3 November 2014

The Interim Chairman
International Ethics Standards Board for Accountants
529 5th Avenue
6th Floor
New York 10017
United States of America

Submission via IESBA website

Dear Mr Kwok

Submission on Exposure Draft: Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client ("the ED")

Chartered Accountants Australia and New Zealand is made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over.

Members of Chartered Accountants Australia and New Zealand are known for professional integrity, principled judgement and financial discipline, and a forward-looking approach to business. We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are represented on the Board of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We commend the IESBA's efforts to promote and enhance objectivity and professional scepticism. We agree it is essential that audit and assurance teams and firms are independent, both of mind and in appearance, of their clients and we support a common international framework for making that assessment. However, while we support review of the framework and continuing work to enhance the framework if required due to changing circumstances, we do not support the specific proposals in this ED.

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We understand that the IESBA is responding to a perceived need for change, and we have always been strong supporters of change that leads to increased audit quality as this is in the public interest. However, we do not believe that a move to a five year cooling-off period for engagement partners will achieve this aim. No evidence has been presented in the proposals to support the proposition that increasing the cooling-off period will improve audit quality. In fact, we believe that increasing the cooling-off period to five years will have a number of consequences which have the potential to adversely impact audit quality. This view is shared by a clear majority of the members we consulted with.

We believe that other approaches which strengthen auditor independence without negatively impacting audit quality, such as a comply or explain model, should be further explored. We do not consider there is an issue in the Australian or New Zealand market with the current requirements in place, including the two year cooling-off period coupled with the ECQR process. We believe these; along with audit firms' own systems of quality control already achieve the objective of maintaining a robust independence framework. In addition, independent internal and external quality reviews, use of an auditor's expert for specialist areas, natural turnover of audit team and client personnel, provide adequate safeguards.

Should the proposals proceed, our members emphasised the importance of an adequate lead time to enable them to plan for engagement partner rotation.

The appendix (attached) provides responses to the specific questions raised in the ED. If you have any questions regarding this submission, please contact Liz Stamford (Audit and Insolvency Leader) via email; Liz.Stamford@charteredaccountantsanz.com.

Yours sincerely

Rob Ward FCA
Head of Leadership and Advocacy

Appendix: Responses to specific questions

Q1. Do the proposed enhancements to the general provisions in paragraph 290.148 provide more useful guidance for identifying and evaluating familiarity and self-interest threats created by long association? Are there any other safeguards that should be considered?

We support the approach taken in this aspect of the ED that familiarity and self-interest threats should be evaluated for all members of the engagement team as opposed to just senior personnel. In practice however, we believe that it would be rare for a junior member of the engagement team to have a familiarity threat due to long association. In addition, other kinds of familiarity threats such as personal relationships are likely to already be managed through the firm's internal processes.

In relation to the proposed safeguards set out in paragraph 290.149A, we question whether changing the role of the individual on the audit team is a feasible safeguard. Lateral movement of individuals would be practically difficult on smaller engagements and it is unclear how this would reduce the significance of any threats. An additional safeguard that may be considered is obtaining the concurrence of those charged with governance for an individual to remain a member of the engagement team, depending on the severity of the threat. Our members also felt that training of audit personnel in independence requirements and professional scepticism provides an important safeguard by providing awareness of the issue of familiarity threats.

Q2. Should the general provisions apply to the evaluation of potential threats created by the long association of all individuals on the audit team (not just senior personnel)?

No. Introducing this requirement will introduce an unnecessary level of complexity in the management of engagement teams. In practice, the junior members of the engagement team do not usually have extended contact with senior personnel at the client. Additionally in the time over which a junior engagement team member becomes more senior, it is likely that there will have been change in client personnel, so it is unlikely that a true familiarity threat would evolve. Some of our members expressed concerns that if too many members of the audit team rotate off the engagement, there are potential adverse impacts to the depth of understanding within the audit team of the entity and its environment which would adversely impact audit quality.

Q3. If a firm decides that rotation of an individual is a necessary safeguard, do respondents agree that the firm should be required to determine an appropriate time-out period?

We support the approach taken in this aspect of the ED that an audit firm should have the discretion to determine its own approach to managing these situations.

Q4. Do respondents agree with the time-on period remaining at seven years for KAPs on the audit of PIEs?

We support the approach taken in this aspect of the ED.

Q5. Do respondents agree with the proposal to extend the cooling-off period to five years for the engagement partner on the audit of PIEs? If not, why not, and what alternatives, if any, could be considered?

We accept that a cooling-off period for the engagement partner provides a mechanism for a 'fresh pair of eyes' to be introduced to the engagement and to help maintain independence. Given the lack of empirical evidence, the number of years that is appropriate for a cooling-off period is arbitrary. Assurance practitioners have confidence that the current mechanism already provides sufficient safeguards to address the threat to independence of mind from long association. In our consultations with the director and preparer community, they similarly did not feel there was any issue with the current two year cooling-off period. Therefore, we do not support this proposal.

If there is a perceived issue with auditor independence, it is necessary to implement a solution that will address the issue without negatively impacting audit quality. There was a near-unanimous view amongst our members that a five year cooling-off period will negatively impact audit quality for the following reasons:

- Below the larger firms, introducing a five year cooling-off period may result in a de facto mandatory audit firm rotation if there are an insufficient number of audit partners to manage engagement partner rotation successfully. Given that other proposals in relation to mandatory rotation have largely been aimed at ensuring that the audit market does not become an oligopoly, this proposal appears to be counterintuitive with the objective of having a competitive market. Additionally, in Australia and New Zealand, there is already a shortage of suitably qualified and experienced auditors in regional areas. Further contraction of the audit market will not promote audit quality.
- Even in firms which have sufficient numbers of audit partners to manage rotation, it is likely that increasing the cooling-off period will result in an increase in the number of engagements where the engagement partner is located in a different geographical location to the client and the engagement team. A high level of consistent audit partner involvement with the client and the engagement team has been acknowledged to be a key driver of audit quality. Where partners are geographically separated it becomes more difficult for partners to sustain this level of involvement, and therefore audit quality may be adversely affected.
- Clients may decide that moving to a firm where they only have to change audit partners rather than change firms altogether is preferable. This could result in engagement partners having to spend additional time in business development activities and securing additional clients. This is time that then cannot be spent on audit quality activities. Clients would also incur additional costs from the time and resources required to conduct a tender process, and then again when a new auditor is selected.
- The coordination of engagement partner rotation is already time consuming and costly for firms. Increasing the administrative complexity by introducing an excessive cooling-off period will only increase these costs, even when the audit firm does not change, without increasing audit quality.

These outcomes could negatively impact audit quality, reducing the progress that the profession has worked hard for over the last decade, which is not in the public interest. Given that there is no evidence that a longer cooling-off period will improve independence, we believe the costs of this proposal clearly outweigh any potential benefits.

Q6. If the cooling-off period is extended to five years for the engagement partner, do respondents agree that the requirement should apply to the audits of all PIEs?

We do not support the proposal.

Q7. Do respondents agree with the cooling-off period remaining at two years for the EQCR and other KAPs on the audit of PIEs? If not, do respondents consider that the longer cooling-off period (or a different cooling-off period) should also apply to the EQCR and/or other KAPs?

EQCR partners have a greater degree of separation from the client and the audit team, therefore it follows that the potential familiarity threat is reduced. Other KAP's have a lesser ability to influence the outcome of the audit, along with a lesser involvement with the client which reduces the significance of the threat to independence. On this basis we support the cooling-off period remaining at two years.

Q8. Do respondents agree with the proposal that the engagement partner be required to cool-off for five years if he or she has served any time as the engagement partner during the seven year period as a KAP?

No. This requirement is inflexible and would further increase complexity and burden to audit practitioners. It does not support flexibility and mobility in the audit profession. In Australia, the Corporations Act 2001 imposes a 'five years out of seven years' approach to partner rotation and we believe this is a more practical approach. Our members expressed a desire for clear and specific guidance being provided to illustrate the final requirements imposed.

Q9. Are the new provisions contained in 290.150C and 290.150D helpful for reminding the firm that the principles in the general provisions must always be applied, in addition to the specific requirements for KAPs on the audits of PIEs?

We support the approach taken in this aspect of the ED.

Q10. After two years of the five year cooling-off period has elapsed, should an engagement partner be permitted to undertake a limited consultation role with the audit team and audit client?

We believe that clients should be able to access specialist knowledge where they feel this is beneficial to them. Therefore, should the proposals proceed; we believe it is appropriate for the engagement partner to be able to perform a limited role in the rare circumstances outlined in the ED after two years of the five year cooling-off period has elapsed. Although we note that permitting such consultation directly with the audit client after such time appears to support keeping the cooling-off period for engagement partners at two years.

Q11. Do respondents agree with the additional restrictions placed on activities that can be performed by a KAP during the cooling-off period? If not, what interaction between the former KAP and the audit team or audit client should be permitted and why?

It was felt that these additional restrictions just introduce unnecessary complexity. In practice they would be too time consuming and difficult for firms to manage which may result in firms imposing their own stricter requirements, such as not allowing interaction with clients at any time during the cooling-off period, which would potentially penalise clients and prevent them from accessing appropriate expertise.

Q12. Do respondents agree that the firm should not apply the provisions in paragraphs 290.151 and 290.152 without the concurrence of TCWG?

We support the approach taken in this aspect of the ED.

Q13. Do respondents agree with the corresponding changes to Section 291? In particular, do respondents agree that given the differences between audit and other assurance engagements, the provisions should be limited to assurance engagements "of a recurring nature"?

Should the proposal proceed, we believe it is appropriate to limit the provisions to other assurance engagements of a recurring nature for PIEs and provide auditor discretion for other assurance engagements.

Q14. Do respondents agree with the analysis of the impact of the proposed changes? In the light of the analysis, are there any other operational or implementation costs that the IESBA should consider?

We disagree with the analysis. We do not believe there is evidence that the proposals support the public interest and we consider the potentially damaging outcomes to audit quality and the audit profession, particularly for smaller firms and competition, have not been appropriately understood or considered.