



4 May 2020

File Ref: OW/XGF/2-0004
AU/APS/6-0012

The International Ethics Standards Board for Accountants
545 Fifth Avenue, 14th Floor
New York, 10017
United States of America

Dear Members of the International Ethics Standards Board for Accountants

EXPOSURE DRAFT – PROPOSED REVISIONS TO THE NON-ASSURANCE SERVICES PROVISIONS OF THE CODE

Thank you for the opportunity to provide comments on the International Ethics Standards Board for Accountants (IESBA) Exposure Draft – *Proposed Revisions to the Non-Assurance Services Provisions of the Code* (the Exposure Draft).

The Auditor-General of New Zealand (the Auditor-General) has a particular responsibility to assist the New Zealand parliament to hold the government to account. That responsibility is set out in legislation – the Public Audit Act 2001 (the Act). This response reflects the Auditor-General's perspective on the questions listed in the Explanatory Memorandum dated January 2020, based on the requirements of the Act.

Our overall observation is that the proposed changes do not go far enough, although they are heading in the right direction.

Appendix 1 to our submission provides responses to the questions on which the IESBA has sought comment.

If you have any questions about our submission, please contact Roy Glass (roy.glass@oag.parliament.nz) or me.

Yours sincerely

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Appendix 1 – Response to matters on which the IESBA has sought comments

Request for specific comments

Prohibition on NAS that will create a self-review threat for PIEs

1. *Do you support the proposal to establish a self-review threat prohibition in proposed paragraph R600.14?*

Non-assurance services can simultaneously create self-interest, self-review and advocacy threats to independence. Those who rely on the independent auditor's report are unlikely to make a distinction between the different types of independence threat. As a consequence the proposal appears to be somewhat academic from the perspective of the "reasonable and informed third party" if the proposal is limited self-review threats in respect of non-assurance services.

Furthermore, almost every non-assurance service will contain an element of self-review threat.

Does the proposal only apply to those services where the auditor makes an assessment that the **predominant** threat is self-interest? If so, the proposal lends itself to abuse because of the commercial incentive to downplay the self-interest component of the threat to independence and to elevate the other threats as a justification for accepting the non-assurance service engagement.

In addition, we have a philosophical issue about the application of different independence requirements to public interest entities vs non-public interest entities. This is because the criteria that is used to distinguish public interest entities from non-public interest entities is arbitrary from an audit independence perspective. We acknowledge, in the case of some very small entities that we regard as "micro-entities", that public accountability is enhanced if auditors can carry out a small number of non-assurance services that create what we would consider to be an acceptable self-review threat. An example of this type of non-assurance service is the compilation of simple cash-based financial statements that are derived from the entity's trial balance or underlying records.

2. *Does the proposed application material in 600.11 A2 set out clearly the thought process to be undertaken when considering whether the provision of a NAS to an audit client will create a self-review threat? If not, what other factors should be considered?*

In our response to question 1 we note that:

- a self-review threat will be present to some extent whenever an auditor provides a non-assurance service; and
- a reasonable and informed third party is unlikely to distinguish a self-review threat and a self-interest or advocacy threat.

In our opinion, this makes the proposed requirement somewhat ineffective and difficult to operationalise.

In addition, the thought process described in 600.11 A2 concentrates on the objective aspects of "independence of mind" and ignores the more challenging "independence in appearance" aspect of independence. In other words, even if the considerations in 600.11 A2 are not present, a non-assurance service could present a significant threat to independence in appearance under the reasonable and informed third party test.

Providing Advice and Recommendations

3. *Is the proposed application material relating to providing advice and recommendations in proposed paragraph 600.12 A1, including with respect to tax advisory and tax planning in proposed paragraph 604.12 A2, sufficiently clear and appropriate, or is additional application material needed?*

The pre-conditions that allow tax advisory and tax planning to be carried out under the Code, as described in 604.12 A2, do not generally exist in New Zealand. A consequence of this situation is that tax advisory and tax planning engagements present an unacceptable threat to independence in the context of audits for which the Auditor-General has responsibility and are not permitted under the Auditor-General's independence requirements.

Paragraph 604.12 A2 is not prominent and its implications can be easily overlooked, particularly when auditors have been providing tax advisory and tax planning services to the entities they audit for many years. The implications of 604.12 A2 could be made more prominent to give proper effect to the Code.

Project on Definitions of Listed Entity and PIE

4. *Having regard to the material in section I, D, "Project on Definitions of Listed Entity and PIE," and the planned scope and approach set out in the approved project proposal, please share your views about what you believe the IESBA should consider in undertaking its project to review the definition of a PIE.*

As noted in our response to question 1, we have a philosophical issue about the application of different independence requirements to public interest entities vs non-public interest entities. This is because the criteria that is used to distinguish public interest entities from non-public interest entities is arbitrary from an audit independence perspective. We acknowledge, in the case of some very small entities that we regard as "micro-entities", that public accountability is enhanced if auditors can carry out a small number of non-assurance services that create what we would consider to be an acceptable self-review threat. An example of this type of non-assurance service is the compilation of simple cash-based financial statements that are derived from the entity's trial balance or underlying records.

Although we are not advocating a distinction between "important" and "less important" entities from an independence perspective, if such a distinction is considered desirable one way of separating such entities is to apply the PIE requirements to listed entities, as described in ISA 701.

Materiality

5. *Do you support the IESBA's proposals relating to materiality, including the proposal to withdraw the materiality qualifier in relation to certain NAS prohibitions for audit clients that are PIEs (see Section III, B "Materiality")?*

We support the proposals relating to materiality, but believe they should be extended to apply to all NAS and to all entities subject to audit.

6. *Do you support the proposal to prohibit the following NAS for all audit clients, irrespective of materiality:*
 - *Tax planning and tax advisory services provided to an audit client when the effectiveness of the tax advice is dependent on a particular accounting treatment or presentation and the audit team has doubt about the appropriateness of that treatment or presentation (see proposed paragraph R604.13)?*
 - *Corporate finance services provided to an audit client when the effectiveness of such advice depends on a particular accounting treatment or presentation and the audit team has doubt about the appropriateness of that treatment or presentation (see proposed paragraph R610.6)?*

We support the proposals relating to materiality, but believe they should be extended to apply to all NAS and to all entities subject to audit.

Communication with TCWG

7. *Do you support the proposals for improved firm communication with TCWG (see proposed paragraphs R600.18 to 600.19 A1), including the requirement to obtain concurrence from TCWG for the provision of a NAS to an audit client that is a PIE (see proposed paragraph R600.19)?*

We support the proposal to communicate with TCWG in advance of accepting a NAS. However, this proposal needs to make it very clear that the concurrence of TCWG can **only** be sought if the auditor has concluded that the NAS is permitted under the Code. We are concerned that this provision might be used as a mechanism whereby TCWG provide a “waiver” to the auditor from complying with the Code.

Other Proposed Revisions to General NAS Provisions

8. *Do you support the proposal to move the provisions relating to assuming management responsibility from Section 600 to Section 400, and from Section 950 to Section 900?*

We support this proposal.

9. *Do you support the proposal to elevate the extant application material relating to the provision of multiple NAS to the same audit client to a requirement (see proposed paragraph R600.10)? Is the related application material in paragraph 600.10 A1 helpful to implement the new requirement?*

We support this proposal.

Proposed Revisions to Subsections

10. *Do you support the proposed revisions to subsections 601 to 610, including:*

The concluding paragraph relating to the provision of services that are “routine or mechanical” in proposed paragraph 601.4 A1?

We do not agree with the examples of routine and mechanical accounting and bookkeeping services described in paragraph 601.4 A1, apart from the final bullet point (in respect of simple financial statements). In our view, the provision of such services present an unacceptable threat to independence.

Where such services are provided it is essential that the auditor does not assume a management responsibility. We therefore support the concluding paragraph relating to the provision of services that are “routine or mechanical” in proposed paragraph 601.4 A1.

The withdrawal of the exemption in extant paragraph R601.7 that permits firms and network firms to provide accounting and bookkeeping services for divisions and related entities of a PIE if certain conditions are met?

We support the proposal to withdraw the exemption in extant paragraph R601.7

The prohibition on the provision of a tax service or recommending a tax transaction if the service or transaction relates to marketing, planning or opining in favour of a tax treatment, and a significant purpose of the tax treatment or transaction is tax avoidance (see proposed paragraph R604.4)?

We support the proposal to prohibit services that are intended to avoid tax.

The new provisions relating to acting as a witness in subsection 607, including the new prohibition relating to acting as an expert witness in proposed paragraph R607.6?

We consider that the provision of litigation support services present an unacceptable threat to independence and should be prohibited entirely.

Proposed Consequential Amendments

11. *Do you support the proposed consequential amendments to Section 950?*

The Auditor-General of New Zealand does not recognise Part 4B of the Code (including Section 950) because we apply the more stringent requirements in Part 4A of the Code to all the work of the Auditor-General. We have no comments to make about the proposed consequential amendments to Section 950.

12. *Are there any other sections of the Code that warrant a conforming change as a result of the NAS project?*

We are not aware of any other sections of the Code that warrant a conforming change as a result of the NAS project.

Request for General Comments

Small- and Medium-Sized Entities (SMEs) and Small and Medium Practices (SMPs) – *The IESBA invites comments regarding any aspect of the proposals from SMEs and SMPs.*

New Zealand is a small country with a population of less than 5 million people. New Zealand is dominated by SMPs, and our responses to the questions raised by the IESBA reflect a SMP perspective.

Developing Nations – *Recognizing that many developing nations have adopted or are in the process of adopting the Code, the IESBA invites respondents from these nations to comment on the proposals, and in particular on any foreseeable difficulties in applying them in their environment.*

Developing nations face difficulties in applying the requirements of the Code when both auditing and financial reporting expertise is in short supply.

Translations – *Recognizing that many respondents may intend to translate the final changes for adoption in their own environments, the IESBA welcomes comment on potential translation issues respondents may note in reviewing the proposals.*

We have no comments to make on potential translation issues.