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New Zealand Auditing and Assurance Standards Board  
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Submitted via: [www.xrb.govt.nz](http://www.xrb.govt.nz)

Dear April,

**Exposure Draft 2021-4 – Proposed Amendments to *Professional and Ethical Standard 1: NonAssurance Services***

EY welcomes the opportunity to comment on the Exposure Draft 2021-4.

EY is supportive of the New Zealand Auditing and Assurance Standards Board's (NZAuASB) efforts to enhance the Non-Assurance Services (NAS) provisions of the NZ Code of Ethics, as well as the new provisions to strengthen and improve the quality of firm communication with Those Charged With Governance surrounding NAS-related matters. Broadly we agree that the NZAuASB's proposed changes will reinforce and strengthen auditor independence, and in turn promote confidence in financial reporting. However, there are certain aspects that we are concerned with, as explained below, and believe further deliberation by the NZAuASB would be beneficial.

EY strongly believes that the provision of permissible NAS enhances stakeholder value and, in some instances, improves audit quality so long as such services do not impair, or appear to impair, the auditor's objectivity and impartial judgment.

In fact, certain NAS are best performed by the company's auditors due to three key factors:

- i) The auditor's independence; ii) Procedures may already be performed in the course of the audit; and
- iii) Knowledge gained about the company during the course of certain non-audit services can improve the quality of the audit.

This view is supported academically, notably by Defond and Zhang in 2014 who, following a comprehensive review of academic literature suggest that tax related NAS improves audit quality. This is consistent with the strongly supported academic view that auditor competency plays an important role in explaining audit quality and that the performance of certain NAS can enhance auditor competency.

Tax implications of a company's business and transactions are complex, even when clearly supported by tax authority precedent, and are often directly relevant to understanding a company's financial statements. A blanket prohibition on tax advisory and tax planning services could negatively impact the auditor's understanding of their client and, consequently, impact on audit quality. Further, the proposed additional NZ prohibition will consequently limit competition and choice of auditors or tax advisors given the relatively small local market if one firm is precluded from providing either audit or tax services, especially for large corporates or multinationals that need specialists capable of dealing with complex and cross-jurisdictional transactions.

EY is concerned that the proposals to the NZ Code of Ethics that go beyond the International Code of



Ethics promulgated by the IESBA will increase the costs of compliance and ultimately undermine the

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purpose of a global Code. The timing of the NZAuASB's proposed revisions fails to provide sufficient opportunity for the market and the profession to assess the impact of the IESBA's enhancements to the NAS provisions, which the NZAuASB are proposing to implement contemporaneously.

In our view, the "compelling reason" test<sup>1</sup> to deviate from the IESBA Code has not been satisfied given the proposed prohibition will not promote significant improvement to audit quality and the associated costs and risk are likely to outweigh the benefits (if any). We are further concerned that the public survey NZAuASB relied on to conclude NAS have negative effects on users' perception on auditor independence may not accurately reflect the broader market consensus given the small sample size of only 115 respondents. Moreover, the survey question that identified tax services tend to have an especially negative effect on perception only had 86 respondents. It is also questionable whether any beneficial effect on auditor independence in appearance by restricting, or even completely prohibiting, NAS will solve the profession's perception challenges.

As reported by the Financial Markets Authority in its 2020 Audit Quality Monitoring Report, the level of NAS fees compared to audit fees has remained low in the past two years at just 16% of the total fees charged to listed entities. This is a positive trend that the profession and company directors should be given the opportunity to continue to effectively manage, particularly since the new IESBA NAS enhancements will further assist this trend. We are concerned that a ban on tax advisory and tax planning services will undermine director responsibilities which has already resulted in the market's natural reduction in auditors providing NAS.

EY believes the proposed prohibition of tax advisory and tax planning services warrants further consideration by the NZAuASB, and we hope our comments will aid these efforts. EY proposes that NZAuASB should assess the effectiveness of the changes made to the IESBA Code before seeking to go beyond these changes, and to understand the impact of these changes on the perception of auditor independence. In the event that these enhancements do not prove effective to improve public interest concerns about any perceived lack of independence, EY would welcome the opportunity to re-consider these prohibitions or any other feasible alternatives, such as:

1. To restrict changes to listed or FMC higher accountability entities as opposed to all PIEs (the NZ PIE definition is very broad, including large charities) and
2. To allow tax advice in situations where the position is highly likely to prevail (or similar thresholds)

Detailed responses to the specific questions and comments posed by the NZAuASB are provided in Appendix 1.

We would be pleased to discuss our comments with NZAuASB and its staff. Should you wish to do so, please contact me ([simonleigh.walker@nz.ey.com](mailto:simonleigh.walker@nz.ey.com) or on +64 27 271 0788).

Yours sincerely

Simon O'Connor  
Managing Partner

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<sup>1</sup> XRB's Principles of Convergence to International Standards, Appendix 1 flowchart

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**Appendix I: Responses to specific questions and comments****Building a better  
working world****604.15 A1)****1. Do you agree that the provision of tax advisory and tax planning services to an audit client that is a PIE should be prohibited? (Refer NZ R604.15 – NZ**

No, we do not believe the provision of tax advisory and tax planning services to an audit client that is a PIE should be prohibited for the following key reasons:

i) Impact to audit quality and limits market choice

EY believes that prohibition of tax advisory and tax planning services would reduce already limited choice in the professional services market in New Zealand. It would not bring any improvement in audit quality and potentially also lower the quality of tax services. Through providing permissible NAS (with appropriate safeguards) audit firms can develop a deeper understanding of the audited company through greater sharing of knowledge but also ensure the appropriate level of challenge in the audit remains. The permissible NAS can further the auditor's insight and competency and can enhance the auditor's professional scepticism, thereby increasing audit quality. Further, if the advice is likely to prevail, there is nothing contentious being audited in terms of subjectivity of tax positions to be taken. Unnecessarily restricting NAS could have unintended adverse effects on the underlying quality of the audit through restrictions in knowledge and skills.

ii) Additional cost to business

The prohibition of tax advisory and tax planning services could create challenges for companies such as extra costs and risks or the inability to find a suitable firm that is independent to perform the work. In particular, the impact would be greater on small-medium sized Public Interest Entities and those with overseas related entities as Those Charged With Governance typically prefer consistency of tax advisors and/or auditors. The need for one firm to advise on tax and another to audit key issues would inevitably increase costs and risks, plus potential loss of audit quality as noted above. Foreign owned NZ PIEs may be particularly disadvantaged by these proposals. They may be forced to have different NAS providers compared with their related entities in different countries. This can result in additional costs, inefficiencies and increased risks.

iii) No compelling reason for additional restriction in NZ

EY is unaware of audit failures tied to independence concerns around the provision of tax services and there is no conclusive evidence that there is an improvement in audit quality subsequent to restrictions on NAS. In fact, the FMA in their 2020 Audit Quality Monitoring Report noted: *When assessing the level of non-assurance services provided by audit firms, we did not find any correlation between the level of non-assurance services provided and the quality of the audit.*

Further, as part of overarching principles of harmonisation with IESBA and Australian standards, the "compelling reason" test, in our opinion, has not been satisfied to justify the additional restrictions. The proposed prohibition is not clear and are not consistent with the NZAuASB's harmonisation approach. As explained above, it also does not promote significant improvement in audit quality, might detract from it and there are associated costs and risks to companies that are likely to outweigh benefits (if any).

We appreciate NZAuASB's effort to resolve the concerns around perception from NAS survey, however only 86 people responded to the negative effect question on the nature of NAS performed by an audit firm. This is by no means a large enough sample size that can be said to reliably reflect the overall market perception and convincingly justify the proposed prohibition.

iv) Undermines directors' role and responsibility

As indicated in the NZAuASB Invitation to Comment paper, there is already evidence<sup>2</sup> that the level of NAS compared to audit services is low for audit clients that are PIEs. With the level of fees for NAS being provided by a listed company's auditor being only 16% of the total fee

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<sup>2</sup> FMA's 2020 Audit Quality Monitoring Report

charged; this is a positive indication that audit firms and Those Charged With Governance are carefully exercising their professional judgement when considering the nature and extent of NAS to be provided by the auditor. This market trend is reflected in Australia and other jurisdictions that apply the IESBA Code. Accordingly, we strongly believe that there is no need for additional restrictions as Those Charged With Governance are exercising their responsibilities in this space judiciously and IESBA code will further this reduction.

- v) Recognising that the NZ PIE definition is very broad, the proposed changes would therefore impact a large number of small-medium sized entities; if a prohibition on tax advisory and planning services is being considered, we could therefore see benefit in only prohibiting such services to only listed PIE entities or to FMC higher accountability entities. However, there should be consideration around inefficiencies created when defining a different set of requirements based on the type of PIE entities.

## 2. Do you foresee any unintended consequences of this prohibition?

EY is concerned that the proposed changes may create unintended consequences for the following reasons:

- i) Less direct knowledge or information sharing between the audit team and the tax professionals on the operations and/or risks of the company that could negatively impact audit and tax quality. ii) The definition of tax advisory and tax planning services is not well understood and therefore the proposed changes result in less clarity on the application of the Code. Please also see response to question 3.

## 3. Do you agree that advising an audit client in their tax return preparation or any adjustments arising therefrom is a form of tax advisory service? As such, consistent with the addition of NZ R604.15 such services would be prohibited for PIEs. (Refer NZ604.5 A1 and NZ604.11 A1)

EY does not support the prohibition applying to tax compliance services (whether preparation or review), which is in line with the current approach from NZAuASB. However, the proposal suggested by NZAuASB will potentially restrict the ability for the audit firm to provide tax compliance services which may require incidental and or additional tax advisory services in relation to the tax return that are being prepared or reviewed. We do not believe advising on the tax return preparation and related adjustments should be considered tax advisory service.

We believe the proposal may result in inconsistent application where the auditor would be permitted to undertake the preparation of the tax returns based on the client's past tax advice but could not separately provide advice to the client on how a past transaction could be treated by the client, if the client is preparing the tax return.

This could lead to Those Charged With Governance engaging their auditors to complete the tax returns on an ongoing basis as they would be unable to individually engage their auditor to provide discreet, potentially one-off, advice.

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NZAuASB should reconsider this, and at a minimum provide further clarity on when tax compliance becomes tax advisory, as it has the potential for misunderstanding and therefore misapplication. The definition and guidance on these interpretations will need to be extensive to avoid inconsistency of application of the proposed restrictions.

## 4. Are there any other tax services contemplated by proposed subsection 604 for which you consider the requirements should be further strengthened and, if so, why?

We do not believe there is compelling reason to depart from the NAS provisions recently approved by the IESBA.

5. The NZAuASB has not identified any further aspects of the IESBA's provisions that need to be strengthened in New Zealand. We are, however, keen to hear whether stakeholders consider there is a need to further strengthen any specific provisions.

We do not believe there is compelling reason for any change from the IESBA NAS provisions.

6. **Do you agree that services performed by the audit firm will generally not create a self-review threat to the firm's independence when the services are related to the audit engagement?**

Yes, some NAS (e.g., attestation reports, pro forma, profit forecast, and comfort letters) necessitate an auditor's independence and sound understanding of the company's financial reporting. The benefit of the auditor providing these services arises from the auditor being able to assess whether the information is consistent with the understanding obtained during the audit of the financial statements.

7. **Do you agree that the examples listed would not generally create a self-review threat to independence? Are there other types of services, that would generally not create a selfreview threat to independence, that you consider need to be included as examples? (Refer NZ600.14 A1)**

Yes, we believe providing advice and recommendations that are unrelated to financial reporting nor have an impact on the financial statements will not create self-review threat to independence.

8. **Do you agree that the additional application material emphasising the need to apply the conceptual framework to identify, evaluate and address threats to independence, other than the self-review threat, is helpful to ensure diligent application of the conceptual framework? (Refer NZ600.14 A1)**

Yes, EY believes additional material will be helpful to ensure diligent application of the conceptual framework.

9. **Do you consider additional requirements or application material is needed in relation to audit-related services, to address perceptions of auditor independence? If yes, please provide details.**

Yes, we encourage NZAuASB to provide more clarity for Those Charged With Governance and auditors to better understand the scope and limitations services that can be provided by the auditor.

10. **For engagements entered into before 15 December 2022, for which work has already commenced, the transitional provision provides that the firm may continue the engagement under the extant provisions of the Professional and Ethical Standard 1 for up to 12 months. Do you agree with the transitional provision? If not, please explain why not and what alternative you propose.**

Yes, EY agrees with the transitional provision should NZAuASB decide to adopt prohibition of tax advisory and tax planning services to an audit client that is a PIE.