

## AGENDA PAPER

**Item Number:** 10.3  
**Date of Meeting:** 10 May 2010  
**Subject:** Draft Exposure Draft ED 02/10 *Proposed Standard: APES 110 Code of Ethics for Professional Accountants*

**Action Required**

**For Information Only**

### Purpose

To seek feedback from the APES Board on Exposure Draft ED 02/10 *Proposed Standard: APES 110 Code of Ethics for Professional Accountants* and to seek direction on the outstanding drafting matters noted in this agenda paper.

### Background

At the May 2009 meeting, the Board approved a project to update APES 110 *Code of Ethics for Professional Accountants* to bring the requirements of APES 110 into alignment with the revisions made internationally by IESBA in July 2009 to its *Code of Ethics for Professional Accountants* (IESBA Code).

At the November 2009 meeting, the Board decided to issue a Consultation Paper seeking views of stakeholders on three key areas:

- Consideration of the IESBA Code in the Australian Context and application of APESB drafting conventions;
- Reference to Australian legislative requirements; and
- Structure of sections 290 and 291 of the IESBA Code.

At the March 2010 meeting, the Board considered responses to its Consultation Paper along with ten potential drafting approaches that could be used to update APES 110.

The Board instructed Technical Staff to draft an Exposure Draft applying the following drafting conventions:

- Change spelling from US to Australian English;
- Capitalise definitions;
- References to professional accountant to be changed to Member, Member in Public Practice or Member in Business as appropriate;
- Mandatory requirements and explanatory guidance will not be shown in separate paragraphs nor will bold or grey type be used to distinguish between mandatory requirements and explanatory guidance;

- Adopt IESBA definitions where possible with amendments or additions where these refer to Australian legislative requirements and Australian Auditing Standards;
- 2006 Board decisions which tailored the IESBA Code (2005) to the Australian environment be reconsidered and retained where there is sufficient justification to do so;
- A review of substantive matters be undertaken and that consideration be given to incorporating guidance to those issues identified as requiring further clarification; and
- A high level redraft of sections 290 and 291 be considered to determine the merit or otherwise of attempting to remove duplication of those sections.

At its April 2010 meeting the Board considered the structure of sections 290 and 291 of the IESBA Code and agreed that the format of sections 290 and 291 in the IESBA Code be retained in the revised APES 110.

The attached draft Exposure Draft ED 02/10 *Proposed Standard: APES 110 Code of Ethics for Professional Accountants* reflects the drafting decisions approved by the Board and identifies the outstanding matters for the Board's consideration.

#### Explanatory Guide to mark-ups

- The draft Exposure Draft 02/10 is a marked up version of the IESBA Code (July 2009) with editorial changes relating to 2006 Board Decisions highlighted in yellow.
- Obvious deletions are not shown in the mark-up (for example, capitalisation of a defined term or a spelling amendment). However, the associated insertion change is reflected with the amended text.
- Additional AUST paragraphs from the existing APES 110 are relocated next to the relevant IESBA paragraph and are highlighted in yellow.
- The definitions section highlights new IESBA defined terms in blue.
- Additional Australian definitions are included directly following IESBA definitions as AUST definitions.

### **Outstanding matters for the Board's consideration**

#### **1. Regulatory Concerns**

Refer Appendix A.

#### **2. Clarity of application of requirements in sections 290 and 291**

The introductory paragraphs of sections 290 and 291 explain the intended structure and application of each section. Section 290 of the IESBA Code has been designed to address independence requirements for audit engagements and review engagements, which are assurance engagements in which a Member in Public Practice expresses a conclusion on historical financial statements. Section 291 addresses independence requirements for assurance engagements that are not audit or review engagements of financial statements. Given that audit or review engagements of financial statements are a form of assurance engagements, section 291 is best described as being applicable to *Other Assurance Engagements* (Refer AUASB framework in Appendix D), which are not audit or review engagements of financial statements.

Aside from the introductory paragraphs, the principles to be applied in section 290 refer mainly to audit engagements whilst section 291 refers to assurance engagements. However, without reading the introductory paragraphs to section 290/291, it is not immediately evident that the requirements relate to only particular types of engagements. For example, after the first few

paragraphs of Section 290, the remainder of the paragraphs mainly refer to audit engagements when the requirements equally apply to review engagements. In the case of 291 it refers to assurance engagements which can be correctly construed to include audit and review engagements. Thus the demarcation of the different types of engagements is not clear unless you read the first few paragraphs of section 290/291.

From a clarity perspective, it would be beneficial to properly define the application of sections 290/291 in a manner that the engagements to which they apply are clear for members, firms, regulators (such as ASIC) and clients.

#### Linkages to AUASB pronouncements

Appendix 1 to the Foreword to AUASB Pronouncements distinguishes between the two types of assurance engagements – i.e. audits and reviews of historical financial information, and assurance engagements other than audits or reviews of historical financial information (refer Appendix D – Extract from Foreword to AUASB Pronouncements).

In October 2009 the Australian Auditing and Assurance Standards Board (AUASB) issued Auditing Standard ASA 102 *Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements*. ASA 102 is a legislative instrument made under the *Corporations Act 2001*. ASA 102 is operative for engagements with reporting periods commencing on or after 1 January 2010.

The definition of relevant ethical requirements in ASA 102 refers to APES 110. Accordingly, to ensure consistency between APES 110 and ASA 102, it would be preferable if defined terms and their associated requirements are used consistently.

The outstanding matter for the Board to consider is whether consistent use of terminology should be used throughout sections 290 and 291 or if full reliance on proper application can be placed on sections 290.1 to 290.3 and 291.1 to 291.3.

#### Technical Staff view

Technical Staff recommend that defined terms are applied more consistently throughout the Code including sections 290 and 291. In particular, the requirements of section 291 should be phrased as applying to Other Assurance Engagements (as per the AUASB Framework). An Australian definition of *Other Assurance Engagements* should be included and this term can be applied in 291 to clearly distinguish the requirements as applicable to *Other Assurance Engagements* as opposed to Assurance Engagements (which by definition include Audits or Reviews).

### **3. 2006 Decisions (including *Corporations Act 2001* matters)**

There are numerous editorial changes within the text of the previous IESBA Code that the APES Board made in 2006. These AUST paragraphs, where appropriate, have been carried forward in the attached Exposure Draft ED 02/10 and are highlighted throughout the draft Exposure Draft in yellow.

#### Technical Staff view

Technical Staff recommend that the 2006 AUST insertions/deletions be retained, modified or removed as outlined in the Appendix B – Overview of APESB 2006 Insertions and Appendix C – Overview of APES 2006 Removals.

**Technical Staff strongly recommend that the amendments made in 2006 in respect of the *Corporations Act* be retained.**

## Definitions

As instructed by the Board, technical staff have used the IESBA definitions as a starting point, overlaid with the 2006 Board Decisions and updated for subsequent changes as reflected in AUASB pronouncements, AUASB *Glossary*, and/or definitions used in APESB pronouncements such as APES 205 *Conformity with Accounting Standards*. Definitions have also been checked for consistency with the AASB *Glossary of Defined Terms* where applicable.

In summary, the Board amended the following definitions in 2006: Assurance Client; Assurance Team; Audit Engagement; Audit Team; Directors; Engagement Quality Control Review; Firm; Member in Public Practice. In 2006, the Board also added the following AUST definitions: Audit Review Partner; Clients; Engagement; Engagement Quality Control Reviewer; Lead Engagement Partner; Managerial Employee; Member; Officer; and Partner. The majority of amendments and additions were driven by Australian legislative requirements or references in Australian Auditing Standards.

### Technical Staff view

Technical Staff recommend:

- Amended defined terms are retained as drafted in Exposure Draft ED 02/10;
- The retention of the additional AUST definitions except for the following: Audit Review Partner; Engagement Quality Control Reviewer and Lead Engagement Partner. Technical Staff are of the view that the IESBA definition of Key Audit Partner acts as a suitable replacement for these previously defined terms.

### Public Interest Entity

The Board sought comments on the definition of public interest entity in the Consultation Paper CP 01/09 Proposed Revision of APES 110 *Code of Ethics for Professional Accountants*.

### Analysis of Respondents' Comments

The joint accounting bodies, EY, G100 (generally) supported the provision of guidance on the application of "public interest entity" in the Australian context. PwC suggested providing guidance outside the standard-setting process. GT (generally) preferred no change to the IESBA Code but noted any amendments could be made via AUST paragraphs. Deloitte and KPMG were opposed. AUASB's submission stated:

*"The AUASB uses IAASB defined terms in the Australian Auditing Standards, where applicable, tailoring them to the Australian environment and legislative framework, as required. The AUASB may add defined terms that are not defined internationally, where they are relevant in the Australian context, or delete IAASB defined terms that do not apply in Australia. Australian-specific differences are identified using the prefix "Aus"*

### Public Interest Entity

The IESBA Code defines Public Interest Entity as follows:

- (a) A Listed Entity; and
- (b) An entity (a) defined by regulation or legislation as a public interest entity or (b) for which the audit is required by regulation or legislation to be conducted in compliance with the same Independence requirements that apply to the audit of Listed Entities. Such regulation may be promulgated by any relevant regulator, including an audit regulator.

### Option 1 – Adopt IESBA definition

Allow Members in Australia to apply their professional judgement to determine if a potential client is a Public Interest Entity.

### Option 2 – Specify the types of entities that fall under limb (b) of the IESBA definition

In February 2010, the Australian Accounting Standards Board (AASB) issued Exposure Draft ED 192 *Revised Differential Reporting Framework* with a comment period up to 23 April 2010. Relevant extracts of ED 192 are attached in Appendix E. In particular we draw the Board's attention to paragraphs 18-21 which discuss the notion of a publicly accountable entity, paragraph 24 which defines public accountability and paragraphs 25-26 which provides further guidance in the Australian context.

For the purposes of limb (b) of the IESBA definition, an option for the Board to consider would be to specify that Tier 1 entities (as per the AASB's proposed differential reporting regime) would be regarded as Public Interest Entities. Technical Staff notes that this approach has been advocated by the New Zealand Professional Standards Board in their recently issued Exposure Draft of the NZ Code.

In effect those who will adopt the full requirements of IFRS will be entities subject to Tier 1 requirements under the proposed AASB differential reporting regime.

### Technical Staff view

As the AASB pronouncements have legislative authority in Australia, Technical Staff recommend Option 2.

## **5. Members in Business Issue – Preparation and Reporting of Information**

Section 320 of the IESBA Code requires a Member in Business who has responsibility to prepare or approve general purpose financial statements to be satisfied that those financial statements are prepared in accordance with an applicable financial reporting framework.

The issue that arises from these requirements relates to a Member in Business who is acting as a preparer of general purpose financial statements. There may be circumstances where a Member in Business who is a preparer has a different opinion to the Board of Directors who have ultimate authority to approve the general purpose financial statements. The Member in Business may be directed to present information in a way that conflicts with their judgement about what is "true and fair" in accordance with an applicable financial reporting framework. In such circumstances the obligation to comply with the Code should be specified in a manner that the Member in Business takes reasonable steps rather than imposing a mandatory obligation to ensure compliance with an applicable financial reporting framework.

### Technical Staff View

The requirements relating to the preparation of general purpose financial statements be clarified to indicate that a Member in Business shall take reasonable steps to ensure compliance with an applicable financial reporting framework.

## 6. Other Editorial Issue – “Shall” Obligations

There are numerous paragraphs in the IESBA Code where it is not clear on whom an obligation is imposed – refer specifically the following paragraphs: 140.8, 210.11, 210.12, 240.2, 240.4, 240.7, 290.11, 290.15, 290.24, 290.105, 290.107, 290.109, 290.113, 290.115, 290.124, 290.126, 290.129, 290.130 [*the remainder of sections 290 and 291 were not checked*], 320.5, 330.3, 340.2 and 350.4.

Paragraph 100.4 of the IESBA Code states:

“The use of the word “shall” in this Code imposes a requirement on the Member or Firm to comply with the specific provision in which “shall” has been used. Compliance is required unless an exception is permitted by this Code.”

On this issue, the IESBA drafting convention is different from APESB drafting convention 5.2(d) which requires a member obligation to be clearly articulated.

The Board to consider whether these requirements should be redrafted in accordance with APESB drafting conventions to clarify on whom the professional obligation is imposed or to adopt the IESBA drafting convention.

### Technical Staff view

APESB Drafting convention 5.2(d) requires:

“the word ‘shall’ is used within mandatory requirements paragraphs to denote the obligations a member is required to comply with;”

Technical Staff recommend that APESB’s drafting convention be adhered to given the legal enforceability of APES 110 (due to the operation of ASA 102) in Australia. Requirements need to be clearly drafted to clarify on whom the obligation is placed.

### **Material Presented**

- Appendix A – Technical Staff comments on substantive issues identified by ASIC [Confidential]
- Appendix B – Overview of APESB 2006 Insertions (excluding definitions);
- Appendix C – Overview of APES 2006 Removals (excluding definitions);
- Appendix D – Extract from Foreword to AUASB Pronouncements – Appendix 1 and Appendix 2; and
- Appendix E – Extract from AASB Exposure Draft ED 192 Revised Differential Reporting Framework.
- Submission received from Australian Securities and Investments Commission (ASIC) on APESB Consultation Paper CP 01/09 Proposed Revision of APES 110 *Code of Ethics for Professional Accountants* [Confidential]
- Exposure Draft ED 02/10 Proposed Standard: APES 110 *Code of Ethics for Professional Accountants* [*marked-up, version 1.09*];

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## Appendix A – ASIC [Confidential]

## Overview of APESB 2006 Insertions (excluding definitions)

APES 110 [2008] AUST Paragraph	ED 02/10 [v1.09] AUST Paragraph	APES 110 [Year]	Nature of Amendment	Staff View
PREFACE (AUST)	PREFACE (AUST)	2006	[F1] Australian context	Retain and modify – rename as scope and application
AUST 100.1.1	AUST 100.1.1	2006	Australian context – defines public interest	Retain
AUST 100.3.1	AUST 100.3.1	2006	[F1] Additional guidance	Retain
AUST 100.3.2	AUST 100.3.2	2006	[F1] Additional guidance	Retain
AUST 100.3.3	AUST 100.3.3	2006	[F1] Additional guidance	Retain
100.17	100.18	2006	Additional guidance	Retain
140.1, 140.6, 140.7, 140.8	140.1, 140.6, 140.7, 140.8	2006	In the Australian context there is only a legal duty to disclose	Retain
AUST 140.7.1	AUST 140.7.1	2006	Additional guidance	Retain
150.1	150.1	2006	[CPC Section B] Clarity	Retain
AUST 200.2.1	AUST 200.2.1	2006	[F7] Additional guidance	Retain
AUST 200.2.2	AUST 200.2.2	2006	[F7] Additional guidance	Retain
200.4	200.4	2006	Additional guidance	Retain
Note before 210.10	Note before 210.9	2006	Additional guidance	Retain
AUST 210.11.1	AUST 210.11.1	2006	[F3] Additional guidance	Retain
AUST 210.18.1	AUST 210.14.1	2006	Additional guidance	Retain
220.4	220.4	2006	Clarity	Retain
230.1	230.1	2006	Clarity	Retain
240.1 + headings	240.1 + headings	2006	Minor editorials	Retain
240.7, 240.8	240.7, 240.8	2006	Deliberate change made from the old IFAC Code to require members to disclose referral fees and commissions in writing to Clients	Retain
250.2	250.2	2006	Additional requirement	Retain
280.1	280.1	2006	Additional guidance	Retain
Section 290 AUST Preface	Section 290/291 AUST Preface	2006	[F1]/Australian context	Retain and modify
AUST 290.7.1	AUST 291.16.1	2006	Australian context	Retain and modify
AUST 290.7.2	n/a	2006	Australian context	Remove

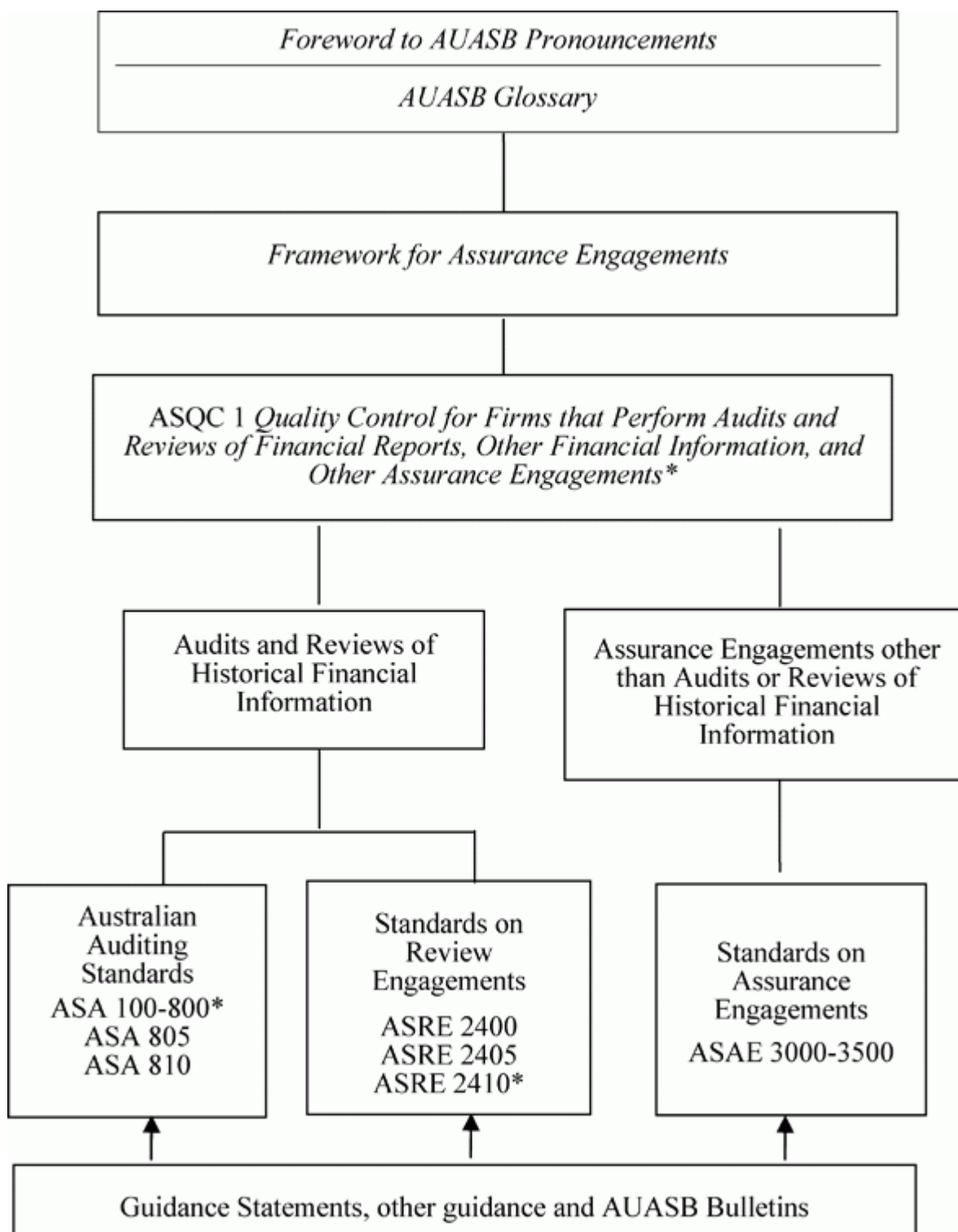
<b>APES 110 [2008] AUST Paragraph</b>	<b>ED 02/10 [v1.09] AUST Paragraph</b>	<b>APES 110 [Year]</b>	<b>Nature of Amendment</b>	<b>Staff View</b>
AUST 290.7.3	n/a	2006	Australian context	Remove
AUST 290.7.4	n/a	2006	Australian context	Remove
AUST 290.35.1	AUST 290.39.1	2006	Australian context	Retain
AUST 290.40.1	AUST 290.29.1	2006	Australian context	Retain
AUST 290.41.2 to AUST 290.41.12	AUST 290.8.1 to AUST 290.8.11 and AUST 291.7.1 to AUST 291.7.11	2006	Australian context – application of the threats and safeguards model	Retain
AUST 290.45.1	AUST 290.31.1	2006	Corporations Act	Retain
AUST 290.47.1	AUST 291.32.1	2006	Additional guidance	Retain
290.126 to 290.130	290.118 to 290.121, 290.123 and 291.113 to 291.116, 291.118	2006	Australian context – Financial institution	Retain
AUST 290.134.1	AUST 290.126.1	2006	[F1] Corporations Act	Retain
Headings after 290.135	Headings after 290.127	2006	Minor editorials	Retain
290.144	290.136	2006	[F1]	Retain
AUST 290.145.1	AUST 290.138.1	2008	Corporations Act	Retain
290.147	290.144	2006	[F1]	Retain
AUST 290.147.1	AUST 290.144.1	2006	[F1]	Retain
AUST 290.148.1	AUST 290.145.1	2006	[F1]	Retain
290.149	290.146	2006	Corporations Act	Retain
290.153, 290.155 and 290.157	290.151, 290.154 and 290.155	2006	[F1] Corporations Act	Retain and modify
AUST 290.206.1	AUST 291.151.1	2006	[F1]	Retain
AUST 290.212.1	AUST 291.156.1	2006	[F1]	Retain
AUST 290 Appendix	AUST 290 Appendix	2006	Corporations Act	Retain – to be reviewed: modify if necessary
290.6	n/a	2006	Additional guidance	Remove – insertion doesn't fit relocated paragraph
300.3	300.3	2006	Minor editorial	Retain
320.2 and 320.3	320.2 and 320.3	2006	Minor editorial	Retain
330.1	330.1	2006	Minor editorial	Retain
350.5	350.5	2006	Minor editorial	Retain

## Overview of APESB 2006 Removals (excluding definitions)

APES 110 [2008] AUST Paragraph	ED 02/10 [v1.09] AUST Paragraph	APES 110 [Year]	Nature of Amendment	Staff View
100.4	100.5	2006	Previously removed	Consider retaining IESBA wording
210.11	210.10	2006	Previously removed	Agree with removal
210.12	210.13	2006	Previously removed	Agree with removal
210.16	210.14	2006	Previously removed	Agree with removal
250.2	250.2	2006	Previously removed	Agree with removal
280.2	280.2	2006	Previously removed	Agree with removal
290.46	290.32	2006	Previously removed	Agree with removal
290.150	290.147 and 291.136	2006	Australian context – Previously removed	Agree with removal
290.151	290.148 and 291.137	2006	Australian context – Previously removed	Agree with removal

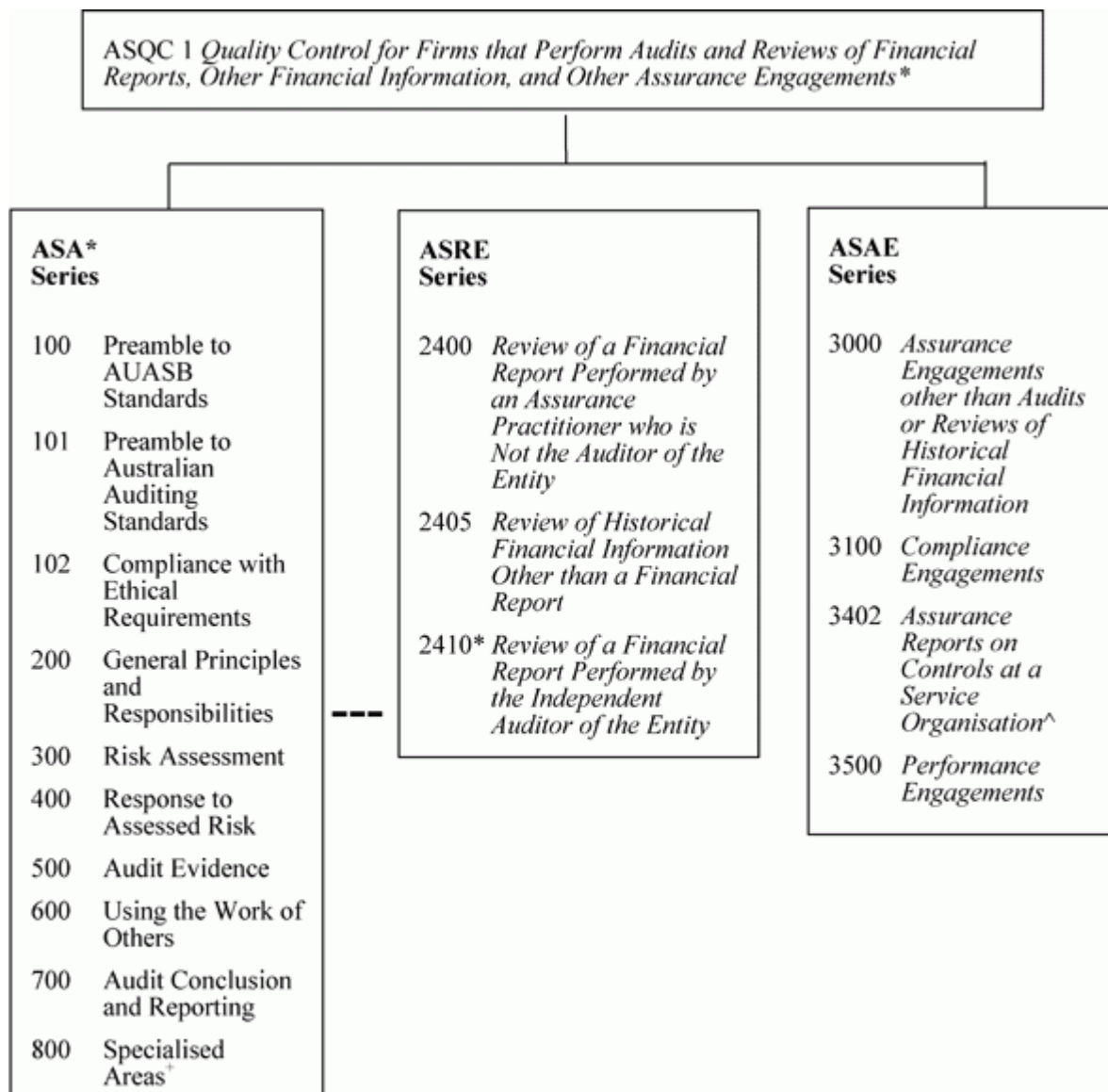
Extract from Foreword to AUASB Pronouncements – Appendix 1 and Appendix 2

Appendix 1 – Structure of Pronouncements issued by the Auditing and Assurance Standards Board



\* Made under section 336 of the *Corporations Act 2001*.

## Appendix 2 – Standards issued by the Auditing and Assurance Standards Board



\* Made under section 336 of the *Corporations Act 2001*.

+ ASA 805 and ASA 810 not made under the *Corporations Act 2001*.

<sup>^</sup> To be released by the AUASB in April 2010.

## Extracts from AASB Exposure Draft ED 192 Revised Differential Reporting Framework

- 18 This Exposure Draft proposes:
- (a) a revised differential reporting framework consisting of two tiers of reporting requirements for preparing GPFs:
    - Tier 1: Full IFRSs as adopted in Australia; and
    - Tier 2: The RDR;
  - (b) disclosures to be required under Tier 2;
  - (c) that publicly accountable for-profit private sector entities should apply Tier 1, and non-publicly accountable for-profit private sector entities have a choice of applying Tier 1 or Tier 2;
  - (d) that not-for-profit private sector entities should have a choice of applying Tier 1 or Tier 2;
  - (e) that public sector entities should have a choice of applying Tier 1 or Tier 2, except:
    - (i) Federal, State and Territory Governments;
    - (ii) Local Governments; and
    - (iii) Universities;
 that should apply Tier 1;
  - (f) a definition of ‘public accountability’ based on the IASB’s definition, supplemented with additional examples of publicly accountable entities from an Australian perspective;
  - (g) a clarification of the meaning of GPFs and modifying the way the reporting entity concept is used; and
  - (h) transitional provisions for entities applying Tier 1 or Tier 2 for the first time and moving between Tiers.
- 19 While Tier 2 requirements would be available to all not-for-profit private sector entities and public sector entities other than those required to apply Tier 1, regulators have the power to require the application of Tier 1 requirements by entities they regulate.
- 20 The AASB may decide to change the categories of entities that will be subject to Tier 1, particularly those in the public sector, pending the deliberation of constituents’ comments on its Consultation Paper and Exposure Draft proposals.

21 The table below summarises the AASB’s revised differential reporting framework.

	Sector		
	For-profit private	Not-for-profit private	For-profit and not-for-profit public
<b>Tier 1</b>  Full IFRSs as adopted in Australia	Publicly accountable (per IASB definition, with additional examples of publicly accountable entities in the Australian context—see paragraph 26 below)	All NFP private sector entities have a choice of applying Tier 1 or Tier 2 requirements unless the relevant regulator requires application of Tier 1	Federal, State and Territory Governments, Local Governments, and Universities
<b>Tier 2</b>  Reduced Disclosure Regime (entities may choose to apply Tier 1, that is, full IFRSs as adopted in Australia)	Non-publicly accountable		Entities other than Tier 1 entities noted above, unless the relevant regulator requires application of Tier 1

## Definitions

24 The following terms are proposed for the purposes of this Exposure Draft with the meaning specified:

**Public accountability** means accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs.

A for-profit private sector entity has public accountability if:

- (a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or
- (b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks. [*IFRS for SMEs Glossary, changes underlined*]

## Public accountability

25 Public accountability is defined in paragraph 24. The notion of public accountability is consistent with the notion adopted by the IASB in its International Financial Reporting Standard for Small and Medium sized Entities (*IFRS for SMEs*). This notion is different from the notion of public accountability in the general sense of the term that is often employed in relation to not-for-profit entities.

- 26 To clarify the application of the IASB notion of public accountability in an Australian context, the following are additional examples of entities having public accountability:
- (a) disclosing entities, even if their debt or equity instruments are not traded in a public market or are not in the process of being issued for trading in a public market;
  - (b) cooperatives that issue debentures;
  - (c) registered managed investment schemes;
  - (d) superannuation plans registered with the Australian Prudential Regulation Authority;  
and
  - (e) Authorised Deposit-taking Institutions.