



25 January 2012

Ms Jan Munro  
Deputy Director  
International Ethics Standards Board for Accountants  
International Federation of Accountants  
545 Fifth Avenue, 14<sup>th</sup> Floor  
New York, New York 10017 USA  
By email: [janmunro@ifac.org](mailto:janmunro@ifac.org)

Dear Jan,

**RE: Proposed Changes to the Code of Ethics for Professional Accountants Related to Provisions Addressing a Breach of a Requirement of the Code**

Accounting Professional & Ethical Standards Board Limited (APESB) welcomes the opportunity to make a submission on *Proposed Changes to the Code of Ethics for Professional Accountants Related to Provisions Addressing a Breach of a Requirement of the Code*.

**APESB's role**

APESB is governed by an independent board of directors whose primary objective is to develop and issue, in the public interest, appropriate professional and ethical standards. These standards apply to the membership of the three Australian professional accounting bodies. A secondary objective of the APESB is to provide the opportunity or forum for the discussion and consideration of issues relating to professional standards for accountants. The APESB is funded by the three major accounting bodies, but has complete independence in its standard-setting activities.

Our essential function is the setting of standards, and in doing this we endeavour to incorporate a strong emphasis on professionalism and the role of sound judgement in those accountants who are obliged to follow our standards. We believe that setting high quality standards with demanding criteria contributes to the professional standing and behaviour of members of the accounting profession.

## **General Comments**

APESB is supportive of the changes proposed in the Exposure Draft (referred to as the 'proposed changes to the Code' in this submission) which aim to provide a more robust framework to evaluate, document and communicate breaches of the Code. APESB believes that these proposed amendments are in the public interest and enhance the transparency of a professional accountant's or audit firm's evaluation of these matters.

APESB has incorporated into APES 110 *Code of Ethics for Professional Accountants* (the Australian Code) additional Australian requirements that specifically address independence breaches of the Code (i.e. inadvertent violations, as per the existing Code).

### ***Paragraph 100.10***

Whilst we are generally supportive of the obligation for a professional accountant to determine whether to report a breach of the Code to appropriate parties, the use of the phrase 'those who may have been affected by the breach' may cast the net too wide. APESB suggests that IESBA consider limiting this requirement to communicate with *'the appropriate parties of the client or employer'*. Further, confidentiality obligations will limit a professional accountant's ability to communicate with parties (other than a party of the client or employer) who may have been affected by the breach.

### ***Termination of audit engagement and resignation of auditor (Paragraphs 290.45 and 291.36)***

APESB believes that IESBA's proposal that an auditor should terminate the audit engagement in circumstances where the auditor is unable to satisfactorily deal with an independence breach significantly strengthens the Code.

### ***Phrase 'as soon as possible' in paragraphs 100.10, 290.46, 291.33 and 291.35***

APESB suggests that IESBA consider revising the phrase 'as soon as possible' used in the paragraphs noted above to 'as soon as practicable'. We believe that there is more subjectivity in 'as soon as possible' compared to 'as soon as practicable'. We note that the existing Code uses 'as soon as practicable' four times (paragraphs 290.105, 290.111, 290.161 and 291.107) whilst 'as soon as possible' is only used once (paragraph 290.116). "As soon as practicable" implies taking action at the first reasonable opportunity and is a higher threshold.

### ***Examples of inadvertent breaches***

APESB suggests that IESBA consider including examples of inadvertent breaches (e.g. inheritance of shares in an audit client, investment by a fund manager in an audit client, spouses/dependents/power of attorney/executors acting independently of the auditor, etc.) which will provide audit practitioners with guidance to identify the most common scenarios.

### ***Paragraph 290.44***

APESB suggests that IESBA consider the use of the term ‘may’ instead of ‘might’ in paragraph 290.44 in order to convey a greater expectation of likelihood of actions.

### **Specific Comments**

APESB’s responses to the specific issues raised by the IESBA are as follows:

- 1. Do respondents agree that the Code should contain provisions that require professional accountants to address the consequences of a breach of a requirement in the Code? If not why not?**

APESB agrees that the Code should contain these provisions. Consistent with the IESBA view, APESB agrees that their inclusion will promote responsible ethical behaviour by professional accountants and strengthens the Code.

- 2. Do respondents agree with the overall approach proposed to deal with a breach of an independence requirement, including the proposal that the firm may continue with the audit engagement only if those charged with governance agree that action can be taken to satisfactorily address the consequences of the breach and such action is taken?**

APESB supports the overall approach of the proposed changes to the Code in dealing with a breach of an independence requirement. APESB further agrees that the decision to continue an audit engagement should rest with those charged with governance taking into consideration whether the breach has been appropriately remedied.

- 3. Do respondents agree that a firm should be required to communicate all breaches of an independence requirement to those charged with governance? If not, why not and what should be the threshold for reporting?**

APESB does not agree that all breaches of independence requirements should be communicated to those charged with governance.

We believe that there should be some consideration of entity specific factors in determining whether to communicate all breaches to those charged with governance. In line with recent amendments to the Code, IESBA should consider the nature of the entity including whether the entity is a Public Interest Entity (PIE). The Code places more restrictive independence requirements on PIEs and similarly IESBA could consider whether the more restrictive reporting of breaches should be in respect of Public Interest Entities.

The other important factor to consider is the role played by those charged with governance in determining the threshold for reporting breaches. There should be some

flexibility for those charged with governance to determine the threshold for reporting breaches by their auditor.

In respect of financial reporting, those charged with governance determine the threshold for the auditor to report errors and misstatements to them and thus the auditor generally would not report all errors or misstatements identified during the course of an audit.

We believe that another reasonable basis for determining the threshold for reporting breaches is the approach adopted in the existing Australian Code to document and communicate with those charged with governance those inadvertent violations that are not *trivial and inconsequential*.

Whilst we note IESBA's concern regarding the subjective nature of this judgment by the auditor, IESBA may consider addressing this concern by incorporating a "*reasonable and informed third party test*" to be used as a basis for determining whether the matter should be reported to those charged with governance.

- 4. Do respondents agree that the reasonable and informed third party test should be used in determining whether an action satisfactorily addresses the consequences of a breach of an independence requirement? If not, why not and what should the test be?**

APESB supports the use of the reasonable and informed third party test. An objective test will provide stakeholders with a mechanism to assess whether consequences of a breach have been appropriately addressed.

- 5. Do respondents agree that the matters that should be discussed with those charged with governance as proposed in section 290.46 are appropriate? If not, why not? Are there other matters that should be included, or matters that should be excluded?**

APESB agrees with the matters listed in section 290.46, subject to our comments on trivial and inconsequential matters in question 3.

- 6. Do respondents agree with the impact analysis as presented? Are there any other stakeholders, or other impacts on stakeholders, that should be considered and addressed by the IESBA?**

APESB agrees with the impact analysis presented and has no additional comments to make in this regard.

- 7. Would the proposal require firms to make significant changes to their systems or processes to enable them to properly implement the requirements? If so, does the proposed effective date provide sufficient time to make such changes?**

As noted in our response to question 3, APESB incorporated into the Australian Code requirements to discuss and document with those charged with governance, inadvertent violations of independence requirements which are not trivial and inconsequential. These

additional Australian requirements were effective from 1 July 2011. To date, APESB has not received any feedback from stakeholders to indicate that implementation of these additional Australian requirements has created significant challenges to stakeholders.

Assuming IESBA is able to issue the proposed standard in the first half of 2012, APESB is supportive of the start date of 1 January 2013. We believe that the effective date should be at least 6 months after publication of the final standard to provide sufficient time for constituents to educate and inform the affected parties as well as for audit firms to make appropriate changes to their systems, policies and procedures.

**8. Is the abbreviated version of the framework described in Section 290 for dealing with a breach of an independence requirement suitable for Section 291? If not, what do respondents believe Section 291 should contain?**

APESB supports the inclusion of an abbreviated version of the framework for section 291.

We hope you find these comments useful in your final deliberations and if you require any additional information, please do not hesitate to contact me at [kspargo@bigpond.net.au](mailto:kspargo@bigpond.net.au) or Channa Wijesinghe, Technical Director at [channa.wijesinghe@apesb.org.au](mailto:channa.wijesinghe@apesb.org.au).

Yours sincerely



Kate Spargo

**Chairman**