

AGENDA PAPER

Item Number: 11

Date of Meeting: 4 November 2013

Subject: Proposed amendments to APES 110 *Code of Ethics for Professional Accountants* due to revisions of the IESBA Code

Action Required

For Discussion

For Information Only

Purpose

To provide the Board with an evaluation of the respondents' comments on the revision of APES 110 *Code of Ethics for Professional Accountants* (the Code) and to obtain the Board's approval to issue the amendments to the Code.

Background

The International Ethics Standards Board for Accountants (IESBA) approved changes to the IESBA *Code of Ethics for Professional Accountants* in respect of the following areas:

- Breach of a requirement of the Code;
- Conflicts of interests;
- Definition of *Those Charged with Governance*; and
- Definition of *Engagement Team*.

In accordance with APESB's due process, APESB proposes to amend APES 110 consistent with the amendments incorporated internationally in the IESBA Code (except for the definition of Engagement Team). In August 2013 the Board determined to expose the proposed amendments to APES 110 for public comment. Seven submissions were received in response to the Exposure Draft for the Board's consideration.

Consideration of Issues

Summary of key issues in submissions received

Australasian Council of Auditors-General (ACAG), Australian Securities & Investments Commission (ASIC), Ernst & Young (EY), Macquarie University (MU), Deloitte Touche Tohmatsu (Deloitte), Institute of Chartered Accountants Australia & CPA Australia (ICAA/CPAA) and the Auditing and Assurance Standards Board (AUASB) were generally supportive of the proposed amendments to the Code subject to the specific matters they

have raised in respect of scope and application, definition of the Engagement Team and Breach of a requirement of the Code

Scope and Application

ACAG were of the view that there is a need to clarify in the "Scope and Application" that legislation takes precedence over the Code. Paragraph 1.2 (compliance by Members in Australia) is silent on the precedence of legislation, whereas paragraph 1.3 (compliance by Members outside Australia) states the exception. ACAG stated that this conjunction may lead users to an incorrect inference that there are no exceptions for Members in Australia.

ACAG further noted that the proposed requirement at paragraph 290.40 cannot be complied with by the Auditors-General as they are unable to terminate their relationships with audit clients under the terms of their legislative mandates.

Refer Items 1 & 2 in the attached Specific Comments table for further details.

Definition of Engagement Team

EY, MU and Deloitte raised concerns on the rationale provided by APESB for its proposal not to amend the definition of Engagement Team in line with the revision made to the IESBA Code of Ethics. They were of the view that APES 110 should be consistent with the IESBA Code of Ethics unless changes are shown to be required for legislative or regulatory reasons specific to the Australian jurisdiction. They argued that the threats and safeguards framework in the revised ISA 610 suffice and that the objectivity of external auditors will not be impaired and audit quality not undermined by internal auditors being used in a direct assistance capacity. Accordingly, they were of the view that direct assistance should be permitted in Australia and in this regard, the Australian definition of Engagement Team should not deviate from the international definition.

ICAA/CPAA agreed with the position adopted by APESB and the rationale expressed in the Exposure Draft. However, they raised concerns on how a prohibition in Australia would affect cross border engagements and group audit scenarios when direct assistance is permitted in other jurisdictions. They were of the view that regardless of whether or not direct assistance is eventually prohibited in Australia, the definition of Engagement Team in APES 110 should be modified to explicitly provide guidance where ISA 610 is applicable for Members in different jurisdictions.

AUASB and ASIC were supportive of APESB not amending the definition of Engagement Team due to the following reasons:

- The internal auditor is employed by the audited entity and would not appear to be independent in fact or appearance. This can affect confidence in the external audit process and the quality of an audited entity's financial report;
- Threats to the objectivity of the internal auditor arise from the internal auditors being remunerated by the audited entity, concerns about their future career prospects, and familiarity with management;
- Involvement of internal auditors may be used by the audited entity to place pressure on external audit fees, which may be a further risk to the quality of external audits;
- it is inappropriate to imply that an internal auditor providing direct assistance is a substitute for an external audit team member and yet not regard that person as part of the Engagement Team and subject to the same independence rules as other Engagement Team members; and

- The independence of the external auditor is fundamental to promoting both actual and perceived overall audit quality, auditor scepticism and to the actual and perceived value to stakeholders of an independent external audit. Given the current environment it is not the time to relax independence requirements for auditors, but to strengthen them where possible.

Refer Items No. 7-12 in the attached Specific Comments table for further details.

Breach of a requirement of the Code

ASIC was generally supportive of the proposed changes to strengthen the Code in connection with breaches of a requirement. ASIC further suggested that auditors should be required to highlight in their audit or review report a breach of the independence requirements in respect of non-Corporations Act financial reports in circumstances where the auditor does not resign. ASIC also suggested that APESB should liaise with the AUASB in this regard.

Refer Item No. 13 in the attached Specific Comments table for further details.

Technical Staff Analysis of Issues

Scope and Application

Paragraph 1.4 of APES 110 clearly states that the Code is not intended to detract from any responsibilities which may be imposed by law or regulation. It is proposed that paragraph 1.2 be amended as shown below to provide clarity that the application of the Code is subject to law and regulation. This is consistent with the AUST preface to Sections 290 and 291 in the Code.

1.2 Subject to paragraph 1.4, aAll Members in Australia shall comply with APES 110 including when providing Professional Services in an honorary capacity.

Definition of Engagement Team

The International Auditing and Assurance Standards Board (IAASB) issued the Revised ISA 610 *Using the work of Internal Auditors* (ISA 610) in March 2013 permitting the use of Internal Audit Staff to perform external audit procedures (referred to as 'Direct Assistance') in certain circumstances. This in turn resulted in the amendment to the Definition of "Engagement Team" in the IESBA Code which excluded Internal Audit from the definition of Engagement Team in the external audit context. IAASB also stated that its requirements and guidance in respect of Direct Assistance will not be applicable in jurisdictions where this practice is prohibited.

The existing definition of 'Engagement Team' in APES 110 does not provide exclusion for Internal Audit Staff from the Engagement Team. Internal Audit Staff who provide Direct Assistance will have similar skills to external auditors, will complete audit work papers on the same engagement file and will most likely have access to the related audit programs and applicable sections of the audit file. Therefore it is inconsistent to imply that an Internal Auditor providing Direct Assistance is a substitute for an External Audit Team Member and yet not regard them as part of the Engagement Team. 11 European audit regulators who responded to the international exposure draft were not in favour of Direct Assistance as in

their view excluding internal auditors that provide direct assistance from the Engagement Team definition did not resolve the issue of the lack of independence of internal auditors.

Breach of a requirement of the Code

ASIC has raised the issue of disclosure of breaches of independence requirements in the audit report for non-Corporations Act audits. Whilst there is an international project underway on Auditor Reporting and it is likely that the Audit Report will be modified in due course, Technical Staff are of the view that matters to be disclosed in an audit report are most appropriately addressed by the AUASB subject to the international developments on Auditor Reporting.

AUASB Board Meeting

At the AUASB Board meeting on the 28th October 2013, the AUASB unanimously approved ASA 610 which prohibits Direct Assistance by Internal Audit Staff in the external audit process in Australia. Accordingly, it is appropriate to continue with the existing definition of Engagement Team in the Code.

Staff Recommendation

The Board note the respondents' comments to ED 02/13 *APES 110 Code of Ethics for Professional Accountants due to revisions to the IESBA Code* and subject to the Board's review comments and editorials, approve the amending standard to the Code.

Material Presented

Attachment 11 (a)	Amendments to APES 110 – General Comments Table;
Attachment 11 (b)	Amendments to APES 110 – Specific Comments Table;
Attachment 11 (c)	AUASB 28 October 2013 Board Meeting Summary Paper – Revised ISA 610;
Attachment 11 (d)	APESB letter to AUASB (Confidential); and
Attachment 11 (e)	Amendments to APES 110 <i>Code of Ethics for Professional Accountants</i> due to revisions to IESBA's <i>Code of Ethics for Professional Accountants</i> .

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Date: 29 October 2013