NEW ZEALAND INSTITUTE OF CHARTERED ACCOUNTANTS

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NOTICE OF DECISION AND ORDER OF THE PROFESSIONAL CONDUCT COMMITTEE

At a meeting of the Professional Conduct Committee ("the Committee) of the New Zealand Institute of Chartered Accountants ("NZICA") held in private on 4 February 2019 in respect of **RICHARD OWEN DEY,** a Fellow Chartered Accountant and licensed auditor of Tauranga ("the Member"), the Committee considered the following matters:

That as a Chartered Accountant in public practice and in relation to a complaint from Jacco Moison on behalf of the Financial Markets Authority ("the Complainant"), the Member:

(1) Performed the audits of four FMC reporting entities[1] when he was not permitted to do so, having been the key audit engagement partner for seven consecutive years, in breach of paragraph 290.149 of PES 1 (Revised) and/or the Fundamental Principles of Objectivity and/or Professional Competence and Due Care and/or Professional Behaviour and/or section 120 and/or paragraphs 100.5(b) and/or 100.5(c) and/or 100.5(e) and/or 130.1 and/or 130.4 and/or 150.1 and/or 280.2 of the Code of Ethics (2014)[2] and/or the conditions applying to licensed auditors prescribed under s 32(1)(b)(i) of the Auditor Regulation Act 2011; and/or

(2) Failed to carry out his role as auditor of Entity D for the financial year ending 31 December 2016 with professional competence and/or due care, in that when performing substantive analytical procedures for revenue and expenses he failed to:

a. comply with the 4-step model as required by ISA (NZ) 520; and/or

b. document appropriate audit procedures and/or obtain appropriate audit evidence as required by ISA (NZ) 230 and/or ISA (NZ) 500,

in breach of the Fundamental Principle of Professional Competence and Due Care and/or paragraphs 100.5(c) and/or 130.1 and/or 130.4 of the Code of Ethics (2014)[3]; and/or

(3) Accepted appointment as auditor and/or commenced performance of the audits of three FMC reporting entities[4] when he was not permitted to do so as he had previously been the key audit engagement partner for eight consecutive years, in breach of paragraph 290.149 of PES 1 (Revised) and/or the Fundamental Principles of Objectivity and/or Professional Competence and Due Care and/or Professional Behaviour and/or section 120 and/or paragraphs 100.5(b) and/or 100.5(c) and/or 100.5(e) and/or 130.1 and/or 130.4 and/or 150.1 and/or 280.2 of the Code of Ethics (2014)[5]; and/or

[1] Entity A, Entity B, and Entity C in respect of the year ending 31 March 2016; and Entity D in respect of the year ending 31 December 2016.
[2] And, as applicable, the equivalent provisions of PES 1 (Revised).
[3] And, as applicable, the equivalent provisions of PES 1 (Revised).
[4] Entity A, Entity B, and Entity C in respect of the year ending 31 March 2017.
[5] And, as applicable, the equivalent provisions of PES 1 (Revised).

(4) Failed to ensure Ingham Mora Limited completed and returned the Annual Survey by the required date and/or notify NZICA of another member's appointment as licensed auditor of three FMC reporting entities[6], in breach of the Fundamental Principles of Professional Competence and Due Care and/or Professional Behaviour and/or paragraphs 100.5(c) and/or 100.5(e) and/or 130.1 and/or 130.4 and/or 150.1 of the Code of Ethics (2014)[7] and/or NZICA's standard conditions applying to firm registration (Corporate Audit Firms) issued under s 28(1) of the Auditor Regulation Act 2011.

The Committee was troubled by the matters raised in the complaint. In particular, the Member's judgement concerning the application of the exception contained within paragraph 290.150 of PES 1 (Revised) and his lack of documentation on the audit file of his consideration and application of the exception. It was also concerned that it appeared that the Member had failed to complete the Annual Survey or notify the NZICA of another member's appointment as auditor of three FMC reporting entities by the required dates.

Particular (1)

In finding particular (1) to be established, the Committee disagreed with the Member's view that the exception contained within 290.150 of PES 1 (Revised) permitted him to remain as key audit partner for an additional year in respect of his audits of Entity A, Entity B, and Entity C for the year ending 31 March 2016; and Entity D for the year ending 31 December 2016.

Paragraph 290.149 expressly required rotation of a key audit partner that had performed the audit of a public interest entity after 7 years. This was to mitigate any actual or perceived long association independence threat to a member's professional scepticism. The Committee noted that independence of both mind and in appearance was necessary to enable an auditor to express a conclusion, and be seen to express a conclusion, without bias, conflict of interest, or undue influence of others. Public interest requires independence not only to be observed, but to be seen to be observed.

The exception contained within paragraph 290.150 enables an audit partner whose continuity is particularly important to the quality of the engagement, in rare cases due to unforeseen circumstances out of the firm's control, to remain as audit partner for an additional year. This is provided safeguards are implemented so as to reduce or eliminate any independence threat to an acceptable level.

The Committee considered the words "rare" and "unforeseen" required a high threshold to be met in order for the exception to become available. In its view exceptional circumstances were required. It noted that the paragraph provided an example of a key audit partner falling ill, suggesting it was not designed to be applied in circumstances involving commercial transactions the subject of negotiation. Though some merger completion scenarios could be described as outside a member's control, commercial demands could make the deal unpalatable to either side at any time. Further, the Committee did not consider that it was unforeseen that a commercial merger involving four audit firms (as was the case in this particular instance) might not eventuate. It was of the view that the Member ought to have been aware of the risk the transaction would not complete, given the complex nature of the negotiations necessary to conclude a four way merger.

[6] Entity A, Entity B, and Entity C in respect of the year ending 31 March 2017.
[7] And, as applicable, the equivalent provisions of the Code of Ethics (2017) and/or PES 1 (Revised).

While in its view the Member had erred in his judgment regarding the application of the exception, it noted that he appeared to have made an honest mistake, and that there was no evidence before it to suggest that he had set out intending to use the exception as a means of remaining the key audit partner in respect of an eighth consecutive year. Given the significance of the judgment made, the Committee considered the Member should have sought legal or other appropriate professional advice regarding application of the exception, or engaged with the regulators on the subject.

The Committee was also concerned by the lack of documentation on the Member's audit files regarding his identification, consideration and application of the exception, particularly so given it was a key judgment call in terms of the audit. While it accepted that the Member wished to keep the merger negotiations confidential from his staff, it considered there were other ways of documenting the matter, such as including a reference on the audit file to a separately held signed and dated confidential document, or by using a project name to anonymise, as far as possible, the details and existence of the potential merger.

Particular (2)

In finding particular (2) to be established, the Committee noted that the Member appeared to accept there were documentation shortcomings in respect of the substantive analytical procedures performed for revenue and expenses.

However, after discussing the matters raised in particular (2) with both the Member and the Complainant, the Committee was of the view that any breach was minor in the context of the complaint overall and did not, when viewed in isolation, meet the threshold to warrant referral to the Disciplinary Tribunal.

Particular (3)

Regarding particular (3), which the Committee considered to be established, the Committee was troubled that it appeared that the Member had accepted appointment as auditor of Entity A, Entity B, and Entity C for the year ending 31 March 2017, prior to formally confirming the contractual arrangement between his firm and another member for the other member to act as engagement partner on the audits. It considered that until the other member had been contractually appointed, the Member remained as the audit engagement partner in circumstances where he was not eligible to perform the engagement.

Notwithstanding that the engagement letters issued in the Member's name on behalf of his firm, dated between 23 May 2017 and 27 June 2017, stated that the other member would be the responsible engagement partner, the other member was not formally contracted by the Member's firm until 17 July 2017.

There was a risk that if the contractual arrangement between the Member's firm and the other member was not able to be concluded, the clients would be left in a compromised position, having not appointed a licensed auditor who could perform the audits. While the Committee noted the contractual arrangement between the Member's firm and the other member was eventually concluded, it considered it unacceptable to take a risk of this nature.

The Committee was not persuaded by the Member's explanation that he had not performed any work in respect of the engagements, despite having signed the engagement letters. While it accepted he may not have performed much substantive work, certain audit procedures are required to be completed ahead of time by the engagement partner. These include acceptance and continuance procedures, assessing the firm's independence, and appointing the

appropriate engagement team to perform the work. In terms of the engagement in respect of Entity B, the Committee noted that the Member's staff had carried out some preparatory work, including performing a stocktake (for which only the Member could be responsible at the relevant time). Given this information, the Committee found it difficult to understand how the Member alleged he had not performed any work in respect of the audit.

Particular (4)

Regarding particular (4), which the Committee noted the Member appeared to accept, while it did not consider the particular, when viewed in isolation, sufficient to meet the threshold to warrant referral to the Disciplinary Tribunal, it was concerned by the matters raised in the particular.

In accordance with NZICA's standard conditions applying to firm registration (Corporate Audit Firms) issued under s 28(1) of the Auditor Regulation Act 2011, audit firms are required to provide NZICA with the information requested as part of the annual disclosure requirements (primarily the information requested in the annual survey); as well as notify NZICA of any change of engagement partner in respect of FMC audits being undertaken by the firm. As at the relevant time the Member was his firm's only licensed auditor, it was primarily his responsibility to do so. He had not done so by the required deadlines.

While it noted his explanation that the delay in submitting the annual survey was, in part, due to the ongoing Quality Review and matters arising out of it, and that he had written to NZICA shortly after the due date explaining this, the Committee considered he should have at least contacted NZICA prior to the deadline expiring and explained this.

In respect of his comments that the FMA was aware of the other member's appointment as engagement partner prior to the deadline within which he was required to notify, the Committee noted that the obligation under the standard conditions was to notify NZICA as the accredited body, not the FMA.

Despite these shortcomings on the Member's part, the Committee was pleased to note that in his subsequent correspondence with NZICA dated 31 October 2017 he had addressed these matters and apologised for the lack of timeliness.

PENALTY

Having regard to the established particulars, the Committee was of the view that, in the round, the complaint met the threshold to warrant referral to the Disciplinary Tribunal. However, the complaint could be appropriately sanctioned by way of a consent order with terms that the Member be severely reprimanded in accordance with Rule 13.7(d)(v); and that he pay costs to NZICA of $4,400.00 in contribution towards the Committee's investigation in accordance with Rule 13.7(d)(vii).

The Committee noted the higher public interest (and higher public expectation) that will generally accompany work undertaken by members who are licensed under the Auditor Regulation Act 2011. That higher public interest will often see license holders found to have breached auditing standards referred to the Disciplinary Tribunal under Rules 13.7(d)(x) and 13.7(e). By a fine margin, the Committee considered such a referral was not necessary on this occasion.

The Committee considered that the sanction above would be a proportionate response to the breaches of the Code of Ethics identified. It noted that it was appropriate for members to pay

a contribution towards the Committee's costs, as otherwise such costs are borne by the wider membership.

PUBLICITY

The Committee determined that it was in the public interest that notice of its decision and orders made be published in CA ANZ's official publication *Acuity*, and on its website with mention of the Member's name and location. The Committee considered that it was appropriate, and in the interests of the pubic and wider membership, for there to be transparency as to its decision and to understand the types of conduct dealt with in this complaint. It was also broadly consistent with recent complaints involving breaches of auditing standards by licensed auditors.

The Committee also determined that pursuant to its obligation under s 42 of the Auditor Regulation Act 2011, and in accordance with Rule 13.75 of NZICA's Rules, notice of its order would be provided to the Companies Office Registrar.

MEMBER'S OPPORTUNITY TO CONSIDER THE ORDER

Written notice of the proposed consent and publicity orders were provided to the Member in writing in accordance with Rule 13.8, and he was given 15 days to consider them and take any advice he wished to. After taking legal advice, the Member confirmed his agreement to the Committee's order.

Rob Pascoe FCA
Chairman
Professional Conduct Committee

27 March 2019