



30/08/21

Mr Channa Wijesinghe
Chief Executive Officer
Accounting Professional & Ethical Standards Board Limited (APESB)
Level 11
99 William Street
Melbourne VIC 3000
Australia

Dear Channa,

Re: EXPOSURE DRAFT – PROPOSED AMENDMENTS TO FEE-RELATED PROVISIONS OF APES 110 CODE OF ETHICS FOR PROFESSIONAL ACCOUNTANTS (INCLUDING INDEPENDENCE STANDARDS)

This submission is made jointly by the following SMSF specialist audit firms:

- Elite Super
- Tactical Super
- Peak Super Audits
- Apex Super Audits
- Red Willow Super
- Terri Scott Accounting

These firms together represent:

- Several decades of expertise & experience in the SMSF audit sphere;
- Outstanding recognition and qualification in SMSF audit;
- A well-recognised standard of best-practice in SMSF audit.

The managing directors of many of the above practices are award-winning SMSF auditors and members of the ATO's SMSF Auditor Stakeholder Group. As specialist SMSF auditors, we all support the alignment of the domestic Code of Ethics issued by APESB with the International Code of Ethics. We welcome the opportunity to make this submission to the APESB regarding the above-mentioned Exposure Draft. Our submission specifically addresses our concerns regarding the 20 per cent threshold to assess referral fee dependency as laid out in paragraph AUST R410.14.1.

Our submission opens by identifying the threats to auditor independence associated with fee dependence. We proceed to challenge the adoption of a 20 per cent fee threshold as neither consistent with international standards nor warranted to ensure auditor independence when dealing with clients that are not public interest entities. We close with recommendations that we believe



would improve the clarity of fee independence and available safeguards within the SMSF audit context.

Thank you for your time in considering this submission.

Yours gratefully,

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APPENDIX A: About Us



1. Fee Dependency and Threats to Auditor Independence

The Issue

It is common in the SMSF audit industry for an audit firm to receive multiple client referrals from a single accounting firm. Where a significant proportion of the SMSF audit firm's revenue is derived from a single referral source, there is a risk that the audit firm will become dependent upon that referral source. The firm's concern regarding potential loss of clients obtained by that referral source is likely to create self-interest threats and possibly also intimidation threats for auditors within the audit firm.

As specialist SMSF auditors, we acknowledge this risk. As owners of relatively small practices that specialise in the superannuation audit function, we have each worked with threats of this nature and implemented safeguards to ensure that our independence is not compromised.

A Benchmark is a Red Flag

We welcome the ATO's request to quantify a referral source fee percentage that should prompt any audit firm to assess self-interest and intimidation threats and ensure appropriate safeguards are instituted. A benchmark provides clarity. As emphasised in early stakeholder discussions with the ATO, a benchmark percentage is a highwater mark guide. It must not be assumed that auditor independence is not threatened by fee referral sources comprising a lower percentage. For example, self-interest and intimidation threats may exist where only 18 per cent of total fees are derived from a single referral source due to qualitative factors that increase the value of that referral source to the audit firm. Referral fee dependency threats are ultimately a question of professional judgement and must be assessed on a case-by-case basis.

To put it simply: a benchmark referral fee percentage is a red flag for the purpose of clarity. It is not, and should not be regarded as, a hard line in the sand.

2. Why a 20 Percent Fee Threshold in the Ethics Code is Not Appropriate

We do not believe it is appropriate to codify this 20 per cent guidance benchmark within the Ethics Code.

The 20 per cent fee threshold was initially presented as guidance by the regulator. Specifically, the ATO stated:

The Code does not specify a number of referral sources, or set percentage of fees from one or more referral sources or clients, required to reduce independence threats to an acceptable level. Nor does it explain what constitutes a 'large proportion' of a firm's total fees. However, for well-established firms that generate most of their income from providing SMSF auditing services, as a guide, if the fees generated from one referral source are less than 20 per cent of the firm's total fees, we would not consider this in itself to create independence threats.



Presenting the 20 per cent threshold as a shot across the bows calling for fee dependency awareness was acceptable, particularly where (as explained above) the Code was silent on an issue that is relatively unique to the SMSF audit industry, where large numbers of audit clients are obtained by referral.

We appreciate that codification of the 20 per cent threshold was proposed due to concerns by the APESB and ATO that the international approach in this area is insufficiently robust. There is concern that a threshold of 30 per cent total audit fees with a 5-year period of grace for young and growing practices is too high. Action is proposed to reduce the Code threshold to 20 per cent of total fees where derivation is linked to the same referral source.

We have several objections to this proposed codification.

Objection 1: Inconsistency between Australian and International Standards

While we appreciate the concerns of APESB and ATO in this area, we do note that the Parliamentary Joint Committee (PJC) on Regulation of Auditing in Australia (see Interim Report, published February 2020) did not identify any specific concerns relating to independence threats created by concentration of fees from a specific referral source.

While this does not mean that action to tighten independence requirements in this area is inappropriate, we feel that the absence of specific recommendation by the PJC should be weighed carefully before Australia departs from the international standard in this matter of fee dependency.

Objection 2: Inconsistency between treatment of Australian audit firms

We are also concerned that the proposed AUST R410.14.1 differentiates unfairly between practices that derive smaller individual fees by referral and those that derive larger audit fees on a client-by-client basis.

As discussed above, SMSF audit firms often derive fees by a referral source, ie an accounting practice. In this sense, fee derivation for SMSF auditors is different from many other areas of audit practice in Australia. All audit firms (large or small, direct fee or referral-based) encounter the same fee dependency threats when experiencing some level of dependency upon a single revenue source. Indeed, while an individual client may exert pressure upon the auditor directly, disgruntled trustees are less able to do so in a referral-type situation. If the referring accountant attempts to influence the auditor on behalf of their client base, the risk is no higher than if that fee source represented the revenue stream from a single, large client. We do **not** believe that it is appropriate to differentiate between a fee dependence threshold for referral-based firms and wider audit practice. If the international standard of 30 per cent and 5-year continuity is inappropriate for SMSF auditors, we feel it is equally inappropriate for other audit firms.

Far from being more at risk in this sense than our wider audit counterparts, it is our view that SMSF auditors already benefit from unique independence safeguards in the form of:



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- Specific ATO reporting thresholds, which compel SMSF auditors to report certain contraventions, irrespective of fee source or client identity;
 - Rigorous review practices by ATO and professional bodies, which are continually scanning for, identifying, and correcting those auditors whose independence is compromised.

Both the APES 110 Code of Ethics and the International Code of Ethics have a clear existing position that where an audit firm receives more than 30 per cent of its total fees from the same audit client over a period of 5 continuous years, the audit firm must consider whether independence safeguards are required. Unless there is a clear reason to regard a referral fee source as creating independence risks different to those presented by an audit client fee source, we do not see any reason for inconsistency in the benchmarks referred to in AUST R410.14.1 and R410.15. Please see our Recommendation below regarding codification of the fee referral source benchmark.

Objection 3: Arbitrary figure & heavy impact upon smaller practices

The 20 per cent threshold is an arbitrary figure. It has not been demonstrated by data or analysis to be a suitable benchmark. The SMSF audit industry has not been adequately consulted as to whether it is appropriate to incorporate this threshold in the APES 110 Code of Ethics.

Inclusion of this percentage in the Code will require audit firms to be prepared to defend their independence in terms of the safeguards outlined in the code, some of which are ambiguous and open to interpretation. Many smaller audit practices will be impacted by the codification of a 20 per cent threshold, and possibly in ways unforeseen by the APESB.

For example, a specialist practice known by this group has raised an interesting dilemma it may face if this threshold is to be codified. The practice in question currently has 7 different referral sources, each of which represents a similar number of engagements each year. No single referral source represents more than 20 per cent total fee revenue for the firm – but if one of those referral sources were to be lost, the audit firm would find itself with several referral sources exceeding the 20 per cent threshold.

In this scenario, the 20 per cent benchmark could have the effect of incentivising SMSF auditors to maintain a specific number of referral sources in order to ‘pass under the radar’. Rather than lose a revenue source that will create fee dependency issues, the auditor may commit very strongly to its existing referral base. The 20 per cent threshold may itself create an independence issue for the auditor as they seek to maintain all existing referral sources.

While smaller practices encounter the same independence threats as larger practices and should not be differentiated, it is important to acknowledge the extent smaller practices will be affected and consider:

- The necessity of using 20 per cent as a catalyst to institute safeguards in the Code;
 - The way in which safeguards may be implemented to address a fee dependency threat.
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There is no clear justification for selecting 20 per cent as a codified benchmark for referral fee dependency. Introduction of this benchmark will impose hardship upon smaller practices and should not be adopted without full consultation with the industry, particularly with smaller players that have navigated this territory and established reputations of excellence.

Objection 4: No specific consideration of new firms

We are concerned to note that the proposed AUST R410.14.1 does not consider the situation of new firms that are actively attempting to grow a client base. While 410.14 A3 notes that the intention to diversify may reduce dependence upon an audit client, building a client base takes time, usually a period of years. New firms will be challenged to finance an extensive engagement review and in practice often turn to other safeguards, such as consultation with another auditor or expert on challenging judgements. We feel that the new firm situation should be acknowledged in the Code. Please see our Recommendation below regarding new firms and a period of grace.

3. Improving Clarity in the Application of Safeguards

The APES 110 Code of Ethics 410.14A7 provides examples of actions that may provide safeguards to address self-interest or intimidation threats that arise as a result of fee dependency.

These are:

- Having an appropriate reviewer who was not involved in the Audit Engagement review the audit work.
- Ensuring that the compensation of the partner is not significantly influenced by the fees generated from the client.
- Reducing the extent of services other than audit provided by the partner or Office to the Audit Client.
- Increasing the client base of the partner or the Office to reduce dependence on the Audit Client.
- Increasing the extent of services provided by the partner or the Office to other clients.

Source: APES 110 Code of Ethics, 410.14 A7

Our concerns in relation to clarity surrounding these safeguards relate to the first item: the appointment of an appropriate reviewer. We feel the concept of 'appropriate reviewer' is well defined by the Code (see APES 110 Code of Ethics, Glossary). The ATO further elaborates upon its



understanding of an ‘appropriate reviewer’ and its expectations for review documentation. We feel however that the words: ‘review the audit work’ are ambiguous and open to interpretation.

Does this mean, review every audit obtained by the referral source of concern? We have spoken with experienced auditors who feel this may be implied. If so, we believe this is overkill and imposes unnecessary cost upon the audit firm. We believe there should be an emphasis in review upon challenging judgments or engagements where the auditor’s independence may be particularly at risk (for example, the audit of partners’ funds). Please see our Recommendation below regarding clarification of this safeguard.

We are also of the opinion that safeguards are available to SMSF auditors in addition to those mentioned above in 410.14A7. If the 20 per cent benchmark is instituted with intended application for the SMSF auditor, we feel it is also appropriate that the Code recognise safeguards that are available to this industry and are frequently used by best-practice firms to strengthen their independence. Please see our Recommendation below regarding this matter.

4. Recommendations:

A. Codify 30 per cent & 5 years as a referral fee dependency benchmark

We strongly recommend a 30 per cent threshold be adopted by the APESB in proposed AUST R410.14.1 as opposed to a 20 per cent threshold. We believe codifying 30 per cent is consistent with both R410.15 and international standards. We believe 30 per cent fee dependency upon a single referral source is an appropriate ‘red zone’ in which any SMSF audit practice should be prepared to defend their independence by use of appropriate safeguards as outlined in the Code.

As specialist SMSF auditors who have each undergone the experience of growing a client base, we do **not** believe that 2 years is a realistic timeframe in which to resolve fee dependency issues by natural growth. We believe that a period of 5 years provides reasonable opportunity for most firms to achieve this. If 5 years has lapsed without sufficient growth to reduce the referral source fees to below 30 per cent, we believe an audit firm should be accountable to demonstrate its independence by use of relevant safeguards presented in the Code.

It should be recalled that fee dependency is an issue that must be considered on a case-by-case basis. A codified threshold is a highwater mark only.

Should APESB, the ATO and professional bodies believe that the 30 per cent / 5-year threshold is inappropriate, we recommend that this be adjusted consistently for both audit firms that derive fees per client and by referral.

B. Insert AUST 410.14.1 A2 to clarify application of ‘appropriate reviewer’ safeguard in situations of referral fee dependency



We believe it would be instructive to add a guidance paragraph AUST 410.14.1 A2, specifying an acceptable approach to applying the ‘appropriate reviewer’ safeguard. We recommend codifying:

1. The manner in which a suitable number of referral source funds should be selected for examination by an appropriate reviewer (in terms of fund selection, we suggest that the appropriate reviewer discuss the independence threat from the referral source with the auditor. Based on their assessment of risk, the reviewer should then select an appropriate sample of funds);
2. That in selecting engagements for review, there should be an emphasis upon both challenging judgements and audits relating to SMSFs of those partners within the referral firm. This is a responsible approach to review and should be codified to prevent a review percentage being made up of ‘easy funds’.

C. Consultation an Additional Safeguard

Many new audit firm and smaller audit practices would find it financially crippling to pay an appropriate reviewer to consider any significant number of audit engagements. Many best-practice firms habitually safeguard their independence when making challenging or difficult audit decisions by consulting with an expert – either a knowledgeable colleague or a professional body with expertise in the relevant area. Consultation is documented and outcomes are included as evidence in the audit file.

In many situations, we feel expert consultation is an appropriate alternative to engaging an appropriate reviewer. Should the APESB proceed with instituting the 20 per cent benchmark for fee referral dependency, we strongly recommend that expert consultation be recognised as an alternative safeguard.



APPENDIX A: About Us



About Elite Super:

Elite Super Auditors are in the top 20 leading SMSF audit firms in Australia. For 16 + years, we have carved out a niche for premium quality Australian based SMSF audits hand in hand with SIS compliance and real-time advice for accountants and SMSF administrators. Katrina Fletcher started the practice early 2005, building the business to numerous staff and contractors doing some 1500+ SMSF audits a year. Being A Chartered Accountant, and further specialising in SMSF Specialist Advisor and Auditor with the SMSF Association. With considerable legal knowledge (majority of a LLB completed at UNE) and 8 years in a legal / accounting practice, Elite Super offers expert SMSF technical advice and assistance to our clients. Elite Super chairs / runs the SMSF Association local events on the mid-North Coast of NSW. We also have representation on the ATO SMSF Auditors Professional Association Stakeholders group. Recently Katrina was awarded Superannuation Auditor of the year from the Australian Accounting Awards.



About Tactical Super:

Tactical Super is a specialist SMSF audit firm that commenced in Geelong in 2008. Deanne Firth FCA, Director of Tactical Super is an SMSF Specialist whose focus is on all things super. She is a fellow of the Institute of Chartered Accountants, member of CA ANZ Regional Council, a CA SMSF Specialist and a registered SMSF auditor. She manages a team of highly experienced auditors and focuses on efficiency to ensure fast turnaround. Deanne also speaks at a variety of conferences on superannuation and audit.



About Peak Super Audits:

Peak Super Audits is an Australian based specialist SMSF auditing firm. Naomi Kewley is Peak's managing director. She is a Tax Masters graduate and chartered accountant, while also being an active member of the SMSF Association, holding both accreditations of SMSF Specialist Auditor and SMSF Specialist Advisor. Prior to joining the audit sphere, Naomi worked as an accountant on a one-on-one basis with SMSF trustees and their advisers. As an auditor, she enjoys assisting accountants & trustees in understanding their obligations within the evolving landscape of SMSF compliance.

In 2018, Naomi was a recipient of the SMSF Association's Specialist Auditor Top Achiever Award. In 2019 and again in 2020, Naomi received the Women in Finance award for Auditor of the Year.



About Apex Super Audits:

Apex Super Audits is an Australian owned and operated specialist SMSF audit practice. As Apex's managing director, Jacob Kewley is passionate about bringing a fresh perspective to the industry - utilising developing technology to maximise timeliness and effectiveness in the SMSF audit. He is a firm believer in the value the specialist auditor can bring to the client relationship. Jacob is a Chartered Accountant and holds dual accreditation with the SMSF Association as an SMSF Specialist Advisor and SMSF Specialist Auditor.



About Red Willow Super:

Red Willow Super is a specialist SMSF audit practice. Marjon Muizer, the managing director is an accredited SMSF specialist auditor and CPA with over 16 years of experience in SMSF administration, education, technical & compliance roles. Marjon has co-written the SMSF auditor's exam and audit training modules for the SMSF Association.



About Terri Scott Accounting:

Terri Scott is the sole director of Terri Scott Accounting Pty Ltd trading as Tax & Super Audits, a specialist independent SMSF audit practice in addition to offering taxation compliance services.

Terri has been in public practice since 2004, is a Chartered Accountant with CAANZ, a Registered Tax Agent, an Associate member of the Tax Institute, and a member of the SMSF Association, holding accreditation of SMSF Specialist Auditor.

In 2011, Terri was a recipient of the SMSF Specialist Auditor Top Achiever Award for achievement in the SMSF Association specialist exam.