Robert Buchanan, Chair
New Zealand Auditing and Assurance Standards Board
PO Box 11250 Manners St Central
Wellington 6142

29 October 2021

Dear Robert

Amendments to Professional and Ethical Standard 1: Non-Assurance Services Exposure Draft NZAuAsB 2021-4

We appreciate the opportunity to comment on the proposed adoption of the IESBA changes regarding non-assurance services and the NZ specific proposed amendments, together with the Amendments to Professional and Ethical Standard 1: Non-Assurance Services Exposure Draft NZAuAsB 2021-4.

This response is filed on behalf of PricewaterhouseCoopers New Zealand (PwC NZ). References to "PwC", "we" and "our" refer to PwC NZ only. This submission is not made on behalf of the global network of member firms.

Overall comments

We are supportive of the objective of IESBA to strengthen the International Independence Standards (IIS) by addressing public interest concerns about the perceived threats to independence when firms provide non-audit services (NAS) to their audit clients, and particularly those that are PIE audit clients. PwC is committed to audit quality and measures to improve stakeholder perception of audit quality.

We also recognise the importance of global conformity and consistency. As set out in our responses to the specific questions below, the more restricted position proposed by the NZAuASB may be difficult to implement in practice for multinational audit clients.

The XRB recognise that diverging from an international standard must be supported by a "compelling reason[1]" and the changes must not "conflict" with the international standards. The PIE definition in New Zealand is broad and captures many more entities than in other comparable jurisdictions. Most of the investor sentiment from the surveys referenced appears to be directed at listed entities. We encourage the NZAuASB to consider whether the prohibitions proposed apply too broadly given our small New Zealand market and whether, should the NZAuASB proceed with the proposals, they are narrowed to apply to New Zealand publicly listed entities only.

We note that the New Zealand specific proposed amendments have been referenced to "investor feedback" and specifically the outcomes of the survey completed by the XRB in April 2021 "Understanding perceptions of audit independence". The survey included responses from 115 respondents. The XRB survey responses appear to have influenced the stricter measures proposed in the New Zealand standard with regard to tax related services. However, our observation, from our assessment of the survey results, is that there appears to be a general lack of understanding amongst the respondents of the threats arising from other services that might be provided to audit clients. Services that would represent a significant threat to auditor independence, such as preparing financial statements or designing and implementing internal control systems or accounting systems were rated as having a lower weighted average "negative effect" by respondents than tax advice or advice relating to financial reporting.

[1] ED paragraph 17

As examples we refer to the weighted average responses[2] to:

- Design and implementation of internal control systems - 1.53
- Preparation of financial statements - 1.69
- Design and implementation of accounting information systems - 1.56

The negative perception rating from respondents for tax related services was higher than for the above services (1.73 – 2.36), yet we would have expected a reasonable and informed third party to have perceived the negative effect to be higher for the three services listed above given the actual independence threat created if such services are provided by an audit firm to an audit client.

CA ANZ Survey Results
Of relevance to investor perceptions is the *2021 New Zealand Investor Confidence Survey* results from the CA ANZ survey which included 524 respondents. The CA ANZ survey confirmed that confidence in auditors is high with auditors remaining number one in the most trusted group when it comes to investor protection and market integrity[3]. 92%[4] of those surveyed had confidence in the audited financial statements. This confidence level is high and a positive reflection of the confidence investors have in auditors.

The CA ANZ survey evaluated the confidence in financial information released by publicly listed New Zealand entities and indicated a strong level of confidence that auditors act ethically and provide honest and independent third-party scrutiny, and only 12[5] of the 524 respondents suggested that either the companies or the auditors have a conflict of interest.

Additionally, the ED acknowledges that there is evidence in New Zealand that the level of NAS compared to audit services is relatively low for audit clients that are PIEs.

The surveys illustrate a potential lack of understanding of how other services may actually impact auditor independence. It is not clear whether the respondents were providing answers based on the reasonable and informed third party test in the *IESBA Code* and *Profession and Ethical Standard 1: International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* (PES1).

We do not believe the outcomes from either of the surveys support a compelling reason to impose further restrictions, over and above those already contained within the IESBA Code, in respect of the services that audit firms provide to PIE audit clients. It would be helpful to understand the other sources of information that the NZAuASB have considered in evaluating the compelling basis for the proposed changes.

If the NZAuASB believe compelling reasons exist, then restricting the proposals to New Zealand publicly listed entities only would seem to more appropriately address the investor concerns noted in the ED with auditor independence and would correlate to the results of the surveys noted above.

We would encourage the NZAuASB to consider whether there is more that could be done to educate investors of the restrictions that exist in the ethical standards around other services an audit firm can perform. More education on the nature of the independence threats, particularly self-review threats, that can arise and potential mitigations would also be helpful to the broader understanding of investors. We would also encourage the NZAuASB to consider whether alternative options exist that would meet their objectives. This could include development of Guidance Notes to assist practitioners with the practical application of the IESBA changes.

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[2] NZAuASB Public Meeting Papers 8 April 2021 page 10
[3] Executive summary, page 3 of the CA ANZ investor confidence report
[4] Executive summary, page 3 of the CA ANZ investor confidence report
[5] Page 7 of the CA ANZ investor confidence report

Concluding comments
PwC supports consistency and conformity with international standards. Adopting the IESBA changes with no further amendment would facilitate consistent auditor compliance with independence requirements particularly for Network firms with multinational audit clients.

The IESBA Code restricts the provision of any service that "might" create a self-review threat for a PIE audit client. Therefore, with appropriate guidance, the restrictions already contained in the IESBA Code would prohibit tax services that may create a self-review threat negating the need to further strengthen PES 1 with the New Zealand specific amendments.

We acknowledge the public interest test that the NZAuASB takes into account in applying its compelling reason test. We encourage the NZAuASB to ensure it has the appropriate level of evidence to support any New Zealand specific changes as part of the compelling reason evaluation, including consideration of the impact for global clients and network firms if New Zealand specific changes to the IESBA code are adopted. We also encourage the NZAuASB to consider whether the population of audits that the proposals would apply to is appropriate given our market size and the survey results.

Our responses to the ED questions are included in the attached appendix.

Yours faithfully

Karen Shires
Chief Risk & Reputation Officer

Specific question responses:

(i) New Zealand specific changes to tax advisory and tax planning services

Question 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 604.15 A1)

The IESBA amendments do not prohibit the provision of tax advisory or tax planning services to a PIE audit client but do recognise that the services are not permitted if the provision of such services **might** create a self-review threat.

We do not agree that all tax advisory and tax planning services are likely to create a self-review threat, as we explain below. IESBA 604.12 A2 provides examples of tax services that will not create a self-review threat. We believe this offers appropriate guidance for the application of the standard.

The additional restrictions for tax services proposed by the NZAuASB removes the professional responsibility for members and assurance practitioners to evaluate whether a self-review threat *might* arise from tax advisory and tax planning services and suggests a self-review threat will always arise from such services.

Further relevant context
It is a reasonable expectation that management of a listed entity has sufficient expertise to make decisions relevant to tax advice and tax planning. Notwithstanding the skills and competence of management, technical advice on tax is a necessary and essential service that businesses require from time to time.

Given the removal of a "materiality" consideration, the effect of the IESBA changes would only permit services that do not create a self-review threat.

Tax advisory and tax planning services can include factual representations of tax law and/or regulations. It may involve consideration of scenarios and the potential impact based on current or proposed tax legislation in any given jurisdiction. The output of the service may provide options or recommendations based on law or regulation, and it is possible that a self-review threat does not arise, and would not be expected to arise, given there is no direct advice to the client.

In respect of the IESBA changes, there is an acknowledgement that a self-review threat does not arise just because a service relates to a number that appears in the financial statements. There has to be more complexity or uncertainty or forward planning/speculation involved before it runs the risk of judgements that would be subject to evaluation by the auditors. The international standard acknowledges that if, for example, there is a ruling request submitted to Revenue authorities, or standard practice to be followed, then the advice is simply bringing that standard practice to the attention of management and so is an application of existing tax rules to an existing commercial transaction or event. This differs from tax planning or advisory work that relates to structuring for the best results in a future transaction.

Tax advice may have an indirect effect (or no actual effect) on the financial statements. The output of the service may prevent the entity incurring significant cost or prevent a negative tax position or breach of tax legislation. The effect of such advice may not be identifiable and would not cause a self-review threat as there is no direct impact on the reported (or historical) results in the financial statements.

Clarity point
We recommend that the NZAuASB consider distinguishing tax advisory or planning services where the effect or outcome will not be subject to audit (i.e. there is no direct or only an indirect impact on the financial results) from other tax services and that the former be permitted in New Zealand under the NZAuASB changes. We acknowledge that this circumstance may not be frequent.

Examples of tax advisory services that may not have a direct effect on the audit subject matter, although they may have an indirect effect:

a) assisting or advising an audit client with a voluntary disclosure for tax or GST (these services are not covered by 604.20 Assistance in the Resolution of Tax Disputes),

b) assisting or advising an audit client on transfer pricing documentation to meet compliance requirements under the Income Tax Administration Act, or

c) other tax advisory or tax planning services for proposed transactions that involve presentation of the options available with the respective impacts based on the Income Tax Act but do not involve a recommendation.

Question 2: Do you foresee any unintended consequences of this prohibition?

We believe that prohibiting all tax advisory and planning services for PIE audit clients may have unintended consequences and cause confusion for auditors and some organisations, particularly for those with cross-territory Group client relationships.

ISA (NZ) 600, and its international equivalent (ISA 600), require audit teams reporting to PIE Group auditors to meet the Group reporting entity's relevant territory independence requirements. The conformity with Global independence requirements facilitates a clear understanding of requirements around the network firms.

The New Zealand specific changes do not appear to take into account the global nature of both audit engagements and tax engagements undertaken by larger firms. Whether it is a global audit engagement (New Zealand outbound or multinational inbound to New Zealand), a global tax engagement, or both, the New Zealand specific prohibitions risk creating confusion because of the inconsistent global approach to service restrictions.

Clarity point
The NZAuASB should clarify the boundaries of the proposed prohibitions, particularly for multinational clients with group audit responsibilities.

As an example: For multinational group audit clients, where the New Zealand entity is a PIE, does the restriction apply only to the New Zealand PIE entity, to subsidiaries in New Zealand and/or subsidiaries offshore? Tax services provided in an offshore territory to a subsidiary may breach the New Zealand PES 1 requirements but comply with IESBA. This would create an independence issue for the New Zealand PIE auditor.

If tax services that would be subject to stricter New Zealand restrictions are provided to an offshore group audit client but have relevance to a New Zealand PIE audit client, is this intended to be captured? This circumstance may not be known by the auditor in New Zealand until the work has been concluded or may not be identified at all if the effect on the financial results is indirect rather than direct, ie: the services may result in tax savings which would not be "visible" to the New Zealand auditor. Such a service cannot create a self-review threat but would nonetheless be prohibited in New Zealand under PES 1 if the NZAuASB amendments are approved.

By way of example to illustrate the complexity of applying the proposed New Zealand restrictions more broadly, the following scenarios are common in respect of the audit and tax services provided to multinational Groups:

1. New Zealand PIE Group with international subsidiaries, audited in New Zealand and offshore by one audit firm (or network of firms);
2. New Zealand PIE Group with international subsidiaries, audited in New Zealand by one firm and offshore by different audit firm(s);
3. New Zealand PIE audited by an offshore audit firm with a licence to audit in New Zealand;
4. Offshore PIE Group with New Zealand subsidiaries subject to PIE group independence requirements, audited offshore and in New Zealand by one audit firm (or network of firms);
5. Offshore PIE Group with New Zealand subsidiaries subject to PIE group independence requirements, audited offshore by an offshore audit firm which also audits the New Zealand subsidiaries;
6. Offshore PIE Group with New Zealand subsidiaries, audited offshore by one firm and in New Zealand by another firm.

There may be other consequences arising from these differences.

Question 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 services? As such, consistent with the addition of **NZ R604.15** such services would be prohibited for PIEs. (Refer NZ 604.11 A1)

We do not agree that tax return and other tax compliance services are a form of tax advisory services that should be incorporated in the proposed additional restrictions.

The IESBA Code has distinguished between activities which are largely mechanical and other services which are more complex or judgemental. IESBA view tax return preparation as procedural, relying on the application of tax rules applied to a defined set of client prepared data. Whilst there may be some judgement in the application of the tax legislation (i.e. is something capital or revenue) the tax practitioner follows standard practice and operates within the boundaries of the law, limiting the ability to apply any significant judgement as to how a balance is "returned" as part of the tax return preparation. We agree with the distinction adopted by IESBA that providing tax return preparation services does not usually create a threat (604.6 A1) because:

(a) Tax return preparation services are based on historical information and principally involve analysis and presentation of such historical information under existing tax law, including precedents and established practice; and

(b) Tax returns are subject to whatever review or approval process the tax authority considers appropriate.

We note NZAuASB's proposed restrictions reference the evidence of investor perception that they have obtained through the market surveys referred to above. However, we suggest that the presentation of the survey questions, and the investor responses to those questions, support the distinction put forward by IESBA. The survey did not incorporate tax return and other tax compliance services together with tax advisory and tax planning services, and incorporating those services now would be inconsistent with that initial distinction. Whilst we have raised earlier our concerns regarding the general level of understanding regarding non-audit services and the threats to independence that may arise, the results of the survey clearly indicate a divergence of the perception of the threat when it comes to tax compliance versus more complex tax advisory work.

A critical element of the tax return preparation that removes any responsibility for the accounting firm having prepared the tax return is that the taxpayer must, under New Zealand law, take responsibility for any tax positions and tax filings. Practically, tax return preparation occurs some time after the financial statements audit has been completed for PIE audit clients. This is because the timeframes for financial statement preparation and the audit requirement for a PIE entity are shorter than the tax return filing period, particularly for clients registered with a tax agent who have an extension of time for filing the tax return.

Some audit clients engage the service of a tax agent to take pressure off filing their annual tax return in terms of capacity and available time. As a client of a registered tax agent, they enjoy an extension of time (EOT) arrangement that would otherwise not be available to them. As the tax agent, the practitioner prepares and files the tax return based on information provided to them by the client. Such services do not, in our view, create a self-review threat.

Clarity point
There appears to be an inconsistency in the proposed changes relating to tax return preparation. Paragraph 604.6 A1 reflects that providing tax return preparation services does not usually create a threat because they are based on historical information and are prepared under existing tax law. In addition, the return is subject to review and approval processes employed by the tax authority. This is consistent with IESBA. Notwithstanding this, the NZAuASB have considered that advising an audit or review client in their tax return preparation constitutes tax advisory services (NZ604.11 A1) and would therefore be not permissible for PIE audit clients (NZR604.15) if the changes proposed are approved. This is confusing.

Clarification of the distinction between section 604.6 A1 that reflects that there would not usually create a self- review threat created from providing tax return **preparation** services and NZR604.15 which prohibits **advising** a PIE audit client in their tax return preparation because it would create a self-review threat would be helpful.

Question 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 requirements of subsection 604 require strengthening, however we do consider subsection 604 requires further consideration to address apparent inconsistencies which we believe may create confusion over what constitutes “tax advisory services”.

As an example, it is not clear whether the provision of regular tax compliance services such as preparing GST, PAYE, Transfer Pricing and FBT returns and filing is captured as tax advisory services (NZR604.15) or tax preparation services as defined in NZ604.5 A1 and 604.6 A1, which would suggest such services would be permissible for all audit or review clients.

A further example of an area where the proposed NZAuASB changes create inconsistency and potential confusion is in determining what will constitute tax advisory services. This currently includes R604.24: Assistance with resolution of tax disputes. This service has not been further restricted by the NZAuASB for PIE audit clients and has not been categorised as a tax advisory service. This seems inconsistent with the position adopted by the NZAuASB on tax advisory services.

(ii) Any other Non-assurance services

Question 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.

PwC supports the application of conformity in adopting global standards to ensure consistency and remove unnecessary additional challenges with delivery of services to global clients.

(iii) Audit-related services

Question 6: Do you agree that additional 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?

PwC agree that audit related services will generally not create a self-review threat to the firm's independence.

Question 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 self-review threat to independence, that you consider need to be included as examples? (Refer NZ 600.14 A1)

PwC agree that the examples listed in paragraph 41 of the consultation document would not generally create a self-review threat.

Question 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 NZ 600.14 A1)

The framework is conceptual and application of the standard involves professional judgement. The additional guidance provides a reminder of the relevant considerations.

Question 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.

An assessment of the threats that might arise from a "perception" is subjective and there is a risk that perceptions are misaligned.

The independence in appearance threat is often referred to by commentators as the basis for challenging the independence of a firm or auditor. However, the broader principles of the conceptual framework, and more particularly the reasonable and informed third party test, are often not reflected when evaluating an appearance threat.

The standards make it clear that independence in appearance must be evaluated with regard to a reasonable and informed third party assessment. A reasonable and informed third party is expected to form a conclusion after weighing all the relevant facts and circumstances. Initial views may be expressed by uninformed third parties which are not helpful in the context of independence and our profession.

Further guidance in this regard may assist third parties to understand the expectation that they weigh all relevant facts and circumstances when evaluating an independence in appearance threat.

(iv) Effective Date

Question 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.

PwC supports consistency with the Global provisions recommended by IESBA.

The IESBA transitional provision provides that, for engagements entered into before 15 December 2022 and for which work has already commenced, the firm or network firm may continue under the extant provisions of the Code until the engagement is completed in accordance with the original engagement terms.

PwC acknowledges the NZAuASB's view that an open-ended transitional provision is broad and their concerns that this could conceivably permit a firm to continue an engagement under the extant provisions for an indefinite period. To address this, the NZAuASB proposes a time limit of 12 months be applied to the transitional provision.

Whilst we acknowledge the concerns of the NZAuASB, we also have concerns that this introduces further complexity and inconsistency for Network firms, particularly in respect of global client relationships. A discreet piece of work that may have Global reach that could not be completed in New Zealand under the proposed NZAuASB transitional provisions would present unnecessary Global challenges for clients and firms.

Further, existing global contracts will have legal and financial consequences that must be considered by the NZAuASB in evaluating any compelling reasons for changing the IESBA transitional provisions.

In circumstances where the prohibition was extended to incorporate tax compliance services (which we do not agree should occur, as discussed above), the proposed transitional timeframe of 12 months may not allow sufficient time for the services to be delivered in line with statutory tax return timeframes (for example a tax return for a client with Dec 2022 balance date would not be due until 31 March 2024. A longer transitional period should be considered, if it is determined that one is required.

Additional Comments - Inconsistencies noted
In completing our submission, we identified instances where the proposed NZAuASB changes create an inconsistency within the PES 1. We have noted these for your further evaluation.

1. As noted in our response to question 3, 604.6 A1 states that providing tax return preparation services does not usually create a threat because of the stated reasons, and is relevant to all audit clients. NZ604.11 A1 states that advising on tax return preparation is a tax advisory service which might create a self review threat, notwithstanding that 604.6 A1 has stated that tax return preparation (not just advising on the preparation) does not usually create an independence threat. NZR604.15 states that tax advisory services are not permitted for PIE audit clients with NZ604.15 A1 explaining that this is because the services create a threat to independence that cannot be eliminated or reduced to an acceptable level. It appears inconsistent and confusing that preparing the tax return at 604.6 A1 does not usually create a threat, but advising on tax return preparation does.
2. NZ604.5 A1 deletes the second bullet point "Advising on the tax return treatment of past transactions". 604.6 A1 states that providing tax return preparation services does not usually create a threat for the stated reasons, including that the services are based on historical information, being past transactions. As noted above, there is an inconsistency in messaging around providing tax return preparation services and advising on tax return preparation.