



# Professional Skepticism

Prof. Annette Köhler, Professional Skepticism Working Group  
(PSWG) Chair

IAASB Meeting, New York

Agenda Item 5

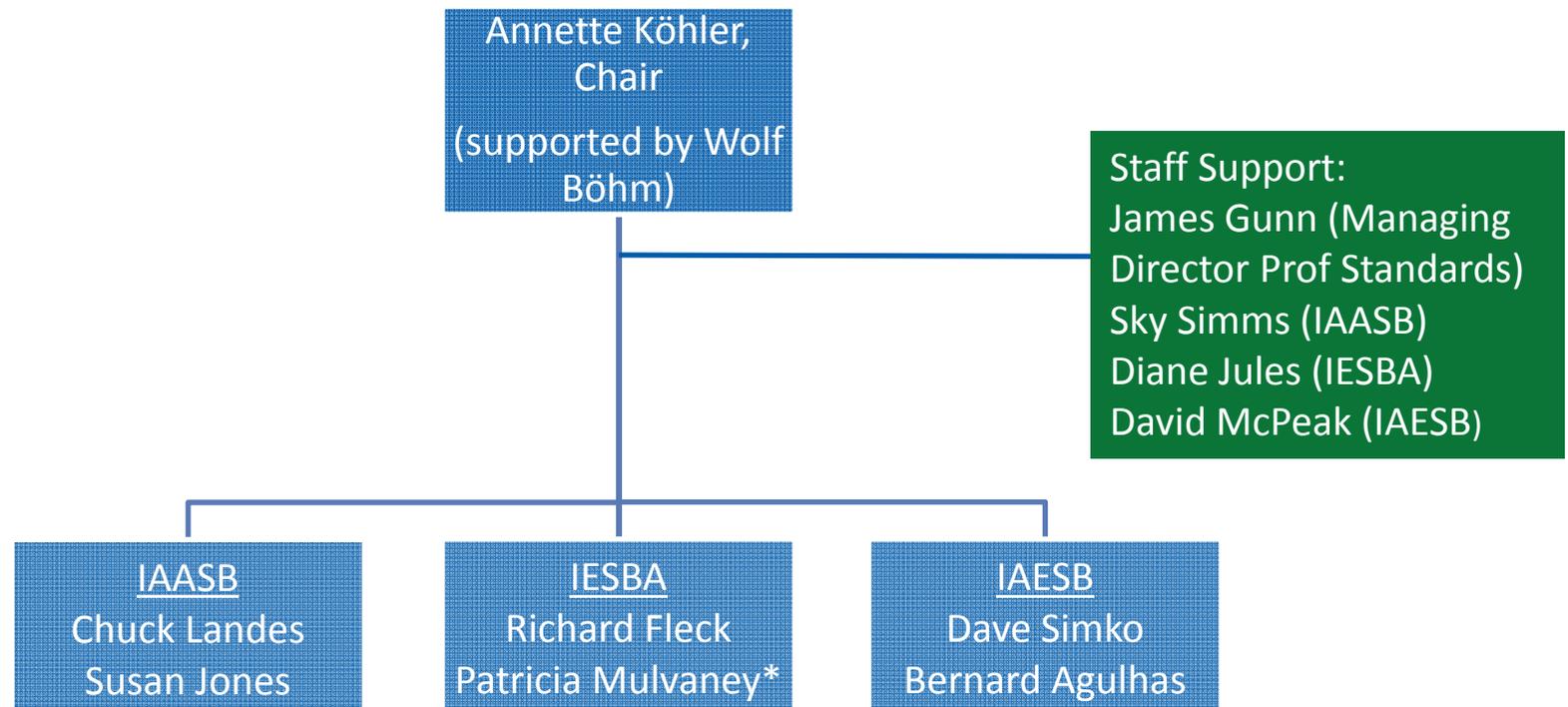
December 7, 2016



## Objectives of the Discussion

- To highlight discussions held by the SSBs and others on the topic of PS (subsequent to the IAASB's September meeting)
  - Highlight discussions of the IAESB's CAG (September 2016) and IAESB (November 2016)
  - Preliminary views from PAIB Committee Outreach
- To inform the IAASB of the PSWG's way forward
  - Joint Professional Skepticism Stakeholder Communication
  - IAASB Subgroup to begin work on an analysis of implications and unintended consequences of potential fundamental changes to the concept of PS within the ISAs
- To receive an update regarding the short-term proposals to be considered by the IESBA next week

## Professional Skepticism Working Group



\* New member

## IAESB September CAG Highlights

- Feedback provided by Representatives of the IAESB CAG was as follows:
  - There should be a consistent definition of PS among the SSBs
  - The concept /definition of PS is not solely an audit concept, but a professional concept that relates to ethical values and applies to all professional accountants
  - The IAESB was intentional when drafting IES4 by using the term “professional skepticism” in order to demonstrate that PS applies to all PAs
  - The IAESB PS Task Force should clearly define the problems/issues they are trying to solve. Only then can solutions be measured against the problem
  - A few CAG members felt the professional skepticism learning outcomes in the IESs are appropriate and suggested that the recently revised IESs should not be changed until a post-implementation review is completed
  - A literature review may be helpful in developing additional implementation guidance, but may not be helpful in solving execution of the standards by auditors

## IAESB November Meeting Highlights

- IAESB members supported the continued coordination of the SSBs and provided the following views with respect to the short-term and longer-term actions related to PS:
  - In the short-term (2017):
    - Support for a literature review and research paper to inform the IAESB’s future decision-making on certain key concepts and the need for future enhancements to the IESs (e.g., behaviors necessary to support the application of PS, completeness of existing learning outcomes)
    - Continue to engage in discussions with the SSBs, the PAIBC, and the SMPC to support expanding the concept of professional skepticism to apply to all professional accountants and explore the benefits and implications of this change
    - Support for monitoring IESBA short-term revisions to the code and assess whether any updates are needed to IES 4 and IES 8
    - Some support to identify education and training good practices designed to create awareness and help professional accountants to apply professional skepticism
  - In the longer-term, the proposed way forward by the Professional Skepticism Task Force:
    - Continue to be engaged in the PSWG
    - Consider the need for additional research to inform on-going decision-making of the IAESB

## PAIB Committee Outreach – Preliminary Views

- As a first step in exploring the implications of fundamental changes to the concept of PS, the Chair of the PSWG presented to the PAIB Committee of IFAC at their September 2016 meeting. Feedback from the Committee was as follows:
  - It is critical that the profession's messaging is not undermined by terminology that implies PAIBs are not part of the profession and do not hold the same professional standards and competence. The need for, and use, of a specific description of PS in the context of assurance engagements does not mean that PS is not applicable to PAIBs
  - The application of PS by PAIBs, particularly in the context of financial statement preparation, makes the work of the auditor easier and is an important part of enhancing audit quality
  - A single narrative of PS for all professional accountants is recommended. However, the current concept of professional skepticism in ISA 200 probably cannot be extended beyond assurance engagements
  - However, PS for PAIBs should not be regulated. Guidance on what PS means and how it might be applied in different professional accountant roles might be useful, for example covering those involved in financial statements preparation and review, but also for other PAIBs such as those involved in planning, forecasting and budgeting, or on boards

## Next steps...A Joint Approach to Feedback

- At its October 2016 physical meeting in Washington DC, the joint PSWG met and discussed several potential ways forward. Two paths were decided...
- **Path #1: The PSWG agreed to develop a joint Professional Skepticism stakeholder communication**
  - Purpose of the document is to give prominence to the work the SSBs will be undertaking, individually and in coordination, and to also highlight the role of others (universities, firms, companies, audit committees, regulators, etc.)
  - The publication will seek to highlight the feedback received from all three SSBs, the impediments (and drivers) to professional skepticism, the linkage to compliance with the fundamental principles, and a “call to action” for others in the financial supporting supply chain
  - Draft outline of this publication will be presented to the IAASB and IESBA at their March 2017 meetings and to the IAESB at its April 2017 meeting

## Next steps...Exploring Fundamental Changes

- **Path #2: The PSWG agreed that given the concept of PS is derived from the ISAs, any potential fundamental changes should first be explored by the IAASB in cooperation with IESBA and the IAESB.**
- To that end, the IAASB Subgroup of the PSWG has begun to explore the implications and unintended consequences of potential fundamental changes to the concept of professional skepticism within the ISAs, including, but not limited to:
  - No definition of PS
  - A shift from a questioning mindset to a more challenging mindset or potentially to presumptive doubt
  - A requirement to seek out contradictory evidence
  - Introducing a concept of levels of professional skepticism rather than the current invariant approach
  - Extension of the concept of PS to all professional accountants

## Matter for IAASB Consideration

The Board is asked to share its preliminary views on the issues raised during this presentation and provide reactions to the planned next steps of the PSWG and the IAASB Subgroup of the PSWG

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## Professional Skepticism

Richard Fleck, IESBA WG Chair

IAASB Meeting

New York

December 7, 2016

## Objective

- To report on
  - IESBA discussion of a PS strawman intended to give greater emphasis on PS in the Code following the IAASB and joint CAG meetings in September 2016
  - A short term (ST) proposal developed by the IESBA PS Working Group for inclusion in the restructured Code which

## Overview of Activities to Date

- September 2016 Joint CAGs and IESBA PS discussion
  - Establishment of an IESBA PS Working Group
- October 2016 PSWG meeting
  - Consideration of, and some support for, proposals for inclusion in the restructured Code
- Upcoming December 2016 IESBA meeting
  - To approve related project proposal
  - To consider proposed text for exposure

## Recap of How PS is Addressed in Standards

- PS is defined in IAASB's standards
  - Applies to PAs who perform audits and other assurance engagements only
- Code only refers to PS as part of description of independence
  - Independence applies to audits and other assurance engagements only
- IAESB standards refer to PS definition in the IAASB's standards
  - PS applies to all PAs, including PAIBs who prepare financial statements

## Overview of Feedback to IESBA about PS (1)

- Information underpinning ethical decisions should be assessed with PS
  - PS is an attitude and public expects all PAs to have it
  - Code should emphasize PS in the same way it does independence
  - Code should address how PS applies to PAIBs
- Linkage between PS and the FPs/ independence should be clarified
  - Drivers and impediments to applying PS and complying with the FPs/ independence requirements are the same

## Overview of Feedback to IESBA about PS (2)

- Important that a coordinated approach be adopted by all SSBs
- Concern that extending PS to all PAs would dilute/conflict with IAASB's standards and its objective to enhance audit quality
- Concern that to extend PS to all accountants might have unintended consequences

## IESBA WG Proposals

- Short term proposals aimed enhancing robustness of the Code include
  - New application material to explain the linkage between PS and the FPs/ independence (for audits and assurance only)
  - New requirement in the conceptual framework for all PAs to apply a critical mindset to achieve compliance with the FPs

Step forward in advance of longer-term discussion about whether PS should apply to all PAs, and whether the IAASB definition of PS should be changed

## New AM – Clarifying Linkage to FPs/ Independence

- Restructured Code to clarify link b/w independence and FPs
  - Opportunity to expand on reference to PS in the Code and explain the linkage between PS and the FPs/ independence of mind
- New AM (applicable for audits and assurance only) explain
  - Except for confidentiality, FPs reinforce PA's ability to apply PS when performing audits, reviews and other assurance engagements
  - How compliance with each FP, other than confidentiality, might reinforce PS
  - Threats to complying with FPs and threats to applying PS are the same

## New Requirement – Applying A Critical Mindset (1)

- Introduces ‘critical mindset’ as a key element of the process by which a PA applies the conceptual framework to achieve compliance with the fundamental principles
- Has the same standing as, and complements the requirements to exercise professional judgment, use the reasonable and informed third party test and to remain alert for changes in the information available
- Further enhances the conceptual framework (i.e., the process for identifying, evaluating and addressing threats)

## New Requirement – Applying A Critical Mindset (2)

- Intended to add a degree of rigor to judgments and conclusions made, because PAs will be required
  - To not simply take information at face value, but rather apply a critical mindset to understand facts and circumstances when identifying, evaluating and addressing threats to compliance with the FPs
  - Think critically when asserting compliance with the FPs while undertaking professional activities
- Does not use term “Professional Skepticism” (or components of definition) to avoid confusion with IAASB standards

## Opportunity for Early Input on Longer Term Activities

- Proposal is a ST measure aimed at enhancing the restructured Code, but might also inform longer term SSBs' discussions about extending the applicability of PS more broadly
- ED questions might seek to understand whether there is support for:
  - New AM to clarify linkage between PS and the FPs/ independence
  - The new requirement to apply a critical mindset
- Feedback on ED might also indicate whether there are some professional activities for which a critical mindset should not be applied

## Small and Medium Practices Committee (SMPC) Feedback

- Emphasized the importance of effective coordination and cooperation between the respective Boards: concern expressed about IESBA-only initiative, potential unintended consequences, coordination implications of fast-track approach unclear
- Is there adequate involvement of the IAASB, specifically as it relates to whether and how the implications for the non-assurance services market have been evaluated and assessed?
  - E.g. AUPs, compilation engagements, other related services engagements
- SMPs are particularly likely to be impacted by any changes ensuing from the initiative in the non-assurance engagements
  - Potential impact on competitiveness in services vs non-“professional accountants”

## Matter for IAASB Consideration

IAASB is asked to consider whether proposals to be considered by IESBA, namely:

- a) New application material in the Code to explain the linkage between PS and the FPs/ independence (for audits and assurance only)
- b) A new requirement for all PAs to apply a critical mindset to achieve compliance with the FPs

are inconsistent with IAASB's standards

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