Proposed Application Material Relating to: (a) Professional Scepticism - Linkage with the Fundamental Principles; and (b) Professional Judgement - Emphasis on Understanding Facts and Circumstances

ICAEW welcomes the opportunity to comment on the *Proposed Application Material Relating to: (a) Professional Scepticism - Linkage with the Fundamental Principles; and (b) Professional Judgement - Emphasis on Understanding Facts and Circumstances* published by IESBA on 11 May 2017, a copy of which is available from this link.

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MAJOR POINTS

1. The proposed application material is indicative of a short term solution for an issue that requires much wider and more detailed consideration. We would therefore urge IESBA to press on with a larger project.

2. Professional scepticism is an 'enabler' for compliance with the fundamental principles, not the other way round.

3. The proposed material on professional judgement is unnecessary, though does raise some interesting questions.

RESPONSES TO SPECIFIC QUESTIONS

Q1: Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?

4. Whilst a closer examination of the concept of professional scepticism is welcome, we are concerned that the proposed application material is simply a short term solution to an issue that requires much wider and more detailed consideration. Indeed, we are told that IESBA is currently considering how the Code should address the applicability of the concept to professional accountants other than auditors and assurance providers. We are concerned that interim changes can have unintended costs and consequences (for example in expectations around documentation)and the subject matter of this consultation should be dealt with as part of a more holistic approach.

5. The proposals also raise questions around the 'status' of the fundamental principles within the conceptual framework. See our comments in paragraph 6 below.

Q2: Do the examples in the proposed application material clearly describe how compliance with the fundamental principles of integrity, objectivity, and professional competence and due care support the exercise of professional scepticism in the context of an audit of financial statements? If not, why not?

6. No. The proposals suggest that complying with the fundamental principles supports the exercise of professional scepticism. We believe the opposite to be true and that professional scepticism is an 'enabler' that supports adherence to the fundamental principles. The definition of independence also implies that professional scepticism is an end in itself but also shows the fundamental principles as an end too. This illustrates that the definition of independence may need revisiting and that parachuting IAASB concepts into the code might not always work, particularly as the notion of scepticism may differ subtly between an audit context and a non-audit specific one.

Q3: Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?

7. No. Professional judgement is described as involving the application of training, knowledge and experience. Whilst this is true there are other important elements such as analytical skills and 'gut feeling', the latter being especially difficult to codify.

8. The specific reference to inconsistency between known facts and auditor expectations raises important questions around confirmation bias and heuristics. The document highlights this with a later reference to preconceptions or bias affecting judgement, and mention of other reasonable conclusions being drawn from evidence. Whilst these topics are most certainly worthy of further consideration the proposals as they stand are inadequate in this respect. This

further supports our assertion that this project is better considered as part of a wider, more holistic exercise.

Q4: Do respondents agree that the proposed application material appropriately emphasises the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgement in applying the conceptual framework? If not, why not?

9. Subject to our comments in paragraph 6 yes. However this is not a new idea and one which we believe is already sufficiently clear. The extant code (100.20) makes specific reference to having the 'relevant facts' in complying with the framework. This supports our assertion that this useful framework should be retained in the restructured code.