



Accounting Professional & Ethical Standards Board

***Six Monthly Review of APES 350 Participation by  
Members in Public Practice in Due Diligence  
Committees in Connection with a Public Document  
issued in December 2009***

Prepared by APESB Technical Staff and APES 350 Taskforce

12 November 2010

## **1. Executive Summary**

### **1.1. Background**

APESB issued APES 350 *Participation by Members in Public Practice in Due Diligence Committees in Connection with a Public Document* issued in December 2009 with an effective date of 1 February 2010.

### **1.2. Reason for this report**

In accordance with the constitution of the APESB, a review needs to be performed six months after a new standard is effective. This report presents a review of issues reported to the APESB by stakeholders such as investment banks, law firms, professional accounting bodies and firms, and proposed recommendations thereon for the consideration of the APES Board.

### **1.3. Issues identified**

1. Stakeholders have stated there is significant concern from several market participants with regard to the wording in APES 350 that suggests that Accountants (or Members in Public Practice) do not have expertise to express an opinion on whether certain financial disclosures meet Corporation Act standards.
2. The definition of “Other Specific Information” is quite broad as it covers specific metrics or ratios and there has been some difficulty with the definition in practice. Further, a stakeholder notes that there is a reluctance by accounting firms to provide a review statement in respect of “Other Specific Information”
3. Stakeholders have again raised the issue of the position taken by accountants to be a DDC Observer when the Client is a US SEC registrant or otherwise subject to US SEC auditor independence requirements. They claim to have received feedback that the Australian Firms use US SEC auditor independence requirements as a ruse to act only as a DDC Observer. Accordingly, they propose that the DDC Observers be required to issue a functionally equivalent “general” sign-off as per the Due Diligence Report and an APES 350 sign-off.
4. Stakeholders have raised the issue regarding uncertainty about whether or not an accounting firm should provide an APES 350 sign-off in connection with low doc

offers. They are of the view that if an accounting firm performs a review mandate or Agreed Upon Procedures mandate that it would be appropriate to provide an APES 350 sign-off with adaptation of language to different legislative context on the work they have performed.

5. APESB should reconsider the Materiality Letter as the AUASB has declined to include it within their pronouncements.
6. The statement of compliance in the example DDC Sign-off in Appendix 1 in APES 350 is not in alignment with the requirements of paragraph 7.3 (f).
7. Stakeholders recommend adding the word ‘Review’ into Appendix 1, paragraph 4 for consistency purposes.
8. Stakeholders recommend adding ‘by or on behalf of the client’ into paragraph 6(c) and 6(f) of Appendix 1, to improve its clarity.
9. Stakeholders have suggested a number of other editorial changes to Appendix 1 *Due Diligence Sign-off*.

#### **1.4. Summary of Recommendations**

It is recommended that:

1. No change is required in respect of this issue as it has been comprehensively dealt with by the APESB when APES 350 was issued in 2009.
2. Stakeholders have suggested a number of solutions to resolve issues relating to ‘Other Specific Information’, please refer to the recommendation in section 2.2
3. No further action is recommended in respect of the DDC Observer role in APES 350 when the Client is a US SEC Registrant. The consequences of breaching the US SEC auditor independence requirements can be quite significant to a Client.

Paragraph 5.9 can be reworded to clarify that the obligation also applies to DDC Observers. This change may also alleviate, to an extent, the stakeholder comment with respect to the obligations of DDC Observers (Refer Section 2.3).

4. The existing paragraph 1.9 of APES 350 allows a Member in Public Practice to apply the standard to the extent practicable in the case of low docs. Accordingly no further amendments are recommended.
5. The APES 350 taskforce is of the view that the Materiality Letter provides useful guidance in practice and if included in an Appendix to the standard will provide

efficiencies in practice. Given the AUASB decision, the taskforce requests that the Board reconsider the Materiality Letter as an inclusion in APES 350 in the future.

6. Wording in Appendix 1 to be revised to reflect compliance with 7.3(f) in the following manner:

*“Our Services have been conducted and this This Due Diligence Sign-Off has been prepared in accordance with APES 350 Participation by Members in Public Practice in Due Diligence Committees in connection with a Public Document.”*

7. In the next revision of APES 350 it is recommended that “Review” be inserted to 4 Basis for Review Statement of Appendix 1 of APES 350 in the following manner:

#### **“4. Basis for Review Statement**

In making the Review Statement we only hold ourselves out as having expertise as [designation of applicable professional body] [in advising on Australian taxation matters (if applicable)]. We disclaim any skills or expertise in any other capacity.”

8. Sub paragraphs (c) of Section 6 Assumptions of Appendix 1 in APES 350 to be amended in the following manner:

#### **“6. Assumptions**

In making the Statement in this Due Diligence Sign-Off, we have assumed that:

c. there were no relevant documents or information other than those which were disclosed, or provided by or on behalf of the Client, to us which are relevant to the Financial Information

No changes are proposed to sub paragraph (f) of Section 6 of Appendix 1.

9. After due consideration of various suggestions proposed by stakeholders, no changes are recommended in respect of the issues raised in Section 2.9.

## **2      Review of Implementation Issues**

- 2.1 Stakeholders have stated there is significant concern from several market participants with regard to the wording in APES 350 that suggests that Accountants (or Members in Public Practice) do not have expertise to express an opinion on whether certain financial disclosures meet Corporation Act standards. [Refer Issue 1 Accounting expertise in Appendix 1]**

### **Issue**

As noted in the stakeholder's comments the issue is with regard to the statements in the standard about a Member in Public Practice's accounting expertise. The stakeholder has requested that the qualification in respect of accounting expertise be removed.

### **Analysis of the issue**

The issue of the Accountant's or Member's expertise is not a new issue. This stakeholder has raised this issue previously and the APES Board dealt with it when APES 350 was developed last year. As raised at the taskforce meeting, the concerns raised recently have been about the specific wording in the standard, rather than the issue more generally.

APES 350 states that Members in Public Practice must only report or advise on matters within their expertise and provide individual sign-offs in respect of the specific work that they have completed. However, Members in Public Practice can provide sign-offs collectively with other Due Diligence Committee (DDC) Members with regard to information in a public document (including financial disclosures) where that information has been subject to the collective consideration of the DDC.

The two primary reasons for this are:

- DDC Members collectively consider what information is appropriate for inclusion in the public document (for example, the client, lawyers, financial advisers, investment banks, underwriters and Member in Public Practice/Firms are all involved in this process) and thus the determination of whether the Corporations Act Standards have been met is made with the benefit of the combined skills, knowledge and expertise of all DDC Members.
- Further, unlike a financial report prepared in accordance with the *Corporations Act* where there is an established framework (i.e. Accounting Standards), in this case there is no established framework stipulated in the *Corporations Act* for a Member in Public Practice to evaluate the Client's financial disclosures in the

public document. This issue was explained in detail in the APES 350 Basis of Conclusions issued by the APESB in December 2009 (Refer to an extract below).

As stated in the Basis of Conclusions of APES 350:

*A respondent noted that a Member in Public Practice who advises on, or provides content for, a Public Document must ensure that the Member's contribution meets the relevant disclosure standard imposed by law. The respondent was of the view that it is appropriate for a Member in Public Practice to confirm to the Client and its DDC that the Member's advice on, or content provided for, a Public Document meets the relevant disclosure standard imposed by law. According to the respondent, a failure by a Member in Public Practice to provide an express confirmation in relation to the Member's work product will mean that others involved in the preparation of a Public Document potentially have inadequate assurance that the Member's work product complies with the relevant disclosure standard. The respondent contended that the effect of this failure by a Member in Public Practice to provide an express confirmation in relation to the Member's own work is to transfer risk on the issue of compliance to others involved in the preparation of the Public Document.*

APESB considered this issue and noted that:

- *the determination of the nature and quantum of information included in a Public Document is a decision for the Client in collaboration with its DDC. It follows that the determination concerning, for example, the number of years of Statements of Financial Position and Statements of Financial Performance included in a Public Document are decisions for the Client. This Financial Information is not the "work product" of a Member in Public Practice, but the "work product" of the Client. Any Due Diligence Sign-Off provided by a Member in Public Practice will be in respect of the disclosed Financial Information and not whether, for example, the Statements of Financial Position and Statements of Financial Performance for additional years should be included.*
- *in relation to the respondent's submission that Members in Public Practice should provide a sign-off that there are no omissions of information required by the Corporations Act 2001 in a Public Document, there is no accepted or approved disclosure framework against which a Member can assess the appropriateness and adequacy of those disclosures relative to the general disclosure requirements of the Corporations Act 2001, in particular those set out in section 710 of that Act; and*
- *unlike the disclosure requirements for a financial report, which are clearly set out in Accounting Standards and the Corporations Act 2001, the disclosure requirements of the Corporations Act 2001 in relation to a Public Document are general in nature. A combination of skills, knowledge and expertise is therefore required to determine the nature and quantum of information to be disclosed in a Public Document. A Member in*

*Public Practice will not possess all those skills and all the necessary knowledge and expertise to enable the Member to report as proposed by the respondent, except in conjunction with the other members of a DDC.*

*Accordingly, APESB is of the view that the responsibility for determining or advising on whether the Financial Information disclosed in a Public Document is appropriate and adequate to meet the relevant disclosure standard should not rest with the Member in Public Practice in isolation. This is the responsibility of the Client and its DDC and accordingly this sign-off on the content of the Public Document should only be provided by the DDC as a whole rather than in the Member's Due Diligence Sign-Off. [Emphasis added]*

In accordance with APES 110 *Code of Ethics for Professional Accountants* (the Code), Members of the professional accounting bodies have a professional obligation to only perform services for which they have the necessary expertise. Accordingly, APES 350 is consistent with the Code when it mandates that Members can only perform work that is within their expertise.

Furthermore, relevant standards in respect of fund raisings in other countries such as the United States and Canada state as follows:

*United States - AU Section 634 of Statement on Auditing Standards 72 "Letters for Underwriters and Certain Other Requesting Parties" states that in circumstances where Accountants are providing a comfort letter in respect of financial information in a US Registration Statement, the Accountants should not comment on information subject to legal interpretation. Specifically, the standard provides that "...the question of what constitutes appropriate information for compliance with the requirements of a particular item of the registration statement is a matter of legal interpretation outside the competence of accountants"*

*Canada - Sections 7110 and 7200 of the Chartered Accountants of Canada Assurance and Related Services Recommendations provides that an Accountant should not: express either positive or negative assurance unless he or she has audited or reviewed the information in accordance with assurance standards;*

- provide any form of assurance relating to the offering document as a whole, whether in a comfort letter or any other communication (para 45 of 7110).
- provide assurance as to the adequacy for the Underwriter's purposes of the disclosures made in a due diligence meeting; or
- provide any form of assurance relating to the offering document as a whole (para 117 of 7200).

Accordingly, it is clear that other jurisdictions have also included within their standards what is appropriate for an Accountant to opine on.

The stakeholder's comment that the APESB is opining on the expertise of each individual accountant in respect of capital raisings is not correct, and demonstrates a lack of understanding of the requirements stipulated by Accounting Professional Standards and how they operate. The position in the Code and APES 350 is that Members must only report or advise on matters within their expertise.

### **Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

### **Recommendation**

It is recommended that no change is required in respect of this issue as it has been comprehensively dealt with when APES 350 was issued in 2009.

- 2.2 The definition of “Other Specific Information” is quite broad as it covers specific metrics or ratios and there has been some difficulty with the definition in practice. Further, a stakeholder notes that there is a reluctance by accounting firms to provide a review statement in respect of “Other Specific Information” [Refer Issue 4 Review statement regarding “Other Specific Information”].**

### **Issue**

Firms have reported that there have been a few issues in practice in the application of the definition of *Other Specific Information*.

APES 350 defines it as:

*Other Specific Information means specifically identified information, other than Financial Information, in a Public Document, which has been the subject of procedures performed by a Member in Public Practice as specified in the Engagement Document. Examples include specific tax-related information, environmental matters, information technology matters and specific metrics or ratios calculated using elements of the Financial Information.*

The issue surrounds the breadth of information captured within *Other Specific Information* definition and its practical application, and whether a review statement could be given in relation to metrics and ratios not capable of review under applicable Auditing and Assurance Standards issued by the Auditing and Assurance Standards Board (AUASB).

The Member in Public Practice may perform review procedures or Agreed Upon Procedures in relation to *Other Specific Information* that is financial information. The

statements that a Member in Public Practice can give in relation to financial information are governed by AUASB standards applicable to Review engagements and Agreed Upon Procedures engagements and depend on the scope of work performed by the Member. For example, if the Member has only performed Agreed Upon Procedures in respect of *Other Specific Information* then they must provide their findings in accordance with AUASB's *AUS 904 Engagements to perform Agreed-upon Procedures* and are unable to provide a review opinion.

In certain circumstances it is not possible to provide a review opinion on Other Specific Information. For example, information which is purely computational, or derived from other information, or sourced from third party or external documentation is more likely to be verified by Agreed Upon Procedures.

Stakeholders who have raised this issue need to develop an understanding that there are specific standards issued by the AUASB that stipulate the work that needs to be carried out prior to a Member in Public Practice providing a statement (either Review or Agreed Upon Procedures). Accordingly, unless work has been performed in accordance with the applicable AUASB standards, then Members in Public Practice are unable to provide relevant statements. Further, as noted above in certain circumstances some information cannot be “audited or reviewed” under the assurance framework, and in these instances it is more appropriate to perform Agreed Upon Procedures.

### **Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

### **Recommendations**

Suggest providing further guidance on the matter. Possible solutions include:

1. Removing the words “and specific metrics or ratios calculated using elements of the Financial Information” from the definition of *Other Specific Information*.
2. Amend subparagraph (g) in 2 Scope of Work and 5 Review Statement of DDC Sign-off in Appendix 1 of APES 350 and separate the square bracket information relating to Other Specific Information into new paragraph titled paragraph 6 *Other Specific Information* in the following manner:

#### **2. Scope of Work**

(g) [Insert scope of work in relation to *Other Specific Information*] being information which is not the object of procedures in (d) above.

## **5. Review Statement**

### **6. Other Specific Information**

[Insert similar statements in relation to Other Specific Information referred to in 2 (g) if applicable]

3. Paragraphs 5.12 and 5.13 of the standard be amended to confirm that where it is part of a Member's scope to assist with verification of disclosures about taxation laws, specific procedures are not to be agreed with the Client and such assistance does not need to be by way of an Agreed Upon Procedures engagement.
  
  4. Amend APES 350 Appendix 1 paragraph 2 Scope Limitations in the following manner:  
  
‘That work did not constitute an audit or review in accordance with Australian Auditing Standards and consequently no assurance or audit opinion or review statement is expressed’.
- 
- 2.3 Stakeholders have again raised the issue of the position taken by accountants to be a DDC Observer when the Client is a US SEC registrant or otherwise subject to US SEC auditor independence requirements. They claim to have received feedback that the Australian Firms use US SEC auditor independence requirements as a ruse to act only as a DDC Observer. Accordingly, they propose that the DDC Observers be required to issue a functionally equivalent “general” sign-off as per the Due Diligence Report and an APES 350 sign-off. For further information refer issue 2 in Appendix 1.**

#### **Issue**

The stakeholder claims that in practice, accounting firms try to use US SEC auditor independence rules to avoid being a DDC Member and not having to provide a DDC sign-off as a DDC Member. The stakeholder suggests that if the Member in Public Practice does not sign the Due Diligence Report of the DDC then there may be a potential gap in the due diligence process.

#### **Analysis of Issue**

The issue of DDC Observer sign off in the case of US SEC Registrants is not a new point raised by this stakeholder. It was raised during the APES 350 development process and the impact of the strict US independence rules which precludes the auditor from

performing this role has been previously explained to them. The APES Board dealt with this issue when APES 350 was developed last year and as stated in the Basis of Conclusions of APES 350 [Refer extract below]:

*In terms of the distinction between a DDC Member and a DDC Observer, the key distinction is that the DDC Observer does not have the same responsibilities as a DDC Member. The DDC Observer will not participate in the decisions of the DDC nor sign the collective report of the DDC to the Client on the overall appropriateness of the due diligence process and the content of the Public Document. In some instances the role of a DDC Observer may be very limited and will not entail any formal reporting.*

*APESB considered this issue and determined to make amendments in the scope and application, definitions and other applicable sections of APES 350 to clarify the role of the DDC Observer. The Due Diligence Sign-Off in Appendix 1 of APES 350, and the content requirements for a Due Diligence Sign-Off set out in paragraph 7.3, have been amended to permit a Member acting in the capacity of DDC Observer to provide a Due Diligence Sign-Off, but only after considering the scope of procedures performed as required by paragraphs 5.14, 7.1 and 7.2.*

A number of Australian Firms have reported that they have received legal advice from US law firms and advice from their US network firms that participating as a DDC Member would be viewed by the SEC as the performance of a management function and thus will breach US Auditor independence requirements. Accordingly, the Firms are in effect complying with the strict US independence requirements by not being a DDC Member in these circumstances. It should be appreciated by market participants that the consequences for a Client if its auditor breaches the US SEC independence rules could be quite significant. For example, in the most extreme cases this could result in the auditor being replaced worldwide and that would result in the Client having to invest significant time and effort and incur costs to replace the incumbent auditor. The stakeholder should be made aware of the seriousness of the US SEC auditor independence requirements.

APES 350 provides that a Member in Public Practice should consider the applicable independence requirements of a foreign jurisdiction. Further, where they have performed procedures equivalent to being a DDC Member then they can provide a due diligence sign off in the capacity of a DDC Observer (APES 350 and the example in Appendix 1 caters for both DDC Member and DDC Observer). However, the Member in Public Practice is precluded from signing the DDC's Report to the Client.

Feedback received from Firms indicates that once the auditor independence position is explained to most Clients it is not an issue for them.

Stakeholders have also noted that it is not clear whether paragraph 5.9 applies to DDC Observers and that this should be clarified. The existing paragraph 5.9 requires a Member in Public Practice to bring to the attention of the DDC any significant concerns identified by the Member.

*"5.9 A Member in Public Practice shall bring to the attention of the Client and/or its Due Diligence Committee any significant concerns relating to the matters set out in paragraph 5.7 which come to the attention of the Member."*

### **Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

### **Recommendation**

Notwithstanding the comments made by the stakeholder, no further action is recommended in respect of the DDC Observer role in APES 350 when the Client is a US SEC Registrant. As noted above, the consequences of breaching the US SEC auditor independence requirements can be quite significant to a Client.

With respect to paragraph 5.9, it can be reworded to clarify that the obligation also applies to DDC Observers. This change may also alleviate, to an extent, the stakeholder comment with respect to the obligations of DDC Observers.

Refer below to the proposed revisions to paragraph 5.9:

*"A Member in Public Practice providing Professional Services to a Client which comprise participating in and/or reporting to a Due Diligence Committee as a DDC Member or DDC Observer or Reporting Person shall bring to the attention of the Client and/or its Due Diligence Committee any significant concerns relating to the matters set out in paragraph 5.7 which come to the attention of the Member in performing the work set out in the Member's Terms of Engagement."*

- 2.4 Stakeholders have raised the issue regarding uncertainty about whether or not an accounting firm should provide an APES 350 sign-off in connection with low doc offers. They are of the view that if an accounting firm performs a review mandate or Agreed Upon Procedures mandate that it would be appropriate to provide an APES 350 sign-off with adaptation of language to different legislative context on the work they have performed. For further information refer issue 3 in Appendix 1.**

### **Issue**

The stakeholder notes that there is currently a great deal of uncertainty about whether or not an accounting firm should provide an APES 350 DD Sign-off in connection with low doc offers.

### **Issue analysis**

APES 350 requires a Member in Public Practice to consider whether the scope of procedures undertaken is sufficient and appropriate to support the provision of a Due Diligence Sign-off. The fact that the work performed by a Member in Public Practice in relation to Financial Information or Other Specific Information has been performed in accordance with applicable AUASB standards on review engagements or Agreed Upon Procedures engagements does not necessarily mean that the Firm is in a position to issue an APES 350 DDC Sign-off. It appears that the stakeholder may not properly understand the operation of these different standards and how they impact on the work undertaken by a Member in Public Practice.

Whether the Member in Public Practice can provide a APES 350 DD Sign-off will depend on matters such as the scope and nature of procedures undertaken and the time table for the due diligence process. Where a transaction occurs in a very short time frame, it is difficult for a Member in Public Practice to make an assessment whether all reasonable inquiries have been performed since detailed enquiries of the kind that are undertaken for a prospectus are not able to be undertaken. Further, in a low doc situation the issuer must be satisfied as to the adequacy of its existing market disclosures and the Firms report that their scope of work would not usually include any procedures in relation to existing market disclosures. It is therefore difficult for them to conclude on whether all reasonable enquires have been made.

Where the Member in Public Practice determines, that given the circumstances, they can provide a Due Diligence Sign-off, then the wording of the statements should be as they are currently set out in APES 350 and must not be prepared in a manner that may imply that it meets a particular legal standard (as then the Member is not acting within his or her expertise – refer issue 2.1). Any tailoring of the statements as suggested by the stakeholder to match the wording in particular sections of the *Corporations Act 2001* would create an impression that the accountant was signing off on compliance with such sections, which is prohibited by APES 350.

The decision to provide, or not provide, a APES 350 DD sign-off needs to be determined on a case by case basis and APES 350 currently has this flexibility.

### **Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

### **Recommendation**

The existing paragraph 1.9 of APES 350 allows a Member in Public Practice to apply the standard to the extent practicable in the case of low docs. Accordingly no further amendments are recommended.

## **2.5 APESB should reconsider the Materiality Letter as AUASB has declined to include it within their pronouncements**

### **Issue**

During the development phase of APES 350, the APES 350 taskforce considered the development of a materiality letter that could be used by a Member in Public Practice in the Due Diligence process. As the AUASB has existing standards in respect of materiality, APESB referred this matter to the AUASB. However, after consideration of the issue it appears that AUASB do not wish to include a pro forma materiality letter in their pronouncements.

### **Analysis of the issue**

The original intention was to include a pro forma materiality letter as an appendix to APES 350. As the taskforce members still believe that it provides useful guidance and will create efficiencies in practice, this matter should be reconsidered by the APES Board.

### **Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

### **Recommendation**

The APES 350 taskforce is of the view that the Materiality Letter provides useful guidance in practice and if included in an Appendix to the standard will provide efficiencies in practice. Given the AUASB decision, the taskforce requests that the Board reconsider the Materiality Letter as an inclusion in APES 350 in the future.

- 2.6 The statement of compliance in the example DDC Sign-off in Appendix 1 in APES 350 is not in alignment with the requirements of paragraph 7.3 (f).**

**Issue**

Paragraph 7.3 (f) mandates that a Member in Public Practice must make a statement (when applicable) that the professional services were conducted and the DDC Sign-off was prepared in accordance with APES 350. Due to an oversight the DDC Sign-off in Appendix 1 does not reflect the intended wording.

**Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

**Recommendation**

Wording in Appendix 1 to be revised to reflect compliance with 7.3(f) in the following manner:

*“Our Services have been conducted and this This Due Diligence Sign-Off has been prepared in accordance with APES 350 Participation by Members in Public Practice in Due Diligence Committees in connection with a Public Document.”*

- 2.7 Stakeholders recommend adding the word ‘Review’ into Appendix 1, paragraph 4 for consistency purposes.**

**Issue**

A stakeholder recommends the wording ‘Review’ to be inserted into Section 4 *Basis for Review Statement* of Appendix 1 of APES 350 for consistency purposes.

**Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

**Recommendation**

In the next revision of APES 350 it is recommended that “Review” be inserted to 4 *Basis for Review Statement* of Appendix 1 of APES 350 in the following manner:

**“4. Basis for Review Statement**

In making the [Review](#) Statement we only hold ourselves out as having expertise as [designation of applicable professional body] [in advising on Australian taxation matters (if applicable)]. We disclaim any skills or expertise in any other capacity.”

**2.8 Stakeholders recommend adding ‘by or on behalf of the client’ into paragraph 6(c) and 6(f) of Appendix 1, to improve its clarity.**

**Issue**

The stakeholder recommends the wording ‘by or on behalf of the Client’ to be inserted into paragraph 6(c) and 6(f) of Section 6 *Assumptions* of Appendix 1 of APES 350. The taskforce considered this and agree that it is appropriate to make the change to 6(c). However, it is not appropriate to make the change to 6(f) as Members in Public Practice relies on information provided via other sources as well.

**Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

**Recommendation**

As the recommended suggestion would improve the existing wording this should be considered in the next revision of the Standard. Please see below marked up sub paragraphs (c) of Section 6 *Assumptions* of Appendix 1 in APES 350:

**“6. Assumptions**

In making the Statement in this Due Diligence Sign-Off, we have assumed that:

- c. there were no relevant documents or information other than those which were disclosed, [or provided by or on behalf of the Client](#), to us which are relevant to the Financial Information

**2.9 Stakeholders have suggested the following changes to Appendix 1 *Due Diligence Sign-off***

**Issue**

Stakeholders have provided a marked up version of the Due Diligence Sign-off in Appendix 1 of APES 350 for the consideration of the APESB.

**Issue Analysis**

**Paragraph 2 Scope of work**

**Point (b)**

*“Prepared materiality ~~guidance~~ guidelines in a letter dated [insert date] for consideration by the [Client] and the DDC; (“Materiality Guidelines”)”*

The use of the term "guidance" is deliberate. The Member in Public Practice provides guidance based on AUASB Standards which do not set down "guidelines" for materiality to be applied to the due diligence process. It is up to the Client and the DDC to consider the applicability of the materiality guidance provided by the Member to the due diligence process and then set the guidelines for the due diligence process.

Further, the materiality criteria adopted by the DDC would be expected to comprise both qualitative and quantitative criteria in comparison to the materiality guidance recommended by a Firm which will only be quantitative. Hence the proposed changes in sections 4 and 5 are also not appropriate.

*Point (c)*

*“considered the adequacy of the due diligence process in so far as it relates to the Financial Information;”*

Scope items should reflect items capable of procedures by the Firm (the work that will be actually performed by the Firm, and not matters that will be collectively considered by the DDC as a whole).

*Point (d)*

*“Prepared and implemented a detailed financial and accounting work plan and presented a written report on the outcome of our due diligence enquiries, the exceptions we noted and our conclusions”*

The relevant procedures that Members in Public Practice undertake when performing review engagements or Agreed Upon Procedures engagements are stipulated in AUASB standards. As per paragraph 2 (c), (d) and (g) in Appendix 1 of APES 350 as the Member in Public Practice stipulates which standards they have followed in performing their work this change is not necessary and demonstrates a lack of understanding by the stakeholder on how Auditing Standards and Professional Standards impact on the work of Members in Public Practice.

*Point (e)*

*“Carried out due diligence enquiries in respect of the financial and accounting matters in accordance with our [work plan/engagement letter] and the DDPM for the purposes of enabling us to give this Due Diligence sign off”*

As noted in the response to point (d) above, this is already covered by the statement that a Member in Public Practice has carried out their work in accordance with applicable AUASB Standards.

Point (f)

*“Read and provided comments on drafts of the DDPM”*

The Member in Public Practice reviews the Due Diligence Planning Memorandum (DDPM) to comply with their professional obligations stipulated in section 4 of APES 350. It is not a scope item and not something the Member in Public Practice has to do to form their views on the Investigating Accountant’s Report or the Due Diligence Sign-Off. It is up to the Client to determine its due diligence process in consultation with its legal advisor. The Member in Public Practice reviews the DDPM to ensure that the Member’s role is being appropriately described in a manner consistent with the Engagement Document.

Point (g)

*“(e)conducted a review, in accordance with [ASRE 2405 or, ASAE 3000, ASIC Regulatory Guide 170 or other standards as appropriate], of the Financial Information furnished to us by the [Client]”*

Members in Public Practice do not perform reviews in accordance with RG 170. That is guidance issued by ASIC for issuers and does not govern how a review under Auditing Standards should be carried out

Point (h)

*“Reviewed and commented on successive drafts of the [describe Public Document] (including the final draft of the [describe Public Document])”*

This is already covered by scope point (a) as supported by paragraph 5.1(a) of APES 350.

Point (i)

*“(d)assisted the Client in its verification of certain statements in the [describe Public Document] by performing the procedures set out in [insert – eg “Appendix 2” or “the Engagement Document”] as agreed by the Client (**Verification Agreed Upon Procedures**)”*

The inclusion of the word "Verification" could be misinterpreted to mean that Members in Public Practice have verified the information. Its inclusion is inappropriate and unnecessary and demonstrates a lack of understanding by the stakeholder of AUASB Standards applicable to Agreed Upon Procedures engagements. A fundamental premise of an Agreed Upon Procedures engagement is that no assurance is provided and the use

of the proposed wording can be misleading. Further, it may convey a level of assurance that is not in accordance with internationally accepted conventions of what is an Agreed Upon Procedures engagement.

Point (j)

*“(e) If prepared and verified an investigating accountant’s report (if applicable) on the Financial Information for inclusion in the [describe Public Document]”*

Members in Public Practice do not verify their own report. Members in Public Practice consent to its inclusion. Once they have consented to its inclusion there is no need for them to verify their own report.

Point (k)

*“Participated in the verification procedures regarding those statements from the [describe Public Document] that were made by us or based on statements that were made by us”*

Similar to response on point (j) above. If there are such statements, and the Member in Public Practice has given their consent to its inclusion, then those statements will not require verification.

Point (m)

*“Performed all our mandatory obligations under APES 350; and”*

The second paragraph of Appendix 1 of APES 350 already states that work has been done in accordance with APES 350 and accordingly this change is not required.

## **Paragraph 6 Assumptions**

Wording “not correct or”

*“Nothing has come to our attention that causes us to believe that these assumptions are not correct or not reasonable. We have not taken any steps to validate these assumptions other than as may be specified in our scope of work in section 2.”*

The stakeholder has made this point previously during the development phase of APES 350. The APES Board considered this issue and determined that an assumption cannot be correct. An assumption can only be reasonable or unreasonable.

## **Paragraph 7 Qualifications**

### **Point (a)**

*"We will have no responsibility to update this Due Diligence Sign-Off for events and circumstances occurring after the date of this Due Diligence Sign-Off, other than as required under the terms of the Engagement Document **and section [insert] of the DDPM adopted by the DDC;**"*

The stakeholder has made this point previously during the development phase of APES 350. The responsibilities of the Member in Public Practice must be those set out in the Member's Engagement Document. As noted in the Basis for Conclusions of APES 350 (refer to an extract below):

*Importantly, in accordance with APES 305 Terms of Engagement, a Member in Public Practice must document and communicate the terms of Engagement with the Client through an Engagement document. The professional obligations of a Member in Public Practice cannot be determined by the due diligence planning memorandum or minutes of DDC meetings which are not documents that the Member controls.*

## **Section 8 Recipients of this Due Diligence Sign Off**

### **Wording "and may be relied upon by"**

*"This Due Diligence Sign-Off is given solely for the benefit of **and may be relied upon by**"*

This is change is unnecessary as "for the benefit of" is sufficient.

### **Wording "to a Recipient's legal advisers or to auditors for audit purposes"**

*"Be disclosed except to persons who, in the ordinary course of a Recipient's business have access to their papers and records **or to a Recipient's legal advisers to obtain legal advice or to auditors for audit purposes** and on the basis that such person will make no further disclosure of it and are not entitled to rely on it for any purpose;"*

The ability to disclose the sign off to the Recipient's, legal advisors is already covered by "in defence of any actual or potential claim" in the continuation of the sentence after sub paragraph (c) of Section 8.

It is highly unlikely that an Auditor who has to perform a statutory financial audit or review in accordance with AUASB Standards will rely on a Due Diligence Sign-Off. Whilst an Auditor may collect the information to understand what has occurred in a company during the period, the work that an auditor has to perform to issue a reasonable assurance opinion means that the Due Diligence Sign-Off will have minimal value to the auditor.

Further, sub paragraph (c) as it is currently worded will allow access to the auditor.

*Wording “or an investigation (including a regulatory hearing)”*

*“Except as required by law, regulation or the rules of any Stock Exchange or government body or ~~in connection with any enquiry conducted by~~ a regulatory body or in the enforcement of the rights of, or in defence of any actual or potential claim against, a Recipient or an investigation (including a regulatory hearing)”*

The recommended wording is not sufficiently different to the existing words to warrant a change.

**Impacted Stakeholders**

Clients, Members in public practice, firms and professional accounting bodies.

**Recommendation**

Due to the accompanying reasons noted above, no changes are proposed in respect of these issues.

## **APPENDIX 1 – AFMA Comments from Baker & McKenzie**

From: Andrade, Craig

To: Channa Wijesinghe

Cc: Sanderson, Guy

Subject: APES 350 - comments from market participants

Sent: Oct 11, 2010 6:56 PM

Dear Channa

Set out below are some comments on the APES 350 standard which we have gathered from the equity capital markets practitioners at several law firms and investment banks. Attached is a proposed mark-up of some changes to the draft form of sign-off which also reflect that feedback and which we encourage the APES 350 task force to consider incorporating in a revised version of the standard.

### **Key comments:**

#### **1 Accountant expertise**

There is significant concern among several market participants about the broad brush wording in the standard that suggests that accountants do not have expertise to express an opinion on whether certain financial disclosures meet Corporations Act standards. This has caused several boards (and other advisers) a significant degree of concern about (and a lot of wasted time has been spent debating):

- the "reasonableness" of involving accountants; and
- the "reasonableness" of relying on accountants in capital raisings. For example, issuers need to seek confirmation of accountants as to their expertise and professional ability in DDCs, which is a source of embarrassment to the accountants and causes unnecessary delays at DDC.

It is the expectation of issuers and all members of DDC that each legal and accountant participant has the requisite expertise to opine on whether certain matters (financial disclosures for accountants) meet Corporations Act standards.

This statement in the standard does a disservice to the professionalism of accountants, most of whom acknowledge that it is a pre-requisite for accepting a role on a public offer that they have the requisite expertise to opine on whether certain matters (financial disclosures for accountants) meet Corporations Act standards. If accountants supposedly have limited expertise along the lines suggested in APES 350, on what basis can they offer an APES 350 sign-off that there on there being no "misleading or deceptive statements, including by omission". What meaning does this opinion have if not interpreted by reference to the Corps Act in the context of a public offer?

We remain concerned about the APES Board's ability to opine authoritatively and definitively on the individual expertise (or limitations thereto) of every accountant in Australia involved in capital

raisings, regardless of their actual level of expertise (or limitations thereto). These words are: - in direct conflict with other passages in the standard; and - not factually true. One adviser has gone so far as to say that they are a misleading representation to the market. Accordingly we request that this qualification be removed.

## **2 Observers**

There still appears to be some confusion in the market about the sign-offs given by an accounting firm when, due to the SEC auditor independence issues, that firm chooses to act only as an observer to a DDC. During the APES 350 deliberations we highlighted our concern that we, and others, had witnessed certain accounting firms attempting to use the ruse of SEC auditor independence issues as a pretext to get off DDCs and only act as an observer. We were criticised during those meetings for having made that point - the suggestion being that that kind of conduct could, and would, never occur. We have again received feedback that this is precisely what is occurring in the market (in other words, there is a problem here about the circumstances in which accounting firms are seeking to become observers of DDCs and we recommend that the APES Board address it specifically in a revised draft of the standard).

An observer in these circumstances should be required to give:

- (a) a functionally equivalent "general" sign-off as per the Due Diligence Report; and
- (b) an APES 350 sign-off.

We (and other advisers) have had some positive experiences where an accounting firm (acting as an observer) has agreed to provide a functionally equivalent sign-off that mirrors a DDC sign-off, but this experience is not uniform.

We think it would be very helpful to the market if these points were clarified and more clearly addressed in a revised version of APES 350 (for example, the definition of DDC Observer could be amended to deal with these points). In addition, market participants will continue to demand it because not having it could undermine the DD process.

## **3 Low doc offers**

There is currently a great deal of uncertainty about whether or not an accounting firm should provide an APES 350 sign-off in connection with low doc offers. Although para. 1.9 of the APES 350 standard states that it should be applied to low doc offers "to the extent practicable", we think that it would be helpful to the market to clarify that if an accounting firm performs a review mandate or Agreed Upon Procedures mandate that it would be appropriate to provide an APES 350 sign-off on the work they have performed.

APES350 does not correctly allow for adaptation to meet the appropriate wording for "reasonable steps" (rather than reasonable enquiries) in a PDS or "low doc" context. As a result, accountants now flatly refuse to sign-off using language adapted to the proper context of the document where it is a PDS or "low doc" deal. The standard should require the accountants to adapt the language to different legislative contexts.

It is generally accepted that it will be difficult to ask an accounting firm to sign-off on a low doc process where they are given only a few days to assist. However, where they have been engaged for a simple raising off the back of results, or where they have been involved in an accounting review over a more extended period of time - there is no reason why a company should not obtain proper accounting input, and a proper sign-off. We understand that some market participants have experienced situations where accounting firms attempt to use APES 350 to justify providing (a) no sign-off; or (b) refuse to provide any sign-off that goes to content of disclosure in a low doc context (even, for example, where significant work is undertaken with regard to forecasts).

We have also received some feedback that accountants are often saying that they won't sign-off on low doc disclosure because it's not a prospectus. If an accountant forms the view that prospectus-standard financial disclosure is needed in order to be able to give a sign-off that the financial disclosure is not misleading or deceptive, then they should be advising their clients to include the additional financial disclosure. The liability tests for misleading and deceptive disclosure are relevant to both prospectuses / PDS and low docs, so there is no substantive legal basis to draw a distinction. While it can certainly be the case that financial disclosure in a low doc may not be as detailed as that which would be included in a prospectus - the financial disclosures in a low doc offer should not give an incorrect impression.

#### **4 Review statement regarding "Other Specific Information"**

There appears to be some confusion, and reluctance by accounting firms, to provide a review statement in relation to "Other Specific Information", despite APES 350 permitting a review statement to be given. It would be helpful if the APES Board could clarify the circumstances in which a review statement should be provided.

#### **5 Description of scope of work and other marked up changes to APES 350**

We have marked up the template APES 350 sign-off to include a few additional scope of work items that arise on most, if not all capital raisings involving a public offer document. In addition, our other mark-ups reflect some commonly made changes to APES 350 sign-offs. Accordingly, we suggest that they be included (in square brackets if necessary) to assist the prompt resolution of the terms of the APES 350 sign-off between the client, the accounting firm and the client's other advisors.

#### **6 Final Observation**

We have received feedback that the disputes with the accounting firms that are occurring on these issues described above, and the deficiencies in sign-offs that end up being put before boards, is leading to communications with boards and management which are harming the professional reputation of the accounting firms and causing delays at DDCs. This is detracting from the valuable work that the accounting firms are doing in capital raising processes.

Our comments made above are intended to try facilitate improving APES 350 and accordingly, we encourage the APES Task Force and Board to consider them in that spirit.

As always, we remain available to discuss any of the points made above.

Kind regards

Craig

Craig Andrade

Partner

Baker & McKenzie

Level 27, AMP Centre

50 Bridge Street

Sydney NSW 2000

Australia

Direct: +61 2 8922 5364

Tel: +61 2 9225 0200

Fax: +61 2 9225 1595

[craig.andrade@bakermckenzie.com](mailto:craig.andrade@bakermckenzie.com)

[www.bakermckenzie.com](http://www.bakermckenzie.com)