CHARTA LEARNING · INTERVIEW PREPARATION

Ethics, Independence and Professional Scepticism

Interview preparation summary · AU track

IN THIS SUMMARY

- Principles
- Judgement in the room

INT.UI.1.a · Principles

State the five fundamental principles of professional ethics, say what each asks of a trainee in practice, and apply them to a simple situation.

Codes of ethics for accountants, which in many jurisdictions follow an international model, rest on five fundamental principles. Integrity means being straightforward and honest, and not being associated with information you know is misleading. Objectivity means not letting bias, conflicts of interest or the influence of others override your judgement. Professional competence and due care means keeping your knowledge current, acting diligently and not accepting work you cannot do properly or without proper supervision. Confidentiality means not disclosing or using client information without authority, unless the law or a professional right or duty requires or permits it. Professional behaviour means obeying the law and avoiding conduct that would discredit the profession. For a trainee these show up in small, checkable things: accurate timesheets, ticking only what you actually tested, asking when you do not understand, and not discussing a named client on a train. Interviewers ask because audit relies on trust and trainees do much of the fieldwork. The usual mistake is to recite the five names with no example. Pick one situation and say what you would do.

WORKED EXAMPLE: AN HONEST TIMESHEET AT DUNMORE FABRICS

Dunmore Fabrics is an invented textile manufacturer. You were given a budget of 40 hours for the payroll section. By Friday you have worked 52 hours because the payroll listing arrived late and had to be re-requested twice. Your senior says: just put 40, the budget is what the manager wants to see. Decide what you do. Convention: overrun is measured against the budget.

Answer: Record the true 52 hours, which is 12 hours or 30.0% over budget, and explain that late payroll data caused it. Recording 40 would be a false record, an integrity and professional behaviour failure, and would hide a cause the manager needs to see.

> **Interview tip:** Give the principle in one phrase, the number, and what you would say to the senior. Sound calm and practical, not rule-quoting.

INT.UI.1.b · Principles

Name the five threats to the fundamental principles, give an example of each, and explain how safeguards are chosen and when none is enough.

Ethics codes group the dangers to the fundamental principles into five threats. Self-interest arises when a financial or other interest of the firm or an individual could influence judgement, for example heavy dependence on one client's fees. Self-review arises when the firm must evaluate its own earlier work, for example auditing accounts the firm helped prepare. Advocacy arises when the firm promotes a client's position so strongly that objectivity suffers. Familiarity arises when a close or long relationship makes the auditor too sympathetic or too trusting. Intimidation arises when actual or perceived pressure, such as a threat to replace the auditor, deters objective action. The method is the same for each: identify the threat, judge whether it is significant by asking whether a reasonable and informed third party would conclude compliance is compromised, then apply safeguards that remove it or reduce it to an acceptable level. Examples are a second partner review, different teams, rotating people, or declining the work. Safeguards reduce threats; they do not make every threat acceptable. Candidates often label the threat and stop. Always finish with what you would do.

WORKED EXAMPLE: FEE DEPENDENCE AT MARLOW RETAIL

Marlow Retail is an invented chain and an audit client. Your firm's total annual fee income is 12.0m. Marlow pays 2.4m a year in audit and other fees. The engagement partner has a personal portfolio of clients worth 4.0m in fees, of which Marlow is the 2.4m. The firm's own policy, assumed here for illustration, treats any client above 15.0% of firm fee income as needing a documented safeguard review. Decide which threat arises and what you would recommend.

Answer: Marlow is 20.0% of firm fees, above the 15.0% policy level, and 60.0% of the partner's portfolio. The threat is self-interest, with some intimidation risk. Use an independent second partner review, an annual fee review and disclosure to those charged with governance, and keep watching the percentage.

> **Interview tip:** Name the threat, show you can size it with a percentage, then name a safeguard and say when you would walk away.

INT.UI.1.c · Principles

Explain independence of mind and independence in appearance, say how non-audit services and long association affect it, and test a fee ratio against a limit.

Independence has two parts. Independence of mind is the state of mind that lets the auditor give an opinion without being affected by influences that compromise professional judgement. Independence in appearance is avoiding facts and circumstances so significant that a reasonable and informed third party would doubt the firm's integrity, objectivity or scepticism. Threats include financial interests in the client, loans, close family in key client roles, recently joining the client, gifts and hospitality, and long association of the same senior people with the same client. Non-audit services need care. Bookkeeping or valuation work by the audit firm creates a self-review threat, and taking decisions for management is not acceptable. Tax compliance, by contrast, is often permitted with safeguards. Rules are usually stricter for listed and other public interest entities, and may include prohibited services, fee limits and rotation of key partners, but practice varies by jurisdiction. The auditor normally discusses these matters with those charged with governance. Weak answers say independence means owning no shares. Good answers cover appearance, services, fees and relationships, and say what is decided case by case.

WORKED EXAMPLE: NON-AUDIT FEES AT CALDER ENERGY SERVICES

Calder Energy Services is an invented listed company. Audit fees for the last three years were 0.80m, 0.82m and 0.85m. This year the firm is asked to provide non-audit services costing 0.60m. Assume, for illustration, a limit that total non-audit fees in a year must not exceed 70.0% of the average audit fee of the last three years. Decide whether the proposal is within the limit and what to do.

Answer: The limit works out at 0.5763m and the proposal is 0.60m, so it is 0.0237m over and must be reduced or declined. Then consider whether any service creates a self-review threat, and discuss the position with those charged with governance.

> **Interview tip:** Say that the ratio is a screen, not the whole answer, and that the nature of each service matters as much as the total.

INT.UI.2.a · Judgement in the room

Distinguish professional scepticism from cynicism, and show how an auditor challenges a management estimate with evidence instead of trust or suspicion.

Professional scepticism is a questioning mind, alertness to conditions that may indicate misstatement from error or fraud, and a critical assessment of evidence. It does not mean assuming management is dishonest, and it does not mean assuming it is honest. Cynicism is the opposite error: rejecting evidence automatically, treating every answer as a lie, and wasting time and goodwill. Typical pressures that weaken scepticism are a friendly client, an experienced finance director, last year's file saying no problem, a senior's view, and the clock. The practical method is to ask what would have to be true for the explanation to be right, and then look for independent evidence that it is. For an estimate that means comparing it with past outcomes, with external data and with other parts of the audit, looking at the range of reasonable values, and noting which way the errors always fall. Document the challenge and the answer. In an interview, avoid both I would trust management and I would never believe them. Say that you would ask a polite, specific question and then test the answer.

WORKED EXAMPLE: SLOW-MOVING STOCK PROVISION AT HARTWELL GARDEN SUPPLIES

Hartwell Garden Supplies is an invented retailer with inventory of 8.0m. Management has provided 3.0% of inventory for slow-moving lines. In the last three years the write-offs on that kind of stock, measured as a percentage of year-end inventory, were 5.8%, 6.5% and 6.3%. Overall materiality is 0.40m and performance materiality is 0.20m. Management says the new supplier returns scheme will cut write-offs. Decide how to respond. Convention: use the three-year figures as the benchmark.

Answer: Management's provision is 0.24m against a benchmark of 0.496m, a gap of 0.256m, above performance materiality. The returns scheme is a plausible reason but not yet evidence, so ask for the contract, test coverage and post year-end returns before accepting or proposing an adjustment.

> **Interview tip:** Show that you neither accept the explanation nor dismiss it. Say what evidence would change your mind.

INT.UI.2.b · Judgement in the room

Explain how to respond to pressure from a client or a senior, and how to handle a conflict of interest or a confidentiality dilemma, with a clear next step.

Pressure in audit rarely looks like a threat. It sounds like: we are out of time, the bank needs the accounts this week, every other auditor has accepted this, or you are being difficult. Pressure may come from the client, who may want a result or a date, or from a senior or manager worried about budget. The auditor's response is to stay polite, restate what evidence or correction is needed and why, raise it up the team if it continues, and record what was agreed. A motive such as a bonus tied to profit makes a misstatement more serious, because intent and bias matter as well as size, so a list of small items may be significant in total. Conflicts arise when the firm or a person has interests that clash, such as acting for two clients in dispute; the answer is to identify them early, involve the ethics partner, and use separate teams and consent only where that really manages the risk, otherwise decline. Confidentiality gives way only where law requires or permits disclosure, so take advice first. Do not promise secrecy you cannot keep.

WORKED EXAMPLE: UNADJUSTED ITEMS AND A BONUS AT BRIGHTWATER COMPONENTS

Brightwater Components is an invented manufacturer. Draft profit before tax is 6.35m. The finance director's bonus is payable only if profit before tax is at least 6.00m. The audit has found four uncorrected misstatements that each overstate profit: a cut-off error of 0.20m, an under-accrual of 0.11m, repairs wrongly capitalised of 0.09m and an inventory error of 0.07m. Overall materiality is 0.40m. The finance director asks you to waive all four because each is below materiality. Decide what the audit team should say.

Answer: Together the items are 0.47m, over materiality of 0.40m, and they lift profit from 5.88m to 6.35m across a 6.00m bonus threshold. They cannot be waived as a group. Request correction of all four, escalate to the manager, and report to those charged with governance if management refuses.

> **Interview tip:** Say that size is not the only test. A motive turns small errors into a real concern, and you escalate calmly without accusing anyone.

INT.UI.2.c · Judgement in the room

Work through a short ethics scenario in a clear order, and explain how to raise a concern and what whistleblowing protection usually means.

A short ethics scenario is best handled in a fixed order. First establish the facts: what do I actually know, and what am I assuming? Then name the principles and threats involved. List the options, including doing nothing, and think through what each leads to. Consult someone: the senior or manager on the engagement, the firm's ethics partner or a confidential helpline. Decide and act, then document what you did and why. Start with your own engagement line unless the concern is about that line, in which case go directly to the ethics route. Do not investigate on your own, accuse anyone, or discuss the matter outside the firm. In many jurisdictions the law protects people who raise genuine concerns in good faith, and also imposes duties to report some matters, such as suspected money laundering, with a ban on tipping off the person concerned; the details differ, so say you would take advice. A common mistake is to say I would report it to the regulator at once. Interviewers want to hear internal escalation first, calm and factual, with a record kept.

WORKED EXAMPLE: A SIGN-OFF THAT DOES NOT MATCH THE FILE AT PELLAM BREWING

Pellam Brewing is an invented client. A fellow trainee has signed a fixed asset working paper saying that 25 additions were agreed to supplier invoices. The file holds only 17 invoices. Total additions are 3.2m, and the 17 invoices on file cover 0.91m. Your senior has asked you to finish the cross-reference of the schedule. Decide what you do. Convention: measure coverage by value against total additions.

Answer: Eight of 25 items, 32.0%, lack invoices and the 17 on file cover only 28.4% of additions by value. Ask the colleague neutrally first. If it is not resolved quickly, give your senior the facts. Do not complete the cross-reference, change the sign-off or investigate alone.

> **Interview tip:** Show a calm sequence: facts, a neutral question, escalation, a record. Avoid language that accuses a colleague of dishonesty.

Summary of the Charta interview-preparation topic. Companies and figures in the examples are invented. Draft content, not yet expert reviewed.