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The Comprehensive Plan for Audit and Risk in Australia

Australians have a fair and reasonable expectation that auditing and other lines of defence will protect them from risks and shocks in their financial and consumer lives, and will similarly provide for confidence, integrity and transparency in business.

Listed company financial statement auditing in Australia is effective, on par with international best practice and enjoys a strong level of confidence from investors and other stakeholders. However, Chartered Accountants Australia and New Zealand recognises the need to revisit independence rules and the assessment of how conflicts of interest are mitigated in an effort to keep pace with consumer and public expectations.

Over the past three years, organisations across the private and public sectors have come under major scrutiny. Clearly, a more integrated and consistent approach to how Australians are covered on risks such as fraud, misconduct and corporate failure is essential.

It is an appropriate time to explore new and better ways to improve and enhance the confidence, relevance, and quality of auditing in Australia. This will also provide an opportunity to re-examine the risks facing Australian businesses and consumers and how these can be well managed.

The following 15 Point Plan sets out in detail how auditors, boards/audit and risk committees, management and CFOs, and other key participants should refocus their approach to ensure:

1. Conflicts of interest are mitigated and meet public expectations
2. The level of risk tolerance and management are in keeping with the business environment, and
3. The quality of audits continue to be well resourced, robust and transparent to key decision makers.

Conflicts/Confidence: To maintain confidence, public expectations must be clearly understood and applied in setting rules for both audit independence and mitigating conflicts of interest.

1. **Clarify and strengthen non-audit services independence rules:** (a) Strengthen prohibitions on non-audit services provided by firms to companies they audit through Australian and international ethics standard setters (b) Pre-approval approach by audit and risk committee chair for non-audit services (c) Support ASIC efforts to clarify fee disclosures for audit, assurance, audit related, and non-audit related services.

2. **If not, why not governance review of audit tenures:** Conduct a governance review of auditor appointments across major listed companies and financial institutions every 15–20 years, with disclosure and explanation required where audits not tendered.

3. **Stricter relationship independence rules:** Restrict auditing entities where a former partner of the audit firm (within 5 years) is on the board or a financial relationship to the firm remains.

4. **Enhance firm transparency and governance:** Enhance audit firm transparency reporting on actions to establish a culture committed to delivering consistently high-quality audits, including oversight of compliance, quality and independence.

5. **Introduce transparency and oversight of auditor removals:** Companies should disclose the reasons for removal of auditors and regulatory oversight should be consistent with requirements for auditor resignation.

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Risk/Relevance: Addressing risks, such as fraud and misconduct in an increasingly complex business environment must involve all lines of defence, including management and CFOs, board/audit and risk committees, together with auditors and regulators.

6. **Integrated lines of defence on risks facing business and consumers:** Develop an integrated approach to lines of defence on key operational and emerging risks facing Australian businesses and consumers such as cyber/data risks, fraud, misconduct and consumer protection. This should encompass the roles of (1) Management/CFO (2) Compliance (3) Internal Audit (4) Board/audit and risk committee (5) External auditor (6) Regulators (7) Institutional investors.

7. **Clarify accountability for the internal control environment and risk management:** Board/audit and risk committee and management/CFO reporting on (1) operating effectiveness of internal control environment for financial reporting, and (2) operating effectiveness of risk management framework including steps to mitigate the risk of significant fraud and misconduct (scope: major listed companies and financial institutions). Assurance conducted under Australian Standards on Assurance Engagements and independence standards.

8. **Corporate reporting clarity and relevance:** Mandate digital reporting, support continued engagement with international standard setters to inform best practice in financial, reporting standards.

9. **Transparency on business failure risks:** Board/audit and risk committee reporting on key risks to business continuity and how these are mitigated (with appropriate safe harbour/caveats), assurance on reasonableness of disclosures under Australian Standards on Assurance Engagements and independence standards.

10. **Don't overburden smaller businesses:** One size doesn't fit all when it comes to auditing arrangements for business. Arrangements should be proportionate to the size and nature of the business.

Quality audits: Constantly improving audit quality is essential – demanding robust, transparent oversight, well-resourced independent audit and risk committees, while continuously sharpening auditors' skillset.

11. **Clarify regulatory oversight on audit quality:** Support ASIC's development of a balanced score card on audit quality, recommend three-grade severity scale for inspection findings, and greater emphasis on reviewing firm-wide quality management processes in addition to audit file reviews. Support Financial Reporting Council promoting continued regulatory co-ordination and enhancing transparency in audit quality oversight.

12. **Formalise audit and risk committees:** Clarify and formalise independent committee remit covering auditor appointment, independence, scope, fees, and other assurance engagements (scoped proportionally and with engagement by relevant governance bodies); enhance skillset and resourcing of audit and risk committees and implement safeguards for independence from management.

13. **Engage investors with the audit:** Improve investor engagement in auditor appointment, fee setting, risk, and assurance, through audit and risk committee chair reporting and auditor involvement at annual general meetings.

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14. **Multidisciplinary firms with reinforced independence and transparency:** A diverse skill base is important for high quality audits of complex entities, but strengthened and clarified independence rules, firm governance, and transparency are a required as per points 1–5 above.

15. **Improve auditors' fraud detection skillset:** Implement profession-wide focused case study-based fraud detection training for auditors at all levels to enhance awareness and responsiveness to fraud risk.

The 15 Point Plan is comprehensive. It sets out for organisations where the focus should be so that the risks are managed well and quality audits are conducted. It is noted that good business practice and governance remain vital tools along with audit to ensure good business outcomes are achieved.

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CA ANZ 15 Point Plan	Inquiry Terms of Reference[1]	Relevant Australian regulation/practice[2]	Relevant international regulation/practice	Pros	Cons
1. **Clarify and strengthen non-audit services independence rules:** (a) Strengthen prohibitions on non-audit services provided by firms to companies they audit through Australian and international ethics standard setters (b) Pre-approval approach by audit and risk committee chair for non-audit services (c) Support ASIC efforts to clarify fee disclosures for audit, assurance, audit related, and non-audit related services.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests.	Principles-based and specific list of restrictions for audit clients.	US: More prescriptive requirements than Australia on prohibited services. International Ethics Standards Board for Accountants (IESBA): currently reviewing requirements (Australian requirements equivalent to current IESBA standard). UK: currently considering a 'permitted' list approach with services not listed prohibited for audit clients.	• Improve confidence and perceptions of independence. • Address concern about independence in appearance.	• Negligible provided appropriate consultation and design in strengthened requirements, and consistency with IESBA.
2. **If not, why not governance review of audit tenures:** Conduct a governance review of auditor appointments across major listed companies and financial institutions every 15–20 years, with disclosure and explanation required where audits not tendered.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests.	Audit partner rotation (listed: 5 yearly).	Multiple jurisdictions: have introduced and removed firm rotation requirements, Europe still under implementation (refer CA ANZ first submission for detail). UK: 10-year mandatory audit tendering. IESBA: Recent strengthened partner rotation requirements.	• Improve confidence and perceptions of independence. • Address concern about independence in appearance.	• Potential market/competition impacts (but largely curbed compared to arbitrary rotation).
3. **Stricter relationship independence rules:** Restrict auditing entities where a former partner of the audit firm (within 5 years) is on the board or a financial relationship to the firm remains.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests.	Principles-based, specific restrictions (2 years for former partners and multiple former partners cannot join same audit client within 5 years of each other), and transparency requirements.	US: 3-year restriction and more prescriptive requirements. IESBA: Australian requirements currently in line with international standard with some specific additional requirements.	• Improve confidence and perceptions of independence. • Address concern about independence in appearance.	• Potential market/competition impacts. • Potential impacts on availability of appropriately skilled audit and risk committee/board members.

[1] Terms of Reference of the Inquiry into the regulation of auditing in Australia, commenced August 2019.
[2] For greater detail, refer to Chartered Accountants Australia New Zealand's Submission of 12 September 2019.

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CA ANZ 15 Point Plan	Inquiry Terms of Reference[1]	Relevant Australian regulation/practice[2]	Relevant international regulation/practice	Pros	Cons
4. **Enhance firm transparency and governance:** Enhance audit firm transparency reporting on actions to establish a culture committed to delivering consistently high-quality audits, including oversight of compliance, quality and independence.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests. ToR 4: Audit quality, including valuations of intangible assets. ToR 5: Matters arising from Australian and international reviews of auditing.	Transparency reporting regime exists for firms auditing 10+ listed companies.	International: Multiple countries have similar transparency reporting regimes, Australia was one of the first countries to require from 2013. Has been mandatory in UK since 2010, now mandatory in EU from 2016. Similar reports are also being produced voluntarily in countries such as the US and Canada.	• Promote strengthened transparency and firm-wide commitment to quality. • Improve confidence and perceptions of independence. • Address concern about independence in appearance.	• Negligible provided appropriate consultation and design in strengthened requirements.
5. **Introduce transparency and oversight of auditor removals:** Companies should disclose the reasons for removal of auditors and regulatory oversight should be consistent with requirements for auditor resignation.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests.	Regulatory oversight exists when auditor resigns, not when removed (except Financial Services Licensees which require approval). Board/AGM approval and disclosure are primary current requirement.	International: Emphasis in most frameworks is transparency on reasons for removal and AGM, where regulatory consent for auditor resignation is required this is normally uniform with requirements for removal.	• Improve confidence and perceptions of independence. • Address concern about independence in appearance.	• Negligible provided appropriate consultation and design in strengthened requirements.
6. **Integrated lines of defence on risks facing business and consumers:** Develop an integrated approach to lines of defence on key operational and emerging risks facing Australian businesses and consumers such as cyber/data risks, fraud, misconduct and consumer protection. This should encompass the roles of (1) Management/CFO (2) Compliance (3) Internal Audit (4) Board/audit and risk committee (5) External auditor (6) Regulators (7) Institutional investors.	ToR 5: Matters arising from Australian and international reviews of auditing. ToR 6: Changes in the role of audit and the scope of audit products. ToR 7: The role and effectiveness of audit in detecting and reporting fraud and misconduct.	Ad-hoc approach to risks with limited integration or assurance, review engagements often not conducted under assurance/independence standards.	International Auditing and Assurance Standards Board (IAASB): The Framework for Audit Quality recognises that all stakeholders in the chain play an important role (including directors/audit committees, regulators, and other key players). UK: Government reviews on audit are focused on importance of accountability and role across the full chain. Netherlands: Government review provisional recommendations focus on all stakeholders in chain.	• Better accountability and coverage for risks impacting on business and consumers. • Integrated approach means more efficiencies and effectiveness compared to a solely regulatory-based approach to addressing risk or siloed approach.	• Negligible provided appropriate consultation and design.

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CA ANZ 15 Point Plan	Inquiry Terms of Reference[1]	Relevant Australian regulation/practice[2]	Relevant international regulation/practice	Pros	Cons
7. Clarify accountability for the internal control environment and risk management: Board/audit and risk committee and management/CFO reporting on 1) operating effectiveness of internal control environment for financial reporting, and 2) operating effectiveness of risk management framework including steps to mitigate the risk of significant fraud and misconduct (scope: major listed companies and financial institutions). Assurance conducted under Australian Standards on Assurance Engagements and independence standards.	ToR 4: Audit quality, including valuations of intangible assets. ToR 5: Matters arising from Australian and international reviews of auditing. ToR 6: Changes in the role of audit and the scope of audit products. ToR 7: The role and effectiveness of audit in detecting and reporting fraud and misconduct.	Ad-hoc approach for different sectors, limited targeted reporting by management/board or assurance.	US: Post-Enron legislation introduced these requirements as relevant to financial internal control environment. Netherlands: Government review on audit provisionally recommends 'control statement' by management, which is audited. UK: Government reviews on audit are examining need for these requirements.	• Improvement in financial reporting quality. • Improved coverage of the risk of fraud and misconduct by companies and auditors. • Better systemic accountability for prevention of fraud and misconduct.	• Cost associated in greater internal control and risk management processes in addition to reporting. • Cost associated with assurance.
8. Corporate reporting clarity and relevance: Mandate digital reporting, support continued engagement with international standard setters to inform best practice in financial, reporting standards.	ToR 4: Audit quality, including valuations of intangible assets. ToR 5: Matters arising from Australian and international reviews of auditing.	Concerns on relevance, understandability and volume of financial reporting, non-financial reporting still developing, very limited voluntary digital reporting.	US: Digital reporting mandated. European Union: Current review into mandating digital reporting. International Accounting Standards Board: Multiple ongoing standard setting projects aimed at clarity and relevance.	• More meaningful and customised reporting for stakeholders, investors (professional and retail) and other stakeholders. • Better informed investors and decision making.	• Initial cost to implement digital reporting with reduced cost over longer term.
9. Transparency on business failure risks: Board/audit and risk committee reporting on key risks to business continuity and how these are mitigated (with appropriate safe harbour/caveats), assurance on reasonableness of disclosures under Australian Standards on Assurance Engagements and independence standards.	ToR 4: Audit quality, including valuations of intangible assets. ToR 5: Matters arising from Australian and international reviews of auditing.	Reporting and assurance not targeted/explicit, subsumed with basis of accounting.	UK: Government reviews on audit are examining need for these requirements.	• Clarity on where failure may occur and how this is addressed. • Better accountability and clarity where risks eventuate and have been disclosed.	• Need to address liability related to disclosures or additive reporting may not be possible. • May impact innovation where risks disclosed are misinterpreted and/or result in over-compensation by investors, particularly in early stage.
10. Don't overburden smaller businesses: One size doesn't fit all when it comes to auditing arrangements for business. Arrangements should be proportionate to the size and nature of the business.	ToR 12: Any related matter.	Increasingly disproportionate impact on SMEs as requirements added to address listed company concerns.	IAASB: Current standard setting project to simplify standards for less complex entities.	• Promote growth in businesses and the economy. • Essential for effective operation of the regulatory framework.	• Negligible provided appropriate consultation and design in scoping of all requirements.

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11. Clarify regulatory oversight on audit quality: Support ASIC's development of a balanced score card on audit quality, recommend three-grade severity scale for inspection findings, and greater emphasis on reviewing firm-wide quality management processes in addition to audit file reviews. Support Financial Reporting Council promoting continued regulatory co-ordination and enhancing transparency in audit quality oversight.	ToR 4: Audit quality, including valuations of intangible assets. ToR 10: The adequacy and performance of regulatory, standards, disciplinary and other bodies. ToR 11: The effectiveness of enforcement by regulators.	ASIC working to address lack of clarity/understanding in current reporting, no indication of severity of regulatory findings.	International: Lack of clarity in regulatory reporting on audit quality widespread, some jurisdictions provide more detail on inspection findings allowing greater assessment of severity in findings.	• Improve confidence and clarity about audit quality. • More accurate and focused insights into issues and areas requiring improvement.	• Challenging to address subjectivity in assessing severity of audit inspection findings.
12. Formalise audit and risk committees: Clarify and formalise independent committee remit covering auditor appointment, independence, scope, fees, and other assurance engagements (scoped proportionally and with engagement by relevant governance bodies); enhance skillset and resourcing of audit and risk committees and implement safeguards for independence from management.	ToR 4: Audit quality, including valuations of intangible assets. ToR 10: The adequacy and performance of regulatory, standards, disciplinary and other bodies.	Rapidly expanding remit and reduced capacity, largely informal sub-committee without independent remit.	UK/US: Formal independent remit for audit and risk committees. International: International Organization of Securities Commission (IOSCO) best practice for audit committees.	• Improved reporting and audit quality, and confidence in reporting and audit. • Address concerns related to audit independence and oversight. • Improved quality in risk management.	• Negligible provided appropriate approach to establishing best practice and/or additional requirements including effective consultation and design.
13. Engage investors with the audit: Improve investor engagement in auditor appointment, fee setting, risk, and assurance, through audit and risk committee chair reporting and auditor involvement at annual general meetings.	ToR 4: Audit quality, including valuations of intangible assets. ToR 5: Matters arising from Australian and international reviews of auditing.	Limited engagement through annual general meetings.	UK: Government Reviews on audit are examining need for these requirements.	• Improved confidence and understanding of reporting and audit. • Address concerns related to audit independence and oversight.	• Challenging to address engagement of diverse investor populations in major listed companies.

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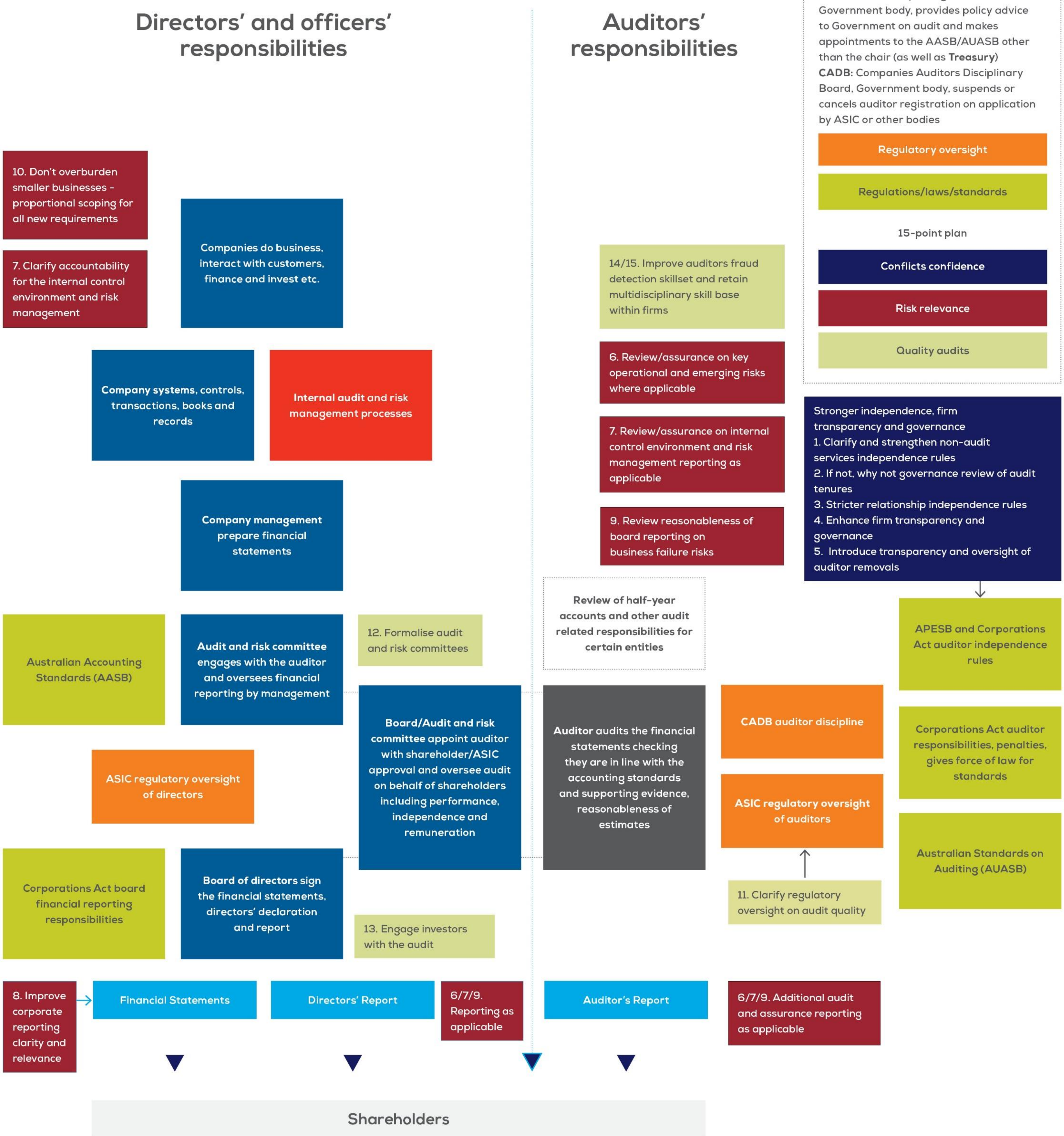
14. **Multidisciplinary firms with reinforced independence and transparency:** A diverse skill base is important for high quality audits of complex entities, but strengthened and clarified independence rules, firm governance, and transparency are a required as per points 1 – 5 above.	ToR 1: The relationship between auditing and consulting services and potential conflicts of interests. ToR 2: other potential conflicts of interests.	Transparency/independence requirements as above.	UK: Competition and Markets Authority conducted study into the need to structurally split firms/ban non-audit services but concluded this would have detrimental impacts on audit quality, UK standing internationally and firms.	• Multidisciplinary skillset essential to conduct high quality audits for increasingly complex entities • Additional demands for confidence and assurance (e.g. fraud/misconduct risk) requires multidisciplinary skillset.	• Concerns about independence in appearance.
15. **Improve auditors' fraud detection skillset:** Implement profession-wide focused case study-based fraud detection training for auditors at all levels to enhance awareness and responsiveness to fraud risk.	ToR 7: The role and effectiveness of audit in detecting and reporting fraud and misconduct.	Some training courses available, content varies.	US: Focused case-study based fraud detection training has been implemented widely by the Center for Audit Quality (CAQ).	• Auditors who have undertaken the training may be more effective in identifying fraud.	• Negligible provided appropriate scoping within current training requirements. • Detection of fraud will remain highly challenging hence importance of steps toward systemic prevention (refer recommendations 7 and 8 above).

Australia's financial reporting and auditing regulatory eco-system

KEY:
AUASB: Australian Auditing and Assurance Standards Board, Government agency
AASB: Australian Accounting Standards Board, Government agency
APESB: Australian Accounting Professional and Ethics Standards Board, independent national body
ASIC: Australian Securities and Investments Commission, Government body, regulator for directors and auditors
FRC: Financial Reporting Council, Government body, provides policy advice to Government on audit and makes appointments to the AASB/AUASB other than the chair (as well as **Treasury**)
CADB: Companies Auditors Disciplinary Board, Government body, suspends or cancels auditor registration on application by ASIC or other bodies

Regulatory oversight
Regulations/laws/standards
15-point plan
Conflicts confidence
Risk relevance
Quality audits



NB: this diagram covers matters related to companies that are 'public interest entities', including listed companies – certain aspects differ for other types of entities