

# Proposed application material relating to professional scepticism and professional judgement

An exposure draft issued for public consultation by the International Ethics Standards Board for Accountants (IESBA)

## Joint submission by Chartered Accountants Australia and New Zealand and the Association of Chartered Certified Accountants

July 2017

ACCA (the Association of Chartered certified Accountants) and CA ANZ (Chartered Accountants Australia and New Zealand) created their strategic alliance in June 2016, forming one of the largest accounting alliances in the world. It represents 800,000 current and next generation accounting professionals across 180 countries and provides a full range of accounting qualifications to students and business. Together, ACCA and CA ANZ represent the voice of their members and students, sharing a commitment to uphold the highest ethical, professional and technical standards.

### Liz Stamford

Head of Policy  
Chartered Accountants Australia and New Zealand  
[liz.stamford@charteredaccountantsanz.com](mailto:liz.stamford@charteredaccountantsanz.com)  
+61 (0)2 8078 5426

### Nicola Hankinson

Senior Policy Advisor  
Chartered Accountants Australia and New Zealand  
[nicola.hankinson@charteredaccountantsanz.com](mailto:nicola.hankinson@charteredaccountantsanz.com)  
+64 (4) 917 4802

### Sundeep Takwani

Director – Regulation  
ACCA  
[sundeep.takwani@accaglobal.com](mailto:sundeep.takwani@accaglobal.com)  
+ 44 (0)207 059 5877

### Ian Waters

Head of Standards  
ACCA  
[ian.waters@accaglobal.com](mailto:ian.waters@accaglobal.com)  
+ 44 (0)207 059 5992



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

## About ACCA

ACCA is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people around the world who seek a rewarding career in accountancy, finance and management.

ACCA supports its 198,000 members and 486,000 students in 180 countries, helping them to develop successful careers in accounting and business, with the skills required by employers. ACCA works through a network of 101 offices and centres and more than 7,200 Approved Employers worldwide, who provide high standards of employee learning and development. Through its public interest remit, ACCA promotes appropriate regulation of accounting and conducts relevant research to ensure accountancy continues to grow in reputation and influence.

The expertise of our senior members and in-house technical experts allows ACCA to provide informed opinion on a range of financial, regulatory, public sector and business areas, including: taxation (business and personal); small business; audit; pensions; education; corporate governance and corporate social responsibility.

[www.accaglobal.com](http://www.accaglobal.com)

## About CA ANZ

CA ANZ is a professional body comprised of over 117,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgement, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations. We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member 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.

[www.charteredaccountantsanz.com](http://www.charteredaccountantsanz.com)



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

## GENERAL COMMENTS

---

### Introduction

ACCA and CA ANZ welcome the opportunity to comment on the proposals, and we welcome the direction of the project, which seeks to determine a relationship between compliance with the fundamental principles and the exercise of professional scepticism. The exercise of professional scepticism is required by International Standards on Auditing, and defined in ISA 200.<sup>1</sup> We would not seek to amend that definition, but would welcome measures to assist professional accountants to exercise professional scepticism effectively.

By way of example, we attach to this consultation response ACCA's research report *Banishing bias? Audit, objectivity and the value of professional scepticism*. We consider that the inclusion of the product of academic research within the Code's application material (as suggested in paragraph 6 of the Appendix) would make the guidance too technical and detailed, and would impact its understandability. Our view is that application guidance should, wherever possible, include 'real-world' examples to assist practitioners in applying the concepts.

### Objectivity and independence

In the Code, professional scepticism is considered only in relation to independence, and it should be understood that independence is very different to the fundamental ethical principle of objectivity. The latter gives rise to decision-making that recognises possible bias, which must be addressed in order to safeguard the professional accountant's objectivity; the former comprises both independence of mind and independence of appearance. The definition of independence refers to professional scepticism and objectivity as separate things;<sup>2</sup> professional scepticism goes beyond taking an objective view, and requires appropriate questioning and challenge; independence helps in the exercise of professional scepticism and being seen to exercise it.

### Relationship between the fundamental principles and professional scepticism

We agree with the suggestion that 'proper application of, and compliance with, the provisions in the Code might also contribute to enhancing the exercise of professional skepticism'<sup>3</sup>, and recognise the advantages of including guidance in the Code to explain how

---

<sup>1</sup> ISA 200 defines professional scepticism as 'an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence'.

<sup>2</sup> The Code defines independence as:

- (a) Independence of mind - the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgement, thereby allowing an individual to act with integrity, and exercise objectivity and professional scepticism
- (b) Independence in appearance - the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit or assurance team's, integrity, objectivity or professional scepticism has been compromised.

<sup>3</sup> May 2017 exposure draft, page 7



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

compliance with the fundamental principles supports the exercise of professional scepticism in the context of audit, review and other assurance engagements. However, this does not lead logically to the statement that '[t]he drivers and impediments to compliance with the fundamental principles and to the exercise of professional skepticism are the same'<sup>4</sup>. Impediments (or threats) to compliance with the fundamental principles are usually identifiable, whereas cognitive bias (which impedes appropriate professional scepticism) often is not.

### **Extending the concept of professional scepticism**

We note the intention of the IESBA to address the question of whether the concept of professional scepticism should apply to professional accountants other than assurance practitioners. Although not considered within the four specific questions below, we believe the time to address this question is now – within the context of the wider discussion of professional scepticism.

Care should be taken to avoid unintended consequences, and we would be concerned if all professional accountants were required to exercise professional scepticism in exactly the same way as those performing audit and other assurance engagements. This would damage relationships between professional accountants and their clients or employers, and stifle innovation, while providing no identifiable benefit to business. It could, in fact, serve as a barrier to employing or engaging professional accountants.

Our response to this exposure draft is provided with the interests of the public paramount. The public interest is served by the ability of auditors and others, who must be perceived as independent, being able to exercise professional scepticism effectively. It is also served by businesses (and other entities) having access to talented, ethical professional accountants who are competent to serve their clients and employers well. There is no doubt that professional scepticism is often important in the context of a particular non-assurance assignment. However, 'professional scepticism' means different things in different contexts.

For example, a professional accountant in business might be expected to exercise professional scepticism more rigorously in the context of an in-depth internal audit than when he or she routinely receives valuations from other parts of the organisation for incorporation into the monthly management information. An example in respect of a professional accountant in practice would be where the professional accountant is examining, on behalf of his or her client, the evidence underlying assertions made about the value of the business. The requirement for rigorous professional scepticism arises out of the nature of the engagement, and addresses the potential for bias within the assertions made by the vendor to the client.

This view is not inconsistent with that expressed by representatives of the PIOB, ie that 'the concept of professional skepticism is relevant to all professional accountants and that it is in the public interest that guidance on professional skepticism be made available to all professional accountants'.<sup>5</sup> However, that guidance must be tailored to a wide range of

---

<sup>4</sup> May 2017 exposure draft, page 7

<sup>5</sup> May 2017 exposure draft, page 11



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

users. Simply extending the concept of professional scepticism as applied in assurance engagements to all areas of a professional accountant's work would, at best, threaten clarity of the Code. We also believe that it would undermine the value of the concept for assurance practitioners, which is contrary to the objectives of the current exposure draft.<sup>6</sup> We suggest that an assignment that does not meet the definition of an assurance engagement requires the exercise of professional scepticism where there is the potential for bias in the production of data being evaluated or used by the professional accountant.

More widely, the fundamental principle of integrity requires the professional accountant to not knowingly be associated with statements of information furnished recklessly, and the principle of professional competence and due care requires the professional accountant to not act recklessly when providing professional services. But the principle of professional competence and due care focuses, to a great extent, on providing a quality service 'in accordance with the requirements of an assignment'.<sup>7</sup> For a non-assurance assignment, there is often a lesser call for professional scepticism, although we acknowledge that the professional accountant must be alert to indications that the fundamental principle of integrity is being threatened. In order to be alert to such indicators, it will be necessary to have an effective understanding of the environment in which the assignment is taking place, including the possibility of bias. This understanding, in fact, provides the necessary context in which to exercise professional judgement throughout the assignment.

We suggest that the IESBA should not dismiss the possibility of using an alternative to 'professional scepticism' to describe the questioning mindset that will often be appropriate for any professional accountant. We accept that 'critical mindset' may not be the appropriate expression.<sup>8</sup> However, it may provide greater clarity to the Code if it were to include an explanation of the circumstances in which a professional accountant is required to exercise a critical examination of the data and explanations provided to him or her.

## Summary

We believe that professional scepticism requires active challenge in the context of an assurance engagement. However, for some other assignments, the professional accountant is only required to challenge information provided by a client or employer when the professional accountant has cause to doubt the integrity of the information (or where the nature of the assignment is to exercise due scepticism on behalf of the client or employer). In order to be able to make that judgement, the professional accountant will require sufficient understanding of the relevant facts and circumstances surrounding the assignment. This might usefully be the subject of new application material within the Code.

---

<sup>6</sup> This appears consistent with the statement on page 12 of the exposure draft, which states that the IESBA's preliminary discussions 'have identified a number of concerns about a potential for dilution of the meaning and importance of professional scepticism in the audit and assurance context if its applicability were to be extended beyond audit and assurance'.

<sup>7</sup> Code of Ethics for Professional Accountants, paragraph 130.4

<sup>8</sup> May 2017 exposure draft, page 8



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

## AREAS FOR SPECIFIC COMMENT:

---

In this section, we set out our responses to the request for specific comments set out on page 10 of the consultation document.

### *Professional scepticism*

#### **Question 1: Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?**

We consider that the objective of this project is not expressed consistently throughout the consultation document. With regard to professional scepticism, we see the project as seeking to determine a relationship between compliance with the fundamental principles and the exercise of professional scepticism. Therefore, the focus of this question on 'understandability of the conceptual framework' seems wrong. Nevertheless, we see value in explaining how the conceptual framework assists the professional accountant in exercising professional scepticism, and being seen to do so.

Preceding the proposed application material is a statement in the restructured Code that '[t]he categories of threats to compliance with the fundamental principles described in paragraph 120.6 A3 are also the categories of threats to compliance with independence'. This does not acknowledge that independence is very different to objectivity. As stated above, the former comprises both independence of mind and independence of appearance. The fundamental principles of objectivity, and professional competence and due care combine to provide independence of mind, and so support the exercise of professional scepticism. The exercise of professional scepticism, in turn, provides independence of appearance, rather than vice versa.

Despite this criticism, we support the inclusion of paragraph 120.13 A1, together with the highlighting of the most relevant fundamental principles – integrity, objectivity and professional competence and due care (subject to our comments under question 2 below). We believe there should be a clear cross-reference to this application material from the International Independence Standards (IISs) if the application material is not to be restated in the IISs in full. Although we strongly advocate conciseness in the Code, repetition of this material in the IISs would be reasonable given that the IISs are standards, and so are of a different nature to the Code itself.

#### **Question 2: Do the examples in the proposed application material clearly describe how compliance with the fundamental principles of integrity, objectivity, and professional competence and due care support the exercise of professional scepticism in the context of an audit of financial statements? If not, why not?**

We support the inclusion of paragraph 120.13 A1, together with the highlighting of the most relevant fundamental principles. It must be clear, within this part of section 120, that the application material applies only to audits, reviews and other assurance engagements. With



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

this in mind, we have the following observations in respect of each of the fundamental principles considered:

**Integrity** – Integrity requires professional scepticism to be exercised honestly and fairly, and so compliance with this fundamental principle will help the professional accountant to respond appropriately to occasions on which evidence provided by a client should be questioned or challenged. This is not always easy, but we would question whether the introduction of requirements or application material into the Code would make it any easier. We believe that the explanation under ‘integrity’ would fit better under ‘professional judgement’ than under ‘professional scepticism’, which relies more on strict objectivity and competence in knowing when and how to challenge information provided.

**Objectivity** – The first sentence of this paragraph mentions both threats to objectivity and the recognition of a risk of bias. But bias may exist without it being recognised, and so there will not be any perceived threat to the principle of objectivity. We also see no reason to mention previous involvement with a client specifically as a threat to objectivity. The main issue is that bias is often difficult to recognise, but it may be made easier by safeguarding one’s objectivity. We suggest this paragraph be reworded and rearranged to read as follows:

*‘Self-awareness of the accountant’s own bias when considering evidence relating to a matter material to the audit of the client’s financial statements is necessary in identifying any additional steps to take to evaluate relevant evidence. In this way, the professional accountant exercises, and is seen to exercise an appropriate level of professional skepticism. Assessing the impact of personal bias will be more effective if the fundamental principle of objectivity is adequately safeguarded. This will require acknowledgement that personal bias may be a threat to objectivity. Bias may arise due to many factors, including the professional accountant’s familiarity with the client.’*

**Professional competence and due care** – In our opinion, this is the most important of the fundamental principles in its support of professional scepticism. We support the text of the proposed application material in this area. However, it could be extended to state specifically that due professional scepticism is threatened by the professional accountant’s personal bias, and he or she should attain the required professional competence to be able to identify and assess the impact of such bias.

### *Professional judgement*

### **Question 3: Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?**

It is not clear that the purpose of the application material is to enhance ‘the understandability of the conceptual framework’, as the purpose of the framework and the elements of its application are clear, and the requirements of the professional accountant remain clear so long as the Code remains concise and is written in plain language. Rather, the purpose of the application material is to help the professional accountant to apply the conceptual framework more effectively – highlighting areas to consider in exercising the necessary



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)

professional judgement. Subject to our comments under question 4 below, we believe that the inclusion of clear application material would be useful.

**Question 4: Do respondents agree that the proposed application material appropriately emphasises the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgement in applying the conceptual framework? If not, why not?**

We believe it is undesirable to simply extend the requirement for professional scepticism, as applied in audit and assurance engagements, to all professional accountants. The requirement for independence attaches to assurance engagements, whereas professional accountants in business and those undertaking non-assurance engagements are expected to act in the best interests of their clients or employers, subject always to compliance with the fundamental principles (including objectivity and integrity). However, we support the proposal to include application material that seeks to improve the understanding of the professional accountant when required to exercise professional judgement. Gaining an understanding of the client's (or employer's) business, and the environment in which it operates, would be expected in accordance with the fundamental principle of professional competence and due care. Therefore, the objective of the application material should be to highlight the importance of the professional accountant ensuring that his or her knowledge of the 'facts and circumstances' is *sufficient*.

We consider the tone of proposed paragraph 120.5 A1 is inappropriate for application material, as it appears somewhat prescriptive. Nevertheless, the guidance it provides is useful. We suggest removing the first sentence, but including the reference to professional judgement in the second sentence with regard to evaluating and addressing threats to compliance. The examples of matters the professional accountant might consider should be clearly related to application of the conceptual framework, which is the focus of this proposed application material. Without this focus, there is a risk that the professional accountant's obligation of due care to his or her client or employer will be overlooked.

We question why the format of the proposed application material in paragraph 120.5 A1 does not follow the same format as paragraph 120.13 A1, and so relate the fundamental principles to the professional accountant's ability to apply professional judgement effectively. We believe it would be useful for the application material to explain how the fundamental principle of objectivity applies when exercising professional judgement. Better awareness of the need for objectivity by all professional accountants, at all times, is possible without compromising the professional accountant's ability to serve a commercial employer or client. With this aim in mind, it is important for the professional accountant to be aware of cognitive bias, and to aim to mitigate the impact of bias on his or her professional judgement. Although bias cannot be eliminated entirely, standard-setters should always be aware of how cognitive bias can impact the professional accountant in many circumstances.



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)



## Request for general comments

### *Small and Medium Practices (SMPs):*

A large proportion of members of ACCA and CA ANZ practise within SMPs. We believe the objectives of this project are particularly relevant to such practitioners, for whom clear, succinct guidance is highly valued, given the limited resources in such practices.

### *Regulators and audit oversight bodies:*

Although we are not in favour of prescriptive documentation requirements, a clear focus on the intended outcomes of the conceptual framework approach to resolving ethical dilemmas would support the work of regulators, and encourage documentation by professional accountants.

### *Developing nations:*

We are not aware of any difficulties that would be encountered by developing nations in particular, as a result of introducing appropriate application material.

### *Translations:*

Section III of the consultation document considers the overall impact of the proposed changes on costs to be insignificant, as the proposed application material would simply clarify what is already implicit in the Code. However, this raises the question of whether the proposed changes are, in fact, necessary. In terms of compliance costs, we would agree with the IESBA's assessment. However, it appears that translation costs have been disregarded, which suggests that the costs of implementing the proposed changes could outweigh the benefits.



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)



33 Erskine Street, Sydney NSW 2000  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



Think Ahead

The Adelphi 1/11 John Adam Street London WC2N 6AU  
United Kingdom  
T +44 (0)20 7059 5000 E [info@accaglobal.com](mailto:info@accaglobal.com)

[accaglobal.com](http://accaglobal.com)