIDANCE - Rule 204.4(20)

1 The use of the same senior personnel on the engagement team on an assurance engagement over a long period of time may create a familiarity threat. The significance of such a threat will depend upon factors such as:

- the length of time that the particular individual has been on the engagement team;
- the role of that individual on the engagement team;
- the structure of the firm; and
- the nature of the assurance engagement including the complexity of the subject matter and degree of professional judgment needed.

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

- discussing the matter with the audit committee;
- replacing the senior personnel on the engagement team;
- involving an additional member of the firm who is not, and never was, on the engagement team to review the work done by the particular individual, or advise as necessary;
- the member or firm is subject to external practice inspection; or
- an independent internal quality review of the assurance work performed by a member of

the firm who was not part of the engagement team.

Audit clients that are reporting issuers or listed entities

- 2 Rule 204.4(20) restricts an audit partner who has completed the permitted term as a lead engagement partner, engagement quality control reviewer, or other key audit partner from participation in the audit until further prescribed time periods have elapsed. Accordingly, such partners may not:
- provide services pertaining directly to the audit or to a review of interim financial statements;
 - provide quality control for either such engagement;
 - consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events; or
 - otherwise directly influence the outcome of any such engagement.

However, such partners may be consulted for the purpose of transferring knowledge of the client to the engagement team.

- 3 When an audit client becomes a reporting issuer or listed entity, the length of time a key audit partner has served in that capacity should be considered in determining when the partner must be replaced on the engagement team. However, Rule 204.4(20)(c) provides that if a key audit partner has served in that capacity for five or more years at the time the client becomes a reporting issuer or listed entity, such person may continue in that capacity for two more years.

204 Independence

RULE:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Audit committee approval of services to a reporting issuer or listed entity audit client**

(21) *A member or firm shall not provide a professional service to an audit client that is a reporting issuer or listed entity, or to a subsidiary thereof, without the prior approval of the reporting issuer's or listed entity's audit committee.*

GUIDANCE - Rule 204.4(21)

- 1 Rule 204.4(21) provides that a member or firm may not provide a service to a reporting issuer or listed entity, that is an audit client, or to a subsidiary thereof, unless the audit committee of the client pre-approves such service. The requirement applies to all audit and non-audit services. For the purpose of Rule 204.4(21) the audit committee recommendation to the entity's board of directors that the particular audit firm be the entity's auditor will be considered to be the approval of the audit service. Subject to paragraph 3 of this Guidance, all non-audit services for the reporting issuer or listed entity and its subsidiaries must be specifically pre-approved by the audit committee.
- 2 The audit committee may establish policies and procedures for pre-approval provided that they are detailed as to the particular services and designed to safeguard the independence of the member and the firm. For example, one or more audit committee members who are independent board directors may pre-approve the service provided decisions made by the designated audit committee members are reported to the full audit committee.
- 3 Notwithstanding Rule 204.4(21), audit committee pre-approval of services other than assurance services provided to an audit client that is a reporting issuer or listed entity, or to a subsidiary of the client, is not required where all such services that have not been pre-approved:
 - do not represent more than five per cent of total revenues paid by the audit client to the member, the firm and network firms in the fiscal year in which the services are provided;
 - were not recognized as non-audit services at the time of the engagement; and
 - are promptly brought to the attention of the audit committee and the audit committee or one or more designated representatives approves the services prior to the completion of the audit.
- 4 For the purposes of Rule 204.4(21) audit services include all those services performed to discharge responsibilities to provide an opinion on the financial statements of the reporting issuer or listed entity. For example, in connection with some audit engagements, a tax partner may be involved in reviewing the tax accrual of the client. Since it is a necessary part of the audit process, the activity constitutes an audit service. Similarly, complex accounting issues may require consultation with a national office technical partner to reach an audit judgment. That consultation, being a necessary part of the audit process, also constitutes an audit service, and as such will be considered to have been pre-approved by the audit committee whether or not the firm charges separately for it. These examples contrast with a situation where a client is evaluating a proposed transaction and requests the member, the firm or a network firm to evaluate it and, after research and consultation, the member, firm or network firm provides an answer to the client and bills for those services. Such services would not be considered to be audit services and, therefore, will not be considered to have been pre-approved with the audit service.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Performance of management functions

(22) (a) A member or firm shall not perform an assurance engagement for an entity if, during the period covered by the assurance report or the engagement period, a member of the firm makes a management decision or performs a management function for the entity or a related entity, including:

- (i) authorizing, approving, executing or consummating a transaction;
- (ii) having or exercising authority on behalf of the entity;
- (iii) determining which recommendation of the member or firm will be implemented; or
- (iv) reporting in a management role to those charged with governance of the entity;

unless the management decision or management function is not related to the subject matter of the assurance engagement that is performed by the member or firm.

(b) A member or firm shall not perform an audit or review engagement for an entity, if a member of the firm or a network firm, during either the period covered by the financial statements subject to audit or review or the engagement period, makes a management decision or performs a management function for the entity or a related entity, including any of the services listed in paragraph 22(a)(i) to (iv), whether or not the management decision or management function is related to the subject matter of the audit or review engagement that is performed by the member or firm.

Preparation of journal entries or source documents

(23) A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, a member of the firm or a network firm:

- (a) prepares or changes a journal entry, determines or changes an account code or a classification for a transaction or prepares or changes another accounting record, for the entity or a related entity, that affects the financial statements subject to audit or review by the member or firm, without obtaining the approval of management of the entity; or
- (b) prepares a source document or originating data, or makes a change to such a document or data underlying such financial statements.

Preparation of accounting records or financial statements for a reporting issuer or listed entity audit client

(24) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, in other than emergency situations, during either the period covered by the financial statements subject to audit or the engagement period, the member, firm, a network firm or a member of the firm or a network firm provides accounting or bookkeeping services related to the accounting records or financial statements including:

- (a) maintaining or preparing the entity's, or related entity's, accounting records;
- (b) preparing the financial statements or preparing financial statements which form the basis of the financial statements on which the audit report is provided; or
- (c) preparing or originating source data underlying such financial statements;

unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during the audit of such financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of the accounting or bookkeeping services will be subject to audit procedures.

In the event of an emergency situation, the member or firm may perform the audit and perform such an accounting or bookkeeping service provided:

- (i) those who provide the service are not members of the engagement team for the audit;*
- (ii) the provision of the service in such circumstances is not expected to recur;*
- (iii) the provision of the service would not lead to any members of the firm or a network firm making decisions or judgments which are properly the responsibility of management; and*
- (iv) the provision of the service receives the prior approval of the audit committee of the reporting issuer or listed entity in accordance with the provisions of Rule 204.4(21).*

GUIDANCE - Rule 204.4(22) to (24)

- 1 Obtaining an understanding of the client's internal controls is required by generally accepted auditing standards. Members often become involved in diagnosing, assessing and recommending to management ways in which internal controls can be improved or strengthened. Notwithstanding Rule 204.4(22) the independence of a member or firm would not be impaired by the provision of services to assess the effectiveness of the internal controls of an assurance client or a related entity and to recommend improvements in the design and implementation of internal controls and risk management control

Preparation of accounting records and financial statements

General provisions

- 2 It is the responsibility of management to ensure that accounting records are kept and financial statements are prepared, although in discharging its responsibility management may request a member or firm to provide assistance.
- 3 Assisting an audit or review client or a related entity in matters such as preparing accounting records or financial statements will create a self-review threat when the financial statements are subsequently audited or reviewed by the member or firm. The significance of any such threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level.
- 4 With respect to Rule 204.4(23), members may be permitted, provided that approval from management is obtained, to prepare or change a journal entry, determine or change an account code or a classification for a transaction, or prepare or change another accounting record for the entity or a related entity, that affects the financial statements subject to audit or review by the member or firm.

However, preparing or changing a source document or originating data in respect of any transaction underlying the financial statements subject to audit or review by the member or firm is not permitted.

- 5 A source document is an initial recording or original evidence of a transaction. Examples of source documents are purchase orders, payroll time cards, customer orders, invoices, disbursement approvals, signed cheques and written contracts. Source documents are often followed by the creation of additional records and reports, such as trial balances, account reconciliations and aged account receivable listings, which do not constitute source documents or initial recordings. Source documents may also be preceded by documents containing calculations and advice, such as bonus calculations for tax purposes, impairment test calculations in the oil and gas industry and sample wording for clauses in a contract that will be prepared by the client's lawyers. The creation of such additional records, reports and documents would not constitute the creation of source documents.

- 6 The financial statement audit and review process involves extensive dialogue between persons on the engagement team and management of the audit or review client. During this process, management will often request and receive input regarding such matters as accounting principles and financial statement disclosure, the appropriateness of controls and the methods used in determining the stated amounts of assets and liabilities. The provision of technical assistance of this nature for an audit or review client is an appropriate method of promoting the fair presentation of the financial statements. The provision of such advice, *per se*, does not generally threaten the member's or the firm's independence. Other services that are usually a part of the audit or review process and that do not, under normal circumstances, threaten independence include:
- assisting with resolving account reconciliation problems;
 - analyzing and accumulating information for regulatory reporting;
 - assisting in the preparation of consolidated financial statements (including assisting in the translation of local statutory accounts to comply with group accounting policies and transition to a different reporting framework such as International Financial Reporting Standards);
 - assisting the drafting of disclosure items;
 - proposing adjusting journal entries; and
 - providing assistance and advice in the preparation of local statutory accounts of subsidiary entities.
- 7 A self-review threat may exist when a member, firm or network firm assists in the preparation of subject matter other than financial statements and subsequently provides assurance thereon. For example, a self-review threat will exist if a member or firm develops and prepares prospective financial information and subsequently provides assurance on it. Consequently, a member or firm should evaluate the significance of any self-review threat created by the provision of such a service. If the threat is other than clearly insignificant, safeguards should be applied to reduce the threat to an acceptable level.

Audit or review clients that are not reporting issuers or listed entities

- 8 Subject to Rule 204.4(23), a member, firm or network firm may provide an audit or review client or a related entity that is not a reporting issuer or listed entity with accounting or bookkeeping services provided that any resulting self-review threat so created is reduced to an acceptable level. Examples of such services include:
- recording transactions for which management has determined or approved the appropriate account classification;
 - posting transactions to the general ledger;
 - preparing financial statements;
 - drafting notes to the financial statements;
 - posting journal entries to the trial balance;
 - performing payroll services which do not involve having custody of the client's or related entity's assets; and
 - preparing tax receipts for charitable donations or tax information returns, such as T4 slips.

Client approval of journal entries

- 9 A member, firm or network firm may prepare journal entries for an audit or review client or related entity that is not a reporting issuer or listed entity provided management approves and takes responsibility for such journal entries. In obtaining this approval, the member, firm or network firm may choose to obtain approval for each journal entry or, alternatively, to obtain approval following a thorough review of the completed financial statements with management. This approval may also be obtained through the management representation

letter.

Evaluation of significance of threats

10 The significance of a threat created by providing accounting and bookkeeping services to an audit or review client or related entity that is not a reporting issuer or listed entity should be evaluated. The significance of such a threat will depend upon factors such as:

- the degree of involvement of the member or firm;
- the complexity of the transactions to be accounted for; and
- the extent of professional judgment required in selecting the appropriate accounting treatment.

If the threat is other than clearly insignificant, safeguards should be applied to reduce the threat to an acceptable level. Such safeguards might include:

- making arrangements so that such services are not performed by a person on the engagement team;
- requiring the client or related entity to create the source data for the accounting entries;
- requiring the client or related entity to develop the underlying assumptions;
- obtaining the views of another professional accountant;
- arranging for another firm to review a significant accounting treatment; or
- discussing a significant accounting treatment with the practice advisory services department of the member's provincial CPA body/institute [or name of other appropriate department].

Complex transactions

11 Preparing the journal entries for a complex transaction would likely create a self-review threat the significance of which could only be reduced to an acceptable level by applying safeguards that involve consultation with others, for example by:

- obtaining the views of another professional accountant;
- arranging for another firm to review a significant accounting treatment; or
- discussing the proposed accounting treatment with the practice advisory services department of the member's provincial CPA body/institute [or name of other appropriate department]

Audit clients that are reporting issuers or listed entities

12 Rule 204.4(24) permits the provision of accounting or bookkeeping services by a member, a firm or a network firm, or a member of the firm or a network firm to an audit client that is a reporting issuer or listed entity, or a related entity in the event of emergency situations provided that the requirements Rule 204.4(24) are met. Such emergency situations might arise when, due to events beyond the control of the member or firm and the client or related entity:

- there are no viable alternative resources to those of the member or firm with the necessary knowledge of the client's or related entity's business to assist in the timely preparation of its accounting records or financial statements, and
- a restriction on the member's or firm's ability to provide the services would result in significant difficulties for the client or related entity, for example, as might result from a failure to meet regulatory reporting requirements, in the withdrawal of credit lines, or would threaten the going concern status of the client or related entity. Significant difficulties would not be created simply by virtue of the fact that the client or related entity would be required to incur additional costs to engage the services of an alternative service provider.

Members and firms are also required by Rule 204.5(b) to document both the rationale

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supporting the determination that the situation constitutes an emergency and compliance with the provisions of subparagraphs (i) through (iv) of Rule 204.4(24).

Members, firms and network firms should fully assess and consider the circumstances that would constitute an emergency situation. Emergency situations are rare, non-recurring and would arise only when clearly beyond the control of the member or firm and the client or related entity. Caution should be exercised when deciding to undertake services under this exception.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Provision of valuation services to an audit or review client that is not a reporting issuer or listed entity

(25)(a) A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or a network firm, provides a valuation service to the entity or a related entity where the valuation involves a significant degree of subjectivity and relates to amounts that are material to the financial statements subject to audit or review by the member or firm, unless the valuation is performed for tax purposes only and relates to amounts that will affect such financial statements only through accounting entries related to taxation .

Provision of valuation services to a reporting issuer or listed entity audit client

(25)(b) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or a network firm, provides a valuation service to the client or a related entity, unless:

- (i) the valuation is performed for tax purposes only and relates to amounts that will affect such financial statements only through accounting entries related to taxation, or
- (ii) it is reasonable to conclude that the results of that service will not be subject to audit procedures during the audit of the financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of the valuation service will be subject to audit procedures.

GUIDANCE - Rule 204.4(25)

General provisions

- 1 A valuation service involves the making of assumptions with respect to future events and the application of certain methodologies and techniques, in order to compute an amount or provide an opinion with respect to a specific value or range of values, for a business as a whole, an intangible or tangible asset or a liability.
- 2 When a member or firm performs a valuation that forms part of the subject matter of an assurance engagement that is not an audit or review engagement, the firm should consider whether there is a self-review threat. If such a threat exists, and it is other than clearly insignificant, safeguards should be applied to eliminate it or reduce it to an acceptable level.

Audit or review clients that are not reporting issuers or listed entities

- 3 Members and firms should refer to paragraph 5 of the Guidance to Rule 204.4(34) when performing a valuation service for an audit or review client or a related entity for tax purposes only that relates to amounts that will affect the financial statements subject to audit or review by the member or firm only through accounting entries related to taxation.
- 4 Performing a valuation service for an audit or review client or a related entity that is not a reporting issuer or listed entity will create a self-review threat when the valuation resulting from the service is incorporated into the financial statements subject to audit or review by the member or firm. The significance of such a threat should be evaluated. The significance will depend on factors such as:
 - the materiality of the results of the valuation service;
 - the extent of the client's or related entity's knowledge, experience and ability to evaluate

- the issues concerned, and the extent of the client's or related entity's involvement in determining and approving significant matters of judgment;
- the degree to which established methodologies and professional guidelines are applied when performing the particular valuation service;
- the degree of subjectivity inherent in the item concerned where the valuation involves standard or established methodologies;
- the reliability and extent of the underlying data;
- the degree of dependence on future events of a nature which could create significant volatility in the amounts involved; and
- the extent and clarity of the financial statement disclosures.

If the threat is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level. Such safeguards might include:

- involving an additional professional accountant who was not a member of the engagement team to review the valuation work or otherwise advise as necessary;
- confirming with the client or related entity its understanding of the underlying assumptions of the valuation and the methodology to be used and obtaining approval for their use;
- obtaining the client's or related entity's acknowledgement of responsibility for the results of the valuation work performed by the firm or network firm; or
- arranging that members of the firm or network firm providing such services do not participate on the engagement team.

5 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.

6 The independence of a member or firm will not be impaired when:

- the firm's valuation specialist reviews the work of an audit or review client or a related entity or a specialist employed by the client or related entity, provided the client, related entity or specialist supplies the technical expertise that the client or related entity uses in determining the required amounts recorded in the financial statements. In such circumstances there will be no self-review threat because a client's or related entity's management or a third-party is the source of the financial information subject to audit or review by the member or firm; or
- the valuation service is provided for non-financial reporting purposes only, for example, transfer pricing studies or other valuations that are performed solely for tax purposes.

204 Independence

RULE:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of actuarial services to a reporting issuer or listed entity audit client**

(26) *A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides an actuarial service to the client or a related entity, unless it is reasonable to conclude that the results of that service will not be subject to audit procedures during the audit of the financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of the actuarial service will be subject to audit procedures.*

GUIDANCE - Rule 204.4(26)

- 1 For the purposes of Rule 204.4(26), actuarial services include the determination of an amount to be recorded in the client's financial statements and related accounts, except for:
- services that involve assisting the client in understanding the methods, models, assumptions and inputs used in determining such amounts; and
 - advising management on the appropriate actuarial methods and assumptions that will be used in the actuarial valuations.

In addition, the firm may use its own actuary to assist in conducting the audit if the client's actuary or a third-party actuary provides management with its actuarial capabilities.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of internal audit services to an audit or review client

- (27)(a) A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm or a network firm or a member of the firm or network firm provides an internal audit service to the entity or a related entity unless, with respect to the entity for which the internal audit service is provided:
- (i) the entity designates an appropriate and competent resource within senior management to be responsible for internal audit activities and to acknowledge responsibility for designing, implementing and maintaining internal controls;
 - (ii) the entity or its audit committee reviews, assesses and approves the scope, risk and frequency of the internal audit services;
 - (iii) the entity's management evaluates the adequacy of the internal audit services and the findings resulting from their performance;
 - (iv) the entity's management evaluates and determines which recommendations resulting from the internal audit services to implement and manages the implementation process; and
 - (v) the entity's management reports to the audit committee the significant findings and recommendations resulting from the internal audit services.

Provision of internal audit services to a reporting issuer or listed entity audit client

- (27)(b) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides an internal audit service to the client or a related entity, that relates to the client's, or the related entity's, internal accounting controls, financial systems or financial statements unless it is reasonable to conclude that the results of that service will not be subject to audit procedures during the audit of the financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of the internal audit service will be subject to audit procedures.

GUIDANCE - Rule 204.4(27)

General provisions

- 1 A self-review threat may exist when a member, firm or network firm provides internal audit services to an audit or review client or a related entity. Such services may comprise an extension of the firm's audit service beyond the requirements of generally accepted auditing standards, assistance in the performance of the client's or related entity's internal audit activities, or outsourcing of the activities. In evaluating any threat to independence, the nature of the service should be considered.
- 2 Services involving an extension of the procedures required to conduct an audit or review in accordance with the *CPA Canada Handbook – Assurance* will not be considered to impair independence with respect to an audit or review client provided that a member of the firm or network firm does not act or appear to act in the capacity of the client's or related entity's management.
- 3 During the course of an audit or review engagement the engagement team considers the client's internal controls and, as a result, may make recommendations for its improvement. This is part of an audit or review engagement and is not considered to be an internal audit

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service.

- 4 In addition to complying with the requirements of Rule 204.4(27)(a), a member or firm should also consider whether internal audit services should be provided to an audit or review client or a related entity only by a member or members of the firm not involved in the audit or review engagement and with different reporting lines within the firm.
- 5 Performing a significant portion of the audit or review client's or related entity's internal audit activities may create a self-review threat and a member, firm or network firm should consider that possibility and proceed with caution before taking on such an activity.

Audit clients that are reporting issuers or listed entities

- 6 Rule 204.4(27)(b) does not prohibit a member, firm or network firm from providing a nonrecurring service to evaluate a discrete item or program, if the service is not in substance the outsourcing of an internal audit function. For example, the member, firm or network firm, or a member of the firm of a network firm, may conduct a nonrecurring specified auditing procedures engagement related to the internal controls of an audit client that is a reporting issuer or listed entity or a related entity.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of information technology systems services to an audit or review client

(28)(a) A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or network firm provides a financial information systems design or implementation service to the entity or a related entity where the service involves the design or implementation of all or part of a financial information technology system that either generates information that is significant to the accounting records or financial statements subject to audit or review by the member or firm, or forms a significant part of either entity's internal controls that are relevant to the financial statements that are subject to audit or review by the member or firm, unless, with respect to the entity for which the information technology service is provided:

- (i) the entity acknowledges its responsibility for establishing and monitoring a system of internal controls;
- (ii) the entity 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;
- (iii) the entity makes all management decisions with respect to the design and implementation process;
- (iv) the entity evaluates the adequacy and results of the design and implementation of the system; and
- (v) the entity is responsible for operating the hardware or software system and for the data it uses or generates.

Provision of information technology system services to a reporting issuer or listed entity audit client

(28)(b) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm provides financial information systems design or implementation services and the services involve:

- (i) directly or indirectly operating, or supervising the operation of, the entity's or a related entity's information system, or managing the entity's or a related entity's local area network; or
- (ii) designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant to the entity's or a related entity's financial statements or other financial information systems taken as a whole;

unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the financial statements. In determining whether such a conclusion is reasonable, there is a rebuttable presumption that the results of the financial information systems design and implementation services will be subject to audit procedures.

GUIDANCE - Rule 204.4(28)

General provisions

- 1 The provision of services by a member, firm or network firm to an audit or review client or a related entity that involve the design or implementation of financial information technology systems that are, or will be, used to generate information forming part of the client's or the related entity's financial statements may create a self-review threat.

There are, however, some information technology systems services that may not create a threat to independence, provided that the member or firm does not make a management decision or perform a management function for the client or the related entity. Such services include the following:

- designing or implementing information technology systems that are unrelated to internal controls over financial reporting;
- designing or implementing information technology systems that do not generate information forming a significant part of the accounting records or financial statements subject to audit or review by the member or firm;
- implementing “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 or related entity’s needs is not significant; and
- evaluating and making recommendations with respect to a system designed, implemented or operated by another service provider or the client or related entity.

Audit or review clients that are not reporting issuers or listed entities

- 2 In addition to complying with the requirements of Rule 204.4(28)(a), a member or firm should also consider whether financial information systems design and implementation services should be provided to an audit or review client or related entity only by members of the firm who are not involved in the audit or review engagement and with different reporting lines within the firm.

Audit clients that are reporting issuers or listed entities

- 3 For the purposes of Rule 204.4(28)(b), information will be considered to be significant if it is likely to be material to the financial statements. Since materiality determinations may not be complete before the financial statements are prepared, the audit client or related entity and the member or firm should evaluate the general nature of the information as well as system output during the period of the audit engagement.
- 4 Rule 204.4(28) does not preclude a member, a firm or a network firm from:
- designing or implementing a hardware or software system that is unrelated to the financial statements or accounting records of the reporting issuer or listed entity, or a related entity;
 - as part of the audit, or another assurance engagement, evaluating and making recommendations to management on the internal controls of a system as it is being designed, implemented or operated; or
 - making recommendations on internal control matters to management or other service provider in conjunction with the design and installation of a system by another service provider.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of litigation support services to an audit or review client**

(29)(a) A member or firm shall not perform an audit or review engagement for a client if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides a litigation support service for the entity or a related entity, or for a legal representative thereof, for the purpose of advancing the entity's or related entity's, interest in a civil, criminal, regulatory, administrative or legislative proceeding or investigation with respect to an amount or amounts that are material to the financial statements subject to audit or review by the member or firm.

Provision of litigation support services to a reporting issuer or listed entity audit client

(29)(b) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides a litigation support service for the entity or a related entity, or for a legal representative thereof, for the purpose of advancing the entity's or related entity's, interest in a civil, criminal, regulatory, administrative or legislative proceeding or investigation.

GUIDANCE - Rule 204.4(29)

General provisions

- 1 Litigation support services include such activities as acting as an expert witness, calculating estimated damages or other amounts that might become receivable or payable as the result of litigation or other legal dispute, and assistance with document management and retrieval in relation to a legal dispute or litigation.
- 2 A self-review threat may exist when a member, firm or network firm provides to an audit or review client or related entity, litigation support services that include the estimation of the possible outcome of a dispute or litigation and thereby affects the amounts or disclosures to be reflected in the client's or related entity's financial statements. The significance of any such threat will depend upon factors such as:
 - the nature of the engagement;
 - the materiality of the amounts involved; and
 - the degree of subjectivity inherent in the matter concerned.

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

- policies and procedures to prohibit individuals who assist the client from making management decisions on the client's or related entity's behalf;
- using a member of the firm who is not part of the engagement team to perform the litigation support service; or
- the involvement of others, such as independent specialists.

If adequate safeguards are not available to reduce a threat to an acceptable level the member, firm or network firm should decline the engagement.

- 3 The effect of Rule 204.4(29) is to prohibit, except for the specified circumstances set out in paragraph 202.4(29)(a), a member, firm or network firm, or a member of the firm or a network firm, from providing specialized knowledge, experience or expertise to advocate or support the audit client's positions, or the positions of a related entity, in an adversarial or similar proceeding such as an investigation, a litigation matter, or a legislative or administrative tribunal. Litigation or other matters frequently escalate to a level, such as a civil, criminal, regulatory, administrative or legislative proceeding or investigation, which creates a self-review or advocacy threat which cannot be reduced to an acceptable level by available safeguards. Accordingly, it is particularly important for members and firms to consider initially, and thereafter reconsider periodically, whether the matter in support of which the service is provided is likely to escalate, or has escalated, to such a level. In addition, members and firms should discuss, with the audit committee, the possibility that a matter could escalate to such a level and the consequential impact on the member's or firm's ability to continue to provide the litigation support service or to continue to perform the audit or review engagement.
- 4 Rule 204.4(29) does not preclude a member, a firm or a network firm, or a member of the firm or a network firm from being engaged by an audit committee of an audit or review client to assist it in fulfilling its responsibilities to conduct its own investigation of a potential accounting impropriety. For example, if the audit committee is concerned about the accuracy of the inventory records at a subsidiary, it may engage the member, the firm or the network firm, or a member of the firm or a network firm, to conduct a thorough inspection and analysis of these records, the physical inventory at the subsidiary and related matters without impairing independence. This type of engagement may include forensic or other fact-finding work that results in the issuance of a report to the audit client. It will generally require performing procedures that are consistent with, but more detailed or more comprehensive than, those required by generally accepted auditing standards.
- 5 In an investigation or proceeding for an audit or review client, or for a related entity, the member, firm or network firm, or a member of the firm or a network firm, may provide an account or testimony with respect to a matter of fact, such as describing the work performed by the member's firm or the predecessor auditor. The member, firm or network firm, or a member of the firm or network firm, may explain the positions taken or the conclusions reached during the performance of any service provided for the audit or review client.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Provision of legal services to an audit or review client

- (30) *A member or firm shall not perform an audit or review engagement for an entity if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or network firm provides a legal service to the entity or a related entity in the resolution of a dispute or litigation in circumstances where the matters in dispute or subject to litigation are material in relation to such financial statements.*

Provision of legal services to a reporting issuer or listed entity audit client

- (31) *A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides a legal service to the entity or a related entity.*

GUIDANCE - Rule 204.4(30) and (31)

General provisions

- 1 A legal service is any service that may only be provided by a person licensed, admitted, or otherwise qualified to practice law in the jurisdiction in which the service is provided. However, where a jurisdiction outside of Canada requires a service to be provided by a person licensed, admitted, or otherwise qualified to practice law in that jurisdiction and the same service could be provided in the relevant jurisdiction in Canada by a person not licensed, admitted, or otherwise qualified to practice law, such a service is not considered to be a legal service for the purposes of this Rule. Legal services encompass a wide and varied range of corporate and commercial services, including contract support, conduct of litigation, mergers and acquisition advice and support and the provision of assistance to client's internal legal departments.
- 2 Threats to independence created by the provision of legal services to an audit or review client or related entity should be considered based on:
 - the nature of the service to be provided (for example, advocacy as opposed to other legal services);
 - whether the service provider is separate from the engagement team; and
 - the materiality of any pertinent matter in relation to the financial statements that are subject to audit or review by the member or firm.
- 3 The provision of a legal service which involves matters that would not be expected to have a material effect on the financial statements subject to audit or review by the member or firm is not considered to create an unacceptable threat to independence with respect to the engagement to perform the audit or review of those financial statements.
- 4 The provision of a legal service to support an audit or review client or related entity in the execution of a transaction (e.g., contract support, legal advice, legal due diligence and restructuring) may create a self-review threat. The significance of any such threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level. Such safeguards might include:
 - using members of the firm who are not on the engagement team to provide the service;
 - ensuring the client or related entity makes the ultimate decision in relation to the advice provided; or
 - ensuring the service involves the execution of what has been decided by the client or

related entity in relation to the transaction.

Audit or review clients that are not reporting issuers or listed entities

- 5** The provision of a legal service to assist an audit or review client that is not a reporting issuer or listed entity or a related entity in the resolution of a dispute or litigation may create an advocacy or self-review threat. When a member, firm or network firm is asked to act in an advocacy role for the client or related entity in the resolution of a dispute or litigation in circumstances where the amounts involved are not material to the client's financial statements, the significance of any resulting threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to eliminate it or reduce it to an acceptable level. Such safeguards might include:
- policies and procedures to prohibit members of the firm or network firm from assisting the client or related entity in making management decisions on behalf of the client or related entity; or
 - using members of the firm who are not on the engagement team to perform the particular legal service.

204 Independence

RULE:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Human resource services for a reporting issuer or listed entity audit client

- (32) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides any of the following services to the entity or a related entity:
- (a) searching for or seeking out prospective candidates for management, executive or director positions;
 - (b) engaging in psychological testing, or other formal testing or evaluation programs;
 - (c) undertaking reference checks of prospective candidates for an executive or director position;
 - (d) acting as a negotiator or mediator with respect to employees or future employees with respect to any condition of employment, including position, status or title, compensation or fringe benefits; or
 - (e) recommending or advising with respect to hiring a specific candidate for a specific job.

GUIDANCE - Rule 204.4(32)

General provisions

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

The significance of any such threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level. In all cases, the firm should not make management decisions and the client should make the hiring decision.

Audit clients that are reporting issuers or listed entities

- 2 Notwithstanding Rule 204.4(32) a member, firm or network firm, or a member of the firm or a network firm may, upon request of the audit client or a related entity, interview candidates and advise the client or related entity on the candidate's competence for financial accounting, administrative or control positions.

204 Independence

RULE:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of corporate finance and similar services to an audit or review client**

- (33) A member or firm shall not perform an audit or review engagement for an entity if, during the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or network firm, provides any of the following services:
- (a) promoting, dealing in or underwriting the entity's or a related entity's securities;
 - (b) advising the entity or a related entity on other corporate finance matters where:
 - (i) the effectiveness of the advice depends on a particular accounting treatment or presentation in the financial statements;
 - (ii) the outcome or consequences of the advice has or will have a material effect on the financial statements; and
 - (iii) the engagement team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework;
 - (c) making investment decisions on behalf of the entity or a related entity or otherwise having discretionary authority over the entity's or a related entity's investments;
 - (d) executing a transaction to buy or sell the entity's or a related entity's investments; or
 - (e) having custody of assets of the entity or a related entity, including taking temporary possession of securities purchased by the entity or a related entity.

GUIDANCE - Rule 204.4(33)

- 1 Rule 204.4(33) sets out in paragraphs (a) to (e) the corporate finance and similar services which a member or firm may not provide to an audit or review client or a related entity.

Where a member or firm has provided advice on corporate finance matters to such a client or entity, Rule 204.4(33)(b) prohibits the member or firm from performing the audit or review engagement if:

- the effectiveness of the advice depends on a particular accounting treatment or presentation in the financial statements;
- the outcome or consequences of the advice has or will have a material effect on the financial statements; and
- the engagement team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework.

Where the efficacy of implementing such corporate finance advice depends upon a particular accounting treatment or presentation, there may be pressure to adopt an accounting treatment or presentation that is inconsistent with the relevant financial reporting framework. If such an inconsistency were to exist, the member or firm would be prohibited from performing the audit or review engagement. Accordingly, where the circumstances set out in Rule 204.4(33)(b) exist the member or firm must review the materiality of the effect of the advice and the appropriateness of the related accounting treatment and presentation with the audit or review engagement team as soon as possible prior to completion of the corporate finance advisory service.

- 2 Corporate finance services other than those that are prohibited by Rule 204.4(33) may create an advocacy or self-review threat that may be reduced to an acceptable level by the application of safeguards. Examples of such services include:
- assisting a client in developing corporate strategies;

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- assisting a client in obtaining bank financing by explaining the financial statements to the bank;
- assisting in identifying or introducing a client to possible sources of capital that meet the client specifications or criteria; and
- providing structuring advice and assisting a client in analyzing the accounting effects of proposed transactions.

The significance of the threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce the threat to an acceptable level. Such a safeguard might be using members of the firm who are not part of the engagement team to provide the services.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Provision of tax planning or other tax advisory services to an audit or review client

- (34) (a) A member or firm shall not perform an audit or review engagement for a client if, during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm, a network firm or a member of the firm or a network firm, provides tax planning or other tax advice to the client or a related entity, where:
- (i) the effectiveness of the advice depends on a particular accounting treatment or presentation in the financial statements;
 - (ii) the outcome or consequences of the advice has or will have a material effect on the financial statements; and
 - (iii) the engagement team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework.

Provision of tax calculations for the purpose of preparing accounting entries for a reporting issuer or listed entity

- (34) (b) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity if, in other than emergency situations, during either the period covered by the financial statements subject to audit or the engagement period, the member, the firm, a network firm or a member of the firm or a network firm, prepares tax calculations of current and future tax liabilities or assets for the reporting issuer or listed entity or a related entity for the purpose of preparing accounting entries that are subject to audit by the member or firm.

In the event of an emergency situation, the member or firm may perform the audit and perform such a tax service provided:

- (i) those who provide the service are not members of the audit engagement team;
- (ii) the provision of the service in such circumstances is not expected to recur;
- (iii) the provision of the service would not lead to any members of the firm or a network firm making decisions or judgments which are properly the responsibility of management; and
- (iv) the provision of the service receives the prior approval of the audit committee of the reporting issuer or listed entity in accordance with the provisions of Rule 204.4(21).

GUIDANCE - Rule 204.4(34)

General provisions

- 1 Tax services usually include:
 - preparation of tax returns;
 - preparation of valuations for tax purposes;
 - provision of tax planning and similar tax advisory services on such matters as how to structure business affairs in a tax efficient manner or on the application of tax laws or regulations;
 - provision of tax advocacy services with respect to tax disputes; or
 - preparation of tax calculations for the purpose of preparing accounting entries.
- 2 The provision of tax services may create a self-review threat where the advice or other service affects or will affect the financial statements subject to audit or review by the member or firm, or an advocacy threat where the services involve resolution of a tax dispute with tax authorities. The existence and significance of any threat will depend on factors such as:
 - the nature of the tax service that is provided;

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- the degree of subjectivity involved in determining the appropriate treatment of tax advice in the financial statements;
- the extent to which the outcome of the tax service has or will have a material effect on the financial statements subject to audit or review by the member or firm ;
- 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.

Providing tax planning advice where the advice is clearly supported by tax authorities or other precedent, by established practice or has a basis in tax law that is likely to prevail does not ordinarily create a threat to independence, unless the circumstances described in Rule 204.4(34)(a) exist.

- 3 The significance of any threat should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level. Examples of such safeguards include:
- using professionals who are not members of the assurance engagement team to perform the tax service;
 - having a tax professional, who was not involved in providing the tax service, advise the assurance engagement team on the service and review the financial statement treatment;
 - obtaining advice on the service from an external tax professional; and
 - obtaining pre-clearance or advice from the tax authorities.

Preparation of tax returns

- 4 Tax return preparation services may involve assisting an audit or review client with its tax reporting obligations by drafting and completing information, including the amount of tax due, as reported on prescribed forms, and as required to be submitted to the applicable tax authorities. Such tax returns are subject to audit or other review by tax authorities. Accordingly, the provision of such services does not ordinarily create a threat to independence provided that management takes responsibility for the returns including any significant judgments made.

Preparation of valuations for tax purposes

- 5 A firm may be requested to perform a valuation to assist an audit or review client or a related entity with its tax reporting obligations or for tax planning purposes.

Rule 204.4(25) permits the provision of certain valuation services for tax purposes only. Where the valuation is performed for tax purposes only and the valuation relates to amounts that will affect the financial statements subject to audit or review by the member or firm only through accounting entries related to taxation, a threat to independence would not ordinarily be created if the amounts related to the valuation are not material to such financial statements or if the valuation is subject to external review at the discretion of a tax authority or similar regulatory authority.

However, a valuation service that is not subject to such an external review and which results in amounts that are material to the financial statements subject to audit or review by the member or firm, may create a threat to independence. The existence and significance of any threat created will depend upon factors such as:

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- 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; and
- the reliability and extent of the underlying data.

The significance of any threat created should be evaluated and, if it is other than clearly insignificant, safeguards should be applied to reduce it to an acceptable level.

Provision of tax planning or other tax advisory services

- 6** Members and firms often provide tax planning or advisory services in order to create tax-efficient outcomes for their clients. Where a member or firm has provided tax planning or other tax advice to an audit or review client or a related entity, Rule 204.4(34)(a) prohibits the member or firm from performing the audit or review engagement if:
- the effectiveness of the advice depends on a particular accounting treatment or presentation in the financial statements;
 - the outcome or consequences of the advice has or will have a material effect on the financial statements; and
 - the engagement team has reasonable doubt as to the appropriateness of the related accounting treatment or presentation under the relevant financial reporting framework.

Where the efficacy of implementing such tax planning or other tax advice depends upon a particular accounting treatment or presentation there may be pressure to adopt an accounting treatment or presentation that is inconsistent with the relevant financial reporting framework. If such an inconsistency were to exist, the member or firm would be prohibited from performing the audit or review engagement. Accordingly, where the circumstances set out in Rule 204.4(34)(a) exist, the member or firm must review the materiality of the effect of the tax planning or other tax advice and the appropriateness of the related accounting treatment or presentation with the audit or engagement team as soon as possible prior to completion of the tax planning or other tax advisory service.

Provision of tax advocacy services

- 7** Tax advocacy services generally involve assisting a client in the resolution of a disputed tax matter with tax authorities. Such services may involve the provision of litigation support services, legal services or both. Accordingly, members and firms should evaluate whether the provision of such a tax advocacy service involves the provision of a service that would be prohibited pursuant to Rules 204.4(29)(a) or (b), (30) or (31).

Audit or review clients that are not reporting issuers or listed entities

- 8** Rules 204.4(29)(a) and (30) do not preclude members and firms from providing a tax advocacy service that involves assistance in the resolution of a dispute with a tax authority to an audit or review client that is not a reporting issuer or listed entity and where the assistance does not involve acting as an advocate before a public tribunal or court.

Members and firms are also not precluded by Rules 204.4(29)(a) and (30) from providing a tax advocacy service that involves assistance in the resolution of a dispute with a tax authority to an audit or review client that is not a reporting issuer or listed entity where the assistance involves acting as an advocate before a public tribunal or court provided that the disputed matter involves amounts that are not material to the financial statements subject to audit or review by the member or firm.

Rules 204.4(29)(a) and (30) do not preclude members and firms from responding to specific requests for information, providing factual accounts or testimony about the work performed or assisting the client in analyzing the tax issues.

Audit clients that are reporting issuers or listed entities

- 9 Rules 204.4(29)(b) and (31) do not preclude members and firms from providing a tax advocacy service that involves assistance in the resolution of a dispute with a tax authority to a reporting issuer or listed entity audit client and where the assistance does not involve acting as an advocate before a public tribunal or court.

Pursuant to Rules 204.4(29) and (31), members and firms may not provide a tax advocacy service that involves assistance in the resolution of a dispute with a tax authority to a reporting issuer or listed entity audit client and where the assistance involves acting as an advocate before a public tribunal or court whether or not the amounts involved are material to the financial statements subject to audit or review by the member or firm.

Rules 204.4(29)(b) and (31) do not preclude members and firms from responding to specific requests for information or providing factual accounts or testimony about the work performed.

Members and firms are cautioned that an engagement to provide a permitted tax advocacy service may, in its performance, escalate to a point where the advocacy or self-review threat so created cannot be reduced to an acceptable level by the application of safeguards. Accordingly, the guidance in paragraph 3 of the Guidance to Rule 204.4(29) applicable to litigation support services may also be helpful when considering the provision of tax advocacy services. One of the factors that impacts the significance of any such threat created is whether the tax advocacy service involves acting as an advocate before a public tribunal or court, which for this purpose is an adjudicative body that is independent of the tax authority.

Preparation of tax calculations for the purpose of preparing accounting entries for a reporting issuer or listed entity

- 10 Rule 204.4(34)(b) permits, in the event of an emergency situation and under specified conditions, a member or firm to prepare tax calculations of current and future tax liabilities or assets for a reporting issuer or listed entity audit client or a related entity for the purpose of preparing accounting entries that are subject to audit by the member or firm. Such emergency situations might arise when, due to events beyond the control of the member or firm and the client or related entity,
- there are no viable alternative resources to those of the member or firm with the necessary knowledge of the client's or related entity's business to assist in the timely preparation of such tax calculations, and
 - a restriction on the member's or firm's ability to provide the services would result in significant difficulties for the client or related entity, for example, as might result from a failure to meet regulatory reporting requirements, in the withdrawal of credit lines, or would threaten the going concern status of the client or related entity. Significant difficulties would not be created simply by virtue of the fact that the client or related entity would be required to incur additional costs to engage the services of an alternative service provider.

Members and firms are also required by Rule 204.5(c) to document both the rationale supporting the determination that the situation constitutes an emergency and compliance with the provisions of subparagraphs (i) through (iv) of Rule 204.4(34)(b).

Members, firms and network firms should fully assess and consider the circumstances that would constitute an emergency situation. Emergency situations are rare, non-recurring and

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would arise only when clearly beyond the control of the member or firm and the client or related entity. Caution should be exercised when deciding to undertake services under this exception.

204 Independence

RULES:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Provision of non-assurance services prior to commencement of audit or review services**

(35)(a) *Where a member, firm, a network firm or a member of the firm or a network firm has provided a non-assurance service referred to in Rules 204.4(22) to (34) to a client prior to the engagement of the member or firm to perform an audit or review engagement for the client but during or after the period covered by the financial statements subject to audit or review by the member or firm, the member or firm shall not perform the audit or review engagement unless the particular non-assurance service was provided before the engagement period and the member or firm:*

- (i) discusses independence issues related to the provision of the non-assurance service with the audit committee;*
- (ii) requires the client to review and accept responsibility for the results of the non-assurance service; and*
- (iii) precludes personnel who provided the non-assurance service from participating in the audit or review engagement,*
such that any threat created by the provision of the non-assurance service is reduced to an acceptable level.

Provision of previous non-assurance services to an entity that has become a reporting issuer or listed entity

(35) (b) *Where a member, firm, a network firm or a member of the firm or a network firm has performed a non-assurance service referred to in Rules 204.4 (22) to (34) for an audit or review client that has become a reporting issuer or listed entity and the provisions of Rules 204.4(22) to (34) would have precluded the member or firm from performing an audit engagement for a reporting issuer or listed entity, the member or firm shall not perform an audit engagement for the client unless the member or firm:*

- (i) discusses independence issues related to the provision of the non-assurance service with the audit committee;*
- (ii) requires the client to review and accept responsibility for the results of the non-assurance service; and*
- (iii) precludes personnel who provided the non-assurance service from participating in the audit engagement,*
such that any threat to independence created by the provision of the non-assurance service is reduced to an acceptable level.

GUIDANCE - Rule 204.4(35)

- 1** The firm and those on the engagement team should be independent of the assurance client during the period of the assurance engagement.

Audit or review engagements

- 2** In the case of an audit or review engagement, independence is also required during the period covered by the financial statements reported on by the member or firm. When an entity becomes an audit or review client during or after the period covered by the financial statements on which the member or firm will report, the member or firm should consider whether any threats to independence may be created by financial or business relationships with the client during or after the period covered by the financial statements, but prior to the acceptance of the engagement.

Similarly, in the case of an assurance engagement that is not an audit or review

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engagement, the member or firm should consider whether any financial or business relationships may create threats to independence.

- 3 In the situation described in Rule 204.4(35)(a), the member or firm is required to take a number of measures to reduce any threat created by the provision of the non-assurance service as described in the Rule to an acceptable level.

The determination as to whether any such threat has been so reduced will require the member or firm to consider the nature and impact of the threat to independence and take any further measures that are necessary to reduce it to an acceptable level. Such further measures might include engaging another firm to review the results of the non-assurance service or having another firm re-perform that service to the extent necessary to enable the other firm to take responsibility for the non-assurance service.

If the provision of the non-assurance service creates such a significant threat to independence that compliance with the requirements of Rule 204.4(35)(a) would still not reduce any such threat to an acceptable level, the member or firm is required to decline the audit or review engagement.

Members and firms are reminded that, even where a non-assurance service that is not specifically addressed by the provisions of Rules 204.4(22) to (35) has been provided to an audit or review client, a threat to independence may still be created by the provision of the non-assurance service. In such circumstances, members and firms are required, in accordance with the provisions of Rule 204.3, to evaluate any threats so created and apply safeguards to reduce them to an acceptable level or decline the audit or review engagement.

Audit clients that are reporting issuers or listed entities

- 4 When an entity becomes a reporting issuer or listed entity by virtue of a public offering, the auditor of the entity is required, from that period forward until the entity ceases to be a reporting issuer or listed entity, to comply with the specific prohibitions contained in Rule 204.4 that relate to an audit of a reporting issuer or listed entity. For example, bookkeeping services may not be provided following the date of an initial public offering, except in emergency situations. The provision of bookkeeping services to the entity prior that date would not impair the firm's independence provided the services were not prohibited by Rule 204.4(23) and provided the firm had complied with the provisions of Rule 204.4(35)(b).

Documentation

- 5 Members and firms are also required by Rule 204.5(e) to document:
- a description of the previously provided non-assurance service;
 - the results of the discussion with the audit committee;
 - any further measures applied to address the threat created by the provision of the previous non-assurance service; and
 - the rationale to support the decision of the member or firm.

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements Fees

- (36) A member or firm shall not provide an assurance engagement for a fee that the member or firm knows is significantly lower than that charged by the predecessor member or firm, or contained in other proposals for the engagement, unless the member or firm can demonstrate:
- (a) that qualified members of the firm have been assigned to the engagement and will devote the appropriate time to it; and
 - (b) that all applicable assurance standards, guidelines and quality control procedures have been followed.

Contingent fees

- (36.1) (a) A member or firm shall not provide, directly or indirectly, an assurance service on a contingent fee basis.
- (b) A member or firm shall not provide an assurance service to a client to whom he provides, directly or indirectly, any non-assurance service on a contingent fee basis when the outcome of the non-assurance service and the amount of the fee is dependent on a contemporaneous or future judgment related to a matter that is material to the subject matter of the assurance engagement.
 - (c) A member or firm shall not perform an audit or review engagement to a client to whom he provides, directly or indirectly, any non-assurance service on a contingent fee basis when:
 - (i) the contingent fee that is charged by the firm to the audit or review client is or is expected to be material to the firm;
 - (ii) a member of the audit or review engagement team for that client will be entitled to a portion of that contingent fee and that portion is material to that member of the audit or review engagement team; or
 - (iii) the outcome of the non-assurance service and the amount of the contingent fee is dependent on a contemporaneous or future judgment related to a matter that is material to the financial statements that are subject to audit or review by the member or firm.
 - (d) A member or firm shall not perform an audit or review engagement if a network firm that participates in a significant part of the audit or review engagement provides a non-assurance service on a contingent fee basis to the audit or review client and that contingent fee is expected to be material to that network firm.

Relative size of fees of a reporting issuer or listed entity audit client

- (37)(a) A member or firm shall not perform an audit engagement for a reporting issuer or listed entity when the total revenue, calculated on an accrual basis, for any services provided to the client and its related entities for the two consecutive fiscal years of the firm most recently concluded prior to the date of the financial statements subject to audit by the member or firm, represent more than 15% of the total revenue of the firm, calculated on an accrual basis, in each such fiscal year, unless:

- (i) *the member or firm discloses to the audit committee the fact that the total of such revenue represents more than 15% of the total revenue of the firm, calculated on an accrual basis, in each of those fiscal years; and*
- (ii) *another professional accountant who is not a member of the firm performs a review, that is substantially equivalent to an engagement quality control review, of the audit engagement, either*
 - (A) *prior to the audit opinion in respect of the financial statements being issued, or*
 - (B) *subsequent to the audit opinion in respect of the financial statements being issued but prior to the audit opinion on the client's financial statements for the immediately following fiscal period being issued.*

Thereafter, when the total revenue, calculated on an accrual basis, for any services provided to the client and its related entities continues to represent more than 15% of the total revenue of the firm, calculated on an accrual basis, in the firm's most recently concluded prior fiscal year, the member or firm shall not perform the audit unless the requirements of paragraphs (37)(a)(i) and (ii)(A) are met.

- (b) *A member shall not perform the review required by Rule 204.4(37)(a)(ii) if the member or the member's firm would be prohibited, pursuant to any provision of Rule 204, from performing an audit of the financial statements referred to in Rule 204.4(37)(a).*

GUIDANCE - Rule 204.4(36), (36.1) and (37)

Fees — Pricing

- 1 Rule 204.4(36) provides that a member or firm may not provide an assurance service at a fee level that the member or firm knows is significantly lower than that charged by the predecessor member or firm, or contained in other proposals for the engagement, unless the member or firm can demonstrate that the engagement will be performed properly by qualified staff and in accordance with all applicable professional standards.

Contingent fees

- 2 Rule 204.4(36.1) sets out the circumstances under which a contingent fee may not be charged for the provision of a non-assurance service to an assurance client.
- 3 However, a threat to independence may also be created by a contingent fee arrangement with an assurance client in situations when such a fee is not prohibited by Rule 204.4(36.1). The significance of any threat created will depend on such factors 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 of the assurance engagement.

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

- having another professional accountant review the relevant assurance work or otherwise advise as necessary; and
- using professionals who are not members of the engagement team to provide the service.

- 4 Corporate finance services are often provided on a contingent fee basis. When, in accordance with Rule 204.4(33), a member or firm is permitted to provide a corporate finance service to an assurance client and the corporate finance service is provided on a contingent fee basis, a threat to independence may be created. The significance of any threat created will depend on such factors as:
- the level of sophistication of the parties to the transaction and whether those parties are carrying out additional due diligence regarding the transaction;
 - whether amounts or disclosures in the financial statements of the client have a material impact on the fee;
 - whether the outcome of the corporate finance service depends upon a judgment relative to a material matter related to the subject matter of the assurance engagement, such as a material balance in the financial statements of the client; and
 - the materiality of the amount of the contingent fee to the member or firm.

The evaluation of the materiality of the amount of the contingent fee to a member requires that consideration be given to whether there is any member involved in providing the corporate finance service who is expected to receive compensation that is material to that member as a consequence of the firm receiving the contingent fee and who is also a member of the assurance engagement team.

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

- having another professional accountant review the relevant assurance work or otherwise advise as necessary; and
 - using professionals who are not members of the engagement team to provide the service.
- 5 Value billing, which is specifically set out as an exception to the definition of a contingent fee, should not be used to justify what is in substance an otherwise inappropriate contingent fee arrangement.

Fees — Overdue

- 6 A self-interest threat may exist if fees due from an assurance client for professional services remain unpaid for a long time, especially if a significant portion is not paid before the assurance report for the following year is issued. Generally the payment of such fees should be required before that report is issued. The following safeguards may be applicable:
- discussing the level of outstanding fees with the audit committee; and
 - involving another member of the firm who is not part of the engagement team, or a professional accountant who is not a member of the firm, to provide advice or review the work performed.

Members are cautioned that the overdue fees might create the same threats to independence as a loan to the client. Therefore, members should consider whether, because of the significance of such threats, it is appropriate for the firm to continue to provide assurance services to that client.

Fees — Relative size

- 7 When the total fees generated from an assurance client represent a significant proportion a member's or firm's total fees, the financial dependence on that client, or group of clients of which it is a part, including the possible concern about losing the client, may create a self-interest threat. The significance of the threat will depend upon factors such as:

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- the structure of the firm; and
- whether the member or firm is well established in practice.

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

- taking steps to reduce the dependency on the client;
- discussing the extent and nature of fees with the audit committee;
- having firm policies and procedures to monitor and implement quality control of assurance engagements;
- involving another member of the firm who is not on the engagement team to review the work done or advise as necessary;
- arranging for external quality control reviews; or
- consulting a third party, such as a professional regulatory body or a professional colleague who is not a member of the firm.

Relative size of fees of a reporting issuer or listed entity audit client

8 Rule 204.4(37)(a) provides that, unless specified measures are taken, a member or firm may not perform an audit engagement for a client that is a reporting issuer or listed entity, when, for the two consecutive fiscal years of the firm most recently concluded prior to the date of the financial statements subject to audit by the member or firm, the total revenue, calculated on an accrual basis, for services provided to that client and its related entities represent more than 15% of the total revenue of the firm, calculated on an accrual basis, in each such fiscal year. The measures required to be taken by the Rule are:

- disclosing, to the audit committee, that the revenue exceeds the 15% threshold; and
- completion, by another professional accountant who is not a member of the firm, of either a “pre-issuance” or “post-issuance” review of the audit engagement.

The Rule requires that either such review be substantially equivalent to an engagement quality control review. In the case of a “pre-issuance” review, the review is to be completed prior to the audit opinion in respect of the financial statements being issued. A “post-issuance” review may be completed after the audit opinion in respect of the financial statements has been issued but prior to the audit opinion on the client’s financial statements for the immediately following fiscal period being issued.

The Rule also requires the performance of a “pre-issuance” review if the total revenue, calculated on an accrual basis, for any services provided to the client continues to represent more than 15% of the total revenue of the firm, calculated on an accrual basis, in the firm’s most recently concluded fiscal year.

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RULE:

**204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Evaluation or compensation of partners**

(38) *A member who is or was a key audit partner shall not be evaluated or compensated based on the member's solicitation or sales of non-assurance services to the particular client or a related entity if such solicitation or sales occurred during the period during which the member is or was a key audit partner.*

GUIDANCE - Rule 204.4(38)

1 Evaluating or compensating a member of the engagement team for an audit or review client for selling non-assurance services to that audit or review client, may create a self-interest threat. The significance of the threat will depend on such factors as:

- the structure of the firm;
- the size of the fee for the assurance service; and
- the size of the fee for the non-assurance service.

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

- discussing the nature and extent of the fees with the audit committee;
- having firm policies and procedures to monitor and implement quality control of assurance engagements;
- involving another member of the firm who is not a member of the engagement team to review the work done or advise as necessary; or
- being subject to external practice inspection.

2 Rule 204.4(38) does not preclude such a key audit partner from being evaluated or compensated in relation to performing such services and sharing in the profits of the audit practice and the profits of the firm. Such a partner's evaluation may take into account a number of factors, including the complexity of the partner's engagements, the overall management of the relationship with the client including the provision of non-audit services, and the attainment of specific goals for the sale of assurance services to a client for which the partner is a key audit partner or for the sale of any services to a client for which the partner is not a key audit partner.

Members and firms should consider documenting their evaluation and compensation processes and systems in order to demonstrate compliance with the requirements of Rule 204.4(38).

**204 Independence
REQUIREMENTS:**

RULE:

***204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Gifts and hospitality***

- (39) *A member, [candidate or student] who participates on an engagement team for an assurance client and the member's, [candidate's or student's] firm shall not accept a gift or hospitality, including a product or service discount, from the client or a related entity, unless the gift or hospitality is clearly insignificant to the member, [candidate, student] or firm, as the case may be.*

204 Independence

RULES:

204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements
Client mergers and acquisitions

(40)(a) *A member or firm shall not perform or continue with an audit or review engagement for a entity where, as a result of a merger or acquisition, another entity merges with or becomes a related entity of the audit or review client, and the member or firm has a previous or current activity, interest or relationship with the other entity that would, after the merger or acquisition, be prohibited pursuant to any provision of Rule 204 in relation to the audit or review engagement, unless:*

- (i) the member or firm terminates, by the effective date of the merger or acquisition, any such activity, interest or relationship;*
- (ii) the member or firm terminates, as soon as reasonably possible and, in all cases, within six months following the effective date of the merger or acquisition, any such activity, interest or relationship and the requirements of Rule 204.4(40)(b) are met; or*
- (iii) the member or firm has completed a significant amount of work on the audit or review engagement and expects to be able to complete the engagement within a short period of time, the member or firm discontinues in the role of audit or review service provider on completion of the current engagement and the provisions of Rule 204.4(40)(b) are met.*

(b) Notwithstanding the existence of the previous or current activity, interest or relationship described in Rule 204.4(40)(a), the provisions of Rule 204.4(40)(a)(ii) and (iii) permit the member or firm to perform or continue with the audit or review engagement provided that:

- (i) the member or firm evaluates and discusses with the audit committee the significance of the threat created by any such activity, interest or relationship and the reasons why the activity, interest or relationship is not terminated or cannot reasonably be terminated by the effective date of the merger or acquisition, or within six months thereof, as the case may be;*
- (ii) the audit committee requests the member or firm to complete the audit or review engagement;*
- (iii) any person involved in any such activity or who has any such interest or relationship will not participate in the audit or review engagement or as an engagement quality control reviewer; and*
- (iv) the member or firm applies an appropriate measure or measures, as discussed with the audit committee, to address the threat created by any such activity, interest or relationship.*

(c) Where the previous or current activity, interest or relationship described in Rule 204.4(40)(a) creates such a significant threat to independence that compliance with the requirements of paragraphs 204.4(40)(a) and (b) would still not reduce any such threat to an acceptable level, the member or firm shall not perform or continue with the audit or review engagement.

GUIDANCE - Rule 204.4(40)

1 Where an activity, interest or relationship that would impair independence is not terminated by the effective date of the merger or acquisition, Rule 204.4(40)(b) describes the circumstances in which the member or firm may perform or continue with the audit or review engagement, including a requirement that the member or firm apply an appropriate measure or measures, as discussed with the audit committee. Examples of such a measure or measures are:

- having another public accountant review the audit or review or any relevant non-assurance work as appropriate;

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- engaging another firm to evaluate the results of any relevant non- assurance service or to re-perform any relevant non-assurance service to the extent necessary to enable it to take responsibility for the service; and
 - having another professional accountant, who is not a member of the firm performing the audit or review engagement, perform a review that is equivalent to an engagement quality control review.
- 2 Rule 204.4(40)(c) provides that even if all of the other requirements of the Rule are met, where an activity, interest or relationship creates such a significant ongoing threat to independence that compliance with paragraphs 204.4(40)(a) and (b) will still not reduce the threat to an acceptable level, the member or firm is required to resign from the particular audit or review engagement. In determining whether the activity, interest or relationship continues to create such a significant threat that the member or firm would be required to resign, consideration should be given to:
- the nature and significance of the activity, interest or relationship;
 - the extent, if any, to which the activity, interest or relationship continues to affect the financial statements subject to audit or review by the member or firm;
 - the nature and significance of the new relationship with the other entity, for example, whether that other entity becomes a parent, a subsidiary or the client itself; and
 - the adequacy of the actions taken, as described in Rule 204.4(40)(b), to address the activity, interest or relationship.

In addition, members and firms are reminded of the requirement pursuant to Rule 202.2 to perform professional services with an objective state of mind.

Documentation

- 3 Members and firms are also required by Rule 204.5(f) to document:
- a description of the activity, interest or relationship that will not be terminated by the effective date of the merger or acquisition and the reasons why it will not be terminated;
 - the results of the discussion with the audit committee and measures applied to address the threat created by any such activity, interest or relationship; and
 - the rationale to support the decision of the member or firm.

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RULES:

204.5 Documentation

- (a) A member or firm who, in accordance with Rule 204.3, has identified a threat that is not clearly insignificant, shall document a decision to accept or continue the particular engagement. The documentation shall include the following information:
- (i) a description of the nature of the engagement;
 - (ii) the threat identified;
 - (iii) the safeguard or safeguards identified and applied to eliminate the threat or reduce it to an acceptable level; and
 - (iv) an explanation of how, in the member's or firm's professional judgment, the safeguards eliminate the threat or reduce it to an acceptable level.
- (b) A member or firm who, in an emergency situation, provides an accounting or bookkeeping service to a reporting issuer or listed entity audit client in accordance with the requirements of Rule 204.4(24) shall document both the rationale supporting the determination that the situation constitutes an emergency and that the member or firm has complied with the provisions of subparagraphs (i) through (iv) of the Rule.
- (c) A member or firm who, in an emergency situation, prepares tax calculations of current and future income tax liabilities or assets for a reporting issuer or listed entity audit client in accordance with the requirements of Rule 204.4(34)(b), for the purpose of preparing accounting entries that are subject to audit by the member or firm shall document both the rationale supporting the determination that the situation constitutes an emergency and that the member or firm has complied with the provisions of subparagraphs (i) through (iv) of the Rule.
- (d) A member or firm who, in accordance with the requirements of Rule 204.4(35)(a), performs an audit or review engagement for a client where the member, firm, a network firm or a member of the firm or a network firm has provided a non-assurance service referred to in Rules 204.4(22) to (34) to the client prior to the engagement period but during or after the period covered by the financial statements subject to audit or review by the member or firm, shall document:
- (i) a description of the previously provided non-assurance service;
 - (ii) the results of the discussion with the audit committee;
 - (iii) any further measures applied to address the threat created by the provision of the previous non-assurance service; and
 - (iv) the rationale to support the decision of the member or firm.
- (e) A member or firm who, in accordance with the requirements of Rules 204.4(35)(b), performs an audit engagement for a client that has become a reporting issuer or listed entity where the member, the firm, a network firm or a member of the firm or a network firm provided a non-assurance service to the client prior to it having become a reporting issuer or listed entity and the provisions of Rules 204.4(22) to (34) would have precluded the member or firm from performing an audit engagement for a reporting issuer or listed entity, shall document:
- (i) a description of the non-assurance service;
 - (ii) the results of the discussion with the audit committee;
 - (iii) any further measures applied to address the threat created by the provision of the non-assurance service; and
 - (iv) the rationale to support the decision of the member or firm.

- (f) A member or firm who, in accordance with the requirements of Rules 204.4(40)(a) and (b), performs or continues with an audit or review engagement where, as a result of a merger or acquisition, another entity merges with or becomes a related entity of the audit or review client, and the member or firm has a previous or current activity, interest or relationship with the other entity that would, after the merger or acquisition, be prohibited pursuant to any provision of Rule 204 in relation to the audit or review engagement, shall document:*
- (i) a description of the activity, interest or relationship that will not be terminated by the effective date of the merger or acquisition and the reasons why it will not be terminated;*
 - (ii) the results of the discussion with the audit committee and measures applied to address the threat created by any such activity, interest or relationship; and*
 - (iii) the rationale to support the decision of the member or firm.*

204 Independence

RULES:

204.6 Breach of a provision of Rule 204.3 or 204.4

- (a) *When a member [candidate or student] identifies a breach of any of the provisions of Rule 204.3 or 204.4 with respect to an assurance engagement, the member [candidate or student] shall immediately communicate the nature of the breach in accordance with the firm's policies and procedures that address the reporting of such breaches.*
- (b) *The individual who has received notification of the breach shall ensure that:*
 - (i) *the significance of the breach is evaluated;*
 - (ii) *the actions set out in (d) to (h) are taken; and*
 - (iii) *the nature of the breach is communicated to a network firm, when appropriate.*
- (c) *Notwithstanding the provisions of Rule 204.2, when a breach of the provisions of Rule 204.3 or 204.4 is identified, the affected assurance engagement may be continued provided that:*
 - (i) *the activity, interest or relationship that caused the breach is terminated, suspended or eliminated and the consequences of the breach are addressed;*
 - (ii) *any legal or regulatory requirements that apply with respect to the breach are met;*
 - (iii) *the significance of the breach and its impact on objectivity and the ability to issue an audit opinion, review engagement report, or other assurance report, as applicable, is evaluated and a conclusion is reached that it is possible to take action that is appropriate in the circumstances to satisfactorily address the consequences of the breach such that a reasonable observer would be likely to conclude that objectivity has not been compromised, and*
 - (iv) *concurrence with that conclusion is obtained in accordance with the provisions of paragraph (d) below:*
 - (A) *in the case of an assurance engagement that is not an audit or review engagement, from the audit committee or those charged with governance, or the party that engaged the firm, as appropriate; or*
 - (B) *in the case of an audit or review engagement, from the audit committee or those charged with governance.*
- (d) *(i) When a conclusion is reached that action has been or can be taken that is appropriate in the circumstances to satisfactorily address the consequences of the breach, the matter shall be discussed with the audit committee or those charged with governance, or, in the case of an assurance engagement that is not an audit or review engagement, the party that engaged the firm, and concurrence with that conclusion shall be obtained.*
 - (ii) *In the case of an assurance engagement that is not an audit or review engagement, the timing for such a discussion shall take into account the circumstances of the engagement and the breach.*
 - (iii) *In the case of an audit or review engagement, such a discussion shall take place as soon as possible, unless an alternative timing for reporting less significant breaches has been specified by the audit committee or those charged with governance and the breach is less significant. In addition, the following matters shall be communicated in writing to the audit committee or those charged with governance:*
 - (A) *the nature, duration and significance of the breach;*
 - (B) *how the breach occurred and was identified;*
 - (C) *the action taken or proposed to be taken and the rationale as to how the action will satisfactorily address the consequences of the breach and enable the audit or review engagement to continue;*
 - (D) *a description of the firm's policies and procedures relevant to the breach designed to provide reasonable assurance that independence is maintained and any steps*

- that the firm has taken or proposes to take to reduce or avoid the risk of further breaches occurring; and*
- (E) the conclusion that objectivity has not been compromised.*
- (e) (i) If a conclusion is reached that it is not possible to take action that is appropriate in the circumstances to satisfactorily address the consequences of the breach, the matter shall be discussed, as soon as possible, with the audit committee or those charged with governance, or, in the case of an assurance engagement that is not an audit or review engagement, the party that engaged the firm, and the necessary steps shall be taken to terminate the engagement in compliance with any applicable legal or regulatory requirements relevant to terminating the engagement.*
- (ii) If the audit committee or those charged with governance, or party that engaged the firm does not concur with the conclusion that action can be taken to satisfactorily address the consequences of the breach, the necessary steps shall be taken to terminate the engagement in compliance with any applicable legal or regulatory requirements relevant to terminating the engagement.*
- (f) If the breach occurred prior to the issuance of a previous audit opinion, review engagement report or other assurance report,*
- (i) consideration shall be given to the impact of the breach, if any, on any previously issued audit opinions, review engagement reports or other assurance reports;*
- (ii) the matter shall be discussed with the audit committee or those charged with governance, or, in the case of an assurance engagement that is not an audit or review engagement, the party that engaged the firm; and*
- (iii) consideration shall be given to whether it is necessary to withdraw such opinions or reports.*
- (g) The following matters shall be documented:*
- (i) the breach;*
- (ii) the action taken;*
- (iii) key decisions made;*
- (iv) the consideration of the impact of the breach, if any, on previously issued audit opinions, review engagement reports or other assurance reports;*
- (v) the conclusion, if such a conclusion is reached, that objectivity has not been compromised such that an audit opinion, review engagement report or other assurance report can be issued;*
- (vi) an analysis supporting that conclusion;*
- (vii) all the matters discussed with the audit committee or those charged with governance, or the party that engaged the firm; and*
- (viii) discussions, if any, with [CPA Province/the Institute], a relevant regulator or other oversight authority.*
- (h) In the event of a breach of the provisions of Rule 204.3 or 204.4 that results in a conclusion to withdraw any previously issued audit opinion, review engagement report or other assurance report, information concerning any such breach shall be reported to [CPA Province/the Institute].*

GUIDANCE- RULE 204.6

- 1** Rule 204.6 addresses a situation when a member [candidate or student] identifies,
- (a) the existence of an activity, interest or relationship that, had it been identified prior to the commencement of the assurance engagement, would have either prohibited the provision of the engagement or would have created a threat to independence which*

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- would have required the evaluation of its significance and the application of safeguards to reduce it to an acceptable level, or
- (b) that the safeguards implemented to address a threat that was previously identified have not been effective in reducing the threat to independence to an acceptable level.

Such circumstances constitute a breach of Rule 204 and may occur despite the firm having policies and procedures designed to provide reasonable assurance that independence is maintained. A consequence of such a breach may be that termination of the assurance engagement is necessary.

- 2 When a member [candidate or student] identifies that such a breach has occurred, Rule 204.6 requires that:
- the breach be reported immediately in accordance with the firm's policies and procedures that address the reporting of such breaches;
 - the activity, interest or relationship that caused the breach be terminated, suspended or eliminated; and
 - the consequences of the breach be addressed.

The firm is required by *The CPA Canada Handbook – Assurance* (CSQC1) to establish policies and procedures designed to provide it with reasonable assurance that it is notified of breaches of independence requirements and to enable it to take appropriate actions to resolve such situations. CSQC 1 also requires that such notification be provided to specified individuals within the firm.

- 3 When a breach is identified the individual who has received notification of the breach is required to ensure that an evaluation is made of the significance of that breach, its impact on objectivity and whether an audit opinion, review engagement report, or other assurance report may still be issued or a previously issued report needs to be withdrawn. Such an evaluation requires the exercise of professional judgment, taking into account whether a reasonable observer would be likely to conclude that objectivity would be compromised. The significance of the breach will depend on factors such as:
- the nature and duration of the breach;
 - the number and nature of any previous breaches with respect to the assurance engagement;
 - whether a member of the engagement team had knowledge of the activity, interest or relationship that caused the breach;
 - whether the individual who caused the breach is a member of the engagement team or another individual for whom there are independence requirements;
 - if the breach relates to a member of the engagement team, the role of that individual;
 - if the breach was caused by the provision of a professional service, the impact of that professional service, if any, on the subject matter of the engagement; and
 - the extent of the threat or threats created by the breach.
- 4 Depending upon the significance of the breach, it may be necessary to terminate the assurance engagement or withdraw a previously issued assurance report, or it may be possible to take action that is appropriate in the circumstances to satisfactorily address the consequences of the breach.
- 5 Examples of actions that may be appropriate include:
- removing the relevant individual from the engagement team;
 - conducting an additional review of the affected assurance engagement work or re-performing that work to the extent necessary, in either case using different personnel;

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- recommending that the client engage another firm to review or re-perform the affected assurance engagement work to the extent necessary; and
- when the breach relates to a non-assurance service that affects the subject matter of the assurance engagement, 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.

204 Independence

RULES:

204.7 Members Must Disclose Prohibited Interests and Relationships

- (a) A member, [candidate or student] who has a relationship or interest, or who has provided a professional service, that is precluded by this Rule shall advise in writing a designated partner of the firm of the interest, relationship or service.*
- (b) A member, [candidate or student] who has been assigned to an engagement team for an assurance client shall advise, in writing, a designated partner of the firm of any interest, relationship or activity that would preclude the person from being on the engagement team.*

204 Independence

RULE:

204.8 Firms To Ensure Compliance

A firm that performs an assurance engagement shall ensure that members of the firm do not have a relationship or interest, do not perform a service and remain free of any influence that would preclude the firm from performing the engagement pursuant to Rules 204.1, 204.3, 204.4 or 204.9.

(Note this rule assumes discipline of firms – the alternate rule applying to members is below)

A member who is a partner or proprietor of a firm, or a member whose professional corporation is a partner or proprietor of a firm, shall ensure that the firm complies with Rules 204.1, 204.3, 204.4 and 204.9 and that members of the firm do not have a relationship or interest, do not perform a service and remain free of any influence that would preclude the firm from performing the engagement pursuant to Rules 204.1, 204.3, 204.4 or 204.9.

GUIDANCE - Rule 204.8

- 1 Members of the firm include all those persons who are associated with the firm in carrying out its activities. Members of the firm, including employees, who are not under the jurisdiction of [CPA province/the Institute] could have an interest or relationship or provide a service that would result in the firm being prohibited from performing a particular engagement. Rule 204.8 requires a member who is a partner or proprietor of a firm to ensure that the firm and all members of the firm, including those who are not registrants, do not have a relationship or interest, do not perform a service and remain free of any influence that would preclude the firm from performing the engagement pursuant to Rules 204.1, 204.3, 204.4 or 204.9.

204 Independence

204.9 Independence: Insolvency Engagements

DEFINITIONS:

For purposes of Rule 204.9

“the Acts” means the federal Companies’ Creditor Arrangement Act, the Bankruptcy and Insolvency Act, the Winding-up and Restructuring Act and relevant provincial or territorial legislation, or any combination of them, as the circumstances may require.

“agent for a secured creditor”, “liquidator”, “inspector”, “receiver”, “receiver-manager”, “trustee”, and “trustee in bankruptcy” all have the meanings ascribed to them under the Acts.

RULE:

A registrant who engages or participates in an engagement to act in any aspect of insolvency practice, including as a trustee in bankruptcy, a liquidator, a receiver or a receiver-manager, shall be and remain independent such that the registrant and members of the firm shall be and shall remain free of any influence, interest or relationship which, in respect of the engagement, impairs the professional judgment or objectivity of the registrant or member of the firm or which, in the view of a reasonable observer, would impair the professional judgment or objectivity of the registrant or a member of the firm.

GUIDANCE - Rule 204.9

- 1 Rule 204.9 deals with objectivity and independence in insolvency practice. This Guidance sets out how, in [the Board's/Council's] opinion, a reasonable observer might be expected to view certain situations related to insolvency practice.
- 2 A registrant, or member of the firm, and their respective immediate families, should not acquire directly or indirectly in any manner whatsoever any assets under the administration of the registrant, provided that any of the foregoing may acquire assets from a retail operation under administration of the registrant where those assets are available to the general public for sale and that no special treatment or preference over and above that granted to the public is offered to or accepted by the registrant or the member of the firm and their respective immediate families.
- 3 A registrant should avoid being placed in a position of conflict of interest and, in keeping with this principle, should not accept any appointment, unless expressly permitted by the court, as a receiver, receiver-manager, agent for a secured creditor, or liquidator, or any other appointment under the Acts, except as an inspector, in respect of any debtor, where the registrant is, or at any time during the two preceding years was:
 - a director or officer of the debtor;
 - an employer or employee of the debtor or of a director or officer of the debtor;
 - related to the debtor or to any director or officer of the debtor; or
 - the auditor, accountant or legal counsel, or a partner or an employee of the auditor, accountant or legal counsel of the debtor.
- 4 Where a conflict of interest may exist, or may appear to exist, a registrant should make full disclosure to, and obtain the consent of, all interested parties and, in keeping with this principle, should not accept any appointment:
 - as trustee where the registrant has already accepted an appointment as receiver, receiver-manager, agent of a secured creditor, liquidator, trustee under a trust indenture

- issued by the bankrupt corporation or by any corporation related to the bankrupt corporation, or on behalf of any person related to the bankrupt without having first made disclosure of such prior appointment. The registrant should inform the creditors of the bankrupt of the prior appointment as soon as reasonably possible;
- as receiver, receiver-manager, agent for a secured creditor or on behalf of any person related to the bankrupt where the member or firm has already accepted an appointment as trustee without first obtaining the permission of the inspectors of the bankrupt estate. Where inspectors have not been appointed at the time that the second appointment is to be taken, the registrant should obtain the approval of the creditors of the bankrupt of having taken the second appointment as soon as reasonably possible; and if the second appointment is taken before obtaining the approval of the creditors, it should be taken subject to their approval;
 - as receiver, receiver-manager, agent for a secured creditor or trustee in respect of any corporation where the registrant is, or at any time during the two-year period commencing at the date of the last audit report or the last review engagement report was, the trustee (or related to such trustee) under a trust indenture issued by such corporation or by any corporation related to such corporation without first obtaining the permission of the creditors secured under such trust indenture. Upon the acceptance of any such appointment as trustee, the member or firm should inform the creditors of the bankrupt corporation of the prior appointment as (or relationship to) the trustee under a trust indenture issued by the bankrupt corporation or by any corporation related to the bankrupt corporation as soon as reasonably possible;
 - as receiver, receiver-manager, agent for a secured creditor, liquidator of an insolvent company, in respect of any corporation where the registrant is related to an officer or director of such corporation; or
 - as receiver, receiver-manager, agent for a secured creditor, or trustee in respect of any person or corporation where the registrant is a creditor, or an officer or director of any corporation that is a creditor, of such person or corporation unless the relationship is sufficiently remote that the member or firm can act having independence in fact and appearance.
- 5 For purposes of paragraphs 3 and 4 of this Guidance, persons are related to each other if they are defined as such under the Acts.
- 6 A registrant engaged in insolvency practice should ensure there are no relationships with retired partners which may be seen to impair the registrant's independence. For more information on retired members, refer to the information set out in the Guidance related to the definition of "member of a firm" in the Definitions section of Rule 204.

204 Independence

RULE:

204.10 Disclosure of Impaired Independence

A member or firm engaged in the practice of public accounting or any related business or practice, who provides a service not subject to the requirements of Rules 204.1 to 204.9, shall disclose any activity, interest or relationship which, in respect of the engagement, would be seen by a reasonable observer to impair the member's or firm's independence such that the professional judgment or objectivity of the member, firm or member of the firm would appear to be impaired, and such disclosure shall be made in the member's or firm's written report or other written communication accompanying financial statements or financial or other information and the disclosure shall indicate the nature of the activity or relationship and the nature and extent of the interest.

GUIDANCE - Rule 204.10

- 1 Members and firms who provide a professional service which does not require the member or firm to be independent are required by Rule 204.10 to disclose any influence, interest or relationship which, in respect of the professional service, would be seen by a reasonable observer to impair the member's or firm's independence. Members and firms should refer to Rules 204.1 to 204.9 and the related Guidance when determining whether they must be independent and would appear to be independent with respect to particular engagements.
- 2 Such disclosure is required whether or not any written report or other communication is provided and should indicate the nature of the influence or relationship and the nature and extent of the interest. Any written communication concerning or accompanying financial statements or financial or other information must include such disclosure.
- 3 Independence is not required for compilation engagements. Where the provider of the compilation service may be seen to be lacking independence, the disclosure requirement of Rule 204.10 applies.
- 4 For the purposes of Rule 204.10 the preparation of accounting records or journal entries in connection with a compilation engagement is not an activity that requires disclosure in the Notice to Reader unless such preparation involves complex transactions as contemplated by paragraph 11 of the Guidance to Rule 204.4(22) to 204.4(24).
- 5 Tax return services may require disclosure in respect of some of the information filed with the return. If the return is simply the assembling and reporting of information provided by the taxpayer, then the member or firm involved has simply processed that information and disclosure should not be necessary.
- 6 Members and firms are cautioned that disclosure under Rule 204.10 does not relieve them from their obligation to comply with the CPA Code and in particular Rules 201, 202, 205 and 206.

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204 Independence

Rules 204.11 to .19 are reserved for future use.

204 Independence

204.20 Audits under elections legislation

DEFINITIONS:

For purposes of Rule 204.20 and its related Guidance.

“the Act” means the Canada Elections Act or the relevant provincial or territorial legislation.

“electoral candidate” means a candidate as defined by the Act.

“registered agent”, “registered party”, “official agent”, “registered association”, “leadership contestant”, “nomination contestant” and “election period” have the meaning given to them in the Act.

RULE:

A member or firm who performs an audit under federal, provincial, territorial or other legislation in relation to an electoral candidate, registered agent, registered party, official agent, registered association, leadership contestant, or a nomination contestant shall comply with the provisions of Rules 204.1 and 204.3.

GUIDANCE - Rule 204.20

Introduction

- 1 The Act requires the filing of audited returns by the chief agents of registered parties, the official agents of electoral candidates and, in some cases, the financial agents of registered associations, leadership contestants and nomination contestants. Each return is to be reported on by an auditor who is a member in good standing of a corporation, an association or a body of professional accountants and includes a firm.

Ineligibility Provision - Statutory

- 2 The Act lists a number of persons (hereinafter referred to as “ineligible persons”) who cannot act as auditors for a registered party, electoral candidate, registered association, leadership contestant or nomination contestant. These are:
 - an election officer or a member of the staff of a returning officer;
 - an electoral candidate;
 - an official agent of an electoral candidate;
 - a chief agent of a registered party or an eligible party;
 - a registered agent of a registered party;
 - electoral district agents of registered associations;
 - leadership contestants and their leadership campaign agents;
 - nomination contestants and their financial agents; and
 - financial agents of registered third parties.
- 3 The Act prohibits an ineligible person from participating in the audit examination of the records or in the preparation of the audit report of an electoral candidate, a leadership contestant or a nomination contestant (except to respond to the auditor’s request for information). There is no similar restriction placed on the auditor of a registered party or a registered association. An eligible person may be appointed as auditor for an electoral candidate notwithstanding that the person is a member of a firm that has been appointed as an auditor for a registered party or for an electoral candidate in another electoral district.

Extension of Ineligibility Provisions

- 4 Without wishing to extend the statutory prohibitions unduly, [CPA Province/the Institute] considers that there are additional interests or relationships to those spelled out in the Act,

which could impair, or appear to impair, an auditor's objectivity. This Guidance, therefore, sets out the profession's views on unacceptable interests or relationships, in respect of audits under the Act, encompassing both those prohibited by the statute and those unacceptable professionally.

- 5 Requirements that are too restrictive, coupled with the widespread involvement of registrants, as citizens, in the political process, could make it almost impossible for the audit provisions of the Act to be given practical effect. Accordingly, this Guidance seeks to cover only the more obvious interests and relationships which might be considered unacceptable. Too narrow an interpretation could, in view of the many conceivable conflicts of interest, make it almost impossible for registrants to serve the community's needs.

Audit of a Candidate

- 6 A registrant may not be complying with Rule 204.1 if the registrant were to act as auditor of an electoral candidate as well as being:
- a paid worker during an election period for any electoral candidate or any registered party;
 - a volunteer worker during an election period for that electoral candidate or the registered party of that electoral candidate where:
 - the registrant exercises any function of leadership or direction in that electoral candidate's or that party's campaign organization, or
 - the registrant carried on any significant function involving the raising, spending or custody of that electoral candidate's or that party's campaign funds;
- or if a registrant's immediate family member, or another person in the firm is:
- a returning officer, deputy returning officer, assistant returning officer or election clerk in the electoral district of that electoral candidate or is the electoral candidate, official agent of that electoral candidate or a registered agent of that electoral candidate's registered party;
 - a paid worker during an election period for that electoral candidate or that electoral candidate's registered party;
 - a volunteer worker as described above, during an election period, for that electoral candidate or the registered party of that electoral candidate.
- 7 Where a registrant is an "ineligible person" in respect of a particular electoral candidate, the application of Rule 204.1 means that the firm with which that registrant is associated may not act as auditor of that electoral candidate.

As noted in paragraph 3, the ineligible persons described in the Act may not participate in the audit examination of any electoral candidate's return. As an extension of this, a registrant who could not act as auditor for an electoral candidate because of any of the relationships detailed in paragraph 6 above, should also not participate in the audit examination of a candidate's return.

Audit of a Registered Party, Registered Association, Leadership Contestant or Nomination Contestant

- 8 In addition to the statutory prohibitions set out in the Act, a registrant may not be complying with Rule 204.1 if the registrant were to act as auditor of a registered party, registered association, leadership contestant or nomination contestant and the registrant, or an immediate family member, or another person in the firm is a paid worker or volunteer worker who exercises any function of leadership or direction or carried on any significant function involving the raising, spending or custody of funds belonging to the party, association or contestant, as the case may be.

Other considerations

- 9 Generally, registrants contemplating acting as auditors for registered parties, electoral candidates, associations or contestants should be alert to any circumstances, not described in this Guidance, which may place them in the position of impairment of objectivity or where an appearance of impairment might be presented. This type of question tends to arise, for example, where a donation of cash or of professional services is made. Registrants, as citizens, have the same responsibility to be involved in the political process as other citizens; such involvement may include financial support of a registered party, candidate association or contestant by a registrant, the registrant's immediate family or other persons in the firm. The making of a financial contribution or the donation of professional services does not, of itself, necessarily create an impairment of objectivity, in these particular circumstances.

Registrants should recognize, however, the need to apply judgment to the question of the amount of any such contribution and must be satisfied that any such contribution does not in fact impair their objectivity or independence.

It is of paramount importance that a registrant accepting an appointment under the Act makes such acceptance known to all other persons in the firm so as to avoid any conflict arising within the provisions of the Act concerning ineligible persons.