



CHARTERED ACCOUNTANTS  
AUSTRALIA + NEW ZEALAND

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Australian Securities and Investments Commission  
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*Submission via email: [douglas.niven@asic.gov.au](mailto:douglas.niven@asic.gov.au)*

Dear Mr Niven

**Consultation Paper 265: Communicating audit findings to directors, audit committees or senior managers**

We are pleased to respond to Consultation Paper 265 *Communication audit findings to directors, audit committees or senior managers* (the Consultation Paper). Chartered Accountants Australia and New Zealand (CA ANZ) is committed to helping the stakeholders in the Australian financial markets to maintain a high standard of audit quality as part of maintaining an effective, high quality, capital market.

**General Comments**

We support the approach of developing and communicating the criteria which the Australian Securities and Investments Commission (ASIC) will use to determine when it will exercise the specific powers it has to communicate with directors, audit committees or senior managers. We note these powers have not yet been exercised.

While we are generally supportive of the proposals in the Consultation Paper, we believe that additional clarification of the criteria and the processes which will be established, as well as further consultation is required to effectively operationalize the powers. We would welcome the opportunity to take part in additional consultations such as roundtable discussions with the firms and the director community.

Our responses to specific questions raised in the paper are included in Appendix 1. Appendix 2 contains more information about Chartered Accountants Australia and New Zealand.

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If you have any questions regarding this submission, please contact Geraldine Magarey (Acting Audit and Insolvency Leader) via email; [Geraldine.Magarey@charteredaccountantsanz.com](mailto:Geraldine.Magarey@charteredaccountantsanz.com).

Yours sincerely



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## **APPENDIX 1: Specific comments**

### **1. Criteria for communicating financial reporting and audit findings**

We support the development of criteria for ASIC to use when determining when to exercise their power to communicate specific audit and financial reporting findings to directors, audit committees and senior managers of the entity (those charged with governance). We also support the development of a regulatory guide to communicate the process and the criteria to the stakeholders in the financial reporting and audit process.

ASIC's goals in relation to communicating with those charged with governance are set out in the Consultation Papers as assisting directors to:

- take action to address deficiencies in the entity's financial report;
- improve systems and processes supporting financial reporting; and
- discuss with the auditors actions to take improve audit quality.

In order to achieve these goals, we believe that it is essential that the criteria, and the processes used when exercising the powers, produce communications that are timely and only occur when there are material impacts on the adequacy of the audit that will impact audit quality.

For this to occur, we believe there are a number of issues that need to be further addressed before the criteria and the regulatory guide are finalised as follows.

#### *Scope*

The Consultation Paper refers to financial reporting surveillance at several points but the majority of the processes and criteria seem to be aimed at findings from audit inspections and audit surveillance. We recommend that the scope be clarified and, if communicating the findings of financial reporting surveillance is within the scope, then the criteria and processes for those should be dealt with separately to those dealing with the audit inspection and surveillance findings as the relationship during financial reporting surveillance should be directly between ASIC and those charged with governance of the entity concerned.

#### *Timeliness*

As the audit inspection process occurs on files where the audits have already been completed and we understand that it can take a significant period of time for ASIC's reports to be finalised, it is important that the criteria and the regulatory guide establishes the timing of such communications (i.e. will they be undertaken while the inspection is still ongoing or at the end of the inspection process) and the level of detail to be disclosed. In determining the timing of the communication it will be necessary to balance the need to inform those charged with governance with due process for the auditor in resolving any issues with ASIC.

#### *Due process where there is a disagreement*

The criteria needs to consider, and the regulatory guide needs to establish, due process for communication of issues where there is a disagreement between ASIC and the auditor as to the finding which has not been resolved. This may require a mediation process involving standard setters or independent experienced industry peers to enable an agreement between ASIC and the auditor to be reached before communications take place.

In paragraphs 16(b) and (c) it is stated that the audit inspection and financial reporting surveillance findings exclude matters that are within a range of reasonable judgement or where there are genuine issues relating to the interpretation of accounting and auditing standards. However, our understanding from our members is that such issues often arise during inspections and are not always easily resolved. If matters where there is disagreement between ASIC and the auditor are not to be communicated, this should be made clear.

#### *Implications for directors' obligations*

The Consultation Paper does not deal with the process which those charged with governance are expected to follow when they receive such a communication. There are a number of potential issues for directors resulting from such a notification, including liability, continuous disclosure obligations, market impacts etc. The guidance needs to clarify what directors are expected to do in response to any such communication with ASIC, otherwise individual entities will respond differently, which will not achieve the aim of enhancing financial reporting and audit quality.

#### *Regulatory and financial impact*

In relation to the questions raised in paragraph 26, we believe there may be additional costs. Our understanding that once an entity is notified of issues by the auditor, there are frequently discussions between the client and the entity. These take time to resolve, may involve the need for legal advice from both parties, particularly for directors to understand the implications for them. There is also the risk of damaging the relationship between those charged with directors and the auditor. Consideration should also be given as to whether this process has potential to undermine the confidence of the director community in the audit process, which will can only harm the goal of furthering financial reporting and audit quality.

#### *Communications with other regulators*

We agree that further consultation is required before ASIC decides whether to communicate findings to other regulators. Other regulators have requirements for auditors such as 'fit and proper' person tests and the impact of such communications on the directors and auditors obligations needs to be understood before such a decision is made.

### **Question B1Q1 Do you have any comments on our proposed criteria set out in Table 1?**

#### *Criteria 1*

This criteria appears to suggest that ASIC would use details from the audit workpapers to support a position they are taking in relation to a matter of they have discovered during financial reporting surveillance. We do not believe this is appropriate. The audit workpapers are prepared for the purpose of the auditor forming their opinion on the financial report and not for other purposes. Using the auditor's workpapers in this manner is also potentially very damaging to the relationship between the client and the auditor. We do not support the inclusion of this criteria.

#### *Criteria 2*

The meaning of 'particularly significant findings' is unclear and should be addressed. The regulatory guide needs to use terminology that is not subjective. Also, this criteria should only be used if there are concerns that the auditor has not obtained reasonable assurance that the financial report is not materially misstated for the current year under inspection as the entity should already have been notified if there were concerns with a previous year's audit under other criteria.

*Criteria 3*

The criteria states that communication will occur when ASIC intends to take enforcement action in relation to an entity's auditor. As this situation would generally be the end of a process which should already have triggered a communication under one or more of the other criteria, we do not believe it is necessary. If ASIC were to wait until an enforcement action to commence before communicating with the entity, it is unlikely that this communication would be timely. Waiting until an enforcement action is underway also raises other issues of due process such as procedural fairness and legal privilege that may impact how this criteria could work in practice.

*Criteria 5*

The current wording is also subjective. Further clarity around the factors and how they will be considered by ASIC should be provided. In addition, terms such as 'relative severity' and 'genuine uncertainty' need to be defined or alternative terms that are not subjective used.

Where there have been audit issues but the conclusion is that the audit opinion is correct and/or the financial report is not materially misstated, we do not believe that those charged governance need to be notified. The directors, audit committee members and management may not have the knowledge or expertise necessary to understand issues of audit methodology or application of audit standards and we are unsure what steps they would be able to take in response to being notified of such issues. There is a risk that this may undermine the confidence of directors in the audit process without improving audit quality. Further consultation is required on this criteria.

***Question B1Q2 Are there any additional criteria that we should consider including?***

We do not believe there are additional criteria which are required.

**2. Advising directors of routine audit file reviews*****Question B2Q1 Do you agree that we should let directors know that we will be reviewing audit files relating to the entity as part of our routine audit firm inspections?***

Our understanding is that the Big 6 audit firms already advise clients when their files are subject to ASIC's inspection. However, we support ASIC providing notice to ensure that all entities are made aware of inspections if they believe that the auditor has failed to notify the entity. It is our understanding that ASIC does not routinely notify entities who are the subject of financial reporting surveillance activities so this appears to be setting a different standard for auditors.

***Question B2Q2 Should we also let directors of an audited entity know that we will be reviewing audit files related to the entity as part of a surveillance activity where we already have reason for concern about the adequacy of the audit?***

We are unsure what kind of surveillance activity is encompassed by this process. If it is financial reporting surveillance, then that seems to be outside the scope of the consultation (which is communicating findings of the audit inspection process). If it is referring to other kinds of auditor surveillance, such as when ASIC acts on a complaint or whistleblowing situation or an issue discovered during financial reporting surveillance then this needs clarification and due process needs to be established.

## **APPENDIX 2: About Chartered Accountants Australia and New Zealand**

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations. We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation accounting professionals across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.