APESB
Accounting Professional & Ethical Standards Board

AGENDA PAPER

Item Number:	4
Date of Meeting:	19 May 2017
Subject:	Proposed amendments to APES 110 *Code of Ethics for Professional Accountants* relating to Long Association

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[x] **Action Required** [ ] **For Discussion** [ ] **For Noting** [ ] **For Information**

Purpose

- To present for Board consideration the key issues raised in submissions relating to Exposure Draft 01/17 *Proposed Amendments to Long Association of Personnel with an Audit or Assurance Client requirements in APES 110 Code of Ethics for Professional Accountants* (ED 01/17); and
- To obtain the Board's approval on proposed actions to address the key issues including amending proposed provisions in ED 01/17.

Background

APESB issued ED 01/17 to seek comments (due 7 April 2017) from stakeholders regarding the proposed amendments to APES 110 *Code of Ethics for Professional Accountants* (the Code) requirements relating to Long Association of Personnel with an Audit or Assurance Client.

APESB has received submissions from various stakeholders which are summarised in Agenda Items 4(a) and 4(b) for General and Specific Comments, respectively.

Key Considerations

Key issues raised by stakeholders in their submissions are in respect of:

1) Concerns relating to implementation of proposed rotation requirements

   Respondents raised the following key concerns:

   - Stakeholders were of the view that the complexity of the proposed rotation requirements, including their interaction with applicable Australian laws and regulations, pose difficulties in their implementation and may result in potential breaches of the requirements.

- Most respondents believe that the proposed rotation requirements (specifically the transition to a 5 year cooling-off period from the proposed 3 year cooling-off period after December 2023) may lead to an audit market contraction and reduced competitiveness in the provision of audit services. A stakeholder noted that this issue could lead to an oligopoly in the audit market, which is contrary to the global view of the importance of preventing such an occurrence.

- Stakeholders cited that the proposed requirements are potentially disadvantageous to small and medium practices as well as firms operating in regional locations and specialised industries. These audit practices may experience difficulties in allocating the best resources to audits of Public Interest Entities (PIEs) including those that require expertise in specialised industries.

- A stakeholder noted that international comparison between Australia and other major jurisdictions (EU, US and UK) in respect of managing the partner rotation requirements are not appropriate. The stakeholder noted that these jurisdictions differ significantly to Australia in terms of population, geographic distribution and type of entities subject to auditor rotation. It should be noted that in the US, only SEC registrants are subject to rotation requirements, not PIEs. The US also has exempted smaller firms with few clients from the rotation requirements, in recognition of their potential adverse impact to the smaller end of the market. In Australia, implementing the same requirements as these other jurisdictions could result in unnecessary regulatory burden to firms and their clients that are disproportionate to their size.

- Respondents were of the view that there is no sufficient empirical data to support that the proposed rotation requirements would result in enhanced audit quality.

- A stakeholder acknowledged the high level of direct involvement from the Engagement Partner and Engagement Quality Control Review (EQCR) Partner as a key driver of audit quality. As the proposed rotation requirements are likely to lead to Engagement Partner and EQCR Partner being in different geographical locations to the client and engagement team, it will potentially cause difficulties in the conduct of the audit and may negatively impact audit quality.

- Some stakeholders noted the long lead times involved in managing the complexities of a firm’s audit rotation planning. Therefore, the stakeholders highlighted the need for sufficient time to amend rotation plans already in place in the lead up to the implementation of the new requirements and throughout the transitional periods and, if it occurs, the end of the transitional period in December 2023.

- Stakeholders have requested that APESB proactively engage with:
  - the International Ethics Standards Board (IESBA) to influence them to remove the sunset to the transitional provision for the jurisdictional requirements; and
  - the Government, to influence the amendment of applicable laws and regulations to be consistent with the Code’s requirements.

Technical Staff understand the concerns raised by the stakeholders, and are of the view that the Board should:

- Continue the engagement with the IESBA and actively contribute to the IESBA’s efforts in evaluating the impact of the jurisdictional requirements during the transitional period;
- Influence the IESBA to consider removing the sunset clause and retain the 3 year cooling-off period as the long-term requirement; and

- Subject to the progress at the international level, consider approaching the Federal Government via Treasury to influence the amendment of laws and regulations that will result in partner rotation requirements which are consistent with the Code.

2) <u>Need to amend Australian specific paragraphs relating to jurisdictional requirements</u>

The proposed jurisdictional requirements in paragraph 290.163 of the Code allow for a 3 year cooling-off period for Engagement Partners where legislation or regulation has established a cooling-off period of *less than 5 years* and the time-on period *does not exceed 7 years*.

The Corporations Act (the Act) and the APRA Prudential Standards generally require a cooling-off period of 2 years after a time-on period of 5 years.

Therefore, the jurisdictional requirement for time-on period in paragraph 290.163 would be satisfied under the Australia laws and regulations, and the 3 year cooling-off period can then be applied.

A stakeholder has recommended:

- replacing the proposed AUST paragraphs in the Exposure Draft with an AUST paragraph that sets out how paragraph 290.163 applies to the audits of PIEs that are subject to the Corporations Act and APRA Prudential Standards; and
- that guidance is needed setting out the interaction of the Code's requirements with those of the Act and APRA Prudential Standards.

Technical Staff agree with the stakeholder's views and propose the following AUST paragraph to replace current AUST paragraphs 290.163.1 and 290.163.2 in the Exposure Draft:

AUST 290.163.1 In Australia, where laws or regulations require a two year cooling-off period for Engagement Partners for audits of Public Interest Entities[1], the cooling-off period shall be three years for periods beginning prior to 31 December 2023.

Footnotes:

1 Refer to s324DA of the *Corporations Act 2001* which has more restrictive Audit Partner rotation requirements for Listed Entities in Australia.

In respect of the references to APRA Prudential Standards, Technical Staff recommend, as part of the Code's revision, that the definition of PIE (AUST paragraph 290.26.1) be updated to make reference to APRA Prudential Standards for applicable regulations to audits. This should draw users' attention to the need to consider relevant APRA regulations whenever a Member performs an APRA related PIE audit engagement.

3) <u>Application of jurisdictional requirements to extensions of time-on period under applicable laws or regulations</u>

A stakeholder has noted the need to clarify the cooling-off requirements for Engagement Partners who have served a time-on period of 6 years.

Technical Staff are of the view that this scenario falls under the Code's requirements of maximum time-on period of 7 years with corresponding 3 years of cooling-off period. To clarify this matter, Technical Staff recommends that the following be added as a new paragraph:

AUST 290.163.2 In Australia, where in accordance with applicable laws or regulations, the time-on period for Engagement Partners has been extended from five years to six years, the cooling-off period shall be three years.

Staff Recommendation

The Board approve:

- the adoption of the proposed revised AUST paragraphs noted above, subject to the Board's editorial comments; and
- the proposed actions relating to engagement with the IESBA and the Government to address the concerns raised by stakeholders in respect of proposed auditor rotation requirements.

Materials Presented

Agenda Item 4 (a)	APES 110 ED 01/17 General Comments Table
Agenda Item 4 (b)	APES 110 ED 01/17 Specific Comments Table

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