

Board Meeting Agenda

2 September 2020
9:00 am to 4.45 pm

Teams meeting

Est. Time	Item	Topic	Objective		Page
A: NON-PUBLIC SESSION					
B: PUBLIC SESSION					
10.00 am	3	<u>Technology</u>			
	3.1	Board meeting summary paper	Consider	Paper	
	3.2	Update from IESBA TF Chair	Note	Verbal	
	3.3	Phase 1 Report	Note	Paper	
11.00 am	4	<u>Group audits</u>			
	4.1	Board meeting summary paper	Note	Paper	
	4.2	Draft submission	Approve	Paper	
11:45 am	5	<u>Meet with Greg Schollum</u>			
	5.1	Board meeting summary paper	Note	Paper	
12:30 pm	<i>Lunch</i>				
1:15 pm	6	<u>Part 2 of the Code</u>			
	6.1	Board meeting summary paper	Note	Paper	
	6.2	Submission OAG	Consider	Paper	
	6.3	Final Standard	Approve	Paper	
	6.4	Signing memo	Approve	Paper	
1:45 pm	7	<u>Monitoring Group Report</u>			
	7.1	Board meeting summary paper	Note	Paper	
	7.2	Staff analysis	Consider	Paper	
	7.3	MG Paper: Strengthening the International Audit And Ethics Standard Setting System	Note	Paper	
2:15 pm	8	<u>Compelling reason test [Late Papers]</u>			
	8.1	Board meeting summary paper	Discuss	Late	
	8.2	Marked -Up Principles of Convergence and Harmonisation Policy	Consider	Late	
3.15 pm	<i>Afternoon tea</i>				
3.30 pm	9	<u>Role and Mindset</u>			
	9.1	Board meeting summary paper	Note	Paper	
	9.2	ED vs amended draft of the revised Code	Note	Paper	
3.45 pm	10	<u>Agreed Upon Procedures</u>			
	10.1	Board meeting summary and issues paper	Consider	Paper	
4.15 pm	11	<u>Environmental Scanning</u>			

Est. Time	Item	Topic	Objective		Page
	11.1	International monitoring update	Note	Paper	
	11.2	Domestic monitoring update	Note	Paper	
	11.3	Academic update: Professional scepticism	Note	Paper	
C: NON-PUBLIC SESSION					

Next meeting: 21 October 2020

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	3.1
Meeting date:	2 September 2020
Subject:	IESBA Technology project
Date:	20 August 2020
Prepared by:	Misha Pieters

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Agenda Item Objectives

To:

- RECEIVE an update from the IESBA Technology Task Force Chair, Brian Friedrich, on the IESBA's technology project.
- PROVIDE feedback to the Task Force Chair on the preliminary views of the Task Force to inform the development of an exposure draft.

Background

1. The objective of this project is to enhance the Code's provisions in response to the transformative effects of major trends and developments in technology in order to maintain the Code's robustness and relevance as a cornerstone of public trust in the global accountancy profession.
2. The IESBA committed in its [Strategy and Work Plan, 2019-2023](#) to a major strategic initiative on Technology. Through this initiative, the IESBA aims to gather an understanding of the transformative effects of trends and developments in technology on the assurance, accounting and finance functions, and explore their ethical implications for the [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) (the Code).
3. In December 2018, the IESBA established a Working Group¹ with a mandate to:
 - (a) Identify potential ethical implications of technology developments on the robustness and relevance of the fundamental principles and independence standards, in terms of both challenges to Professional Accountants' (PAs) compliance with requirements

¹ In view of the interoperability of the Code with the standards of the International Auditing and Assurance Standards Board (IAASB) and the strategic priority given by both Boards to addressing the developments in technology, the IESBA agreed to coordinate its work in this area with the IAASB. As a result, the IESBA's Technology Task Force is linked to the IAASB's Technology Working Group through the participation of a correspondent member from each Board on the other Board's Task Force/Working Group.

under the Code and ways in which technologies could be used to support and enhance compliance;

- (b) Develop proposed responses to address any identified ethical implications, whether through revisions to the Code or through developing non-authoritative material; and
 - (c) Identify specific outreach and partnership opportunities to share knowledge and to promote the Code as an effective tool for PAs to refer to in addressing ethics issues related to the use and effects of technology on their professional activities.
4. In pursuing its objectives, the IESBA took a phased approach to the technology initiative. Phase 1 focused on the two areas of (a) artificial intelligence (AI) and robotic process automation (RPA), and (b) Big data and data analytics. This focus reflected the fact that these technological developments are currently the most pervasive and affect the broadest population of PAs.
 5. Following fact finding, including a substantial program of outreach to stakeholders, the Working Group delivered its report of findings and recommendations to the IESBA in December 2019 ([Phase 1 Final Report](#)). At the March 2020 meeting, the IESBA approved a [project proposal](#) to develop enhancements to the Code based on the findings and recommendations in the Phase 1 Final Report and established the Technology Task Force.
 6. The Task Force has commenced its work to pursue the seven recommendations for enhancements to the Code as set out in the approved project proposal.

Matters to consider

7. During the meeting, Brian will provide a brief summary of the Phase 1 Final Report and an update on the preliminary views of the Task Force on each of the recommendations (time permitting). Board members are encouraged to read the Phase 1 Final Report, included in agenda item 3.3, ahead of the presentation (and/or listen to a recording of the [webinar](#) presentation from March).
8. This project covers all PAs (i.e., is scoped broader than an assurance context). We expect that the NZAuASB will be especially interested in Recommendation 7 related to Independence, Recommendation 2 related to Complexity and Recommendation 3 on Transparency.

Next steps

9. During the 4th quarter of 2020, the Task Force intends to focus its time on outreach with key stakeholders, including regulators, firms, national standard setters, and others, to receive additional directional input on the options identified and some of the preliminary drafting.
10. The project plan anticipates the approval of an exposure draft at the June 2021 IESBA meeting.

Material Presented

Agenda item 3.1	Board Meeting Summary Paper
Agenda item 3.2	Presentation from IESBA Technology Task Force Chair
Agenda item 3.3	Phase 1 Report

IESBA Technology Initiative



Final Report | December 2019

IESBA

Technology Initiative, Phase 1

Final Report

December 2019

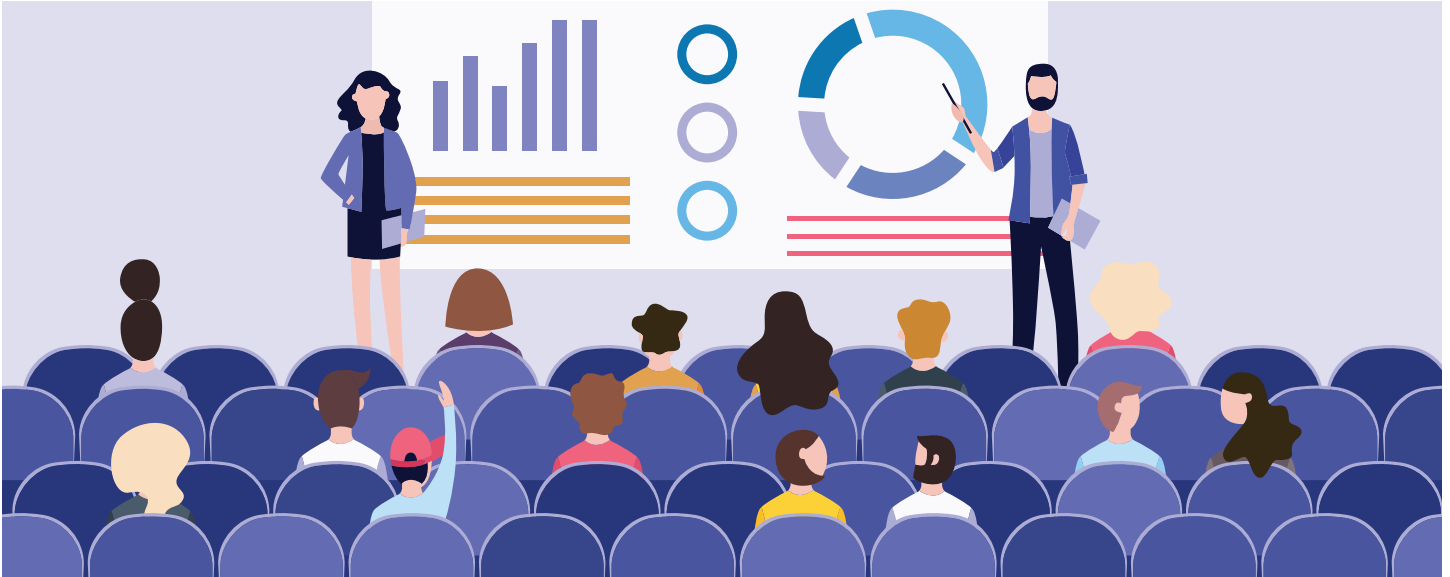
The IESBA Technology Working Group:
Trish Mulvaney, IESBA Member (Chair)
Greg Driscoll, IESBA Technical Advisor
Brian Friedrich, IESBA Member
Hironori Fukukawa, IESBA Member
Myriam Madden, IESBA Member

The Working Group would like to acknowledge the contributions made throughout the year by Laura Friedrich, Ellen Goria, and Robert Juenemann. Additionally, the Working Group wishes to recognize the invaluable staff support provided by Geoffrey Kwan, Principal, IESBA.

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I. Executive Summary



In accordance with its [Terms of Reference \(ToR\)](#), the Technology Working Group (TWG) conducted information gathering and analysis of the impact of trends and developments in technology on the ethical behavior of professional accountants (PAs) as part of Phase 1 of IESBA's technology initiative.

Under this phase, the TWG focused its information gathering on artificial intelligence (AI) and the related areas of big data and data analytics. In addition to desk research, the TWG also conducted in-person meetings with diverse stakeholder groups including firms, professional accountancy organizations, regulators, national standard setters, academics and ethics organizations. The TWG analyzed the sufficiency of the IESBA's [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) (the Code) in addressing the technology-related ethics issues identified, and evaluated whether the IESBA should consider further revisions to the Code to address these issues. As part of its analysis, the TWG compared the principles embodied in a number

of AI ethics frameworks published by some governments, transnational organizations and corporations to the fundamental principles in the Code. It then considered the impact of any differences on the sufficiency of the requirements and application material included in the Code. Additionally, the TWG sought views from the IESBA, IESBA Consultative Advisory Group (CAG) and the International Auditing and Assurance Standards Board's (IAASB's) Technology Working Group, among others, prior to presenting its findings and recommendations in this report.

The TWG's analysis concluded that, generally, the Code currently provides high level, principles-based guidance for most technology-related ethics issues that PAs and firms might encounter. However, Section II of this report cites various ***Findings and Recommendations for Enhancements to the Code***, grouped into five key topical areas where consideration should be given by the IESBA to enhancing material currently set out in the Code. In summary, the TWG's recommendations include:

TWG's Findings and Recommendations for Enhancements to the Code by Topic Area

Building Trust – The Critical Role of Ethics and Professional Judgment

#1

Add new application material in Part 1 of the Code (*Complying with the Code, Fundamental Principles and Conceptual Framework*) to more clearly highlight a broader societal role for PAs in promoting ethical behavior as a critical, consistent foundation for businesses, firms and other organizations, particularly when developing and using technology.

Complexity of the Professional Environment

#2

Revise the Code to more effectively deal with the threats created by the complexity of the professional environment in which PAs perform their professional activities, giving consideration to options such as those described in the Complexities of the Professional Environment subsection.

Suitability of the Fundamental Principles for the Digital Age

#3

Revise Subsection 113 (*Professional Competence and Due Care*) by expanding a PA's responsibility to be transparent, which is not currently expressly stated in the Code. Circumstances that impact the extent of transparency that may be appropriate (e.g., in an audit, the type and timing of audit procedures, and in business, proprietary commercial information) would need to be considered.

#4

Strengthen the concept of accountability in the Code by:

- Including new material in Subsection 111 (*Integrity*) on a PA's willingness to accept responsibility. This would need to take into account whether this aspect of accountability is already covered sufficiently in the proposed new material in Subsection 111 under the IESBA's Role and Mindset Expected of Professional Accountants project (Role and Mindset project).
- More clearly explaining the concept of accountability in Subsection 113 in light of the increasing use of external experts and intelligent agents.
- Including appropriate references to technology in the provisions relating to relying on the work of others in Section 220 (*Preparation and Presentation of Information*). Further consideration should also be given to how best to progress these changes in light of the IESBA's Role and Mindset project.

#5

Revise Subsection 114 (*Confidentiality*) in light of the increased availability and use of personal and other sensitive data to give appropriate consideration to privacy-related matters and the need to actively protect information.

Enabling Competencies and Skills

#6

Add new application material to Subsection 113 to highlight the importance of professional or “soft” skills and provide examples of the emergent technical skills needed in the digital age.

Auditor Independence

#7

With a view to strengthening the provisions in Part 4A of the Code (*Independence for Audit and Review Engagements*) relating to auditor independence:

- Consider whether Section 520 (*Business Relationships*) or other provisions in Part 4A should be revised to address the threats to independence created by the sale or licensing of technology applications to audit clients and the use of an audit client’s technology tool in the delivery of non-assurance services (NAS) to another entity.
- Revise Section 600 (*Provision of Non-assurance Services to an Audit Client*), particularly Subsection 606 (*Information Technology Systems Services*), with respect to the provision of technology-related NAS, taking into account the proposals under the IESBA’s NAS project to be released for exposure in Q1 2020.
- In relation to the concept of an “office,” consider whether Section 510 (*Financial Interests*) should be revised to better capture the threats to independence created by the use of modern communication technologies by firms. Such technologies potentially challenge the notion of an engagement partner’s physical office location being a determining factor in whether that engagement partner or the audit engagement can be unduly influenced by another partner in that same office.

The TWG recommends that the IESBA establish a project and related Task Force as part of Phase 2 of the Technology initiative to action the above recommendations, which largely aim to modernize the Code and enhance the contextual relevance of some of its sections, and thereby support the Code’s effective application in an evolving digital age.

The TWG has also developed **Recommendations for Non-authoritative Guidance Material** related to several of the topical areas of findings noted above. These recommendations are set out in Section III of this report.

Additionally, the TWG’s **Recommendations for Phase 2 of the Technology Initiative** are included in Section IV of this report.

II. Background



The IESBA recognizes the transformational impact digital technologies – such as artificial intelligence (AI), data analytics, robotic process automation, blockchain and cloud computing – have on organizations, governments, economies and societies. These technologies are also impacting the accountancy profession with respect to the types of professional activities undertaken, as well as the tools and approaches used by PAs when undertaking professional activities.

In recognition of the pace and magnitude of change caused by disruptive technological innovations, the IESBA established a working group in 2018 to gain an understanding of the transformative effects of these technological trends and developments on the assurance, accounting and finance functions, and explore their ethical implications.

Following approval of its ToR, the IESBA Technology Working Group (TWG) commenced its information gathering activities in January 2019 as part of Phase 1 of the initiative. Given the IESBA's remit, the focus of the TWG is on the ethical behavior of both PAs working in accounting firms (professional accountants in public practice (PAPPs)) and those working in businesses, the public sector or other sectors (professional accountants in business (PAIBs)).

During this first phase, the TWG gathered information relating to (i) AI and (ii) big data and data analytics. The IESBA agreed to focus on these technologies in Phase 1 based on its view that the impacts of these technological developments are currently the most pervasive and affect the broadest population of PAs. These areas also appear to have a more direct impact on a greater number of the Fundamental Principles (FPs).¹

1. The five fundamental principles in the Code are integrity, objectivity, professional competence and due care, confidentiality, and professional behavior.

In addition to conducting desk research, the TWG also engaged with a broad range of stakeholder groups, particularly in Europe and North America, to hear views, share knowledge and identify issues. To date, the TWG has met with representatives from IFAC member bodies, firms, business groups, accounting software vendors, regulators and academics. See Appendix for a list of the stakeholders and outreach events conducted by the TWG in 2019.

To reach its findings and recommendations below, the TWG also sought views and feedback from the IESBA, the IESBA CAG, the IAASB's Technology Working Group (formerly Data Analytics Working Group), representatives of the former International Accounting Education Standards Board (IAESB)² as well as various IFAC committees. In particular, the IESBA and the IESBA CAG provided their input to the TWG's Phase 1 preliminary report in September 2019.

The Continuum of Artificial Intelligence Systems

The TWG notes the importance of recognizing that the development and use of AI systems by PAs and others vary along a continuum of different types of machine intelligence depending on the level of decision making retained by humans. This continuum ranges from assisted intelligence or robotic process automation where machines mimic the tasks already done by humans who continue to make decisions; to *augmented* intelligence where there is machine-human collaboration in the decision-making, allowing humans to do more than they are currently capable of; to *autonomous* intelligence at the other end of the continuum where machines fully accomplish tasks and make decisions on their own without any human interventions.³



The TWG observed that the technologies being discussed by stakeholders today are more in the realms of assisted and augmented intelligence and that any widespread adoption of autonomous intelligence is unlikely to take place in the short to medium term. As such, the TWG's assessment of the impact of technology on the ethical behavior of PAs is focused on these first two types of machine intelligence. The TWG is of the view that the impact of autonomous intelligence on PAs may be difficult to predict and, therefore, any recommendations to the Board based on such predictions may lack sufficient evidence at this time. Active monitoring of this area is, however, important given the rapid pace and dynamic nature of technological change.

2. On August 3, 2018, the International Federation of Accountants (IFAC) announced that it was transitioning the IAESB to a new model based on a comprehensive and integrated approach to international accountancy education. In this document, reference to the IAESB includes its successor body.
3. <https://preview.thenewsmarket.com/Previews/PWC/DocumentAssets/476830.pdf>

II. Findings and Recommendations for Enhancements to The Code



Building Trust: The Critical Role of Ethics and Professional Judgment in the Digital Age

Trust and ethics have long been associated with the accountancy profession and are also foundational elements of sustainable societies, economies, organizations and personal relationships. Many stakeholders and others have observed that trust is becoming an increasingly important currency in the digital age. Recent cases of the misuse of personal data by organizations serve as examples of the importance that trust plays and highlight the need to strengthen policies and ethical behavior around the use and protection of data.

Alongside the transformational and far reaching benefits of modern technologies for organizations, governments and societies are ethics issues and dilemmas, such as undue influence, biased decisions and unfair treatment, breach of privacy and threats to public health and safety. The speed

at which technology works and its pervasiveness suggest there needs to be appropriate attention to ethical values when both developing and applying technology. Potential negative ramifications of the impact of technology, if not properly addressed early on, can result in a loss of confidence in organizations, governments and institutions and the community at large. Consequently, ethics are rising to center stage in the discussions of technology disruptions.

Broader Role to Promote Ethical Behavior

The Code currently recognizes a PA's role in promoting an ethics-based culture in the PA's organization. As trust and ethics gain a higher profile in conversations about technology and its impact, various professional accountancy bodies have recognized the opportunity to step up and promote the profession and its members' ability to create and maintain trust. Along these same lines, the TWG believes there is an opportunity for the Code to more expressly reference a broader societal role for PAs in

promoting ethical behavior beyond their current role of contributing to building public trust in the organizations and professional activities they are directly associated with.

Such a broader role for PAs in society as champions of the importance of ethics in developing and applying technology might encompass, amongst other things, promoting an ethical culture across organizations and among business partners and third parties, influencing others to act ethically as well as holding oneself and others accountable for upholding ethical principles.

In having a responsibility to act in the public interest, PAs have historically had a strong appreciation of the importance of public trust and in third parties having confidence in and ascribing value to their work. They also understand that adhering to a code of high ethics standards helps maintain that trust. Currently, Section 200 (*Applying the Conceptual Framework – Professional Accountants in Business*) of the Code contains application material about the expectation of PAIBs to encourage and promote an ethics-based culture in their organizations, taking into account their position and seniority within those organizations.

The TWG notes that in the Exposure Draft, Proposed Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants (Role and Mindset ED), the IESBA has proposed changes to recognize the wide-ranging impact PAs have in society as a result of the skills and values they bring to their work, the centrality of ethical behavior when undertaking professional activities and the role of a PA in championing ethical behavior in their organizations. Additionally, the ED proposes revisions to the description of professional behavior to specifically require a PA to behave in a manner that is consistent with the profession's responsibility to act in the public interest. The proposed ED also contains new material in Section 120 (*The Conceptual Framework*) that emphasizes the importance of an organizational culture that promotes ethical behavior in the context of PAs applying the conceptual framework.

As current provisions in the Code and in the proposed Role and Mindset ED primarily refer to the PA's role in the organization in which the PA carries out professional activities, the TWG is of the view that further consideration should be given by the IESBA to including new application material in Part 1 of the Code to more clearly highlight a broader societal role for PAs in promoting ethical behavior as a critical, consistent foundation for businesses and other institutions when developing and using technology. The TWG also considers that non-authoritative material on this subject would be helpful to inform and inspire PAs to act as active champions of ethical behavior in the dynamic, technology-enabled workplace irrespective of the timing or type of technological disruption.

Recommendation 1

The TWG recommends that the IESBA consider adding new application material in Part 1 of the Code to more clearly highlight a broader societal role for PAs in promoting ethical behavior as a critical, consistent foundation for businesses, firms and other organizations, particularly when developing and using technology.

Importance of Professional Judgment

Stakeholders have consistently cited the importance of professional judgment as business and society adapt and evolve in a world of dynamic change brought about by ongoing digital transformation.

New developments in AI such as deep machine learning, coupled with the availability of big data, will lead to intelligent agents that can take on ever more complex analysis and prediction. This rise of machine analysis and prediction will also generate more demand for decision-making, giving rise to enhanced opportunities to exercise human judgment.

Additionally, some have suggested that whilst AI can improve prediction, it is not always able to judge which outcomes are better or best serve the public interest. Such decisions require considering factors such as hidden costs, social trade-offs, intangible rewards, or risks that machines are currently incapable of effectively evaluating. Consequently, human judgment continues to play an important role in decision-making.

As technology such as deep learning continues to evolve, the value of machine prediction will also increase as machines are able to take into consideration more factors and become more accurate, quicker, and more cost effective. In this regard, the TWG notes the concept of intelligent augmentation as a different way to conceptualize the role of AI whereby humans remain at the center of the decision-making process and AI enhances human intelligence rather than replacing it. Aligned with the concept of AI, some have suggested that as the value of machine prediction increases, the value of, and need for, human judgment will also increase. The considerable benefit of combining machine prediction and professional judgment is an ability to make better decisions faster, based on more comprehensive and more accurate information.

As the accountancy profession evolves in the digital age and sets its path for the future, it seems clear that PAs' professional judgment will continue to play a significant role.

The revised and restructured Code includes new application material that provides additional guidance to the requirement for PAs to exercise professional judgment in paragraph R120.5. Such application material (paragraphs 120.5 A1 to 120.5 A3 of the Code) describes, amongst other matters, the important role professional judgment plays when PAs are applying the conceptual framework.

The TWG agrees with the observation that with the availability of machine-generated information comes a risk of over-reliance on AI or other forms of technology due

to a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to whether such output is reliable or fit for purpose. Such tendency (referred to as "automation bias") may impair a PA's exercise of professional judgment. In recognition of this risk, the IESBA agreed to include automation bias in the proposed list of examples of bias in the Role and Mindset ED.

As part of its deliberations on the Role and Mindset proposals, the IESBA agreed that the Code already recognizes the importance of professional judgment to a PA's application of the conceptual framework and that no further changes to the material on professional judgment is needed.

Based on its work in Phase 1, the TWG does not propose any further revisions to the Code regarding the importance of professional judgment. However, the TWG is of the view that it would be helpful for non-authoritative guidance material to be developed that highlights the importance of a PA's professional judgment when carrying out professional activities in a dynamic, technology-enabled environment.

Complexities of the Professional Environment

PAs today find themselves working in a complex operational, legal and regulatory environment, brought on by, amongst other factors, the impact of new technologies. New technology applications, such as those combining the use of AI and big data, can produce information and perform certain tasks more efficiently and accurately than human agents. However, in order to rely on the outputs of these technology applications, PAs need to attain sufficient knowledge of the design and application of the technology involved, which can often be a complex, time-consuming and arduous task. In addition to complexities of technology, the PA must also have appropriate knowledge of and adhere to an expanding array of regulatory

requirements and professional standards, for example, the myriad of differing tax schemes available across multiple jurisdictions with differing laws and regulations that need to be considered when providing tax planning advice to clients. These factors – which often occur concurrently – also impact employing organizations and client business operations, adding another layer of complexity to the professional activities of PAs.

The Code states: “Threats to compliance with the FPs fall into one or more of the following categories:”. It then sets out the definitions of self-interest, self-review, advocacy, familiarity and intimidation threats. The TWG considered at length whether these five categories of threats as defined are sufficient for applying the conceptual framework to identify, evaluate and address the ethics risks arising from the complex professional environment in which PAs operate. This consideration resulted from the TWG’s discussion of a potential gap in the Code related to threats to the FP of professional competence and due care caused by complexity associated with new technologies.



To better capture the threats caused by complex professional environments, the TWG considered a number of options and approaches to amend the Code (which are not mutually exclusive):

- Add a new category of threat (e.g., “complexity”, “self-confidence” or “pace of change” threat) in paragraph 120.6 A3, taking into account the potential

flow-on impact of adding a new category of threat to the rest of Code. Upon further consideration, the TWG came to the view that adding a new category of threat might not be necessary as complexity could be captured by two of the existing categories of threat:

- Self-interest threat in the sense that a PA does not invest or prioritize the time, money and other resources needed to develop competence in new technologies or new compliance rules. The TWG is of the view that such a threat exists despite the benefit and self-interest of improving one’s competence and knowledge of technology and the associated risk of becoming obsolete otherwise. It may be argued that the current description of self-interest threat in paragraph 120.6 A3 (a) already covers this type of threat.
- Intimidation threat in the sense that a PA is deterred from acting properly because the PA feels intimidated by the complexity of certain technology applications or compliance rules. The TWG is of the view that this variation of the threat is not currently covered in the existing description of intimidation threat in paragraph 120.6 A3 (e) and that expansion would be helpful.

- Highlight “complexity” under Section 120, in a manner similar to the approach taken by the IESBA in adding application material on bias and organizational culture in the Role and Mindset ED.
- Modify the lead-in language to paragraph 120.6 A3 of the Code so it would read less definitively (i.e., currently the language could be interpreted as meaning if a circumstance or a situation does not fall into one of the categories listed then there is no threat to evaluate).
 - In this regard, the TWG notes in particular the American Institute of Certified Public Accountants (AICPA) Code of Professional Conduct which states [emphasis added] “...**many** threats fall into one or more of the following seven broad categories: adverse interest, advocacy, familiarity, management participation, self-interest, self-review, and undue influence...”

- Furthermore, the TWG noted that the lead-in sentence to the five categories of threats in paragraph 200.3 of the Code released in March 2008 also states [emphasis added] "...**Many** threats fall into the following categories...".
- The TWG is of the view that the Board should consider such a construct as it allows for some flexibility in how PAs can identify and address a threat such as complexity without necessarily "shoehorning" it into one of the five categories currently stated in the Code. Such fluidity is particularly useful in light of the constantly evolving professional environment in the digital age. The TWG believes that allowing for the possibility that some threats may fall outside the five existing categories of threats should not weaken the construct of the conceptual framework or the building block approach of the Code.
- In the Code, Section 200 and Section 300 (*Applying the Conceptual Framework – Professional Accountants in Public Practice*) provide examples of threats as well as the work and operating environments of employing organizations and firms and the operating environment of clients that might impact the evaluation of the level of a threat. The TWG is of the view that it might be helpful to include references to, or examples of, technology and the complexity of work environments in these provisions.
- The TWG is also of the view that PAs will increasingly work with multidisciplinary teams, subject matter experts, remote teams and/or intelligent agents both internal and external to the organization when performing professional activities. In this regard, the TWG is of the view that the Board should consider reviewing the Code to expand references to individuals in the Code to include machines and intelligent agents as appropriate. For instance, it may be argued that the description of self-review threat in paragraph 120.6 A3 should be updated to include not only activity

performed by individuals but also by an intelligent agent that was developed and is owned by the PA's firm or employing organization.

In addition to considering the items noted above that might affect the Code, the TWG believes that it would be helpful to develop non-authoritative guidance material to discuss the ethical implications of complex professional environments linked to the impact of technology.

Recommendation 2

The TWG recommends that the IESBA consider revising the Code to more effectively deal with the threats created by the complexity of the professional environment in which PAs perform their professional activities, giving consideration to options such as those described in the Complexities of the Professional Environment subsection.

Suitability of the Fundamental Principles for the Digital Age

Inter-related Nature of the Impact of Technology

While the individual FPs are defined broadly and in a way that generally addresses technology-related risks, the TWG believes that the impact of new technology developments cuts across all five FPs in an interrelated manner. As a result, missing or not fully understanding the threat to complying with one FP resulting from the impact of technology might also lead to non-compliance with another FP. This combined or pervasive effect, along with the fast pace of work that technology enables, suggests that it is especially important for a PA to consider the inter-related nature of the impact of technology on compliance with the FPs.

The proper consideration of the potential impact of machine bias associated with the use of AI provides an example of this pervasive, inter-related impact. Whilst traditional robotic process automation focuses on repetitive, rule-based and high-volume activities (process driven), AI technology such as machine learning simulates human intelligence and is often able to make accurate predictions through the analysis of large volumes of data (data driven). However, the accuracy of AI predictions might be affected by bias that could be either present in the datasets consumed by the AI system, or in the algorithms that reflect biases of the human AI system's developers and coders, and/or in the interpretation of the system's outputs. Consequently, a PA needs to think concurrently and holistically about compliance with the FPs in a technology-enabled organizational environment:

- *Objectivity* could be impaired when undue reliance is placed on AI system outputs, especially when such outputs have been generated from biased data or information that might compromise a PA's professional judgment.
- In order to avoid undue reliance, the PA must have the appropriate *professional competence and due care* to sufficiently understand and evaluate the business and technical aspects of how AI system outputs were generated. Whilst a PA is not expected to have the same level of knowledge and skills as a data scientist, it is important that the accountant is capable of asking appropriate questions to ensure that high quality data are being used.
- If the PA knew or should have known that the AI system's outputs were not objective, then this implies a lack of fair dealing or truthfulness, namely *integrity*.
- Furthermore, since AI systems are fueled by consuming large amounts and different types of data, privacy considerations arise and can heighten the level of threat to complying with the FP of *confidentiality*.
- Lastly, the consequences of one or more such lapses in compliance with these FPs may also discredit the

profession under the FP of *professional behavior*, particularly in light of the increasing public expectations for trust in the digital age.

The TWG does not believe further enhancement to the Code to highlight the pervasive and inter-connected nature of the impact of technology is necessary. Instead, the TWG is of the view that non-authoritative material on the overall impact of technology in terms of the FPs, including the example of machine bias, would be helpful to stakeholders.

Key Principles in AI Ethics Frameworks

In recognizing trustworthiness as a key factor to the acceptance of AI, many governments, transnational organizations and corporations have been proactively proposing and implementing ethics frameworks for the development and application of AI. Such organizations are also committed to developing AI ethics frameworks in order to maximize the potential of AI in bringing positive transformations to society and to minimize the risk of significant societal damage.

Given the importance of trust to the brand and the expectations the public has of PAs, the TWG compared the ethics principles embodied in a number of published AI ethics frameworks to the descriptions of the FPs and related application material in the Code.

In reviewing various AI ethics frameworks and the ethics principles embodied in them, the TWG observed that the concepts of fairness, transparency, explainability, accountability and privacy/confidentiality are consistently included. As a result, the TWG considered whether, and if so how, these concepts are covered in the Code and whether there might be a need or benefit to more explicitly relate these ethics principles to the FPs. A summary of the TWG's deliberations and related recommendations are set out below.

Common Principles Used for AI Ethics Frameworks

Microsoft

- Fairness
- Transparency
- Inclusiveness
- Reliability
- Safety
- Privacy and Security
- Accountability
- Accountability

IBM

- Value alignment
- Explainability
- Fairness
- User Data Rights

European Commission

- Respect for human autonomy
- Prevention of harm
- Fairness and Explicability

OECD

- Inclusive growth
- Sustainable development and Well-being
- Human-centred values and Fairness
- Transparency & Explainability
- Robustness
- Security and safety
- Accountability

Australian Gov't Consultation Paper

- Do not Harm
- Regulatory and Legal Compliance
- Privacy Protection
- Fairness
- Transparency and Explainability
- Contestability
- Accountability
- Generates net benefit

Fairness

The TWG is of the view that there is a public expectation for a PA to act fairly when undertaking professional activities. The TWG considers that the application of the concept of fairness has the following ethical implications for a PA:

- A PA must be impartial and not be biased against any individuals or organizations in the PA's decisions or actions, including presentation of information. In this regard, the PA must not cherry-pick datasets. (FP: Objectivity)
- A PA must include all relevant known information when making decisions and have the necessary competence to identify and understand the information required to make such decisions. (Professional Judgment and FP: Professional Competence and Due Care)
- To act unfairly might also impact the good reputation of the profession. (FP: Professional Behavior)

Currently in the Code, the FP of integrity alludes to the concept of fairness by requiring a PA to be straightforward

and honest as well as explaining that the principle implies fair dealing and truthfulness. However, some may perceive there is no requirement for a PA to act fairly. In addition, there is no guidance on what that concept means in the context of undertaking professional activities.

Upon deliberation, the TWG is of the view that further enhancement to the Code to include the concept of fairness is not necessary for the following key reasons:

- It may be argued that compliance with the FPs and proper application of the conceptual framework already provide the necessary assurance that a PA will act fairly.
- The proposed revisions to the Code in the Role and Mindset ED, such as the inclusion of "having an inquiring mind" and guidance material on bias under Section 120, will further reduce the risk of a PA acting unfairly.
- The TWG also recognized that the term "fairness" is a value-laden concept which might make it difficult to develop a global view on how the concept should be applied.

Transparency

Digital transformation in business and society has resulted in a greater call for, and public expectation that, businesses and organizations will be transparent in their dealings with customers and other stakeholders. With large amounts of individuals' private data being collected and used by businesses, governments and other organizations, there is greater public expectation and demand on these entities to demonstrate that individual privacy is being respected. Shareholders are also increasingly asking companies to demonstrate their commitment to corporate social responsibilities in addition to delivering bottom-line profit. As such, companies are expected to be more transparent about their strategies and performance in addressing these broader social and environmental considerations. In order to build trust, organizations must find ways to become more transparent to their stakeholders.

The Code currently contains several provisions that promote transparency without using the term specifically. Examples include requiring PAs and firms to disclose certain information to relevant parties in certain circumstances described in Subsection 114 for the FP of confidentiality. Under the FP of professional competence and due care, a PA is required to make certain parties such as clients and employing organizations aware of the limitations inherent in the PA's services or activities (see paragraph R113.3). Additionally, disclosure of the nature of a conflict of interest in Sections 210 (*Conflicts of Interest*) for PAIBs and 310 (*Conflicts of Interest*) for PAPPs, as well as disclosure of fee-related information to those charged with governance of an audit client in Section 410 (*Fees*), are additional examples of "transparent" actions to be taken by a PA under the provisions of the Code.

Given the importance of trust and transparency in the digital age, the TWG is of the view that more express language on a PA's responsibility to be transparent in their professional activities may be necessary in the Code. In this regard, the TWG notes that both the IESBA's NAS and Fees projects have referenced the importance of transparency

from an independence perspective. As a result, these projects have developed proposals that firms disclose information relating to the provision of NAS and fees charged to audit clients to those charged with governance and to the public.

Consistent with the concept of transparency underpinning these NAS and Fees proposals, the TWG has formed the view that in times of technological or other types of change and uncertainty, a PA has an overarching *responsibility* to be transparent, as appropriate considering the circumstances, when carrying out professional activities, and this responsibility should be more prominently featured in the Code. In determining the circumstances and level of appropriate transparency, a PA needs to exercise professional judgment. Furthermore, transparency serves to support compliance with the fundamental principles. Transparency concerning how decisions are reached, the processes applied, how the information the PA relied on has been derived, and for auditors, how AI is used in audit work are examples of where potential impacts of technology on the ethical behavior of PAs can be addressed by transparency.

Based on these considerations, the TWG recommends that the IESBA consider adding new application material in Subsection 113 to explain a PA's *responsibility* to be transparent which is not currently expressly stated in the Code. In doing so, the IESBA would need to be mindful of circumstances that impact the extent of transparency that may be appropriate (e.g., in an audit, the type and timing of audit procedures, and in business, proprietary commercial information).

The TWG also considered that the concept of transparency ties in with professional judgment as they both are important elements of the decision-making process. A PA should be able to demonstrate how professional judgment has been exercised and the robustness of a decision. The TWG believes that it would be helpful that the relationship between transparency and professional judgment be highlighted as part of non-authoritative material.

Recommendation 3

The TWG recommends that the IESBA consider revising Subsection 113 by expanding a PA's *responsibility* to be transparent which is not currently expressly stated in the Code. Circumstances that impact the extent of transparency that may be appropriate (e.g., in an audit, the type and timing of audit procedures, and in business, proprietary commercial information) would need to be considered.

Explainability

The TWG is of the view that a PA should have the requisite knowledge and skills to explain how they derive a decision or the decision-making process in such a way as to establish trust in the robustness of that decision. As machine algorithms become more sophisticated over time and begin to operate like a "black box", it is important that PAs find ways to explain their decisions without the need to dissect the algorithms.

The TWG notes that the FP of professional competence and due care in Subsection 113 requires a PA to attain and maintain the necessary professional knowledge and skills, which includes having a continuing awareness and understanding of relevant technical, professional and business developments. The TWG is of the view that the material in Subsection 113 sufficiently covers the need for PAs to have the requisite knowledge and skills to explain their decisions and that revisions are not necessary.

Accountability

The TWG believes there is a public expectation and, therefore, it is in the public interest for a PA to be accountable for the decisions, actions or outcomes for which the PA has due responsibility. Accountability goes beyond just having someone to blame when things do

not go as planned, and sanctions when someone is found at fault. As highlighted in a recent report by the Institute of Chartered Accountants in England and Wales (ICAEW) titled New technologies, ethics and accountability, the right accountability framework serves as a driver to acting appropriately in the moment to avoid shame and embarrassment at a later date.

As the discharging of professional activities becomes more complex and services become more integrated, both PAPPs and PAIBs are becoming more reliant on the work of subject matter experts as well as the outputs from technologies such as AI systems. Whilst an intelligent agent does not at this point have any legal, ethical or moral responsibility, reliance on the work produced by such an agent is in many ways no different than reliance on the work of a human agent such as a junior staff member or a subject matter expert.

In considering the appropriate accountability of PAs when operating in a technology-enabled professional environment, the TWG has formed the view that PAs must (i) be willing to be held accountable for their work – regardless of whether other human or intelligent agents contribute to their conclusions and decision-making processes, and (ii) take the necessary steps to ensure that they properly discharge their duties. In reaching its view, the TWG also acknowledges that in today's complex work environment whereby PAs are relying more and more on decisions by machines, responsibility might need to be shared with other human agents that have some causal connection with the decision such as the technology developers.

With regards to having a willingness to be held accountable, the TWG considers that this concept aligns best to the FP of integrity in Subsection 111 as this principle requires a PA to be straightforward and honest. In this regard, the TWG has also taken into consideration the proposed new material in the Role and Mindset ED on having the determination to act appropriately when confronting dilemmas or difficult situations. The TWG is of

the view the whilst the willingness to accept responsibility may be broadly covered in the proposed new material in the ED, there is room for potential enhancement to the Code to strengthen this aspect of accountability in the Code.

The FP of professional competence and due care set out in Subsection 113 of the Code includes the requirement that a PA take the necessary steps to fulfil the PA's responsibilities (see paragraphs 113.1 A3 to R113.3). The TWG is of the view that these paragraphs might be further strengthened in order to more clearly explain the concept of accountability in light of the increasing use of external experts and intelligent agents.

The TWG has also reviewed the material relating to relying on the work of others in paragraphs R220.7 to 220.7 A1 of the Code as well as the proposed revisions to paragraph R220.7 in the Role and Mindset ED. The TWG noted that in approving the proposed revisions to paragraph R220.7, the IESBA agreed to remove a proposed reference to reliance on technology suggested by the Role and Mindset Task Force on the grounds that the TWG is better placed to consider the inclusion of any such references in these two paragraphs. Having reflected upon the matter, the TWG is of the view that the IESBA should consider including material on reliance on technology in paragraphs R220.7 and 220.7 A1 as part of its post-Phase 1 Technology Initiative activities.

The TWG also noted that there is no equivalent section or material on preparing and presenting of information that specifically addresses a PA's reliance on the work of others in Part 3 of the Code. In considering how the applicability provisions in paragraphs 200.4(b) and R300.5 to 300.5 A1 would apply in these situations, the TWG has concluded that any review of the applicability provisions may be best addressed as part of the IESBA's implementation review of the revised and restructured Code in the future.

Recommendation 4

The TWG recommends that the IESBA consider strengthening the concept of accountability in the Code by:

- Including new material in Subsection 111 on a PA's willingness to accept responsibility. This would need to take into account whether this aspect of accountability is already covered sufficiently in the proposed new material in Subsection 111 under the IESBA's Role and Mindset project.
- More clearly explaining the concept of accountability in Subsection 113 in light of the increasing use of external experts and intelligent agents.
- Including appropriate reference to technology in the provisions relating to relying on the work of others in Section 220. Further consideration should also be given to how best to progress these changes in light of the IESBA's Role and Mindset project.

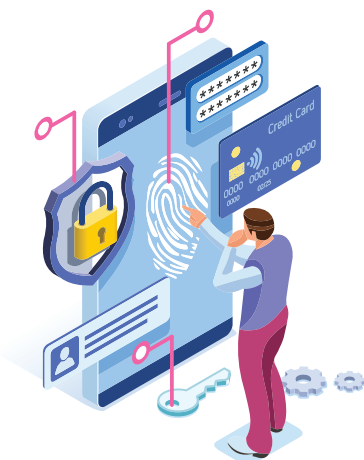
The TWG also recommends that the IESBA consider, as part of its strategic commitment to undertake an implementation review of the revised and restructured Code, the effectiveness of the "applicability provisions" set out in paragraphs 200.4(b) and R300.5 to 300.5 A1 with regards to Section 220.d.

Privacy and Confidentiality

The concept of privacy is closely related to the concept of confidentiality. In the context of information, privacy relates to the legal right of a person protecting, and controlling access to, his or her personal information or data. In contrast, confidentiality refers to how personal information or other information that needs to be kept confidential (such as commercially sensitive information) will be protected from unauthorized access.

The TWG has heard that when considering how privacy should be protected, due consideration must be given to how the ownership of personal information is viewed in different jurisdictions. Some stakeholders have noted that whereas some jurisdictions consider that the ownership of private information rests with individuals, other jurisdictions view private information to be owned by corporations or the State.

In today's "information" economy where data are considered by many as a new form of asset, the sharing and use of large amounts of digital data have become accepted (and somewhat expected) in order to create value for businesses, employees, customers and clients. Technology has also allowed data to proliferate and be transferred more easily and quickly, leading to threats to



data integrity and security. With the flow of large data sets that often include personal and other sensitive information, the protection of confidential information becomes a significant matter for consideration by firms and other organizations that have access to these datasets.

With the growing availability and use of big data, there is also a need for developing and implementing proper data governance and frameworks that, amongst other things, include the appropriate collection, use, and disclosure of personal and sensitive information as well as safeguarding against its abuse. The TWG heard from some stakeholders

that the profession is well placed to be a contributor to the discussion of the need for effective data governance frameworks given its traditional role in handling financial and other sensitive data, and its role in standard setting. These concepts are expressed, for example, in the Chartered Professional Accountants of Canada's (CPA Canada's) report [The Way Forward: Transforming Insights into Action](#). CPA Canada notes that the accounting profession is in a position to leverage its core attributes of trust and integrity and its responsibility to act in the public interest to provide the necessary data governance and the assurance that decisions are being made based on the value that data brings. See also discussion on Section 350 (Custody of Assets) relating to custody of assets in the Data as an Asset subsection below.

In reviewing the material on the FP of confidentiality set out in Subsection 114 of the Code, the TWG has formed the view that the Subsection should be further enhanced. The TWG noted that, amongst other matters, the following may require further consideration by the IESBA:

- Whether the language and terminology should be updated to take into consideration new risks such as the use of social media, the use of cloud storage, and other changes to the concept of confidentiality. When considering how Subsection 114 can be modernized, it might be helpful to also review existing data governance principles and privacy laws.
- Whether the material should be less descriptive and be further summarized into higher level principles to avoid the risk of becoming obsolete.
- Whether Subsection 114 should cover other aspects of data and information stewardship beyond "use" and "disclosure." Other stages of a typical data management life cycle control framework include collection, storage, transmission, processing and destruction.
- Whether terms such as "data," "information" and "confidential information" should be defined.

- Whether there should be a scalability concept included in the Code whereby the actions that need to be taken to protect confidential information depend on the sensitivity of the information (e.g., greater sensitivities related to health, racial, biometric information and religious beliefs).
- In addition to a responsibility to not disclose confidential information, whether there should also be a responsibility to ensure such information is protected from cyberattack or other forms of hacking. The TWG is of the view that any proposals to strengthen the FP of confidentiality should be developed in conjunction with the information gathering on the topic of cybersecurity and cybercrime.
 - Whilst the material is sufficiently broad to include protection of an individual's right to privacy, the TWG considered that it might be appropriate for the Code to expressly include this concept as a reminder to PAs of its importance.
- Whether PAs should be permitted, and potentially encouraged or required, to disclose more information as public expectation for transparency continues to increase in the digital age.

Recommendation 5

The TWG recommends that the IESBA consider revising Subsection 114 in light of the increased availability and use of personal and other sensitive data to give appropriate consideration to privacy-related matters and the need to actively protect information.

Enabling Competencies and Skills

As the capability and capacity of new technological developments continue to grow, more and more existing accounting roles and functions will be replaced by machines and automation whilst opportunities for other roles such as consultancy and advice will open up. This

evolution means that the accountancy profession will need to rethink the competences and skills required of PAs in the future. There seems to be a consistent acknowledgement by stakeholders that PAs need to upskill themselves on understanding how these technologies work and keep this knowledge current in the face of ongoing technological advancements.

The TWG also observed a general view amongst stakeholders that in addition to having the requisite knowledge about various technologies and their application, there will be a greater need for PAs to develop their professional or “soft” skills. Stakeholders have suggested that the pervasive impact of technological breakthroughs is a key driver for how the accountancy profession is changing, which in turn creates a need for new knowledge and skills. In its report Professional Accountants – the Future: Drivers of Change and Future Skills, the Association of Chartered Certified Accountants (ACCA) identified the spread of digital technologies as one of the key driving forces that will have the most impact on PAs and financial professionals, including the skills that are required of them. Technology-related external factors such as the development of intelligent automated accounting systems, adoption of cloud computing and data mining and the use of social media have been identified as key factors that will have the most impact on the profession. In order to adjust to these changes, PAs will need to strengthen their integration of technical skills with professional skills in areas such as emotional intelligence, ethics, communications, agility and leadership.

In its report The Future of Talent: Opportunities Unlimited, Chartered Accountants Australia and New Zealand (CAANZ) observed that the accountancy profession rated its top four very important skills for the future as: problem solving, communication skills, collaboration, and the ability to work with data and the latest technology and systems. This report also suggests that this is a reflection of the increased use of technology and move from lower level processing work, which in turn allow PAs to focus on value-add work such as strategic advice.

The TWG also observed from discussions with stakeholders that having the right mindset is an important component of success for a PA in the digital age. Such a mindset ranges from one that adapts to new technology to expanding the PA's mindset from a compliance-oriented one to an advisory-oriented one. Of note, some have highlighted the importance of a growth mindset given the pace of change in the age of digital transformation. Whilst there are various definitions of "growth mindset," each of them includes similar concepts, such as a belief that abilities and acumen can be developed, and "the capacity to feel comfortable in one's ability to overcome obstacles and challenge one's own identity, and to extend oneself into new areas."¹ These concepts align with an earlier ACCA report, Ethics and Trust in a Digital Age, which highlights the need for continuous learning and the importance of the FP of professional competence and due care in a digital age.

Currently, the FP of professional competence and due care as set out in Subsection 113 of the Code requires PAs to have certain levels of professional knowledge and skill that are based on current technical and professional standards and relevant legislation. Paragraph 113.1 A1 also highlights the importance of exercising sound judgment when applying professional knowledge and skills. Further, paragraph 113.1 A2 notes that maintaining professional competence requires a continuing awareness and understanding of relevant technical, professional and business developments. In this regard, the TWG noted that the Role and Mindset ED has proposed that technology-related developments be added to this paragraph.

In light of the growing importance of professional skills for PAs of the future as a result of the pervasive impact of technology on the profession and businesses, the TWG is of the view that Subsection 113 should provide new application material about the soft skills aspect of professional competence. The TWG has considered the option of referencing the appropriate International Education Standard (IES) issued by the IAESB in Subsection

113. However, the TWG determined that this may not be the most suitable approach given that the IESs are addressed to IFAC member bodies instead of individual PAs. In this regard, the TWG notes that IES 3, Initial Professional Development – Professional Skills (Revised), describes "professional skills" as "(a) intellectual, (b) interpersonal and communication, (c) personal, and (d) organizational skills that a professional accountant integrates with technical competence and professional values, ethics, and attitudes to demonstrate professional competence."

The TWG also considers that non-authoritative material on the subject of professional competence, highlighting the relevant considerations pertaining to technology, would be helpful to stakeholders.

Recommendation 6

The TWG recommends that the IESBA consider adding new application material to Subsection 113 to highlight the importance of professional or "soft" skills and provide examples of the emergent technical skills needed in the digital age.

Auditor Independence

The TWG research confirmed that firms of varying size are investing in the development and use of new technologies related to the performance of audits and the provision of NAS. Additionally, applications developed by firms, for example to improve operational efficiency or control environments, are being sold or licensed to clients or other organizations. Some of these services and applications could result in new threats to independence that require further consideration by the IESBA.

1. ACCA, *Emotional Quotient in a Digital Age*, 2018

The TWG believes it is helpful to consider the impact of technology on auditor independence based on how the technology is used by the auditor and/or provided to a client:

- Is it a tool used by a firm to assist with the performance of an audit?
- Is it a software application developed by the audit firm that is sold or licensed to an audit client?
- Is it a technology-related NAS, such as data analytics or modeling, that is provided to an audit client?

Technology Tools Used in an Audit

With respect to the use of tools by firms exclusively to assist with performing audits, such as audit sampling tools, the TWG is of the view that when firms are using these tools primarily to make audits more efficient and to improve audit quality, such use does not generally raise any new threats to independence. However, the TWG noted that firms need to remain alert for situations where this general evaluation of the level of threat to independence might change. An example of such a situation would be when an audit client observes the firm effectively applying one of its audit applications, such as a proprietary fraud detection tool, and then seeks to purchase or license the tool from the firm for its own use.

Technology Applications Sold to Audit Clients

Some firms are developing technology solutions as commercial products for sale or licensing to third parties, such as blockchain-based business applications. The TWG is of the view that the sale or licensing of these applications to audit clients might create threats to independence that would require evaluation by the firm. In certain circumstances, the TWG believes these transactions might not be considered NAS, and would therefore not be sufficiently addressed by the Code. The TWG believes the sale or licensing of these commercial products might create a business relationship between

the firm and the audit client purchasing the application, and therefore might be addressed through revisions to Section 520 (Business Relationships). This is because this section currently provides guidance only in relation to goods and services purchased from an audit client by a firm, a network firm, an audit team member or any of that member's immediate family. In this regard, the TWG notes that as part of its review, the IESBA might also need to clarify what transactions or relationships constitute business relationships for the purposes of the Code. Any provision of ancillary services relating to the sale of these products such as implementation or ongoing maintenance of the application should be dealt with under Section 600 (Provision of Non-Assurance Services to an Audit Client) and related subsections. The TWG also considered the situation of a firm using an audit client's technology tool in its delivery of a NAS to another entity. The TWG is of the view that in such a situation, further consideration should be given by the IESBA to whether these circumstances create close business relationships to be dealt with under Section 520.

Provision of Technology-related Non-assurance Services

The growing market demand for technology-related services and interest of firms in providing such services to their clients have created a heightened awareness of potential independence issues among regulators and other stakeholders.

Although the scope of the project initially undertaken by the NAS Task Force was to review all of Section 600 and related subsections of the Code, the Board agreed at the September 2019 meeting that, beyond proposed refinements to subsection 606, any further revisions to modernize the NAS sections of the Code in relation to technology would be developed as part of the IESBA's Technology initiative.

In response to this development and in order to formulate

some initial high-level directional comments for the Board to consider going forward, the TWG reviewed various potential technology-related revisions in Section 600 (more specifically to Subsection 606) prepared by the NAS Task Force over the course of its work. Based on this review, the TWG discussed with the NAS Task Force its view that rather than making any technology-related changes to these sections in the NAS ED, there would be greater benefit in addressing the impact of technology relating to NAS holistically in the Technology initiative. At its December 2019 meeting, the IESBA agreed with this approach.

The TWG suggests that the following broad considerations be kept in mind in the development of any proposed new material for the Code to address the impact of technology and technology-related services:

- Factors relevant to evaluating the level of threats, including but not limited to:
 - The use and purpose of the service.
 - The degree of reliance that will be placed on the output of the particular service as part of the audit.
 - The extent to which the firm or network firm retains access to the underlying data relating to the service provided.
 - The location and accessibility of the technology.
 - Responsibility for ongoing monitoring and maintenance.
- The categories of threats to independence that could be created through the provision of technology-related services such as hosting, and under what circumstances providing these services becomes assuming a management responsibility.
- Specific considerations for engagements when a technology solution involves both services and products to an audit client.
- The implications of audit firms selling technology-related software products or tools.

Modernization of Terms and Concepts

As part of its review of Part 4A of the Code, the TWG considered whether the definition of independence itself might require revision in light of the impact of technology on firms and auditors. Ultimately, the TWG formed the view that the two components of independence – independence of mind and independence in appearance – and their descriptions in Part 4A of the Code remain relevant and do not require revision at this time.

The TWG also considered whether certain terms and concepts and their uses in Part 4A might need to be updated in light of the impact of the digital transformation. The results of this analysis are described below.

Office and Workforce Mobility

Given the increasing use of virtual or remote offices by PAPPs and firms, the TWG considered whether the term “office,” as used in Sections 410 and 510, should be updated. The Code defines “office” as “a distinct subgroup, whether organized on geographical or practice lines.” In this regard, the TWG considers that the current definition sufficiently covers the use of a virtual or remote office.

In reviewing the use of the term “office” in Section 410, the TWG noted that it is in the context of the fee dependency provisions. The TWG formed the view that use of the term in this context does not require any further revision as the aggregation and measurement of revenue by geographic or practice lines is generally not impacted by whether a PAPP is able to work virtually as a consequence of using remote technology connections or other technology tools.

With regards to Section 510, the TWG notes that the term “office” is used in the context of financial interests held by a firm, network firm, team members and others. In particular, paragraph R510.4(c) prohibits the holding

of a financial interest or an indirect financial interest in an audit client by any “other partner in the office in which an engagement partner practices in connection with the audit engagement, or any of that partner’s immediate family.” This requirement is based on the notion of identifying individuals who might have the ability to influence the engagement partner or the audit engagement and might have the ability to obtain information related to the engagement.

Paragraph 510.4 A1 provides further guidance on how to determine the office of the engagement partner. The use of “office” in this paragraph appears to focus on physical location where a partner can exert undue influence over an engagement partner in the same office location, thus impairing independence, at least in appearance. The TWG is of the view that the IESBA should consider if this idea of physical influence continues to be appropriate. With advancements in communication technologies, a partner who holds a financial interest in an audit client may have the ability to influence an engagement partner or an audit engagement without being assigned the same physical office of the engagement partner. Further, that partner may also be able to gain access to sensitive information without being in the physical office. Also, with advancements in workforce mobility, an engagement partner may be able to consistently perform their responsibilities without accessing their physical office, thereby limiting the extent of their relationships with other partners from that office.

Accordingly, the TWG is of the view that the IESBA should consider revising Section 510 to better capture the threats to independence created in the circumstance of a partner with such a financial interest in light of the use of modern communication technologies by firms.

Financial Interest, Cryptocurrencies and Blockchain

The Code currently defines a financial interest as “an interest in an equity or other security, debenture, loan or

other debt instrument of an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.”



The TWG briefly discussed whether the concepts of financial interests as used in Subsection 510 (Financial interests) and “bank and similar institution” in Subsection 511 (Loans and Guarantees) require revision to capture cryptocurrencies and the use of non-traditional mechanisms, such as blockchain, to transfer funds.

As the scope of Phase 1 is directed towards AI and data/ data analytics and sufficient work has not yet been undertaken on the impact of cryptocurrencies and blockchain, the TWG recommends that a further review of these concepts and potential impacts on the Code be included as part of information gathering and analysis in the next phase of the IESBA’s Technology initiative.

Data as an Asset

Organizations are increasingly recognizing data and information as assets with strategic value, and are taking steps to maximize their monetization, such as the appointment of a chief data officer and the development of information strategies.

Paragraph 400.8 of the Code states that one of the factors to be taken into consideration in determining whether an entity should be treated as a public interest entity is the

nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders. In an era of cloud providers, shared technology infrastructure providers, cryptocurrency exchanges, and data protection companies on which the public and the government rely, the TWG considered whether the holding of assets in a fiduciary capacity for a large number of stakeholders would (or should) include the holding of data or intellectual assets. The TWG is of the view that this issue might be best addressed in the IESBA's new project on revisiting the definition of a public interest entity.

The TWG has also considered the potential impact of data as assets on Section 350 of the Code, which is focused on financial and physical assets. The TWG discussed if Section 350 should be broadened to include the custody of not only financial and physical assets but also data as part of a PA's ethical responsibility towards data governance. The TWG considered whether, alternatively, a new Section should be developed to deal with custody or handling of client data because of ethical considerations unique to the nature of data as assets. The TWG suggests that a further review of Section 350 and data governance be included as part of the next phase of the IESBA's Technology initiative.

Routine and Mechanical Tasks

The TWG considered whether the term "routine and mechanical" as used in Subsections 601 (*Accounting and Bookkeeping Services*) and 602 (*Administrative Services*) should be amended in light of the increasing use of automation tools which take advantage of the capacity for machines to take on routine tasks with greater speed and accuracy than humans. Consideration was also given to the nature of machine learning, which enables a machine, over time and when programmed to do so, to learn from the data it processes and thereby take on attributes akin to applying human judgment.

Subsection 601 explains "routine and mechanical" accounting and bookkeeping services as requiring "little

or no professional judgment." It also provides a list of examples of such services such as "calculating depreciation on fixed assets when the client determines the accounting policy and estimates of useful life and residual values." Subsection 602 describes administrative services as involving the assistance of clients with their routine or mechanical tasks within the normal course of operations. The Subsection also provides examples of administrative services.

The TWG takes the view that whilst the automation of a task might cause that task to become "routine and mechanical," it does not necessarily mean that a firm or network firm should be permitted to perform that task for its audit client in accordance with Subsections 601 and 602. In this regard, the TWG believes that the litmus test of whether a task is considered "routine and mechanical" or an administrative service is whether the task requires little or no professional judgment and not whether the task can be executed in a routine and mechanical manner.

Accordingly, the TWG is of the view that the term "routine or mechanical" should be removed from Subsections 601 and 602 to focus on the level of professional judgment used in performing a task. This would also avoid any confusion about the nature of the services that might be permitted under these subsections with the continued evolution of automated services. The TWG has conveyed its view to the NAS Task Force for its consideration as it finalizes its proposals for the December 2019 IESBA meeting.

Long Association

With respect to long association, the TWG is of the view that familiarity with a client's information technology systems might create a familiarity threat in some circumstances. In this regard, the TWG has considered whether the list of factors that are relevant in evaluating the level of familiarity and self-interest threats in relation to an audit client in paragraph 540.3 A3 (b) should be

expanded to include a reference to technology, such as the nature and complexity of the audit client's information system that affects the accounting records or financial statements.

The TWG considers that this potential issue may be best addressed as part of the IESBA's long association implementation review in due course.

Independence for Assurance Engagements Other Than Audit and Review Engagements

The TWG also conducted a review of Part 4B² of the Code as part of its review of the Code's International Independence Standards. Based on this review, the TWG did not identify any additional issues beyond those already cited elsewhere in this report. It is anticipated that any subsequent revisions to Part 4A will be carried through to Part 4B as conforming amendments as appropriate.

Recommendation 7

The TWG recommends that the IESBA consider strengthening the provisions in Part 4A of the Code relating to auditor independence by:

- Considering whether Section 520 or other provisions in Part 4A should be revised to address the threats to independence created by the sale or licensing of technology applications to audit clients, and the use of an audit client's technology tool in the delivery of NAS to another entity.
- Revising Section 600, particularly Subsection 606, with respect to the provision of technology-related NAS, taking into account the proposals under the IESBA's NAS project to be released for exposure in Q1 2020.
- In relation to the concept of an "office," considering whether Section 510 (Financial Interests) should be revised to better capture the threats to independence created by the use of modern communication technologies by firms. Such technologies potentially challenge the notion of an engagement partner's physical office location being a determining factor in whether that engagement partner or the audit engagement can be unduly influenced by another partner in that same office.

The TWG also recommends that the IESBA consider, as part of its strategic commitment to undertake an implementation review of the Long Association provisions, whether the list of factors in paragraph 540.3 A3 (b) of the Code should be expanded to include a reference to technology, such as the nature and complexity of the audit client's information system that affects the accounting records or financial statements.

2. Part 4B, *Independence for Assurance Engagements Other Than Audit and Review Engagements*

IV. Recommendations for Non-Authoritative Guidance Material



The TWG recommends the development of non-authoritative guidance material covering various topics, some of which may also be related to areas where recommendations have been made for potential revisions to the Code. Determining the most appropriate format of each piece of guidance material will depend on factors such as the targeted audience, nature and complexity of the topic, existing provisions in the Code, and resources available. Formats that would be suitable may include:

- TWG Updates/Communiques
- Thought leadership publications
- Other papers or reports
- Digital and other formats (e.g., articles, webinars and/or interviews)

Potential topics for development

1. Impact of technology

Aim: To *educate* stakeholders on the pervasive nature of technology and its inter-related impact across all the FPs. The publication may include discussions on the impact of machine bias as an example, the relationship between AI ethics principles and the FPs as well as the complex work environment in a digital age.

Targeted Audience: Regulators, NSSs and PAOs

2. Leadership in promoting ethical behavior

Aim: To *educate* and *motivate* PAs about promoting an ethics-based culture and how they can contribute to building public trust, using examples/scenarios and taking into consideration implications in different jurisdictions.

Targeted Audience: PAOs and individual PAs

3. Professional Competence

Aim: To *educate* stakeholders about the importance of keeping a PA's competence levels and skills up to date, the importance of soft skills and having the right mindset in a digital age. The IESBA may consider a joint publication with IFAC in the context of IFAC's new education initiative.

Targeted Audience: PAOs, firms, higher education institutions

4. Confidentiality

To educate and inform stakeholders about maintaining confidentiality in a digital age and how related concepts such as data governance are expressed in the Code.

Targeted Audience: PAs

The TWG suggests developing the material in consultation with subject matter experts or in collaboration with other bodies such as professional accountancy bodies or international/national standard setters.

The TWG notes that the development of any recommended guidance material may also be considered as part of the collaboration efforts between IFAC and the IESBA regarding adoption and implementation of the Code.

V. Recommendations for Phase 2 of the Technology Initiative



The TWG recommends the next phase of the Technology initiative move forward in Q1 2020 with two distinct work streams, each with a different focus and remit:

A **formal project and related Task Force**, the objectives of which are to consider potential enhancements to the Code as set out in Section II of this report. This project will adhere to standard-setting due process for any revisions to the Code.

A **Technology Working Group**, which would be responsible for:

- Information gathering and analysis of technologies beyond AI and data/data analytics, including identification of suitable academic research.
- Contributing to the development of non-authoritative guidance material as stated in Section III of this report in accordance with collaborative processes agreed between IFAC and the IESBA.

- Coordination with the IAASB's Technology Working Group to identify and work on matters of mutual interest.

In recommending this approach for Phase 2 work, the TWG believes the Technology initiative would be best served in terms of speed and effective use of the IESBA's resources if a Working Group leads the initial research and identification and analysis of potential ethical issues arising from the use of a particular technology or its application. A Task Force could then pick up on findings from the Working Group and lead a focused standard-setting component of the Technology initiative to ensure it progresses in a timely fashion. This dual work stream approach would also allow for some flexibility by the Working Group in topics it pursues in its research given the dynamic nature of technology and potential impact it has on the ethical behavior of PAs.¹

1. At its December 2019 meeting, the IESBA agreed to the TWG's recommendations of the two work streams subject to availability of resources.

Information Gathering and Analysis

Subject to additional input from the Board, stakeholders or current developments in the marketplace, the TWG recommends the following technology-related topics be considered as priorities for Phase 2:

- Blockchain, Cryptocurrencies and Initial Coin/Security Token Offerings
- Cyber-crime and Cyber-security
- Internet of Things
- Data governance

The Phase 2 TWG would leverage the lessons learnt from the Phase 1 approach to accelerate its information gathering and analysis as well as the completion of findings and recommendations. Consideration might also be given to the option of bringing together multidisciplinary stakeholders such as technologists, subject-matter experts and academics to discuss specific topics, such as blockchain.

With respect to who should continue on with the information gathering activities, the TWG considered the alternative of merging the TWG with the IESBA's Emerging Issues and Outreach Committee (EIOC), and adding these activities to the EIOC's remit given that many emerging issues are likely to be technology-related. Upon deliberation, the TWG formed the view that the technology and EIOC workstreams should remain separate and that the EIOC should continue to bring to the TWG's attention any specific technology-related emerging issue for its consideration as appropriate.

Academic Research

The TWG also explored the merits of recommending that the IESBA commission academic research on a technology-related topic. The purpose of such commissioned

research is to assist the Board in gaining a more in-depth understanding of the types of technology and their impact on the ethical behavior of PAs. Such research should provide more robust evidence for the IESBA to determine if further enhancement to the Code or issuance of guidance material is necessary.

Based on its analysis of the information received in Phase 1, including academic research reviewed and discussions with those from the academic community, the TWG did not identify any specific areas or issues that warrant further academic research at this time. However, it is important to continue to assess and remain alert for potential research topics as the Technology initiative moves forward.



Coordination with IAASB

As the IESBA's and IAASB's technology work streams progress, matters of mutual interest will be identified, discussed and managed at the staff, working group and Board levels in accordance with the agreed coordination framework between the two Boards.

As part of the coordination arrangement for the technology work streams, a member from the IAASB's Technology Working Group (formerly its Data Analytics Working Group) was added to the TWG as a correspondent member, and vice versa. The purpose of this correspondent member arrangement is to facilitate discussions and optimize coordination and collaboration on

matters of mutual interest between the two Boards. This would enable timely inputs to agenda papers and mutual participation in working group discussions as appropriate.

In this regard, the IAASB's current technology work streams will continue to be monitored, including the development of any non-authoritative guidance material by its TWG as well as the work of its Audit Evidence Working Group relating to audit evidence.

Recommendation 8

The TWG recommends that two distinct work streams be established in accordance with the first paragraph of Section IV of this report:

(a) A formal project and related Task Force, the objectives of which are to consider potential enhancements to the Code as set out in Recommendations 1–7 in Section II of this report.

(b) A Technology Working Group, which would be responsible for:

- Information gathering and analysis of technologies beyond AI and data/data analytics, including identification of suitable academic research.
- Contributing to the development of non-authoritative guidance material as stated in Section III of this report in accordance with collaborative processes agreed between IFAC and IESBA.
- Coordination with the IAASB's Technology Working Group to identify and work on matters of mutual interest.

Appendix

List of Stakeholders and Outreach Events Conducted as of December 2019

Stakeholders/Events	MB	PAIBs	Firms	NSS	Reg	Academics	Vendor	Others	Region	Date
Association of Chartered Certified Accountants (ACCA)	•								Europe	Jan 2019
Chartered Institute of Management Accountants (CIMA)		•							Global	Jan 2019
Inflo (audit and accounting software vendor)							•		Europe	Jan 2019
Institute of Business Ethics (IBE)								•	Europe	Jan 2019
Institute of Chartered Accountants in England and Wales (ICAEW)	•								Europe	Jan 2019
Chartered Professional Accountants of Canada (CPA Canada)	•			•					North America	Jan 2019
University of Waterloo Centre for Accounting Ethics– 4 th Ethics Symposium	•		•			•			North America	Apr 2019
IESBA National Standard Settlers (NSS) 2019 Meeting				•					Global	May 2019
Accountancy Europe (AE)	•								Europe	May 2019
European Commission (EC)					•				Europe	May 2019
Organization for Economic Co-operation and Development (OECD)								•	Global	May 2019
Meeting with Paris-based Firms			•						Europe	May 2019
Cercle d’Ethique des Affaires (CEA)								•	Europe	May 2019
CPA Canada – Foresight Meeting	•		•		•	•			North America	Jun 2019
AICPA	•								North America	Oct 2019
Rutgers Business School						•			North America	Oct 2019
U.S. Public Company Accounting Oversight Board (PCAOB)					•				North America	Oct 2019
U.S. Government Accountability Office (GAO)								•	North America	Oct 2019
U.S. Securities and Exchange Commission (SEC) (via teleconference)					•				North America	Oct 2019
Partner, Cotton & Company			•						North America	Oct 2019
Ordre des Comptables Professionnels Agréés du Québec (CPA Québec)	•			•					North America	Nov 2019

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	4.1
Meeting date:	2 September 2020
Subject:	ED 600 Group Audits
Date:	20 May 2020
Prepared by:	Peyman Momenan

<input checked="" type="checkbox"/> Action Required
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Agenda Item Objectives

To:

- APPROVE the draft submission on the IAASB exposure draft, ISA 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors) (ED- 600)*.

Background

1. The International Auditing and Assurance Standards Board released an exposure draft of proposed ISA 600 (Revised) (ED-600) in April 2020. Submissions are due on 2 October 2020.
2. A communique was sent to constituents requesting comments on ED-600 by 20 August 2020. We also held virtual round tables in June and July. The round tables were targeted at NZ practitioners who are engagements partners of listed NZ entities that prepare group financial statements.
3. ED-600 intends to achieve the following public interest matters:
 - Keeping the IAASB's standard on group audits fit for purpose
 - Encouraging proactive management of quality at the engagement level
 - Fostering an appropriately independent and challenging sceptical mindset of the auditor
 - Reinforcing the need for robust communication and interactions during the audit.
4. The more significant changes proposed in ED ISA 600 are:
 - (a) Clarified the scope of the standard, through the introductory paragraphs and definitions and related application material, including whether, and how, ED ISA 600 applies for:
 - Shared service centres;

- Entities with branches and divisions; and
 - Non-controlled entities, including equity-accounted investees and investments carried at cost.
- (b) New definitions including the definitions of component and group financial statements.
- (c) Clarified and reinforced that all International Auditing Standards need to be applied in a group audit engagement through establishing stronger linkages to the other International Auditing Standards, in particular to proposed ISA 220, ISA 315 (Revised 2019) and ISA 330.
- (d) Introduced a principles-based approach that is adaptable to a wide variety of circumstances, and scalable for audits of groups of different complexity, for example by:
- Focusing the group engagement team’s attention on identifying, assessing and responding to the risks of material misstatement; and
 - Including separate sections throughout to highlight the requirements and application material for circumstances when component auditors are involved.
- (e) Enhanced the documentation requirements and included application material to emphasise the linkage to the requirements in ISA 2301 and to clarify what the group engagement team may need to document in different situations, including when there are restrictions on access to component auditor documentation.
- (f) Clarified how the requirements in proposed ISA 220 apply to manage and achieve audit quality in a group audit, including sufficient and appropriate resources to perform the engagement, and the direction and supervision of the engagement team and the review of its work.
- (g) Focused the group engagement team’s attention on identifying, assessing and responding to the risks of material misstatement of the group financial statements, and emphasised the importance of designing and performing procedures that are appropriate to respond to those assessed risks of material misstatement.
- (h) Clarified how to address restrictions on access to people and information in a group audit, including restrictions on access to component management, those charged with governance of the component, component auditors, or information at the components.
- (i) Clarified how the concepts of materiality and aggregation risk apply in a group audit.
- (j) Emphasised the importance of professional scepticism, including when:
- Determining the direction, supervision and review of the component auditor’s work; and
 - The group engagement team’s evaluation of whether sufficient appropriate audit evidence has been obtained (including by component auditors) to provide a basis for forming an opinion on the group financial report.
5. ED-600 also includes conforming amendments to ISA 220 (Revised)¹, ISA 300², and ISA 402³.

¹ ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

² ISA 300, *Planning an Audit of Financial Statements*

6. Outreach activities consisted of:
 - A targeted interview with the FMA;
 - A round table attended by representatives of 2 large firms and 1 mid-tier firms and CA ANZ;
 - Requests for submissions to the NZAuASB on the ED (closed on 20 August 2020).
7. The NZAuASB s discussed the ED at the NZAuASB June meeting and provided feedback which has informed the draft submission.
8. In general, the stakeholders we heard from are supportive of the proposed standard and do not see the standard as substantively different to the extant. Even the risk-based approach replacing the “significant component” approach is not expected to cause a significant change to how group audits are conducted in NZ. However, there are some main issues in group audits that the ED does not address, including:
 - Associates, non-controlled entities and joint ventures which may be material components but are not controlled by group management, continue to cause access issues in the New Zealand environment. In particular, privacy/confidentiality laws or regulations may have regulations that preclude information from being shared with a group engagement team. The requirement in the acceptance/continuance stage of a group audit for the Group Management to agree to provide unrestricted access to persons within the group that is outside of the control of group management or else the engagement could not be accepted would be particularly impractical to implement. This is particularly important as the ED now have clarified that the scope includes entities that have investments carried at cost. This is likely to cause significant issues in case of auditing “fund of funds” entities (e.g. an investment management fund) that have non-controlling interests at cost.
 - Applying the introduced concept of “consolidation process” to internally structured components (e.g. branches, divisions and business units) based on how the group structured is general ledger would cause inconsistencies in practice.
 - The ED refers to challenges that arise from components that operate in environments that have different legal requirements and regulations, culture, language etc. However no practical solutions are proposed how to address these challenges. These challenges are some of the key driving factors behind some significant audit inspections findings and the proposed standard will not help to improve this situation.
 - With new independence requirements and rotation requirements in many jurisdictions becoming stricter, some group auditors may find it increasingly difficult to find competent auditors to act as component auditors in a group audit.
9. To date of this summary paper, no formal submissions have been received. However, CA ANZ shared CA ANZ’s initial feedback on the proposals contained in the ED (please refer to Agenda item 4.3).

³ ISA 402, *Audit Considerations Relating to An Entity Using a Service Organisation*

10. The extant ISA 600 does not include any compelling reason amendments to be considered for carrying forward to the proposed standard. The Board has not identified any compelling reason amendments to the proposed standard.
11. At this stage of the exposure process, Australian compelling reason amendments have not yet been considered by the AUASB. The AUASB only considers introducing compelling reasons amendments after a standard is finalised. The NZAuASB will consider any compelling reason amendments identified for NZ based on any proposed amendments of AUASB in due course.

Matters for Consideration

12. For the Board to:

- APPROVE the draft submission on ED-600.

Material Presented

Agenda item 4.1	Board Meeting Summary Paper
Agenda item 4.2	The NZAuASB draft submission on Proposed ISA 600 (Revised), <i>Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)</i>
Agenda item 4.3	CA ANZ preliminary feedback on revised ISA 600

? September 2020

Willie Botha
Technical Director
International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, 10017
USA

Dear Willie,

IAASB Exposure Draft – Proposed ISA 600 (Revised), Special Considerations-Audits of Group Financial Statements (Including the Work of Component Auditors)

Thank you for the opportunity to comment on this Discussion Paper. We submit the feedback from the New Zealand Auditing and Assurance Standards Board (NZAuASB) to the specific questions raised in the attachment.

The External Reporting Board (XRB) is a Crown Entity responsible for developing and issuing accounting and auditing and assurance standards in New Zealand. The XRB's outcome goal is to contribute to the creation of dynamic and trusted markets through the establishment of an accounting and assurance framework that engenders confidence in New Zealand financial reporting, assists entities to compete internationally and enhances entities' accountability to stakeholders. The NZAuASB has been delegated responsibility by the XRB for developing and issuing auditing and assurance standards.

The NZAuASB undertook various outreach activities to obtain feedback from its constituents on the ED, including a webinar and one-on-one interviews with practitioners from both small and large firms. Their feedback helped inform the Board in developing its response.

The NZAuASB supports the IAASB's proposals to revise ISA 600. The NZAuASB acknowledges the importance of **some of the other recent IAASB's activities** to improve the quality of audits of group financial statements, in particular the revisions of ISA 220, *Quality Control for an Audit of Financial Statements*, *Quality Management at Firm Level - ISQM 1* and *Engagement Quality Reviews, ISQM 2*.

The NZAuASB also notes that the proposed standard has been unable to address many of the practical challenges that inspired the revision of the standard (e.g. access issues and documentation issues). The circumstances caused by COVID 19 further demonstrates the need for active involvement of all key stakeholders to address issues that cannot be resolved by any single party. Addressing such concerns would require participation of other key stakeholders and measures other than standard-setting activities. It is therefore important for the IAASB to continue the conversation on audit quality in group audits and facilitates engagements between key stakeholders to explore other avenues to improve audit quality.

We are very interested in this project and are happy to offer our assistance to the task force if needed. Should you have any queries concerning our submission please contact either myself at the address details provided below or Sylvia van Dyk (sylvia.vandyk@xrb.govt.nz).

Yours sincerely,



Robert Buchanan

Chairman

Email: robert@buchananlaw.co.nz

Submission of the New Zealand Auditing and Assurance Standards Board

IAASB Exposure Draft – Proposed ISA 600 (Revised)

I Schedule of Responses to the IAASB's Specific Questions

1. Question 1: With respect to the linkages to other standards:
 - (a) Does ED-600 have appropriate linkages to other ISAs and with the proposed ISQMs?
 - (b) Does ED-600 sufficiently address the special considerations in a group audit with respect to applying the requirements and application material in other relevant ISAs, including proposed ISA 220 (Revised)? Are there other special considerations for a group audit that you believe have not been addressed in ED-600?

Response:

The NZAuASB is of the view that there is a mixed result in this regard. In some areas ED-600 is successful in achieving the objectives stated in the question 1. These include:

- Paragraph 15 to 17 and corresponding application guidance, which address special considerations in applying ISA 2101, specifically considering access issues.
- Paragraph 24 and corresponding application guidance, which addresses how applying the requirements of ISA 315 (Revised 2019) for understanding the entity and its environment, the applicable financial reporting framework and system of internal controls may have specific considerations for a group audit. The application material to support this paragraph is directly relevant to a group engagement and are helpful and needed for conducting a group engagement (e.g. risks that are particularly relevant to a group structure, special considerations that apply when a group prepares consolidated financial statements, some significant elements for internal controls in a group structure and how they may affect audit etc).
- Paragraph 29 and corresponding application guidance, which addresses a special form of materiality that would only apply in a group audit situation (i.e. the component performance materiality)
- Paragraph 55 which addresses how the requirements in ISA 2652 for communicating significant audit findings applies to audit findings at a component.

However, there are other instances that ED-600 is not as successful in achieving the stated objectives. For example:

1. Paragraph 31 simply reminds the group auditors that they are responsible for applying ISA 315 (Revised 2019) for identifying and assessing the risks of material misstatements. The application guidance in paragraphs A78 repeats what is already in ISA 315 (Revised 2019) without adding anything specific to group audits.

The same is true for A80, where guidance already included in ISA 240³ is repeated. Specific considerations in applying these standards in group audits seem to arise when component auditors are involved. Paragraph 32 of the ED does address these considerations. In this light, paragraph A79 is also superfluous and could easily be built into paragraph A82. However, even then the

¹ ISA 210, *Agreeing the Terms of Audit Engagements*

² ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

³ ISA 240, *The Auditors Responsibilities Relating to Fraud in an Audit of Financial Statements*

requirement can be clarified by specifically requiring the group auditor to:

- i. Consider whether they should involve component auditors in risk identification and assessment at components (Appendix 1 provides appropriate guidance to help auditors in this relation).
 - ii. If yes, what are the respective responsibilities and how best to have these communicated, documented and evaluated etc.
2. In a similar fashion paragraph 33 simply reminds auditors that they are required to apply ISA 330. The real considerations of applying ISA 330 for group engagements are:
- i. Should they involve component auditors as part of their response (paragraphs A86 to A90 provide relevant and useful guidance about this)
 - ii. If yes, what are the respective responsibilities and how best to have these communicated, documented and evaluated (paragraphs A96 to A101 provide useful and relevant guidance in this regard).
3. Paragraph 47 relating to applying ISA 560⁴ is similarly void of specific group engagement connection.

In relation to linkage with ISA 220 (Revised), ED-600 does seem to provide strong linkage to ISA 220 (Revised). Paragraphs 12 (relating to leadership responsibilities), 20 (ethical requirements), 21-22 (engagement resources), 23 (engagement performance) all link to ISA 220, and the corresponding application material provides relevant and helpful guidance.

However, the application guidance lacks coherence as it does not have a comprehensive framework to reflect how ISA 220 requirements may apply to a group audit. It may be helpful to provide guidance for the group auditor to look at the application material through the following lenses:

Lens	Aspects to consider
Who are the component auditors?	<ol style="list-style-type: none"> 1) Same firm, network firm, different firms 2) Similarity of regulatory and audit monitoring environment 3) Similarity of cultures, languages, education system etc
What is their expected level of involvement	<ol style="list-style-type: none"> 1) High (e.g. in all stages of audit) 2) Moderate (e.g. fully involved in some stages) 3) Low (limited involvement to perform specific procedures)
What is the expected level of assignment of responsibilities	<ol style="list-style-type: none"> 1) High (e.g. highly competent with in-depth knowledge of the component trusted with high level of autonomy in how they go about their responsibilities) 2) Moderate (e.g. the group engagement team provides principle-based instructions and allow a moderate level of autonomy to the component auditor) 3) Low (detailed and comprehensive instructions for the component auditors regarding their responsibilities)
What is the expected level of impact from the involvement of the component auditor on overall audit conclusion?	<ol style="list-style-type: none"> 1) High (e.g. audit evidence from the work undertaken by the component auditor is a major contributor to the group auditor's conclusion about a significant risk at the group financial statements) 2) Moderate 3) Low
What is the expected level of access to the underlying information	<ol style="list-style-type: none"> 1) High (e.g. access to the audit file as if it was in the group engagement team head office) 2) Moderate (e.g. a good level of access but not to all documents) 3) Low (significant restrictions)

⁴ ISA 560, *Subsequent Events*

2. With respect to the structure of the standard, do you support the placement of sub-sections throughout ED-600 that highlight the requirements when component auditors are involved?
Response:

Response:

The NZAuASB supports the placement of sub-sections through ED-600 as it helps the flow of the standard. Nevertheless, the NZAuASB also suggests including all the requirements relating to involving component auditors in a separate appendix.

3. Do the requirements and application material of ED-600 appropriately reinforce the exercise of professional skepticism in relation to an audit of group financial statements??

Response:

The NZAuASB acknowledges that ED-600 does emphasise the importance of professional scepticism. However, it may be helpful to provide some examples of potential impediments to professional scepticism that may apply in a group audit engagement. For example, it may be helpful to draw the attention of the group auditors to potential impediments that may impact the component auditor's exercise of professional scepticism and how they can be addressed. Examples of such potential impediments may include:

- Time pressure to complete a component audit in a short time to meet the deadlines determined by the group engagement team.
- Unconscious bias by believing **it is the group auditor's role to be professionally sceptical and the component auditor to simply follow instructions from the group.**
- Perceived differences between the group engagement team's professional prestige or fear of reprisal may deter component auditors from challenging the accuracy and appropriateness of the instructions they receive, even when they find them inadequate or inaccurate.

4. Is the scope and applicability of ED-600 clear? In that regard, do you support the definition of group financial statements, including the linkage to a consolidation process? If you do not support the proposed scope and applicability of ED-600, what alternative(s) would you suggest (please describe why you believe such alternative(s) would be more appropriate and practicable).

Response:

The definition of group financial statements is clear and straightforward to apply where the audited entity must account for its interest in other separately structured entities in accordance with the applicable financial reporting framework. The NZAuASB supports ED-600 to link the definition of group financial statements with aggregation requirements under the applicable financial reporting framework (including consolidated entities, joint arrangements, associated entities as well as consolidation of entities under common control).

However, using the consolidation process to try to scope in group structures other than those mentioned above (e.g. the case of branches or divisions that are not formal separate structures) is problematic. According to paragraph A17 of ED-600 whether such structures are scoped in or out revolves around how **an entity's financial reporting system organizes financial information.** Consequently, if an entity uses financial information for several locations that is aggregated using a separate system or process, it will be scoped in. However, if the same entity designs its financial information system in a way that **geographical location is first part of the group's financial reporting system** and then disaggregated by group management for operating purposes, there is no consolidation process, and the audit is scoped out of ISA 600. The NZAuASB believes that in such circumstances professional judgement is required to carefully consider the engagement circumstances to determine whether a group structure exists, and what parts of ISA 600 would apply.

The NZAuASB suggests a two-step approach to determine whether group financial statements exist:

1. For separately structured entities, where the applicable financial reporting framework requires aggregation of their financial statements into a group financial statements via consolidation, proportionate consolidation, or the equity methods of accounting.
2. For internally structures business units (e.g. branches and divisions), the auditor exercises professional judgement in determining whether ISA 600 applies. In making such determination, the auditors consider the following:
 - i. Specific inherent risk factors (para A56 of the ED includes a good list of these risk factors).
 - ii. Whether there is a need to aggregate the financial information of such units in a way that involves elimination of inter-units transactions and balances or accounting for different reporting periods.
 - iii. specific considerations relating to understanding and **evaluation of the group's system of internal controls**, including matters such as Commonality of Controls (A59-A63), use of Centralised Activities (A64-A65) **and the entity's IT systems**.
 - iv. The increased aggregation risk applying to materiality determination where there are many components.
 - v. Increased concerns for inadequate access to appropriate and sufficient audit evidence, especially when accepting or continuing a client
5. Do you believe the proposed standard is scalable to groups of different sizes and complexities, recognizing that group financial statements, as defined in ED-600, include the financial information of more than one entity or business unit? If not, what suggestions do you have for improving the scalability of the standard?

Response:

The NZuASB believes ED-600 is scalable.

6. Do you support the revised definition of a component **to focus on the 'auditor view' of the entities and business units comprising the group for purposes of planning and performing the group audit?**

Response:

The NZuASB supports the ED-600 **requirement to take an "auditor view" of the group for the purposes of planning and performing the group audit.**

7. With respect to the acceptance and continuance of group audit engagements, do you support the enhancements to the requirements and application material and, in particular, whether ED-600 appropriately addresses restrictions on access to information and people and ways in which the group engagement team can overcome such restrictions?

Response:

As noted by the IAASB and ISA 600 Task Force, access issues for entities that are not under **the group's** control (e.g. associates accounted for using equity method of accounting) are likely to continue to be a challenge in practice. And while paragraph A29 of ED-600 include examples of activities an auditor may be able to do to overcome restrictions, it is unlikely that this additional explanation material will make a meaningful difference in practice, as the suggested activities are common sense measures that are likely to have been applied in practice for many

years (and not being adequate to prevent the identified issues). ED-600 also provides very little guidance whether the strength of potential evidence obtained from undertaking these activities is adequate to offset access restrictions. For example, what is the value of an audited financial statement of an associated entity?

8. Will the risk-based approach result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks? In particular, the IAASB is interested in views about:
 - (a) Whether the respective responsibilities of the group engagement team and component auditors are clear and appropriate?
 - (b) Whether the interactions between the group engagement team and component auditors throughout the different phases of the group audit are clear and appropriate, including sufficient involvement of the group engagement partner and group engagement team?
 - (c) What practical challenges may arise in implementing the risk-based approach?

Response to questions 8 (a) and (b)

ED-600 allows the group engagement team to assign a significant portion of risk assessment and risk response stages of the audit to component auditors while clarifying that the group engagement team is responsible for such assigned work. In the NZAuASB's view, while this is clear, practical issues are likely to arise in relation to how the group engagement team:

- 1) Considers the appropriateness and sufficiency of work performed by component auditors (the higher the degree of assigned work the greater the need for a more robust evaluation).
- 2) How, and to what extent such evaluation and the consequent conclusions are documented.

Paragraph A126 of ED-600 provides some guidance on the matters that are needed to be documented, but as expected (given the nature of the issue and the wide spectrum of possible circumstances) the level, extent and nature of such documentation is a matter of professional judgement. So while respective responsibilities are conceptually very clear (the group engagement team is responsible for all audit matters as if they performed all of the audit themselves), demonstrating the adequate level of direction, supervision and review of component auditors' work and documentation as well as ongoing involvement in their activities will remain a significant challenge.

We further consider that ED-600 does not clearly explain the meaning of performing audit procedures on the entire financial information of the component. We note that paragraph A98 explains that the component auditor may need to consider the sufficiency and appropriateness of audit evidence obtained in performing further audit procedures with respect to the financial statements. There seems to be a lack of clarity in specifying what is the objective of assigning **performance of audit procedures on "entire financial information of a component"**. For example, whether ISA 600 expect the component auditor to obtain reasonable assurance that the component financial information as presented to be included in the group accounts is free from material misstatement. We recommend this to be made clearer.

Response to question 8 (c)

The NZAuASB have not identified any practical challenges that may arise in implementing the risk-based approach at this stage.

9. Do you support the additional application material on the commonality of controls and centralized activities, and is this application material clear and appropriate?

Response:

The NZAuASB supports the additional application material on the commonality of controls and centralised activities.

10. Do you support the focus in ED-600 on component performance materiality, including the additional application material that has been included on aggregation risk and factors to consider in determining component performance materiality?

Response:

The NZAuASB supports the ED-600 approach to component performance materiality. The NZAuASB encourages the IAASB to consider whether some practical examples can be included in implementation guidance to help a better understanding of the concept.

11. Do you support the enhanced requirements and application material on documentation, including the linkage to the requirements of ISA 230? In particular:
- (a) Are there specific matters that you believe should be documented other than those described in paragraph 57 of ED-600?
 - (b) Do you agree with the application material in paragraphs A129 and A130 of ED-600 **relating to the group engagement team's audit documentation** when access to component auditor documentation is restricted?

Response:

As discussed in our response to question 8, the most significant documentation challenge in a group audit is likely to be related to the work performed by component auditors. While the additional explanation material in paragraphs A124-A128 of ED-600 is an improvement on the extant ISA 600, it is unlikely to be adequate in resolving the most challenging documentation consideration that are left **to the group engagement team's professional judgement**.

Similarly the additional paragraphs in A129 and A130, while logical, are in nature common sense responses auditors would adopt in such situations. It is the nature and extent of such documentation that is important **and those are left to auditors' professional judgement**.

12. Are there any other matters you would like to raise in relation to ED-600?

Response:

The NZAuASB would like to draw the IAASB attention to recent research indicating that users of group financial statements are interested to know about whether component auditors were involved in the group audit and how their involvement is managed. The NZAuASB encourages the IAASB to consider including some application and other explanatory paragraph for group auditors to consider whether it is appropriate to include a Key Audit Matter or Other Matter paragraph to communicate this matter in their auditor report .

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	5.1
Meeting date:	2 September 2020
Subject:	Meeting with the Deputy Controller and Auditor-General
Date:	20 August 2020
Prepared By:	Sylvia van Dyk

Action Required

For Information Purposes Only

Agenda Item Objectives

To have a discussion with Greg Schollum, Deputy Controller and Auditor-General about matters of mutual interest and how the NZAuASB can continue to collaborate with the OAG in future.

Background

1. We have invited Greg to share his views on the following topics, and any other matters he would like to raise with the Board.
 - The impact of Covid-19 on the public sector and the OAG's response to it, and areas where potential collaboration would be beneficial.
 - The OAG's thoughts on the Monitoring Group's report recommendations, and the PIOB's public interest framework for development of standards.
 - The OAG's approach to non- assurance services (NAS), noting the NZAuASB's view is that the IESBA has not gone far enough with its recent proposals and that the NAS proposals do not sufficiently address perceptions that the assurance practitioner is not independent, particularly in respect of audit clients that are public interest entities (PIEs). The Board's recommendation to the IESBA is that NAS to audit clients that are PIEs should be prohibited. Depending on the outcome of the IESBA's due process, there may be an opportunity to consider the New Zealand position further once the changes to the Code have been confirmed later this year.

About Greg Schollum

2. Greg started a five-year term as the Deputy Controller and Auditor-General on 28 September 2015.
3. The Deputy Controller and Auditor-General is appointed under the Public Audit Act 2001 in the same way as the Controller and Auditor-General, and is also an Officer of Parliament. The Deputy has the same responsibilities under the Act as the Auditor-General, but to be carried out subject to the Auditor-General's control.
4. Greg joined the Office of the Auditor-General in September 2004. He was a member of the Financial Reporting Standards Board of the New Zealand Institute of Chartered Accountants for eight years, and has served on numerous working groups and

committees of the Institute. He also served as New Zealand's representative on the International Public Sector Accounting Standards Board from 2004 to 2008, and on the New Zealand Accounting Standards Board from 1 July 2011 to 31 December 2015.

5. Greg is a Fellow of the Institute and gained his Business Management Studies qualification from the University of Waikato. Before joining the Office of the Auditor-General, Greg was the Chief Financial Officer for Greater Wellington Regional Council and prior to that an Audit Director with Audit New Zealand.

Recommendation

6. We recommend that the Board note the contents of this memo and participate in the discussion.

Material Presented

Agenda item 5.1 Board meeting summary paper

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	6.1
Meeting date:	2 September 2020
Subject:	Amending PES 1 to Include Part 2 of the IESBA Code
Date:	11 August 2020
Prepared by:	Sharon Walker

<input checked="" type="checkbox"/>	Action Required	<input type="checkbox"/>	For Information Purposes Only
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Agenda Item Objectives

1. The objective for this agenda item is for the Board to:
 - CONSIDER and APPROVE as a final standard *Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm* and the related consequential amendments.
 - CONSIDER and APPROVE the draft signing memorandum.

Background

2. Because Part 2 of the IESBA Code sets out requirements and application material for professional accountants in business, historically it was excluded from Professional and Ethical Standard 1, as the provisions were considered outside the mandate of the NZAuASB. However, as part of the IESBA's restructure project, the IESBA sought to clarify the applicability of Part 2 to professional accountants in public practice, recognising that in certain circumstances the provisions for professional accountants in business may be relevant to professional accountants in public practice, for example, section 270 *Pressure to Breach the Fundamental Principles*. The IESBA included a requirement¹ in Part 3 that states,

“When dealing with an ethics issue, the professional accountant shall consider the context in which the issue has arisen or might arise. Where an individual who is a professional accountant in public practice is performing professional activities pursuant to the accountant’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions of Part 2 that apply to these circumstances.”

¹ *International Code of Ethics for Professional Accountants, including International Independence Standards*, paragraph **R300.5**

3. Accordingly, in April 2020, the NZAuASB issued [ED NZAuASB 2020-1](#)². The proposal amends Professional and Ethical Standard 1 to include Part 2 of the IESBA International Code of Ethics, with contextual amendments for application in New Zealand.
4. Submissions on ED NZAuASB 2020-1 closed on 20 July 2020 following a 90-day comment period. We received one submission, from the OAG. In the matters discussed below, grey shaded text represents wording from the submission.

Matters raised in the Submission

5. If our understanding is correct, we would conclude that Part 2 of the Code of Ethics will not apply to assurance practitioners who do not have a relationship with a firm.
6. The intent of the amendment to PES-1 is to clarify the applicability of Part 2 of the IESBA Code to an assurance practitioner's relationship with a firm. We therefore agree with this observation, in the context of a definition of a "firm".
7. Professional and Ethical Standard 1 defines "firm" as
 - A sole practitioner, partnership or corporation undertaking assurance engagements;
 - An entity that controls such parties, through ownership, management or other means, and
 - An entity controlled by such parties, through ownership, management or other means.
8. We consider the Code is clear in how firm has been defined, and that no amendments are required.
9. We are not sure if the reference to **employing organisation** in paragraph 200.3 in the Exposure Draft, is deliberate. If this reference is deliberate it creates confusion as to whether the exposure draft is concerned with
 - An assurance practitioner in their relationship with the firm; or
 - An assurance practitioner in their relationship to their employing organisation;
 - or both
10. Prior to issuing the revised and restructured International Code, the International Code was made up of distinct parts. A professional accountant was either a professional accountant in practice or a professional accountant in business. While, within the International Code, these distinctions still exist, the Code acknowledges that in some ethical situations, the professional accountant in public practice will need to look to the provisions relevant to professional accountants in business.
11. As acknowledged in the invitation to comment, a key strategic objective set by the XRB Board for the NZAuASB is to adopt auditing and assurance standards, including professional and ethical standards, in New Zealand unless there are strong reasons not to. Also acknowledged

² ED NZAuASB 2020-1 *Proposed Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship With the Firm*

in the invitation to comment is that a number of the provisions in Part 2 may be less relevant to an assurance practitioner and that there is duplication of material between parts 2 and 3. Given the holistic nature of the revised and restructured International Code, the NZAuASB determined that it is appropriate to amend PES 1 to incorporate Part 2 in its entirety.

12. Accordingly, while Part 2 is written for the professional accountant in business, i.e., the professional accountant employed by the organisation, the assurance practitioner needs to be aware of and consider this part also. References within this part to the “employing organisation” are, therefore, appropriate within this context. The intent of incorporating Part 2 into Professional and Ethical Standard 1 is to make it clear to assurance practitioners that this is a part of the Code that they need to be aware of and consider if faced with an ethical situation to which Part 2 relates.
13. The mandate of the NZAuASB, includes issuing of professional and ethical standards that govern the professional conduct of audit or assurance practitioners. As such, Part 2 of the International Code applies only to assurance practitioners when performing professional activities pursuant to the assurance practitioner’s relationship with the firm, whether as a contractor, employee or owner. The NZAuASB does not have the mandate to impose ethical requirements on professional accountants in business.
14. Paragraph NZ 200.4 is included to explain the context in which Part 2 applies to assurance practitioners.

“In this Part, the term “assurance practitioner” refers to an individual who is an assurance practitioner when performing professional activities pursuant to the assurance practitioner’s relationship with the assurance practitioner’s firm, whether as a contractor, employee or owner. The provisions in Part 2 deal mainly with matters that are relevant to professional activities that occur internally within the employing organisation. A number of the provisions may be less relevant to an assurance practitioner. The assurance practitioner uses professional judgement when determining which of those provisions are relevant to the assurance practitioner. More information on when Part 2 is applicable to assurance practitioners is set out in paragraphs R120.4, R300.5 and 300.5A1.

15. We believe paragraph NZ 200.4 clearly conveys the context in which Part 2 applies to assurance practitioners, i.e., to assurance practitioners when performing professional activities pursuant to their relationship with their firm.
16. It is our understanding that Part 2 is intended to apply to “professional activities, other than assurance services.”
17. “Professional activity” is defined in the Glossary to Professional and Ethical Standard 1 as, “an activity requiring accountancy or related skills undertaken by an assurance practitioner, including accounting, **auditing**, tax, management consulting, and financial management.” [emphasis added]

18. We therefore disagree that Part 2 is intended to apply to professional activities other than assurance services. Rather, the assurance practitioner is required to consider the context in which the issue has arisen or might arise, and when performing professional activities pursuant to the assurance practitioner's relationship with the firm, whether as a contractor, employee or owner, comply with the provisions of Part 2 that apply to the circumstances³.

19. We noted two matters that may need to be reconsidered under paragraph 300.5 A1. That paragraph states:

Examples of situations in which the provisions in Part 2 apply to an assurance practitioner include:

- Preparing or presenting financial information for the assurance practitioner's client or firm. The requirements and application material set out in Section 220 apply in these circumstances.

In our view the reference to the assurance practitioner's "client" is problematic.

The reference to "client" presumably refers to "assurance client", "audit client" or "review client". PES 1 already contain provisions that effectively prohibit an assurance practitioner from preparing or presenting financial information for a "client". It seems inappropriate to suggest this is a possibility.

- Facing pressure from an engagement partner to report chargeable hours inaccurately for a client engagement. The requirements and application material set out in Section 270 apply in these circumstances.

The cited example of pressure from an engagement partner to report chargeable hours inaccurately for a client engagement seems to miss the mark to some extent. Although it is undesirable behaviour, we're not necessarily convinced this is always a breach of PES 1. It depends on where the chargeable hours were re-allocated. If they were charged to a different client then that could be a problem. If the hours were charged to on-the-job training or some administration code then that may fall within firm policy.

In addition, this example is not included in Section 270. This raises an internal inconsistency within PES 1.

20. These examples appear in extant Professional and Ethical Standard 1. The consequential change to these paragraphs is to add the reference to the applicable sections in Part 2.

21. We disagree with the notion that the example citing pressure from an engagement partner to report chargeable hours inaccurately for a client engagement misses the mark. Key concepts in this example are (1) the pressure exerted by a more senior member of the firm and (2) the

³ Proposed Consequential amendments to the Code, paragraphs R120.4 and R300.5

intent to inaccurately report hours. The Financial Reporting Council, UK, recently announced sanctions against an engagement partner for a similar scenario⁴.

22. We further disagree that there is an internal inconsistency within Professional and Ethical Standard 1 arising from this example. The purpose of the guidance in paragraph 300.5 A1 is to provide examples of situations to which the provisions in Part 2 might apply. Section 270 addresses *Pressure to Breach the Fundamental Principles*. There are no equivalent provisions in Part 3.

23. Overall, we do not consider that we need to make any changes based on the submission.

24. Does the Board agree?

Matters to Consider

25. The Board is asked to:

- APPROVE *Amendments to PES 1: Part 2 – Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm*, including consequential amendments
- APPROVE the draft signing memorandum

Material Presented

Agenda item 6.1	Board Meeting Summary Paper
Agenda item 6.2	OAG submission
Agenda item 6.3	Amendments to PES 1: Part 2
Agenda item 6.4	Draft signing memorandum

⁴ [FRC announces sanctions against Audit Engagement Partner](#)



20 July 2020

File Ref: AU/APS/2-0002
AU/APS/6-0012

April Mackenzie
Chief Executive
External Reporting Board
PO Box 11-250
Manners Street Central
WELLINGTON 6142

Dear April

EXPOSURE DRAFT NZAuASB 2020-1 - PROPOSED AMENDMENTS TO PES 1: PART 2, ASSURANCE PRACTITIONERS PERFORMING PROFESSIONAL ACTIVITIES PURSUANT TO THEIR RELATIONSHIP WITH THE FIRM

Thank you for providing the opportunity to comment on *Exposure Draft NZAuASB 2020-1 - Proposed Amendments to PES 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to their Relationship with the Firm* (the Exposure Draft).

Our understanding of the purpose of the Exposure Draft

We understand the purpose of the proposed amendment to PES 1 is to remind assurance practitioners, who have a relationship with a firm, of their obligation to comply with all of the requirements of the Code of Ethics.

If our understanding is correct, we would conclude that Part 2 of the Code of Ethics will not apply to assurance practitioners who do not have a relationship with a firm.

Some observations

“Firm” versus “employing organisation”

We note that “Firm” is defined in PES 1 as:

- (a) *“A sole practitioner, partnership or corporation undertaking assurance engagements;*
- (b) *An entity that controls such parties, through ownership, management or other means; and*
- (c) *An entity controlled by such parties, through ownership, management or other means.”*

We note, in accordance with paragraph 200.3, that an assurance practitioner who performs professional activities pursuant to their relationship with a firm might be an employee, contractor, partner, director (executive or non-executive), owner-manager, or a volunteer of an **employing organisation**.

We would observe that, for the purposes of the Exposure Draft, the firm may not be the employing organisation but that an individual may be an assurance practitioner who has a relationship with a firm. This situation would apply, for example, when an assurance practitioner is engaged to carry out assurance services for a firm as a contractor to the firm. It would appear, in accordance with

paragraph 200.1, that an assurance practitioner's relationship with the firm is the "condition" that triggers the application of Part 2 of the Code.

We are not sure if the reference to **employing organisation** in paragraph 200.3, and many other paragraphs in the Exposure Draft, is deliberate. If this reference is deliberate it creates confusion as to whether the Exposure Draft is concerned with:

- an assurance practitioner in their relationship with a firm; or
- an assurance practitioner in their relationship to their employing organisation; or
- both.

"Professional activity" versus "assurance services"

We note that "professional activity" is defined as:

"An activity requiring accountancy or related skills undertaken by an assurance practitioner, including accounting, auditing, tax, management consulting, and financial management."

Assurance services *"comprise of any assurance engagements performed by an assurance practitioner"*.

It is our understanding that Part 2 is intended to apply to "professional activities, other than assurance services".

Consequential amendment – paragraph 300.5 A1

We noted two matters that may need to be reconsidered under paragraph 300.5 A1. That paragraph states:

Examples of situations in which the provisions in Part 2 apply to an assurance practitioner include:

- Preparing or presenting financial information for the assurance practitioner's client or firm. The requirements and application material set out in Section 220 apply in these circumstances.

In our view the reference to the assurance practitioner's "client" is problematic.

The reference to "client" presumably refers to "assurance client", "audit client" or "review client". PES 1 already contain provisions that effectively prohibit an assurance practitioner from preparing or presenting financial information for a "client". It seems inappropriate to suggest this is a possibility.

- Facing pressure from an engagement partner to report chargeable hours inaccurately for a client engagement. The requirements and application material set out in Section 270 apply in these circumstances.

The cited example of pressure from an engagement partner to report chargeable hours inaccurately for a client engagement seems to miss the mark to some extent. Although it is undesirable behaviour, we're not necessarily convinced this is always a breach of PES 1. It depends on where the chargeable hours were re-allocated. If they were charged to a different client then that could be a problem. If the hours were charged to on-the-job training or some administration code then that may fall within firm policy.

In addition, this example is not included in Section 270. This raises an internal inconsistency within PES 1.

If you have any questions about our submission please contact Roy Glass at roy.glass@oag.parliament.nz or myself at todd.beardsworth@oag.parliament.nz.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'T. Beardsworth', with a long horizontal flourish extending to the right.

Todd Beardsworth
Assistant Auditor-General
Audit Quality Group



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

AMENDMENTS TO PROFESSIONAL AND ETHICAL STANDARD 1: PART 2, ASSURANCE PRACTITIONERS PERFORMING PROFESSIONAL ACTIVITIES PURSUANT TO THEIR RELATIONSHIP WITH THE FIRM

This Standard was issued on **xx September** 2020 by the New Zealand Auditing and Assurance Standards Board of the External Reporting Board pursuant to section 12(b) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on **[date]**.

The amendments in this Standard are effective on 15 December 2020. Early adoption is permitted.

In finalising this Standard, the New Zealand Auditing and Assurance Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to incorporate Part 2 of the International Code of Ethics for Professional Accountants, including International Independence Standards, into Professional and Ethical Standard 1.

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PART 2 – ASSURANCE PRACTITIONERS PERFORMING PROFESSIONAL ACTIVITIES PURSUANT TO THEIR RELATIONSHIP WITH THE FIRM

SECTION 200

APPLYING THE CONCEPTUAL FRAMEWORK – ASSURANCE PRACTITIONERS PERFORMING PROFESSIONAL ACTIVITIES PURSUANT TO THEIR RELATIONSHIP WITH THE FIRM.

Introduction

- 200.1 This Part of the Code sets out requirements and application material for assurance practitioners, performing professional activities pursuant to their relationship with the firm, when applying the conceptual framework set out in Section 120. It does not describe all of the facts and circumstances, including professional activities, interests and relationships, that could be encountered by assurance practitioners, which create or might create threats to compliance with the fundamental principles. Therefore, the conceptual framework requires assurance practitioners to be alert for such facts and circumstances.
- 200.2 Investors, creditors, employing organisations and other sectors of the business community, as well as governments and the general public, might rely on the work of assurance practitioners. Assurance practitioners might be solely or jointly responsible for the preparation and reporting of financial and other information, on which both their employing organisations and third parties might rely. They might also be responsible for providing effective financial management and competent advice on a variety of business-related matters.
- 200.3 An assurance practitioner might be an employee, contractor, partner, director (executive or non-executive), owner-manager, or volunteer of an employing organisation. The legal form of the relationship of the assurance practitioner with the employing organisation has no bearing on the ethical responsibilities placed on the assurance practitioner.
- 200.4 *[Amended by the NZAuASB]*
- NZ 200.4 In this Part, the term “assurance practitioner” refers to an individual who is an assurance practitioner when performing professional activities pursuant to the assurance practitioner’s relationship with the assurance practitioner’s firm, whether as a contractor, employee or owner. The provisions in Part 2 deal mainly with matters that are relevant to professional activities that occur internally within the employing organisation. A number of those provisions may be less relevant to an assurance practitioner. The assurance practitioner uses professional judgement when determining which of those provisions are relevant to the assurance practitioner. More information on when Part 2 is applicable to assurance practitioners is set out in paragraphs R120.4, R300.5 and 300.5 A1.

Requirements and Application Material

General

- R200.5** An assurance practitioner shall comply with the fundamental principles set out in Section 110 and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to compliance with the fundamental principles.
- 200.5 A1 An assurance practitioner has a responsibility to further the legitimate objectives of the assurance practitioner's employing organisation. The Code does not seek to hinder assurance practitioners from fulfilling that responsibility, but addresses circumstances in which compliance with the fundamental principles might be compromised.
- 200.5 A2 Assurance practitioners may promote the position of the employing organisation when furthering the legitimate goals and objectives of their employing organisation, provided that any statements made are neither false nor misleading. Such actions usually would not create an advocacy threat.
- 200.5 A3 The more senior the position of an assurance practitioner, the greater will be the ability and opportunity to access information, and to influence policies, decisions made and actions taken by others involved with the employing organisation. To the extent that they are able to do so, taking into account their position and seniority in the organisation, assurance practitioners are expected to encourage and promote an ethics-based culture in the organisation. Examples of actions that might be taken include the introduction, implementation and oversight of:
- Ethics education and training programs.
 - Ethics and whistle-blowing policies.
 - Policies and procedures designed to prevent non-compliance with laws and regulations.

Identifying Threats

- 200.6 A1 Threats to compliance with the fundamental principles might be created by a broad range of facts and circumstances. The categories of threats are described in paragraph 120.6 A3. The following are examples of facts and circumstances within each of those categories that might create threats for an assurance practitioner when undertaking a professional activity:
- (a) Self-interest Threats
- An assurance practitioner holding a financial interest in, or receiving a loan or guarantee from, the employing organisation.
 - An assurance practitioner participating in incentive compensation arrangements offered by the employing organisation.
 - An assurance practitioner having access to corporate assets for personal use.
 - An assurance practitioner being offered a gift or special treatment from a supplier of the employing organisation.

- (b) Self-review Threats
 - An assurance practitioner determining the appropriate accounting treatment for a business combination after performing the feasibility study supporting the purchase decision.
- (c) Advocacy Threats
 - An assurance practitioner having the opportunity to manipulate information in a prospectus in order to obtain favourable financing.
- (d) Familiarity Threats
 - An assurance practitioner being responsible for the financial reporting of the employing organisation when an immediate or close family member employed by the organisation makes decisions that affect the financial reporting of the organisation.
 - An assurance practitioner having a long association with individuals influencing business decisions.
- (e) Intimidation Threats
 - An assurance practitioner or immediate or close family member facing the threat of dismissal or replacement over a disagreement about:
 - The application of an accounting principle.
 - The way in which financial information is to be reported.
 - An individual attempting to influence the decision-making process of the assurance practitioner, for example with regard to the awarding of contracts or the application of an accounting principle.

Evaluating Threats

- 200.7 A1 The conditions, policies and procedures described in paragraphs 120.6 A1 and 120.8 A2 might impact the evaluation of whether a threat to compliance with the fundamental principles is at an acceptable level.
- 200.7 A2 The assurance practitioner's evaluation of the level of a threat is also impacted by the nature and scope of the professional activity.
- 200.7 A3 The assurance practitioner's evaluation of the level of a threat might be impacted by the work environment within the employing organisation and its operating environment. For example:
- Leadership that stresses the importance of ethical behaviour and the expectation that employees will act in an ethical manner.
 - Policies and procedures to empower and encourage employees to communicate ethics issues that concern them to senior levels of management without fear of retribution.
 - Policies and procedures to implement and monitor the quality of employee performance.

- Systems of corporate oversight or other oversight structures and strong internal controls.
- Recruitment procedures emphasising the importance of employing high calibre competent personnel.
- Timely communication of policies and procedures, including any changes to them, to all employees, and appropriate training and education on such policies and procedures.
- Ethics and code of conduct policies.

200.7 A4 Assurance practitioners might consider obtaining legal advice where they believe that unethical behaviour or actions by others have occurred, or will continue to occur, within the employing organisation.

Addressing Threats

200.8 A1 Sections 210 to 270 describe certain threats that might arise during the course of performing professional activities and include examples of actions that might address such threats.

200.8 A2 In extreme situations, if the circumstances that created the threats cannot be eliminated and safeguards are not available or capable of being applied to reduce the threat to an acceptable level, it might be appropriate for an assurance practitioner to resign from the employing organisation.

Communicating with Those Charged with Governance

R200.9 When communicating with those charged with governance in accordance with the Code, an assurance practitioner shall determine the appropriate individual(s) within the employing organisation's governance structure with whom to communicate. If the assurance practitioner communicates with a subgroup of those charged with governance, the assurance practitioner shall determine whether communication with all of those charged with governance is also necessary so that they are adequately informed.

200.9 A1 In determining with whom to communicate, an assurance practitioner might consider:

- (a) The nature and importance of the circumstances; and
- (b) The matter to be communicated.

200.9 A2 Examples of a subgroup of those charged with governance include an audit committee or an individual member of those charged with governance.

R200.10 If an assurance practitioner communicates with individuals who have management responsibilities as well as governance responsibilities, the assurance practitioner shall be satisfied that communication with those individuals adequately informs all of those in a governance role with whom the assurance practitioner would otherwise communicate.

200.10 A1 In some circumstances, all of those charged with governance are involved in managing the employing organisation, for example, a small business where a single owner

manages the organisation and no one else has a governance role. In these cases, if matters are communicated with individual(s) with management responsibilities, and those individual(s) also have governance responsibilities, the assurance practitioner has satisfied the requirement to communicate with those charged with governance.

SECTION 210

CONFLICTS OF INTEREST

Introduction

- 210.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 210.2 A conflict of interest creates threats to compliance with the principle of objectivity and might create threats to compliance with the other fundamental principles. Such threats might be created when:
- (a) An assurance practitioner undertakes a professional activity related to a particular matter for two or more parties whose interests with respect to that matter are in conflict; or
 - (b) The interest of an assurance practitioner with respect to a particular matter and the interests of a party for whom the assurance practitioner undertakes a professional activity related to that matter are in conflict.
- A party might include an employing organisation, a vendor, a customer, a lender, a shareholder, or another party.
- 210.3 This section sets out specific requirements and application material relevant to applying the conceptual framework to conflicts of interest.

Requirements and Application Material

General

- R210.4** An assurance practitioner shall not allow a conflict of interest to compromise professional or business judgement.
- 210.4 A1 Examples of circumstances that might create a conflict of interest include:
- Serving in a management or governance position for two employing organisations and acquiring confidential information from one organisation that might be used by the assurance practitioner to the advantage or disadvantage of the other organisation.
 - Undertaking a professional activity for each of two parties in a partnership, where both parties are employing the assurance practitioner to assist them to dissolve their partnership.
 - Preparing financial information for certain members of management of the assurance practitioner's employing organisation who are seeking to undertake a management buy-out.
 - Being responsible for selecting a vendor for the employing organisation when an immediate family member of the assurance practitioner might benefit financially from the transaction.
 - Serving in a governance capacity in an employing organisation that is approving certain investments for the company where one of those investments will increase

the value of the investment portfolio of the assurance practitioner or an immediate family member.

Conflict Identification

R210.5 An assurance practitioner shall take reasonable steps to identify circumstances that might create a conflict of interest, and therefore a threat to compliance with one or more of the fundamental principles. Such steps shall include identifying:

- (a) The nature of the relevant interests and relationships between the parties involved; and
- (b) The activity and its implication for relevant parties.

R210.6 An assurance practitioner shall remain alert to changes over time in the nature of the activities, interests and relationships that might create a conflict of interest while performing a professional activity.

Threats Created by Conflicts of Interest

210.7 A1 In general, the more direct the connection between the professional activity and the matter on which the parties' interests conflict, the more likely the level of the threat is not at an acceptable level.

210.7 A2 An example of an action that might eliminate threats created by conflicts of interest is withdrawing from the decision-making process related to the matter giving rise to the conflict of interest.

210.7 A3 Examples of actions that might be safeguards to address threats created by conflicts of interest include:

- Restructuring or segregating certain responsibilities and duties.
- Obtaining appropriate oversight, for example, acting under the supervision of an executive or non-executive director.

Disclosure and Consent

General

210.8 A1 It is generally necessary to:

- (a) Disclose the nature of the conflict of interest and how any threats created were addressed to the relevant parties, including to the appropriate levels within the employing organisation affected by a conflict; and
- (b) Obtain consent from the relevant parties for the assurance practitioner to undertake the professional activity when safeguards are applied to address the threat.

210.8 A2 Consent might be implied by a party's conduct in circumstances where the assurance practitioner has sufficient evidence to conclude that the parties know the circumstances at the outset and have accepted the conflict of interest if they do not raise an objection to the existence of the conflict.

210.8 A3 If such disclosure or consent is not in writing, the assurance practitioner is encouraged to document:

- (a) The nature of the circumstances giving rise to the conflict of interest;
- (b) The safeguards applied to address the threats when applicable; and
- (c) The consent obtained.

Other Considerations

210.9 A1 When addressing a conflict of interest, the assurance practitioner is encouraged to seek guidance from within the employing organisation or from others, such as a professional body, legal counsel or another assurance practitioner. When making such disclosures or sharing information within the employing organisation and seeking guidance of third parties, the principle of confidentiality applies.

SECTION 220

PREPARATION AND PRESENTATION OF INFORMATION

Introduction

- 220.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 220.2 Preparing or presenting information might create a self-interest, intimidation or other threats to compliance with one or more of the fundamental principles. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 220.3 A1 Assurance practitioners at all levels in an employing organisation are involved in the preparation or presentation of information both within and outside the organisation.
- 220.3 A2 Stakeholders to whom, or for whom, such information is prepared or presented, include:
- Management and those charged with governance.
 - Investors and lenders or other creditors.
 - Regulatory bodies.

This information might assist stakeholders in understanding and evaluating aspects of the employing organisation's state of affairs and in making decisions concerning the organisation. Information can include financial and non-financial information that might be made public or used for internal purposes.

Examples include:

- Operating and performance reports.
 - Decision support analyses.
 - Budgets and forecasts.
 - Information provided to the internal and external auditors.
 - Risk analyses.
 - General and special purpose financial statements.
 - Tax returns.
 - Reports filed with regulatory bodies for legal and compliance purposes.
- 220.3 A3 For the purposes of this section, preparing or presenting information includes recording, maintaining and approving information.

R220.4 When preparing or presenting information, an assurance practitioner shall:

- (a) Prepare or present the information in accordance with a relevant reporting framework, where applicable;
- (b) Prepare or present the information in a manner that is intended neither to mislead nor to influence contractual or regulatory outcomes inappropriately;
- (c) Exercise professional judgement to:
 - (i) Represent the facts accurately and completely in all material respects;
 - (ii) Describe clearly the true nature of business transactions or activities; and
 - (iii) Classify and record information in a timely and proper manner; and
- (d) Not omit anything with the intention of rendering the information misleading or of influencing contractual or regulatory outcomes inappropriately.

220.4 A1 An example of influencing a contractual or regulatory outcome inappropriately is using an unrealistic estimate with the intention of avoiding violation of a contractual requirement such as a debt covenant or of a regulatory requirement such as a capital requirement for a financial institution.

Use of Discretion in Preparing or Presenting Information

R220.5 Preparing or presenting information might require the exercise of discretion in making professional judgements. The assurance practitioner shall not exercise such discretion with the intention of misleading others or influencing contractual or regulatory outcomes inappropriately.

220.5 A1 Examples of ways in which discretion might be misused to achieve inappropriate outcomes include:

- Determining estimates, for example, determining fair value estimates in order to misrepresent profit or loss.
- Selecting or changing an accounting policy or method among two or more alternatives permitted under the applicable financial reporting framework, for example, selecting a policy for accounting for long-term contracts in order to misrepresent profit or loss.
- Determining the timing of transactions, for example, timing the sale of an asset near the end of the fiscal year in order to mislead.
- Determining the structuring of transactions, for example, structuring financing transactions in order to misrepresent assets and liabilities or classification of cash flows.
- Selecting disclosures, for example, omitting or obscuring information relating to financial or operating risk in order to mislead.

R220.6 When performing professional activities, especially those that do not require compliance with a relevant reporting framework, the assurance practitioner shall exercise professional judgement to identify and consider:

- (a) The purpose for which the information is to be used;

- (b) The context within which it is given; and
- (c) The audience to whom it is addressed.

220.6 A1 For example, when preparing or presenting pro forma reports, budgets or forecasts, the inclusion of relevant estimates, approximations and assumptions, where appropriate, would enable those who might rely on such information to form their own judgements.

220.6 A2 The assurance practitioner might also consider clarifying the intended audience, context and purpose of the information to be presented.

Relying on the Work of Others

R220.7 An assurance practitioner who intends to rely on the work of others, either internal or external to the employing organisation, shall exercise professional judgement to determine what steps to take, if any, in order to fulfil the responsibilities set out in paragraph R220.4.

220.7 A1 Factors to consider in determining whether reliance on others is reasonable include:

- The reputation and expertise of, and resources available to, the other individual or organisation.
- Whether the other individual is subject to applicable professional and ethics standards.

Such information might be gained from prior association with, or from consulting others about, the other individual or organisation.

Addressing Information that Is or Might be Misleading

R220.8 When the assurance practitioner knows or has reason to believe that the information with which the assurance practitioner is associated is misleading, the assurance practitioner shall take appropriate actions to seek to resolve the matter.

220.8 A1 Actions that might be appropriate include:

- Discussing concerns that the information is misleading with the assurance practitioner's superior and/or the appropriate level(s) of management within the assurance practitioner's employing organisation or those charged with governance, and requesting such individuals to take appropriate action to resolve the matter. Such action might include:
 - Having the information corrected.
 - If the information has already been disclosed to the intended users, informing them of the correct information.
- Consulting the policies and procedures of the employing organisation (for example, an ethics or whistle-blowing policy) regarding how to address such matters internally.

220.8 A2 The assurance practitioner might determine that the employing organisation has not taken appropriate action. If the assurance practitioner continues to have reason to believe that the information is misleading, the following further actions might be

appropriate provided that the assurance practitioner remains alert to the principle of confidentiality:

- Consulting with:
 - A relevant professional body.
 - The internal or external auditor of the employing organisation.
 - Legal counsel.
- Determining whether any requirements exist to communicate to:
 - Third parties, including users of the information.
 - Regulatory and oversight authorities.

R220.9 If after exhausting all feasible options, the assurance practitioner determines that appropriate action has not been taken and there is reason to believe that the information is still misleading, the assurance practitioner shall refuse to be or to remain associated with the information.

220.9 A1 In such circumstances, it might be appropriate for an assurance practitioner to resign from the employing organisation.

Documentation

220.10 A1 The assurance practitioner is encouraged to document:

- The facts.
- The accounting principles or other relevant professional standards involved.
- The communications and parties with whom matters were discussed.
- The courses of action considered.
- How the assurance practitioner attempted to address the matter(s).

Other Considerations

220.11 A1 Where threats to compliance with the fundamental principles relating to the preparation or presentation of information arise from a financial interest, including compensation and incentives linked to financial reporting and decision making, the requirements and application material set out in Section 240 apply.

220.11 A2 Where the misleading information might involve non-compliance with laws and regulations, the requirements and application material set out in Section 260 apply.

220.11 A3 Where threats to compliance with the fundamental principles relating to the preparation or presentation of information arise from pressure, the requirements and application material set out in Section 270 apply.

SECTION 230

ACTING WITH SUFFICIENT EXPERTISE

Introduction

- 230.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 230.2 Acting without sufficient expertise creates a self-interest threat to compliance with the principle of professional competence and due care. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- R230.3** An assurance practitioner shall not intentionally mislead an employing organisation as to the level of expertise or experience possessed.
- 230.3 A1 The principle of professional competence and due care requires that an assurance practitioner only undertake significant tasks for which the assurance practitioner has, or can obtain, sufficient training or experience.
- 230.3 A2 A self-interest threat to compliance with the principle of professional competence and due care might be created if an assurance practitioner has:
- Insufficient time for performing or completing the relevant duties.
 - Incomplete, restricted or otherwise inadequate information for performing the duties.
 - Insufficient experience, training and/or education.
 - Inadequate resources for the performance of the duties.
- 230.3 A3 Factors that are relevant in evaluating the level of such a threat include:
- The extent to which the assurance practitioner is working with others.
 - The relative seniority of the assurance practitioner in the business.
 - The level of supervision and review applied to the work.
- 230.3 A4 Examples of actions that might be safeguards to address such a self-interest threat include:
- Obtaining assistance or training from someone with the necessary expertise.
 - Ensuring that there is adequate time available for performing the relevant duties.
- R230.4** If a threat to compliance with the principle of professional competence and due care cannot be addressed, an assurance practitioner shall determine whether to decline to perform the duties in question. If the assurance practitioner determines that declining is appropriate, the assurance practitioner shall communicate the reasons.

Other Considerations

230.5 A1 The requirements and application material in Section 270 apply when an assurance practitioner is pressured to act in a manner that might lead to a breach of the principle of professional competence and due care.

SECTION 240

FINANCIAL INTERESTS, COMPENSATION AND INCENTIVES LINKED TO FINANCIAL REPORTING AND DECISION MAKING

Introduction

- 240.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 240.2 Having a financial interest, or knowing of a financial interest held by an immediate or close family member might create a self-interest threat to compliance with the principles of objectivity or confidentiality. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- R240.3** An assurance practitioner shall not manipulate information or use confidential information for personal gain or for the financial gain of others.
- 240.3 A1 Assurance practitioners might have financial interests or might know of financial interests of immediate or close family members that, in certain circumstances, might create threats to compliance with the fundamental principles. Financial interests include those arising from compensation or incentive arrangements linked to financial reporting and decision making.
- 240.3 A2 Examples of circumstances that might create a self-interest threat include situations in which the assurance practitioner or an immediate or close family member:
- Has a motive and opportunity to manipulate price-sensitive information in order to gain financially.
 - Holds a direct or indirect financial interest in the employing organisation and the value of that financial interest might be directly affected by decisions made by the assurance practitioner.
 - Is eligible for a profit-related bonus and the value of that bonus might be directly affected by decisions made by the assurance practitioner.
 - Holds, directly or indirectly, deferred bonus share rights or share options in the employing organisation, the value of which might be affected by decisions made by the assurance practitioner.
 - Participates in compensation arrangements which provide incentives to achieve targets or to support efforts to maximise the value of the employing organisation's shares. An example of such an arrangement might be through participation in incentive plans which are linked to certain performance conditions being met.

240.3 A3 Factors that are relevant in evaluating the level of such a threat include:

- The significance of the financial interest. What constitutes a significant financial interest will depend on personal circumstances and the materiality of the financial interest to the individual.
- Policies and procedures for a committee independent of management to determine the level or form of senior management remuneration.
- In accordance with any internal policies, disclosure to those charged with governance of:
 - All relevant interests.
 - Any plans to exercise entitlements or trade in relevant shares.
- Internal and external audit procedures that are specific to address issues that give rise to the financial interest.

240.3 A4 Threats created by compensation or incentive arrangements might be compounded by explicit or implicit pressure from superiors or colleagues. See Section 270, *Pressure to Breach the Fundamental Principles*.

SECTION 250

INDUCEMENTS, INCLUDING GIFTS AND HOSPITALITY

Introduction

- 250.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 250.2 Offering or accepting inducements might create a self-interest, familiarity or intimidation threat to compliance with the fundamental principles, particularly the principles of integrity, objectivity and professional behaviour.
- 250.3 This section sets out requirements and application material relevant to applying the conceptual framework in relation to the offering and accepting of inducements when undertaking professional activities that does not constitute non-compliance with laws and regulations. This section also requires an assurance practitioner to comply with relevant laws and regulations when offering or accepting inducements.

Requirements and Application Material

General

- 250.4 A1 An inducement is an object, situation, or action that is used as a means to influence another individual's behaviour, but not necessarily with the intent to improperly influence that individual's behaviour. Inducements can range from minor acts of hospitality between business colleagues to acts that result in non-compliance with laws and regulations. An inducement can take many different forms, for example:
- Gifts.
 - Hospitality.
 - Entertainment.
 - Political or charitable donations.
 - Appeals to friendship and loyalty.
 - Employment or other commercial opportunities.
 - Preferential treatment, rights or privileges.

Inducements Prohibited by Laws and Regulations

- R250.5** In many jurisdictions, there are laws and regulations, such as those related to bribery and corruption, that prohibit the offering or accepting of inducements in certain circumstances. The assurance practitioner shall obtain an understanding of relevant laws and regulations and comply with them when the assurance practitioner encounters such circumstances.

Inducements Not Prohibited by Laws and Regulations

250.6 A1 The offering or accepting of inducements that is not prohibited by laws and regulations might still create threats to compliance with the fundamental principles.

Inducements with Intent to Improperly Influence Behaviour

R250.7 An assurance practitioner shall not offer, or encourage others to offer, any inducement that is made, or which the assurance practitioner considers a reasonable and informed third party would be likely to conclude is made, with the intent to improperly influence the behaviour of the recipient or of another individual.

R250.8 An assurance practitioner shall not accept, or encourage others to accept, any inducement that the assurance practitioner concludes is made, or considers a reasonable and informed third party would be likely to conclude is made, with the intent to improperly influence the behaviour of the recipient or of another individual.

250.9 A1 An inducement is considered as improperly influencing an individual's behaviour if it causes the individual to act in an unethical manner. Such improper influence can be directed either towards the recipient or towards another individual who has some relationship with the recipient. The fundamental principles are an appropriate frame of reference for an assurance practitioner in considering what constitutes unethical behaviour on the part of the assurance practitioner and, if necessary by analogy, other individuals.

250.9 A2 A breach of the fundamental principle of integrity arises when an assurance practitioner offers or accepts, or encourages others to offer or accept, an inducement where the intent is to improperly influence the behaviour of the recipient or of another individual.

250.9 A3 The determination of whether there is actual or perceived intent to improperly influence behaviour requires the exercise of professional judgement. Relevant factors to consider might include:

- The nature, frequency, value and cumulative effect of the inducement.
- Timing of when the inducement is offered relative to any action or decision that it might influence.
- Whether the inducement is a customary or cultural practice in the circumstances, for example, offering a gift on the occasion of a religious holiday or wedding.
- Whether the inducement is an ancillary part of a professional activity, for example, offering or accepting lunch in connection with a business meeting.
- Whether the offer of the inducement is limited to an individual recipient or available to a broader group. The broader group might be internal or external to the employing organisation, such as other customers or vendors.
- The roles and positions of the individuals offering or being offered the inducement.
- Whether the assurance practitioner knows, or has reason to believe, that accepting the inducement would breach the policies and procedures of the counterparty's employing organisation.

- The degree of transparency with which the inducement is offered.
- Whether the inducement was required or requested by the recipient.
- The known previous behaviour or reputation of the offeror.

Consideration of Further Actions

250.10 A1 If the assurance practitioner becomes aware of an inducement offered with actual or perceived intent to improperly influence behaviour, threats to compliance with the fundamental principles might still be created even if the requirements in paragraphs R250.7 and R250.8 are met.

250.10 A2 Examples of actions that might be safeguards to address such threats include:

- Informing senior management or those charged with governance of the employing organisation of the assurance practitioner or the offeror regarding the offer.
- Amending or terminating the business relationship with the offeror.

Inducements with No Intent to Improperly Influence Behaviour

250.11 A1 The requirements and application material set out in the conceptual framework apply when an assurance practitioner has concluded there is no actual or perceived intent to improperly influence the behaviour of the recipient or of another individual.

250.11 A2 If such an inducement is trivial and inconsequential, any threats created will be at an acceptable level.

250.11 A3 Examples of circumstances where offering or accepting such an inducement might create threats even if the assurance practitioner has concluded there is no actual or perceived intent to improperly influence behaviour include:

- Self-interest threats
 - An assurance practitioner is offered part-time employment by a vendor.
- Familiarity threats
 - An assurance practitioner regularly takes a customer or supplier to sporting events.
- Intimidation threats
 - An assurance practitioner accepts hospitality, the nature of which could be perceived to be inappropriate were it to be publicly disclosed.

250.11 A4 Relevant factors in evaluating the level of such threats created by offering or accepting such an inducement include the same factors set out in paragraph 250.9 A3 for determining intent.

250.11 A5 Examples of actions that might eliminate threats created by offering or accepting such an inducement include:

- Declining or not offering the inducement.

- Transferring responsibility for any business-related decision involving the counterparty to another individual who the assurance practitioner has no reason to believe would be, or would be perceived to be, improperly influenced in making the decision.

250.11 A6 Examples of actions that might be safeguards to address such threats created by offering or accepting such an inducement include:

- Being transparent with senior management or those charged with governance of the employing organisation of the assurance practitioner or of the counterparty about offering or accepting an inducement.
- Registering the inducement in a log maintained by the employing organisation of the assurance practitioner or the counterparty.
- Having an appropriate reviewer, who is not otherwise involved in undertaking the professional activity, review any work performed or decisions made by the assurance practitioner with respect to the individual or organisation from which the assurance practitioner accepted the inducement.
- Donating the inducement to charity after receipt and appropriately disclosing the donation, for example, to those charged with governance or the individual who offered the inducement.
- Reimbursing the cost of the inducement, such as hospitality, received.
- As soon as possible, returning the inducement, such as a gift, after it was initially accepted.

Immediate or Close Family Members

R250.12 An assurance practitioner shall remain alert to potential threats to the assurance practitioner's compliance with the fundamental principles created by the offering of an inducement:

- (a) By an immediate or close family member of the assurance practitioner to a counterparty with whom the assurance practitioner has a professional relationship; or
- (b) To an immediate or close family member of the assurance practitioner by a counterparty with whom the assurance practitioner has a professional relationship.

R250.13 Where the assurance practitioner becomes aware of an inducement being offered to or made by an immediate or close family member and concludes there is intent to improperly influence the behaviour of the assurance practitioner or of the counterparty, or considers a reasonable and informed third party would be likely to conclude such intent exists, the assurance practitioner shall advise the immediate or close family member not to offer or accept the inducement.

250.13 A1 The factors set out in paragraph 250.9 A3 are relevant in determining whether there is actual or perceived intent to improperly influence the behaviour of the assurance

practitioner or of the counterparty. Another factor that is relevant is the nature or closeness of the relationship, between:

- (a) The assurance practitioner and the immediate or close family member;
- (b) The immediate or close family member and the counterparty; and
- (c) The assurance practitioner and the counterparty.

For example, the offer of employment, outside of the normal recruitment process, to the spouse of the assurance practitioner by a counterparty with whom the assurance practitioner is negotiating a significant contract might indicate such intent.

250.13 A2 The application material in paragraph 250.10 A2 is also relevant in addressing threats that might be created when there is actual or perceived intent to improperly influence the behaviour of the assurance practitioner or of the counterparty even if the immediate or close family member has followed the advice given pursuant to paragraph R250.13.

Application of the Conceptual Framework

250.14 A1 Where the assurance practitioner becomes aware of an inducement offered in the circumstances addressed in paragraph R250.12, threats to compliance with the fundamental principles might be created where:

- (a) The immediate or close family member offers or accepts the inducement contrary to the advice of the assurance practitioner pursuant to paragraph R250.13; or
- (b) The assurance practitioner does not have reason to believe an actual or perceived intent to improperly influence the behaviour of the assurance practitioner or of the counterparty exists.

250.14 A2 The application material in paragraphs 250.11 A1 to 250.11 A6 is relevant for the purposes of identifying, evaluating and addressing such threats. Factors that are relevant in evaluating the level of threats in these circumstances also include the nature or closeness of the relationships set out in paragraph 250.13 A1.

Other Considerations

250.15 A1 If an assurance practitioner is offered an inducement by the employing organisation relating to financial interests, compensation and incentives linked to performance, the requirements and application material set out in Section 240 apply.

250.15 A2 If an assurance practitioner encounters or is made aware of inducements that might result in non-compliance or suspected non-compliance with laws and regulations by other individuals working for or under the direction of the employing organisation, the requirements and application material set out in Section 260 apply.

250.15 A3 If an assurance practitioner faces pressure to offer or accept inducements that might create threats to compliance with the fundamental principles, the requirements and application material set out in Section 270 apply.

SECTION 260

RESPONDING TO NON-COMPLIANCE WITH LAWS AND REGULATIONS

Introduction

- 260.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 260.2 A self-interest or intimidation threat to compliance with the principles of integrity and professional behaviour is created when an assurance practitioner becomes aware of non-compliance or suspected non-compliance with laws and regulations.
- 260.3 An assurance practitioner might encounter or be made aware of non-compliance or suspected non-compliance in the course of carrying out professional activities. This section guides the assurance practitioner in assessing the implications of the matter and the possible courses of action when responding to non-compliance or suspected non-compliance with:
- (a) Laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the employing organisation's financial statements; and
 - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the employing organisation's financial statements, but compliance with which might be fundamental to the operating aspects of the employing organisation's business, to its ability to continue its business, or to avoid material penalties.

Objectives of the Assurance Practitioner in Relation to Non-compliance with Laws and Regulations

- 260.4 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. When responding to non-compliance or suspected non-compliance, the objectives of the assurance practitioner are:
- (a) To comply with the principles of integrity and professional behaviour;
 - (b) By alerting management or, where appropriate, those charged with governance of the employing organisation, to seek to:
 - (i) Enable them to rectify, remediate or mitigate the consequences of the identified or suspected non-compliance; or
 - (ii) Deter the non-compliance where it has not yet occurred; and
 - (c) To take such further action as appropriate in the public interest.

Requirements and Application Material

General

260.5 A1 Non-compliance with laws and regulations (“non-compliance”) comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:

- (a) The assurance practitioner’s employing organisation;
- (b) Those charged with governance of the employing organisation;
- (c) Management of the employing organisation; or
- (d) Other individuals working for or under the direction of the employing organisation.

260.5 A2 Examples of laws and regulations which this section addresses include those that deal with:

- Fraud, corruption and bribery.
- Money laundering, terrorist financing and proceeds of crime.
- Securities markets and trading.
- Banking and other financial products and services.
- Data protection.
- Tax and pension liabilities and payments.
- Environmental protection.
- Public health and safety.

260.5 A3 Non-compliance might result in fines, litigation or other consequences for the employing organisation, potentially materially affecting its financial statements. Importantly, such non-compliance might have wider public interest implications in terms of potentially substantial harm to investors, creditors, employees or the general public. For the purposes of this section, non-compliance that causes substantial harm is one that results in serious adverse consequences to any of these parties in financial or non-financial terms. Examples include the perpetration of a fraud resulting in significant financial losses to investors, and breaches of environmental laws and regulations endangering the health or safety of employees or the public.

R260.6 In some jurisdictions, there are legal or regulatory provisions governing how assurance practitioners are required to address non-compliance or suspected non-compliance. These legal or regulatory provisions might differ from or go beyond the provisions in this section. When encountering such non-compliance or suspected non-compliance, the assurance practitioner shall obtain an understanding of those legal or regulatory provisions and comply with them, including:

- (a) Any requirement to report the matter to an appropriate authority; and
- (b) Any prohibition on alerting the relevant party.

- 260.6 A1 A prohibition on alerting the relevant party might arise, for example, pursuant to anti-money laundering legislation.
- 260.7 A1 This section applies regardless of the nature of the employing organisation, including whether or not it is a public interest entity.
- 260.7 A2 An assurance practitioner who encounters or is made aware of matters that are clearly inconsequential is not required to comply with this section. Whether a matter is clearly inconsequential is to be judged with respect to its nature and its impact, financial or otherwise, on the employing organisation, its stakeholders and the general public.
- 260.7 A3 This section does not address:
- (a) Personal misconduct unrelated to the business activities of the employing organisation; and
 - (b) Non-compliance by parties other than those specified in paragraph 260.5 A1.
- The assurance practitioner might nevertheless find the guidance in this section helpful in considering how to respond in these situations.

Responsibilities of the Employing Organisation’s Management and Those Charged with Governance

- 260.8 A1 The employing organisation’s management, with the oversight of those charged with governance, is responsible for ensuring that the employing organisation’s business activities are conducted in accordance with laws and regulations. Management and those charged with governance are also responsible for identifying and addressing any non-compliance by:
- (a) The employing organisation;
 - (b) An individual charged with governance of the employing organisation;
 - (c) A member of management; or
 - (d) Other individuals working for or under the direction of the employing organisation.

Responsibilities of All Assurance Practitioners

- R260.9** If protocols and procedures exist within the assurance practitioner’s employing organisation to address non-compliance or suspected non-compliance, the assurance practitioner shall consider them in determining how to respond to such non-compliance.
- 260.9 A1 Many employing organisations have established protocols and procedures regarding how to raise non-compliance or suspected non-compliance internally. These protocols and procedures include, for example, an ethics policy or internal whistle-blowing mechanism. Such protocols and procedures might allow matters to be reported anonymously through designated channels.
- R260.10** Where an assurance practitioner becomes aware of a matter to which this section applies, the steps that the assurance practitioner takes to comply with this section shall

be taken on a timely basis. For the purpose of taking timely steps, the assurance practitioner shall have regard to the nature of the matter and the potential harm to the interests of the employing organisation, investors, creditors, employees or the general public.

Responsibilities of Senior Assurance Practitioners

260.11 A1 Senior assurance practitioners are directors, officers or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organisation's human, financial, technological, physical and intangible resources. There is a greater expectation for such individuals to take whatever action is appropriate in the public interest to respond to non-compliance or suspected non-compliance than other assurance practitioners within the employing organisation. This is because of senior assurance practitioners' roles, positions and spheres of influence within the employing organisation.

Obtaining an Understanding of the Matter

R260.12 If, in the course of carrying out professional activities, a senior assurance practitioner becomes aware of information concerning non-compliance or suspected non-compliance, the senior assurance practitioner shall obtain an understanding of the matter. This understanding shall include:

- (a) The nature of the non-compliance or suspected non-compliance and the circumstances in which it has occurred or might occur;
- (b) The application of the relevant laws and regulations to the circumstances; and
- (c) An assessment of the potential consequences to the employing organisation, investors, creditors, employees or the wider public.

260.12 A1 A senior assurance practitioner is expected to apply knowledge and expertise, and exercise professional judgement. However, the assurance practitioner is not expected to have a level of understanding of laws and regulations greater than that which is required for the assurance practitioner's role within the employing organisation. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

260.12 A2 Depending on the nature and significance of the matter, the senior assurance practitioner might cause, or take appropriate steps to cause, the matter to be investigated internally. The assurance practitioner might also consult on a confidential basis with others within the employing organisation or a professional body, or with legal counsel.

Addressing the Matter

R260.13 If the senior assurance practitioner identifies or suspects that non-compliance has occurred or might occur, the assurance practitioner shall, subject to paragraph R260.9, discuss the matter with the assurance practitioner's immediate superior, if any. If the assurance practitioner's immediate superior appears to be involved in the matter, the

assurance practitioner shall discuss the matter with the next higher level of authority within the employing organisation.

260.13 A1 The purpose of the discussion is to enable a determination to be made as to how to address the matter.

R260.14 The senior assurance practitioner shall also take appropriate steps to:

- (a) Have the matter communicated to those charged with governance;
- (b) Comply with applicable laws and regulations, including legal or regulatory provisions governing the reporting of non-compliance or suspected non-compliance to an appropriate authority;
- (c) Have the consequences of the non-compliance or suspected non-compliance rectified, remediated or mitigated;
- (d) Reduce the risk of re-occurrence; and
- (e) Seek to deter the commission of the non-compliance if it has not yet occurred.

260.14 A1 The purpose of communicating the matter to those charged with governance is to obtain their concurrence regarding appropriate actions to take to respond to the matter and to enable them to fulfil their responsibilities.

260.14 A2 Some laws and regulations might stipulate a period within which reports of non-compliance or suspected non-compliance are to be made to an appropriate authority.

R260.15 In addition to responding to the matter in accordance with the provisions of this section, the senior assurance practitioner shall determine whether disclosure of the matter to the employing organisation's external auditor, if any, is needed.

260.15 A1 Such disclosure would be pursuant to the senior assurance practitioner's duty or legal obligation to provide all information necessary to enable the auditor to perform the audit.

Determining Whether Further Action Is Needed

R260.16 The senior assurance practitioner shall assess the appropriateness of the response of the assurance practitioner's superiors, if any, and those charged with governance.

260.16 A1 Relevant factors to consider in assessing the appropriateness of the response of the senior assurance practitioner's superiors, if any, and those charged with governance include whether:

- The response is timely.
- They have taken or authorised appropriate action to seek to rectify, remediate or mitigate the consequences of the non-compliance, or to avert the non-compliance if it has not yet occurred.
- The matter has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.

R260.17 In light of the response of the senior assurance practitioner's superiors, if any, and those charged with governance, the assurance practitioner shall determine if further action is needed in the public interest.

260.17 A1 The determination of whether further action is needed, and the nature and extent of it, will depend on various factors, including:

- The legal and regulatory framework.
- The urgency of the situation.
- The pervasiveness of the matter throughout the employing organisation.
- Whether the senior assurance practitioner continues to have confidence in the integrity of the assurance practitioner's superiors and those charged with governance.
- Whether the non-compliance or suspected non-compliance is likely to recur.
- Whether there is credible evidence of actual or potential substantial harm to the interests of the employing organisation, investors, creditors, employees or the general public.

260.17 A2 Examples of circumstances that might cause the senior assurance practitioner no longer to have confidence in the integrity of the assurance practitioner's superiors and those charged with governance include situations where:

- The assurance practitioner suspects or has evidence of their involvement or intended involvement in any non-compliance.
- Contrary to legal or regulatory requirements, they have not reported, or authorised the reporting of, the matter to an appropriate authority within a reasonable period.

R260.18 The senior assurance practitioner shall exercise professional judgement in determining the need for, and nature and extent of, further action. In making this determination, the assurance practitioner shall take into account whether a reasonable and informed third party would be likely to conclude that the assurance practitioner has acted appropriately in the public interest.

260.18 A1 Further action that the senior assurance practitioner might take includes:

- Informing the management of the parent entity of the matter if the employing organisation is a member of a group.
- Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
- Resigning from the employing organisation.

260.18 A2 Resigning from the employing organisation is not a substitute for taking other actions that might be needed to achieve the senior assurance practitioner's objectives under this section. In some jurisdictions, however, there might be limitations as to the further actions available to the assurance practitioner. In such circumstances, resignation might be the only available course of action.

Seeking Advice

260.19 A1 As assessment of the matter might involve complex analysis and judgements, the senior assurance practitioner might consider:

- Consulting internally.
- Obtaining legal advice to understand the assurance practitioner's options and the professional or legal implications of taking any particular course of action.
- Consulting on a confidential basis with a regulatory or professional body.

Determining Whether to Disclose the Matter to an Appropriate Authority

260.20 A1 Disclosure of the matter to an appropriate authority would be precluded if doing so would be contrary to law or regulation. Otherwise, the purpose of making disclosure is to enable an appropriate authority to cause the matter to be investigated and action to be taken in the public interest.

260.20 A2 The determination of whether to make such a disclosure depends in particular on the nature and extent of the actual or potential harm that is or might be caused by the matter to investors, creditors, employees or the general public. For example, the senior assurance practitioner might determine that disclosure of the matter to an appropriate authority is an appropriate course of action if:

- The employing organisation is engaged in bribery (for example, of local or foreign government officials for purposes of securing large contracts).
- The employing organisation is regulated and the matter is of such significance as to threaten its license to operate.
- The employing organisation is listed on a securities exchange and the matter might result in adverse consequences to the fair and orderly market in the employing organisation's securities or pose a systemic risk to the financial markets.
- It is likely that the employing organisation would sell products that are harmful to public health or safety.
- The employing organisation is promoting a scheme to its clients to assist them in evading taxes.

260.20 A3 The determination of whether to make such a disclosure will also depend on external factors such as:

- Whether there is an appropriate authority that is able to receive the information, and cause the matter to be investigated and action to be taken. The appropriate authority will depend upon the nature of the matter. For example, the appropriate authority would be a securities regulator in the case of fraudulent financial reporting or an environmental protection agency in the case of a breach of environmental laws and regulations.
- Whether there exists robust and credible protection from civil, criminal or professional liability or retaliation afforded by legislation or regulation, such as under whistle-blowing legislation or regulation.

- Whether there are actual or potential threats to the physical safety of the senior assurance practitioner or other individuals.

R260.21 If the senior assurance practitioner determines that disclosure of the matter to an appropriate authority is an appropriate course of action in the circumstances, that disclosure is permitted pursuant to paragraph R114.1(d) of the Code. When making such disclosure, the assurance practitioner shall act in good faith and exercise caution when making statements and assertions.

Imminent Breach

R260.22 In exceptional circumstances, the senior assurance practitioner might become aware of actual or intended conduct that the assurance practitioner has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. Having first considered whether it would be appropriate to discuss the matter with management or those charged with governance of the employing organisation, the assurance practitioner shall exercise professional judgement and determine whether to disclose the matter immediately to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach. If disclosure is made, that disclosure is permitted pursuant to paragraph R114.1(d) of the Code.

Documentation

260.23 A1 In relation to non-compliance or suspected non-compliance that falls within the scope of this section, the senior assurance practitioner is encouraged to have the following matters documented:

- The matter.
- The results of discussions with the assurance practitioner's superiors, if any, and those charged with governance and other parties.
- How the assurance practitioner's superiors, if any, and those charged with governance have responded to the matter.
- The courses of action the assurance practitioner considered, the judgements made and the decisions that were taken.
- How the assurance practitioner is satisfied that the assurance practitioner has fulfilled the responsibility set out in paragraph R260.17.

Responsibilities of Assurance Practitioners Other than Senior Assurance Practitioners

R260.24 If, in the course of carrying out professional activities, an assurance practitioner becomes aware of information concerning non-compliance or suspected non-compliance, the assurance practitioner shall seek to obtain an understanding of the matter. This understanding shall include the nature of the non-compliance or suspected non-compliance and the circumstances in which it has occurred or might occur.

260.24 A1 The assurance practitioner is expected to apply knowledge and expertise, and exercise professional judgement. However, the assurance practitioner is not expected to have a

level of understanding of laws and regulations greater than that which is required for the assurance practitioner's role within the employing organisation. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

260.24 A2 Depending on the nature and significance of the matter, the assurance practitioner might consult on a confidential basis with others within the employing organisation or a professional body, or with legal counsel.

R260.25 If the assurance practitioner identifies or suspects that non-compliance has occurred or might occur, the assurance practitioner shall, subject to paragraph R260.9, inform an immediate superior to enable the superior to take appropriate action. If the assurance practitioner's immediate superior appears to be involved in the matter, the assurance practitioner shall inform the next higher level of authority within the employing organisation.

R260.26 In exceptional circumstances, the assurance practitioner may determine that disclosure of the matter to an appropriate authority is an appropriate course of action. If the assurance practitioner does so pursuant to paragraphs 260.20 A2 and A3, that disclosure is permitted pursuant to paragraph R114.1(d) of the Code. When making such disclosure, the assurance practitioner shall act in good faith and exercise caution when making statements and assertions.

Documentation

260.27 A1 In relation to non-compliance or suspected non-compliance that falls within the scope of this section, the assurance practitioner is encouraged to have the following matters documented:

- The matter.
- The results of discussions with the assurance practitioner's superior, management and, where applicable, those charged with governance and other parties.
- How the assurance practitioner's superior has responded to the matter.
- The courses of action the assurance practitioner considered, the judgements made and the decisions that were taken.

SECTION 270

PRESSURE TO BREACH THE FUNDAMENTAL PRINCIPLES

Introduction

- 270.1 Assurance practitioners are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 270.2 Pressure exerted on, or by, an assurance practitioner might create an intimidation or other threat to compliance with one or more of the fundamental principles. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- R270.3** An assurance practitioner shall not:
- (a) Allow pressure from others to result in a breach of compliance with the fundamental principles; or
 - (b) Place pressure on others that the assurance practitioner knows, or has reason to believe, would result in the other individuals breaching the fundamental principles.
- 270.3 A1 An assurance practitioner might face pressure that creates threats to compliance with the fundamental principles, for example an intimidation threat, when undertaking a professional activity. Pressure might be explicit or implicit and might come from:
- Within the employing organisation, for example, from a colleague or superior.
 - An external individual or organisation such as a vendor, customer or lender.
 - Internal or external targets and expectations.
- 270.3 A2 Examples of pressure that might result in threats to compliance with the fundamental principles include:
- Pressure related to conflicts of interest:
 - Pressure from a family member bidding to act as a vendor to the assurance practitioner's employing organisation to select the family member over another prospective vendor.See also Section 210, *Conflicts of Interest*.
 - Pressure to influence preparation or presentation of information:
 - Pressure to report misleading financial results to meet investor, analyst or lender expectations.
 - Pressure from elected officials on public sector accountants to misrepresent programs or projects to voters.
 - Pressure from colleagues to misstate income, expenditure or rates of return

to bias decision-making on capital projects and acquisitions.

- Pressure from superiors to approve or process expenditures that are not legitimate business expenses.
- Pressure to suppress internal audit reports containing adverse findings.

See also Section 220, *Preparation and Presentation of Information*.

- Pressure to act without sufficient expertise or due care:
 - Pressure from superiors to inappropriately reduce the extent of work performed.
 - Pressure from superiors to perform a task without sufficient skills or training or within unrealistic deadlines.

See also Section 230, *Acting with Sufficient Expertise*.

- Pressure related to financial interests:
 - Pressure from superiors, colleagues or others, for example, those who might benefit from participation in compensation or incentive arrangements to manipulate performance indicators.

See also Section 240, *Financial Interests, Compensation and Incentives Linked to Financial Reporting and Decision Making*.

- Pressure related to inducements:
 - Pressure from others, either internal or external to the employing organisation, to offer inducements to influence inappropriately the judgement or decision making process of an individual or organisation.
 - Pressure from colleagues to accept a bribe or other inducement, for example to accept inappropriate gifts or entertainment from potential vendors in a bidding process.

See also Section 250, *Inducements, Including Gifts and Hospitality*.

- Pressure related to non-compliance with laws and regulations:
 - Pressure to structure a transaction to evade tax.

See also Section 260, *Responding to Non-compliance with Laws and Regulations*.

270.3 A3 Factors that are relevant in evaluating the level of threats created by pressure include:

- The intent of the individual who is exerting the pressure and the nature and extent of the pressure.
- The application of laws, regulations, and professional standards to the circumstances.
- The culture and leadership of the employing organisation including the extent to which they reflect or emphasise the importance of ethical behaviour and the expectation that employees will act ethically. For example, a corporate culture

that tolerates unethical behaviour might increase the likelihood that the pressure would result in a threat to compliance with the fundamental principles.

- Policies and procedures, if any, that the employing organisation has established, such as ethics or human resources policies that address pressure.

270.3 A4 Discussing the circumstances creating the pressure and consulting with others about those circumstances might assist the assurance practitioner to evaluate the level of the threat. Such discussion and consultation, which requires being alert to the principle of confidentiality, might include:

- Discussing the matter with the individual who is exerting the pressure to seek to resolve it.
- Discussing the matter with the assurance practitioner's superior, if the superior is not the individual exerting the pressure.
- Escalating the matter within the employing organisation, including when appropriate, explaining any consequential risks to the organisation, for example with:
 - Higher levels of management.
 - Internal or external auditors.
 - Those charged with governance.
- Disclosing the matter in line with the employing organisation's policies, including ethics and whistleblowing policies, using any established mechanism, such as a confidential ethics hotline.
- Consulting with:
 - A colleague, superior, human resources personnel, or another assurance practitioner;
 - Relevant professional or regulatory bodies or industry associations; or
 - Legal counsel.

270.3 A5 An example of an action that might eliminate threats created by pressure is the assurance practitioner's request for a restructure of, or segregation of, certain responsibilities and duties so that the assurance practitioner is no longer involved with the individual or entity exerting the pressure.

Documentation

270.4 A1 The assurance practitioner is encouraged to document:

- The facts.
- The communications and parties with whom these matters were discussed.
- The courses of action considered.
- How the matter was addressed.

CONSEQUENTIAL AMENDMENTS

This appendix sets out consequential amendments to Professional and Ethical Standard 1 as a result of approval of the Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm
Amended paragraphs are shown with new text underlined and deleted text struck through.

GUIDE TO THE CODE

How the Code is Structured

4. The Code contains the following material:
 - Part 1 – *Complying with the Code, Fundamental Principles and Conceptual Framework*, which includes the fundamental principles and the conceptual framework.
 - ~~[Part 2 – deleted by the NZAuASB]~~ Part 2 –Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm, is applicable to individuals who are assurance practitioners when performing professional activities pursuant to their relationship with the firm, whether as a contractor, employee or owner.
 - Part 3 – *Application of the Code, Fundamental Principles and Conceptual Framework*, which sets out additional material that applies to assurance practitioners when providing assurance services.
 - *International Independence Standards (New Zealand)*, which sets out additional material that applies to assurance practitioners when providing assurance services, as follows:
 - Part 4A – *Independence for Audit and Review Engagements*, which applies when performing audit or review engagements.
 - Part 4B – *Independence for Assurance Engagements Other than Audit and Review Engagements*, which applies when performing assurance engagements that are not audit or review engagements.
 - *Glossary*, which contains defined terms (together with additional explanations where appropriate) and described terms which have a specific meaning in certain parts of the Code.
- ...

NEW ZEALAND PREFACE

Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*, (“the Code”), issued by the NZAuASB is based on ~~Parts 1, 3, 4A and 4B~~ of the International Code of Ethics for Professional Accountants (including International Independence Standards (“the International Code”). The International Code is issued by the International Ethics Standards Board for Accountants. It is published by the International Federation of Accountants (IFAC) and used with permission of IFAC, as it applies to assurance practitioners in New Zealand.

New Zealand additions and deletions are prefixed with NZ in the Code.

The Code is based on a number of fundamental principles that express the basic tenets of professional and ethical behaviour and conduct. Assurance practitioners must abide by these fundamental principles when performing assurance engagements.

The International Independence Standards (New Zealand) set out requirements that apply to all entities and all assurance practitioners. Small entities and small firms, in certain circumstances, may face difficulties implementing the requirements. Many of the examples provided of actions that might reduce the threat may not be available to small entities and small firms. For example, involving individuals within the firm who are not members of the assurance team in, for example, providing non-assurance services to an assurance client, may not reduce the threats to independence to an acceptable level given the likely closeness of relationships of staff within small firms.

PART 1 – COMPLYING WITH THE CODE, FUNDAMENTAL PRINCIPLES AND CONCEPTUAL FRAMEWORK

SECTION 120

THE CONCEPTUAL FRAMEWORK

Introduction

Requirements and Application Material

General

R120.3 The assurance practitioner shall apply the conceptual framework to identify, evaluate and address threats to compliance with the fundamental principles set out in Section 110.

120.3 A1 Additional requirements and application material that are relevant to the application of the conceptual framework are set out in:

- (a) Part 2 – Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm;
- (b) Part 3 – *Application of the Code, Fundamental Principles and Conceptual Framework*; and
- (c) *International Independence Standards (New Zealand)*, as follows:
 - (i) Part 4A – *Independence for Audit and Review Engagements*; and
 - (ii) Part 4B – *Independence for Assurance Engagements Other than Audit and Review Engagements*.

R120.4 ~~*[Amended by the NZAuASB. Refer to NZ R120.4.1]*~~ When dealing with an ethics issue the assurance practitioner shall consider the context in which the issue has arisen or might arise. Where an individual who is an assurance practitioner is performing professional activities pursuant to the assurance practitioner’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions in Part 2 that apply to these circumstances.

~~**NZ R120.4.1** ——— When dealing with an ethics issue, the assurance practitioner shall consider the context in which the issue has arisen or might arise. Where an individual who is an assurance practitioner is performing assurance services pursuant to the assurance practitioner’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with any other ethical standards that apply to these circumstances.~~

PART 3 – APPLICATION OF THE CODE, FUNDAMENTAL PRINCIPLES AND CONCEPTUAL FRAMEWORK

SECTION 300

APPLYING THE CONCEPTUAL FRAMEWORK

Requirements and Application Material

General

R300.4 An assurance practitioner shall comply with the fundamental principles set out in Section 110 and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to compliance with the fundamental principles.

R300.5 ~~[Deleted by the NZAuASB. Refer to NZ-R300.5]~~ When dealing with an ethics issue, the assurance practitioner shall consider the context in which the issue has arisen or might arise. Where an individual who is an assurance practitioner is performing professional activities pursuant to the assurance practitioner’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions in Part 2 that apply to these circumstances.

~~**NZ-R300.5** — When dealing with an ethics issue, the assurance practitioner shall consider the context in which the issue has arisen or might arise. Where an individual who is an assurance practitioner is performing assurance services pursuant to the assurance practitioner’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with any other ethical provisions that apply to these circumstances.~~

300.5 A1 Examples of ~~such~~ situations in which the provisions in Part 2 apply to an assurance practitioner include:

- Facing a conflict of interest when being responsible for selecting a vendor for the firm when an immediate family member of the assurance practitioner might benefit financially from the contract. The requirements and application material set out in Section 210 apply in these circumstances.
- Preparing or presenting financial information for the assurance practitioner’s client or firm. The requirements and application material set out in Section 220 apply in these circumstances.
- Preparing or presenting financial information for the assurance practitioner’s client or firm. The requirements and application material set out in Section 220 apply in these circumstances.
- Being offered an inducement such as being regularly offered complimentary tickets to attend sporting events by a supplier of the firm. The requirements and application material set out in Section 250 apply in these circumstances.
- Facing pressure from an engagement partner to report chargeable hours inaccurately for a client engagement. The requirements and application material set out in Section 270 apply in these circumstances.

GLOSSARY

In the *International Code of Ethics for Professional Accountants (including International Independence Standards) (New Zealand)*, the singular shall be construed as including the plural as well as the reverse, and the terms below have the following meanings assigned to them.

In this Glossary, explanations of defined terms are shown in regular font; italics are used for explanations of described terms which have a specific meaning in certain parts of the Code or for additional explanations of defined terms. References are also provided to terms described in the Code.

Non-compliance with laws and regulations (assurance practitioners performing professional activities pursuant to their relationship with the firm) *Non-compliance with laws and regulations (“non-compliance”) comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:*

- (a) An assurance practitioner’s employing organisation;*
- (b) Those charged with governance of the employing organisation;*
- (c) Management of the employing organisation; or*
- (d) Other individuals working for or under the direction of the employing organisation*

This term is described in paragraph 260.5 A1.

Non-compliance with laws and regulations (assurance practitioners) *Non-compliance with laws and regulations (“non-compliance”) comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:*

- (a) A client;*
- (b) Those charged with governance of a client;*
- (c) Management of a client; or*
- (d) Other individuals working for or under the direction of a client.*

This term is described in paragraph 360.5 A1.

Senior assurance practitioner *Senior assurance practitioners are directors, offices or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organisation’s human, financial, technological, physical and intangible resources.*

This term is described in paragraph 260.11 A1

Substantial harm *This term is described in paragraphs 260.5 A3 and 360.5 A3.*

Memorandum

Date: 2 September 2020

To: Michele Embling, Chair XRB Board

From: Robert Buchanan, Chair NZAuASB

Subject: Certificate Signing Memorandum: *Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm*

Introduction

1. In accordance with the protocols established by the XRB Board, the NZAuASB seeks your approval to issue *Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm*.

Background

2. Because Part 2 of the IESBA Code sets out requirements and application material for professional accountants in business, historically it was excluded from Professional and Ethical Standard 1 as the provisions were considered outside the mandate of the NZAuASB. However, as part of the IESBA's structure project, the IESBA sought to clarify the applicability of Part 2 to professional accountants in public practice, recognising that in certain circumstances the provisions for professional accountants in business may be relevant to professional accountants in public practice, for example, section 270 *Pressure to Breach the Fundamental Principles*. The IESBA included a requirement¹ in Part 3 that states,

“When dealing with an ethics issue, the professional accountant shall consider the context in which the issue has arisen or might arise. Where an individual who is a professional accountant in public practice is performing professional activities pursuant to the accountant’s relationship with the firm, whether as a contractor, employee or owner, the individual shall comply with the provisions of Part 2 that apply to these circumstances.”

¹ *International Code of Ethics for Professional Accountants, including International Independence Standards*, paragraph **R300.5**

3. Accordingly, in April 2020, the NZAuASB issued [ED NZAuASB 2020-1](#)². The proposal amends Professional and Ethical Standard 1 to include Part 2 of the IESBA International Code of Ethics, with contextual amendments for application in New Zealand.
4. Submissions on ED NZAuASB 2020-1 closed on 20 July 2020 following a 90-day comment period. One submission was received, from the OAG.
5. The main comments related to whether the exposure draft is concerned with:
 - an assurance practitioner in their relationship with a firm;
 - an assurance practitioner in their relationship to their employing organisation; or
 - both;with the overall conclusion that Part 2 of the NZAuASB Code of Ethics will not apply to assurance practitioners who do not have a relationship with a firm.
6. Following due consideration of the submission, the NZAuASB determined that no changes to the exposure draft were required, as the intent of the amendment to PES 1 is to clarify the applicability of Part 2 of the IESBA Code to an assurance practitioner's relationship with a firm.

Privacy

7. The Financial Reporting Act 2013, section 22(2) requires that the External Reporting Board consult with the Privacy Commissioner where an accounting or assurance standard is likely to require disclosure of personal information. The amendments do not require such disclosure.

Due Process

8. The due process followed by the NZAuASB complied with the due process requirements established by the XRB Board and in the NZAuASB's view meets the requirements of section 12(b) of the Financial Reporting Act 2013.

Consistency with XRB Financial Reporting Strategy

9. The key strategic objectives set by the XRB Board for the NZAuASB include:

² ED NZAuASB 2020-1 *Proposed Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship With the Firm*

- To adopt international auditing and assurance standards, including the professional and ethical standards, in New Zealand unless there are strong reasons not to (which the Board describes as “compelling reasons”); and
- To work with the Australian Auditing and Assurance Standards Board (AUASB) towards the establishment of harmonised standards based on international standards.

10. Modifications for the application in New Zealand may be acceptable provided such modifications consider the public interest, and do not conflict with or result in lesser requirements than the international standards.

Other matters

11. There are no other matters relating to the issue of this standard that the NZAuASB considers to be pertinent or that should be drawn to your attention.

Recommendation

12. The NZAuASB recommends that you sign the attached certificate of determination on behalf of the XRB Board.

Attachments

Amendments to Professional and Ethical Standard 1: Part 2, Assurance Practitioners Performing Professional Activities Pursuant to Their Relationship with the Firm

Robert Buchanan
Chair
NZAuASB

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	7.1
Meeting date:	2 September 2020
Subject:	Monitoring Group Report
Date:	17 August 2020
Prepared by:	Misha Pieters

<input checked="" type="checkbox"/>	Action Required
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Agenda Item Objectives

To seek feedback on a staff analysis of the impact of the Monitoring Group's (MG) recommendations on the NZAuASB.

Background

1. The MG began its considerations of the need for reform of the audit-related standard setting system in 2015. The NZAuASB has been monitoring and been kept updated of developments on an ongoing basis. The MG released its recommendations in July 2020. At the NZAuASB July 2020 meeting the Board received a verbal summary of the key aspects of the MG's recommendations, noting the inclusion of a Public Interest Framework, and of particular importance and relevance to New Zealand, a broadening of a focus beyond listed entities.

Impact globally

2. The Public Interest Oversight Board (PIOB) is confident that the implementation of these recommendations will enhance the independence of the standard-setting system and its responsiveness to the public interest.
3. Both the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA) have welcomed the recommendations and support change that can advance their ability to deliver enhanced standards in the public interest.
4. Key aspects of the recommendations are aimed at enhancing engagement with wide ranging stakeholders to further promote a balanced outcome in the public interest. Time will tell how these changes will be funded, operationalized and how the changes will impact on the international standards to be developed and issued.
5. In many ways, both the IAASB and IESBA have previously applied many of the characteristics now formalised in the Public Interest Framework e.g., scalability has been an increasing issue and focus for both Boards. (i.e. none of these are "new"). We expect that the recommendations

will either retain the existing quality of the standards that the NZAuASB have adopted to date, and/or continue to enhance or improve the standards for application globally. Continuing to balance practitioner views with the wider stakeholder group may assist in reducing any perception of “undue practitioner influence”.

Matters to consider

6. NZAuASB members will be asked for views on how the MG’s recommendations impact on the NZAuASB as explored in agenda item 7.2, including:
- Outreach and stakeholder engagement;
 - Incorporating the qualitative characteristics into the NZAuASB’s due process including both the compelling reason test and/or into the way in which any domestic requirements are developed, from the project plan approval through to issue.
 - Enhancing transparency as to how the NZAuASB has factored in the public interest when issuing new or revised standards through explanation in the New Zealand explanation for decisions made documents.
 - The need to address public interest characteristics explicitly when developing the Signing Memorandum seeking approval to issue a standard by the XRB
 - Board composition and operating procedures
 - Influencing the international standards

Material Presented

Agenda item 7.1	Board Meeting Summary Paper
Agenda item 7.2	Staff analysis
Agenda item 7.3	Monitoring Group report

Staff analysis of the Monitoring Group's Report

1. The purpose of this analysis is to consider the impact of the [MG's recommendations](#) on the XRB/NZAuASB. This memo is structured as follows:

Section 1: Overview of the monitoring group's (MG) report

Section 2: The Public Interest Framework

Section 3: Impact of the Public Interest Framework on the work of the NZAuASB

Section 4: Impact of the MG's recommendations on the XRB/NZAuASB

2. The Board will be asked for feedback on the MG's recommendations, the public interest framework and the impact of the report on the NZAuASB.

Section 1: Overview of the MG's report

3. The MG's report was issued in July 2020. The recommendations are designed to:
 - a. Achieve an independent and inclusive, multi stakeholder standard setting structure
 - b. Reinforce consideration of the public interest throughout the full cycle of development
 - c. Foster development of timely, high quality standards responsive to accelerating change.
4. In summary the MG recommends:
 - a. The standard-setting activity to be housed in a separate legal entity from IFAC.
 - b. The IAASB and IESBA to continue to exist as separate boards within their current mandates, operating with approximately the same size of membership and based in New York City. Enhanced co-ordination between the two Boards is highlighted as essential.
 - c. Multi-stakeholder representation on the IAASB and IESBA and the PIOB and enhanced PIOB transparency.
 - d. New nominations arrangements that address the perception of undue influence by the profession on IAASB and IESBA.
 - e. A Public Interest Framework, which acknowledges, amongst other elements, the importance of scalability, operability, usability, and readability of the standards.
 - f. The formation (or reformation as the case may be) of stakeholder advisory councils reflecting diverse stakeholders including national standards setters.
 - g. Further clarity around the oversight responsibilities of the PIOB versus the Boards' responsibilities as well as enhanced transparency and accountability processes.
5. Funding remains a key issue and the MG continues to work towards an appropriate, long-term sustainable funding policy. Diversification of funding is seen to be key to its successful implementation. In the short term, the MG aims to reduce the contribution of the profession to less than 50%, and to further reduce this in the long term.
6. The report recommends the development of a transition plan within 9 months and a three year implementation plan.

Section 2: The Public Interest Framework

7. The report includes a Public Interest Framework (the Framework) to ensure that the future development of international standards can be more responsive to the public interest. The “Public Interest” has not been defined but reference to the public interest has been broadened to reflect the importance of serving the primary users of general purpose financial reports while also recognising the needs of other relevant stakeholders. The standards serve the needs of both developed and developing financial markets and all types of entities, including public interest entities, smaller and medium sized enterprises, government and public sector bodies, and not-for-profit institutions. The Framework identifies different classes of stakeholders that have a legitimate interest in the standards, including: Users (mainly investors, lenders and creditors), the profession, NSS, regulators, market authorities, public sector bodies and professional bodies, preparers from entities of all sizes and others including consumers, taxpayers, employees, competition authorities, central banks and those granting public contracts.
8. Without defining the public interest, the framework highlights the dynamic nature of a concept that evolves over time. The standard setting system therefore needs to be alert to shifting needs and perception, and to be capable of flexibility in its response. At the same time, the system must maintain fundamental stability and long-term credibility of principles-based standards.
9. The framework sets out the following qualitative characteristics to be used to assess the standards responsiveness to the public interest, including but not limited to:
 - a. Consistency with priorities established in the strategic planning process
 - b. Coherence with the overall body of standards, to avoid conflict
 - c. Appropriate scope to address key issues, and to specify to whom the standard applies
 - d. Scalability, including proportionality
 - e. Timeliness, without sacrificing quality
 - f. Relevance in recognising and responding to emerging issues, changes in business environment, developments in accounting practices or technology
 - g. Completeness, reflecting results of broad consultation and balancing stakeholder priorities
 - h. Comprehensiveness, by limiting exceptions to the principles
 - i. Clarity and conciseness
 - j. Implementability and ability to be consistently applied
 - k. Enforceable, through clearly stated responsibilities
10. The public interest responsiveness is assessed by applying the qualitative characteristics in the following steps:
 - a. Identify the perspectives and needs of groups with legitimate interests
 - b. Define the desired goal that would allow the standard to best serve user needs.
 - c. Identify criteria to assess responsiveness to the goal

- d. According to the criteria, reasonably weigh input from different groups
- e. Assess the expected contribution of the standard to meeting its goal and consider whether it is responsive to the public interest.

11. The following quotes from the PIOB annual report are also relevant:

“The concept of public interest attracts a lot of attention, yet it is difficult to define, particularly in a global context with its wide diversity of cultures and expectations. It is often invoked by legislators, judges, overseers, the audit profession, and many others, but without an agreed definition. The public interest is not the sum of private interests, because the interests of different groups are often not aligned or are contradictory; they cannot simply be added up. How can the interests of different stakeholders be weighed, considered, and assessed to understand what constitutes the public interest?”

“However, the social impact of the audit function implies that audit and ethics standards affect many interests in addition to those of the profession, including those of the audited entity, preparers, investors, creditors, workers, pension funds, taxpayers, and society in general, who, ultimately, bear the loss of value caused by a failure of market confidence. These interests collectively are what is meant by the “public interest.”

- 12. Assessing public interest requires the application of judgement. Judgement is best informed when the process and consultation elicits views from all interested stakeholders and balances the merits of the views, irrespective of the minority or majority view.
- 13. The merit of the application of the public interest framework is to enhance transparency and accountability of the process.

Section 3: Impact of the Public Interest Framework on the work of the NZAuASB

- 14. The qualitative characteristics listed in the framework include characteristics that the NZAuASB discuss all the time, and in many ways explicitly state what is implicitly considered by the NZAuASB. It is however, useful to have these characteristics explicitly articulated and grouped together. It may be helpful to adopt these characteristics more formally into the NZAuASB's processes.
- 15. In many respects, these characteristics will be dependent on the international boards application when developing the standards that the NZAuASB intend to adopt. For example, clarity and conciseness or timeliness. However, the characteristics do provide a useful framework to overlay again in the New Zealand context to inform additional areas of priority for the Board.
- 16. We consider that the public interest framework impacts the processes and procedures of the NZAuASB in the following ways, each of which are analysed below:
 - a. Outreach and stakeholder engagement;
 - b. Incorporating the qualitative characteristics into the NZAuASB's due process including both the compelling reason test and/or into the way in which any domestic requirements are developed, from the project plan approval through to issue.
 - c. Enhancing transparency as to how the NZAuASB has factored in the public interest when issuing new or revised standards through explanation in the New Zealand explanation for decisions made documents.

- d. The need to address public interest characteristics explicitly when developing the signing memorandum seeking approval to issue a standard by the XRB

Outreach and stakeholder engagement

17. One qualitative characteristic in the framework is Completeness, reflecting results of broad consultation and balancing stakeholder priorities.
18. The NZAuASB's consultation process is open and does encourage input from all stakeholders whose interests are impacted. The challenge both internationally and domestically is that in many instances the proposals are so specialised and technical, that few interest groups outside of the profession have the technical understanding, time or resources to participate in the consultation. When we do manage to get stakeholders to attend roundtables, often participation is limited to practitioners.
19. The NZAuASB has recently tried using different outreach techniques, including:
 - a. Seeking input from the NZASB, the XRB Board and the XRAP (on the topics of interim reporting and EER)
 - b. Additional webinars and user-friendly alerts to engage with users in response to COVID-19
 - c. Targeted one on one calls (NAS consultation, interviews on KAMs with investors)
 - d. Close collaboration with the regulator
 - e. Online virtual roundtables (EER consultation, and Group audits),however generally participation is low. This makes it challenging to truly obtain views from all stakeholders and then balance the various views.
20. New innovative techniques to engage broadly with all those who may be impacted by a loss of confidence in the market are needed. Board members are asked to consider contacts, ideas or techniques we could leverage. Initial suggestions include:
 - a. A first step in each project to prioritise and identify specific outreach, considering each stakeholder outlined in the framework, which matters and how best to engage, to ensure that all relevant views are received.
 - b. Identifying ways to consult with the XRAP and better connect and leverage off the XRAP members' networks.
 - c. Consider ways to make the international consultation material more accessible to a broader audience. Often the international consultation material is lengthy, technical and often does not even engage with the profession, let alone more broadly. We may also need to prioritise key projects, or aspects of key projects, of most interest, rather than consulting broadly on every topic across the NZAuASB (and NZASB). This will require a co-ordinated effort.
 - d. The formation of an investor consultative group/mechanism to facilitate XRB consultation. Such consultation would need to be targeted and prioritized across the organization, so as to remain relevant to the audience and not result in outreach fatigue.
 - e. Consider ways to make the submission process less intimidating or time consuming for stakeholders and leveraging off online capabilities.

- f. Staff and Board consideration of whether all relevant/prioritised stakeholders have been at least approached as an integral part in the process prior to finalisation.

At the same time, we recognise that there is only so much we can do to encourage participation. If stakeholders have no appetite to engage, it will continue to challenge us. Survey and outreach fatigue are and will remain key challenges.

21. We seek feedback from the Board with respect to the impact of the Public Interest Framework on outreach and stakeholder engagement in New Zealand.

Due process considerations and the Compelling reason test

- 22. All of the characteristics will impact on the consideration of the compelling reason test. The following two qualitative characteristics may be of particular relevance: Coherence with the overall body of standards, to avoid conflict and Comprehensiveness, by limiting exceptions to the principles.
- 23. The NZAuASB and the AUASB have a joint project to update the compelling reason test (Refer to agenda item 8). The existing test sets a high bar for modifying the international standards, in that one or more of the following tests must be met:
 - a. The international standard does not reflect, or is not consistent with the New Zealand regulatory arrangements; or
 - b. The international standard does not reflect, or is not consistent with, principles or practices that are considered appropriate in New Zealand (including use of significant terminology).
- 24. We recommend that the compelling reason test be amended to reflect the Public Interest Framework and the qualitative characteristics to ensure alignment of and consideration of the public interest in New Zealand as an overlay.
- 25. Similarly, we recommend that these public interest qualitative characteristics should be explicitly incorporated into all domestic and/or Trans-Tasman projects. The steps identified in paragraph 10 should be included as part of the project plan and flowed through each project through to completion.
- 26. The Public interest framework could either be formally adopted by the NZAuASB and/or the key aspects referenced or reflected in a number of our due process documents. E.g., a revision of EG Au2 *Overview of the Auditing and Assurance Standard Setting Process*. We recommend incorporation as relevant, as the Framework is articulated and developed from a global standard setting perspective.
- 27. Do you consider that the Public Interest Framework should be separately adopted by the XRB or that the principles and aspects relevant to our own due processes should be incorporated as relevant (e.g. into the compelling reason test and EG Au2)?**

Enhancing transparency when issuing new or revised standards

- 28. Enhancing transparency is a key recommendation described throughout the report. The Framework states that “the public interest is best served when the standards are developed by *independent, transparent and publicly accountable* boards that set standards with the *relevant expertise focusing on the public interest* and are subject to *direct oversight* by an independent oversight body, which is equally focused on the public interest.”

29. In order to remain accountable to acting in the public interest, the New Zealand explanations for decisions made documents may similarly need to explain how the NZAuASB applied the steps articulated in the framework and summarised in paragraph 10 of this memo to each relevant project. This may even be required where no New Zealand changes are made, to enhance transparency as how the NZAuASB applied its judgement in the public interest.
30. We recommend that a new section be added to the “template” for the “Explanation for decisions made” documents and that the Board consider whether such a feedback mechanism should always be provided, or more regularly provided on key topics, even if no New Zealand specific changes are made.
31. **Do you consider that the NZAuASB could enhance transparency about how new or revised standards work in the public interest in New Zealand? If yes, do you have views about how what actions or processes should be enhanced or developed?**

XRB oversight

32. The recommendations address the responsibilities of the PIOB and the Boards. The PIOB will engage with the Boards on a timely and ongoing basis to ensure the public interest responsiveness of standards but the IAASB and IESBA have responsibility for consideration of public interest responsiveness. The Boards will provide a public written statement that the new or revised standard is responsive to the public interest.
33. We recommend that the signing memorandum also include a separate section to explain how the NZAuASB applied the steps articulated in framework and summarised in paragraph 10 of this memo. This will focus the NZAuASB and the XRB on the public interest explicitly. In addition, the Approval Certificate, signed by the XRB Chair, may also reference the public interest. The XRB will need to consider whether the protocols established between the XRB and the NZAuASB, and the Terms of Reference for the NZAuASB should more formally incorporate aspects of the Public Interest Framework.
34. **Do you have any additional suggestions on how the Public Interest Framework may impact on the protocols established between the XRB and the NZAuASB?**

Section 4: Impact of the MG’s recommendations on the work of the NZAuASB

35. The MG Report makes a number of recommendations related to the Structure and Process of Standard-Setting in the international context. We consider how these recommendations might apply or impact on the NZAuASB more specifically.

Board Composition

36. The MG recommends that the International Boards will each comprise of 16 members. This will reduce the size of both Boards by 2 members. Practitioner representation will be limited to five audit practitioners, including from SMPs and public sector organizations. This will be a reduction of audit practitioner members. Currently both the IAASB’s and the IESBA’s requirements limit the number of practitioner members to no more than 9, and no less than 3 public members. I.e. practitioner representation is effectively reduced from a maximum of half to a maximum of just under a third. These changes may also effectively reduce representation from the big 4 to a maximum of three (given the need to include SMPs and public sector organizations).

37. The international Boards are to be supported by an expanded and enhanced technical staff. This is aimed at reducing the reliance on technical advisors that exists today.
38. The size of the NZAuASB has recently been reduced to 9 members. Practitioner representation on the NZAuASB is at 30%. The NZAuASB already has multi-stakeholder representation, including academics, governance, investor/users and an independent Chair. In many respects the MG recommendations have already been entrenched in the multi-stakeholder representation of the NZAuASB since its inception. SMPs are not currently represented on the NZAuASB. Nor is the not-for-profit sector as it has been in the past.
39. The MG report recommends a two-thirds majority of all Board members required to vote in favour for the issuance of an ED, final standard or amendment. The NZAuASB Terms of Reference already include this same protocol "The affirmative vote of two-thirds of all members (not just members present) is required for all decisions involving the issuing of an exposure draft, standard, guidance material or the like. A simple majority of all members (not just members present) is required for other decisions."
40. The XRB should compare the details of the MG recommendations to the operating policies and Terms of Reference of the NZAuASB as there are recommendations that relate or compare to the Board's operating policies. In our initial analysis, no significant changes were identified based on these recommendations., however a more explicit reference to the public interest may be beneficial.

Board Operating Procedures

41. The MG recommends that the board develop a comprehensive strategy and related agenda priorities, including SMEs, in a way that serves the public interest. The MG recommends enhancing the use of the Basis for Conclusions to provide context surrounding the objectives of new requirements, the issues intended to be addressed and enhance transparency as to how the Board considered and responded to input received.
42. The international Boards will have the responsibility for consideration of public interest responsiveness within the standard setting process. Once approved, the Board will provide a written statement that the new or revised standard is responsive to the public interest in accordance with the Public Interest Framework.
43. The PIOB will provide a separate public certification on an approved new standard that the PIOB considered that the new or revised standard is responsive to the public interest in accordance with the Public Interest Framework.
44. The operating procedures of the XRB/NZAuASB could also more explicitly reference the Public Interest, however there would be a need to adopt/reference the public interest framework or equivalent in New Zealand.
45. The NZAuASB's strategy is linked to the XRB strategy. Staff recommendation related to the use of the NZ Explanations for Decision above relate to both the Public Interest Framework and this recommendation.
46. **Do Board members have any comments on the Board Composition or Board Operating Procedures?**

Influencing international standards

47. The international Boards are to reconfigure stakeholder advisory councils reflecting diverse stakeholders, specifically including national standard setters. As standards-related needs arise, the Boards shall have flexibility to appoint ad-hoc advisory groups.
48. The NZAuASB has historically always focused more broadly than the listed entities/regulated entities space, with a focus across all three sectors and all sizes of audit firms and entities. The recognition of all sectors and size entities in the Public Interest Framework is reflective of the way the NZAuASB has always worked.
49. There may be increased opportunity to influence international standard setting through increased participation on stakeholder advisory councils given the increased recognition to the role of national standard setters. New Zealand has already had successful participation on Project Advisory Panels (PAPs) including Marje Russ's participation in the EER guidance and an upcoming opportunity for Craig Fisher to participate on the LCE PAP.
50. **Do Board members have any comments on influencing international standards?**

**STRENGTHENING THE
INTERNATIONAL AUDIT AND
ETHICS STANDARD-SETTING
SYSTEM**

THE MONITORING GROUP

July 2020



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A. Purpose of the paper

The purpose of this Paper is to present the Monitoring Group's recommendations to strengthen the international audit-related standard-setting¹ system, including the Public Interest Framework, so that future development and oversight of international audit-related standards can be more responsive to the public interest.

The Monitoring Group is committed to advancing the public interest in international audit-related standard-setting and improving audit quality. The members of the Monitoring Group are the Basel Committee on Banking Supervision, European Commission, Financial Stability Board, International Association of Insurance Supervisors, International Forum of Independent Audit Regulators, International Organization of Securities Commissions, and the World Bank Group. The Monitoring Group's mission² is to:

- Cooperate in the interest of promoting high-quality international auditing and assurance, ethical and education standards for accountants;
- Monitor the implementation and effectiveness of the International Federation of Accountants (IFAC) Reforms, and in that connection, to undertake an effectiveness assessment of the IFAC Reforms and other aspects of IFAC's operations that involve the public interest;
- Through its Nominating Committee, appoint the members of the Public Interest Oversight Board (PIOB);
- Monitor the execution by the PIOB of its mandate;
- Consult and advise the PIOB with respect to regulatory, legal and policy developments that are pertinent to the PIOB's public interest oversight; and
- Convene to discuss issues and share views relating to international audit quality as well as to regulatory and market developments having an impact on auditing.

¹ We use this term in the paper to refer to standards issued by the International Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants, which include standards for audit, review, other assurance, and related services engagements, standards on quality control for those engagements, and ethics and independence requirements for accountants.

² See https://www.iosco.org/about/monitoring_group/pdf/monitoring_group_charter.pdf.

The Monitoring Group began to consider the need for further reforms to the audit-related standard-setting system in support of its mission in 2015. It developed a public consultation in November 2017³ to address the following perceptions: (1) the public interest is not given sufficient weight throughout the standard-setting process, (2) stakeholder confidence in the standards is adversely affected as a result of the perception of influence of the accountancy profession on two grounds: (a) IFAC's role in funding and supporting the standard-setting boards and running the standard-setting board nomination process; and (b) audit firms and professional accountancy bodies providing a majority of standard-setting board members and input to the consultation processes for development of standards, and (3) in a constantly changing audit and business environment, standards as currently developed might lack the necessary relevance and timeliness to underpin audit quality and user confidence.

The consultation was supplemented by outreach including regular meetings with IFAC, the PIOB and the Global Public Policy Committee (GPPC).⁴ The MG received 179 responses to the public consultation that are available on the Monitoring Group website.⁵ After analysis and release of a summary of the responses in May 2018,⁶ the Monitoring Group continued to undertake further work and engage in discussion and consultation with a wide range of stakeholders. The Monitoring Group has given careful consideration to and analyzed the feedback from these consultations in developing these recommendations. As a result, the Monitoring Group believes it is in the public interest to issue these recommendations such that these improvements can be implemented as soon as reasonably possible.

³ See <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD586.pdf>.

⁴ The Global Public Policy Committee (GPPC) of the six largest international accounting networks comprises representatives of BDO, Deloitte, EY, Grant Thornton, KPMG and PwC.

⁵ See the responses at http://www.iosco.org/about/?subSection=monitoring_group&subSection1=reforms-to-the-global-audit-standard-setting-process.

⁶ See https://www.iosco.org/about/monitoring_group/pdf/2018-05-31-Monitoring-Group-publishes-Summary-of-Feedback.pdf.

B. The Monitoring Group's Approach

Objectives

The Monitoring Group's recommendations are consistent with its commitment to advancing the public interest in international audit-related standard-setting and improving audit quality. The Monitoring Group recognizes the importance of an independent standard-setting process that provides for the establishment and maintenance of high quality principles-based standards, developed in the public interest by standard setters safeguarded from undue influence. In this regard, these recommendations are principally designed to support and enhance the following objectives associated with the development of high quality standards that are widely adopted and implemented:

- To achieve an independent and inclusive, multi-stakeholder standard-setting structure;
- To reinforce the consideration of the public interest within the standard-setting process and throughout the full cycle of standards' development, including through appropriate independent oversight; and
- To foster the development of timely, high quality standards that respond to an accelerating pace of change.

Scope

The scope of the recommendations covers the responsibilities of the:

- International Auditing and Assurance Standards Board (IAASB);
- International Ethics Standards Board for Accountants (IESBA); and
- Public Interest Oversight Board (PIOB).⁷

The IAASB and IESBA are referred to as the Board or jointly as the Boards in this paper.

⁷ The PIOB refers to the Public Interest Oversight Board, housed within the PIOB Foundation. See <https://www.ipiob.org/>.

C. The Monitoring Group's Recommendations

The Monitoring Group's recommendations are organized to consider the following:

- Accountability, public interest oversight, and governance;
- Purpose, structure, and process of standard-setting;
- Funding; and
- Transition.

Accountability, Public Interest Oversight, and Governance

Accountability

1. The Monitoring Group recommends all levels of the governance and oversight framework be subject to transparent accountability processes, including regular effectiveness reviews and enhanced reporting in the public domain.

2. Specifically, the Monitoring Group recommends to retain the three-tier model,⁸ with the roles and responsibilities of each level clearly delineated and properly balanced, to demonstrate transparency and accountability. The aim of the Monitoring Group is to provide a formal link between the PIOB and public authorities in order to protect the PIOB from undue influence while also enhancing its public accountability.

3. The Monitoring Group will periodically review⁹ the effectiveness of the system as a whole to address any public concerns and to safeguard the effectiveness of oversight. The Monitoring Group will perform its effectiveness review of these recommended reforms no later than five years after their implementation.

⁸ The three-tier model is described at <https://www.ipiob.org/index.php/global-standard-setting-in-the-public-interest/three-tier-standard-setting-model>.

⁹ See the Monitoring Group Charter located at https://www.iosco.org/about/monitoring_group/pdf/monitoring_group_charter.pdf for effectiveness assessment responsibilities.

Public Interest Oversight

4. The PIOB will provide oversight of the standard-setting process to ensure that international audit-related standards are responsive to the public interest, including that they are developed in accordance with the principles of the Public Interest Framework.¹⁰ It shall oversee that the standard-setting activities follow due process throughout the standard-setting development cycle, including that the Boards appropriately considered and balanced input from stakeholders.¹¹

The PIOB's remit will retain the direct oversight of the public interest responsiveness of final standards, including through ongoing engagement with the standard-setting Boards throughout the standard-setting development cycle.

The PIOB's governance responsibilities will include the nomination and appointment process for Board members,¹² protecting the Boards from undue influence, such as commercial, political, and economic influence, in the public interest and overseeing the administration that supports standard-setting, including the ethics and conduct criteria for the PIOB, Boards and staff.

The PIOB will have the appropriate powers, resources, staffing, and expertise to support these additional responsibilities.

Governance

5. The PIOB will include ten¹³ objective and gender diverse members, including the Chair, committed to the public interest. Members shall be drawn from a geographically and experientially diverse variety of stakeholder groups, with experience in the preparation, audit, oversight, delivery and use of financial statements, and with the ability to analyze if the work of the Boards is responsive to the public interest and undertaken in accordance with the Public Interest Framework.

¹⁰ See Section D for the Public Interest Framework.

¹¹ The PIOB will develop operating procedures to support the delivery of its remit.

¹² For the nomination and appointment of Board members other than the Chair, the PIOB will consult with the standard-setting Board Chair. The PIOB will establish and appoint a Nominating Committee (with consideration of diversity in stakeholder groups) to be responsible for facilitating the nomination process and recommending for appointment of members of the Boards, following clearly articulated guidelines. Reference is made to recommendation 8 in relation to conflicts of interest. As described in the "Transition" section of the paper, administrative support may be provided under a service level agreement with IFAC.

¹³ The PIOB Chair will hold a casting vote in the case of a tie.

6. The IOB Chair will demonstrate significant experience in identifying and understanding:

- Interests of users of financial statements;
- The regulatory framework in which capital markets operate; and
- The importance of reliable financial information to transparent markets and thus contributing to promoting financial stability.

7. The IOB members, including the Chair, will be identified through an open call for nominations with clearly articulated guidelines. The method for appointment will be determined by the Monitoring Group with consideration of a skills matrix that fosters leadership, expertise, and diversity of thought and geography. IOB appointments will be made by the Monitoring Group, consistent with currently established terms of three years, renewable once.¹⁴

8. The IOB Foundation¹⁵ will have a written policy on conduct that governs potential conflicts of interest for the IOB, standard-setting Boards, and staff.¹⁶ The Foundation's policies and procedures should set forth a responsibility of members of the IOB, standard-setting Boards and staff to act in the best interest of the Foundation by not putting any personal interest ahead of the interests of the Foundation.¹⁷ These policies must balance the IOB Foundation's role, responsibilities, threats, and safeguards so that the competence and expertise needed for high quality standard-setting is achieved while addressing conduct that raises legitimate concerns regarding the potential for conflicts of interest. Among other topics, the policies should address where conduct associated with outside employment or other outside activities actually conflict or appear to conflict with duties owed to the IOB Foundation.

¹⁴ See Article 10 of IOB consolidated bylaws at [https://www.ipob.org/media/files/about/IOB%20consolidated%20bylaws%20\(English%20Version\)%2020092018.pdf](https://www.ipob.org/media/files/about/IOB%20consolidated%20bylaws%20(English%20Version)%2020092018.pdf).

¹⁵ The IOB Foundation is the legal entity that houses the IOB. See also footnote 7.

¹⁶ In establishing the conflict of interest policies, the IOB shall consider the responsibilities of each group individually as well as collectively. Such policies shall maintain the principles established in the recommendations outlined herein.

¹⁷ See also recommendation 12 on the relationship of the standard-setting board legal entity structure to the IOB Foundation.

9. The PIOB will assess each Board's effectiveness. The PIOB will:

- Assess the effectiveness of each Board's Chair, taking input from stakeholders;
- Assess each Board's delivery against its agreed strategy and workplan;
- Hold the Boards accountable for the use of its approved budget; and
- Hold the Boards accountable for the results of periodic effectiveness reviews.

10. PIOB meetings will be open to the public with the summaries of minutes published on its website. The PIOB may, at its discretion, hold certain sessions of meetings in private.¹⁸ PIOB will post briefing and observation memos on its website explaining how it discharges its oversight role. The PIOB Foundation will make publicly available an annual report and related financial statements.

Purpose, Structure, and Process of Standard-Setting

Purpose

11. International audit-related standard-setting activities will be undertaken in accordance with the Public Interest Framework. International audit-related standard-setting should reflect the importance of serving the needs of the primary users of general-purpose financial reports, i.e., existing and potential investors, lenders, and other creditors, while also recognizing the needs of other relevant stakeholders to underpin trust in the capital markets.¹⁹ The standards serve the needs of both developed and developing financial markets and all types of entities, including public interest entities, smaller and medium sized enterprises, government and public sector bodies, and not-for-profit institutions.

Structure

12. The PIOB will be responsible for the governance of the Boards and public interest oversight of their agreed responsibilities. The recommendations are written with an over-arching objective

¹⁸ For example, certain sessions of meetings can be held in private if the session is likely to result in discussion of administrative matters including personnel matters.

¹⁹ See Section D for the Public Interest Framework.

that standard-setting activity would be independent from IFAC and that the associated governance and public interest oversight activities will reside within the PIOB Foundation legal entity. The legal structure should be defined considering that the standard-setting Boards should be housed in a separate legal entity outside of and independent from IFAC. The form of the legal structure for standard-setting needs to ensure that recommendations established in this document can be effectively discharged.²⁰

For future fundamental changes to the standard-setting structure, the PIOB, IFAC, and the Monitoring Group will sign a Memorandum of Understanding which will set out, among other things, the due process to accomplish any such fundamental future change. For clarity, this would not change the existing responsibilities of the Monitoring Group, including its ability to perform periodic effectiveness assessments as described in Recommendation 3 and the right to make future recommendations.

13. The governance structure will include a separation between the source of funding and the management of the funds, including their allocation to oversight and standard-setting activities.

Process of Standard-Setting: Board Remit and Composition

14. Standard-setting activities will be carried out by two expert and objective multi-stakeholder Boards. One Board would continue to be responsible for setting audit, review, assurance, and quality control standards and the other Board would continue to be responsible for setting international ethics standards for professional accountants, including auditor independence requirements. In this regard, the Boards will retain the current mandates of the IAASB and IESBA, respectively. Continued enhanced coordination between the Boards is essential to enable each to work more closely on key projects that impact their respective mandates.

15. Each Board will comprise 16 remunerated members, all appointed to act in the public interest.

²⁰ Similar to the existing IFAC reforms that are embedded in the Monitoring Group Charter, the Monitoring Group envisages that these recommendations will be a component of the legal arrangements and statutes of the new structure, in order to ensure stability and legal certainty.

Each board will be composed of a full-time independent Chair,²¹ one part-time Vice Chair, and 14 part-time members.²²

All members will be nominated through an open call and appointed using a skills matrix to be developed for each Board that prioritizes the public interest and fosters leadership, expertise, and diversity of thought and geography. The multi-stakeholder Boards shall be comprised of a balanced group of individuals drawn from diverse stakeholder groups including for example: investors and other users of the financial statements, accountants, regulatory members,²³ audit committee members, academics in the field of accounting or auditing, and audit practitioners.²⁴

16. In order to balance the risk of undue influence by the audit profession with the need for relevant technical expertise in setting high quality international audit-related standards, appointments to each Board are limited to five audit practitioners, including those with recent experience in audits of small and medium sized enterprises and public sector organizations. In this regard, an audit practitioner is defined as an individual who is or has been a member or employee of or otherwise affiliated with a public accounting firm within the last four years, determined at the time of appointment. The classification of a Board member as an audit practitioner shall remain unchanged throughout the individual's board term, including during a period of his/her reappointment.²⁵

Appointments will be for three years, renewable once. Initial appointments may be for a shorter period to allow for a gradual rotation of Board members.

²¹ Existing independence requirements shall be considered. For example, see <https://www.ifac.org/system/files/uploads/IAASB/Independence%20Requirement%20for%20IAASB%20Chair%20-%20Jan%202012.pdf> and <https://www.iaasb.org/publications/call-applications-iaasb-chair>.

²² As part of its periodic effectiveness review, the Monitoring Group will consider whether the part-time nature of members provides the Boards with sufficient capacity and independence.

²³ The reference to regulatory members encompasses the different regulatory and supervisory institutions, and their respective constituents, including those represented in the Monitoring Group. It shall also encompass national standard setters.

²⁴ Individuals might not have just one background, but often – over the course of their careers – individuals will have a combination thereof.

²⁵ For example, an appointed Board member who was employed by a public accounting firm within the last two years prior to appointment would be considered an audit practitioner during all of his/her initial term of three years and the term of reappointment, notwithstanding that it would have been five years since he/she had been employed by a public accounting firm at the date of his/her reappointment to the Board.

17. The Chair, Vice Chair, and members will bring a strategic mindset to each Board and, as a body, advance the timely development in the public interest of new or revised standards. As a whole, each Board along with its staff collectively must have the necessary technical competence, and appropriate expertise to be able to deliver their roles effectively.

For each Board, a two-thirds majority²⁶ of all Board members is required to vote in favor for the issuance of due process documents, such as an exposure draft, final standard, or amendment.

18. The Boards will have sufficient resources and be supported by an expanded and enhanced technical staff, with the capability to take forward the development of relevant, timely, high-quality standards. This can also lead to removing reliance on technical advisors that exists today. Each Board should determine the staffing needed to address the demands and expertise required to support its project work plan. The staff will work under the direction of the respective Board within the new legal entity housing the Boards.

19. Throughout the full development cycle of each standard, the PIOB will engage with the Boards on a timely and ongoing basis to ensure the public interest responsiveness of standards. Notwithstanding the certification process described in Recommendation 21, the Boards will have the ultimate responsibility and accountability for the approval and withdrawal of standards.

Process of Standard-Setting: Board Operating Procedures

20. Each Board will develop a comprehensive and integrated strategy for standards and related agenda priorities. The approach will balance the priorities including of smaller and medium sized enterprises, in a way that serves the public interest. Board meetings will continue to be open and the Boards will consider video streaming. Further, the Boards shall consider enhanced use of their basis for conclusion documents to provide context surrounding the objectives of a new or revised

²⁶ A two-thirds majority of a fully appointed Board (with 16 members) requires 11 Board members to vote in favor for the issuance of due process documents such as an exposure draft, final standard or amendment. A two-thirds majority is needed to prohibit a blocking minority by the accountancy profession. This principle of prohibiting a blocking minority shall be maintained and managed through the establishment of operating procedures which will address more specific fact patterns and required remedies to uphold this principle.

standard, key requirements and issues the standard intends to address, and enhanced transparency as to how the Boards considered and responded to input received during the consultation process.

21. The Boards will regularly engage with the PIOB throughout the full development cycle of each standard to ensure its public interest responsiveness. The Boards will have the responsibility for consideration of public interest responsiveness within the standard-setting process. In its oversight role, the PIOB will timely communicate to the relevant Board any concern around how the public interest is being captured during development of a particular standard and the relevant Board will seek to find an agreed upon solution.

Once a new or revised standard is approved, the relevant Board will provide a public written statement that:

- The Board developed the new or revised standard in accordance with agreed due process; and
- The new or revised standard is responsive to the public interest, in accordance with the Public Interest Framework.²⁷

Subsequently, the PIOB will provide a separate public certification on the approved new or revised standard. The certification will state that:

- The PIOB oversaw the standard-setting process throughout the full development cycle;
- The PIOB considered that the new or revised standard was developed in a manner consistent with agreed due process; and
- The PIOB considered that the new or revised standard is responsive to the public interest, in accordance with the Public Interest Framework.

These operating procedures should contribute to the outputs of the relevant Board's deliberations being appropriate in light of public interest considerations. Considering that the PIOB oversees the standard-setting process throughout the full development cycle, it will timely communicate to the relevant Board any concern around how the public interest is being captured. This would reinforce

²⁷ Existing standards will be grandfathered.

the role of the oversight body in ensuring transparent deliberations of the Boards and evaluating the degree to which standard-setting operates independent of undue interference and remains accountable to the public interest.²⁸ As a consequence of timely communication by the PIOB to the relevant Board throughout the standard-setting process, as well as the multi-stakeholder composition of each Board,²⁹ the Monitoring Group anticipates non issuance of PIOB certification to be very unlikely. If the PIOB is unable to issue a certification, the PIOB will publicly state its reasons.³⁰ In this very unlikely circumstance, the relevant Board will consider the issues identified by the PIOB in determining the best way to resolve the matter, including whether revisions to the standard are appropriate.

22. The Boards will have access to stakeholder advisory councils reflecting diverse stakeholders including national standard setters. The Boards and PIOB will discuss and finalize the nature and form of these advisory councils with consideration that members of the councils will have a term, periodically rotate, be appointed through an open call for nominations, and subject to periodic effectiveness reviews. As standard-related needs arise, the Boards shall have flexibility to appoint ad-hoc advisory groups.

Process of Standard-Setting: Adoption of Standards

23. The adoption and implementation of the standards will be fostered through multiple stakeholders, including IFAC and the PIOB. IFAC will maintain its role in promoting global adoption, convergence, education, implementation, and compliance to ensure that professional accountancy organizations comply with their membership obligations, advocacy, non-

²⁸ See page 7 of the Monitoring Group's 2013 Statement on Governance, https://www.iosco.org/about/monitoring_group/pdf/Monitoring-Group-Statement-on-Governance-and-Feedback-Statement.pdf?v=1.

²⁹ See, for example, the IFRS Due Process handbook- Section 2 at <https://www.ifrs.org/-/media/feature/about-us/legal-and-governance/constitution-docs/due-process-handbook.pdf>.

³⁰ The reason for not issuing a certification shall not be based on a technical disagreement. For further consideration of technical matters and oversight of due process, see also page 7 of the Monitoring Group's 2013 Statement on Governance, https://www.iosco.org/about/monitoring_group/pdf/Monitoring-Group-Statement-on-Governance-and-Feedback-Statement.pdf?v=1.

authoritative guidance, sharing of best practices, surveying for implementation challenges and building capacity of professional accountancy organizations.

Funding

24. Availability of sufficient financial resources will be essential for funding the recommended structure, both initially and over time. The Monitoring Group, giving consideration to the views of IFAC and the PIOB, will continue working for the development of an appropriate, long-term, sustainable funding policy. Acknowledging its key importance to the standard-setting process, the Monitoring Group will prioritize approaches that result in a funding mechanism consistent with the guiding principles of these recommendations, specifically to:

- Strengthen the international audit-related standard-setting system through an independent and inclusive, multi-stakeholder standard-setting structure;
- Enhance the consideration of the public interest throughout the full cycle of standards' development, including through appropriate independent oversight; and
- Foster the development of timely, high quality standards that respond to an accelerated pace of change.

Such a structure, which is key to the successful implementation of the recommended reforms, will have the following features:

- Diversification of contributions from around the world received from the following groups of stakeholders: investors and other users of financial statements, regulators,³¹ and the accountancy profession;
- Stability through medium and long term commitment from contributors and adequate reserves built over time; and
- Prudence and public accountability in the use of funds.

Funding commitments should foster the independence and continuity of the standard-setting activities. This will enable the development of high quality standards as a result of inclusive and

³¹ See footnote 23.

comprehensive consultation with stakeholders globally, public interest oversight and activities in support of wide adoption of the standards.

25. The Monitoring Group acknowledges that achieving the aforementioned funding goals will require time and in the short and medium term recommends to enhance the diversification of funding for the activities of the PIOB, with a goal that contributions from the accountancy profession will become less than fifty percent of the total budget of those activities. The accountancy profession funding should further diminish over the longer term. In order to achieve this goal, the Monitoring Group will perform outreach with stakeholder groups to seek commitments on funding for the PIOB. The Monitoring Group anticipates such outreach to include the regulatory and investor community, including Monitoring Group member organizations. Additionally, the Monitoring Group will aspire to achieve its funding goals for the PIOB by two years after the publication of these recommendations.

26. While IFAC continues to fund standard-setting activities and part of PIOB activities, in order to mitigate risk of undue economic influence, there will be separation between the source of funding and the management of the funds, including their allocation to oversight and standard-setting activities (PIOB and the standard-setting Boards' structure).

Transition

27. The Monitoring Group acknowledges the importance of timely implementation of these recommendations. With this in mind, the Monitoring Group will leverage the support of IFAC and the PIOB, along with input from the standard-setting Boards, in developing a transition plan within nine months from the publication of these recommendations. The transition plan will address the critical components of transition.³² The Monitoring Group, giving consideration to the importance of timely implementation of these recommendations, would not expect implementation to extend beyond a period of three years after the development of the transition plan. While these changes

³² The Monitoring Group anticipates the recommendations in this paper will result in an increase in cost associated with international audit-related standard-setting due mainly to expanded technical staff and remuneration of the Boards' members. The estimation of funds for the revised structure will be developed as a component of transition.

are coming into effect, we expect that the current standard-setting agendas and work of the existing Boards will continue to be delivered. Further, to mitigate disruption risk, the Boards and the PIOB Foundation will continue to be based in their current respective locations.

28. The Monitoring Group anticipates that the new structure will enter into a service level agreement with IFAC for necessary support services (for example, nominations, staffing, communications, and facilities) provided at fully transparent cost. This would be subject to the oversight of the PIOB to advance standard-setting activities while safeguarding against any threat to independence.

D. Public Interest Framework (Framework) for the Development of International Audit-Related Standards

The Framework's Context

All parties who have interest in international audit-related standards recognize that the public interest is best served when the standards are developed by *independent, transparent and publicly accountable* boards that set standards with the *relevant expertise focusing on the public interest* and are subject to *direct oversight* by an independent oversight body, which is equally focused on the public interest, ensuring that the standards appropriately address all stakeholder needs and that no undue influence is exercised by any stakeholder.

This Framework sets out the way development and oversight of international audit-related standards are responsive to the *public interest*.³³

The Framework has been developed in the context of the Monitoring Group recommendations presented in the previous sections. The Monitoring Group also contemplates that in order to maintain its relevance, the Public Interest Framework should periodically be evaluated and refreshed as deemed necessary by the PIOB and the standard-setting Boards. Changes to the Public Interest Framework shall be made in accordance with normal due process requirements.

The Framework sets out considerations essential to the judgments needed by the Boards when developing their standards and by the PIOB in its oversight of the responsiveness of the standard-setting process to the public interest. The Framework, together with due process,³⁴ articulate the public interest responsiveness of international audit-related standard-setting.

The Framework recognizes the criticality of well-functioning, competent and authoritative standard-setting boards, and a competent, alert, and well-informed oversight body, with clarity

³³ This would include standards for audit, review, and related services engagements. This would also include standards on quality control for those engagements along with ethical and independence requirements for accountants.

³⁴ The Boards follow due process as approved by the PIOB and subject to Monitoring Group oversight. Adherence to, and oversight of, due process by the Boards ensures that all necessary procedures for the development of high-quality international standards have been executed, thereby enabling the appropriate evaluation, balancing and weighing of evidence and diverse stakeholder viewpoints.

around their respective roles. A public interest mindset must permeate both. Transparency, monitoring and continuous dialogue are essential.

The Framework's Goal, Approach and Structure

The goal of the Framework is to ensure that standards are responsive to the public interest, through:

- Reinforcement of the importance of independence in a standard-setting process benefitting from deep technical expertise and diversity of perspectives;
- A common understanding by the Boards and PIOB about the meaning of responsiveness to the public interest and which judgments are required for achieving that objective;
- Focus by the Boards on the public interest in their development of the standards;
- Independent PIOB oversight, giving stakeholders confidence that the two Boards set standards that are in the public interest; and
- Appropriate accountability of the PIOB and the two Boards in fulfilling their mandates.

The Framework is developed with the view that the public interest is observed throughout the full cycle of a standard's development: this includes the standard-setting planning, structure and process level, as well as the PIOB's independent oversight.

The Framework is structured around responses to the following questions:

- For whom are standards developed?
- What interests need to be served?
- How are the interests of users best served?
- What qualitative characteristics should the standards exhibit?
- How is the public interest responsiveness of a standard assessed?
- What special considerations are required for international audit-related standards, given their particular public interest relevance?

For whom are standards developed?

Different classes of stakeholders can have legitimate interest in the adequacy of any given standard. For the purposes of this Framework, five broad groups of stakeholders are considered:

- *Users of financial statements* (“the users”) – mainly investors, lenders, and other creditors, who rely on the audited financial statements to make resource allocation decisions.
- The *profession* – all auditors and assurance providers, and other professional accountants in public practice and business who apply the standards.
- Those in charge of *adoption, implementation and enforcement* of the standards as well as monitoring of the capital markets who rely on such standards– including national standard setters, regulators and audit inspectors, market authorities, public sector bodies, and professional accountancy organizations.
- *Preparers* – management and professional accountants in business, for entities of all sizes, in either the public or private sectors, as well as those charged with governance (e.g., audit committees who oversee the audit process), the latter group being relevant to addressing the information asymmetries among different parties involved in the functioning of companies, and who also provide the basis for the auditor’s work.
- *Other users* – the reliability of financial and non-financial information affects a very wide range of interests in society, including consumers, taxpayers, employees, competition and prudential authorities, central banks and bodies in charge of financial stability oversight, and those granting public contracts.

The public interest of standards cannot be ensured through a mere aggregation of all stakeholder interests. Such interests may be mutually inconsistent; some will reflect a stakeholder group’s ability and resources to access the information necessary to protect their interests, while others may have limited capacity to do so; and different stakeholders have different capacities to convey their views. The public interest therefore requires weighing and balancing all stakeholder views.

While the Framework recognizes the importance of all of the above stakeholders, it focuses primarily on the interests of users, and more specifically the longer-term interests of creditors and

investors and the protection of those interests. Creditor and investor decisions are key to the correct functioning of financial markets, but there are creditors and investors who may not always be equipped to contribute effectively to the standard-setting process. These include direct shareholders, debt holders, and those indirectly holding a company's equity or debt, for instance through investment funds or pension funds.

What interests need to be served?

Standards are more likely to respond to users' needs when developed primarily with a view to building trust in the financial and non-financial reporting process. This compels standard setters to carefully consider input from stakeholders seeking standards that:

- Promote consistent practice and behaviors by auditors and assurance providers, other professional accountants in public practice, and professional accountants in business across jurisdictions;
- Facilitate identification of areas most relevant to the business of an audited company, and drive effective measures to respond to related risks;
- Reinforce the professional accountant's role and mindset and the auditor's professional skepticism needed in gathering evidence, challenging assumptions, and developing conclusions; and
- Ensure transparent, independent, rigorous and balanced reporting that prompts the adoption of appropriate measures by those charged with governance, as well as corrective action by oversight bodies, including prudential and market authorities, also to address any potential threat to financial stability.

How are the interests of users best served?

In order to address those interests, the development of standards requires:

- A permanent *structure* that commits explicitly to pursuing the public interest through: i) independence of the Boards in making decisions concerning the standards, ii) balanced, diverse and global participation of stakeholder groups while preventing undue and

dominant influences; iii) stable funding, adequate resources, and appropriately skilled and experienced staff; iv) mechanisms to ensure adherence to sound governance and operating procedures; v) meaningful accountability; and vi) appropriately diverse expertise in board members.

- A standard-setting *process* to ensure that the defined structure: i) considers all stakeholder input and identifies the different stakeholder interests that affect the public interest; ii) defines relevant public interest criteria to consider how to appropriately weigh the input received in terms of the public interest impact of the relative interests; and iii) appropriately balances alternative outcomes and interests in terms of their expected responsiveness to the public interest. This process should recognize the importance of all stakeholders referred to previously but it should focus primarily on the interests of users.
- *Independent, direct oversight* by the PIOB of the Boards' adherence to their agreed strategies, due process, and responsiveness to the public interest, during the development of a standard and, on reflection, upon the final outcome of the process.

User needs, and therefore the public interest, are dynamic, societal concepts that evolve over time. The entire system comprising independent standard-setting and oversight therefore must also remain alert to shifting needs and perceptions and be capable of flexibility of responses; the system must, however, also maintain fundamental stability and the long-term validity and credibility of principles-based standards in order to ensure continuity and inspire confidence.

What qualitative characteristics should the standards exhibit?

A set of qualitative characteristics are to be used as criteria by the Boards and PIOB to assess a standard's responsiveness to the public interest. A non-exhaustive list of such characteristics includes a standard's:

- *Consistency* with priorities established through a strategic planning process, based on the assessment of public interest and stakeholder needs;
- *Coherence* with the overall body of standards, including that requirements addressing the same subject matter are not in conflict;

- Appropriate *scope* to address the identified key issues, and to clearly specify to whom the standard applies;
- *Scalability*, including the proportionality to the standard's relative impact on different stakeholders, e.g., how a standard addresses the audit or assurance needs of small and medium sized enterprises (SMEs) as well the needs of complex, listed entities;
- *Timeliness* in addressing identified needs without sacrificing quality;
- *Relevance*, through recognizing and responding to emerging issues, changes in business or public practice environments, developments in accounting practices, or changes in technology, and developing principles-based requirements that enable the objectives of those requirements to be achieved in differing circumstances;
- *Completeness*, in reflecting the results of broad consultation and in balancing stakeholder priorities;
- *Comprehensiveness*, through limiting the extent to which there are exceptions to the principles set out;
- *Clarity and conciseness*, to enhance understandability and minimize the likelihood of differing interpretations, and thus supporting proper intended application and facilitating implementation;
- *Implementability*, and ability of being *consistently applied and globally operable* across entities of all sizes and regions, respectively, as well as considerations of the different conditions prevalent in different jurisdictions. Standards that cannot be adopted, or cannot be implemented by practitioners are not of much use; and
- *Enforceability*, through clearly stated responsibilities that make it possible to ascertain the extent to which an auditor or professional accountant has complied with the standards.

How is the public interest responsiveness of a standard assessed?

The public interest responsiveness of any new or revised standard is assessed through the Boards considering the qualitative characteristics discussed above and the following steps:

- Identify the varying perspectives and needs of groups with legitimate interests in relation to each standard, throughout the full cycle of its development;
- Define the desired goal that would allow the standard to best serve users' needs. Such goal could be defined in terms of a required audit or assurance practice or auditor/professional accountant behavior, or the introduction of guidance informing the application of practice or behavior already agreed upon;
- Identify criteria to assess the standard's responsiveness to the defined goal, in terms of the qualitative characteristics that the standard should exhibit;³⁵
- According to the criteria, reasonably weigh input from the different groups; and
- Given the defined goal, assess the expected contribution of the standard to users' needs, and consider whether it is responsive to the public interest according to this Framework.

Assessing whether standards are in the public interest requires careful application of judgment, which this Framework seeks to guide both for the Boards and for the PIOB. This judgment is best informed when the standards' development and consultation process elicits all stakeholder views and focus is placed on assessing the merits of the various views, irrespective of whether the views are a minority or majority.

The PIOB should provide oversight of the standard-setting process, by ensuring that due process has been followed by the Boards in developing a standard and that the standards respond to the public interest in accordance with steps and qualitative characteristics set out above. For that purpose, the PIOB has full access to all necessary information of the Boards.

The PIOB communicates its views and the basis thereof to the Boards, in a timely manner throughout the standard-setting process and works collaboratively with the Boards to understand the input received, how decisions were made and then to resolve any remaining differing views.

³⁵ As an example, if reinforcing the auditor's exercise of professional skepticism was considered a goal to be pursued through a particular standard, ensuring that auditors remained professionally skeptical in the wake of changes in measurement bases would be key to determining the standard's responsiveness to public interest, and hence the qualitative characteristics of *timeliness* and *relevance* would be important assessment criteria.

What special considerations are required for international audit-related standards, given their particular public interest relevance?

External audit is intended to provide reasonable assurance around management's fair representation of a company's financial position and performance in all material respects, in the context of the applicable financial reporting framework and taking account of its business model and risk profile. It improves transparency, mitigating the risks of particular information being obscured to the detriment of users of financial statements, and thus enhancing their confidence and ability to make efficient resource allocation decisions. High quality external audit supports the smooth functioning of capital markets, overall economic performance and financial stability.

The Framework assumes that external audits should contribute to mitigating the information asymmetries among different parties involved in the functioning of companies, thus enhancing the reliability of financial information and contributing to more efficient resource allocation decisions. This contributes to the efficient functioning of capital markets, improving overall economic performance and financial stability. This Framework seeks to ensure high quality and relevance through internationally recognized and accepted standards that are consistently applied, and considers the interests of users of financial statements, particularly a broad range of creditors and investors irrespective of their size and sophistication, as those most likely to contribute to such goal. Giving those interests prominence when developing a standard is in accordance with the remit of the Monitoring Group member organizations.

Standards setting out the appropriate requirements and guidance, and promoting consistent audit practice across jurisdictions, are a necessary step to the development of audits that reassure the confidence of users in the reliability of financial statements. When appropriately implemented and enforced, standards contribute to ensuring the high quality of external audits. International audit-related standards promote the integrity and consistency of practices in capital markets, and encourage mobility of auditors between different jurisdictions.

In the long term, standards also enhance the confidence in, and reputation of the global auditing and assurance profession, promoting trust in the decisions of those tasked with enforcement, and contributing to the recognition of management's stewardship role.

E. Appendix: Impact Assessment

The Monitoring Group's impact assessment setting out the benefits of its recommendations is conducted in relation to the status quo. The anticipated benefits of the recommendations set out in this paper are:

- Greater focus on public interest, which may in turn result in standards requiring an increased work effort, likely to have a mitigating impact on the risk of audit failure in future;
- A transparent and accountable process which sets out the importance of the Boards' carrying out impact assessments and post-implementation reviews which demonstrate how effective a standard has been in meeting the objectives set for it. That process also includes public accountability for the PIOB in the allocation of resources to further the public interest;
- Enhanced staffing capacity, providing greater flexibility in resource allocation to reduce the development time for new or revised standards, better supporting the needs of the market through more timely and relevant material;
- The use of a multi-stakeholder model for the Boards, PIOB and due process that broadens participation and the diversity of views available to support the standard-setting process in a way that better serves the public interest. This in turn is supported by advisory councils, which include stronger participation by national standard setters; and
- Through addressing stakeholder concerns, maintaining the value to the global economy of a high-quality and consistent approach to deliver audits.

The Monitoring Group does not have data which would support the accurate estimation of the benefits that arise from the recommendations in this paper, as they have yet to be implemented. However, the Monitoring Group believes those benefits would be significant in qualitative terms to stakeholders, and strongly align to matters of (a) stakeholder confidence, and in particular that of primary users of financial statements, as defined in the Public Interest Framework; and (b) the effective functioning of capital markets and resulting economic and financial stability.

Additionally, as the starting point for standard-setting remains the existing standards, we do not believe this would be disruptive to those who use these standards for the delivery of audits and other assurance-based engagements, thus minimizing costs. Indeed, the Monitoring Group believes that a new model that is better resourced to bring revised standards to market more quickly, and better respond to the increasingly complex needs of audits will deliver a further benefit.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 9.1
Meeting date: 2 September 2020
Subject: ED 600 Group Audits
Date: 20 August 2020
Prepared by: Peyman Momenan

Action Required

For Information Purposes Only

Agenda Item Objectives

To:

- RECEIVE an update on the amendments (subsequent to feedback received from stakeholders) to the IESBA's ED, *Proposed Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants*

Background

1. The IESBA released an exposure draft of Proposed Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants in July 2019.
2. The ED propose to:
 - revise paragraph R120.5 of the Code to include a new element that professional accountants should "have an inquiring mind" when applying the conceptual framework (and avoid using the term professional scepticism when discussing such expectation).
 - Highlight the wide-ranging role of the accountancy profession in society and the relationship between compliance with the Code and a professional accountant's responsibility to act in the public interest.
 - Include enhancements to the fundamental principles of objectivity and professional behaviour.
 - Strengthen the fundamental principle of integrity to include the determination to act appropriately in difficult situations.
 - Include some enhancements that reflect the impact of technology.
 - Highlight the importance of being aware of bias and having the right organizational culture.

3. The NZAuASB submitted its comments on the ED to the IESBA in October 2019 (agenda item 9.3 includes a copy of the submission). The NZAuASB agreed with the proposed changes and supported the ED. The NZAuASB made one suggested change to the introduction paragraph of the revised section of the Code. The IESBA, in considering stakeholder feedback, has amended this paragraph according to the NZAuASB's suggestions.
4. In March 2020, the IESBA considered the feedback received from stakeholders on the ED and the IESBA technical team's analysis of these comments. Overall, the respondents were generally supportive of the objectives of the Role and Mindset project and the proposals in the ED. Consequently, the IESBA only introduced limited amendments to improve the proposals. None of the amendments are substantively changing the nature of the proposals in the ED.
5. Agenda item 9.2 shows the original proposal in the ED, the NZAuASB's comment on the corresponding questions raised in the ED's Invitation to Comment and the final draft of the revised Code (amended for received feedback as necessary) that was approved by the IESBA at its June 2020 meeting, to be released after PIOB approval.
6. We have not identified any compelling reasons to amend the IESBA's approved revisions to the Code to promote the role and mindset expected of Professional Accountants. We intend to amend PES-1 for the revisions to the IESBA Code for the Board's approval at the October meeting, subject to approval by the PIOB.

Matters for Consideration

7. For the Board to:
 - NOTE the changes to the ED in finalising the *Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants*

Material Presented

Agenda item 9.1	Board Meeting Summary Paper
Agenda item 9.2	A comparison between the proposed changes in the ED, the NZAuASB comments and the amended revised Code
Agenda item 9.3	The NZAuASB submission regarding the IESBA's <i>Proposed Revisions to the Code to Promote the Role and Mindset Expected of Professional Accountants</i>

1. Do you support the proposals in Section 100 that explain the role and values of professional accountants as well as the relationship between compliance with the Code and professional accountants acting in the public interest? Are there other relevant matters that should be highlighted in these paragraphs?

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p>General Introduction</p> <p>100.1 A1 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. The Code sets out the ethical behaviors and approach to professional activities expected of professional accountants. Compliance with the Code enables accountants to meet their responsibility to act in the public interest and involves upholding the ethical values upon which the Code is based as well as complying with the specific requirements of the Code. In acting in the public interest, a professional accountant's responsibility is not exclusively to satisfy the needs, preferences or requirements of an individual client or employing organization when performing professional activities. Therefore, the Code contains requirements and application material to enable professional accountants to meet their responsibility to act in the public interest.</p> <p>100.1 A2 Businesses, governments and other organizations involve professional accountants in a broad range of matters. Accountants understand and acknowledge that these organizations do so because they recognize the skills and values that the accountants bring to the professional activities they undertake through:</p> <p>(a) Adherence to ethical principles and professional standards; (b) Use of business acumen; (c) Application of expertise on technical and other matters; and (d) Exercise of professional judgment.</p> <p>The application of these skills and values enables professional accountants to provide advice or other output that is fit for the purpose for which it was provided, and which might be relied upon by intended users of such output.</p> <p>100.1 A3 The Code sets out high quality ethics standards for adoption by professional accountancy organizations which are members of the International Federation of Accountants (IFAC), or for use by such members as a basis for their codes of ethics. The Code may also be used or adopted by those responsible for setting ethics standards for professional accountants in their jurisdictions and by firms in developing their ethics policies.</p> <p>Fundamental Principles and Conceptual Framework</p> <p>100.2 A1 The Code sets out the ethical behaviors and approach to professional activities expected of professional accountants in meeting their responsibility to act in the public interest.</p> <p>100.2 A2 The Code establishes five fundamental principles to be complied with by all professional accountants. It also includes a conceptual framework that sets out the approach to be taken to identify, evaluate and address threats to compliance with those fundamental principles and, for audits and other assurance engagements, threats to independence.</p> <p>100.2 A3 The remainder of the Code applies the fundamental principles and the conceptual framework to a range of facts and circumstances that professional accountants may encounter, whether in business or in public practice.</p>	<p>We support the proposed additions to paragraph 100.1 A1 of the Code. However, in our opinion the paragraph will have a better flow if the last sentence of the proposed paragraph is moved up to follow the first sentence. We suggest the following edits to paragraph 100.1 A1</p> <p>100.1 A1 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. In acting in the public interest, a professional accountant's responsibility is not exclusively to satisfy the preferences or requirements of an individual client or employing organization when performing professional activities. <u>A professional accountant is also responsible for maintaining and enhancing the public trust in the profession.</u> The Code sets out the ethical behaviors and approach to professional activities expected of professional accountants. Compliance with the Code enables accountants to meet their responsibility to act in the public interest and involves upholding the ethical values upon which the Code is based as well as complying with the specific requirements of the Code. <u>In acting in the public interest, a professional accountant's responsibility is not exclusively to satisfy the preferences or requirements of an individual client or employing organization when performing professional activities.</u></p> <p>100.1 A2 The public trust in the accountancy profession underpins why businesses, governments and other organizations involve professional accountants in a broad range of matters. <u>Accountants understand and acknowledge that these organizations do so because they recognize the skills and values that the accountants bring to the professional activities they undertake through:</u></p> <p>(a) Adherence to ethical principles and professional standards; (b) Use of business acumen; (c) Application of expertise on technical and other matters; and (d) Exercise of professional judgment;</p> <p>are fundamental for upkeeping this public trust. The application of these skills and values enables professional accountants to provide advice or other output that is fit for the purpose for which it was provided, and which might be relied upon by intended users of such output.</p>	<p>Introduction</p> <p>100.1 A1 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest.</p> <p>100.1 A2 <u>Public trust in the accountancy profession is the reason why</u> businesses, governments and other organizations involve professional accountants in a broad range of matters. <u>Accountants understand and acknowledge that these organizations do so because they recognize the skills and values that the accountants bring to the professional activities they undertake are fundamental to maintaining public trust and include through:</u></p> <p>(a) Adherence to ethical principles and professional standards; (b) Use of business acumen; (c) Application of expertise on technical and other matters; and (d) Exercise of professional judgment.</p> <p>The application of these skills and values enables professional accountants to provide advice or other output that <u>is fit for</u> the purpose for which it was provided, and which might be relied upon by the intended users of such output.</p> <p>100.1 A3 <u>The Code sets out high quality standards of ethical behavior and the approach to professional activities expected of professional accountants. The Code sets out high quality ethics standards for adoption by professional accountancy organizations which are members of the International Federation of Accountants (IFAC), or for use by such members as a basis for their codes of ethics. The Code may also be used or adopted by those responsible for setting ethics standards for professional accountants in particular sectors or their jurisdictions and by firms in developing their ethics and independence policies.</u></p> <p>Fundamental Principles and Conceptual Framework</p> <p>100.2 A1 The Code sets out the ethical behaviors and approach to professional activities expected of professional accountants in meeting their responsibility to act in the public interest.</p> <p>100.1 A2 The Code establishes five fundamental principles to be complied with by all professional accountants. It also includes a conceptual framework that sets out the approach to be taken to identify, evaluate and address threats to compliance with those fundamental principles and, for audits and other assurance engagements, threats to independence.</p> <p>100.2 A3 The remainder of the Code also applies the fundamental principles and the conceptual framework to a range of facts and circumstances that professional accountants may encounter, whether in business or in public practice.</p> <p>100.1 A5 <u>(Moved from 100.1 A1) The Code sets out the ethical behaviors and approach to professional activities expected of professional accountants. Upholding the ethical concepts embodied in the fundamental principles and compliance with the specific requirements of the Code. Compliance with the Code enables assist professional accountants to in meeting their responsibility to act in the public interest and involves upholding the ethical values upon which the Code is based as well as complying with the specific requirements of the Code. In acting in the public interest, in meeting this public interest responsibility, a professional accountant's responsibility is not does not consider only exclusively to satisfy the preferences or requirements of an individual client or employing organization when performing professional activities.</u></p>

The IESBA did not agree to include the NZAuASB suggestion to emphasize that "A professional accountant is also responsible for maintaining and enhancing the public trust in the profession". This is not a fatal flaw in our opinion.

The IESBA has amended this paragraph (paragraph 100.1 A2) according to the NZAuASB suggestions.

2. Do you support the inclusion of the concept of determination to act appropriately in difficult situations and its position in Subsection 111?

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p>SUBSECTION 111 – INTEGRITY</p> <p>R111.1 A professional accountant shall comply with the principle of integrity, which requires an accountant to be straightforward and honest in all professional and business relationships.</p> <p>111.1 A1 Integrity implies fair dealing and truthfulness.</p> <p>111.1 A2 Integrity also includes having the determination to act appropriately when confronting dilemmas or difficult situations. This would involve, for example:</p> <ul style="list-style-type: none"> • Standing one's ground when facing pressure to do otherwise during the course of performing professional activities, or • Challenging others as and when appropriate, even when doing so creates potential adverse personal or organizational consequences. 	<p>Yes. We support the proposed additions in paragraph 111.1 A2.</p>	<p>SUBSECTION 111 – INTEGRITY</p> <p>R111.1 A professional accountant shall comply with the principle of integrity, which requires an accountant to be straightforward and honest in all professional and business relationships.</p> <p>111.1 A1 Integrity implies involves fair dealing, and truthfulness, and</p> <p>111.1 A2 Integrity also includes having the strength of character to act appropriately when confronting dilemmas or difficult situations.</p> <p>111.1 A2 Acting with integrity This would also involve, for example:</p> <ul style="list-style-type: none"> • Standing one's ground when facing pressure to do otherwise during the course of performing professional activities; or • Challenging others as and when appropriate, during the course of performing professional activities even when doing so might create potential adverse personal or organizational consequences.

The IESBA concluded that no further changes (other than some editorial and language usage editions) is needed as the majority of stakeholders supported the proposals and the suggested amendments were unlikely to make a substantive change to the ED.

3. Do you support the proposal to require a professional accountant to behave in a manner that is consistent with the profession's responsibility to act in the public interest in paragraphs 110.1 A1 (e) and R115.1.

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p>110.1 A1 There are five fundamental principles of ethics for professional accountants:</p> <p>(a) Integrity – to be straightforward and honest in all professional and business relationships.</p> <p>(b) Objectivity – not to compromise exercise professional or business judgments without being compromised by because of:</p> <p>(i) Bias;</p> <p>(ii) Conflict of interest, or (iii) undue influence of others, or undue reliance on individuals, organizations, technology or other factors.</p> <p>(c) Professional Competence and Due Care – to:</p> <p>(i) Attain and maintain professional knowledge and skill at the level required to ensure that a client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation; and</p> <p>(ii) Act diligently and in accordance with applicable technical and professional standards.</p> <p>(d) Confidentiality – to respect the confidentiality of information acquired as a result of professional and business relationships.</p> <p>(e) Professional Behavior – to:</p> <p>(i) Behave in a manner that is consistent with the profession's responsibility to act in the public interest;</p> <p>(ii) Avoid any conduct that the professional accountant knows or should know might discredit the profession, and</p> <p>(iii) Comply with relevant laws and regulations, and.</p> <p>R110.2 A professional accountant shall comply with each of the fundamental principles.</p> <p>110.2 A1 The fundamental principles of ethics establish the standard of behavior expected of a professional accountant. The conceptual framework establishes the approach which an accountant is required to apply to assist in complying with those fundamental principles. Subsections 111 to 115 set out requirements and application material related to each of the fundamental principles.</p>		<p>110.1 A1 There are five fundamental principles of ethics for professional accountants:</p> <p>(a) Integrity – to be straightforward and honest in all professional and business relationships.</p> <p>(b) Objectivity – to exercise professional or business judgments without being compromised by:</p> <p>(i) Bias;</p> <p>(ii) Conflict of interest; or</p> <p>(iii) Undue influence of, or undue reliance on, individuals, organizations, technology or other factors.</p> <p>(c) Professional Competence and Due Care – to:</p> <p>(i) Attain and maintain professional knowledge and skill at the level required to ensure that a client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation; and</p> <p>(ii) Act diligently and in accordance with applicable technical and professional standards.</p> <p>(d) Confidentiality – to respect the confidentiality of information acquired as a result of professional and business relationships.</p> <p>(e) Professional Behavior – to:</p> <p>(i) Behave in a manner that is consistent with the profession's responsibility to act in the public interest when performing professional activities;</p> <p>(ii) Avoid any conduct that the professional accountant knows or should know might discredit the profession; and</p> <p>(iii) Comply with relevant laws and regulations.</p> <p>R110.2 A professional accountant shall comply with each of the fundamental principles.</p> <p>110.2 A1 The fundamental principles of ethics establish the standard of behavior expected of a professional accountant. The conceptual framework establishes the approach which an accountant is required to apply in complying with those fundamental principles. Subsections 111 to 115 set out requirements and application material related to each of the fundamental principles.</p>

The IESBA concluded that no further changes (other than some editorial and language usage editions) is needed as the majority of stakeholders supported the proposals and the suggested amendments were unlikely to make a substantive change to the ED.

5. Do you agree with the concept of an inquiring mind as set out in the proposals in Section 120?

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p>R120.5 When applying the conceptual framework, the professional accountant shall:</p> <ul style="list-style-type: none"> (a) Exercise professional judgment; (b) Have an inquiring mindRemain alert for new information and to changes in facts and circumstances; and (c) Use the reasonable and informed third party test described in paragraph 120.5 A6. <p>Exercise of Professional Judgment</p> <p>120.5 A1 Professional judgment involves the application of relevant training, professional knowledge, skill and experience commensurate with the facts and circumstances, including the nature and scope of the particular professional activities, and the interests and relationships involved.</p> <p>120.5 A2 In relation to undertaking professional activities, the exercise of professional judgment is required when the professional accountant applies the conceptual framework in order to make informed decisions about the courses of actions available, and to determine whether such decisions are appropriate in the circumstances. In making this determination, the accountant might consider matters such as whether:</p> <ul style="list-style-type: none"> • The accountant's expertise and experience are sufficient to reach a conclusion. • There is a need to consult with others with relevant expertise or experience. • The accountant's own preconception or bias might be affecting the accountant's exercise of professional judgment. <p>Inquiring Mind</p> <p>120.5 A12 An understanding of known facts and circumstances is a prerequisite to the proper application of the conceptual framework. Determining the actions necessary to obtain this understanding and coming to a conclusion about whether the fundamental principles have been complied with also require the exercise of professional judgment. Obtaining this understanding entails having an inquiring mind, which means:</p> <ul style="list-style-type: none"> (a) Being open and alert for situations and information (or the lack thereof) that might require further investigation; and (b) Considering whether there is a need to critically evaluate the information obtained, having regard to the nature, scope and outputs of the professional activity being undertaken. <p>120.5 A13 In exercising professional judgment to obtain this understanding in determining if further investigation is necessary, the professional accountant might consider, among other matters, whether:</p> <ul style="list-style-type: none"> • New information has emerged or whether there have been changes in facts and circumstances • There is reason to be concerned that potentially relevant information might be missing from the facts and circumstances known to the accountant. • There is an inconsistency between the known facts and circumstances and the accountant's expectations. • The accountant's expertise and experience are sufficient to reach a conclusion. • There is a need to consult with others with relevant expertise or experience. • The information provides a reasonable basis on which to reach a conclusion. • The accountant's own preconception or bias might be affecting the accountant's exercise of professional judgment. • There might be other reasonable conclusions that could be reached from the available information obtained. <p>120.5 A5 When undertaking any professional activities, paragraph R120.5 requires all professional accountants to have an inquiring mind when applying the conceptual framework. Additionally, accountants performing audits, reviews and other assurance engagements are required to exercise professional skepticism as described in paragraphs 120.16 A1 and 120.16 A2.</p>	<p>Yes, we agree with the proposed concept. We support the IESBA proposed approach to restrict the use of professional scepticism when discussing audit, review and other assurance engagements and support the addition of the proposed paragraph 120.5 A5 to clarify this approach.</p>	<p>R120.5 When applying the conceptual framework, the professional accountant shall:</p> <ul style="list-style-type: none"> (a) Exercise professional judgment; (b) Have an inquiring mind; and (c) Use the reasonable and informed third party test described in paragraph 120.5 A6. <p>Exercise of Professional Judgment</p> <p>120.5 A1 Professional judgment involves the application of relevant training, professional knowledge, skill and experience commensurate with the facts and circumstances, including having regard to the nature and scope of the particular professional activities, and the interests and relationships involved.</p> <p>120.5 A2 Professional judgment is required when the professional accountant applies the conceptual framework in order to make informed decisions about the courses of actions available, and to determine whether such decisions are appropriate in the circumstances. In making this determination, the accountant might consider matters such as whether:</p> <ul style="list-style-type: none"> • The accountant's expertise and experience are sufficient to reach a conclusion. • There is a need to consult with others with relevant expertise or experience. • The accountant's own preconception or bias might be affecting the accountant's exercise of professional judgment. <p>Having an Inquiring Mind</p> <p>120.5 A3 An inquiring mind is a prerequisite to obtaining a understanding of known facts and circumstances is a prerequisite to necessary for the proper application of the conceptual framework. Obtaining this understanding entails h Having an inquiring mind involves considering, which means:</p> <ul style="list-style-type: none"> (a) The source, relevance and sufficiency of information obtained having regard to the nature, scope and outputs of the professional activity being undertaken; and (a) Being open and alert for situations and information (or the lack thereof) that might require further investigation; and (b) Considering whether there is a need to critically evaluate for further investigation or other action the information obtained, having regard to the nature, scope and outputs of the professional activity being undertaken. <p>120.5 A4 In When considering the adequacy of the source, relevance and sufficiency of information obtained determining if further investigation is necessary, the professional accountant might consider, among other matters, whether:</p> <ul style="list-style-type: none"> • New information has emerged or whether there have been changes in facts and circumstances. • There is reason to be concerned that potentially relevant information might be missing from the facts and circumstances known to the accountant. • There is an inconsistency between the known facts and circumstances and the accountant's expectations. • The information provides a reasonable basis on which to reach a conclusion. • There might be other reasonable conclusions that could be reached from the information obtained. <p>120.5 A5 When undertaking any professional activities, p paragraph R120.5 requires all professional accountants to have an inquiring mind when applying the conceptual framework to identify, evaluate and address threats to the fundamental principles. Having an inquiring mind has a different purpose to the exercise of professional skepticism. Additionally, a accountants performing audits, reviews and other assurance engagements are required to exercise professional skepticism in order to critically assess evidence as described in paragraphs 120.16 A1 and 120.16 A2.</p>

With respect to the first key consideration in having an inquiring mind (paragraph 120.5 A3(a)) the IESBA agreed to clarify that the concept of inquiring mind involves professional accountants not accepting information at face value but rather needing to duly consider the source, relevance and sufficiency of the information obtained in order to inform the next steps.

This revision also clarifies that the extent of the consideration and evaluation will depend on the scope and outputs of the professional activities.

6. Do you support the approach to addressing bias? If so, do you agree with the list of examples of bias set out in paragraph 120.12 A2? Should any examples be omitted or new ones added?

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p>Other Considerations when Applying the Conceptual Framework</p> <p><u>Bias</u></p> <p>120.12 A1 Being aware of the risk of bias, whether conscious or unconscious, is important to the exercise of professional judgment when identifying, evaluating and addressing threats to compliance with the fundamental principles.</p> <p>120.12 A2 Examples of bias to be aware of when exercising professional judgment include:</p> <ul style="list-style-type: none"> • Anchoring bias, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed. • Automation bias, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to whether such output is reliable or fit for purpose. • Availability bias, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not. • Confirmation bias, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief. • Groupthink, which is a tendency to think or make decisions as a group that discourages creativity or individual responsibility. • Overconfidence bias, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions. • Representation bias, which is a tendency to base an understanding on a pattern of experiences, events or beliefs that is considered to be representative. • Selective perception, which is a tendency for a person's expectations to influence how the person views a particular matter or person. <p>120.12 A3 The impact of bias might be mitigated by involving others or seeking advice from experts to provide additional input or appropriate challenge as part of the evaluation process.</p>	<p>Yes, we support the approach and the examples included. We would also recommend including the definition of bias in the Glossary.</p>	<p>Other Considerations when Applying the Conceptual Framework</p> <p><u>Bias</u></p> <p>120.12 A1 Being aware of the risk of bias, whether conscious or unconscious, bias affects is important to the exercise of professional judgment when identifying, evaluating and addressing threats to compliance with the fundamental principles.</p> <p>120.12 A2 Examples of <u>potential</u> bias to be aware of when exercising professional judgment include:</p> <ul style="list-style-type: none"> • Anchoring bias, which is a tendency to use an initial piece of information as an anchor against which subsequent information is inadequately assessed. • Automation bias, which is a tendency to favor output generated from automated systems, even when human reasoning or contradictory information raises questions as to whether such output is reliable or fit for purpose. • Availability bias, which is a tendency to place more weight on events or experiences that immediately come to mind or are readily available than on those that are not. • Confirmation bias, which is a tendency to place more weight on information that corroborates an existing belief than information that contradicts or casts doubt on that belief. • Groupthink, which is a tendency to think or make decisions as a group that discourages creativity or individual responsibility. (Alternative: "...a tendency for a group of individuals to reach a consensus without critical reasoning or evaluation of the consequences or alternatives") • Overconfidence bias, which is a tendency to overestimate one's own ability to make accurate assessments of risk or other judgments or decisions. • Representation bias, which is a tendency to base an understanding on a pattern of experiences, events or beliefs that is considered to be representative. • Selective perception, which is a tendency for a person's expectations to influence how the person views a particular matter or person. <p>120.12 A3 Actions that might mitigate the impact of bias might be mitigated by include, for example:</p> <ul style="list-style-type: none"> • involving others or seeking advice from experts to provide additional input. • Consulting with others to ensure appropriate challenge as part of the evaluation process. • Receiving self-awareness training on the risk of bias as part of professional development.

The IESBA concluded that the received feedback did not indicate a need to change the proposed changes in the ED. The only additional change is the addition of "Self-awareness training on the risk of bias as part of professional development" added to paragraph 120.12 A3

7. Are there any other aspects about organizational culture in addition to the role of leadership that you consider should be addressed in the proposals?

The proposed changes in the ED	The NZAuASB feedback to the IESBA on the proposed change	The IESBA amendments to the ED due to stakeholders' feedback.
<p><u>Organizational Culture</u></p> <p>120.13 A1 The effective application of the conceptual framework is enhanced when the importance of ethical values that align with the fundamental principles and other provisions set out in the Code is promoted through the internal culture of an organization.</p> <p>120.13 A2 The promotion of that ethical culture within an organization is most effective when:</p> <p>(a) Leaders and those in managerial roles hold themselves and others accountable for demonstrating the ethical values of the organization;</p> <p>(b) Appropriate education and training programs, management processes, and performance evaluation criteria that promote that ethical culture are in place; and</p> <p>(c) Ethical values are adhered to in dealings with third parties.</p> <p>Considerations for Audits, Reviews and Other Assurance and Related Services Engagements</p> <p><u>Firm Culture</u></p> <p>120.14 A1 For professional accountants in public practice, [proposed] ISQM 1 sets out requirements and application material relating to firm culture in the context of a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements or other assurance or related services engagements.</p>	<p>We believe it is important for any organisation to understand what are the potential drivers and pressures that encourage departure from ethical values and principles.</p>	<p><u>Organizational Culture</u></p> <p>120.13 A1 The effective application of the conceptual framework is enhanced when the importance of ethical values that align with the fundamental principles and other provisions set out in the Code is promoted through the internal culture of an organization.</p> <p>120.13 A2 The promotion of that an ethical culture within an organization is most effective when:</p> <p>(a) Leaders and those in managerial roles <u>promote the importance of, and</u> hold themselves and others accountable for demonstrating the ethical values of the organization;</p> <p>(b) Appropriate education and training programs, management processes, and performance evaluation <u>and reward</u> criteria that promote that an ethical culture are in place; and</p> <p><u>(c) Effective whistle-blowing policies and procedures are in place to protect those who report illegal or unethical behavior; and</u></p> <p><u>(d) The organization adheres to</u> Ethical values are adhered to in its dealings with third parties.</p> <p><u>120.13 A3 Professional accountants are expected to encourage and promote an ethics-based culture in an organization, to the extent that they are able to do so, having regard to their position and seniority.</u></p> <p>Considerations for Audits, Reviews, Other Assurance and Related Services Engagements</p> <p><u>Firm Culture</u></p> <p>120.14 A1 For professional accountants in public practice, [p]roposed ISQM 1 sets out requirements and application material relating to firm culture in the context of a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements.</p>

The IESBA introduced two changes to ED due to the received feedback.

- 1) Some respondents highlighted the importance of whistle-blowing policies and procedures that protect those who choose to report unethical behavior in promoting an ethical organizational culture. They recommended that such policies be included in paragraph 120.13 A2. The IESBA has included paragraph 120.13 A2 (c) to reflect this feedback.
- 2) Several respondents noted that the responsibility to promote an ethical culture within an organization is not restricted to those at the top. They suggested that the material should highlight a PA's responsibility in promoting such culture, irrespective of their role and the prevailing organizational ethical culture. Accordingly, the IESBA added paragraph 120.13 A3 to reflect this feedback.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 10.1
Meeting date: 2 September 2020
Subject: Agreed-Upon Procedures Engagements
Date: 18 August 2020
Prepared By: Sharon Walker

Action Required

For Information Purposes Only

Agenda Item Objectives

1. The objective of this agenda item is for the Board to:
 - Provide initial views on proposed compelling reason changes to the Agreed-Upon Procedures Engagements standard being considered by the AUASB, including whether such proposed changes would be appropriate for the New Zealand standard.

Background

2. The NZAuASB issued ED 2020-2 Proposed International Standard on Related Services (ISRS) (NZ) 4400 *Agreed-Upon Procedures Engagements* in June 2020. ED 2020-2 is based on the IAASB's ISRS 4400. The NZAuASB has not identified any compelling reasons for modification of the international standard.
3. Consistent with the XRB's trans-Tasman harmonisation principles, the NZAuASB also considers compelling reason changes made by the AUASB in finalising its standard.
4. The AUASB issued its exposure draft 01/20 *Proposed Standard on Related Services ASRS 4400 Agreed-Upon Procedures Engagements* in February 2020. The comment period ended May 2020, with the AUASB considering the submissions and the disposition of responses received from stakeholders at its June 2020 meeting.
5. The following matters identify areas where the AUASB is considering modifications to the international standard.

Matters for consideration

Restriction on Use or Distribution

6. Proposed ISRS (NZ) 4400 does not require the AUP report to be restricted to those parties that have agreed to the procedures to be performed or have been specifically included as intended users in the engagement letter. This is in recognition that AUP reports are often provided to users who are not parties to the terms of the engagement.

7. The proposed standard requires the report to contain an identification of the purpose of the AUP report and a statement that the AUP report may not be suitable for another purpose;¹ as well as a statement that the practitioner makes no representation on the appropriateness of the agreed-upon procedures.
8. The practitioner is not precluded from including a restriction paragraph. Application material in proposed ISRS (NZ) 4400 provides guidance on factors that the practitioner may consider in deciding whether to restrict the distribution or use of the AUP report.
9. Six of the eight respondents to the AUASB supported the wording as drafted in the exposure draft, i.e., restriction paragraph not required in the AUP report. Two respondents, however, consider that there should be a restriction on distribution paragraph similar to that of extant ASRS 4400. The AUASB agreed at its June 2020 meeting to a potential compelling reason reflecting principles and practices considered appropriate in maintaining or improving engagement quality in Australia.
10. In New Zealand, APS-1 (revised) requires the use of the report to be restricted to those parties that have either agreed to the procedures to be performed or have been specifically included as users in the engagement letter.

11. What are your initial views about whether a compelling reason change should be considered to ISRS 4400 to require a restriction paragraph be included in all AUP reports in New Zealand?

Other Proposed Amendments

12. The ED does not require the practitioner to be independent when performing an AUP engagement, nor is there a requirement for the practitioner to determine independence. This is consistent with ISRS 4400 and Professional and Ethical Standard 1 which also does not require the practitioner to be independent to perform an AUP engagement. However, requirements pertaining to independence may be specified in national ethical requirements, laws or regulations, other professional requirements, or conditions of a contract, program, or arrangement relation to the subject matter for the agreed-upon procedures engagement, or the practitioner may agree with the engaging party, in the terms of the engagement, to comply with independence requirements.
13. The ED requires disclosure of independence in the AUP report.
 - If the practitioner is not required to be independent and has not otherwise agreed in the terms of the engagement to comply with independence requirements, the AUP report includes a statement that, for the purposes of the engagement, there are no independence requirements.
 - If the practitioner is required to be independent or has agreed in the terms of the engagement to comply with independence requirements, the AUP report includes a statement that the practitioner has complied with relevant ethical requirements and identifies those requirements.

¹ Paragraph 30(d) of proposed ISRS (NZ) 4400.

14. Seven of the eight respondents to the AUASB supported the independence and reporting requirements as drafted in the exposure draft. One respondent does not support the independence requirements and reporting in the exposure draft; rather this respondent considers the extant provision of ASRS 4400 should be retained.
15. The AUASB will consider including example wording in the illustrative engagement letter for situations where the practitioner is required to be independent. This proposed modification has no impact on the requirements of the proposed standard; rather it clarifies a circumstance that is permitted by the proposals.
16. To clarify the assurance practitioner's ethical obligations, the AUASB will consider adding example wording in the illustrative AUP report to indicate that the practitioner is always objective when performing an AUP engagement. Extant ASRS 4400 requires the practitioner to be independent. Modifications to the independence requirements are permitted provided the engaging party explicitly agrees to the modifications in the terms of the engagement.
17. The AUASB is also considering including, as an Appendix, a summary of differentiating factors between agreed-upon procedures engagements and assurance engagements similar to the summary included in extant [ASRS 4400, Appendix 1](#) (refer appendix 1 of this paper).
18. APS-1 (revised)² issued by the New Zealand Institute of Chartered Accountants requires the member, when conducting an agreed-upon procedures engagement, to comply with ethical requirements equivalent to the ethical requirements applicable to "other assurance engagements". Modifications to the independence requirements are permitted provided the engaging party explicitly agrees to these modifications in the terms of the engagement.

19. What are the Board's initial views on:

- Amending the illustrative engagement letter to include example wording to address situations where the practitioner is required to be independent?
- Amending the illustrative AUP report to include a specific reference to objectivity in the statement regarding compliance with ethical requirements when the practitioner is not required/has not agreed to be independent?
- Amending the proposed standard to include a summary of differentiating factors?

Action Requested

20. The Board is asked to provide initial views on proposed compelling reason changes to the Agreed-Upon Procedures Engagements standard being considered by the AUASB,

² APS-1 (revised) Agreed Upon Procedures Engagements to Report Factual Findings

including whether such proposed changes would be appropriate for the New Zealand standard.

Material Presented

Agenda item 10.1

Board Meeting Summary Paper

Appendix 1

(Ref: Para. A5)

Differentiating Factors between Agreed-Upon Procedures Engagements and Assurance Engagements

Differentiating Factor	Agreed-Upon Procedures Engagement	Assurance Engagement
Nature, timing and extent of procedures responsibility of:	Engaging party	Assurance practitioner
Nature, timing and extent of procedures determined in:	Terms of the engagement	Engagement plan
Changes to the nature, timing and extent of procedures are documented in:	Terms of the engagement	Engagement plan
Extent of assurance practitioner's professional judgement exercised in selecting procedures:	Professional judgement may be exercised in assisting the engaging party to identify procedures when agreeing the terms of the engagement, but only professional competence is exercised when conducting the agreed-upon procedures.	Professional judgement exercised in selecting procedures
Sufficiency and appropriateness of evidence assessed by:	Intended user	Assurance practitioner
Form and content of report:	Factual findings, no conclusion or assurance provided	Conclusion providing assurance
Reporting of procedures performed:	Detail of the exact nature, timing and extent of all procedures performed are reported	Summary of work performed
Reporting of findings:	Detail of exact findings resulting from each procedure performed, including errors and exceptions identified, even if rectified.	No detail of findings, unless a modified report is to be issued when the basis for modification is provided or if a management letter is provided in addition to the assurance report.

Agenda Item 11.1



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

DATE: 20 August 2020

TO: Members of the New Zealand Auditing and Assurance Standards Board

FROM: Peyman Momenan

SUBJECT: International Update

Introduction

1. This Update summarises the significant news of the IAASB, other national auditing standards-setting bodies and professional organisations for the Board's information, July and August 2020.

International Federation of Accountants (IFAC)

1. Following the issuance by the Monitoring Group July 14 of [Strengthening The International Audit And Ethics Standard-Setting System](#) (the Paper), the International Federation of Accountants (IFAC) has announced its support for moving immediately to the transition planning phase.

The Paper, which sets forth a series of recommendations to enhance the process by which global audit, assurance and ethics standards for the accountancy profession are developed and issued in the public interest, was the result of a lengthy, multi-stakeholder consultation process.

IFAC is pleased that the Paper recognizes the important and necessary role that IFAC and the profession will continue to play in the standard setting process and that the recommendations are aligned with IFAC's strategy. There are, however, a number of important issues still to be addressed before moving forward with implementation. While IFAC does not underestimate the challenges this presents, we remain confident that we will be able to work collaboratively with all key stakeholders involved to reach a satisfactory resolution during the transition planning phase.

Anti-Fraud Collaboration (AFC):

1. The CAQ's Margot Cella, Vice President, Research and Anti-Fraud Initiatives, [interviews](#) Azlo's Senior Director of Compliance and Internal Control, Dana Lawrence, to explore the pervasiveness of big data and its data ethics and governance implications during the COVID-19 crisis.

International Auditing and Assurance Standards Board (IAASB)

1. The IAASB Ongoing projects (refer to appendix 1)
2. On 26th of June 2020, the IAASB released COVID-19 pandemic-related guidance on auditing accounting estimates and related disclosures. This guidance may help auditors in the current uncertain and evolving environment. Click [here](#) to learn more.
3. On 2nd of July 2020, the IAASB released COVID-19 pandemic-related guidance on Review Engagements on Interim Financial Information. This guidance may help auditors in the current uncertain and evolving environment. Click [HERE](#) to learn more.

4. The IAASB invites interested stakeholders to complete an online survey sharing their experience with, and providing feedback relating to, the Auditor Reporting Standards that were issued in 2015. The Survey also asks for input on your experiences with ISA 720 (Revised), *The Auditor's Responsibilities relating to Other Information*. The link below will direct you to the IAASB webpage for further information on the Auditor Reporting PIR, including the online Survey.
[Auditor Reporting PIR](#)

International Ethics Standards Board for Accountants (IESBA)

1. In July 2020, the Staff of the Accounting Professional & Ethical Standards Board (APESB) and the International Ethics Standards Board for Accountants (IESBA) released a new publication, [Applying the Code's Conceptual Framework in COVID-19 Circumstances: Scenarios in Taxation and Valuation Services](#), providing guidance to professional accountants in applying the conceptual framework in the [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) (the Code) during certain circumstances brought on by the COVID-19 pandemic. The publication uses four hypothetical scenarios covering services or activities relating to taxation and valuation services. Two scenarios include guidance for professional accountants in public practice, and two scenarios are focused on professional accountants in business.

Accountancy Europe (AE) (former FEE)

1. AE response to the IAASB's consultation on proposed guidance: *extended external reporting (EER) assurance* can be accessed [here](#).

Public Interest Oversight Board of IFAC (PIOB)

1. There have been no significant developments related to audit and assurance to report in the period.

International Integrated Reporting Council (IIRC)

1. There have been no significant developments related to audit and assurance to report in the period.

Global Reporting Initiative (GRI)

1. A new report assessing the regulatory landscape for sustainability reporting has found that environmental, social and governance (ESG) disclosure has never been more pervasive globally – and is now firmly in the mainstream of disclosure on organizational performance. As the market implications of certain ESG topics become more evident, interest in the quality of disclosures is also sharpening.

The fifth edition of [Carrots & Sticks](#) (C&S) provides an analysis of the latest trends in reporting provisions, covering 614 reporting requirements and resources (a substantial increase on the 383 assessed in the previous report in 2016) across over 80 countries, including the world's 60 largest economies. A new addition in 2020 is insights and context gathered through interviews with policymakers, who give their views on good practices in phasing in ESG disclosure requirements.

International Forum of Independent Audit Regulators (IFIAR)

1. There have been no significant developments related to audit and assurance to report in the period.

International Organization of Supreme Audit Institutions (INTOSAI)

1. The INTOSAI Working Group on SDGs and Key Sustainable Development Indicators has published its first [Newsletter](#).

International Organization of Securities Commissions (IOSCO)

1. There have been no significant developments related to audit and assurance to report in the period.

Australia

The Australian Auditing and Assurance Standards Board (AUASB)

1. The AUASB amends Auditor's Responsibilities **Statement 1** and **Statement 2** resulting from the revised APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) which became effective from 1 January 2020.

These **statements** provide a description of the auditor's responsibilities referred by **ASA 700** paragraph 41 (c) in the Auditor's Responsibilities for the Audit of the Financial Report section of the audit report.

Where auditors refer to the Auditor's Responsibilities Statements by including a specific reference to the AUASB website in the body of their Audit Report they are reminded to ensure the correct URL is included. This includes updating any relevant report templates and electronic tools where necessary.

United Kingdom

FRC

1. The Financial Reporting Council (FRC) released its latest audit inspection results on 14 July 2020.

Each year the FRC reports publicly on the findings of its inspection activity at the seven largest firms. Together with an assessment of each firm's quality control systems, the Audit Quality Review (AQR) team reviewed 88 audits across these firms and concluded that only two thirds of the audits were of a good standard or required limited improvement.

In the reports, the FRC sets out a number of significant steps that it is taking or intends to take in the short to medium term to ensure that the audit firms take swift actions to respond robustly to our concerns.

A link to the seven inspection reports can be viewed [here](#).

Institute of Chartered Accountants in England and Wales

1. There have been no significant developments related to audit and assurance to report in the period.

The Charity Commission

1. There have been no significant developments related to audit and assurance to report in the period.

Association of Chartered Certified Accountants (ACCA)

1. There have been no significant developments related to audit and assurance to report in the period.

United States of America

Public Company Accounting Oversight Board (PCAOB)

As part of the Public Company Accounting Oversight Board's (PCAOB) strategic goal of enhancing transparency and accessibility through proactive stakeholder engagement, the Board has committed to engaging more directly and more often with audit committees. In 2019, PCAOB reached out to nearly 400 audit committee chairs of U.S. issuers whose audits we inspected and offered them the opportunity to speak with us. PCAOB reported out on those discussions in [Conversations with Audit Committee Chairs: What We Heard & FAQs](#). PCAOB have continued this outreach to audit committee chairs during our 2020 inspections. Given the unprecedented challenges for auditors, audit committees, and issuers created by the COVID-19 pandemic, PCAOB asked audit committee chairs how they are thinking about the effect of COVID-19 on financial reporting and the audit as they perform their oversight duties. The report can be accessed [here](#).

American Institute of Certified Public Accountants (AICPA)

1. There have been no significant developments related to audit and assurance to report in the period.

Center for Audit Quality (CAQ) - (affiliated with AICPA)

1. There have been no significant developments related to audit and assurance to report in the period.

Canada

Canadian Auditing and Assurance Standards Board (AASB)

1. There have been no significant developments related to audit and assurance to report in the period.

CPA Canada

1. CPA Canada published [an article](#) on the effects of COVID-19 on audit client, their internal controls, and the audit

Project	Overview of the project and its current status
<p data-bbox="204 293 432 416">Quality Control</p> <p data-bbox="204 349 432 416">No Update for the period</p>	<p data-bbox="459 293 1388 600">Objective of the Project: Initial activities in scoping the project will focus on whether there is a need to revisit specific aspects of the quality control standards to enhance clarity and consistency of their application. This may include restructuring ISQC 1, additional requirements or guidance within the standard or additional guidance in support of the standard. Specific aspects within ISQC 1 and ISA 220 being explored include, governance, engagement partner responsibilities, engagement quality control reviews, monitoring, remediation, alternative audit delivery models and specific issues pertaining to small- and medium-sized practices</p> <p data-bbox="459 633 1388 837">Background and current status: The proposed changes to QC were included in the IAASB Audit Quality ITC. The ITC response period is closed now. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, and developed project proposals for quality control that were presented at the September 2016 IAASB meeting.</p> <p data-bbox="459 871 1388 936">The IAASB considered the Quality Control Other Working Group's (QCOWG) proposals in respect of:</p> <ul data-bbox="459 969 1388 1106" style="list-style-type: none"> • Setting the objective of an engagement quality control (EQC) Revising the definition of an EQC review; • Determining the scope of the engagements subject to an EQC review; and • The execution of an EQC review. <p data-bbox="459 1140 1388 1205">At its March 2017 meeting, the IAASB discussed matters to do with the eligibility of the engagement quality control reviewer.</p> <p data-bbox="459 1238 651 1265">QC-Firm Level</p> <p data-bbox="459 1299 1388 1644">In June 2017 the Board discussed the Quality Control Task Force's (QCTF) recommendations on the possible revisions to ISQC 1, a result of incorporating a quality management approach (QMA) into ISQC 1, that included a discussion of a working draft of ISQC 1 (Revised) and how the proposals are expected to change firm behaviors. The Board was supportive of the overall direction proposed by the QCTF and emphasized the importance of outreach with a variety of stakeholders to seek input on the practicality of the proposals. The Board also encouraged the QCTF to develop guidance and examples to accompany the revised standard in order to explain the implementation and application of the standard.</p> <p data-bbox="459 1677 1388 1845">In its September 2017, the Board discussed the Quality Control Task Force's (QCTF) recommendations on the possible revisions to ISQC1 in relation to documentation of the system of quality management. The Board was supportive of the QCTF's proposals and suggested various refinements. Some of the key proposals were as follow:</p> <ul data-bbox="459 1879 1388 1980" style="list-style-type: none"> • the proposal to retain the requirement for an EQC review for all audits of financial statements of listed entities, i.e., not only for general purpose financial statements

- the proposals in relation to other engagements for which the firm determines that an EQC review is required (see here for details)
- the objective of ISQC 2, including whether it is appropriate to locate the responsibilities of the EQC reviewer in ISQC 2, instead of ISA 220
- the IAASB supports the proposal to remove the reference to “team” from the definition of an EQC reviewer, and instead explain the use of a team in the application material supporting the appointment of the EQC reviewer
- the proposed requirements and application material in relation to the eligibility of the EQC reviewer.

The Board also discussed the QCTF’s recommendations in relation to EQC reviews that would be incorporated in ISQC 1 and the proposed new standard, ISQC2. The Board confirmed that the purpose of the EQC review is to evaluate the significant judgments made by the engagement team. In addition to various recommendations to further enhance and clarify the various requirements and application material, the Board encouraged the QCTF to improve the robustness of the requirement relating to the scope of the engagements subject to EQC review.

In December 2017, the Board discussed a first read of the proposed exposure draft of ISQC 1 (Revised) 5 and was broadly supportive of the direction of the standard. The Board focused on the scalability of the standard, clarifying the interrelationship of the components, and the appropriate placement of the governance and leadership component. As well as requesting the Task Force to clarify the meaning of deficiencies and major deficiencies, the Board asked that a framework be developed for assessing deficiencies in the system of quality management and requested clarification of how such deficiencies may impact the achievement of the overall objective of the standard. The Board also asked the Task Force to reconsider the threshold for the identification of quality risks and encouraged the Task Force to explore the development of appropriate guidance to accompany the proposed exposure draft that addresses the application of the standard to a spectrum of firms.

The Board discussed the exposure draft (ED) of proposed ISQC 1 (Revised)1 and was supportive of the direction that the Quality Control Task Force was taking the standard, noting the improvement in the readability and understandability overall. The Board encouraged the Quality Control Task Force to consider whether there are further opportunities to address scalability, including further refinement and simplification of the standard, where possible. The Board also discussed changing the title of the standard

In finalizing the ED in December 2018, the Board discussed the definition of deficiencies and bringing more emphasis to positive findings from the firm’s monitoring activities and how they may be used in the system of quality management. The Board also discussed the requirement for the firm to establish additional quality objectives beyond those required by the standard and further clarifying the identification and assessment of quality risks. In addition, the Board suggested further simplification of the requirement addressing communication with external parties, although in general agreed to retain an explicit reference to transparency reports in the requirement. The Board also discussed network requirements or network services, and

adjusted the requirement to clearly reflect the expectations of the firm regarding the effect of network requirements or network services on the firm's system of quality management.

The Board supported the Quality Control Task Force's recommendations regarding matters to be addressed in the Explanatory Memorandum, including the proposed questions.

In September 2019, the Board discussed the comment letters received on certain areas of the Exposure Draft (ED) of ISQM 1 (ED-ISQM 1)³ relating to the quality management approach, implementation challenges, the components and structure of the standard and the firm's risk assessment process. The Board concurred that four significant themes had emerged from the comments: scalability; prescriptiveness; addressing firms who do not perform audit or assurance engagements; and challenges with implementation. The Board, in general, supported proposals to address the structure of the standard and clarify the nature of the components and how they interrelate. The Board also supported addressing the granularity of the quality objectives, introducing quality risk considerations, and refining the required responses. The Board agreed with the ISQM 1 Task Force's proposals to simplify the firm's risk assessment process, including addressing concerns about the threshold for the identification of quality risks. The Board did not support the proposal to develop a separate standard for quality management for related services engagements and encouraged exploration of other ways to address scalability concerns. The ISQM 1 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting.

In December 2019, the Board continued to discuss the key issues highlighted by respondents to the Exposure Draft (ED) of ISQM 13 (ED-ISQM 1) including the scalability, complexity and prescriptiveness of the standard. appropriate tailoring of the system of quality management for their circumstances and the making sure the standard that can be applied in all circumstances.

The Board supported the changes to the structure of the standard, adjusting the quality objectives and responses in the components to be more streamlined and the revisions to the drafting and presentation of the standard to simplify and improve the readability of the standard. The Board also agreed with proposed revisions to the firm's risk assessment process, including introducing factors to consider in identifying and assessing quality risks.

The Board supported the ISQM 1 Task Force's proposals to embed a risk-based approach in the monitoring and remediation component, improve the selection of engagements for inspection such that it is more risk-based, and further clarify the framework for evaluating findings and identifying deficiencies.

In its March 2020 meeting, the IAASB discussed a full draft of proposed ISQM 1. The IAASB particularly focused on the identification and assessment of quality risks, external communications, findings and deficiencies, the inspection of completed engagements, service providers, and the annual

evaluation of the system of quality management. The IAASB also discussed the meaning of the effective date of proposed ISQM 1.

The IAASB broadly supported the proposals and encouraged the ISQM 1 Task Force to further simplify the identification and assessment of quality risks, clarify the definition of deficiencies, and enhance the standard to encourage communication externally. With respect to the evaluation of the system of quality management, the IAASB also suggested adopting a less binary conclusion about the system of quality management to encourage a positive approach to evaluating the system.

The ISQM 1 Task Force will present certain sections of proposed ISQM 1 to the IAASB via videoconference on April 8, 2020.

The Board discussed revisions to a number of areas of proposed ISQM 1,1 including how the standard addresses public interest, the firm's risk assessment process, the definitions of deficiencies and findings and key aspects of monitoring and remediation, information and communication, service providers, relevant ethical requirements and the evaluation of the system of quality management. The Board in general supported the proposals. The Board encouraged the ISQM 1 Task Force to continue developing the definitions of deficiencies and quality risks, and also requested the Task Force to clarify certain requirements related to the firm's risk assessment process. In supporting the proposals to address external communications, the Board suggested that the requirement focus on the firm's determination of when it is appropriate to communicate with external parties.

In June 2020, the Board discussed revisions to certain areas of proposed ISQM 1,1 including the firm's risk assessment process, resources, relevant ethical requirements, monitoring and remediation, and the evaluation of the system of quality management. The Board also discussed external communications, in particular the firm's communication with those charged with governance when performing an audit of financial statements of a listed entity. The Board supported the proposals, and encouraged the ISQM 1 Task Force to further simplify the approach to human resources, in particular the application material explaining the firm and engagement team responsibilities in addressing the competence and capabilities of individuals assigned to the engagement team. The Board also provided varying comments on external communications, although was generally supportive of the direction proposed by the ISQM 1 Task Force. The ISQM 1 Task Force will present a full draft of proposed ISQM 1 for IAASB approval via videoconference in September 2020.

Quality Control – Engagement Level

In December 2017, The IAASB supported the direction of the proposed changes to ISA 220.4 In particular, the Board supported the proposed changes that emphasize that the engagement partner is responsible and accountable for audit quality. The Board encouraged the ISA 220 Task Force to consider, as it progresses revisions to ISA 220, how the proposed changes will strengthen the performance of quality audits.

The Board discussed a draft ED of proposed ISA 220 (Revised)² and was supportive of the proposed changes. The discussions focused on whether changes were needed to the objective of the standard and the wording of the requirement regarding the engagement partner being “sufficiently and appropriately involved.” The Task Force plans on presenting the ED of proposed ISA 220 (Revised) for approval by the Board at the December 2018 meeting.

In December 2018 the Board supported the requirement for the firm to establish policies or procedures addressing limitations on the engagement partner moving into the role of engagement quality reviewer, including the reference to a cooling-off period in the application material. The Board agreed that stakeholder views were needed relating to the objectivity of the engagement quality reviewer and a cooling-off period and supported the ISQM 2 Task Force’s recommendation for including specific questions in the Explanatory Memorandum on this matter to be developed in coordination with the IESBA. The Board also clarified the requirement for notifications by the engagement quality reviewer to the engagement partner and, when applicable, individual(s) within the firm, as well as the documentation requirements.

The Board discussed the requirements that address firm policies or procedures, the role of the engagement partner vis-à-vis other members of the engagement team and the difference between the usages of the phrases “the auditor shall determine” and “the auditor shall be satisfied.” The board also discussed how best to clarify the requirement addressing communications from the firm about the firm’s monitoring and remediation process.

In September 2019, the Board discussed the comment letters received to ED-ISA 2205 and the ISA 220 Task Force’s proposals for addressing the key issues respondents raised. The Board supported the fundamental principle that the engagement partner has overall responsibility for managing and achieving quality and being sufficiently and appropriately involved in the engagement. The Board also supported clarifying the requirement addressing circumstances when the engagement partner assigns procedures or tasks to other engagement team members, the principles underpinning the proposed engagement team definition and proposals to address scalability of the requirements to audits of larger or more complex entities. The ISA 220 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting.

The Board generally supported the ISA 2205 Task Force’s proposals to clarify the engagement team definition, to make clear that the engagement team can ordinarily depend on the firm’s system of quality management, and to better deal with large, complex audit engagements. The Board also discussed professional skepticism, the stand-back provision and the documentation requirements. The ISA 220 Task Force will consider the comments received in preparing a revised full draft of proposed ISA 2202 for discussion at the March 2020 IAASB meeting.

In March 2020 The Board discussed clarifications to distinguish requirements that are the sole responsibility of the engagement partner and those the

	<p>engagement partner is permitted to assign to another engagement team member and the meaning of “resources made available by the firm” in the case of engagement team members who are external to the firm, among other matters.</p> <p>In June 2020, the Board discussed amendments to proposed ISA 220 (Revised)⁴ to clarify how to treat component auditors that are not directly engaged by the firm. The ISA 220 Task Force will present a full draft of proposed ISA 220 (Revised) for IAASB approval via videoconference in September 2020</p>
<p>Group Audits– ISA 600</p> <p>No Update for the period</p>	<p>Objective of the project: Determining the nature of the IAASB’s response to issues that have been identified, relating to Group Audits, from the ISA Implementation Monitoring project and outreach activities, inspection reports from audit regulators, discussion with NSS and responses to the IAASB’s Work Plan consultation (i.e., whether standard-setting activities are appropriate to address the issues, and if so, whether specific enhancements within ISA 600 or a more holistic approach to the standard would be more appropriate).</p> <p>Background and current status: The IAASB commenced work on one aspect of this project relating to the responsibilities of the engagement partner in circumstances where the engagement partner is not located where the majority of the audit work is performed in December 2014. A Staff Audit Practice Alert on this aspect was published in August 2015. Information gathering on the broader aspects of group audits commenced in March 2015.</p> <p>The issues identified and discussed at the IAASB meetings form part of a combined Invitation to Comment on Enhancing Audit Quality in the public interest which was issued in December 2015 and is open for comments till May 16, 2016. The ITC is now closed. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, presented the results to IAASB at the September 2016 IAASB meeting.</p> <p>In its June 2017 meeting, the IAASB received an update on the activities of the GATF. The IAASB supported the proposal of the GATF to engage more directly with the QCTF, ISA 220 TF and ISA 315 (Revised)³ TF, to help ensure that the requirements in those standards provide appropriate connection points between those projects and ISA 600.⁴ The IAASB also supported the proposal of the GATF to publish a short project update and asked the GATF to consider topics that are related to standards not under revision, for example, materiality and audit evidence.</p> <p>In December 2017, the Board received a presentation about the interconnections between ISA 600 and other ongoing projects, and how the Task Force is monitoring the activities of the other task forces, providing input and considering implications of changes in the other standards on ISA 600.</p>

In March 2019, the Board was updated on the work performed by the Group Audit Task Force since the start of the project to revise ISA 600¹ and was asked for its views on issues related to scoping a group audit, the definitions, and the linkages with other ISAs. The Board continued to support developing a risk-based approach for scoping a group audit and generally supported the Group Audit Task Force's approach on the definitions and the issues that were presented in relation to the responsibilities of the group engagement partner, acceptance and continuance, understanding the group and its components, understanding the component auditor, identifying and assessing the risks of material misstatement and responding to assessed risks, the consolidation process, communication between the group auditor and component auditors, and evaluating the audit evidence obtained. These and other issues need to be further developed in the context of the risk-based approach and changes made to other of the IAASB's International Standards. The Group Audit Task Force will continue to work on the issues related to scoping a group audit, the definitions and other issues identified in the [Invitation to Comment](#), and will present it for further discussion at the June 2019 IAASB meeting.

In June 2019, the Board was updated on the ISA 6003 Task Force's progress since the March 2019 meeting and discussed the public interest issues that the ISA 600 Task Force identified, the ISA 600 Task Force's proposals with respect to the risk-based approach to scoping a group audit, and the special considerations related to auditing a group. The Board also discussed indicative drafting related to the risk-based approach to scoping a group audit and the special considerations related to proposed ISA 220 (Revised).⁴ Generally, the Board was supportive of the approach taken but had suggestions on the way forward and the indicative drafting. The ISA 600 Task Force will take these comments into account and will present further drafting at the September 2019 meeting. The ISA 600 Task Force will also continue its outreach to key stakeholders and coordinate with IESBA and other IAASB Task Forces as needed.

In September 2019, the Board was updated on the work of the ISA 600 Task Force since the June 2019 meeting, including the outreach performed and the feedback received from the IAASB's Consultative Advisory Group. The Board discussed, among other matters, the updated public interest issues, a draft of a significant part of the standard and the ISA 600 Task Force's proposals with respect to the scope and structure of the standard, materiality considerations in a group audit and a proposed stand-back requirement. The ISA 600 Task Force will take these comments into account in preparing revised drafting and issues for discussion at the December 2019 IAASB meeting.

In December 2019, the Board was updated on the work of the ISA 600 Task Force since the September 2019 meeting, including the outreach performed, and discussed a full draft of the proposed revised standard (except the appendices). The draft of proposed ISA 600 (Revised)¹ included updated requirements and application material on sections that were presented to the

¹ International Standard on Auditing (ISA) 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

	<p>Board in September 2019 and new requirements and application material on, among other matters, materiality, communications with component auditors and documentation.</p> <p>The ISA 600 Task Force will take the Board's comments on the proposed revised standard into account and will present an updated version for approval for public exposure at its March 2020 meeting. The Task Force will discuss the conforming amendments and the appendices to proposed ISA 600 (Revised) in the January 23, 2020 Board teleconference.</p> <p>In March 2020, after making amendments in response to the IAASB's comments received during the meeting, the IAASB approved the Exposure Draft (ED) of proposed ISA 600 (Revised)¹ and related conforming and consequential amendments for public exposure with 18 affirmative votes out of the 18 IAASB members present. The ED will be issued in mid-April with a comment period of 120 days.</p> <p>In finalizing the ED, the IAASB continued to discuss whether it is sufficiently clear how the standard described the involvement of component auditors. On balance, the IAASB was satisfied that the draft sets out acceptable proposals on all significant areas for this project and that it is appropriate to proceed to seek stakeholder views whether the proposals could be effectively implemented.</p> <p>The IAASB also discussed possible matters to be addressed in the explanatory memorandum that will accompany the ED.</p>
<p>Professional Scepticism</p> <p>No Update for the period</p>	<p>Objective of the project: To make recommendations on how to more effectively respond to issues related to professional scepticism.</p> <p>Background and current status: The IAASB commenced its initial information gathering on the topic of professional scepticism in June 2015. The issues identified and discussed at the IAASB meetings are part of the Invitation to Comment on Enhancing Audit Quality in the Public Interest which was issued in December 2015 and is open for comments till May 16, 2016.</p> <p>The working group is comprised of representatives from the IAASB, the International Ethics Standards Board for Accountants (IESBA), and the International Accounting Education Standards Board (IAESB) to explore the topic of professional scepticism, enabling the three independent standard-setting Boards to consider what actions may be appropriate within their collective Standards and other potential outputs to enhance professional scepticism.</p> <p>Together with the Quality Control and ISA 600-Group Audits project, this project is part of the Audit Quality Enhancements Coordination Group (AQECG). The AQECG intends to coordinate the various inputs to the invitation to comment developed at the individual working group level, and take a holistic approach as to how the matters are presented in one invitation to comment. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, presented the results to IAASB at the September 2016 IAASB meeting.</p>

	<p>Subsequent to the December 2016 IAASB meeting, the joint PSWG held a teleconference to discuss matters related to potential changes to the concept/definition of professional scepticism in the ISAs. The March meeting papers are available here.</p> <p>In June 2017 meeting, the IAASB received an update on the activities of the Professional Skepticism Working Group (PSWG) and the Professional Skepticism IAASB Subgroup since the last Board meeting in March 2017. The Board supported the release of a communication to update stakeholders about the actions and current status of the PSWG’s work. The Board also discussed the concept of “levels” of professional skepticism and supported the recommendations of the Professional Skepticism IAASB Subgroup not to introduce the concept into the ISAs.</p> <p>The IAASB discussed the Professional Skepticism Subgroup’s analysis and related conclusions regarding different “mindset” concepts of professional skepticism and the use of the words in the ISAs in its December 2017. The Board supported the conclusions of the Subgroup, including that the current concept of the attitude of professional skepticism involving a “questioning mind” continues to be appropriate and should be retained within the ISAs. The IAASB Professional Skepticism Subgroup will liaise as needed with the Professional Skepticism Joint Working Group.</p> <p>In September 2018 meeting, The Board received an update on the activities of the IAASB’s Professional Skepticism Subgroup (Subgroup) since March 2018. The Chair of the Subgroup also presented the Board with a draft publication that seeks to highlight the IAASB’s efforts to appropriately reflect professional scepticism into the IAASB standards as well as other relevant news and information on professional skepticism, including collaboration with the International Ethics Standards Board for Accountants (IESBA) and International Accounting Education Standards Board (IAESB). The Board supported the issuance of the publication and future publications of this nature.</p>
<p>Data Analytics</p> <p>No Update for the period</p>	<p>Objective of the project: The objective of the Data Analytics Working Group (WG) is to:</p> <p>A) Explore emerging developments in audit data analytics; and B) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe.</p> <p>Background and current status: Information gathering on data analytics began in April 2015 and the Data Analytics Working Group will continue with its planned outreach activities in future. The DWAG published its first publication “The IAASB’s Work to Explore the Growing Use of Technology in the Audit” in June 2016.</p> <p>At the March meeting, the IAASB received a video presentation of a panel discussion among members of the DAWG that was presented at the International Forum of Independent Audit Regulators Inspections Workshop.</p>

	<p>The Chair of the DAWG provides an update on the project in February 2017 on the IFAC website.</p> <p>In its June 2017 meeting, the IAASB received a presentation of high-level observations from respondents to the IAASB's Request for Input: Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics. It was noted that respondents supported the IAASB in undertaking this work and encouraged continued active participation of the Data Analytics Working Group in other current standard-setting projects of the IAASB underway.</p>
<p>Emerging External Reporting Update for the period No the</p>	<p>Objective of the project: The objective of the Integrated Reporting Working Group (IRWG) is to:</p> <ul style="list-style-type: none"> A) Explore emerging developments in integrated reporting and other emerging developments in external reporting; B) Gather further information on the demand for assurance, the scope of the assurance engagement and the key assurance issues; and C) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe. <p>Background and current status: At its September 2014 meeting the Innovation WG proposed, and the IAASB agreed to establish a WG to specifically monitor the developing interest in integrated reporting and the demand for assurance on integrated reports. This includes initial thinking on the nature of such engagements, including the scope of the assurance engagement, the suitability of the criteria, and other matters related to assurance on integrated reports. The Board considered the draft working paper prepared by the IRWG Supporting Credibility and Trust in Emerging Forms of External Reporting in its June 2016.</p> <p>The Discussion Paper was issued in August 2016.</p> <p>In its June 2017 meeting, the IAASB received a presentation about the high-level observations from the comment letters received to the Discussion Paper, Supporting Credibility and Trust in Emerging Forms of External Reporting. It was noted that respondents generally supported the development of guidance on how to apply existing international assurance standards rather than developing new standards, and that the IAASB should continue to provide thought leadership on assurance issues and coordinate its work with other relevant organizations.</p> <p>The Board received an update on the project in December 2017. It was noted that the grant agreement with the World Business Council for Sustainable Development (WBCSD) was finalized for the funding of the project and that the Project Proposal and Feedback Statement has been finalized to be published on the IAASB's website. The board also received an update on the plan for developing the framework for the non-authoritative guidance for EER during the next year, including the required research to be gathered and the establishment of a Project Advisory Panel (PAP).</p> <p>In its September 2018 meeting, the EER Task Force presented the remaining Phase 1 'issues' that were not presented in June alongside a first draft of the Phase 1 guidance. The Board noted the need for the guidance to demonstrate</p>

its full alignment with the requirements of ISAE 3000 (Revised), 5 and for the EER Task Force to provide further explanations about any guidance that goes beyond the requirements and application material in ISAE 3000 (Revised). The EER Task Force expects to receive further input from stakeholders during its forthcoming series of discussion events and will present a revised draft of the guidance to the IAASB in December 2018.

In December 2018 The EER Task Force presented an updated version of the Phase 1 draft guidance, which reflects changes to address feedback received from the IAASB at the September 2018 IAASB meeting, and from other stakeholders, including in relation to a 'materiality process' and assertions as they relate to the characteristics of suitable criteria. The Board noted that the draft guidance had significantly improved since discussions at the September 2018 meeting, but that further work on the drafting is enquired. The Board will discuss a further version on a teleconference in January 2019 before the draft guidance is published for public comment.

In March 2019, the Board approved for public comment Phase 1 of the draft guidance in January 2019. At its March 2019 meeting, the Board discussed several challenges related to Phase 2 of the guidance. The challenges include: determining the scope of an EER assurance engagement; communicating effectively in the assurance report; exercising professional skepticism and professional judgment; obtaining the competence necessary to perform the engagement; and obtaining evidence in respect of narrative and future-oriented information. The Board's deliberations of the challenges concerned were facilitated through breakout sessions, after which each breakout group reported back to the Board in a plenary session. The EER Task Force will consider the inputs that were received in progressing the development of Phase 2 of the guidance for further discussion at the June 2019 IAASB meeting.

In June 2019, the Board was updated on the work of the EER Task Force on the challenges allocated to Phase 2 of the project. These challenges include: determining the scope of an EER assurance engagement; obtaining evidence in respect of narrative and future-oriented information; exercising professional skepticism and professional judgment; obtaining the competence necessary to perform the engagement; and communicating effectively in the assurance report. The Board discussed views on the EER Task Force's initial proposals to address each of these challenges in the Phase 2 guidance. The EER Task Force will consider the inputs received from the Board, together with responses to the Phase 1 EER Consultation Paper in so far as they impact the Phase 2 guidance, in developing the draft Phase 2 guidance, which will be presented for discussion at the September 2019 IAASB meeting.

In September 2019, the Board received an overview of the comment letters received on the EER Assurance Consultation Paper. The Board discussed respondents' comments on the Consultation Paper, that included the draft Phase 1 guidance, and the EER Task Force's proposals for addressing the comments. The Board also discussed the initial drafting of the Phase 2 guidance developed to date by the EER Task Force. A revised draft of the

	<p>combined Phase 1 and Phase 2 guidance will be presented to the Board, for approval of an exposure draft at the December 2019 IAASB meeting.</p> <p>In December 2019, the Board approved the combined restructured and redrafted non-authoritative EER Guidance, Special Considerations in Performing Assurance Engagements on Extended External Reporting, for public consultation. The consultation period will be 120 days from the date of publication. In finalizing the draft Guidance for public consultation, the Board agreed to emphasize that the guidance is non-authoritative and is not required to be read in its entirety, but is a useful reference source in applying particular requirements of the Standard. The Board also clarified the possible approaches to the use of framework criteria and entity-developed criteria and included additional guidance on fraud and on misstatements that might affect the practitioner's assessment of the control environment.</p>
<p>Agreed-Upon Procedures</p> <p>No Update for the period</p>	<p>The objective of the project is to:</p> <p>A) Revise International Standard on Related Services (ISRS) 4400, Engagements to Perform Agreed-Upon Procedures Regarding Financial Information in the Clarity format; and</p> <p>B) Consider whether standard-setting or other activities may be appropriate for engagements that use a combination of procedures derived from review, compilation and agreed-upon procedures engagements (also known as "hybrid engagements"), in light of the existing standards that may be applicable to these services in the IAASB's current suite of standards.</p> <p>Background and current status: During consultations on the IAASB's 2015-2019 Strategy and the related 2015-2016 Work Plan, many stakeholders expressed the need to revise ISRS 4400 to meet the growing demand for agreed-upon procedure engagements. In response to the stakeholders' comments, the IAASB established a working group to explore issues involving agreed-upon procedure engagements. The issues identified and discussed at the IAASB meetings will be used to revise ISRS 4400 and possibly develop new standard(s) or guidance that would address engagements where there is a combination of agreed-upon procedures and assurance.</p> <p>The Agreed-Upon Procedures (AUP) Working Group presented a first draft of its Discussion Paper, <i>Exploring the Growing Demand for Agreed-Upon Procedures Engagements and Other Services and the Implications for the IAASB's Standards</i>, to the Board in June 2016. The IAASB provided the AUP Working Group with input to enhance the Discussion Paper and suggested that the paper pose a question to explore whether the IAASB should develop guidance on multi-scope engagements. The AUP Working Group will present a revised draft of the Discussion Paper at the September 2016 IAASB meeting.</p> <p>In its September 2017 meeting, the Board discussed the feedback received on the Discussion Paper and approved a standard-setting project proposal to revise ISRS 4400, subject to clarifications around the use of judgment, independence, restriction of the report of factual findings and required documentation.</p> <p>In its September 2018 meeting, The Board approved the ED of ISRS 4400 (Revised)³ for public exposure. In finalizing the ED, the Board agreed that</p>

	<p>independence is not required for an AUP engagement and that the AUP report would include statements addressing circumstances when the practitioner is (or is not) required to be independent, and whether the practitioner is (or is not) independent. The ED will be issued in early November with a 120 day comment period.</p> <p>In June 2019 the Board received an overview of the responses to proposed ISRS 4400 (Revised)² (ED-4400). The Board discussed, among other matters, respondents' comments on the application of professional judgment when performing procedures, the independence disclosure requirements, and the effective date.</p> <p>The Board also acknowledged areas of broad support, including not including a precondition for the practitioner to be independent, using the term "findings" and requiring an explanation of this term in the engagement letter and the AUP report, not requiring or prohibiting a reference to the practitioner's expert in the AUP report, and not requiring a restriction on use or distribution of the AUP report. The AUP Task Force will deliberate the Board's input and will present the first read of the post-exposure ISRS 4400 (Revised) to the Board in the second half of 2019.</p> <p>The Board approved ISRS 4400 (Revised)² with 17 Board members voting for approval and one vote against. The revised ISRS will be effective for agreed-upon procedures engagements for which the terms of engagement are agreed on or after January 1, 2022. Once the PIOB's confirmation that due process was followed is received, the Board will formally release the standard. In finalizing ISRS 4400 (Revised), the Board carefully deliberated the effective date and continued to focus on issues relating to compliance with independence requirements.</p>
<p>No Update for the period</p>	<p>In March 2019 the Board discussed a proposed Discussion Paper (DP), <i>Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Implementing the ISAs</i>. The discussion highlighted the shift in focus on complexity of the entity rather than its size in driving the ongoing discussions and activities to address issues and challenges in audits of less complex entities (LCEs). The Board was supportive of the DP's overall direction, noting the importance of the project and the need for action by the IAASB and others.</p> <p>The Board liked the simple, clear way the DP had been presented and noted it was appropriate for its key target audience (i.e., auditors of LCEs). The Board made suggestions for improvements, particularly with respect to the issues and challenges, the possible actions presented within the DP and the questions to be posed to respondents in order to obtain relevant and useful feedback. Proposed changes to the DP will be presented in a Board call on April 10th, with the final DP targeted to be published for public consultation before the end of April 2019.</p> <p>The Board discussed the feedback received to date related to audits of less complex entities, including from the Discussion Paper (DP), <i>Audits of Less Complex Entities (LCEs): Exploring Possible Options to Address the Challenges in Applying the ISAs</i>, and other related outreach. The key messages received from the feedback highlighted the strong support for the</p>

	<p>IAASB's work in this area, as well as the need for a timely and global solution. The Board asked the LCE Working Group to continue to analyze the feedback from stakeholders to help determine the most appropriate way forward, and it was agreed that further information gathering activities would continue until June 2020, at which time it is anticipated that a decision about the way forward will be made. As part of the proposal for work in this area, the IAASB had agreed that it was important to keep stakeholders informed of its progress in relation to its work on audits of LCEs. Accordingly, the Board agreed to publish a Feedback Statement in December 2019 detailing what the IAASB had heard from its consultation and related outreach.</p>
<p>Audit Evidence</p> <p>No Update for the period</p>	<p>The Board discussed the analysis undertaken by the Audit Evidence Working Group of the issues across the ISAs related to audit evidence and the use of technology more broadly, and the possible actions to address the issues. The Board concurred that guidance should be developed on the effect of technology when applying certain aspects of the ISAs, and that this should be actioned expeditiously.</p> <p>The Board also indicated that more extensive information gathering and research need to be undertaken to understand the issues related to audit evidence, so that the Board is fully informed of the issues in determining the need for revisions to ISA 5005 and possibly other related standards.</p> <p>In September 2019, the Board was provided with an overview of the development of the Audit Evidence Workstream Plan. The Audit Evidence Working Group will accordingly undertake further information gathering and research, and develop recommendations for possible further actions to be presented to the Board in the first half of 2020.</p> <p>In June 2020, the Board discussed the outcome of the Audit Evidence Working Group's information gathering and targeted outreach activities. Based on the feedback, the Board agreed with the Audit Evidence Working Group's conclusion that the listing of audit evidence related issues, as presented, is appropriate. The Board supported the Audit Evidence Working Group's recommendation to develop a project proposal to revise ISA 500,5 including conforming and consequential amendments to other standards, for approval at the December 2020 IAASB meeting, and to continue in the interim to evolve its approach, as presented, to progress the revision of ISA 500 (and conforming and consequential amendments to other standards). The Board also recommended that the Working Group publish a project update to inform stakeholders about the activities undertaken to date.</p>
<p>LCE</p> <p>No Update for the period</p>	<p>In June 2020, the Board discussed the LCE Working Group's recommendations for developing a separate standard for Audits of Less Complex Entities (LCEs) on the basis of overarching principles outlining how the separate standard could be developed.</p> <p>Notwithstanding the support for some of the overarching principles outlined, the Board requested the LCE Working Group to further consider how the separate standard could be developed so that it is standalone, while also clarifying the linkage back to the ISAs as appropriate. In doing so, the Board also encouraged</p>

	<p>further consideration of materials to help apply the separate standard, either within the standard (as application material) or outside as support materials. The Board highlighted the importance of the description of an LCE to help in developing the content of the separate standard. The Board encouraged a more prescriptive definition for the application of the standard, although the Board recognized there would always be a level of judgment in making this determination. On this basis, the Board supported that the LCE Working Group commence development of the separate standard as well as prepare a project proposal for approval at the December 2020 IAASB meeting.</p>
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Agenda Item 11.2



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

DATE: 20 August 2020
TO: Members of the New Zealand Auditing and Assurance Standards Board
FROM: Peyman Momenan
SUBJECT: Domestic Update

Introduction

1. This Update summarises the significant news from Financial Market Authority, New Zealand Institute of Chartered Accountants and other organisations for the Board's information, for the period July and August 2020.

Financial Markets Authority (FMA)

1. The Financial Markets Authority (FMA) has today released an [information sheet](#) outlining its priorities over the next three to six months as New Zealand continues to respond to COVID-19.

Rob Everett, FMA CEO, said COVID-19 has significantly impacted the global economy and the FMA is focused on ensuring the financial sector can respond to future challenges, and support customers and investors.

"Outlining our short-term priorities will help the industry, customers and investors understand where we are focusing our efforts, primarily at monitoring changing regulatory risks and ensuring that we can respond appropriately," said Mr Everett.

Key regulatory risks the FMA will focus on include:

1. Investor and customer behaviour and decision-making
2. Fair, efficient and transparent capital markets
3. Financial sector resilience
4. Reintroduction of regulatory activities
5. Treatment of customers and investors
6. Scams and fraud

The FMA usually publishes an Annual Corporate Plan at this time of the year, outlining the work the regulator intends to undertake. The FMA will release a plan later this year and in the meantime is publishing this short-term priorities document.

Mr Everett has also written a related article for the FMA website, [Keeping our eyes on the road ahead](#).

The New Zealand Institute of Chartered Accountants

1. Responding to COVID-19 audit and reporting: a guide for preparers, directors and auditors. Please see webpage link [Financial reporting and audit issues stemming from COVID-19](#).
2. To help members navigate this non-financial risk landscape, Chartered Accountants ANZ has produced [a guide to non-financial risks in 2020 \(the guide\)](#). The guide provides members with a starting point to understanding and addressing non-financial risks. In particular, the guide covers the five broad areas of governance, strategy and risk management, disclosure and reporting and assurance, drawing on domestic and international information from organisations such as The World Economic Forum (WEF), Australian Securities and Investment Commission (ASIC), and NZ Financial Market Authority (FMA).

CPA Australia

1. The CPA Australia published this article: [Audit in Australia: A way forward](#)

The Institute of Directors (IoD)

1. No update for the period.

Using More Effective Instructional Verbs to Elevate Auditors' Professional Skepticism

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This paper is based on the first author's MPhil thesis at UNSW Sydney. We appreciate the helpful feedback of Gary Pflugrath, Paul Coram, Michael Davern, and Karla Zehms. We thank participants at the UNSW Behavioral Accounting Research Seminar, the Accounting Workshop on Experiments (AWE) and AFAANZ for their helpful comments and suggestions. We also thank the management of audit firms for their assistance with participant recruitment and auditors who participated in this study. We gratefully acknowledge financial assistance from the Australian Government Research Training Program Scholarship (RTP), UNSW Business School Bill Stewart Memorial Scholarship, as well as the financial and the technical support provided by the UNSW BizLab.

Written instructions, such as those contained in auditing standards and audit programs, and verbal instructions from supervisors guide auditors' work and stimulate the type of mindset (e.g., deliberative, implemental, skeptical mindset) individuals adopt to prepare for and complete a task efficiently (Gollwitzer 1990; Fujita et al. 2007). Verbs used in these instructions (e.g., investigate) elaborate on what is required. Both academics (e.g., see Nolder and Kadous 2018) and regulators (e.g., IAASB 2017) suggest that the type of instructional verbs currently used in auditing standards represent an important factor potentially contributing to the ongoing professional skepticism 'shortfalls'. This is because different verbs, which are often viewed and used interchangeably as synonyms, can cognitively tune auditors' thinking towards a more / less appropriate mindset (Nolder and Kadous 2018, Bloom et al. 1956; Anderson et al. 2001; Krathwohl 2002).

In this study, we investigate whether instructing auditors using verbs argued to encourage *higher order thinking* 'higher order thinking verbs', as opposed to verbs argued to promote *lower order thinking* 'lower order thinking verbs', leads to increased levels of skepticism and motivates auditors to form more skeptical intentions. Whereas *lower order thinking* involves finding and remembering concepts (remembering), explaining these concepts (understanding), and applying them in new contexts (applying), *higher order thinking* involves breaking complex concepts into parts, understanding their relationships (analysing), critically evaluating these concepts (evaluating) and synthesizing them in creating something new (creating) (Bloom et al. 1956; Anderson et al. 2001). In auditing context, auditors engage in *lower order thinking* in information recall (Carpenter 2007; Griffith et al. 2015; Kim et al. 2017), in gaining understanding about their client and in applying knowledge in new contexts (e.g., how to perform audit procedures) (Nolder and Kadous 2018).¹ Auditors engage in *higher order thinking*, cognitive processes that are vital to high quality judgments, when analysing, evaluating and synthesizing audit information.

Extant auditing standards predominately employ lower order thinking instructional verbs which may not be effective in encouraging the depth of processing that supports the application of professional skepticism. Audit researchers (Nolder and Kadous 2018) argue that this may result in unintended negative consequences for judgement quality, particularly on the audit steps completed by less experienced auditors who rely more on audit instructions to guide their work. The IAASB has also deliberated in its discussions regarding professional skepticism

¹ Lower order thinking provides an important foundation for higher order thinking (Bloom et al. 1956; Anderson et al. 2001).

on whether the appropriate instructional verbs are used in auditing standards to guide auditors work (e.g., IAASB 2017).

We argue that higher order thinking is more consistent with the exercise of professional skepticism as it involves analysis, critical evaluation and synthesis of available information. We expect that using higher order thinking verbs in audit instructions will motivate auditors to exercise higher levels of professional skepticism. Specifically, we predict that auditors instructed with higher order thinking verbs will feel less comfortable with managements' assertions, be less likely to believe that audit evidence collected by an audit assistant is sufficient to support the managements' assertions and form more skeptical intentions.

We test our predictions in an experiment with 48 Big-4 practicing auditors serving as participants.² We examine whether lower order thinking instructional verbs currently used in auditing standards ('review' and 'identify') versus higher order thinking instructional verbs as identified by Anderson et al. (2001) ('consider' and 'evaluate') influence auditor skepticism and impact their skeptical intentions.³ We further test whether this effect is more pronounced for less experienced auditors who gravitate more heavily on instructions in guiding their work.

We present auditors with background information on a hypothetical client and ask them to rate the risk of material misstatement due to fraud and to write reasons for their judgment. Auditors then indicate the extent to which they believe that the evidence they have is sufficient to support managements' assertions (beliefs) and how comfortable they are with managements' explanation of the unexpected increase in gross margin ratio (feelings). In the last step, auditors make evidence collection decision (i.e., select additional audit procedures from a list) (Table 2) to address the risk of material misstatement (skeptical intentions).

Consistent with our expectations, we show that auditors instructed with higher order thinking verbs indicate intentions that are more consistent with higher levels of professional skepticism than auditors instructed with lower order thinking verbs (Table 3). Specifically, we find that auditors instructed with higher order thinking verbs intend to test the veracity of managements' assertions more broadly by selecting evidence items that address more of the 4 procedural targets (see Table 2). In addition, we find that using instructional verbs that

² All auditors had at least two years of audit work experience. There were 20 audit assistants (mean experience 27.55 months), 22 audit seniors (mean experience 47.05 months), and 6 audit managers (mean experience 93.00 months).

³ The wording of our task instructions was derived from para 21 ISA 540. Table 1 in the Appendix shows the wording of the two sets of audit instructions.

encourage higher order thinking motivates more skeptical intentions irrespective of auditor experience. Our data further show that instructional verbs have no impact on auditors' beliefs regarding sufficiency of audit evidence and their feelings of comfort.

Our study has important implications for audit practice. The results highlight that seemingly innocuous changes to the way in which auditors are directed or the way in which requirements are presented in auditing standards can have a significant impact on professional skepticism and audit quality.

Our results provide important insights to standard setting bodies. To encourage professional skepticism, standard setters should consider using instructional verbs shown to encourage higher order thinking rather than, as is often currently the case, instructional verbs that encourage skepticism inhibiting lower order thinking. The IAASB has recently made changes to the wording of audit requirements of ISA 540 and replaced the verbs 'review' and 'identify' with the verb 'evaluate' in paragraph 21 of the standard (IAASB 2018). Our findings inform the veracity of this decision.

The study's results are also relevant to accounting educators as the profession looks to universities for properly trained entry level professionals. Tertiary educators need to understand the effects of different types of instructions on developing appropriate mindsets to ensure graduates are adequately prepared for the professional work environment.

Notwithstanding the importance of our findings, limitations suggest both caution and the need for further research. We manipulated two verbs in each set of instructions, and therefore, it is not possible to definitively conclude whether one or both of the changed verbs drive our results. Caution is also warranted with reference to generalizing our findings to other tasks and to auditors with different experience. We acknowledge that although the use of higher order thinking instructional verbs helps auditors to exercise appropriate levels of skepticism in tasks that are complex and / or ill-defined (e.g., risk-assessment), the positive effect of these verbs may be less pronounced in tasks that are simpler and / or well-defined (e.g., confirmation of accounts receivable). We encourage further research examining different verbs, tasks and auditors.

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Appendix

TABLE 1
Task Instructions

Condition	Audit Instructions
Lower order thinking verbs	In this study, you shall <i>review</i> the judgments and decisions made by management in the making of accounting estimates and <i>identify</i> whether there are indicators of possible management bias.
Higher order thinking verbs	In this study, you shall <i>consider</i> the judgments and decisions made by management in the making of accounting estimates and <i>evaluate</i> whether there are indicators of possible management bias.

This table shows audit instructions used in this study.
In the 'Lower order thinking verbs' condition, the wording of instructions is based on wording of para 21 ISA 540.

TABLE 2
Additional Audit Procedures

Target A: The new fashion items have a higher selling price

1. Examine sales invoices comparing the selling price of new fashion items to that of existing lines.
2. Review sales revenue relative to sales volume month-by-month for the last two years.
3. Review fashion periodicals for evidence on pricing of the new fashion items.

Target B: There were larger orders of the new fashion line items later in the year.

1. Compare order size by customer to the corresponding period in the previous year.
2. Compare actual sales volume to sales forecast data for the final quarter.
3. Confirm large orders in the last quarter with customers.

Target C: New fashion items were well received with an increase in customer satisfaction

1. Make enquiries of the marketing director with reference to their perceptions of consumer demand for the new fashion items.
2. Review balanced scorecard data for customer satisfaction results.
3. Study the most recent customer satisfaction survey results compiled by a well-respected market research company for product ranges in the fashion industry.

Target D: Other fraud related explanations not directly related to management's explanation.

1. Trace sales of new fashion items in the final quarter to evidence that the items have been shipped.
2. Review inventory turnover (COGS/Inventory) ratios by product month-by-month for the last year.
3. Compare sales returns relative to sales in the first month of the new year to the corresponding period in the previous year.

This table shows 12 audit procedures related to the auditors' consideration of the financial controller's explanation regarding the discrepancy in the increase in wholesale sales and gross margin ratio. Each of the 12 procedures addresses 1 of the 4 procedural targets (i.e., selling price, orders, customer satisfaction, and others). Auditors are asked to select up to 5 procedures from the list by assuming that each procedure requires approximately the same amount of audit resources.

A breadth score (2 to 4) is calculated by counting how many of the four procedural targets were addressed by the selected audit procedures. Higher the breadth score is indicative of more skeptical intentions.

TABLE 3
Descriptive Statistics

	Full Sample n = 48	Higher Order Thinking Verbs n = 25	Lower Order Thinking Verbs n = 23
<u>Panel A – Beliefs</u>			
Mean	5.56	5.28	5.87
Standard Deviation	1.945	2.112	1.740
Range	4.50 – 6.69	4.50 – 6.06	5.05 – 6.69
<u>Panel B – Feelings</u>			
Mean	4.98	5.12	4.83
Standard Deviation	1.657	1.424	1.899
Range	4.13 – 5.79	4.45 – 5.79	4.13 – 5.53
<u>Panel C – Skeptical Intentions</u>			
Mean	3.10	3.28	2.91
Standard Deviation	0.515	0.542	0.417
Range	2 – 4	2 – 4	2 – 4
<u>Panel D – Audit Work Experience</u>			
Mean	44.67	46.40	42.78
Standard Deviation	26.585	24.176	29.41
Range	24 – 154	24 – 108	24 – 154

This table shows descriptive statistics of beliefs, feelings, intentions, and audit work experience.

Beliefs: Auditors indicate on a nine-point scale, anchored by 1= extremely weak support for the controller’s explanation and 9 = extremely strong support for the controller’s explanation, the extent to which they believe that the evidence collected by their assistant is sufficient to support the financial controller’s assertions.

Feelings: Auditors indicate on a nine-point scale, anchored by 1= not at all comfortable and 9 = very comfortable, their degree of comfort with the financial controller’s explanation for the discrepancy in the increase in the wholesale sales and gross margin ratio.

Skeptical intentions: Auditors receive a list of 12 potential audit procedures that could be conducted to test the veracity of the financial controller’s assertions. Each of the 12 audit procedures addresses one of the four procedural targets: higher selling price, larger orders, higher customer satisfaction and others. A breadth score (2 to 4) is calculated by counting how many of the four procedural targets were addressed by the selected audit procedures.

Audit Work Experience: Auditors indicate the length of their audit work experience in years and months.