

18 August 2014

Mr Ken Siong
Technical Director
International Ethics Standards Board for Accountants
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, NY 10017
USA

Dear Ken,

IESBA Exposure Draft *Proposed Changes to Certain Provision of the Code Addressing Non-Assurance Services for Audit Clients.*

Thank you for the opportunity to comment on the IESBA exposure draft of proposed changes to certain provisions of the Code addressing non-assurance services for audit clients. We submit the feedback from the New Zealand Auditing and Assurance Standards Board (NZAuASB) in the attachment.

Overall the NZAuASB supports the project and proposed changes, and considers that these changes will support a more rigorous approach to independence as well as promoting harmonisation globally. The project to review the non-assurance services prohibitions is relevant and timely, given recent global regulatory reforms and interest in this topic. We consider that to the extent possible, prohibited non-assurance services should be consistent around the world as this will:

- bolster confidence in the independent auditor,
- remove uncertainty about what rules apply; and
- reduce complexities for audit firms and companies that operate across borders.

We consider that the prohibitions included in the IESBA Code for auditors of Public Interest Entities are robust and comparable to many countries in the world. In New Zealand, the NZAuASB has adopted the IESBA Code and is harmonised with respect to the provision of non-assurance services to an audit client. We support the principled approach adopted by IESBA. In relatively smaller jurisdictions, like New Zealand, a more restrictive rules based approach could put considerable pressure on the supply of auditors without identifiable benefits to enhancing auditor independence.

We do however consider that the visibility and clarity of these prohibitions could be improved. We therefore support the current project to restructure the Code, as we consider that these prohibitions would be further enhanced by improving the readability, understandability and accessibility of the requirements. (For example, creating an accessible black list of prohibited non-assurance services for public interest entities would assist both the auditors in applying the prohibitions and users and regulators in understanding the prohibitions). We recommend that the IESBA continue to monitor the provisions of the Code in relation to valuation, taxation and internal audit services as these are areas where there continues to be international divergence.

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,

A handwritten signature in blue ink, consisting of several overlapping loops and a long horizontal stroke extending to the right.

Neil Cherry
Chairman – New Zealand Auditing and Assurance Standards Board

Email: neil.cherry@xrb.govt.nz

Submission of the New Zealand Auditing and Assurance Standards Board

IESBA Exposure Draft *Proposed Changes to Certain Provision of the Code Addressing Non-Assurance Services for Audit Clients.*

I Schedule of Responses to the IESBA's Specific Questions

Emergency Provisions

1. Are there any situations that warrant retention of the emergency exceptions pertaining to bookkeeping and taxation services?

Response:

We consider that the removal of these exceptions will strengthen the Code and will better serve the public interest as they relate to public interest entities and the exception creates the potential for misuse. Prohibiting such an action is undermined where an exception is given. We also agree that such circumstances should be so rare that if and when they do occur, the appropriate action would be to consult with the professional body and or regulator rather than for the auditor or client to make the decision. With the addition of the breaches of the code provisions, we consider that this exception is no longer necessary.

Management Responsibilities

2. Does the change from "significant decisions" to "decisions" when referring to management responsibilities (paragraph 290.162) enhance the clarity of a management responsibility?

Response:

The NZAuASB agrees that all decision-making is the responsibility of management, and therefore removing "significant" does enhance clarity. This also better distinguishes decision making from administrative or mechanical tasks in the later paragraphs.

3. Are the examples of management responsibilities in paragraph 290.163 appropriate?

Response:

The NZAuASB agrees that all of the examples listed in paragraph 290.163 are relevant management responsibilities. We support the addition of examples including: hiring or terminating employees, supervising activities for the purposes of management oversight, and the control or management of bank accounts or investments.

4. Are there any challenges in understanding and applying the prerequisite set out in paragraph 290.165 for non-assurance services that should be considered?

Response:

The NZAuASB considers that proposed paragraph 290.165 better clarifies how the auditor can be satisfied that the client makes all appropriate judgements and decisions. We consider that it is appropriate that the client designates a staff member to oversee any non-assurance services provided by the auditor and that these additions strengthen the Code, as it more clearly articulates that the responsibility for the services performed rests with the client. We consider that the audit client should acknowledge its responsibilities when agreeing the terms of an engagement for non-assurance services.

5. Will the enhanced guidance assist engagement teams to better meet the requirement of not assuming a management responsibility?

Response:

The NZAuASB considers that the additional examples and amendments clarify the prohibition and should assist engagement teams to better understand the requirement not to assume a management responsibility. We support the clear statement that a firm shall not assume a management responsibility.

6. Does the relocation of the guidance pertaining to administrative services into its own subsection provide greater clarity?

Response:

Yes, the NZAuASB agrees that relocating this material to its own subsection provides greater clarity. The management responsibilities section now relates more specifically to decision making, and administrative services is dealt with as its own class of service, isolating out routine and mechanical tasks from the decision making functions.

We do however have further recommendations on ordering and edits we consider will enhance the clarity of the management responsibility paragraphs. Within the management responsibilities section, we recommend, as illustrated below, that:

- the prohibition on assuming management responsibilities in paragraph 290.164 should be stated as the first paragraph. We suggest that this enhances clarity, as then the section would first clearly set out whether this service is permitted or prohibited, and then add further guidance to assist in applying the prohibition. We consider that this sets the appropriate frame of reference for the section on management services;
- the duplication of references to deciding which recommendations of the firm to implement in proposed paragraph 290.163 and 290.164 should be removed, and only referred to in 290.163;
- the proposed addition to paragraph 290.164, that cross refers to 290.165 should be moved to the end of paragraph 290.165, avoiding the need for the cross reference.

These recommendations are illustrated as follows:

290.162 A firm shall not assume a management responsibility for an audit client. The threats created would be so significant that no safeguards could reduce the threats to an acceptable level. ~~For example, deciding which recommendations of the firm to implement will create self-review and self-interest threats.~~ Further Assuming a management responsibility creates self-review and self-interest threats for any decisions made by the auditor and a familiarity threat because the firm becomes too closely aligned with the views and interests of management.

290.163 Management responsibilities involve controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, physical, technological and intangible resources.

290.164 Examples of activities that would be considered a management responsibility include:

.....

290.165 When providing non-assurance services to an audit client, the firm shall be satisfied that client management makes all judgements and decisions that are the responsibility of management. This includes ensuring that the client's management:

- Designates an individual....;
- Provides oversight....;
- Accepts responsibility for the actions....

Providing advice and recommendations to assist management in discharging its responsibilities is not assuming a management responsibility, where client management makes all relevant decisions and judgements. [Moved from proposed 290.164], with context added.

Routine or Mechanical

7. Does the proposed guidance on “routine or mechanical” clarify the term, or is additional guidance needed?

Response:

The NZAuASB supports the proposed changes but recommends further clarification.

We recommend that the following additional words would make it even clearer what is meant by “routine or mechanical”:

290.171 “Services that are routine or mechanical in nature require little to no professional judgement from the professional accountant and do not result in the professional accountant making decisions on behalf of the client.”

The NZAuASB also considers that some of the examples listed of routine or mechanical services involve judgement and decision making and therefore it is not appropriate for the auditor to perform these tasks. We therefore recommend removing the following examples:

- Providing payroll services based on client-originated data.

We recommend deleting this example. Payroll services cover a broad range of activities, which are usually packaged together. We consider that most payroll services should not be permitted as they go beyond routine or mechanical procedures. Preparing payroll calculations or reports based on client originated data by itself is a mechanical calculation, however paying the staff (based on this data) or the relevant tax authority, reviewing these reports for reasonableness and any payroll related tax matter would not be. If this example is retained it should be articulated more strictly to avoid misinterpretation as follows: “Preparing payroll calculations or reports for approval and payment by management;”

- Recording a transaction involving a significant degree of subjectivity, for example the valuation of an asset when the client has determined the classification and amount to be recorded.

Care should be taken not to imply that the valuation of the asset may be performed by the auditor;

- Preparing financial statements based on information in the client-approved trial balance.

We recommend deleting this example. We consider that aggregating items from the trial balance may be a mechanical process by itself in filling in the balance sheet or statement of comprehensive income, however, writing up the notes to the financial statements is a more complicated process that involves the exercise of judgement to determine how best to describe events. We consider that including this as an example of a routine and mechanical service contradicts the example of management responsibilities which includes assuming the responsibility for the preparation of the financial statements. We consider that auditing financial statements compiled by the auditor should be prohibited as there are not sufficient safeguards that can be put in place to reduce the threat to independence of auditing one’s own work. If retained we would recommend that this example should be more narrowly described as follows, “Aggregating the client approved trial balance as part of preparing the financial statements”.

8. Is the meaning and identification of source documents sufficiently clear, taking into account documents that may be generated by software?

Response:

The NZAuASB considers that the meaning of source documents is sufficiently clear. We presume that this does not cover the preparation of the trial balance.

Section 291

9. Do the changes proposed to Section 291, specifically the additional requirements to proposed paragraph 291.146, enhance the clarity of a management responsibility?

Response:

The NZAuASB is supportive of the proposed requirements in 291.146, which align with the equivalent changes to section 290. As recommended above, we would prefer that the prohibition on assuming management responsibilities be stated upfront. We therefore recommend reordering the paragraphs in section 291 consistently with our response to question 6.

10. Are the examples of management responsibilities in paragraph 291.144 appropriate?

Response:

Yes, the NZAuASB considers that these examples, which align with the examples in section 290 are appropriate.

11. Does the relocation of the guidance pertaining to administrative services provide greater clarity?

Response:

Yes, the NZAuASB considers that this does provide greater clarity. As detailed above, the management responsibilities section now relates more specifically to decision making, and administrative services is dealt with as its own class of service, isolating out routine and mechanical tasks from the decision making functions.

General comments

Effective date – The IESBA proposes that the effective date for the changes will not be less than 12 months after issuance of the final changes. Earlier application would be permitted. The IESBA welcomes comment on whether this minimum period would be sufficient to support effective implementation of the changes.

Response:

Yes, we consider that a minimum period of not less than 12 months after issuance of the final changes is appropriate.