

Six monthly review of APES 110 Code of Ethics for Professional Accountants issued in June 2006

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1. Executive Summary

1.1. Background

The Accounting Professional and Ethical Standards Board (APESB) issued APES 110 *Code of Ethics for Professional Accountants* in June 2006 with an effective date of 01 July 2006. The exposure period for this standard was limited due to the necessity of introducing this standard by 01 July 2006 to be in line with the force of law auditing standards issued by the Auditing and Assurance Standards Board (AUASB).

1.2. Reason for this report

In accordance with the constitution of the APESB, a review needs to be performed six months after an issue of a new standard. This report presents a review of the issues identified and a proposed course of action to address them.

1.3. Issues identified

The issues identified since issue of the standard are summarised below:

- 1 Use of footnoting of the code to identify the corresponding reference/section in the *Corporations Act*.
- 2 Use of terminology “Financial Statement Audit Client”.
- 3 Use of terminology “Financial Statement” rather than “Financial Report”.
- 4 Communication between an audit firm and the audit committee
- 5 The International Ethics Standards Board for Accountants (IESBA) has issued an exposure draft of Section 290 (and proposed new Section 291) of the code which now incorporates a definition of a network firm.
- 6 Lack of statement of conformity with the applicable International Standard
- 7 Use of terminology “Professional Services” rather than “Public Accountancy Services”.
- 8 Formatting error of heading in paragraph 290.170 of the code
- 9 The development of guidance notes for matters relating to issues included in the previous joint code of conduct but not included in the new code.
- 10 Development of a new standard for the previous Professional Statement F 2: *Prospectus and reports on Profit Forecasts*

1.4. Summary of Recommendations

The following is a list of the recommendations contained in the main report. It is recommended that:

1. Issues raised in respect of cross referencing the Code to the *Corporations Act*, either by members, firms or regulatory bodies be monitored and to revisit this issue during the 12 month review of the Code.
2. The terminology be updated later in the year along with the revision of Section 290 and 291.
3. As the term Financial Report is defined in the AUASB glossary and is broadly consistent with the definition of financial statements in the code no further action is required.
4. Due to the proposed international changes to the Code, it is no longer appropriate to limit the communication with the audit committee to financial statement audit clients. Thus no further action is proposed in this regard.
5. The APESB issues an exposure draft in respect of the revised S.290 issued by the IESBA in June 2006 and invite comments, to evaluate the need to issue Australian guidance on what business and operating arrangements between firms would be considered to be a network.
6. In the next version of APES 110 include a Statement of conformity with the IFAC Code of Ethics for Professional Accountants
7. APESB Board to consider whether the wording noted above is appropriate and consider amending the definition of Professional Services in the next revision of the Code.
8. Amend the formatting error in the header of S.290 in the next issue of the standard.
9. A summary of issues that require further guidance will be provided to the APESB by the ICAA.
10. In terms of Professional Statement F 2: *Prospectus and reports on Profit Forecasts* the need for a new standard addressing these issues have been recognized and it has been added to the APESB work program.

1. Review of Implementation Issues

2.1 Draft footnoting of the code to identify the corresponding reference/section in the Corporations Act.

Issue

At the time of issuing the standard the APESB considered the need to footnote the code to identify the corresponding reference/section to the *Corporations Act*. However, it was expected that stakeholders will comment on this issue and the Board decided to revisit this issue in the future.

Analysis of the issue

As the code currently stands, no cross references have been provided against the *Corporations Act*. ASIC has raised a few issues in respect of consistency of terminology between the code and the *Corporations Act*. However, the examples given to date are not significant. Previously the RDG Independent Task Force also has noted this as a potential issue.

During the post implementation period, members of the ICAA has not raised any concerns or requested a mechanism to cross reference the code with the *Corporations Act*.

Impacted Stakeholders

Professional Accountants, Auditors and regulatory bodies

Recommendation

It is recommended that issues raised in this context either by members, firms or regulatory bodies be monitored and to revisit this issue during the 12 month review of the Code.

2.2 Use of terminology “Financial Statement Audit Client”

Issue

The Board has been advised that the International Ethics Standards Board for Accountants (IESBA) is considering a change in the use of this terminology, and resolved to monitor this issue with a view to reconsidering it in the future, for possible adoption in APES 110.

Analysis of the issue

In the redraft of Section 290 and 291, the IESBA has removed the definition of the term “Financial Statement audit client” and has included a definition of “audit client”. Thus the IESBA appear to have redrafted the code in such a way that there is no longer the need to distinguish between a “Financial Statement audit client” and another form of “audit client”.

Stakeholders

Auditors and professional accountants.

Recommendation

It is recommended that this terminology be updated later in the year when Section.290 & 291 of the Code is being revised.

2.3 Use of terminology “Financial Statement” rather than “Financial Report”.

Issue

The Board had resolved to use the terminology “financial statement” because it was a term defined in the IFAC Code, rather than the term used in the Australian auditing standards, “financial report”, which was undefined. The Board also resolved to reconsider this issue at a future time.

Analysis of the issue

The code (APES 110) defines “Financial Statement” as follows:

“The balance sheets, income statements or profit and loss accounts, statements of changes in financial position (which may be presented in a variety of ways, for example, as a statement of cash flows or a statement of fund flows), notes and other statements and explanatory material which are identified as being part of the financial statements”

The AUASB Glossary does have a definition and it defines “Financial Report” as follows:

“ Means a structured representation of the financial information, which ordinarily includes accompanying notes, derived from accounting records and intended to communicate an entity’s economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial framework. The term may refer to a complete financial report, but in some jurisdictions, it may also refer to a single financial statement, for example, a balance sheet, or a statement of revenues and expenses, and related explanatory notes. The requirements of the financial reporting framework determine the form and the content of the financial report and what constitutes a complete financial report. A financial report, as defined under sections 295 and 303 of the Corporations Act 2001 and Accounting Standard AASB 101 Presentation of Financial statements, consists of financial statements for the year and half year respectively, notes to the financial statements and the director’s declaration about the statements and the notes”.

The AUASB definition is broader and incorporates the requirements of the *Corporations Act* as well. However, on an overall basis the definitions are not inconsistent with each other.

Stakeholders

Auditors and professional accountants.

Recommendation

As the term “Financial Report” has been defined in the AUASB Glossary and the definition is consistent with the definition of “Financial Statement” in the code, no further action is proposed in respect of this issue.

2.4 Communication between an audit firm and the audit committee

Issue

Deloitte submission on the exposure draft recommended that S.290.29 be amended to make it clear that the obligation to communicate with the audit committee under the *Corporations Act* and the code rests solely when a firm conducts financial statement audits engagements of listed companies, registered schemes and disclosing entities.

Analysis of issue

S.290.29 states that audit committees can have an important corporate governance role and that there should be regular communication between the audit committee and the firm performing the audit role regarding relationships and other matters that might have a bearing on independence. The Australian guidance then expands it to include disclosing entities and registered schemes.

Based on discussions held by the APESB with Deloitte, the issue raised in the submission is to limit the communication with the audit committee in respect of Financial Statement Audits of listed clients, disclosing entities and registered schemes.

The proposal to limit the communication to financial statement audits of listed clients is not appropriate, as in certain instances an audit firm will conduct audit engagements for listed clients which are not financial statement audits. For example audits of specific items in the financial statements which may require sign off for a regulatory purpose or an audit of internal controls.

Further, based on the new developments of Section 290 and Section 291 (discussed in issue 2.2) whereby the new proposed code only defines audit clients the proposed limitation may no longer be appropriate.

Stakeholders

Professional Accounting firms and audit clients.

Recommendation

Based on the discussion above no further action is proposed in this regard.

2.5 The International Ethics Standards Board for Accountants (IESBA) has re-issued Section 290 of the code which now incorporates a definition of a network firm.

Issue

Section 290 of the *Code of Ethics for Professional Accountants* was revised by the IESBA in July 2006. The main change is the inclusion of paragraphs S. 290.14 to S. 290.26 which defines and explains what would be considered to be networks and network firms. In line with this the definitions of a network and

network firms have also been amended. The effective date of the revised standard is for reports dated on or after December 31, 2008.

Analysis of issue

In respect of assurance engagements, it is imperative that the firm performing the assurance role and when applicable network firms, be independent of the assurance client. A network is defined as a larger structure that is aimed at co-operation and has one or more of the following elements:

- Profit or cost sharing
- Shares common ownership
- Shares control or management
- Common quality control policies and procedures
- Common business strategy
- Use of common brand name
- Use of a significant part of professional resources

Professional accounting firms who perform assurance engagements and that have business/operating agreements or referral networks with other firms will need to evaluate the requirements of this standard and evaluate whether they will be deemed to be in a network. If the answer is affirmative then prior to accepting an assurance engagement the firm will need to ensure that the network of firms is independent of the prospective assurance client.

Stakeholders

Professional Accounting firms who are operating in a network or who may be deemed to be operating in a network under the guidelines issued by the new standard.

Recommendation

The Board needs to consider the following action item:

1. Issue an exposure draft in respect of the revised S.290 of the code and invite comments and then issue a revised version later in the year.

There is a necessity to issue this guidance as soon as possible as firms will need to review their business arrangements to determine whether they operate in a “network” and then introduce appropriate processes to check whether there are independence issues prior to accepting an assurance client.

The most appropriate course of action to follow would be to issue an exposure draft and invite comments, to evaluate the need to issue Australian guidance on what business or operating arrangements between firms would deem them to be operating in a network.

2.6 Statement of conformity with the applicable International Standard

Issue

APES 110 does not currently have a statement of conformity with its equivalent issued by the IESBA.

Analysis of issue

As a matter of best practice APES 110 should have a comparison paragraph comparing it to the international code.

Stakeholders

Professional Accountants.

Recommendation

It is recommended that the next revision of the standard incorporate a paragraph which compares APES 110 with the *Code of Ethics for Professional Accountants* issued by the IESBA.

2.7 Use of terminology “Professional Services” rather than “Public Accountancy Services”

Issue

The code has a definition of “professional services” which is from the IFAC code. The ICAA defines a concept of “Public Accountancy Services”. There are subtle differences and the ICAA has proposed that perhaps the code’s definition can be expanded by the addition of words such as “and other services as identified by a professional body that adopted this code as applicable to its members”.

Analysis of issue

Professional services are defined in the code in the following manner:

Services requiring accountancy or related skills performed by a professional accountant including accounting, auditing, taxation, management consulting and financial management services

ICAA defines Public Accountancy Services as follows:

Means accounting, auditing, management consulting, taxation, financial management and insolvency services as the Board may from time to time determine to be “public accountancy services”

Each of the professional bodies will have a definition that will be broadly similar to the definition included in the IFAC code. In order to ensure member compliance in the next revision of the code the definition of Professional Services could be extended to include wording such as “ *and other services as identified by a professional body that has adopted this code as applicable to its members*”.

Stakeholders

APESB and Members of the professional accounting bodies.

Recommendation

APES Board to consider whether the wording noted above is appropriate and consider amending the definition of Professional Services in the next revision of the Code.

2.8 Formatting error of heading in paragraph 290.170 of the code

Issue

The heading of paragraph 290.170 is in bold when it should be in italics.

Analysis of issue

No analysis requires as it is a formatting error.

Stakeholders

APESB

Recommendation

To be amended in the next version of the standard.

2.9 Other Matters

Detailed below are other matters that need to be addressed. These issues do not directly impact on APES 110, however, for completeness is presented in this review.

Issue	Proposed resolution
Issues included in the previous Joint Code of Professional Conduct such as advertising and practice names now not in the current Code of Ethics for Professional Accountants require further guidance	Paul Meredith, Manager Professional Standards, ICAA, will prepare a paper covering the issues and present it to the APESB for consideration.
Professional Statement F2 : <i>Prospectus and reports on Profit Forecasts</i>	The development of a standard in this regard has been included in the work program of the APESB.