

Strengthening Auditor Independence Requirements

CA ANZ Audit Conference 2023

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Agenda

- Background to recent changes to APES 110
- Non-Assurance Services provisions
- Fee-related provisions
- Long Association
- Listed Entity and Public Interest Entity (PIE)
- Q&A

Global Audit Regulation & Ethics

UK – Kingman and CMA Reviews, Brydon Report, FRC overhaul and Big 4 operational separation as a result:

- Carillion – KPMG fined £14,4m + £4m in costs by UK FRC
- BHS – PwC fined £6.5m. Auditor fined £325k and banned for 15 years

EU - Wirecard collapse in Germany 2020 – €1.9b fictitious assets, unqualified audit reports and alleged audit failures

USA – US SEC & PCAOB Independence and ethics breaches

- 2022 - US\$ 100M fine for EY
- 2021 - US\$ 450K fine for KPMG
 - CA ANZ undertaking review of Professional Conduct Framework



PJC Inquiry into the Regulation of Auditing in Australia

Led by Parliamentary Joint Committee on corporations and financial services.

 **2019**
August

Inquiry established

Focus on the regulation of auditing, conflicts of interest and performance of regulators


 **2020**
November

Final report issued

No changes to interim recommendations

Interim report released

- 10 recommendations
- no major structural changes to legislative & regulatory frameworks

 **2020**
February

Government yet to respond

To date



PJC Inquiry recommendations relating to NAS & Fees

- **Recommendation 3**

- Establish defined categories and associated fee disclosure requirements in relation to audit and non-audit services
- Establish a list of non-audit services that audit firms are explicitly prohibited from providing to an audited entity

Recommendation 4

- The auditor's independence declaration must specifically confirm that no prohibited non-audit services have been provided

Recommendation 5

- Consider revising APES 110 to include a safeguard that no audit partner can be incentivised, through remuneration advancement or any other means or practice, for selling non-audit services to an audited entity

Background for change

Whilst the International Code provides a strong foundation, there was impetus for IESBA to strengthen International Independence Standards particularly for PIE Audit clients:

- Public expectations on auditor independence
- Changes in laws, regulations and firm policies in various jurisdictions
- Research, public consultations and global outreach

Result → New Non-Assurance Services (NAS) and Fee-related provisions in the Code.

★ APESB recent release: [Compiled Code \(Dec 2022\)](#) incorporates these new provisions. ★

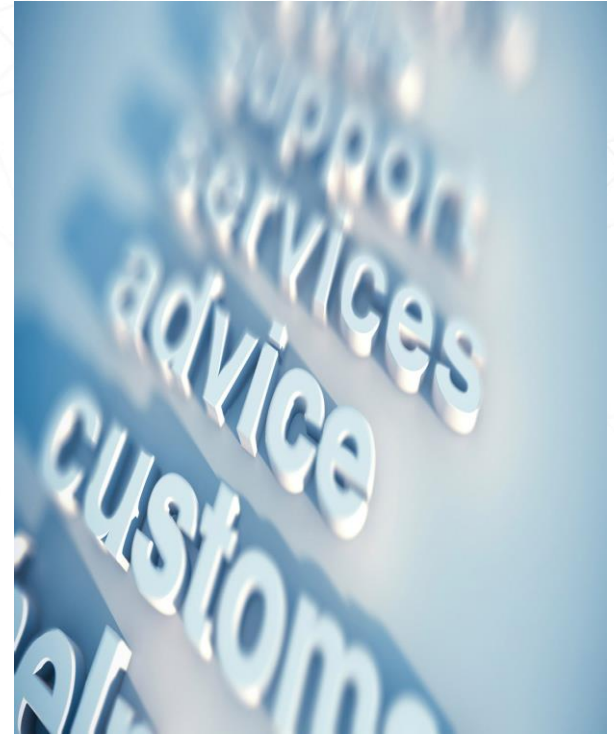
Non-Assurance Services Provisions in the Code



High-level overview of NAS Provisions in the Code

Effective 1 July 2023 (globally 15 December 2022):

- New overarching self-review threat prohibition for PIE audit clients
- Materiality qualifier for NAS withdrawn for PIE audit clients
- New requirements to communicate and obtain concurrence from Those Charged with Governance of PIE audit clients
- Assuming management responsibilities provisions moved to Section 400



Self-review Threat – All audit clients

Before providing a NAS, Firms must evaluate whether there is a risk that (R600.14):

- a) The results of the NAS will form part of or affect the accounting records, the internal controls over financial reporting, or the financial statements; **and**
- b) In the course of the audit of those financial statements, the audit team will evaluate or rely on any judgments made or activities performed when providing the NAS.

For non-PIE audit clients:

- it may be possible to implement safeguards in certain circumstances.
- in certain situations safeguards might not be available or capable of addressing threats.

Self-review Threat Prohibition – PIE audit clients

For PIE audit clients, a NAS that **might create** a self-review threat is prohibited (R600.16) because the threat:

- cannot be eliminated, and
- safeguards are not able to reduce the threat to an acceptable level

‘Might’ used rather than ‘will’ to avoid firms incorrectly concluding the NAS will not:

- create a self-review threat; or
- be subject to audit procedures

Materiality not relevant to whether NAS might create a self-review threat



Advice & Recommendations

Advice and recommendations might create a self-review threat (600.11 A1):

- Non-PIE audit clients – apply the conceptual framework.
- PIE audit clients – prohibited (R600.16) unless exception in R600.17 applies.

Exception for PIE audit clients: advice and recommendations allowed if it arises during the audit and the Firm:

- does not assume management responsibility, and
- applies the conceptual framework in relation to threats other than self-review.



Tax Services

A firm must not provide tax services or recommend transactions related to marketing, planning, or opining in favour of tax treatment initially recommended by the firm unless the firm is confident the treatment has a basis in applicable tax law or regulation that is likely to prevail (AUST R604.4).

Australian specific content:

- removed “*where a significant purpose is tax avoidance*” (R604.4 in IESBA Code)
- added guidance on ‘confident’ and ‘likely to prevail (AUST 604.4 A1.1)
- added a documentation requirement (AUST R604.4.1)



Tax advisory and planning services

Providing tax advisory and tax planning services will not create a self-review threat if such services (604.12 A2):

- a. Are supported by tax authority/precedent;
- b. Are based on established practice; or
- c. Have a basis in tax law that the firm is confident is likely to prevail.

Australian specific content (consistent with NZ):

- Additional guidance on 'confident' and 'likely to prevail' (AUST 604.12 A2.1)
- Additional documentation requirement (AUST R604.12.1)



Firm communication with TCWG – PIE audit clients

New requirements on communication with Those Charged with Governance (TCWG) (600.20 A1 to R600.22)

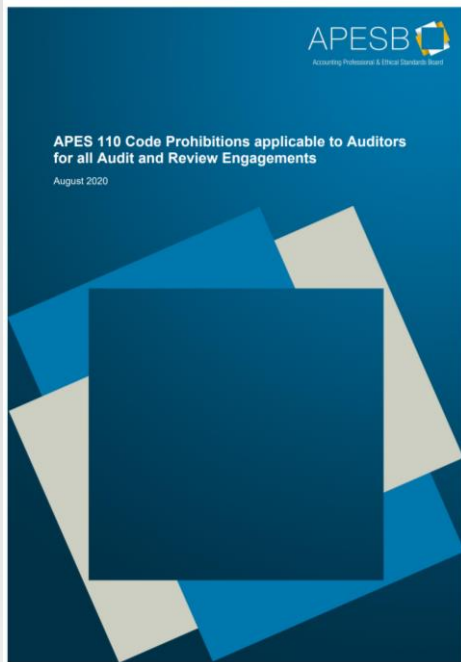
For PIE audit clients (including its parent entity and entities it controls), a firm must, before providing NAS:

1. Inform TCWG that the firm has determined the NAS is not prohibited and will not create a threat to independence, or that any threats are at an acceptable level
2. Provide TCWG with information to enable them to make an informed decision about the impact of the NAS on independence
3. Obtain concurrence from TCWG



Resources – Non-assurance Services

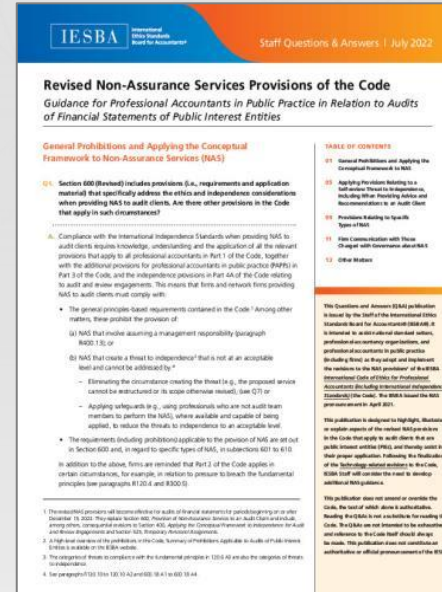
APESB 110 Code Prohibitions *to be issued*



- summarises prohibitions on NAS, interests, relationships and actions for all audit clients
- Updated version incorporating new NAS & Fees provisions expected to be released June 2023

Available on [APESB's website](https://www.apesb.org.au)

IESBA Staff Q&As - NAS



- Covers general prohibitions & applying the conceptual framework
- Self-review threats
- Specific prohibitions
- Providing advice & recommendations
- Communication with Those Charged with Governance

Available on the [IESBA's website](https://www.iesba.org)

Fee-related Provisions in the Code



Overview of Fee-related provisions in the Code

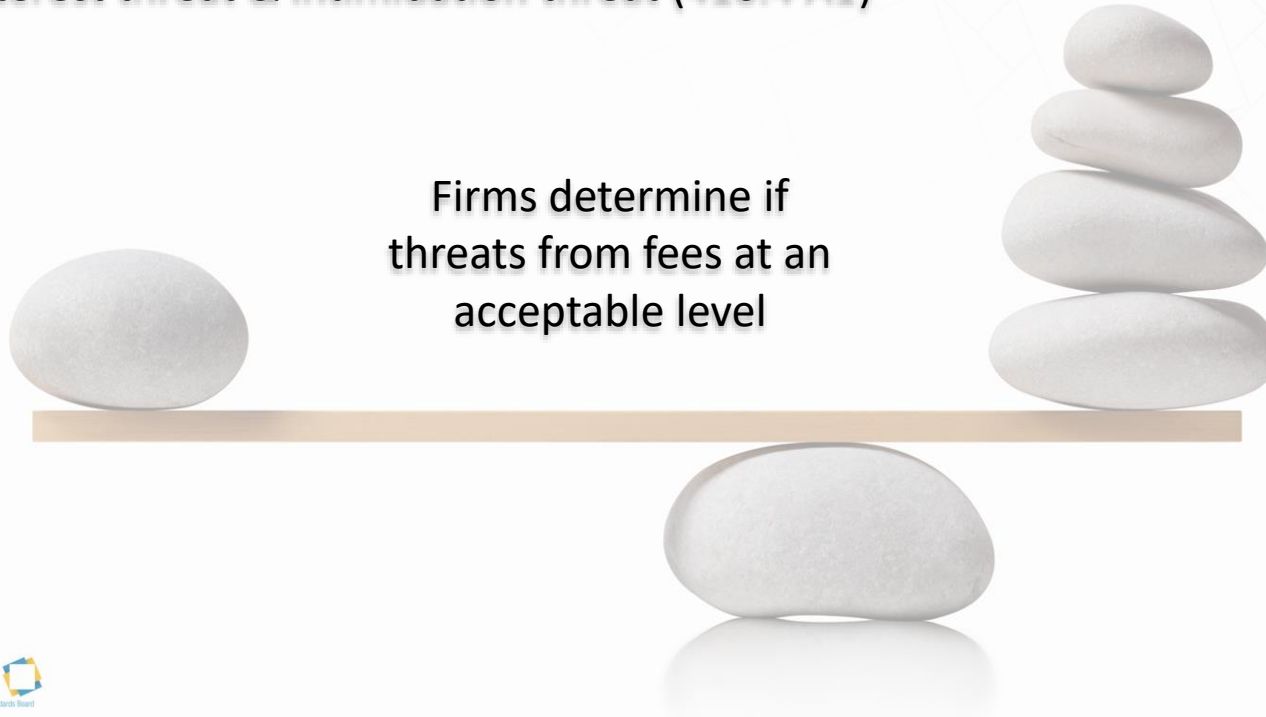
Effective 1 January 2023:

- New guidance on evaluating threats caused by existing fee paying model
- Prohibition on allowing other services to influence audit fees
- Guidance to help firms determine what constitutes a large proportion in specific circumstances (no specific cap)
- Fee dependency thresholds for PIE and Non-PIE audit clients
- For PIEs – transparency of fee information and fee dependency to TCWG and the public
- Strengthening prohibitions on compensation of audit partners



Self-interest threats created by fees

Fees negotiated with & paid by audit client could create self-interest threat & intimidation threat (410.4 A1)



Circumstances that create threats:

- High ratio of non-audit fees
- Overdue fees
- Fee dependency

Level of Audit Fees

Requirement for audit fee to be standalone:

- the provision of other services is not allowed to influence the level of audit fees (i.e., no discounts on audit fee if other services provided) (R410.6)
- Exception for cost savings based on experience gained from providing the other services

New guidance on when large proportion of fees are for services other than audit (410.11 A1 to A3)



Fee Dependency – PIE audit clients

Fee dependency threshold for PIEs remains at **15%** (over 2 consecutive years) (R410.18)

- Must perform a pre-issuance review on 2nd year audit work by a member from outside the firm
- Post-issuance review no longer considered a safeguard

For joint audits, a pre-issuance review not required where **both firms** perform sufficient work to take responsibility for the audit opinion, and only one exceeds the 15% threshold (R410.19)

Fee dependency cannot continue indefinitely :

- **Must cease as auditor after 5 consecutive years** (R410.20)
- Exception for public interest reasons (if certain conditions met) or if required by laws and regulation (R410.21)

Fee Dependency - non-PIE audit clients

New fee dependency threshold for non-PIE audit clients:

- Audit fee is **30%** of firm's total fees for **5 consecutive years**
- Must undertake either a (R410.15):
 - a) pre-issuance review of 5th year's financial statements by Member external to the Firm
 - b) post-issuance review of 5th year's work by Member external to the Firm or professional body

If fee dependency continues past 5 consecutive years, make determination and take action each year (R410.16)

For joint audits, a pre-issuance review not required where **both firms** perform sufficient work to take responsibility for the audit opinion, and only one exceeds the 30% threshold (R410.19)



Fee Dependency – Referral Source

- Referral source provisions were an Australia addition to APES 110 in 2013 – specific to **SMSFs**.
- Provisions have been revised to align with IESBA fee dependency provisions including:
 - Reference to ‘large proportion of fees’ replaced with **30%** threshold.
 - Applies to firm, individual partner and office.
 - 5 year cumulative period before requirement applies
 - pre-issuance review to be completed at 5 years by an appropriate reviewer not involved in the audit
 - Required to clarify position if dependency continues beyond 5 years



Resources – Fee-related provisions

The screenshot shows the IESBA Staff Questions & Answers page for January 2022. The main heading is "Revised Fee-related Provisions of the Code" with the subtitle "Guidance for Professional Accountants in Public Practice". The specific topic is "Q&As Relevant to Non-Public Interest Entities (Non-PIEs) and PIEs".

Q1: Section 410 includes provisions relevant to fees and other types of remuneration received from an audit client. It states a particular method a firm should use to determine which fee for a specific service (e.g., fee quoted, charged or paid) it should take into consideration when evaluating the level of the threats to independence created by the provision of that service to the audit client?

A: Given that fee arrangements and methods of payment vary widely in practice, the IESBA does not believe it would be appropriate for the Code to be overly prescriptive in terms of the method a firm should use to determine the fees and other types of remuneration (for example, the fees quoted, charged or paid) that should be taken into consideration for purposes of identifying, evaluating and addressing threats to independence.

A firm should consider any type of payment received from the audit client for purposes of evaluating and addressing the level of the threats created. In line with the Code's conceptual framework, the firm should exercise professional judgment in determining the amount of the fee or other type of remuneration received for providing audit or any other services to the audit client, including any payment-in-kind. To evaluate the level of the threats created by fees from an audit client, the firm may consider the fee quoted or charged or actually paid for the specific service, depending on the time and circumstances of the evaluation.

Q2: Section 410 refers in various places to "audit fees" and "fee for the audit of the financial statements." Are these the same?

A: No, they are not the same. Paragraph 410.3.A3 provides that for the purposes of Section 410, audit fees comprise fees or other types of remuneration for an audit or review of financial statements. This is consistent with the general drafting convention established in paragraph 400.2 for Part 4A, whereby the term "audit" applies equally to "review". However, where reference is made in paragraphs 8410.23(a), 410.25.A1 and 8410.31(a) specifically to the "fee for the audit of the financial statements," this does not include any fee for an audit of special purpose financial statements or a review of financial statements.

1: In this document, the term "fee" is used in line with its definition in the Glossary to the Code.

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- Q&As Relevant to PIEs Only
 - Fee Dependency
 - Enhanced Transparency with Respect to PIE Audit Clients
 - Communication with Those Charged with Governance
 - Public Disclosure

This Questions and Answers (Q&A) publication is issued by the Staff of the International Ethics Standards Board for Accountants (IESBA). It is intended to address national standard setters, IESAC member bodies, and professional accountants. It is not intended to be used as a substitute for public practice guidance. It is intended to be used in conjunction with the fee-related provisions of the IESBA International Code of Ethics for Professional Accountants (Including International Independence Standards) (the Code). The IESBA issued its first pronouncement in April 2022.

This publication is designed to highlight, illustrate or explain aspects of the revised fee-related provisions in the Code, and thereby assist in their proper application.

This publication does not amend or override the Code, the text of which alone is authoritative. Reading the Q&As is not a substitute for reading the Code. The Q&As are not intended to be exhaustive and reference to the Code should always be made. This publication does not constitute an authoritative or official pronouncement of the IESBA.

IESBA Staff Q&As - Fees

- Relevant to both PIE & non-PIE audit clients
- Threats created by fees paid by audit client
- Proportion of Fees
- Fee Dependency
- Transparency for PIE audit clients:
 - Communication with Those Charged with Governance
 - Public Disclosure

Available on the [IESBA's website](https://www.iesba.org/)

Audit Partner Rotation (Long Association)



Audit Partner Rotation (Long Association) requirements

- Audit partner rotation requirements in Australia align with international requirements in the IESBA Code.
- Effective from 1 January 2019
- Interaction of Code and *Corporations Act 2001* requirements led to separate outcomes for some PIE entities
- For audit client PIEs other than Listed Entities and APRA regulated entities, Firm applied the Code requirements
- For Listed Entities and APRA regulated entities, a transition period applied
- **The transition period ends 31 December 2023**



Partner Rotation – Listed & APRA-Regulated Entities

| Role | Transition (1 Jan 2019 to pre 31 Dec 2023) | | Full Provisions (from 31 Dec 2023) | |
|--------------------------|---|-------------------------|---|-------------------------|
| | Time on (yrs) | Cooling off (yrs) | Time on (yrs) | Cooling off (yrs) |
| Engagement Partner | 5/7** | 3 | 5/7** | 5 |
| EQCR Partner | 5/7** | 3 | 5/7** | 3 |
| Other Key Audit Partners | 7 | 2 | 7 | 2 |

*** In accordance with applicable laws and regulations, Audit Engagement and EQCR Partners can serve in the same role for a maximum of five years, but may be extended by the Audit Client or a regulator in accordance with applicable laws and regulations.*

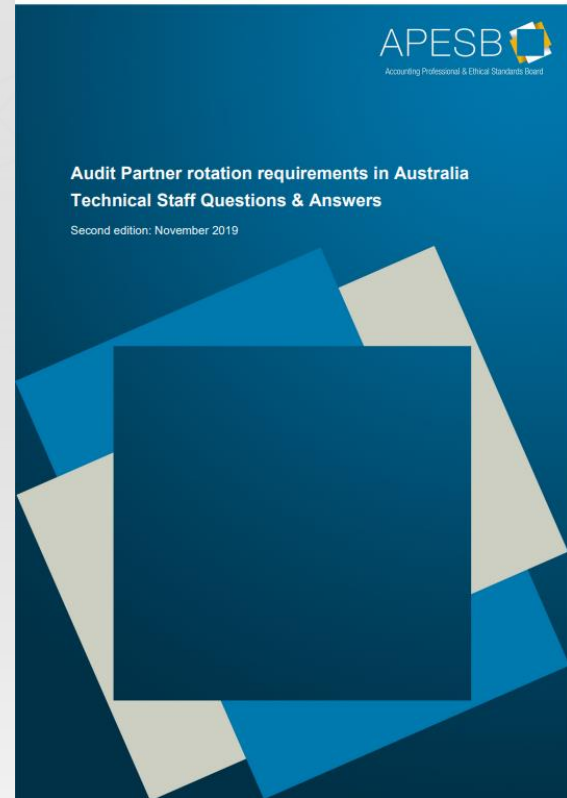
Resources – Audit Partner rotation

APESB Technical Staff Q&As

Audit Partner rotation requirements in Australia

- General provisions – all audit clients
- Specific provisions – PIE audit clients
- Combination of roles
- Determination of cooling-off period
- Flowcharts mapping application of provisions
- First edition: December 2017
- Second edition: November 2019

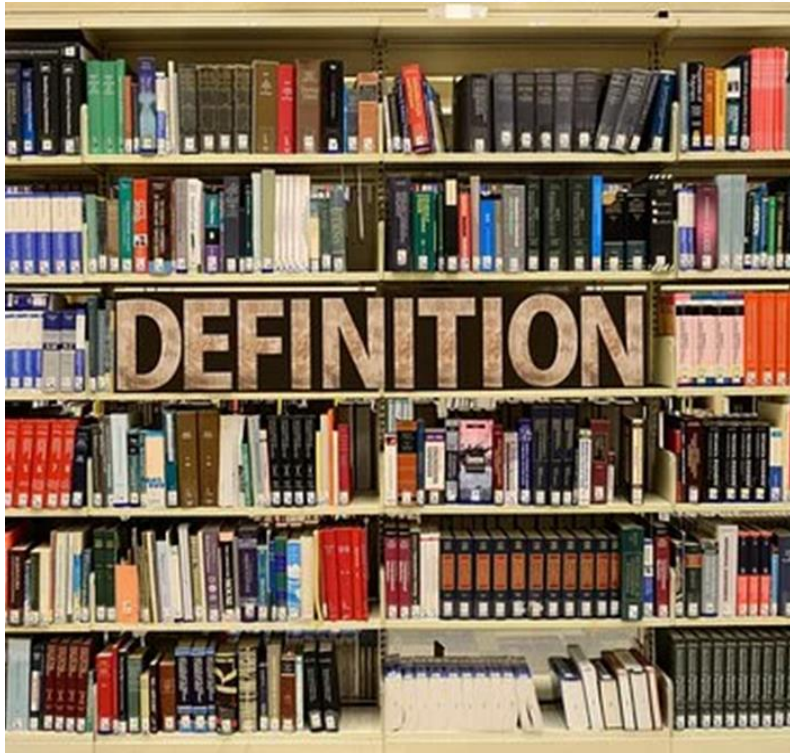
Available on [APESB's website](#)



Definitions of Listed Entity and Public Interest Entity



Current Australian requirement on PIEs



- Definition of Public Interest Entity (PIE) includes listed entities
- From 1 January 2013, APESB mandated Firms to determine whether additional entities are PIEs (para AUST R400.8.1)
- Determination is based on large number/wide range of stakeholders and considering nature of the business, size & number of employees
- APES 110 requirement higher than IESBA Code

Supporting Australian application material on PIEs

The following entities will generally be considered as PIEs (AUST 400.8.1 A1):

- Authorised deposit-taking institutions and authorised non-operating holding companies (NOHCs) regulated by APRA
- Authorised insurers and authorised NOHCs regulated by APRA
- Life insurance companies and registered NOHCs regulated by APRA
- Private Health Insurers regulated by APRA
- Disclosing Entities
- Registrable superannuation entity (RSE) licensees, and RSEs under their trusteeships that have five or more members regulated by APRA
- Other issuers of debt and equity instruments to the public

New proposed definition of PIE

IESBA Code

3 specific mandatory categories:

- Publicly traded entity (*replaces listed entity*)
- Deposit-taking institutions
- Insurers

1 broad mandatory category:

- Entity required under local law, regulation or professional standards (*Guidance in para 400.18 A2*)



APES 110

Guidance on Australian PIEs in proposed para AUST 400.18 A3 (*retains existing categories*)

Determining PIEs

APES 110 proposes to retain firms being mandated to determine PIEs

Expanded non-exhaustive list of factors to evaluate the level of public interest in the financial condition of an entity

Nature of the business or activities (e.g., financial obligations to the public)

Subject to regulatory supervision over the entity's financial obligations

Size of the entity

The importance of the entity to its sector (e.g., replaceable in the event of financial failure)

Number and nature of stakeholders (e.g., investors, customers, creditors & employees)

Potential systemic impact in the event of financial failure

Transparency Requirement



Transparency

R400.20 and R400.21

- To meet the public expectations on transparency of firm independence
- Firms are required to publicly disclose if they have applied the independence requirements for PIE to an audit
- The disclosure has to be in a manner deemed appropriate
 - What is appropriate?
 - IAASB PIE project - Auditor report disclosures
- Exception when disclosure will result in disclosing confidential future plans of the entity (e.g., IPO plan)

Resources – Listed Entity and Public Interest Entity

The screenshot shows the IESBA Staff Questions & Answers page for March 2023. The main heading is "Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code". Below this is a section titled "Overarching Objective for Additional Independence Provisions for PIEs" with a sub-heading "1.1". The text discusses paragraph 405.8 and its application to public interest entities (PIEs). A table of contents is visible on the right side of the page, listing sections 1 through 3. The bottom of the page contains a disclaimer stating that the publication is not a substitute for reading the Code and that the Q&As are not intended to be exhaustive or reference to the Code text should always be made.

IESBA Staff Q&As – Definition of Listed Entity & PIEs

- Overarching objective - additional independence for PIEs
- Evaluating extent of public interest in an entity's financial condition
- Publicly traded entities
- Proportion of Fees
- Adoption of PIE definition by local bodies
- Determining other entities as PIEs
- Public Disclosure of application of PIE Independence requirements

Available on the [IESBA's website](https://www.iesba.org/)

Q & A



Further Information

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