

Institute of Chartered Accountants of New Zealand

ADVISORY ENGAGEMENT STANDARD 1

OPINIONS ON ACCOUNTING AND REPORTING MATTERS

Issued by the Council of the Institute of Chartered Accountants of New Zealand

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Introduction

Purpose of Standard

- 1 The purposes of this Standard are to outline procedures to be followed by members when approached to provide opinions on accounting and reporting matters, and to outline reporting requirements.

Background

- 2 Generally accepted accounting practice (GAAP) and applicable financial reporting standards evolve in response to changing economic conditions and to new transactions and financial products. As diverging views may arise on how to apply GAAP or the applicable financial reporting standards in a particular set of circumstances, various people, such as management, accountants and others, may consult with members on the application of GAAP or the applicable financial reporting standards. Such consultations are useful because they may provide information and insights not otherwise available.
- 3 When the opinion of a member (the advising member) is sought on an accounting or reporting engagement issue by or on behalf of an entity that is not an existing client, there is a danger that the opinion the advising member expresses may not be based on the same facts available to the entity's incumbent member, such as an auditor, engaged to perform reporting engagements. The opinion the advising member expresses may also be based on inadequate knowledge of the facts and circumstances and the opinion may be difficult to modify if further facts become apparent. An advising member should be alert to possible undue pressure on the judgement and objectivity of an incumbent member, and should accordingly seek to minimise the risk of giving inappropriate guidance because of limited knowledge of facts and circumstances.

Applicability

- 4 **This Standard applies when a member is requested to provide, or provides:**
 - (a) **a written opinion where the primary purpose of that opinion relates to the application of GAAP or applicable financial reporting standards to a specific set of circumstances (or on a transaction either completed or contemplated) for an entity for which the member is not the incumbent member; or**
 - (b) **a written generic opinion where the primary purpose of that opinion relates to the application of GAAP or reporting engagement standards.**
- 5 This Standard does not apply to:
 - (a) an opinion provided pursuant to litigation involving accounting, reporting engagement matters or expert testimony in connection with such litigation;
 - (b) the usual work of liquidators, receivers and trustees in bankruptcy;
 - (c) the inspection or disciplinary processes of the Institute of Chartered Accountants of New Zealand;
 - (d) assistance provided to an incumbent member in reaching a position on an accounting or reporting engagement matter;
 - (e) assistance provided to an advising member in reaching a position on an accounting or reporting engagement matter, provided the advising member agrees not to refer to such assistance in any opinion provided or position taken;
 - (f) the processes of a regulatory authority in reaching its position on an accounting or reporting engagement matter, including any assistance or expert testimony provided in connection with such processes, provided that the regulatory authority agrees not to refer to such assistance in any opinion provided or position taken;
 - (g) an opinion intended for publication or communication in the public domain; or

- (h) opinions expressed by members of an entity's governing body or employees of an entity in relation to the accounting or general purpose financial reporting of the entity.
- 6 Compliance with this Standard is mandatory in terms of paragraph 130.1(b) of the *Code of Ethics*. Failure to observe this Standard may expose a member to disciplinary action.
- 7 Mandatory provisions are paragraphs in bold type-face in this Standard. Where appropriate, interpretative guidance or commentary paragraphs in plain type-face follow the mandatory provisions.

Effective Date

- 8 **This Standard applies to opinions on accounting and reporting matters sought on or after 1 January 1997.**

Definitions

- 9 For the purpose of this Standard, the following terms have the meanings specified:

Advising member means a member providing an opinion on the application of generally accepted accounting practice or applicable financial reporting standards.

Applicable financial reporting standard means a financial reporting standard that applies to the entity and to the accounting period.

Entity means an organisation, including its subsidiaries and associates, or an intermediary acting on the organisation's behalf, for which the advising member does not have an ongoing professional relationship to provide reporting engagement services.

Generally accepted accounting practice (GAAP); financial statements, group financial statements, a report, or other information complies with GAAP only if the report, statements, or other information complies with applicable financial reporting standards.

Generic opinion means an opinion on the application of generally accepted accounting practice or applicable financial reporting standards not involving the specific facts or circumstances of a particular entity.

Incumbent member means a member with an ongoing professional relationship to provide reporting engagement services for an entity.

Third party means a party other than the entity, advising member or incumbent member.

Advisory Engagement Standards

General Principles Relating to an Advisory Engagement

- 10 **The advising member must comply with the *Code of Ethics*.**
- 11 In particular, the *Code of Ethics*, contains the Fundamental Principles which guide members of the profession in the performance of their professional responsibilities and express the basic tenets of ethical and professional conduct. The Fundamental Principles are:
- Integrity;
- Objectivity;
- Professional Competence and Due Care;
- Confidentiality; and
- Professional Behaviour.
- 12 **Where an advising member expresses an opinion, the member must be, and appear to be, free of any interest which might be regarded, whatever its actual effect, as being incompatible with integrity and objectivity.**
- 13 [Deleted].

Performance of an Advisory Engagement

- 14 The advising member must plan the advisory engagement work so that the engagement will be performed in an effective manner.**
- 15 The advising member must plan and perform the engagement with an attitude of professional scepticism.**
- 16 The advising member must document matters which are important in providing evidence to support the opinion given and in providing evidence that the engagement was carried out in accordance with the Advisory Engagement Standards.**

Nature and Terms of the Engagement

- 17 The advising member must seek a written understanding and agreement with the party engaging the advising member as to the nature of the engagement, the information to be provided to the advising member, the type of report to be issued, and any restriction on the distribution or use of the report. The terms of the advisory engagement must be recorded in an advisory engagement letter, or other suitable form, and be communicated to the party engaging the advising member.**

Performance Standards and Procedures

- 18 When providing an opinion in accordance with this Standard, the advising member must obtain sufficient information on the circumstances or transactions.**
- 19 The advising member should obtain an understanding of the form and substance of the circumstances or transactions. For situations involving specific circumstances or transactions, most of the appropriate information can be provided by the entity and the incumbent member. Corroboration of the relevant facts and assumptions by the incumbent member may provide sufficient evidence of the completeness and accuracy of the relevant facts and assumptions.
- 20 When providing an opinion in accordance with this Standard, the advising member must ensure that the opinion is prepared using an appropriate basis.**
- 21 The advising member should identify applicable generally accepted accounting practices or applicable financial reporting standards. It may also be necessary to perform further procedures such as consulting with other professionals or specialists, or identifying and considering analogous situations and appropriate precedents.

An Opinion on Specific Circumstances or Transactions Requested by an Entity

- 22 When requested by an entity to provide an opinion on a specific set of circumstances or on a transaction either completed or contemplated, the advising member must:**
 - (a) obtain written permission from the entity to contact the incumbent member. Unless the permission is obtained, the advising member must not accept the engagement;**
 - (b) obtain from the entity a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements between the entity and the incumbent member or a third party; and**
 - (c) contact the incumbent member to confirm that the information provided by the entity is complete and consistent with the incumbent member's knowledge, if any, of the circumstances or transactions.**

An Opinion on Specific Circumstances or Transactions Requested by a Third Party

- 23 When requested by a third party to provide an opinion on a specific set of circumstances or on a transaction either completed or contemplated, the advising member must:**

- (a) **obtain written permission from the:**
 - (i) **third party to contact the entity;**
 - (ii) **third party to contact the incumbent member; and**
 - (iii) **entity to contact the incumbent member.**

Where this permission is not obtained and the third party is in a position to significantly influence the appointment of the entity's incumbent member, the advising member must not accept the engagement. In all other circumstances where this permission is not obtained this will constitute a limitation on scope which must be referred to in the advising member's opinion to the third party;

- (b) **obtain from the third party a written statement of all relevant facts and assumptions known to the third party, and a description of the circumstances and the nature of any relevant disagreements between the third party and the entity or the incumbent member; and**
 - (c) **If permitted by the third party, contact the entity and the incumbent member in writing to confirm that the information provided by the third party is complete and consistent with their knowledge, if any, of the circumstances or transactions.**
- 24 In responding to a request from a third party, circumstances may arise which limit the information available to the advising member. For example:
- (a) the entity may choose not to confirm all relevant facts and assumptions or to preclude the advising member from contacting the entity's incumbent member; or
 - (b) the third party may preclude the advising member from contacting the entity or the incumbent member.

In such circumstances before proceeding with the engagement, and provided that the third party is not in a position to significantly influence the appointment of the entity's incumbent member, the advising member should consider carefully whether the information available is sufficient to result in a meaningful report. If the advising member decides that a meaningful report can be provided based on the available information, the report would include a reservation of opinion for the limitation on scope.

A Generic Opinion

- 25 **When requested to provide a written generic opinion, or when providing a written generic opinion, the advising member must obtain a written statement of the relevant facts and assumptions from the person or entity requesting the opinion.**
- 26 A generic opinion does not deal with the specific facts or circumstances of a particular entity. Rather, it deals with items such as new transactions, products or financial instruments. For example, a financial institution might request a generic opinion for use when marketing a new financial product or service.
- 27 An advising member should be aware that the circumstances relating to a generic opinion engagement may change and give rise to a specific opinion engagement. Before accepting a change in the nature of the engagement, the member should be aware of the consequences of the proposed change and any new requirements placed on the member as a result of that change.

Advisory Engagement Report

- 28 **The advising member's report must:**
- (a) **describe the nature of the engagement;**
 - (b) **state that the engagement was performed in accordance with New Zealand Advisory Engagement Standard No. 1 *Opinions on Accounting and Reporting Matters*;**

- (c) **include or refer to a statement of relevant facts and assumptions, and the source of the information;**
 - (d) **express an opinion on the appropriate generally accepted accounting practices or applicable financial reporting standards to be applied to the matters described in the statement of relevant facts and assumptions, and refer to available authoritative support and supporting rationale;**
 - (e) **state either:**
 - (i) **that the responsibility for the proper accounting treatment rests with the preparers of the financial report, who should consult with the incumbent member; or**
 - (ii) **that the responsibility for a final assessment on the application of applicable financial reporting standards in the particular circumstances rests solely with the incumbent member;**
 - (f) **state that the opinion is based on the facts and assumptions provided and may not apply if there is a change or discrepancy in those facts or assumptions;**
 - (g) **disclose the addressee, the name of the advising member, the date of the report and the place of issue; and**
 - (h) **when applicable:**
 - (i) **identify hypothetical transactions;**
 - (ii) **state any limitations on the application of the opinion; and**
 - (iii) **state any limitation on the scope of the engagement such as the inability to obtain the response of the entity or the incumbent member, or any other restriction in obtaining necessary facts.**
- 29** A generic opinion may be used subsequently as support for a particular treatment in a financial report or for the application of applicable financial reporting standards. As a generic opinion does not deal with the specific facts or circumstances of a particular entity, such use may not be appropriate and it is important for this caution to appear in the report.
- 30** Circulation of an advising member's proposed report to the other parties involved is encouraged as a means of promoting an atmosphere of open and direct discussion between the parties involved.
- 31** **When the terms of the engagement restrict distribution of the report, such a restriction must be disclosed in an additional paragraph of the report.**

Appendix 1

Comparison of AES-1 with International and Australian Standards

This appendix, which was prepared as at 30 September 1996 and deals only with significant differences, is produced for information purposes and does not form part of the standards in AES-1.

There is no corresponding International Standard on the provision of opinions on accounting and reporting matters. However, limited guidance is contained in the International Federation of Accountants (IFAC) *Code of Ethics for Professional Accountants*.

AES-1 is consistent in all material respects with the guidance contained in the IFAC *Code of Ethics* except that the IFAC Code requires the advising member to provide a copy of the final report to the incumbent member. AES-1 contains no such requirement. AES-1 encourages the circulation of the advising member's proposed report as a means of promoting open and direct discussions between the parties involved. AES-1 requires that where the terms of the engagement restrict distribution of the report, such a restriction shall be disclosed in the advising member's report.

There is no corresponding Australian Standard on the provision of opinions on accounting and reporting matters. However, limited guidance is contained in the following Australian promulgations; Rules of Ethical Conduct No. 3 (REC 3): *Professional Appointments*, issued by the Institute of Chartered Accountants in Australia, and AUP 32 *Audit Independence*, issued by the Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants in Australia.

AES-1 is consistent in all material respects with the requirements in REC 3 except that REC 3's requirement for the advising member to contact the incumbent member is limited only to advising them of the request by the entity or third party. AES-1 imposes additional requirements on the advising member to confirm the facts provided by the entity or third party with the incumbent member.

AES-1 is consistent in all material respects with the guidance contained in AUP 32 except for the following matters:

- (a) AUP 32 provides authoritative guidance only. AES-1 establishes mandatory principles and procedures that must be followed by members engaged to provide opinions on accounting and reporting matters.
- (b) AUP 32 states that the incumbent auditor should have the right to comment to the governing body and/or audit committee on the opinion provided by the advising member. AES-1 makes no comment on this matter.

Appendix 2

Examples of Advisory Engagement Reports

Note: This appendix is included for illustrative purposes only and does not form part of the standards in AES-1.

Example A

Opinion provided to an entity on a specific transaction

To [governing body engaging the advising member]

I have been engaged to report on the appropriate application of generally accepted accounting practice to the transaction described below. This report is being issued to assist the governing body to evaluate the accounting treatment for the described transaction. My engagement has been conducted in accordance with Advisory Engagement Standard No. 1 *Opinions on Accounting and Reporting Matters* issued by the Institute of Chartered Accountants of New Zealand.

I have been provided with the following facts and assumptions concerning the transaction.

[describe the transaction and relevant facts and assumptions provided by the entity]*

In my opinion, the appropriate accounting treatment to be applied to the transaction described above is as follows.

[describe how the transaction should be accounted for]

My opinion is based on the following authoritative support and other supporting rationale.

[set out and discuss authoritative support and supporting rationale]

The ultimate responsibility for the decision on the appropriate application of generally accepted accounting practice for the transaction described above rests with the governing body who, as preparer of the financial report should consult with its auditor (or other incumbent member). My judgement on the appropriate application of generally accepted accounting practice for the transaction described above is based on the facts and assumptions provided to me. Should the facts or assumptions described above differ from the actual circumstance, my opinion may not be applicable to those circumstances.

[Signed].....

Chartered Accountant Date

* Alternatively, refer to an attached statement of facts and assumptions.

Example B

Opinion provided to a third party on a specific transaction when the entity and its incumbent member choose not to confirm all relevant facts

To [person engaging the advising member]

I have been engaged to report on the appropriate application of generally accepted accounting practice to the transaction of (name of entity) described below. This report is being issued to assist you to evaluate the accounting treatment for the described transaction. Except as explained below, my engagement has been conducted in accordance with Advisory Engagement Standard No. 1 *Opinions on Accounting and Reporting Matters* issued by the Institute of Chartered Accountants of New Zealand.

You have provided me with the following facts and assumptions concerning the transaction.

[describe the transaction and known relevant facts and assumptions provided by the third party]*

Neither [name of entity] nor its auditor [or other incumbent member] was prepared to fully discuss this matter or confirm the facts. If they had done so, it is possible other facts would have come to my attention that would have caused me to arrive at a different opinion.

In my opinion, apart from revisions, if any, which I might have determined to be necessary had I been able to discuss the matter and confirm the facts with [name of entity] and its auditor [or other incumbent member], the appropriate accounting treatment to be applied to the transaction described above is as follows.

[describe how the transaction should be accounted for]

My opinion is based on the following authoritative support and other supporting rationale.

[set out and discuss authoritative support and supporting rationale]

The ultimate responsibility for the decision on the appropriate application of generally accepted accounting practice for the transaction described above rests with the entity's governing body who, as preparer of the financial report should consult with its auditor (or other incumbent member). My judgement on the appropriate application of generally accepted accounting practice for the transaction described above is based on the facts and assumptions provided to me. Should the facts or assumptions described above differ from the actual circumstances, my opinion may not be applicable to those circumstances.

[Signed].....

Chartered Accountant Date

* Alternatively, refer to an attached statement of facts and assumptions.

Example C

Generic opinion

To [person engaging the advising member]

I have been engaged to report on the appropriate application of generally accepted accounting practice to the hypothetical transaction described below. This report is being issued to assist you to evaluate the accounting treatment for the described hypothetical transaction. My engagement has been conducted in accordance with Advisory Engagement Standard No. 1 *Opinions on Accounting and Reporting Matters* issued by the Institute of Chartered Accountants of New Zealand.

You have provided me with the following facts and assumptions concerning the hypothetical transaction.

[describe the hypothetical transaction and known relevant facts and assumptions provided by the person or entity requesting the opinion]*

In my opinion, the appropriate accounting treatment to be applied to the hypothetical transaction described above is as follows.

[describe how the hypothetical transaction should be accounted for]

My opinion is based on the following authoritative support and other supporting rationale.

[set out and discuss authoritative support and supporting rationale]

The application of this opinion to a particular entity may not be appropriate as it does not deal with the facts or circumstances of that entity.

The ultimate responsibility for the decision on the appropriate application of generally accepted accounting practice for an actual transaction rests with the entity's governing body who, as preparer of the financial report should consult with its auditor (or other incumbent member). My judgement on the appropriate application of generally accepted accounting practice for the hypothetical transaction described above is based on the facts and assumptions provided to me. Should the facts or assumptions described above differ from the actual circumstances, my opinion may not be applicable to those circumstances.

[Signed].....

Chartered Accountant Date

* Alternatively, refer to an attached statement of facts and assumptions.