

## TECHNICAL BRIEFING PAPER

**Subject:** APES GN 41 *Management Representations*

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### Background

A Member in Business who is a Chief Financial Officer (CFO) or a Senior Finance Person (SFP) of the organisation will often provide representations to Those Charged with Governance (TCWG) or external parties on various matters to provide them with comfort that the organisation has complied with applicable laws, regulations and the established policies and procedures of the organisation. In Australia the most common management representations are in respect of the annual financial statements in accordance with the *Corporations Act 2001*.

### Management Representations

The Chief Executive Officer (CEO) and CFO/SFP have to fulfil statutory and other duties to their employer as executive officers in respect of management representations. These include:

- for listed entities, providing a declaration to the Board under section 295A of the *Corporations Act 2001* (Corporations Act) stating that the financial records of the entity have been properly maintained, the annual financial statements comply with Accounting Standards and that the financial statements represents a true and fair view. This obligation is also a recommended practice for other entities as per Recommendation 7.3 of the *Corporate Governance and Best Practice Recommendations*; and
- providing a written representation to the external auditor that they have fulfilled their responsibility for the preparation of the financial report in accordance with the applicable financial reporting framework, and to confirm certain matters or to support other audit evidence<sup>1</sup>.

### Historical Development of Management Representations

In 1985, Statement of Auditing Practice AUP 25 '*Representations by Management*' (AUP 25) was issued in Australia. Subsequently when Australian Auditing Standards became operative on 1 July 1996, AUS 520 '*Management Representations*' replaced AUP 25.

Stricter requirements in respect of management representations arose from the enactment of the Sarbanes-Oxley Act (SOX) in the US in 2002 in response to corporate scandals (e.g. Enron, Arthur Andersen, WorldCom and Tyco) that occurred at that time. SOX resulted in increased Board oversight, stricter auditor independence requirements including audit partner rotation, greater financial disclosures, and conflict of interest disclosures. Non-compliance with SOX obligations can result in significant penalties for US registrants.

Similar legal developments occurred in Australia due to the CLERP 9 reforms which resulted in Australian Accounting Standards and Auditing and Assurance Standards being issued as legally enforceable instruments. Accordingly, in April 2006, ASA 580 '*Management Representations*' (ASA 580) was issued

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<sup>1</sup> Auditing Standard ASA 580 Written Representations (Amended and compiled July 2013)

as a legally enforceable Standard by the Auditing and Assurance Standards Board (AUASB) to replace AUS 520. In October 2009, ASA 580 was reissued as 'Written Representations' and its requirements were strengthened whereby 'management' is now deemed to mean 'management, and, where appropriate, Those Charged with Governance (TCWG)'. The auditor must re-evaluate management's integrity and consider the effect on the audit report, where management has declined to provide representations or those provided by management are inconsistent with other evidence.

### Examples of Management Representations

There are various management representation provided by management to TCWG or external parties in the following circumstances:

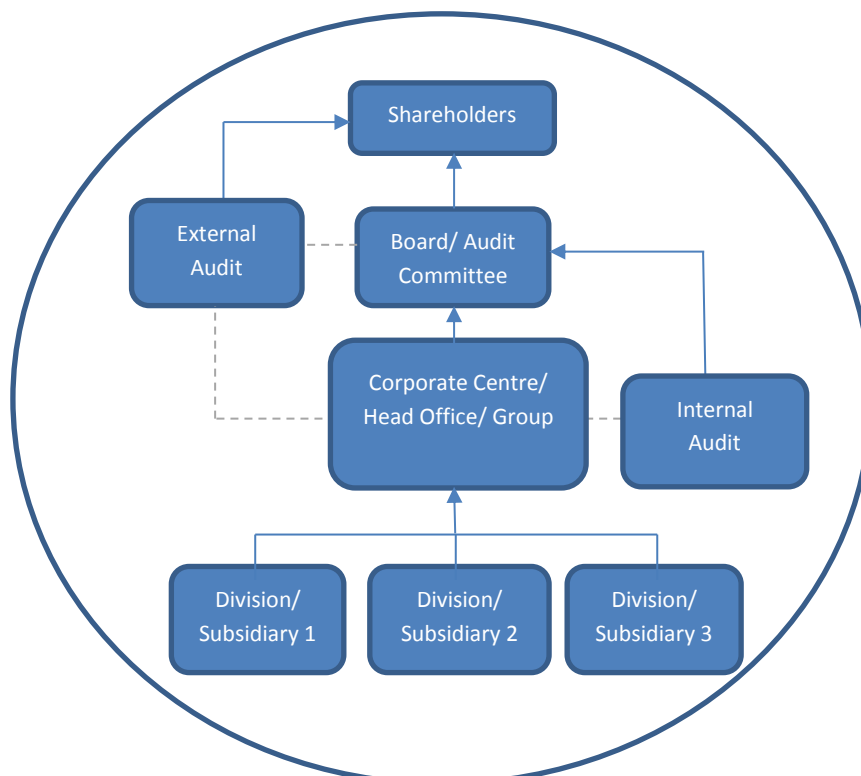
- Annual Financial Statements and in some cases, on a voluntary basis, Half-Year Financial Statements;
- Representations to an organisation's financiers or lenders when obtaining finance or in respect of ongoing compliance with loan covenants;
- Representations to Rating Agencies who are performing evaluations of the financial stability of the organisation;
- When preparing prospectus and similar capital raising situations; or
- When an organisation performs Due Diligence processes in respect of acquisitions, divestments, restructures or raising finance from capital and debt markets.

### APES GN 41 Project Objective

The objective of the APES GN 41 project is to assist a Member in Business who is a CFO or SFP in understanding the content, ethical implications and ethical responsibilities associated with signing management representations to TCWG or an external party.

In order to develop the framework, initially the project will focus on the underpinning principles, values and attributes required of a half year and annual financial statements management representation process undertaken by the CFO or SFP. Thereafter the other circumstances in which management representations are made (as noted above) can be considered.

### Principles, Attributes and Values of a Management Representation Process:



Detailed below are the professional obligations of a Member in Business who may be employed at the different organisational levels in an organisation with cross references to where similar professional obligations exist in APES standards in different contexts. Whilst we have used APES 320 which is applicable to Members in Public Practice, similar principles in respect of quality control can be applied by Members in Business to the management representation process. Where appropriate, cross references are also provided to current IESBA EDs.

### Subsidiary/Division Level

<b>Professional obligations</b>	<b>APES Reference</b>
The CFO or the SFP of a subsidiary (or material business segment or division) should:	
<ul style="list-style-type: none"> <li>• be professionally competent to oversee the financial matters of the subsidiary and have the requisite time, resources and skills to complete the Management Representations within the reporting deadline;</li> </ul>	APES 110 sections 130 & 330  APES 320 para 38 (a)  APES GN 40 section 9
<ul style="list-style-type: none"> <li>• exhibit the ethical values of integrity and objectivity and comply with Relevant Ethical Requirements and applicable Professional Standards;</li> </ul>	APES 110 sections 110 and 120 &  APES 320 para 38 (b)  APES GN 40 section 3
<ul style="list-style-type: none"> <li>• be knowledgeable of the subsidiary's industry and other subject matter on which they are providing Management Representations;</li> </ul>	APES 110 section 130  APES 320 para 39  APES GN 40 section 9
<ul style="list-style-type: none"> <li>• comply with the applicable legal, regulatory and financial reporting requirements;</li> </ul>	APES 205  APES 315 para 1.11  APES 320 para 39
<ul style="list-style-type: none"> <li>• prepare and present Management Representations provided to external parties fairly, honestly and in accordance with Relevant Ethical Requirements and applicable Professional Standards so that the Management Representations will be understood in its context;</li> </ul>	APES 110 para 320.1 and section 340  APES GN 40 section 8
<ul style="list-style-type: none"> <li>• assume overall responsibility for the preparation or approval of a subsidiary's Financial Statements to the corporate centre and shall be satisfied that those Financial Statements are presented in accordance with the applicable financial reporting standards;</li> </ul>	APES 110 para 320.2  APES 205 sections 5 & 6
<ul style="list-style-type: none"> <li>• take reasonable steps to maintain information for which the CFO/SFP is responsible in a manner that:               <ul style="list-style-type: none"> <li>➢ describes clearly the true nature of business transactions, assets or liabilities;</li> <li>➢ classifies and records information in a timely and proper manner; and</li> </ul> </li> </ul>	APES 110 para 320.3

<ul style="list-style-type: none"> <li>➤ represents the facts accurately and completely in all material respects.</li> </ul>	
<ul style="list-style-type: none"> <li>• communicate group's policies and procedures (including any changes) in respect of financial reporting to the subsidiary's senior management in a timely manner;</li> </ul>	APES 110 paras 130.4 & 300.14
<ul style="list-style-type: none"> <li>• select or oversee the selection process of finance team staff who have the ethical values, competence, skills, and ability to perform the subsidiary's work and possess the appropriate characteristics to enable them to perform their tasks with integrity and objectivity;</li> </ul>	APES 110 para 130.5 & 300.14 APES 320 paras 47-48
<ul style="list-style-type: none"> <li>• put in place systems or processes to develop competence of staff to complete the Management Representations checklist through a variety of methods, including the following: <ul style="list-style-type: none"> <li>➤ continuing Professional Education on relevant ethical issues, Professional Standards, legal obligations and other regulations (e.g. insider trading, corporate governance, IFRS).</li> <li>➤ providing work experience in a manner to continuously develop their skills.</li> <li>➤ coaching by more experienced staff.</li> </ul> </li> </ul>	APES 110 paras 300.14 & 340.4 APES 320 para 49
<ul style="list-style-type: none"> <li>• encourage staff to be alert for circumstances and relationships that could be encountered by staff during the Management Representations process that create or may create threats to compliance with the fundamental principles of the Code: <ul style="list-style-type: none"> <li>➤ to not knowingly engage in any business transaction or activity that impairs or might impair the subsidiary's and group's good reputation as a responsible corporate citizen;</li> <li>➤ to be aware of potential accounting and any tax schemes or arrangements which may not be in accordance with applicable legal and regulatory requirements;</li> <li>➤ must not knowingly be associated with any arrangement which involves documents or accounting entries that are intended to misrepresent a transaction or which is dependent upon lack of disclosure for its effectiveness; and</li> <li>➤ to be aware of ethical issues, legal obligations and other regulations around potential insider trading.</li> </ul> </li> </ul>	APES 110 sections 150, 300, 310, 340 & 350 APES GN 40 section 3 APES 220 para 5.1 APES 220 para 5.1 APES 110 para 340.4
<ul style="list-style-type: none"> <li>• create an organisational environment where staff are able to make Management Representations with integrity and objectivity regardless of whether the impact /outcome is positive or negative;</li> </ul>	APES 110 sections 110, 120, 310 & IESBA ED section 370
<ul style="list-style-type: none"> <li>• provide guidance to a staff Member to first obtain legal advice or consult with the staff's Professional Body when considering disclosure of information about the subsidiary's business in circumstances where it would otherwise be a breach of the staff's professional obligation of confidentiality or statutory obligations; and</li> </ul>	APES 110 para 100.23 & section 140 APES GN 40 sections 5 & 12
<ul style="list-style-type: none"> <li>• develop mechanisms to report potential internal control weaknesses in the subsidiary's internal control environment to Management or TCWG.</li> </ul>	APES 110 para 100.16

**Group/ Head Office/ Corporate Centre Level**

Professional obligations	APES Reference
The group CFO/SFP of the group or head office or corporate centre should, in addition to relevant aspects of the above:	
<ul style="list-style-type: none"> <li>• establish policies and procedures designed to provide the group with reasonable confidence that it has sufficient finance staff with the competence, capabilities and commitment to ethical principles in order to:               <ul style="list-style-type: none"> <li>➢ perform Management Representations in accordance with Professional Standards and applicable legal and regulatory requirements; and</li> <li>➢ enable the CFO/SFP to provide Management Representations to TCWG or external parties that are appropriate in the circumstances.</li> </ul> </li> </ul>	<p>APES 110 section 130, 330 &amp; para 300.14</p> <p>APES 320 para 47</p> <p>APES GN 40 section 3</p>
<ul style="list-style-type: none"> <li>• use the expertise of suitably qualified people (e.g. internal auditors and external auditors) in the development of the group Management Representation checklist during the planning stage of the financial reporting year-end process;</li> </ul>	<p>APES 110 para 300.14</p> <p>APES 320 para 51</p>
<ul style="list-style-type: none"> <li>• establish policies and procedures designed to provide the group with reasonable confidence that Management Representations are appropriate including:               <ul style="list-style-type: none"> <li>➢ matters relevant to promoting consistency in the group's Management Representation process; and</li> <li>➢ supervision and review responsibilities.</li> </ul> <p>Supervision of the Management Representation process includes the following:</p> <ul style="list-style-type: none"> <li>- tracking the progress of the Management Representation process;</li> <li>- consider the skills, competence and capabilities of the staff involved and whether they understand group reporting instructions</li> <li>- assessment of whether the Management Representation process is carried out in accordance with the group Management Representation checklists;</li> <li>- addressing significant matters or discrepancies arising from the process; and</li> <li>- an evaluation and assessment of potential omissions of representations that should be included in the subsidiary's Management Representations.</li> </ul> <p>A review consists of consideration of whether:</p> <ul style="list-style-type: none"> <li>- the Management Representations performed by less experienced staff is reviewed by a more experienced staff;</li> <li>- the Management Representation process has been performed in accordance with Professional Standards and applicable legal and regulatory requirements;</li> <li>- sufficient inquiries and test checks have been performed to ensure that subsidiaries (notwithstanding the complex group structures) are in compliance with the group's accounting policies and Management Representation processes;</li> <li>- reasonable confidence over the validity and reliability of the information has been obtained (e.g. sample reviews by internal audit and Senior Finance Staff); and</li> </ul> </li> </ul>	<p>APES 110 sections 110,120,130,150, 300 &amp; 340</p> <p>APES 320 para 58</p> <p>APES 320 para 61, 62 &amp; 63</p>

<ul style="list-style-type: none"> <li>- subsidiary Management Representations have been reviewed to determine if discrepancies exist between what the subsidiary auditor reported in respect of financial matters and the Management Representation made by the subsidiary, and vice versa.</li> </ul>	
<ul style="list-style-type: none"> <li>• create an organisational culture and environment of compliance with group reporting requirements;</li> </ul>	APES 110 para 300.5 and section 310
<ul style="list-style-type: none"> <li>• provide mechanisms and guidance (for staff to communicate internally within the group) in respect of potential next steps where internal control weaknesses, fraud, irregularities or suspected non-compliance with laws and regulations are identified including reporting such matters, where material, to TCWG;</li> </ul>	APES 110 sections 100, 310, 350 & IESBA ED section 370 APES GN 40 sections 7 & 12
<ul style="list-style-type: none"> <li>• implement appropriate remedial action for deficiencies noted or matters raised for management's attention and report material matters to TCWG: <ul style="list-style-type: none"> <li>➢ If employees identify potential issues that may not have been dealt with by management previously, the group CFO/SFP needs to have reasonable confidence that the right processes are in place to identify those issues or matters raised and that they have been dealt with appropriately by the relevant staff.</li> </ul> </li> </ul>	APES 110 sections 100 and 310 APES 320 para 115 APES GN 40 section 5
<ul style="list-style-type: none"> <li>• develop a process whereby a review of external/internal audit findings in respect of the group and its subsidiaries is performed periodically to ensure appropriate remedial action is being taken to resolve issues identified by the external and internal auditors (noting issues which may be pervasive in particular); and</li> </ul>	APES 110 section 100
<ul style="list-style-type: none"> <li>• implement procedures to document and report to TCWG how material contentious issues are resolved in respect of financial reporting matters or related risk management issues.</li> </ul>	APES 110 section 100 APES 205

### **Board/Audit Committee Level**

<b>Professional obligations</b>	<b>APES Reference</b>
A Member in Business who is a Board member or Audit Committee member who is evaluating the group's or subsidiary's Management Representation process should:	
<ul style="list-style-type: none"> <li>• consider the group's and/or subsidiary management's: <ul style="list-style-type: none"> <li>➢ leadership responsibilities for Management Representations;</li> <li>➢ expertise, experience, training and/or education;</li> <li>➢ adherence and commitment to Relevant Ethical Requirements;</li> <li>➢ performance in so far as it reflects any issues of an ethical nature;</li> <li>➢ monitoring and review processes; and</li> <li>➢ documentation and communication of policies and procedures.</li> </ul> </li> </ul>	APES 110 sections 100,110,120,130 & 150 APES 320 para 10 APES GN 40 sections 3,8 & 9
<ul style="list-style-type: none"> <li>• evaluate whether the group's policies and procedures are designed to promote an internal culture with strong ethical values. Such policies and procedures shall require the group's Chief Executive Officer (CEO) and CFO (or equivalents) or, if appropriate, the group's TCWG to assume ultimate responsibility for the group's management representations;</li> </ul>	APES 110 section 300 APES 320 para 14
<ul style="list-style-type: none"> <li>• evaluate whether the group's policies and procedures establishes that any person or persons assigned operational responsibility by the group's CEO/CFO or TCWG has sufficient skills, competence, appropriate experience and the necessary authority, to assume that responsibility;</li> </ul>	APES 110 sections 130 & 330 APES 320

	paras 17, 18
<ul style="list-style-type: none"> <li>evaluate whether the group's policies and procedures are designed to provide it with reasonable confidence that the group and its staff comply with Relevant Ethical Requirements. Ethical requirements are contained in the Code of Ethics and Professional Standards;</li> </ul>	<p>APES 110 sections 100 &amp; 130</p> <p>APES 320 para 19</p>
<ul style="list-style-type: none"> <li>evaluate whether the group policies and procedures are designed to provide it with reasonable confidence that it deals appropriately with: <ul style="list-style-type: none"> <li>complaints and allegations that management representations performed fails to comply with Professional Standards and applicable legal and regulatory requirements; and</li> <li>allegations of non-compliance with the group's policies and procedures.</li> </ul> <p>As part of this process, the group shall establish clearly defined channels for group's staff to raise any concerns to group's management or TCWG in a manner that enables them to come forward without fear of reprisals;</p> </li> </ul>	<p>APES 110 sections 100 &amp; 140</p> <p>APES 320 para 119</p>
<ul style="list-style-type: none"> <li>evaluate whether management has implemented group policies and procedures in a manner to identify, assess, manage and resolve key organisation risks, governance risks, business risks, financial risks and regulatory risks as covered within the management representations process;</li> </ul>	<p>APES 110 sections 100, 300 &amp; 340</p>
<ul style="list-style-type: none"> <li>evaluate whether management have implemented safeguards in the group's work environment (i.e. systems of corporate oversight, ethics and conduct programs, recruitment procedures, strong internal controls, appropriate disciplinary processes, quality of employee performance) to eliminate or reduce threats of non-compliance with the fundamental principles created by conflicts of interest, incentives, business and family relationships, offers of inducements and undue pressures to breach;</li> </ul>	<p>APES 110 sections 100, 300, 310, 340, 350 &amp; IESBA ED section 370</p> <p>APES GN 40 sections 3, 5, 7 &amp; 12</p>
<ul style="list-style-type: none"> <li>evaluate whether management have monitored the group's control environment, assessed adequacy of safeguards over the control environment, information systems and group processes;</li> </ul>	<p>APES 110 sections 100 &amp; 300</p>
<ul style="list-style-type: none"> <li>evaluate whether management has overseen performance of test reviews to ensure the adequacy, efficiency and effectiveness of group management's representation process;</li> <li>Develop channels for internal/external audit to provide direct feedback to the Audit Committee; and</li> </ul>	<p>APES 110 section 330</p>
<ul style="list-style-type: none"> <li>perform an assessment of the impact of any deficiencies in the group's management representations on the internal control environment or in the business and the resulting impact on the financial statements.</li> </ul>	<p>APES 110 sections 150 &amp; 320</p> <p>APES 205</p>

#### Applicable sections of the Code

- S100 Fundamental Principles
- S110 Integrity
- S120 Objectivity
- S130 Professional Competence and Due Care
- S140 Confidentiality
- S150 Professional Behaviour
- S310 Conflict of Interest
- S320 Preparing and Reporting of Information (IESBA currently reviewing this section)
- S330 Acting with Sufficient Expertise
- S340 Financial Interests, Compensation and Incentives Linked to Financial Reporting and Decision Making
- S350 Inducements

#### Potential new sections currently under development by IESBA

- S360 Non-Compliance with Laws and Regulations
- S370 Pressures to Breach the Fundamental Principles

#### Applicable APES standards

- APES 205 Conformity with Accounting Standards
- APES 220 Taxation Services
- APES 315 Compilation of Financial Information
- APES 320 Quality Control for Firms
- APES GN 40 Ethical Conflicts in the Workplace – Consideration for Members in Business

#### Examples of potential Professional Obligations

- A Member in Business who is a CFO (or SFP equivalent) should be professionally competent, exhibit the ethical values of integrity and objectivity, and comply with the Relevant Ethical Requirements and the group's corporate governance practices and reporting requirements, when performing the Management Representation process.
- A Member in Business who is a CFO (or SFP equivalent) should take reasonable steps to ensure that the group's and subsidiary's finance functions are appropriately resourced.