

25 April 2017

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Dear Ken,

IESBA Exposure Draft – Proposed Revisions Pertaining to Safeguards in the Code – Phase 2 and Related Conforming Amendments

Thank you for the opportunity to comment on the IESBA exposure draft of proposed revisions pertaining to safeguards in the Code Phase 2 and related conforming amendments. We submit the feedback from the New Zealand Auditing and Assurance Standards Board (NZAuASB) 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, including ethical standards for assurance practitioners.

Overall comment

The NZAuASB supports the proposed revisions to clarify and enhance the safeguards-related provisions in the independence section of the Code pertaining to non-assurance services provided to audit clients, as well as the safeguards-related conforming amendments to sections of the Code that were covered in Phase 1 of the Structure Project.

Independence standards for other assurance engagements

The NZAuASB is of the view that the provisions in the international independence standards pertaining to non-assurance services provided to assurance clients, and more generally, the provisions pertaining to independence for other assurance engagements, could be significantly more robust.

The aim of the IESBA's structure project is to comprehensively review the structure and drafting of the IESBA Code to enhance its understandability and usability, thereby facilitating its adoption, effective implementation, consistent application, and enforcement. Within the Code, the independence requirements pertaining to the provision of non-assurance services to an assurance client are less robust than the independence requirements pertaining to audit [and review] clients. In an audit [or review] engagement, the objective of the auditor is to obtain reasonable assurance [or limited assurance]. In an other assurance engagement, the objective of the assurance practitioner is to obtain reasonable or limited assurance.

Accordingly, the NZAuASB considers the framework proposed for auditors [and reviewers] is equally appropriate to other assurance practitioners. Applying the same safeguards-related provisions in the independence section of the Code pertaining to non-assurance services provided to audit clients to assurance clients will increase quality, be more consistent with other assurance standards and the expectations of the users of assurance reports, avoid confusion and streamline the Code.

Meaning of audit engagement

Section 600, and more generally Part 4A of the Code, applies equally to audit and review clients, however, some of the language used in Section 600 is “audit centric.” For example, the discussion of materiality in relation to an audit client’s financial statements, specifically references ISA 320, *Materiality in Planning and Performing an Audit*. There is no discussion of materiality in the context of a review engagement which is equally relevant. Care needs to be taken when drafting not to use audit specific wording when referring to both audit and review engagements. The NZAuASB’s preference is to refer separately to audit and review engagements rather than using the term audit engagement as short-hand. Indeed, to ensure clarity for our stakeholders this is one of the modifications the NZAuASB made when adopting the extant Code.

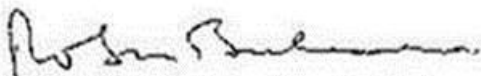
Consistency of wording between IFAC standard setting boards

In the following “Schedule of Responses to IESBA’s Specific Questions” a number of inconsistencies are noted between the IAASB standards and the proposed IESBA Code. The NZAuASB encourages the IESBA to continue to work with IAASB to ensure that, where possible, consistent wording is used throughout the standards set by the IFAC standard setting boards.

In formulating this response, the NZAuASB sought input from New Zealand constituents.

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

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Submission of the New Zealand Auditing and Assurance Standards Board

IESBA Exposure Draft – Proposed Revisions Pertaining to Safeguards in the Code – Phase 2 and Related Conforming Amendments

I Schedule of Responses to the IESBA’s Specific Questions

Section 600, Provision of Non-Assurance Services to an Audit Client

1. Do respondents support the proposals in Section 600? If not, why not?

Response:

The NZAuASB supports the proposed revisions to clarify and enhance the safeguards-related provisions in the independence section of the Code pertaining to non-assurance services provided to audit clients.

The NZAuASB has the following comments on specific paragraphs.

Paragraph 600.5 A1

As noted in the introduction, the use of “audit” to mean “audit or review” is problematic in paragraph 600.5 A1 where the concept of materiality is referenced to ISA 320, *Materiality in Planning and Performing an Audit*. There is no reference made to materiality in a review engagement.

The second sentence could be moved to a footnote and revised as follows

“The concept of materiality is addressed in ISA 320, *Materiality in Planning and Performing an Audit*, and ISRE 2400, *Engagements to Review Historical Financial Information*, for audit and review engagements respectively.”

Paragraph R600.10

This paragraph is labelled as a requirement but does not contain requirement language. The clarified wording is less clear than the extant wording. In addition, reference to the prohibitions may also be helpful.

A firm or network firm may assume management responsibilities or provide certain non-assurance services that would otherwise be prohibited under Section 600-prohibits assuming management responsibilities or providing certain non-assurance services to audit clients. As an exception to those requirements, a firm or network firm may assume management responsibilities or provide non-assurance services that would otherwise be prohibited to the following related entities of the client on whose financial statements the firm will express an opinion:...

(iv) The firm applies the conceptual framework to eliminate or reduce to an acceptable level any threats created ~~or reduce them to an acceptable level~~.

Paragraphs R601.6 and R601.7 – These paragraphs are complicated and confusing. The extant wording is much clearer and easier to understand. The reference to audit client implies that the

professional accountant will be expressing an opinion (or in the case of a review engagement, a conclusion). Accordingly, the words “on which the firm will express an opinion, or financial information which forms the basis of the financial statements on which the firm will express an opinion” may not be necessary in this context. In addition, accounting and bookkeeping services is defined in paragraph 601.3 A1.

~~R601.6 A firm or a network firm shall not provide to an audit client that is not a public interest entity, services related to accounting and bookkeeping services on which the firm will express an opinion, or financial information which forms the basis of the financial statements on which the firm will express an opinion, to an audit client that is not a public interest entity unless only if:~~

(a) The services are of a routine or mechanical nature; and

~~(b) The firm addresses any threats created by providing such services are reduced to an acceptable level.~~

~~R601.7 A firm or a network firm shall not provide to an audit client that is a public interest entity accounting and bookkeeping services including preparing financial statements on which the firm will express an opinion or financial information which forms the basis of the financial statements to an audit client that is a public interest entity.~~

Paragraph R605.7 – In sub-paragraph (b) “significant” is changed to “material”. The NZAuASB supports this change. The NZAuASB also notes that in this paragraph and throughout the Code, when referring to materiality, the words “separately or in the aggregate” are used. Throughout the International Standards on Auditing, the wording used is “individually or in the aggregate.” The NZAuASB encourages the IESBA to continue to work with IAASB to ensure that, where possible, consistent wording is used throughout the standards set by the IFAC standard setting boards.

In particular, do respondents agree with the proposal to extend the scope of the prohibition on recruiting services as described in paragraph 26(h) to all audit client entities? If not, please explain why.

Response:

The NZAuASB supports the proposal to extend the scope of the prohibition on recruiting services with respect to a director or officer of the entity or senior management in a position to exert significant influence over the preparation of the client’s accounting records or the financial statements on which the firm will express an opinion to all audit clients.

Section 950, Provision of Non-Assurance Services to an Assurance Client

2. Do respondents support the proposals in Section 950? If not, why not?

Response:

The NZAuASB supports the proposals in Section 950, however, as noted in the introductory comments, the NZAuASB considers the framework proposed for auditors [and reviewers] is equally appropriate to other assurance practitioners. Applying the same safeguards-related provisions in the independence section of the Code pertaining to non-assurance services provided to audit and review clients to non-

assurance services provided to other assurance clients will increase quality, be more consistent with other assurance standards and the expectations of the users of assurance reports, avoid confusion and streamline the Code.

Examples of Safeguards

- 3. Do respondents have suggestions for other actions that might be safeguards in the NAS and other sections of the Code that would meet the revised description of a safeguard?**

Response:

The NZAuASB has no further suggestions.

Conforming Amendments Arising from the Safeguards Project

- 4. Do respondents agree with the proposed conforming amendments set out in:**

- a. Chapter 2 of this document
- b. The gray text in Chapters 2-5 of Structure ED-2

Response:

The NZAuASB generally agrees with the proposed conforming amendments set out in Chapter 2 of Safeguards ED-2 and the grey text in Chapters 2-5 of Structure ED-2. The NZAuASB offers editorial suggestions on Phase 2 of the Safeguards project including conforming amendments in Section II below.

- 5. Respondents are asked for any comments on any other matters that are relevant to Phase 2 of the Safeguards project.**

Response:

The NZAuASB has the following specific comments on other matters relevant to the Safeguards project:

Use of “might”

Throughout the conforming amendments, removing an individual from the audit team is frequently cited as an action that *might* eliminate the threat [emphasis added]. Introducing the word “might” implies that the action might not work. Further, “might” is generally used to express what is hypothetical, counterfactual, or remotely possible.¹ Removing the individual from the audit team will eliminate the threat. Accordingly, the following wording may be more accurate:

An example of an action that ~~might~~ will eliminate the threat is...

Addressing threats vs reducing to an acceptable level

¹ <http://writingexplained.org/may-vs-might-difference>

The construct used throughout the proposed conforming amendments, is “an example of an action that might be a safeguard to address threats created by ... is...” However, the professional accountant is required by paragraph R120.10 to reduce threats to an acceptable level by applying safeguards. Accordingly, the following construct may more accurately reflect the requirement,

An example of an action that might be a safeguard to reduce ~~address~~ threats created by...to an acceptable level is...

II Editorial Suggestions

Suggested added text is underlined, deleted text is struck through.

Safeguards ED-2

Paragraph 600.2 – delete repetition of “threats to” in the last sentence. Also the use of “might” in the first sentence is confusing. When might is used in the Code it denotes the possibility of a matter arising, an event occurring or a course of action being taken. Rather than using “might” to denote possibility, it may be more accurate to use “may” indicating that such non-assurance services are permitted or alternatively, state that this is “often” the case.

Firms and network firms ~~might~~ often provide a range of non-assurance services to their audit clients, consistent with their skills and expertise. Providing non-assurance services to audit clients might create threats to compliance with the fundamental principles and ~~threats to~~ independence.

Paragraph 600.3 –The last sentence can be simplified by changing “...there can be no safeguards to reduce them to an acceptable level” to “...reduced to an acceptable level.” This wording is consistent with paragraph R120.10². Also, in the second sentence, “specific” and “relevant” are not both necessary. It is the requirements and application material that are specific to the providing certain non-assurance services.³

Section 600 sets out requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence when providing non-assurance services to audit clients. The subsections that follow set out ~~specific~~ requirements and application material specific relevant to providing certain non-assurance services to audit clients and indicate the types of threats that might be created as a result. In some cases, these subsections expressly prohibit a firm or network firm from providing certain services to an audit client because the threats cannot be eliminated or ~~there can be no safeguards to reduced~~ them to an acceptable level.

Paragraph 600.4 A2 - In accordance with the Structure project drafting guidelines, refer to “the Code” rather than “this Code.”

New business practices, the evolution of financial markets and changes in information technology, are amongst the developments that make it impossible to draw up an all-inclusive list of non-

² See Compilation of Proposed Restructured Code (as of January 2017), page 20

³ This comment applies to paragraphs under the heading “introduction” in each of the Sections and Subsections of the proposed Code.

assurance services that might be provided to an audit client. As a result, ~~this the~~ Code does not include an exhaustive listing of all non-assurance services that might be provided to an audit client.

Paragraph 600.4 A3 – In the last sentence, it is not clear whether “more specific factors” means, (1) additional factors, (2) factors that are more specific than those identified in the current paragraph, or (3) factors that are specific to providing a particular type of non-assurance service. The words “more specific” could be deleted from this paragraph to clarify its meaning.

...The subsections that follow include ~~more specific~~ factors that are relevant in evaluating the level of any threats created by providing certain non-assurance services.

Paragraph 600.7 A2 - Consider placing paragraph 600.7 A2 before 600.7 A1 so that management responsibilities are described before discussing the threats that assuming a management responsibility can create.

Paragraph 601.1 – Providing accounting and bookkeeping services to an audit client does create a self review threat. Delete “might” in this paragraph.

Providing accounting and bookkeeping services to an audit client ~~might creates~~ a self-review threat.

Paragraph 601.3 A1 – In the second bullet point, remove “bookkeeping and” as bookkeeping is already included in the lead in to the paragraph.

Accounting and bookkeeping services comprise a broad range of services including:

- Preparing accounting records and financial statements.
- ~~Bookkeeping and p~~Payroll services.

Paragraph 602.3 A2 – Consider deleting the word “audit” in the final bullet point. The other bullet points do not specify audit client.

- ... Monitoring statutory filing dates, and advising ~~an audit~~ client of those dates.

Paragraph R601.8 – The exception in this paragraph should reference R601.7.

As an exception to paragraph R601.67

Paragraph R603.6 –The wording “separately or in the aggregate” is used throughout the Code when referring to materiality whereas the IAASB’S standards use “individually or in the aggregate.” The NZAuASB supports consistency of wording between the sets of international standards, where possible.

Paragraph 604.1 – The NZAuASB considers that providing taxation services to an audit client does create a self-review or advocacy threat, accordingly the NZAuASB recommends deleting “might”. In addition, the extant Code indicates that providing certain tax services creates both self-review and advocacy threats.

Providing taxation services to an audit client ~~might creates~~ a self-review ~~or~~ and advocacy threats.

Paragraph 604.3 A1 – The wording of the final sentence in this paragraph is clearer in the extant Code.

While ~~this subsection deals with different types of~~ taxation services are described [in the Code] above separately under separate headings, in practice, the activities involved in providing taxation services are interrelated.

Paragraph 604.16 A2 – in the third bullet point, the words “in the matter” are repetitive of the lead-in and are not needed.

Paragraph R604.16 does not preclude a firm from having a continuing advisory role in relation to the matter that is being heard before a public tribunal or court, for example:...

- Assisting the client in analyzing the tax issues ~~in the matter~~.

Paragraph 604.16 A3 – Consider the following rewording to simplify the third bullet point in this paragraph.

Whether the firm or network firm provided the advice which is the subject of the tax dispute ~~has been provided by either the firm or network firm~~.

Paragraph R605.4 – In sub-paragraph (a)(ii), the NZAuASB questions the addition of “monitoring” and recommends that it be deleted. The Glossary of Terms to the Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements defines internal control as, “the process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity’s objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.” As noted previously, the NZAuASB supports consistency of wording across the international standards.

(a)(ii) Acknowledge responsibility for designing, implementing, ~~monitoring~~ and maintaining internal control.

Paragraph 607.2 – Section 600 sets out both requirements and application material. Accordingly, the second sentence should read,

...The requirements and application material set out in Section 600 ~~is~~ are relevant to this subsection.

Paragraph 608.1 – As drafted, this paragraph implies that self-review and advocacy threats are mutually exclusive. This is not the case. Accordingly, the NZAuASB recommends using the following wording.”

Providing legal services to an audit client ~~might~~ may create a self-review and ~~of~~ advocacy threats.

Paragraph R610.6 – To avoid repetition

A firm or network firm shall not provide corporate finance advice to an audit client where the effectiveness of ~~corporate finance~~ such advice depends on a particular accounting treatment or presentation in the financial statements and: ...

Conforming Amendments to Agreed-in-Principle Text - Structure and Safeguards Phase 1

Paragraph 321.5 A1 To correct an editorial error, the following amendment is suggested.

Factors that are relevant in evaluating the level of a threat created by providing a second opinion to an entity that ~~are~~ is not an existing client ~~is~~ depend on the circumstances of the request and all the other available facts and assumptions relevant to the expression of a professional judgment.

Paragraph 321.5 A2 – In the first bullet point, consider changing “obtaining” to “requesting.” The professional accountant can request to communicate with the existing/predecessor accountant, however the professional accountant may not be able to obtain information from the existing/predecessor accountant. How the existing/predecessor accountant responds to the professional accountant will affect whether the safeguard has addressed the threat.

Examples of actions that might be safeguards to address the threats created by providing a second opinion include:

- With the client’s permission, ~~obtaining~~ requesting information from the existing or predecessor accountant.

Chapter 2 - Conforming Amendments Arising from the Safeguards Project Not Included in Structure ED-2

Paragraph 410.9 A2 – in the second bullet point, delete “or” before “review the work performed” to correct this sentence.

... Having an additional professional accountant, who did not take part in the audit engagement ~~or~~ review the work performed.

Paragraph 521.5 A3 – delete “s” on actions and safeguards as singular not plural.

An example of an ~~actions~~ that might be a ~~safeguards~~ to address the threats set out in paragraph 521.5 A1 is:...

Proposed Conforming Amendments included in the Structure ED-2

Paragraph 905.7 – in sub-paragraph (b), the words “because of the significance of the overdue fee” appear to be unnecessarily repetitive of the beginning of the paragraph which states, “when a significant part of fees due from an assurance client remains unpaid for a long period of time...”

When a significant part of fees due from an assurance client remains unpaid for a long time, the firm shall determine:

- (a) Whether the overdue fees might be equivalent to a loan to the client; and
- (b) Whether it is appropriate for the firm to be re-appointed or continue the assurance engagement ~~because of the significance of the overdue fee.~~

Paragraph 911.6 A2 – In the circumstances described, the firm is receiving the loan. Accordingly, the last sentence of this paragraph can be deleted. In addition, the words “received the loan” are much clearer and easier to understand than “is a beneficiary of the loan” and are consistent with wording used earlier in the paragraph.

If a loan from an assurance client that is a bank or similar is made under normal lending procedures, terms and conditions and it is material to the assurance client or firm receiving the

loan, it might create a self-interest threat. An example of an action that might be a safeguard to address such a threats is having the work reviewed by a professional accountant from a network firm who is not a member of the assurance team that is neither involved with the assurance engagement nor received is a beneficiary of the loan. ~~If the loan is to a firm, the reviewing professional might be someone from a network firm.~~

Paragraph 921.4 A1 – the “closeness of the relationship” could be a separate bullet point.

- The role of the family member of other individual within the client, ~~and the closeness of the relationship.~~
- The closeness of the relationship.

Paragraph R924.5 – The construct used in paragraph 291.127 of the extant Code is clearer and more succinct than the revised wording.

If a former assurance team member or partner joins an assurance client ~~of the firm or a former assurance team member joins the assurance client~~ as:

- (a) A director or officer; or
- (b) An employee in a position to exert significant influence over the subject matter information of the assurance engagement,

~~The such~~ individual shall not continue to participate in the firm’s business or professional activities.

Paragraph 924.5 A1 – Adding a reference to paragraph R924.5 would make clear who “if one of those individuals” is referring to.

If one of those individuals referred to in 924.5 has joined the assurance client ...

Paragraph 924.6 A2 – The following wording more clearly identifies the threats that are being discussed in this paragraph. In addition, using the word “individual” to refer to both an appropriate person who reviews significant judgements and the former assurance team member is confusing.

An example of an action that might be a safeguard to address a familiarity or intimidation threats ~~set out in paragraph 924.4 A1~~ is having an appropriate individual review any significant judgements made by ~~that individual~~ the assurance team member while on the team.

An example of an action that ~~might~~ will eliminate those threats is removing the ~~individual~~ assurance team member from the assurance engagement.