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CPA Australia Ltd

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Dear Ken

Exposure Draft: Improving the Structure of the Code of Ethics for Professional Accountants - Phase 1

CPA Australia is pleased to provide comments in relation to this Exposure Draft (ED). CPA Australia represents the diverse interests of more than 155,000 members in 118 countries. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders. We make this submission on behalf of our global membership and in the broader public interest.

As mentioned in our comments to IESBA's Consultation Paper: *Improving the Structure of the Code of Ethics for Professional Accountants* (CP), CPA Australia supports IESBA's commitment to an approach that is primarily principles and professional judgement based. We are of the opinion that a code of ethics and the exercise of professional judgement are key characteristics of the profession.

Overall, we are of the view that the proposed revised Code requires further refinement and review and we urge IESBA to prioritise the quality and completeness of the restructured Code rather than the expeditiousness of its issue.

Specifically, we are of the view that this project provides the best opportunity to create a Code which contains a section for all professional accountants, thus merging extant parts A and C, and a section that addresses specific requirements for public practitioners and independence for audit and review engagements.

We do not support the insertion of the concept of standards in the Code's title. Standards are typically understood as regulation and we are of the view that while accounting and auditing standards are exactly that, the Code provides the principles that form the foundation of the accounting profession.

CPA Australia considers it necessary for the Code to clarify and explain the interaction between independence, the principles and the conceptual framework.

Our comments in this submission will not address specific issues raised in our submissions to IESBA's Exposure Draft: *Proposed Revisions Pertaining to Safeguards in the Code – Phase 1*, particularly in relation to the conceptual framework, the 'Reasonable and Informed Third Party' and 'Acceptable Level', or *Consultation Paper: Improving the Structure of the Code of Ethics for Professional Accountants*. We provide comments to the specific questions below.

Specific Comments

Refinements to the Code

1. Do you agree with the proposals, or do you have any suggestions for further improvement to the material in the ED, particularly with regard to:

(a) Understandability, including the usefulness of the Guide to the Code?

CPA Australia supports the inclusion of the Guide to the Code. However, we are of the view that some of the content included in the Guide should be placed in the Conceptual Framework Section of the Code, particularly the content of the Exceptional Circumstances section.

Paragraph 11 of the Guide encourages professional accountants to consult on all ethical dilemmas, whenever there are competing duties or principles, and provides a regulator as an appropriate party for consultation. Making a professional judgement is about resolving ethical dilemmas and while we are of the view that the other parties listed in this paragraph may be appropriate, we do not see how a regulator could or should fulfil this role.

We find the first paragraph of the Guide confusing. It also contradicts the second paragraph, which refers to the application of the conceptual framework whereas paragraph one refers to standards that are established. Paragraph one also introduces the concept of standards in the Code. We do not think this is appropriate or helpful, as the Code does not set standards.

(b) The clarity of the relationship between requirements and application material?

While we appreciate that the accounting and auditing standards use the term 'application material', we support use of the term 'guidance' in the Code. This will be better understood in different jurisdictions and we find the more complex term unnecessary.

We support the inclusion of the guidance together with the requirements in each section.

(c) The clarity of the principles basis of the Code supported by specific requirements?

The approach adopted in the Code is confusing and we are concerned that it may become more so in the restructured Code. As mentioned previously we support the principles and conceptual framework approach of the Code. However, to argue that the Code is principles and conceptual framework based is misleading as it contains several rules and prescriptions that go beyond the requirement to comply with the fundamental principles by applying the conceptual framework using professional judgement. We therefore are of the view that the restructured Code should clarify its actual approach and disclose it in the proposed guide - while it is fundamentally principles and conceptual framework based, it provides some prescriptions in relation to professional accountants in public practice. The creation of two sections in the Code as we suggest in our response to question (f) (i) will aid this distinction and explanation.

The statement 'principles-based foundation and the inclusion of specific requirements' in paragraph 27 of the ED attempts to address our concern but we do not think it does so effectively, because it is not clear what a 'principles based foundation' means when there are specific prescriptions.

We do not support the inclusion of the header 'The conceptual framework contained in Section 120 applies in all circumstances' on every page of the Code, as we are not convinced that it is necessary or accurate, particularly when there are specific prescriptions that do not require the application of the conceptual framework.

(d) The clarity of the responsibility of individual accountants and firms for compliance with requirements of the Code in particular circumstances?

Subject to our comments below regarding merging extant parts A and C and creating a section that addresses specific requirements for public practitioners and independence for audit and review engagements, CPA Australia agrees with the adopted approach.

(e) The clarity of language?

There are several occurrences where the language needs to be reviewed, simplified and clarified. Earlier, we suggested the use of the term guidance instead of application material. Without providing every instance we identified of language related issues, we provide the following examples:

- Paragraph 6 of the Guide states: 'The Code requires professional accountants to comply with the fundamental principles of professional ethics'. The fundamental principles of the Code are the principles of the accounting profession not general professional ethics principles. So we think the term professional ethics should be removed.
- Paragraph 8 of the Guide states: 'In addition to requirements, the Code contains application material that provides context relevant to a proper understanding of the Code.' We do not think we are certain as to the intended meaning of this sentence and we are also of the view that guidance does not provide context but rather explanation.
- Paragraph 120.1 states: 'It [the conceptual framework] accommodates the many variations in facts and circumstances that create threats to compliance with the fundamental principles and deters an accountant from concluding that a situation is permitted if it is not specifically prohibited by this Code'. The term 'deter' is commonly understood as 'prevent' and we do not think the conceptual framework has the capacity to achieve that outcome.
- Paragraphs R120.9 and 300.2 A12 state: 'The reasonable and informed third party test described in Section 120 is relevant to this assessment.' Given that paragraph R120.4 requires the professional accountant to 'take into account whether a reasonable and informed third party would likely conclude that the accountant has complied with the fundamental principles', we are of the view that the word relevant is inappropriate as it is not optional but required.
- Paragraph 300.2 A1 (a) states: 'A firm having undue dependence on total fees from a client or the possibility of losing a significant client.' The second part of this sentence is missing 'being concerned about' or similar.
- Paragraph 300.2 A3 states that the level of a threat may be impacted by: 'An audit client and whether the audit client is a public interest entity'. We do not think that the nature of the audit client impacts the level of the threat.
- Paragraphs R320.4 and 320.4 A1 refer to reasons that may be 'professional or otherwise'. We do not think 'otherwise' is a helpful term, despite its use in the extant Code, and it is not clear what a professional and non-professional reason may be. We suggest that reference to 'any reason' is adequate. CPA Australia urges IESBA to clarify the interaction between independence, the principles and the conceptual framework and then review the description of each to ensure consistency in language and application.

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(f) The navigability of the Code, including:

(i) Numbering and layout of the sections;

We find the numbering more complex than that in the extant Code, so we do not think it supports the objectives of the project. We are of the view that the entire content of the Code is a requirement and professional accountants should be familiar with all of its content so we do not support distinguishing requirements from application.

We urge IESBA to consider a new structure for the Code that contains a section for all professional accountants, thus merging extant parts A and C and a section that addresses specific requirements for public practitioners and independence for audit and review engagements. This will be appropriate for a number of reasons:

- Public practitioners face the threats and circumstances addressed in extant part C as employees or in their interactions with the firm.
- The term 'Members in Business' does not reflect its meaning and therefore impedes understandability and application. If the proposed division between professional accountants in public practice and the rest is to be retained, we suggest that the term 'professional accountants in business' is replaced with 'professional accountants in organisations' – thus distinguishing from professional accountants in firms. Similarly, the expression 'professional or business', which is used in the extant code in relationships or judgements would need to be revised. We suggest that the term 'professional' is adequate to describe judgements and professionals, as it relates to the professional accountant, regardless of context, and judgements made by any professional accountant are professional judgements.
- The newly developed parts of the Code addressing presentation of information and pressure to breach the fundamental principles is of relevance and importance to all professional accountants.
- The interaction between, firm, network firm and professional accountant and the applicability and responsibility for compliance could be addressed with more ease and efficiency. The section that applies to all professional accountants can then refer to professional accountants, while the section that addresses public practice could make the necessary distinctions.

(ii) Suggestions for future electronic enhancements; and

CPA Australia believes that the Code should be available in multiple formats to accommodate different users and usage. However, we note that flexibility of format is crucial at the national or local jurisdiction level. Professional accountants use the Code adopted locally rather than the IESBA version, as is the case in Australia with APES 110 *Code of Ethics for Professional Accountants*.

(iii) Suggestions for future tools?

As mentioned, CPA Australia's experience indicates that tools are more appropriately developed at the local level so they can be tailored to the specific needs. CPA Australia has developed an overview tool for the extant Code as

adopted in Australia and we intent to provide more resources and tools when the restructured Code is issued.¹

(g) The enforceability of the Code?

We note that IESBA's aim for this project is 'to enhance the understandability and usability of the Code, thereby facilitating its adoption, effective implementation, consistent application, and enforcement'. So we understand that enforcement is expected to be the outcome of improved understandability and usability, though we have not identified any evidence to support this assertion.

2. Do you believe the restructuring will enhance the adoption of the Code?

We do not think that the restructuring will enhance adoption but we would expect that, provided the restructured Code is more accessible, it will lead to better 'understandability' and thus application.

3. Do you believe that the restructuring has changed the meaning of the Code with respect to any particular provisions? If so, please explain why and suggest alternative wording.

We have provided some examples in our response to 1(e).

Other Matters

4. Do you have any comments on the clarity and appropriateness of the term "audit" continuing to include "review" for the purposes of the independence standards?

In line with the objectives of this project, we support the unambiguous and consistent use of terms, so we urge the use of the term 'audit or review'.

5. Do you have any comments on the clarity and appropriateness of the restructured material in the way that it distinguishes firms and network firms?

We support the restructured approach adopted.

6. Is the proposed title for the restructured Code appropriate?

We do not support the inclusion of the word standards in the title. Standards are typically understood as regulation and we are of the view that while accounting and auditing standards are exactly that, the Code provides the principles that provide the foundation of the accounting profession.

¹ The overview of the Code can be accessed at: www.cpaaustralia.com.au/professional-resources/ethics/apes/overview

Additional Comments

We are of the view that this project provides a timely opportunity to review the use of the term 'technical' in the Code, which is generally used together with professional. We think the term 'technical' is no longer appropriate and the distinction between technical and professional is not evident. We are of the view that professional standards encompass all standards of the accounting profession. Further, the term 'ethics requirements' is also used alongside technical standards both in the extant Code and in paragraph 114.1 A2 (c)(iv). We suggest that the term be changed from ethics requirements to professional standards or the Code of Ethics as applicable, as ethics requirements does not have a clear meaning that can be applied consistently in different jurisdictions.

The 'intimidation threat' is described as the threat that a professional accountant will be deterred from acting objectively, as it is in the extant Code. We are of the view that an intimidation threat may affect compliance with other principles and we think it should be described more broadly like the other threats and not only with reference to one principle.

Paragraph 330.3 A9, like extant paragraph 240.7, presents disclosure as a safeguard. Research suggests that disclosure of a conflict of interest may in fact be counter-productive and lead to moral licensing. We therefore urge IESBA not to use disclosure as an effective safeguard, as is done in section 310.11.

If you have any questions regarding this submission please do not hesitate to contact Dr Eva Tsahuridu, Manager – Accounting Policy, at eva.tsahuridu@cpaaustralia.com.au or +61 3 9606 5159.

Yours sincerely

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