

8 July 2019

Mr. Ken Siong
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International Ethics Standards Board for Accountants (IESBA)
International Federation of Accountants (IFAC)
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By email: KenSiong@ethicsboard.org

Dear Mr. Siong,

IESBA's Exposure Draft *Proposed Revisions to Part 4B of the Code to Reflect Terms and Concepts Used in ISAE 3000 (Revised)*

Accounting Professional & Ethical Standards Board Limited (APESB) welcomes the opportunity to make a submission on the IESBA's Exposure Draft *Proposed Revisions to Part 4B of the Code to Reflect Terms and Concepts Used in ISAE 3000 (Revised)* (Part 4B ED).

APESB is governed by an independent board of directors whose primary objective is to develop and issue, in the public interest, high-quality professional and ethical pronouncements. These pronouncements apply to the membership of the three major Australian professional accounting bodies (Chartered Accountants Australia and New Zealand, CPA Australia and the Institute of Public Accountants). In Australia, APESB issues APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (APES 110), which includes the Australian auditor independence requirements, as well as a range of professional and ethical standards that address non-assurance services.

Overall comments

APESB is generally supportive of the IESBA's project to revise Part 4B of the IESBA's *International Code of Ethics for Professional Accountants (including International Independence Standards)* (the IESBA Code) to reflect terms and concepts used in ISAE 3000 (Revised). The proposed amendments will assist stakeholders to clarify the roles and responsibilities of parties in direct and attestation assurance engagements and the various types of relationships which could create threats to auditor independence. However, we are of the view that some of the proposed revisions add unnecessary complexity to Part 4B.

APESB understands that the IESBA Code has historically differentiated between the underlying subject matter and the subject matter information in respect of certain circumstances and relationships in respect of other assurance engagements, placing greater emphasis on circumstances associated with the subject matter information creating threats to auditor independence. However, it is not clear why Part 4B limits certain relationships that create threats to auditor independence to attestation engagements and to the subject matter information (and not the underlying subject matter) for these engagements. This may potentially result in some relevant parties not being considered by auditors when assessing matters that impact on their independence.

APESB's key recommendations are noted below. Appendix A provides APESB's responses to the IESBA's specific and general questions and other suggestions for the IESBA's consideration under Other Editorial Comments.

Recommendations

APESB's key recommendations for the IESBA's consideration in relation to the Part 4B ED are:

- The overarching requirement to be independent in Part 4B, in principle, should remain consistent with Part 4A of the IESBA Code. Where there are differences or where there may be other parties relevant to the assessment of threats to the auditor's independence, then this must be clearly specified in the introductory or application material in Part 4B.
- Review the requirements and application material of Part 4B to ensure that the intent of the provisions has been applied appropriately in relation to the differential treatment of the underlying subject matter and subject matter information. If deemed appropriate, the IESBA could consider including introductory paragraphs to explain why there is a different treatment in relation to the two elements in appropriate sections of Part 4B.
- Simplify and make the definitions clearer, including assurance client, assurance engagement, attestation engagement, and responsible party.
- Enhance the definition of financial statements to clarify that the form and content of financial statements are determined by the applicable reporting framework.
- Limit the terminology to be included in Part 4B to only those necessary to demonstrate that multiple potential parties may be relevant to assess threats to independence, particularly for attestation engagements. As stakeholders are directed to ISAE 3000 (Revised) for the elements and objectives of an assurance engagement and the Assurance Framework, it is not necessary to replicate all of this terminology in Part 4B.

Concluding comments

We trust you find these comments useful in your final deliberations. Should you require additional information, please contact APESB's Chief Executive Officer, Mr. Channa Wijesinghe at channa.wijesinghe@apesb.org.au.

Yours sincerely



Nancy Milne OAM
Chairman

APPENDIX A

APESB's Specific Comments

APESB's responses to the specific matters raised by the IESBA in Part 4B ED are as follows:

1. Do you believe that the changes in the key terminology used in the Exposure Draft, including the definition of 'assurance client', are clear and appropriate to use in Part 4B?

APESB agrees with the IESBA's approach to making the key terminology in Part 4B consistent with ISAE 3000 (Revised). However, we are concerned that some of the proposed definitions are complex and will impact on the readability of the IESBA Code and note that not all definitions are consistent with ISAE 3000 (Revised).

While the proposed revised definition of an assurance client in the Part 4B ED aims to simplify the extant definition and be consistent with ISAE 3000 (Revised), APESB believes the revised definition is not as clear and is circular. To clarify the parties who would be an Assurance Client, the definition could be revised to mean *'the responsible party and any other party in an attestation engagement who takes responsibility for the subject matter information'*. If this definition is amended, then the IESBA would need to consider consequential amendments in paragraph 900.14 A1.

APESB has noted that while the definitions have been included to be consistent with ISAE 3000 (revised), the definition of responsible party has been unnecessarily amended. APESB is of the view that there is no need to reference direct or attestation engagements in the definition of responsible party, and that the definition in ISAE 3000 (Revised) should be maintained in the IESBA Code (i.e., the parties responsible for the underlying subject matter). If the IESBA believes further clarification is needed, the words *'in an assurance engagement'* could be added to the end of the definition in the IESBA Code.

APESB also considers that refinements could be made to the following definitions:

- *Assurance engagement* – an addition could be included at the end of the definition to state that an assurance engagement can be either an attestation or direct engagement.
- *Attestation engagement* – is overly complicated and could be simplified and refer stakeholders to the source definition and application material in ISAE 3000 (Revised).
- *Financial Statements* - there is scope to enhance this definition by referring to the applicable financial reporting framework. For example, APESB has included the following text in the definition of financial statements in the Australian Code (APES 110):

'The requirements of the financial reporting framework determine the form and content of the Financial Statements and what constitutes a complete set of Financial Statements. For the purposes of this Code, financial report is considered to be an equivalent term to Financial Statements.'

- *Underlying subject matter* – the reference to phenomenon may not be understandable to many stakeholders as it is not a commonly used term and we query whether this definition is necessary to understand the proposed revisions to Part 4B (refer to the response to question 3 below).

2. **Do you have any comments on the application of the IESBA's proposals to the detailed independence requirements and application material as explained above and summarized in the appendix?**

Part 4B requires professional accountants to apply the conceptual framework to identify and address any threats to independence in relation to both the underlying subject matter and the subject matter information. However, the IESBA Code has historically differentiated between these two elements in respect of certain circumstances and relationships, with greater emphasis placed on the subject matter information creating threats to independence.

For example, Part 4B highlights that a threat is created where an immediate family member of an assurance team member is an employee in a position to exert significant influence over the underlying subject matter (paragraph 921.4 A1), which then needs to be evaluated and addressed under the conceptual framework. As this situation relates to the underlying subject matter, it is applicable to both direct and attestation engagements. Whereas, if an individual's immediate family member is an employee in a position to exert significant influence over the subject matter information (applicable to attestation engagements only) that individual is automatically prohibited from participating in the audit team (paragraph R921.5(b)), negating any application of the conceptual framework.

The proposed revisions to Part 4B limits certain relationships that create threats to independence to attestation engagements and to the subject matter information (and not the underlying subject matter) for these engagements. This is noted in paragraphs 921.6 A1(b), R921.7(b), 921.8 A1(b), R922.3(b), 922.4 A1(b), 924.3 A1 and R924.4(b). APESB is concerned that this may result in auditors not considering other relevant parties when assessing the auditor's independence.

In contrast, a firm or assurance team member shall not have a close business relationship with an assurance client (paragraph R920.4), which would include both the underlying subject matter and the subject matter information. Further, Part 4B highlights that potential threats may exist due to a long association with either of these elements (paragraph 940.3 A1(c)).

There are also differences between how Part 4A and Part 4B of the IESBA Code apply. For example, paragraph R521.5 under *Family and Personal Relationships* prohibit "an employee in a position to exert significant influence over the preparation of the **client's accounting records** or the **financial statements** on which the firm will express an opinion" from participating in the audit team. It would seem that 'accounting records' would be akin to the underlying subject matter, and 'financial statements' would be akin to the subject matter information.

Also paragraph 521.4 A1 refers to those employees in a position to exert significant influence over the client's financial position, financial performance or cash flows (which are major components of financial statements and would likely relate to both the underlying subject matter and subject matter information).

APESB is of the view that the provisions in the Part 4B ED for different circumstances or relationships are inconsistently applied and it is not clear as to why this is the case. APESB recommends that the IESBA consider reviewing the requirements and application material of Part 4B to ensure that the intent of the provisions has been applied appropriately.

If deemed appropriate, the IESBA could consider including introductory paragraphs to explain why there is a different treatment in relation to the underlying subject matter and subject matter information. For example, this could be included in a new paragraph 921.3 in relation to *Family and Personal Relationships* and similarly under Sections 922 and 924. We believe this would improve the understandability and readability of Part 4B.

The Part 4B ED refers to potential threats in an attestation engagement if the firm is involved in the preparation of the subject matter information which subsequently becomes the subject matter information in an assurance engagement (paragraph 950.8 A1). It is unclear how this would occur in practice when in an attestation engagement, the professional accountant is not responsible for the subject matter information. APESB queries whether this requirement is more relevant to direct engagements or, if relevant to attestation engagements, the IESBA should provide additional guidance to clarify this obligation.

Also, APESB believes the reference to an attestation engagement in subparagraph 950.8 A1(b) is unnecessary as paragraph 950.8 A1 has also been amended to refer to attestation engagements.

3. Do you have any comments on the other proposed changes, including on the consistency of terms and concepts in Part 4B in relation to the text of ISAE 3000 (Revised)? If so, please specify the area of inconsistency and suggest alternative wording.

APESB agrees that there should be a link from Part 4B to the source material in ISAE 3000 (Revised). Professional accountants should be utilising the source material to determine the type of assurance engagement being undertaken and the parties involved. Part 4B is then subsequently applicable to determine whether there are any threats to independence from relationships with these parties. As stakeholders are appropriately directed to ISAE 3000 (Revised) for the elements and objectives of an assurance engagement and the Assurance Framework (paragraph 900.7), it is unnecessary to replicate some of this terminology in Part 4B.

APESB is of the view that the crucial part of these amendments is to ensure stakeholders are clear that different and potentially multiple parties may be relevant in assessing threats to the auditor's independence, particularly in an attestation engagement.

However, we do not believe all the key terminology from ISAE 3000 (Revised) which has been included in the Part 4B ED is required. For example, the definitions '*underlying subject matter*' or '*subject matter information*' are unnecessary (these terms are in extant Part 4B and not defined) and the definition of '*criteria*' appears only to be included as it is a component of the definition of '*subject matter information*'. These terms do not impact on the assessment of threats to independence and overcomplicate the proposed amendments.

APESB believes that the overarching requirement to be independent in Part 4B (paragraph 900.14) should remain consistent with Part 4A of the IESBA Code (paragraph 400.11). A key achievement in the restructured IESBA Code was making the Parts of the Code consistent. It is preferable that the overarching requirements remain the same, with the application material clarifying what this requirement means for other assurance engagements, regarding potential other parties relevant to the assessment of threats to independence (refer paragraphs 900.14 A1 and A2 and 900.16 A1).

4. **Are there any other matters that you consider should be addressed with respect to the alignment with ISAE 3000 (Revised) in Part 4B or in other material, for example in an IESBA staff publication? If so, please provide sufficient explanation, including practical examples of the matter where available.**

APESB has no comments on this specific question.

5. **Do you agree with the proposed effective date? If not, please indicate why not and explain your reasoning.**

APESB agrees with the proposed effective date of June 15, 2021.

APESB's General Comments

APESB's general comments on Part 4B ED are as follows:

(a) Impact of the proposed changes for Small and Medium Practices (SMPs)

APESB believes some of the key terminology in Part 4B ED may create confusion for SMPs. For example, although the definition of attestation engagement is consistent with ISAE 3000 (Revised), it is overly complicated and could be simplified. Should stakeholders require additional information in respect to what an attestation engagement consists of, they should refer to the source (ISAE 3000 (Revised)). Further, the reference to the phenomenon in the definition of the underlying subject matter may not be understandable to SMPs as it is not a commonly used term.

(b) Developing Nations

Not applicable.

(c) Translation

Not applicable.

Other Editorial Comments

APESB notes the following editorial comments on Part 4B ED for the IESBA's consideration:

- The numbering jumps from 900.8 to 900.12 without a note between the paragraphs about the paragraphs being intentionally left blank.
- Paragraph 900.14 A2 includes the words '**or the engaging party**' which is a phrase not used elsewhere in Part 4B.
- The second and third dot points of paragraph 920.3 A2 could refer to '*assurance client*' rather than just '*client*' for greater clarity.
- The meaning of paragraph R921.5(c) as a subparagraph of R921.5 is unclear. The inclusion of the words '*such a position as listed in (a) or (b) above*' would clarify this subparagraph.

- It is not clear in paragraph 940.3 A1(c) as to whom the long association is with. APESB suggest adding wording to the effect it is with a person “*in a position to exert significant influence*” before “*the underlying subject matter and/or subject matter information of the assurance engagement.*”
- Paragraph 940.3 A4 uses different wording to other paragraphs by referring to an individual being ‘*responsible*’ for the underlying subject matter or subject matter information whereas other paragraphs refer to individuals being “*in a position to exert significant influence*” (for example, see paragraph 921.6 A1).
- The heading for section 990 includes “*other than audit and review engagements*” which has been removed from other headings in Part 4B.
- The definition for reasonable and informed third party and reasonable and informed third party test incorrectly refers to paragraph R120.5 A4. This reference should be amended to 120.5 A4.