

The Restructured Code of Ethics

Webinar – 3 October 2019

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Accounting Professional & Ethical Standards Board



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Channa has been with the APESB for 12 years and manages the implementation of the Board's strategy, national and international stakeholder engagement, operations and technical work program. He functions as the Chair of the Board's taskforces and has overseen the issue of APESB's suite of 21 pronouncements for the Australian accounting profession. Channa also represents APESB at the IESBA National Standards Setters Group.

Agenda

- Importance of Professional Ethics
- Restructured Code of Ethics
 - Conceptual Framework
 - Audit Partner Rotation (Long Association)
 - Non-assurance services
 - Inducements
 - NOCLAR & new Whistleblowing legislation
- Future projects

Importance of professional ethics

Importance of Professional Ethics

UK Enquiries

- Parliamentary enquiries into the roles of directors, regulators and the audit profession
- **Kingman Review** of FRC UK and creation of new regulator – **ARGA**
- **CMA Review** calls for accountability of audit committees, joint audits and operational separation
- **BEIS Review** calls for audit remit to be forward looking, enhanced shareholder engagement and reporting of audit fees
- Calls for ban on all but **essential audit-related services** for audit clients
 - **March 2019**, FRC UK commences consultation on this matter

Potential implications

- Call for more regulation – removal of self-regulation by profession
- Call for Big 4 firms to be broken up between audit and consulting (non-assurance)

Importance of Professional Ethics

PJC inquiry into regulation of Auditing in Australia

- Inquiry focused on:
 - the role and scope of audits (including fraud and misconduct),
 - the relationship between audit and consulting services and conflicts of interest
 - the effectiveness of competition in audit and related consulting services
 - audit quality
 - Matters from other review of auditing
 - the regulation of auditing and the performance of regulators
- Submissions due to PJC - 28 October 2019
- Final report issued by PJC - 1 March 2020

Importance of Professional Ethics

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

Reported many instances of misconduct:

- Fees for no service – approx. **\$3 billion**
- Inappropriate advice provided to customers
- Financial services entities **broke the law** and not held to account
- **Primary responsibility** for Misconduct with Boards and Senior Management

Final report contained **76** recommendations

Importance of Professional Ethics

Impacts:

- Large remediation costs forecasted in excess of **\$7 billion**:
 - AMP – \$1.2 billion
 - CBA – \$1.5 billion
 - NAB - \$1.2 billion
 - ANZ – \$1.5 billion
 - Westpac - \$1.8 billion
- Grandfathered commissions to be banned

Potential implications

Possible criminal breaches for entities and stricter enforcement from ASIC

Role of the auditor?

Importance of Professional Ethics

- Protects **public interest**
- Maintain and increase **trust** in the accounting profession
- Assists accountants to address professional and ethical issues
- If **adhered** to, establishes robust standards of professional conduct

The restructured APES 110 Code of Ethics for Professional Accountants (including Independence Standards)

Global adoption of extant IESBA Code

- Adopted, used as basis for national ethical standards or codes in **120+** jurisdictions
- Adopted by the largest **27** international networks of firms (the [Forum of Firms](#)) for transnational audits
- Translated in about **40** languages, including all major UN languages



Global adoption of extant IESBA Code – G20 Countries

Adopted / Based on (12)		Converged/Convergence path (4)		Committed to adopt (1)
	Australia		South Africa	
	Brazil		Saudi Arabia	
	China		South Korea	
	Italy		Mexico	
	Japan		Turkey	
	Russia		United Kingdom	
	Canada			
	Indonesia			
	Germany			
	USA (Unlisted entities)			
	India			

Highlights of the restructured Code

- New **user guide** and updated glossary
- Requirements now **separate** to guidance material
- Increased **focus** on compliance with the **fundamental principles** and **independence**
- **Enhanced** conceptual framework
- Auditor independence sections are now **Independence Standards**
- Audit Partner Rotation (Long Association): effective **1 Jan 2019**
- Non-compliance with Laws and Regulations (NOCLAR): effective **1 Jan 2018**

Highlights of the restructured Code

- Strengthened provisions on **Non-assurance Services**
- New **Inducements** provisions
- Enhanced **PDF features** in APES 110:
 - Bookmarks and pop-ups of definitions
 - Dynamic links to sections and sub-sections
 - Increased navigation within the document and externally
- **Mapping table** of the new Code vs Extant Code on the APESB Website

New Structure of the Code – APES 110

SCOPE AND APPLICATION

(All Members)

GLOSSARY

(All Members)

PART 1

Complying with the Code, Fundamental Principles and Conceptual Framework

(Sections 100 to 199)

(All Members)

PART 2

Members in Business
(including employment
relationships of
Members in Public Practice)

(Sections 200 to 299)

PART 3

Members in Public Practice

(Sections 300 to 399)

PARTS 4A & 4B

Independence Standards

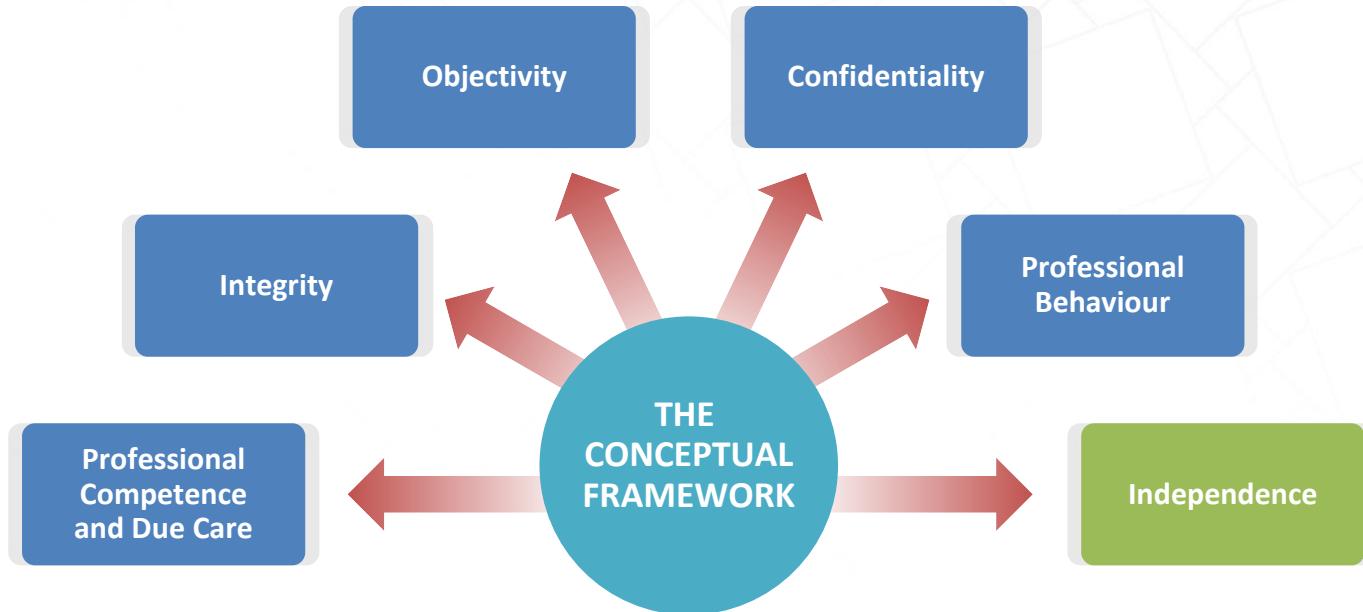
Part 4A—Independence for Audits & Reviews

Part 4B—Independence for Assurance Engagements Other
than Audit & Review Engagements

(Sections
400 to 899)

(Sections
900 to 999)

Overarching requirements



Category of threats

Self-interest

Self-review

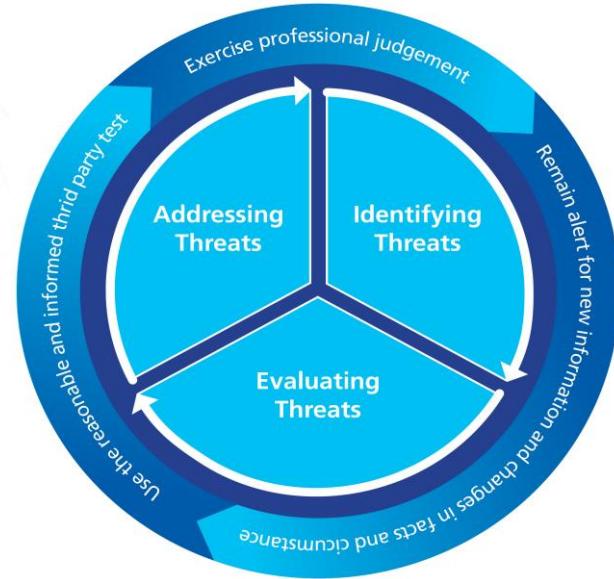
Advocacy

Familiarity

Intimidation

Enhanced conceptual framework

- No longer threats & safeguards approach - **not all** threats addressed by safeguards
- Identified threats that are **not** at Acceptable Level must be addressed in one of three ways:
 - **Eliminate** circumstances creating the threats;
 - **Apply** safeguards; or
 - **Decline** or **end** the specific professional activity/service
- **New requirements** –form an overall conclusion on effectiveness of actions, and remain alert to new information or changes in circumstances



Conceptual framework and independence

Conceptual framework now **explicitly** addresses **Independence**

New application material:

- Independence **required** for audits and other assurance engagements
- Independence **linked** to fundamental principles (e.g. objectivity and integrity)
- Conceptual framework **applies** to compliance with independence requirements
- Independence standards explain application of conceptual framework
- Categories of threats are **the same** for fundamental principles and independence

POLLING QUESTION

What is the effective date of the restructured Code of Ethics?

- a) 1 January 2019
- b) 1 July 2019
- c) 1 January 2020
- d) 1 July 2020

Long Association – Key Matters

- General provisions apply to all audit engagements
- **'Jurisdictional provision'** for PIEs
- Shorter cooling-off period specified in local laws of a jurisdiction, subject to a **floor of 3 years**
- Jurisdictional provision available for audits beginning prior to **31 December 2023**
- Effective from calendar **2019** audits
- IESBA's commitment to review these provisions early **2021**



Long Association – Strengthened Requirements



5-year cooling-off for EP subject to jurisdictional provision



Prohibition on acting as client relationship partner during cooling-off



3-year cooling-off for EQC reviewer



Additional restrictions on permissible activities during cooling-off



Technical consultations during cooling-off prohibited



Strengthened general provisions

Restructured Long Association Provisions

- Consistent with the Amending Standard to extant Code (Issued **April 2018**)
- Impact for Listed/APRA entities post 2023:
 - **5 years time-on period/5 year cooling-off period**
- **Australian focused** Technical Staff Q&As (includes flowcharts)



Partner Rotation – Listed APRA-Regulated Entities

Role	Current		Transition (1 Jan 2019 to pre 31 Dec 2023)		Full Provisions (from 31 Dec 2023)	
	Time on (yrs)	Cooling off (yrs)	Time on (yrs)	Cooling off (yrs)	Time on (yrs)	Cooling off (yrs)
Engagement Partner	5/7**	2	5/7**	3	5/7**	5
EQCR Partner	5/7**	2	5/7**	3	5/7**	3
Other Key Audit Partners	7	2	7	2	7	2

** In accordance with applicable laws and regulations, Audit Engagement and EQCR Partners can serve in the same role for a maximum of five years, but may be extended by the Audit Client or a regulator in accordance with applicable laws and regulations.

Partner Rotation – other Public Interest Entities (excludes Listed & APRA-Regulated Entities)

Role	Current		Full provisions (from 1 Jan 2019)	
	Time on (yrs)	Cooling off (yrs)	Time on (yrs)	Cooling off (yrs)
Engagement Partner	7	2	7	5
EQCR Partner	7	2	7	3
Other Key Audit Partners	7	2	7	2

Partner Rotation – Scenario 1

ABC Pty Ltd is a large proprietary company that is required to undergo an annual audit.

John has been the Engagement Partner for the audit of ABC for 5 years.

John is trying to figure out how the new auditor rotation rules affect his role.

After the 30 June 2019 audit, what are the implications for John?

- Option a) Stay on for 2 more years and then cool-off for 2 years
- Option b) Stay on for 2 more years and then cool-off for 3 years
- Option c) Stay on for 2 more years and then cool-off for 5 years
- Option d) He can continue for more than 2 years as long as he complies with the general provisions of the Long Association provisions

Partner Rotation – Scenario 2

ABC Ltd is a large public utility that is required to undergo an annual audit. It is not a Listed Entity.

Dave has been the Engagement Partner for the audit of ABC for 6 years as at the 30 June 2019 audit. Dave is trying to figure out how the new auditor rotation rules affect his role.

After the 30 June 2019 audit, what are the implications for Dave?

- Option a) stay on for 1 more year and then cool-off for 2 years
- Option b) stay on for 1 more year and then cool-off for 5 years
- Option c) stay on for 1 more year and then cool-off for 3 years
- Option d) He can continue for more than 1 year as long as he complies with the Long Association general provisions

Non-assurance services (NAS)

- New and improved guidance to assist in proper application of CF for all types of NAS:
 - New factors for evaluating threats
 - Enhanced guidance on addressing threats, including revised safeguards provisions
- Clarity about when threats created by NAS cannot be addressed
- Key prohibition on assuming management responsibilities



Prohibition – Management responsibilities (NAS)

Management responsibilities include

- Setting policies and strategic direction
- Directing and taking responsibility for work of employees of the entity
- Controlling or managing bank accounts and investments
- Reporting to TCWG on behalf of management
 - Internal control systems – design, implementation, monitoring & maintaining
- Hiring or dismissing employees
- Authorising transactions
- Deciding which recommendations of third parties to implement
- The preparation and fair presentation of financial statements

Key Changes – Non-Assurance Services (NAS)

Prohibition on providing recruiting services for a **director, officer or a person** who may have **significant influence** over the accounting records or financial statements:

- now applies to **all Audit Clients** (para 609.7)
- Ban on Recruiting Services – Kim Gibson IESBA

New guidance on:

- **Materiality** in relation to financial statements (para 600.5 A3)
- The combined effect of **threats from multiple** NAS (para 600.5 A4)
- **Factors** to assist in **identifying threats** when providing Taxation Services, IT Systems Services or Litigation Support Services for an Audit or Assurance Client

NAS prohibitions for PIEs

The Code sets out **prohibitions** for specific NAS when auditing a PIE. The prohibitions include:

- Performing accounting and bookkeeping services
- Serving as general counsel
- Promoting, dealing in, or underwriting client's shares
- Negotiating for the client
- **Recruiting** directors/officers, or senior management who have significant influence over financial statements
- **Compensating** audit partner based upon sale of NAS to their audit clients

NAS prohibitions based on materiality

Some NAS are prohibited if they would have a **material impact** on the financial statements. The prohibitions include:

- Valuation services
- Calculation of deferred and current taxes
- Tax or corporate finance advice dependent on treatment or presentation where reasonable doubt as to its appropriateness
- Acting as an advocate before a public tribunal or court to resolve a tax matter
- Acting as an advocate to resolve a dispute
- Internal audit services relating to financial reporting, financial accounting systems or financial statement disclosures and amounts
- Designing/implementing financial reporting IT systems

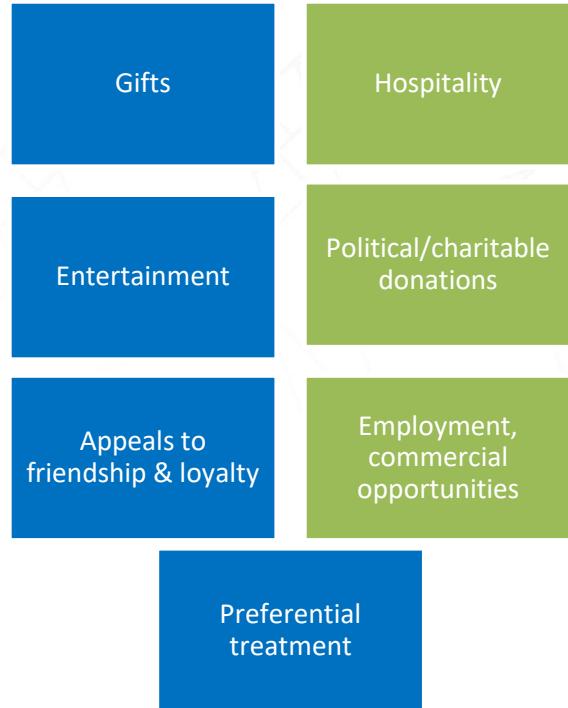
Safeguards & Non-Assurance Services

Examples of actions that might be **safeguards** generally include professionals who are not audit team members:

- Performing the NAS
- Reviewing the NAS performed by audit team members
- Reviewing the audit work or result of the NAS
- Reviewing the accounting treatment or presentation in the financial statements

Inducements

- Clarifies appropriate boundaries for **offering** and **accepting of inducements**
- Inducement can be illegal (e.g. bribery / corruption)
- Even if not illegal, prohibition on offering or accepting inducements with **intent** to improperly influence behavior (even if trivial and inconsequential)
- If no improper intent, **apply** conceptual framework



Key elements of the Inducements Framework

- Follow applicable laws and regulations
- Determine if there is **actual** or **perceived** intent to improperly influence behavior
- If no perceived intent, consider if the inducement is trivial or inconsequential
- Apply the conceptual framework, if necessary, to determine whether to offer or receive the inducement

Assessing intent – relevant considerations

- Nature, frequency, value, cumulative effect? (e.g. frequent expensive meals, lavish birthday gifts)
- Timing? (e.g. contract soon to be awarded)
- Made for right reason? (e.g. wedding)
- Ancillary to main business? (e.g. accepting lunch)
- No preferential treatment?
- Roles and positions of offeror/offeree?
- Made openly?
- Given freely?



NOCLAR

An act that causes substantial harm contrary to prevailing laws or regulations

- Committed by a client, employer, TCWG, management, or other individuals employed by the client
- Involves serious **adverse consequences** to investors, creditors, employees, general public in **financial or non-financial** terms
- Has wide **public interest** implications

NOCLAR provisions set out a **thought process, relevant factors** to consider a **response framework**

NOCLAR

NOCLAR or suspected NOCLAR that can cause **substantial harm** relates to matters that:

- Have a **direct and material** effect on a client's or employer's **financial statements**
- Are **fundamental** to an entity's **business/operations** or to **avoid material** penalties

Excludes:

- Inconsequential matters
- Personal misconduct unrelated to business
- Non-compliance **not** committed by a client or employer

NOCLAR

1. Obtain an understanding of the matter
2. Address the matter
3. Determine whether further action is needed
4. Determining whether to disclose the matter to an appropriate authority
5. Documentation

NOCLAR Framework – four variations

Framework specifies different **but proportionate** approach for each category of accountants:

- Recognises the remits of **four** categories of accountants
- Members' spheres of influence
- Members' level of authority, responsibility and decision-making power
- Levels of **public expectations** on members

NOCLAR Framework – 2 variations for Members in Public Practice

Auditors	Other Members in Public Practice
<ul style="list-style-type: none">• Comply with requirements under Auditing and Assurance Standards• Communicate in the context of group audit:<ul style="list-style-type: none">- Component Auditor to communicate with the Group Engagement Partner (EP)- Group EP to Communicate with component auditors• Documentation <u>required</u>	<ul style="list-style-type: none">• Where the client is an audit client of the Firm or Network Firm, communicate the matter within the Firm/Network Firm and with the Audit Engagement Partner• Where the client is not an audit client of the Firm or Network Firm, consider communicating with the external auditor• Documentation is <u>encouraged</u> as per NOCLAR but note APES 320 <i>Quality Control for Firms</i>

NOCLAR Framework – 2 variations for Members in Business

Senior Members in Business	Other Members in Business
<ul style="list-style-type: none">• Set the right tone at the top within the organisation.• Establish appropriate policies and procedures to prevent NOCLAR• Establish internal whistle-blowing procedures as a necessary part of good governance• Disclose to External Auditor in accordance with obligation to provide information to conduct audit	<ul style="list-style-type: none">• Escalate the identified, or suspected NOCLAR to immediate superior or next higher level of authority• Resigning from the employing organisation• Documentation is encouraged

NOCLAR – Key considerations for disclosure

- Disclosure to an **appropriate authority** depends on various factors:
 - precluded by law or regulation?
 - credible **evidence** of **substantial harm** to entity, stakeholders and general public
 - **existence** of an appropriate authority
 - any legislative or regulatory **protection** for whistleblowing
 - likelihood of **physical harm** to member or other individuals.
- In case of **imminent breach**, immediate disclosure to authorities is permitted

NOCLAR - Existing legal & regulatory mechanisms

RG 34 Auditor's obligations: Reporting to ASIC

- Suspected contraventions of the Corps Act (**Sec. 311** and Sec. 601HG)
- Contraventions/suspected contraventions by AFSL licensees (Sec. 990k) or credit licensees (Sec. 104 of National Credit Act)

ASIC information sheet 52 Guidance for Whistleblowers

- Protection of whistleblowers for breaches in companies under the Corps Act (protected disclosures)

AUSTRAC: reporting of money laundering activities (under AML-CTF Act 2006)

APRA reporting for misconduct in APRA-regulated entities

Federal and state public sector whistleblower protections

New Whistleblower protection legislation

New **whistleblowing protection** legislation **expected** to be effective from 1 July 2019:

- *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2019*
- Applies to **corporate and financial sectors**
- Not applicable to public sector – different legislation in place
- Provides protection for reporting of corruption, fraud, tax evasion or avoidance and misconduct
- Now **applies** to disclosure of **tax law** breaches and tax misconduct
- Penalties apply for breaches of the regimes

New Whistleblower protection legislation

- Whistleblower definition is broader: includes **former relationships** with an entity
- Disclosures can be made to **eligible recipients, APRA, ASIC, ATO**
- Disclosure to a politician or a journalist if in public interest or an emergency – but not for tax matters
- **Protections** include:
 - right to remain anonymous
 - provision of immunity so information cannot be used against them in a prosecution
- Whistleblowers may be eligible for compensation if they suffer detriment
- Public companies and some proprietary companies must have whistleblower policies

Other key obligations in the Code

Prohibition on being:

- Director/officer (including management of administration) for audit clients
- Company secretary for audit clients

Requirement to:

- Consider multiple threats in **aggregate**
- Evaluate threats for **multiple client referrals** from one source
- Determine if an audit or assurance client is a public interest entity (PIE) (para AUST R400.8.1)
 - Guidance on entities who will generally be considered PIEs in Australia
 - **Private Health Insurers** regulated by APRA now included as example of PIEs

Future projects

What's on the agenda for the IESBA?

Current projects:

- Role and mindset expected of professional accountants (formerly professional skepticism)
- Non-assurance services
- Fees
- Technology
- Alignment of Part 4B with ISAE 3000 (Revised)



IESBA: Non-Assurance Services project

Objective: increase confidence in the independence of audit firms.

Proposals include:

- **Prohibit** firms from providing NAS to audit clients that are PIEs if outcome of service might be included directly or indirectly in financial statements
- Distinction between NAS provisions between PIEs and non-PIEs
- **Explicit** provisions for auditor communications with TCWG about NAS matters

IESBA: Fees project

Objective: Review the provisions in the Code related to fees including those impacting perceived auditor independence.

Provisions to be reviewed include those relating to:

- The level of audit fees for individual engagements
- Fee dependency at firm, office and partner level including considering specific thresholds for audit clients that are not PIEs
- Safeguards in the Code relevant to the project scope

What's on the agenda for the APESB?

All APESB pronouncements require revision:

- Cross-references to the restructured Code
- Reviews of existing pronouncements, consideration of technology and its impact

Due process

- Pronouncements batched into groups
- EDs released progressively from March to October 2019
- Effective date of the Code and all revised pronouncements 1 January 2020

Purpose and Disclaimers

This set of PowerPoint slides has been developed by APESB Technical Staff using some of the resources developed by the IESBA Technical Staff for National Standards Setters on the revised and restructured *International Code of Ethics for Professional Accountants (including International Independence Standards)*, which the IESBA issued in April 2018.

These slides provide only an overview of the new Code and do not purport to present all the detailed changes. The slides should be read in conjunction with the new Code, the text of which alone is authoritative. The slides do not form part of the Code.

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