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30 August 2013

Dear Doug,

Response to Consultation Paper 209 (CP 209): Resignation, removal and replacement of auditors

We appreciate the opportunity to comment on the proposed update to Regulatory Guide 26 (RG 26) on the resignation, removal or replacement of auditors. We welcome ASIC's consultation on this area of legislation which is complex and therefore, at times, difficult for entities and auditors to effectively navigate.

We support a fundamental change in Australia's approach to the resignation, removal or replacement of auditors to simplify the current process.

We believe that simplification of this process, including potentially removing ASIC's responsibilities regarding the approval of a change in auditor, is appropriate for the following reasons:

- *International alignment of auditor regulation*
  As set out in the Appendix to CP 209 Canada, the European Union, the United Kingdom and the United States do not require regulator consent to auditor resignations and removals. Further, we note that the UK Competition Commission recently stated[1] that they were minded not to give their regulator responsibility for auditor replacement. Therefore, other jurisdictions do not consider regulator involvement necessary to effective market operation and instead require appropriate disclosure to the market and regulators as part of the change in auditor framework. Government has sought to align auditor regulation to international developments, where appropriate, and this provides an opportunity for further alignment.

[1] The Competition Commission published a provisional decision regarding the remedies it is considering introducing when it publishes its final report on the supply of statutory audit services to large companies in the United Kingdom later in the year. Refer paragraph 17(d) of the Summary of Provisional Decision on Remedies.

Moreover, we believe that ASIC's role is inconsistent with the principles of corporate governance which acknowledges the important role those charged with governance, or in many cases the audit committee plays in the auditor appointment and selection process. The fact that ASIC has a right to veto, is in our view, inconsistent with this principle.

- *Better reflection of changes to Auditor independence and professional standards*
  As noted in CP 209.3 there have been significant legislative amendments since RG 26 was published, including giving compliance with auditing standards and APES 110 *Code of ethics for professional accountants* ("APES 110") the force of law and the requirement for auditors to provide an independence declaration.

  This has strengthened the independence framework in Australia and also created obligations for auditors which render elements of the current RG 26 in conflict with current legal and professional requirements (refer Appendix 1, for our comments on your Tables 2 and 3 for examples).

  We believe that the legislation and ASIC's application of the legislation for changing auditors should now change to recognise the new environment in which auditors' operate.

- *Reduction in red tape for business*
  The current system is complex, with different auditor appointments (e.g. public companies, private companies, registered schemes, AFSL's etc.) subject to different requirements and timings. This creates confusion in the marketplace and clients are unable to use the auditor they believe best meets their needs because they were unaware of the complex timing requirements.

Whilst we recognise that a fundamental change in the process may not be a legislative priority for Treasury at this time we believe that the Treasury should consider abolishing ASIC's responsibilities regarding the approval of a change in auditor. As this requires legislative change, we recommend that roundtables be held to discuss possible options.

We have provided our detailed comments on the draft RG 26 in the attached appendix and would also like to make the following high level comments in regards to draft RG26:

- *Compliance with the independence requirements*
  We are concerned that under the draft RG 26 ASIC has the power to refuse an auditor's consent to resign and effectively override the auditor's assessment of their independence.

- *Compliance with other ethical obligations and auditing standards*
  We are concerned that the rationale cited by ASIC, that is, that they "ensure the independence of auditor is not affected by the existence of an unresolved decision during the completion of the audit process" does not appropriately recognise an auditor's legal and ethical obligations, which include to conduct an audit in accordance with auditing standards. The auditing standards and professional requirements require rigorous continuance processes. It is the auditor's responsibility to comply with these requirements and should not be subject to concurrence by the regulator.

- *Inconsistency between the requirements*
  As drafted, RG 26 recommends that in all instances the request to ASIC's consent to resignation occur before the signing of the auditor's report. In the case of public companies where the resignation is to take effect at the AGM, RG26 proposes the application be lodged before the signing of the audit report, but in the case of compliance plans, registered schemes, AFSL licensees and credit licensees it requires the application be lodged prior to the end of the financial year. No explanation is given as to the rationale for the different proposals.

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- *Streamline the current processes*
  ASIC should as an interim measure consider streamlining the requirements so that there are one or two processes covering *all* entity types that clients and auditors are required to know and follow. We believe this is achievable as many of the requirements are established in ASIC policy and guidance rather than legislation; for example, the timing of resignation of auditors of compliance plans.

I would be pleased to discuss our comments with you. If you wish to do so, please do not hesitate to contact me on (02) 9322 5060.

Yours sincerely,

Kristen Wydell

Partner

Deloitte Touche Tohmatsu

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Appendix 1: Detailed responses to the Draft Updated Regulatory Guide

Reference	Comment
RG 26.3	Within the context of the current legislation, the requirements for the different auditor appointments should be aligned or simplified.
RG 26.17, 33, 48 & 63	We recommend deleting the last two sentences from paragraph 17 and other similar references throughout the report. In practice, there is often uncertainty at the time of completing the audit (for example, tender process or private company) as to whether the auditor will continue as the appointed auditor of the entity. As auditors are bound by legal and professional requirements, we consider the risk that an auditor's conduct will be negatively impacted by the knowledge that a change in auditor may occur to be low.
RG 26.18	Whilst we agree with ASIC that an audit is a continuous process we would recommend deleting this paragraph from the RG as it implies that there is no time in the financial reporting and auditing cycle where an auditor could resign.
RG 26.24(a), 41(a), 26.54(a) & 26.69(a)	It would be helpful if ASIC provides examples of what 'acceptable' reasons are, either in the Guide or relevant ASIC form.
RG 26.24(h), 26.41(h), 26.44(f), 26.54(h), 26.59(f), 26.69(g) & 26.73(f)	The resignation of the incumbent auditor and the appointment of the new auditor should be independent of each other. In practice for public companies they will both be considered at the AGM. We do not support the current approach where ASIC only consents to the resignation of an auditor of a public company if a replacement auditor is identified by the company. Auditors have legal obligations to comply with the auditing standards concerning acceptance and continuance of audit engagements and therefore ASIC should not be able to prevent an auditor from complying with these requirements. We believe it would be rare that a replacement auditor would not be identified and that this should be the responsibility of the directors and not impact the resigning auditor.
RG 26.32, 24(i)	We strongly disagree with the requirement for consent to the resignation of an auditor of a public company to be lodged before the signing of the auditor's report. This is inconsistent with the requirements for other entities and creates practical difficulties where the change of auditor process commences after the audit report is signed. As noted above auditors are bound by legal and professional requirements, and therefore we consider the risk that an auditor's conduct will be negatively impacted

Reference	Comment
	by the knowledge that a change in auditor may occur to be low. For a public company there are a number of timeline related rules for the calling of an AGM that provide sufficient time for the auditors to seek ASIC's consent to resign, the introduction of this rule (to apply prior to signing the audit report) would further complicate the process rather than simplify it.
RG 26.41(i), 26.44(g), 54(k), 26.59(h), 69(i) & 26.73(h)	We strongly disagree with the requirement for consent to the resignation or removal of an auditor of a registered scheme, compliance plan, AFS licensees and credit licensees to be lodged before the end of the financial year. This is inconsistent with the requirements for other entities and creates practical difficulties where the change of auditor process commences after the year end. As noted above auditors are bound by legal and professional requirements, and therefore we consider the risk that an auditor's conduct will be negatively impacted by the knowledge that a change in auditor may occur to be low. CP 209.46 comments that it is important for the auditor to be available for one month after the auditor's report is issued to answer questions. There is no requirement at law to do so and therefore we believe this is not relevant.
RG 26.86	We support ASIC including guidance in the RG regarding changes to an audit firm's structure. At RG26.86 you have directed auditors to advise you in writing prior to commencing the resignation process, our experience is that these matters are quite complex and early engagement with ASIC should be encouraged. ASIC's determination may impact the structure of the arrangement and drafting of the contract between the relevant parties.
RG 26.87	At paragraph 87 you have highlighted that if the firm holding the current auditor appointment is dissolved or ceases to have any registered company auditors, the auditor appointment vests in each of the individual former partners of the firm that were registered company auditors. This provides significant practical difficulties; for example: • From a client perspective, the entities are highly unlikely to find it acceptable to have their auditor's report signed by each of the registered company auditors in their individual capacity without a recognised audit firm brand. We think this would lead to market confusion and potential concern about the entity and therefore not be in the public interest. • From an individual auditor perspective, the individuals are not set up as sole practitioners – they would need to register for taxes (GST etc.), establish bank accounts, obtain Professional Indemnity insurance and address other logistical matters that are not practical or cost-effective and do not make commercial sense. Given the significant practical difficulties, we recommend that these circumstances be included in RG 26 as an early consent circumstance. We recognise that ASIC may

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	want to establish protocols around the changeover and suggest the following may provide a practical solution: • The directors of each entity to pass a resolution to appoint the merged/ new firm or authorised audit company as the auditor, appointment to continue only to the AGM at which time members will get to appoint the auditor. • In the event that the directors do not pass the resolution to appoint the merged/ new firm as auditor, but nominate say another firm as auditor, that the early consent be applied permitting that firm be appointed as auditor subject to confirmation of its independence. • The merged/ new firm/ authorised audit company to provide ASIC with confirmation of their independence in relation to the entities. Also refer comment below at Table 3 Item 5.
Table 2, item 2	The proposed revised Appendix in RG 26 includes 'Loss of independence' as an early consent consideration for particular conflicts defined under the Corporations Act 2001 (the "Act"). We believe this it too limiting. Auditors have established policies which are designed to ensure auditors meet or exceed the independence requirements of APES 110 and the Corporations Law. Where the auditor and/or client are of the opinion that there is a conflict of interest or the auditor believes they will be unable to issue an unmodified independence declaration, the auditor should be allowed to resign. This should not be subject to independent consideration by ASIC. Currently, ASIC has the power to refuse the request if it does not fit within the early consent circumstances defined in the appendix to RG 26. One example of where a conflict may arise under APES 110.290.223 is the non-payment of audit fees – refer below Table 3, Item 7.
Table 3, Item 5	Where an audit firm changes its structure to become an authorised audit company and the existing registered company auditors move from one legal framework to another the current system (requiring individual resignation and reappointment) seems unduly burdensome given that there is no change to the substance of the arrangement from a client perspective. A potential solution would be for the relevant entities to be notified and company records updated as part of the authorised audit company registration process.
Table 3, Item 7	Non-payment of audit fees should be deleted from Table 3 as an example where early consent circumstances do not exist. Per the above recommendation, where applicable, this would be captured as part of our proposed 'loss of auditor independence' early consent circumstance. Resolution of audit fee disputes may be more complex than communicating with the client as proposed in CP209.37. Resolution may be achieved by communication in certain circumstances but not in all circumstances. In addition, as an audit firm is a commercial venture the auditor should not be required to continue the engagement with no or little expectation of recovery.

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Reference	Comment
Other comments	*Group of entities* The auditor appointment and resignations requirements in the Act have been drafted on a single entity basis. As noted in RG 26, the appointment of the auditor of a public company is subject to shareholder approval at an AGM. Many public entities have a number of wholly owned controlled entities. Based on the Act, the directors of each of these controlled entities which are proprietary companies must pass a resolution to change auditor, and must obtain the appropriate consents from the proposed auditor and then lodge the relevant documentation on an entity by entity basis with ASIC. In instances where the controlled entity is a public company ASIC consent is required for the resignation of the incumbent auditor. This is quite an administrative burden on entities. We recommend that the Act is amended to acknowledge that an approval by the members at the AGM of a change of auditor would apply to all wholly owned controlled entities. If not possible to amend the Act, we propose that ASIC seek to streamline that process by allowing one form to be used for notification of the change of auditor for multiple entities. *Companies Limited by Guarantee* The introduction of the differential reporting framework exempts certain public companies limited by guarantee from requiring an audit, even though the Act requires them to appoint an auditor. This results in uncertainty around the responsibilities of the appointed auditor (for example, section 311 obligations) where no audit is required. Furthermore, we note that certain companies limited by guarantee are required to have an annual review of the financial information performed, albeit, this does not have to be done by someone who is a registered company auditor. We recommend that the Act be amended to only require the appointment of an auditor for a company limited by guarantee if the entity is required to have an audit performed. The Act could state that this needs to occur within one month of registration of a large company limited by guarantee or within one month of a smaller one triggering the requirements to have an audit performed. *Auditor of company and auditor of AFS licensee not the same auditor* A frequent difficulty that auditors and their client's experience is when the entity wishes to change their financial statement auditor but is prohibited by ASIC from also changing the auditor of their ASFL. We believe that this problem arises most commonly due to a lack of awareness of the timing requirements of ASIC. We would encourage ASIC to increase the information on their website and seek other methods to publish the requirements for changes of auditors. We believe that the auditor of the AFSL and the auditor of the entity should be the same because it is more difficult to obtain the necessary assurance on compliance with certain requirements if the financial statement audit is not also conducted. In addition, it would be more costly for the client if the auditors are different. Where a circumstance arises where the financial statement auditor and the compliance auditor are different we consider an early consent circumstance exists to achieve alignment.