

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 8.1
Meeting date: 2 September 2020
Subject: Review of Compelling reason test and Harmonisation Policy
Date: 18 August 2020
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Action Required **For Information Purposes Only**

Agenda Item Objectives

- a. To CONSIDER preliminary views about proposed amendments to the compelling reason test and harmonisation policy, and
- b. To PROVIDE feedback on the proposed amendments which will be considered by NZAuASB and the AUASB staff in preparation for the joint NZAuASB/AUASB meeting scheduled for 21 October 2020.

Background

1. The key strategic objectives set by the XRB Board for the NZAuASB include:
 - to adopt international auditing and assurance standards, including the professional and ethical standards for assurance practitioners, and standards for related services¹, 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 Board (AUASB) towards the establishment of harmonised standards based on international standards.
2. The XRB Board recognises that the NZAuASB may consider modifying international standards for application in New Zealand under either of those objectives. The XRB Board considers such modifications acceptable, provided they consider the public interest, and do not conflict with or result in lesser requirements than the international standards.
3. The NZAuASB and the AUASB jointly considered and agreed [Principles of Conversion to International standards and the Harmonisation Policy](#), which applied from 1 July 2012, and was revised in July 2014.

¹ Agreed upon procedures or other non-assurance work that may ordinarily be carried out by an audit or assurance practitioner.

4. A specific action within the NZAuASB's SAP for 2019-2021 is to review the compelling reason test and the harmonisation policy jointly with the AUASB, to determine if it remains fit for purpose in the current auditing and assurance environment, both globally and in the two jurisdictions.
5. NZAuASB and AUASB staff have reviewed the compelling reason test and harmonisation policy as set out in the Agreed Principles of Convergence and Harmonisation Policy, and have worked together to develop proposed amendments for both Boards to consider and provide feedback on at their respective September meetings.
6. The AUASB will consider the proposed amendments at their meeting on 5 September. The proposed amendments are the same, other than references to New Zealand, NZAuASB and the XRB Board in the AUASB paper have been amended to refer to Australia, the AUASB and the FRC, where appropriate.
7. Staff will jointly consider the feedback from both Boards resulting from the September meetings and develop a joint final position for the Boards to discuss at the joint October meeting.

Issues with the existing principles

8. Both the NZAuASB and the AUASB have applied the existing policies for a number of years. Largely this policy has assisted the Boards to align the domestic standards even more closely with the international standard. However, possible areas of concern arising include:
 - a. A potential for a backward-looking focus on existing practices. The policy may need to be more flexible to recognise that practice evolves over time.
 - b. The high level of judgement necessary to identify if a compelling reason exists, potential different interpretations (by individuals, new board members or across the Tasman) as to what is a compelling reason and difficulty in articulating and rationalising when a matter meets the compelling reason test.
 - c. Various interpretations as to what is meant by ISA minus.

Matters to Consider

9. NZAuASB and AUASB staff have identified the following key areas where we believe the compelling reason test and harmonisation policy can be enhanced and/or clarified within the strategic parameters of each Board.
 - The requirement to consider the public interest when amending the international standards for principles and practices considered appropriate.
 - The requirement for amendments not to conflict with or result in lessor requirements than the international standards.
10. The marked-up Principles of Conversion and Harmonisation Policy document is available at agenda 8.2. We explain the key proposed amendments below.

Requirement to consider the public interest when amending the international standards for adoption

11. The existing compelling reason test and harmonisation policy includes consideration of the public interest, as per the strategy set by the XRB Board for the NZAuASB. As noted

above, the XRB Board considers modifications the international standards acceptable, provided they consider the public interest, and do not conflict with or result in lesser requirements than the international standards.

12. The existing compelling reason test references IFAC's definition for public interest. IFAC defines the public interest as "*The net benefits derived for, and procedural rigor employed on behalf of, all society in relation to any action, decision or policy*". Refer IFAC Policy Position 5 *A Definition of the Public Interest*, June 2012.
13. As noted in agenda item 7.2, where we consider the Monitoring Group report, the PIF does not define public interest, but sets out useful characteristics to be used to assess the international standards' responsiveness to the public interest. The qualitative characteristics listed in the PIF include characteristics that the NZAuASB discuss all the time, and in many ways explicitly state what is implicitly considered by the NZAuASB.
14. The PIF sets out the following qualitative characteristics to be used to assess the international 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.
15. 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.
16. In many respects, as noted before in agenda 7.2, 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.
17. However, in our view the characteristics do provide a useful framework to overlay in the New Zealand context to inform additional areas of priority for the Board when considering the adoption of the international standards in New Zealand. We therefore propose the following amendments to the existing compelling reason test to incorporate the PIF.
 - Where we refer to the public interest in the compelling reason and harmonisation policy, to include a reference to the qualitative characteristics in the PIF. We consider

this will provide a more detailed/explicit framework under which the Boards can exercise this judgement.

- To allow a compelling reason amendment to be one that reflects principles and practices, whether current or emerging, that are considered appropriate in the public interest in New Zealand, as considered against the qualitative characteristics in the PIF. We consider it is necessary to be clear that compelling reason amendments do not only include existing principles and practices, but also allows the Board to be able to recognise and respond to emerging issues, changes in business environment, developments in accounting practices or technology, etc. in New Zealand, where it is in the public interest to do so. For example, where we may consider going further than IESBA with the NAS provisions.
18. The proposed changes to incorporate the qualitative characteristics in the compelling reason test are shown in mark-up in the Principles of Conversion and Harmonisation Policy document at agenda 8.2.
19. We are also proposing to include the PIF characteristics in the Principles of Conversion and Harmonisation Policy document rather than just referencing to the MG report, for completeness and clarity.

Questions for the Board:

1. What is the Board's view about incorporating the qualitative characteristics of the PIF in the compelling reason test? If the Board agrees about incorporating it, with reference to paragraphs 16-18 in agenda 8.2, what is the Board's view about how we are proposing to incorporate it?
2. What is the Board's view about the proposed amendment to allow for a compelling reason amendment to be one that reflects current and emerging principles and practices, that are considered appropriate in the public interest in New Zealand, as considered against the qualitative characteristics in the PIF? Refer paragraph 19 in agenda 8.2
3. What is the Boards view about including the PIF characteristics in the Principles of Conversion and Harmonisation Policy document? If so, with reference to the marked-up document at agenda 8.2, is the Board happy with where it has been included in paragraphs 7-10 of the marked- up document, or would the Board prefer it to be included as an Appendix?
4. What is the Board's view about keeping the reference to significant improvement in audit quality for an amendment to meet the compelling reason test? Is significant necessary if the benefits exceed the cost? Refer paragraphs 19, 23, and 24 in agenda 8.2.
5. Does the NZAuASB believe there are other elements that should be considered when updating the Principles of Conversion and Harmonisation Policy?

Requirement to not conflict with or result in lessor requirements than the international standards.

20. As noted, the XRB Board considers modifications to the international standards acceptable, provided they consider the public interest, and do not conflict with or result in lesser requirements than the international standards.

21. The existing compelling reason test includes a requirement that any amendment to the international standards should not conflict with or result in lesser requirements than the international standard.
22. However, this is not clearly explained in the Principles of Conversion and Harmonisation Policy document and may be open to inconsistent interpretation.
23. The [IAASB Policy Position, Modifications to International Standards of the IAASB-A Guide for National Standard Setters that Adopt IAASB's International Standards but Find it necessary to Make Limited Modifications \(July 2006\)](#) sets out the policy that NSSs must comply with in order to assert compliance with the international standards when making amendments.
24. We therefore propose to add the following to the Principles of Conversion and Harmonisation Policy document. Other than the highlighted change in wording in paragraph a(ii) below the words are identical to the IAASB Policy Position:

13. To enable the NZAuASB to assert compliance with the international standards when making amendments, for the purpose of conformity under the IAASB's policy position:

- a. Additions to an international standard are limited to the following:
 - i. National legal and regulatory requirements.
 - ii. Other requirements or guidance that are not **lesser or in conflict** with the current requirements or guidance in the IS. Additions falling within paragraph ii are to be communicated to the IAASB for future consideration.
- b. Deletions from, or other amendments to, an international standard are limited to the following:
 - i. The elimination of options (alternatives) provided for in the international standard.
 - ii. Requirements or guidance, the application of which law or regulation does not permit, or which require amendment to be consistent with law or regulation.
 - iii. Requirements or guidance, where the international standard recognises that different practices may apply in different jurisdictions and the NSS is in such a jurisdiction. In the case of paragraph ii - iii, however, the objective of any deleted requirement must still be met.

14. The principles of convergence set out in this paper adhere to the principles set out in the IAASB's Policy Position, which will enable the NZAuASB to assert compliance with the international standards when making amendments.

Question for the Board:

6. What is the Board's view about adding this material to the Principles of Conversion and Harmonisation Policy? If the Board agrees that it should be included, with reference to the marked-up document at agenda 8.2, is the Board happy with where it has been included in paragraph 13-14 of the marked-up document, or would the Board prefer it to be included as an Appendix?

Proposed amendments to the Harmonisation Policy

25. We are proposing amendments to the harmonisation policy with the AUASB in paragraphs 22-26 of agenda 8.2 to align with the proposed amendments to the compelling reason

Commented [SvD1]: The IAASB policy paper includes the word "inconsistent" here. We suggest amending it to "lesser or in conflict" to align with the XRB Board strategy. We believe this meets the intent of the IAASB Policy as well as the XRB Board strategy

test, and to reflect current practices on developing domestic standards jointly with the AUASB.

Question for the Board

7. What is the Board's view about the proposed amendments to the harmonisation policy?

Recommendations

26. We recommend that the Board consider and provide feedback on the proposed amendments for further consideration at the joint meeting with the AUASB in October.

Material Presented

Agenda item 8.1	Board Meeting Summary Paper
Agenda item 8.2	Marked- up Principles of Convergence and Harmonisation Policy