

## **APESB Project Proposal**

### **Risk Management Standard**

**From:** CPA Australia Ltd and the Institute of Chartered Accountants in Australia

#### **Background**

In May 1982 the Institute of Chartered Accountants in Australia and CPA Australia issued APS 4 *Statement of Quality Control Standard* and APS 5 *Quality Control Policies and Procedures*. Then in October 2003 CPA Australia issued a revision for its members referred to as APS 4/5, together with the Risk Management Statement RMS 1. RMS 1 has mandatory application to all CPA members and practices, requiring them to document their risk management policies and procedures.

RMS 1 states at paragraph 8 that "Risk Management is identified as one of the elements of the Quality Control Standard APS 4/5 whereby a practice must develop, implement and maintain a process to ensure that management of risk becomes an integral part of the planning management process and culture of the practice".

It is understood that the prevailing view within the Institute was that risk management was not an element of quality control, as the authors of RMS 1 had expressed it, but rather that quality control was a consequence of good risk management. This divergence of views led to the diversity of approaches to dealing with risk management between the two bodies.

In February 2004 IFAC issued ISQC 1 *Quality Control for Firms That Perform Audits and Reviews of Historical Financial Information and Other Assurance Related Services Engagements*. Consequently, the two professional bodies undertook a revision of APS 4 and 5 and of APS 4/5. As part of that revision, the relationship between quality control and risk management was again explored.

Consensus was reached at that time to issue a new quality control standard, APS 5, to be complemented by a standard on risk management, APS 4, which would extend the obligation to document risk management policies and procedures to Institute members. It was agreed that RMS 1 would form the basis for the new risk management standard, following suitable revisions.

APS 4 and 5 and APS 4/5 were replaced in July 2005 by a reissued APS 5 *Quality Control for Firms*.

The revision of RMS 1 and the issuing of a new risk management standard had not taken place by the time of the establishment of the APESB in January 2006. However, the professional bodies recognise that there is a need for a risk management standard. Today's complex business environment presents substantial risks to accountants and their clients. Risk management is recognised as a key component of good governance, whether of a listed company, or of an accountancy practice. The consensus view now is that it is important for all accounting practices to have a risk management plan so that accountants do not expose themselves, their clients and the profession generally to avoidable business risk and litigation. Adopting a risk management policy and processes is a necessary element of professional conduct.

#### **An appropriate risk management framework**

Two of the most commonly used Risk Management Frameworks are (i) AS/NZS 4360:2004, issued by Standards Australia and Standards New Zealand, and (ii) the COSO Enterprise Risk Management Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Whilst each may use different language and headings, the basic concepts are consistent. Both frameworks require the user to:

- Identify the context within which they operate, including the internal and external environment, as well as the entity's objectives
- Identify the factors, both negative or positive, that may impact the entity's objectives
- Assess, analyse and evaluate the impact of such factors
- Treat or respond to the above risks or opportunities
- Monitor the risk management process in its entirety
- Communicate and consult throughout the entire process.

Both provide guidance on how to develop and incorporate the framework. The most significant difference between the two frameworks is the detail of the COSO guidance. The guidance provided in the COSO

framework is useful, but perhaps excessive. However, on the other hand, whilst the approach and content provided by the AS/NZS 4360:2004 framework is more succinct and easier to use, this could be improved by incorporating some of the material contained in the COSO framework.

CPA Australia Ltd's RMS 1 was based on AS/NZS 4360:2004.

**Objectives:**

The objective of the proposal is to develop a standard that will see practitioners allocate an appropriate level of effort and professionalism toward enterprise risk management. A suitably drafted risk management standard would increase accountants' awareness of, and compliance with, applicable principles and processes as well as the business environment relevant to them and their clients.

Adopting a risk management policy and processes will enable practitioner members to:

- Better identify threats, opportunities and exposure to risk
- Remain aware of potential risks
- Better manage incidents and reduce losses
- Reduce the chance of litigation
- Reduce the cost of non compliance with relevant standards
- Reduce insurance premiums
- Provide a more professional service to clients

**Stakeholders:**

Members of CPA Australia, ICAA and NIA in public practice

CPA Australia, ICAA and NIA

Clients of public practitioners

**Impact on other APESB standards:**

A risk management standard would complement APES 320 and assist quality reviewing against that standard.

**Impact on accounting, auditing or other relevant standards:**

N/A

**Other legislative developments:**

Principle 7 of the ASX *Principles of Good Corporate Governance and Best Practice Recommendations* specifies the desirability of establishing "a sound system of 'risk oversight and management.'"

**Benefits of the standard:**

See above under 'objectives'.

**Project proposal submitted by:**

Denis Pratt  
Director Professional Standards  
CPA Australia  
(03) 9606 9798

Paul Meredith  
Manager Professional Standards  
ICAA  
(02) 92905535