

PROFESSIONAL AND ETHICAL STANDARD 1

INTERNATIONAL CODE OF ETHICS FOR ASSURANCE PRACTITIONERS (including INTERNATIONAL INDEPENDENCE STANDARDS) (NEW ZEALAND)

Explanation of Decisions made by the NZAuASB in Finalising Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*

Issued December 2018

This document relates to, but does not form part of *Professional and Ethical Standard 1, International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*, which was approved by the NZAuASB in December 2018. It summarises the changes made by the NZAuASB to the *International Code of Ethics for Professional Accountants (including International Independence Standards)* issued by the International Ethics Standards Board for Accountants of the International Federation of Accountants. It also summarises the major issues raised by respondents to Exposure Draft 2018-1 *Professional and Ethical Standard 1, International Code of Ethics for Assurance Practitioners (including International Independence Standards)*, and how the NZAuASB has addressed them.

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INTERNATIONAL CODE OF ETHICS FOR ASSURANCE PRACTITIONERS (including INTERNATIONAL INDEPENDENCE STANDARDS) (NEW ZEALAND)

Explanation of Decisions made by the NZAuASB in Finalising the Amendments

Issued by the New Zealand Auditing and Assurance Standards Board

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BACKGROUND

1. In April 2018, the International Ethics Standards Board for Accountants (IESBA) released a completely rewritten and revamped Code of Ethics. Renamed “International Code of Ethics for Professional Accountants (including International Independence Standards”) (the “International Code”), it packages all substantive advancements in ethics and independence over the last four years into a single document. It includes the new provisions relating to non-compliance with laws and regulations, which are already effective, and the revised independence provisions relating to long association which come into effect in December 2018.
2. In July 2018, the NZAuASB approved for exposure, [ED NZAuASB 2018-1, Professional and Ethical Standard 1, International Code of Ethics for Assurance Practitioners \(including International Independence Standards\) \(New Zealand\)](#), with a 90 day comment period. The ED, based on the International Code, included certain additions for the New Zealand environment, as well as the usual New Zealand terminology and spelling changes.
3. In preparing the ED, the NZAuASB took the opportunity to reconsider whether the compelling reason test continues to be met in respect of previous modifications to the extant International Code. This reconsideration was driven, in part, by responses to the NZAuASB’s Invitation to Comment on [ED NZAuASB 2017-1](#)¹ highlighting concerns about the proposed changes to align the long association provisions for other assurance engagements with the provisions for audit and review engagements. While conceptually respondents agreed that the independence requirements should be the same for all assurance engagements, many questioned whether the compelling reason test is met, given the impact of the long association changes.
4. In applying the compelling reason test to the New Zealand modifications in extant Professional and Ethical Standard 1 (Revised)², the NZAuASB took into account the impact of the recent significant revisions to the International Code, as well as the interactions between the various standards: engagement standards; quality control standards; and the code of ethics.
5. As described in the Invitation to Comment, the NZAuASB determined that the compelling reason test is no longer met with respect to certain extant New Zealand modifications. Accordingly, those paragraphs were not included in the ED. Previously, the NZAuASB had made changes to the International Code on the basis that threats to independence do not differ whether the subject matter of the engagement is financial statements or another subject matter.
6. Submissions were received from two stakeholders. These respondents were generally in support of the ED noting no concerns with the proposal not to include the previous New Zealand paragraphs, but rather to follow the principles of the International Code.

¹ ED NZAuASB 2017-1, Proposed Amendments to PES 1 (Revised) *Provisions Addressing the Long Association of Personnel with an Assurance Client*

² PES 1 (Revised), *Code of Ethics for Assurance Practitioners*

RATIONALE FOR AMENDMENTS MADE TO THE INTERNATIONAL CODE OF ETHICS

7. The NZAuASB has developed this *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)* based on the International Code issued by the IESBA. The NZAuASB applied the [Principles of Convergence to International Standards](#) in developing this standard, and has only amended the International Code where there are compelling reasons to do so. Additional requirements are clearly identifiable as NZ paragraphs and are also described in the conformity with international requirements section at the end of the standard. This Explanation of Decisions made explains the compelling reasons identified by the NZAuASB to amend the International Code.

Scope

8. The NZAuASB's mandate is limited to assurance engagements and therefore the scope of PES 1 differs from the International Code. PES 1 is intended to apply to all assurance practitioners appointed or engaged to provide assurance services. To reflect this New Zealand regulative structure, PES 1 does not include Part 2 of the International Code, *Professional Accountants in Business*, or any references thereto. In addition, Section 321, *Second Opinions*, has been deleted by the NZAuASB as it is not related to the performance of an assurance engagement.

Conflicts of Interest

9. PES 1 includes stricter requirements for dealing with conflicts of interest than the International Code. Paragraph NZ R310.9.1 has been added and paragraphs 310.9 A3 and 310.9 A4 have been deleted. PES 1 always requires the disclosure in writing of the nature of a conflict of interest and related safeguards, if any, to all clients or potential clients affected by a conflict. The International Code states that disclosure is generally necessary.
10. In addition, paragraphs R310.12, 310.12 A1 and R310.13 have been deleted and replaced by NZ R310.12.1 which requires that an assurance practitioner disengage from the relevant assurance engagement if adequate disclosure to the client is restricted as a result of confidentiality requirements. The International Code permits the firm to accept or continue the engagement in limited situations.
11. The NZAuASB recognises that the International Code requirements have a broader application than assurance engagements. The NZAuASB believes that disclosures and a transparent process for handling conflicts of interest are always appropriate for assurance engagements.
12. Managing conflicts of interest in a small country like New Zealand is inevitable and has resulted in stricter requirements than in the International Code. New Zealand best practice has emerged to address these conflicts through the Office of the Auditor-General and guidance issued by the Institute of Directors. New Zealand's best practice has been incorporated into PES 1 which the NZAuASB believes to be appropriate in

the New Zealand context for assurance engagements, and which will promote audit quality.

Referral Fees or Commissions

13. PES 1 contains stricter provisions around accepting or paying referral fees or commissions than the International Code. Paragraphs 330.5 A1 to 330.5 A2 are deleted and replaced with NZ R330.5 and NZ 330.5 A1.1. NZ R330.5 prohibits such fee arrangements. NZ 330.5 A1.1 explains that a fee arrangement in connection with an assurance engagement creates a threat to independence that no safeguards could reduce to an acceptable level. This New Zealand paragraph harmonises with a similar explicit requirement in Australia.

Multiple Threats to Independence

14. PES 1 explicitly requires, in paragraphs NZ R400.12.1 and NZ R900.15.1, that an assurance practitioner evaluate multiple threats to independence identified in aggregate, which individually may not be significant. The International Code includes a reference to the consideration of multiple threats in paragraph 120.8 A1. However, this guidance is not as specific and is far removed from the assurance practitioner's consideration of the threats to independence in sections 400 and 900. This New Zealand paragraph harmonises with the same explicit requirement in Australia.
15. The NZAuASB is of the view that there is a compelling reason to explicitly state this as it provides clarity to assurance practitioners on how to appropriately consider and evaluate threats to independence.

Liquidator or Receiver

16. PES 1 specifically prohibits a firm from providing assurance services to an entity if the partner or an employee of the firm serves as a director or officer of the assurance client, or as a liquidator or receiver of the property of the entity, or in a similar role. The International Code has a similar prohibition, but only in respect of a partner or employee serving as a director or officer of an assurance client.
17. This change to extend the prohibition of undertaking assurance services where the partner or employee of the firm serves as a liquidator or receiver of the property of the entity or a similar roles is consistent with legislative requirements in New Zealand and therefore a compelling reason to include in PES 1.

Application of Part 4A to Prospective Financial Information

18. Part 4A of the International Code applies only to audit and review engagements to report on a complete set of financial statements or on a single financial statement. The NZAuASB believes the nature of assurance provided where the subject matter is prospective information included in any offer document of an issuer and the importance of those services to the broader public interest warrants the same

independence requirements. Accordingly, the scope of Part 4A is extended to apply also to offer documents.

Definitions

19. To reflect the New Zealand business practice and legislative/regulative environment, a number of definitions have been revised and some new definitions have been included. Additional New Zealand definitions are included for assurance practitioner, assurance services, FMC reporting entity considered to have a higher level of public accountability, key assurance partner, and offer document. The defined terms of assurance client, assurance team, audit client proposed assurance practitioner, and public interest entity have been tailored from the defined terms in the International Code.