



28 October 2011

The Manager
Corporate Reporting and Accountability Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: auditquality@treasury.gov.au

Dear Sir/Madam,

RE: Corporations Legislation Amendment (Audit Enhancement) Bill 2011

Accounting Professional & Ethical Standards Board Limited (APESB) welcomes the opportunity to make a submission on the Corporations Legislation Amendment (Audit Enhancement) Bill 2011.

APESB's role in the accounting profession

APESB is governed by an independent board of directors. Its primary objective is to develop and issue, in the public interest, appropriate professional and ethical standards which apply to the membership of the three Australian professional accounting bodies. A secondary objective of APESB is to provide an opportunity or forum for the discussion and consideration of issues relating to professional and ethical standards for accountants. APESB is funded by the three major accounting bodies, but has complete independence in its standard-setting activities.

In setting standards, we endeavour to incorporate a strong emphasis on professionalism and the role of sound judgement in those accountants obliged to follow our standards. We believe that setting high quality standards with demanding criteria contributes to the professional standing and behaviour of members of the accounting profession.

Within its mandate, APESB promotes the importance of compliance with professional and ethical standards. We would always be pleased to discuss ways to improve compliance with Treasury, ASIC, FRC and other relevant bodies. We are in regular dialogue with the three accounting professional bodies in relation to their approach to monitoring professional and ethical behaviour. We are also close to the work of the International Ethical Standards Board for Accountants (IESBA) in this

area, and have some influence on its activities, particularly with my role as a public interest member of that board for the last 2 years.

General comments

We commend Treasury on its work on audit quality in Australia. We believe that the proposed amendments will contribute to enhancing audit quality in Australia and will align the Australian Auditing framework with contemporary best practice adopted by other major jurisdictions such as the United States, United Kingdom and Canada.

APESB's Code of Ethics and Professional Standards

The major platform for the APESB standards of professional and ethical behaviour is APES 110 *Code of Ethics for Professional Accountants* (APES 110), which is based on the international Code issued by the IESBA.

APES 110 includes auditor independence requirements applicable for members of the three Australian professional accounting bodies who are auditors and conduct assurance engagements. The revised APES 110 which we issued in December 2010 contains some key changes in respect of auditor independence requirements as follows:

- Introduction of the concept of Public Interest Entities to which the more stringent independence requirements of the Code (such as audit partner rotation) are applicable;
- Introduction of the Key Audit Partner concept in respect of Public Interest Entities and widening of the partner rotation requirements to include Key Audit Partners. Previously the rotation requirements were only applicable to the Lead Engagement Partner, Audit Review Partner (if any) and Engagement Quality Control Reviewer. The expansion of the new definition means that, for example, Partners who audit significant subsidiaries of Public Interest Entities or make significant judgements on an audit engagement will now be subject to the seven year rotation requirement; and

- The separation of the independence requirements for Audit and Review Engagements of financial statements from the independence requirements for Other Assurance Engagements.

We note that your explanatory material for the bill refers to listed entities and other Public Interest Entities. In the other Public Interest Entities category you have included authorised deposit taking institutions and insurance companies subject to APRA regulations. Currently APESB is working on defining a Public Interest Entity in the Australian context and hopes to finalise this work in the next few months. APESB's current proposals are broadly consistent with your views of what constitutes a Public Interest Entity in the Australian context.

APESB issued an Exposure Draft (ED) in September 2011 which proposed that the provisions applicable to Public Interest Entities will commence from 1 January 2013. APESB's proposals in regard to which entities are Public Interest Entities and which entities are likely to be Public Interest Entities in the Australian context are specified in ED 03/11 Proposed Amendments to the Definition of Public Interest Entity in APES 110 *Code of Ethics for Professional Accountants*. An extract of ED 03/11 is provided in Appendix A for your information.

Specific comments

Proposed auditor rotation requirements

APESB supports Treasury's proposal for maintaining the existing five year mandatory rotation period for audit partners and the current two year time out period.

APESB also supports Treasury's proposal to introduce additional flexibility to extend the rotation period up to an additional two years subject to the Directors and/or the Audit Committee of the relevant entity complying with certain specified requirements. We believe that these requirements and the process that the Directors and/or the Audit Committee of the entity will need to follow to grant the extension will provide adequate safeguards.

We note that the maximum seven year audit partner rotation period possible with the proposed added flexibility will be consistent with the seven year partner rotation period in APES 110.

Other comments

We also support the following measures which we believe will contribute to the enhancement of audit quality in Australia:

- Annual transparency reports for audit firms which audit 10 or more Australian listed companies, listed registered schemes, authorised deposit-taking institutions and insurance companies. However, we caution that there should be some flexibility in the reporting requirements for smaller and medium practices that just exceed the threshold compared to a major audit firm that audits a significant number of listed entities ;
- Proposed amendments to the ASIC Audit deficiency notification and reporting process; and
- Proposed amendments to allow ASIC to communicate with those charged with governance of corporations, registered schemes and disclosing entities in certain specified circumstances.

If you would like to discuss further or require any additional information, please do not hesitate to contact me at kspargo@bigpond.net.au or Channa Wijesinghe, Technical Director at channa.wijesinghe@apesb.org.au.

Yours sincerely



Kate Spargo
Chairman

Appendix A – Extract of ED 03/11

Extract of the current proposals in ED 03/11 for your information on entities which are Public Interest Entities and likely to be Public Interest Entities in the Australian context.

Public Interest Entities

290.25 *Section 290 contains additional provisions that reflect the extent of public interest in certain entities. For the purpose of this section, a Public Interest Entity is:*

- (a) A Listed Entity; or*
- (b) An entity (a) defined by regulation or legislation as a public interest entity; or (b) for which the audit is required by regulation or legislation to be conducted in compliance with the same Independence requirements that apply to the audit of Listed Entities. Such regulation may be promulgated by any relevant regulator, including an audit regulator.*

AUST 290.25.1 The following entities in Australia satisfy the conditions in paragraph 290.25:

- Listed Entities as defined in Section 9 of the Corporations Act 2001;*
- Authorized Deposit-taking Institutions that are subject to Prudential Standard APS 510 Governance issued by the Australian Prudential Regulatory Authority (APRA);*
- General Insurance Companies that are subject to Prudential Standard GPS 510 Governance issued by APRA; and*
- Life Insurance Companies that are subject to Prudential Standard LPS 510 Governance issued by APRA.*

290.26 *Firms shall determine whether to treat additional entities, or certain categories of entities, as Public Interest Entities because they have a large number and wide range of stakeholders. Factors to be considered include:*

- The nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders. Examples may include financial institutions, such as banks and insurance companies and pension funds;*
- Size; and*
- Number of employees.*

AUST 290.26.1 The following entities in Australia will generally satisfy the conditions in paragraph 290.26 as having a large number and wide range of stakeholders and thus are likely to be classified as Public Interest Entities. In each instance Firms shall consider the nature of the business, its size and the number of its employees.

- *Disclosing Entities as defined in Section 111AC of the Corporations Act 2001;*
- *Regulated Superannuation Funds other than small APRA funds as defined by APRA Superannuation Circular No. III.E.1 Regulation of Small APRA Funds, December 2000; and*
- *Other issuers of debt and equity instruments to the public.*