In relation to AUST R410.14.1 and from the point of view of a SMSF auditor

I believe that the 20% benchmark should at least be raised to 30% to be consistent with Australian and international standards. Given the benchmark is based on referred fees and not individual fees then perhaps the percentage should be even higher than 30%, at 40% or 50%?

I also would like to separately comment on self-interest and intimidation threats arising specifically applied to parcels of SMSF audits under a referral arrangement.

Self interest

The exposure draft makes an assumption that an entire parcel of fees may be taken away from the auditor by a referrer if just one opinion on one fund (or a small number) is disagreed with. I think this is unlikely for a number of reasons. In the case of a single client with their large fee being individually a large source of audit revenue, I can understand this, but in a referral situation I believe other factors come into play which mitigate the risk of a referrer changing auditor. These factors appear to have not been considered in the ruling and the main one being that it is not quite so simple to change auditor on an entire parcel of fees.

For a loss of a parcel of fees to happen arising from disagreement over an audit opinion, three things must occur:

1) The client disagrees with the audit opinion
2) The referrer sides with the client and also disagrees with the audit opinion (even after explanation from the auditor)
3) The referrer decides that siding with their client and retaining their individual fee is important and worth disrupting their staff, incurring costs, creating uncertainty and disrupting their entire SMSF client base for, and they change auditor.

I have set out various scenarios on the second page. Further I have spoken to my large referrers both when I started the referral arrangement, and more recently regarding these independence changes and they confirmed that they have previously done and will always accept any audit opinion which can be backed up with legislation and they also accept the risk that one of the funds may choose to find a new auditor and even new accounting firm, based on an audit opinion, but this will not impact their referring. They all understand that clients can be difficult and loss of one client from disagreement over an audit opinion is just one of the risks of doing business. Losing a parcel of fees over poor or unprofessional service is a higher risk.

The truth is that in a referral arrangement once logistical procedures such as document transfers, turnaround times, query reporting, annual fee ranges, permanent documents etc are all in place and bedded in running efficiently, the referrer is quite reluctant to change auditor. The costs and disruption to change auditor outweigh the potential that they may lose an accounting fee over an opinion that is disagreed with. This also goes back to my first point in that independence risks from single fees are not the same as from parcels of fees. Simply, the disruption created by changing auditor is far more expensive to a referrer than the cost of losing a single client – that's if the client was even deciding to go.

Some scenarios below explain my thoughts and conclude that it is unlikely, at least from my perspective, that loss of an entire fee parcel will occur from a disagreement over an audit opinion.

Lastly, I would say that it is a poor auditor who is not able to sufficiently explain a contravention to another professional (the referrer) in such a way that the professional understands and accepts.

Scenario	Impact on auditor	Impact on referrer	Likelihood of this scenario in a compliance breach situation
The fund trustees **agree** with an auditor's qualified opinion. The referrer also **agrees** with the qualified audit opinion.	None.	None.	High. Trustees and referrers generally accept when they have contravened the rules – particularly as the rules are clear and can be explained easily.
The fund trustees **disagree** with an auditor's qualified opinion so drastically that they appoint a new auditor. The referrer actually agrees with the audit opinion.	Very low – one fee is lost.	Very low. Accounting fee is retained. Referrer sends fund to a different auditor each year.	Low, although typically if the auditor and referrer believe a contravention has occurred then it is not so difficult to also convince the client.
The fund trustees **disagree** with an auditor's qualified opinion so drastically that they appoint a new auditor and accountant. The referrer also disagrees with the audit opinion.	Low – one fee is lost.	Low – one fee is lost. Accountant may blame audit for the loss of a fee.	Very low. Typically, referrers understand SIS rules well and actually agree with the auditor particularly when the contravention can be explained and backed up with legislation.
The trustees and referrer **disagree** with an auditor's qualified opinion so drastically that the referrer decides to no longer provide any work to the auditor.	High - auditor loses a portion of their fees significant to their operation.	High - referrer will have to research new auditors, appoint new auditors, cause disruption to their staff and clients with potentially new processes in place as well as new engagements, changes in audit fees, etc.	Low - typically referrers agree with an auditor's opinion which can be backed up with legislation, case law, etc. leaving little room for argument. I cannot see that a referrer would prefer to change auditor for the entire parcel of fees over losing one of their own fees – That also assumes that they would lose the accounting fee!
The referrer flat-out **disagrees** with an auditor's qualified opinion so drastically that they will no longer provide any work to the auditor.	High - auditor loses a portion of their fees significant to their operation. Auditor is probably happy as they don't want to do any work for a referrer who cannot understand and accept SIS legislation.	High - referrer will have to research new auditors, appoint new auditors, cause disruption to their staff and clients with potentially new processes in place as well as new engagements, changes in audit fees, etc.	Low - typically referrers agree with an auditor's opinion which can be backed up with legislation, case law, etc. leaving little room for argument. I cannot see that a referrer would prefer to change auditor for the entire parcel of fees over losing one of their own fees – That also assumes that they would lose the accounting fee!

Intimidation

I believe the following two items add pressure to an auditor to produce a standard / favourable opinion and are key differences in the amount of pressure or perceived pressure, between the audits of SMSF vs the audits of other entities with more stakeholders.

1) the potential negative financial effect on all stakeholders of the entity being audited arising from a negative audit view / opinion

2) the complexity of the entity's operations and financial reporting where significant judgements are required (basically the key audit matters)

In more detail:

1) in a listed entity, a larger number of stakeholders exist (such as shareholders and management) who may put pressure on an auditor because they want to see certain results - to create or retain wealth either through their shareholdings or remuneration schemes or in the case of a smaller entity, wanting to sell, for example. A SMSF does not have such stakeholders.

2) With regard to complexity, a listed entity may have various matters requiring professional judgement and additional work which typically a SMSF does not. A couple of pretty common examples would be impairment of goodwill, or valuation of receivables/work in progress. I find SMSF audits are much more black and white in terms of SIS and financial statement reporting and therefore the pressure on the auditor to apply "positive" or "lenient" professional judgement is simply not there. The stakeholders (Trustees) of a fund are not really creating the same pressure that stakeholders (shareholders and management) of a larger audit entity might.

Conclusion

Hopefully this document explains why threats in SMSF audit fee referral arrangements are inherently lower than those in other audits and perhaps the legislation needs to include an additional category of entity with lower risks (and fewer stakeholders), under para R410.14.1.