

## **GUIDELINES ON NETWORKS AND NETWORK FIRMS**

### **Introduction:**

When a firm forms a larger structure with the co-operation of other firms or entities with an aim to enhance their ability to provide Professional services to the intended parties, this formation of a larger structure becomes a Network firm. Formation of a larger structure in itself does not make a network firm. Creation of a larger structure to function as a network firm depends on the particular fact and circumstances. It does not depend on the fact whether the involved firms or entities are legally separate and distinct.

### **Objectives:**

Main objectives of the formation of the Network firm are to enhance:

- their ability to provide professional services to the intended parties;
- their standard of performing professional services in accordance with the requirements of IFRS/NFRS, ISAs, ISEs, ISQCs, ISREs and other pronouncements made by the IFAC and the Accounting Professional Regulatory bodies of the local jurisdiction;
- their reputation and thereby enlarging their professional activities; and
- their earnings

### **Facts and circumstances:**

Requirements to identify whether a larger structure so created in fact is a network firm has to be first determined by the associate firm itself by considering the following fact and circumstances:

- by exercising professional judgement to identify whether a network indeed is created;
- by considering that a reasonable and informed third party would be likely to conclude that involved firms are associated in a such a way that a network firm exists; and
- apply this judgment consistently throughout such a large structure.

Facts and circumstances to identify whether a firm is a Network firm are but not limited to the followings:

### **Whether the larger structure:**

- is aimed at creating cooperation within the network firms and entities; and also
- clearly aimed at sharing profit or loss among the entities within the structure;

***Further to above the entities within the structure;***

- share common ownership, control or management;
- share common quality control policies and procedures;
- share common business strategy;
- share the use of a common brand name; and
- share a significant part of professional resources.

**Professional Resources include:**

Sharing of the professional resources is a very significant element to identify whether a firm is indeed a network firm. Sharing of professional resources includes but not limited to, the following:

- Common systems that enable firms to exchange information such as a client data, billing and time records;
- Partners and other personnel;
- Technical departments that consult on technical or industry specific issues, transactions or events for assurance engagements;
- Audit methodology or audit manuals; training courses and facilities

Some examples in brief could explain clearly that which element of sharing of resources enables sharing of resources as “**significant element of sharing of resources:**

- Shared resources might be limited to common audit methodology or audit manuals with no exchange of personnel or client or market information. In this situation it is unlikely that the shared resources would be significant. the same applies to common training endeavor;
- The shared resources might involve the exchange of personnel or information for example where personnel are drawn from a shared pool of the larger structure of the network firm; or
- Where a technical pool of experts is created within the larger structure of firm to provide participating firms with technical advice that participating firms are required to follow in discharging their professional responsibilities. In such circumstances a reasonable and informed third party is more likely to conclude that the shared resources are significant.

**Conditions and circumstances enabling the formation of network firm:**

Conditions and circumstances indicated hereunder throw more insights to distinguish and determine the real status of the formation of larger structure to be identified as a network firm:

- The larger structure might be aimed only at facilitating referral of work which in itself does not meet the criteria necessary to constitute a network;

- The sharing of immaterial costs for example sharing of costs related to development of audit methodologies, manuals or training courses etc. does not in itself create a network;
- The association between a firm or an otherwise unrelated entity jointly to provide a service or develop a product does not in itself create a network;
- A cooperation merely with another entity with a sole aim to respond jointly to the request or an offer for a professional service does not in itself create a network;
- Merely using a common brand name does not create a network unless it includes common initials or common name: for example, the common brand name as part of, or along with, its firm name when a partner of a firm signs an audit report;
- Firms and entities *shall take due care* to prevent the perception that might be created that a firm belongs to a network firm even if that firm does not belong to a network firm and does not use the common brand name as part of the firm name for example: by using brand name on stationery or sign board or presenting as a network by virtue thought other means such as only taking the membership or other materials which do not fulfill the above criteria of becoming network firm.

### **Requirement of Independence**

A network firm shall be independent of the audit clients of the other firms within the network.

Independence requirements that apply to the network firm shall apply to any entity or firm that meets the definition of network firm. However, it is not necessary for the entity also to meet the definition of a firm for example, a consulting practice or professional Law practice might be a network firm but not a firm. It could be a proprietary, partnership or a company

Independence of Professional Accountants in public Practice or in business (PAIPP or PAIB) is all about the independence of professional judgement in course of discharging professional responsibility. Independence in other word is the judgement concluded in course of professional activities with being pressurized or coerced and also avoiding influences to compromise the concluded judgement so made by the Professional accountants in discharging professional responsibilities. This is the hallmark of the accounting profession that has earned the confidence of the intended users in this accounting profession.

### **Requirement of disclosure**

in the event of sale of a component of its practice and the component firm continues to use all or part of the firm's or network firm's name for a limited time, the relevant parties shall determine how to disclose that they are not network firm when presenting themselves to the outside parties.

Documentation:

The network firm and involved firms in the network larger structure of firm are required to maintain all significant matters from the date of formation of network firm till the continuation of network;

Network firm and its involved firms shall document the measures undertaken to safeguard threats to independence during their continuation of network in a manner that when a reasonable and informed third party is more likely to conclude that that suitable measures were taken to reduce the threat to an acceptable level and the that the independence of the network firm is not compromised.

#### **Registration of the network firm:**

Professional Accountants in public practice (firm or individual) holding valid Certificate of Practice (COP) from the Institute of Chartered accountants of Nepal (ICAN) shall have to submit authenticated documentary evidence such as signed contract or agreement with the network firm together with the stipulated amount of fees for registration and for renewal as the case may be, with ICAN in form: A. The contract or agreement for the networking in between the foreign firm of larger structure and the local firm shall meet all conditions and circumstances required for enabling the formation of network firm stated herein before in the headlines “*Conditions and circumstances enabling the formation of network firm*”.

#### **Name of the network firm:**

After the registration of the network firm, the Institute of Chartered Accountants of Nepal (ICAN) approves the local network form to use the words such as: “affiliate to ..... (name of the international network firm. In no condition the local network firm shall further add any words excepting “affiliate to .....(name of the international network firm).

#### **Use of name or brand name of network firm on the stationery of affiliate firm:**

Subsequent to the registration or renewal of the network firm with Institute of Chartered Accountants of Nepal (ICAN), the affiliate firm shall be allowed to use the brand name or the name of the international network firm *but not “the logo of any kind”* on the stationery, letter head or visiting card in course of performing and submitting any report on assurance or non-assurance engagements

In case of not continuing or having not renewed the network firm with the concerned international network firm and with the Institute of Chartered Accountants of Nepal (ICAN) the affiliate firm ceased to be a network firm. In such condition the affiliate network firm shall not in any manner, creates misrepresentation whereby the intended knowledgeable third party may

conclude that the network firm is still continuing. In such circumstances, the affiliate firm shall be held liable disciplinary action for noncompliance with the provisions of Code of Ethics.

**Payment of withholding and income taxes: other applicable taxes and repatriation of network firm's share of profit:**

Withholding, income tax and other taxes shall be paid by the affiliate network firm in Nepal in time to concerned tax authorities of Nepal along with the documentary evidence thereof. The affiliate network firm of Nepal after repatriating the share of profit to the network firm shall have to submit the evidence of repatriation through banking channel at least the end of each financial year along with the Income tax return of affiliate network firm.

**Requirements of Compliance with Ethical and professional standards:**

Once the relation of network firm is established it becomes the obligation of both the international and local affiliate network firm to comply with the requirements of "Fundamental principles of section 100"; the "Conceptual framework of section 120"; independence of Part - 4A relating to "Independence for Audit and Review engagements" which applies when performing audit or review engagements and Part-4B relating to "Independence for Assurance engagements other than audit and review engagements" which applies when performing assurance engagements that are not audit or review engagements of the International Code of Ethics and other professional standards such as : IFRS, NFRS and ISAs of both IFAC and ICAN.

In case any provision of this guidelines is found inconsistent and conflicting with the provisions of the Code of ethics such inconsistent and conflicting provisions shall be ultra vires and the provisions of Code of Ethics of IFAC and ICAN shall supersede such inconsistent and conflicting provisions of this guidelines.

*For better and comprehensive understanding, refer "Hand book of the International Code of Ethics for professional Accountants including Independence International Standards. Section 100; section 120; independence of Part -4 A and B and for network firm section 400.50 A1 to R 400.60 A1 which consist of "Requirement marked as" R" before the number of respective sections for mandatory compliance of the matters of the said provision and "Application materials meant for further explanations to safeguard against various kinds of threats explained in the conceptual framework marked as "A" after the subsection numbers.*