

**FRC'S AUDIT QUALITY TASK FORCE  
COMMENTS ON DRAFT CORPORATIONS LEGISLATION AMENDMENT  
(AUDIT ENHANCEMENT) BILL 2011**

**Auditor rotation requirements**

- There was general support for these proposals which are broadly based on a similar approach adopted by the UK Financial Reporting Council (UKFRC).
- There was a discussion around proposed paragraph 324DAB(2)(b) which requires 'a resolution passed by the members of the audit committee'. The point was raised as to whether the resolution should be unanimous or passed by a specified majority of the members of the audit committee. It was agreed that the existing formulation of the proposed requirement was adequate.

**Annual transparency reports**

- There was general support for the annual transparency report requirements in the draft Bill.
- One issue that it was agreed should be raised with Treasury was whether the scope of proposed 332D was broad enough to permit ASIC to allow related audit firms that practised under the same name but were formed as separate partnerships or audit companies in different states or territories, to prepare a single annual transparency report in relation to all the separate networked firms or audit companies.

**Proposed FRC audit quality function**

- The Task Force discussed whether the FRC would be able to adequately fulfil its new audit quality functions given that the FRC's information gathering powers had been narrowed down to the professional accounting bodies. In this context, it was noted that:
  - The power to seek information from audit firms had been removed because this power duplicated ASIC's powers and responsibilities in relation to its ongoing audit inspection program. The purpose of the amendments is to remove the existing duplication of functions in relation to auditor independence.
  - There is currently no information gathering powers vested in the FRC in relation to ASIC. However, there is already an existing framework for the sharing of information between ASIC and the FRC which has been relied on for purposes of the FRC carrying out its existing auditor independence function.
    - : paragraph 127(4)(a) of the ASIC Act permits ASIC to disclose information to the FRC where the ASIC Chairman is satisfied that the particular information will enable or assist the FRC to perform or exercise any of the FRC's functions or powers;
    - : paragraph 237(2)(d) permits the FRC to disclose information to ASIC for the purposes of its performance of its functions under the corporations legislation;
    - : the existing memorandum of understanding (MOU) between ASIC and the FRC records an understanding reached between ASIC and the FRC to facilitate liaison, cooperation, assistance and the exchange of information between the two agencies in accordance with the relevant statutory provisions. It is noted that when the FRC's audit quality function commences after the enactment of the

legislation, it will be necessary for ASIC and the FRC to amend the existing MOU by deleting references to the FRC's auditor independence function and substituting references to the FRC's new audit quality function; and

- it is also important to bear in mind the proposed audit quality function is advisory in nature and is not intended to be an operational function.

#### **Audit deficiency reports**

- The release by the US Public Company Accounting Oversight Board (PCAOB) on 17 October 2011 of an inspection report on Deloitte & Touche in the US that was written in 2008 and covered audits undertaken in 2007, was noted and discussed in the context of the proposals in the Audit Enhancement Bill in relation to audit deficiency reports.
- The Task Force also noted that the amendments in relation to audit deficiency reports were broadly based on the approach that had been adopted in relation to public audit inspection reports by the Canadian Public Accountability Board (CPAB).
- Notwithstanding the due process requirements already built in to the proposals, including the six month period before ASIC can prepare and publish an audit deficiency report on its website, there is a view within the audit profession that some form of independent review should be available before ASIC exercises its power to publish an audit deficiency report.
  - The Task Force agreed that the AAT is probably not appropriate as the review body given the delay before a hearing could be held and the lack of specialist financial reporting and audit expertise within the AAT.
  - The Task Force discussed whether a reconstituted Financial Reporting Panel (FRP) or reconstituted Companies Auditors and Liquidators Disciplinary Board (CALDB) may be more appropriate (acknowledging that these options would have resource implications, would require legislative change and that any third party review would inevitably delay the process, having regard to the fact that ASIC already must allow for a six month period before it can publish an audit deficiency report).
  - There was a view that an ASIC regulatory guide on how it proposed to administer the audit deficiency report provisions may be also be helpful. There may be scope for the AUASB to assist ASIC in developing a regulatory guide.

#### **ASIC communication with audited bodies**

- The Chairman of the FRC requested the Task Force to consider the requirement in proposed subsection 127(2D) of the ASIC Act which authorises ASIC to communicate with 'the directors, the audit committee or a senior manager'. The Chairman is concerned that an ASIC communication to a senior manager may not be passed onto the directors or the audit committee.
  - The Task Force noted that the communication to a senior manager was intended to enable ASIC to disclose information to the CFO and reflects a comment made by the G100 to Treasury during the consultative process.
  - It was considered that in the larger entities there would invariably be an internal governance rule that required management to pass onto the board any communication from a regulator.

- However, the Chairman’s concern may be relevant in the context of smaller entities where the internal governance arrangements may not be as rigorous as in larger entities. Accordingly, the Task Force concluded that Treasury should consider the possibility of amending subsection 127(2D) to ensure that an ASIC communication to a senior manager should be required to be passed onto the directors or the audit committee by the senior manager.
- While the Task Force was of the view that the concept underlying the provisions was sound, it was felt that it was always desirable to encourage direct communication between the auditor and the audited body. In that context, the Task Force discussed whether the existing words in subsection 127 (2D) might allow the ASIC Chairman to authorise the auditor to communicate the relevant information to the audited body in appropriate cases.
- The Task Force also considered that a regulatory guide as to how ASIC proposes to administer these provisions would be helpful. There may be scope for the AUASB to assist ASIC in developing a regulatory guide.

