



**Subject:** Agenda for the 86th meeting of the AUASB  
**Venue:** Executive Boardroom  
Tertiary Education Quality and Standards Agency (TEQSA) offices  
Tower Level 14, 530 Collins Street Melbourne  
**Time:** Tuesday, 29 November 2016 from 8.30 a.m. to 5.00 p.m.

Note: Agenda papers marked

P	Distributed Previously
E	Enclosed
F	To Follow
T	To be Tabled at Meeting
V	Verbal Report

Time	Agenda Item No.	Type	Resp.
8.30 am.	<b>1. Preliminary Session</b>		
	(a) Welcome	V	MK
	(b) AUASB Declarations of Interest	E	MK
	(c) Minutes of Previous AUASB Meeting	E	MK
	(d) Matters Arising from Previous Meetings and Action List	E	All
8.45 am	<b>2. ASAE 3100 Compliance Engagements</b>		
	(a) Comments and proposed disposition paper	E	MM
	(b) Final draft ASAE 3100 Standard for approval (marked up)	E	MM
9.45 am	<b>3. Audit Committee Guide Review and Comment First Draft</b>	E	RH
<b>10.15 am</b>	<b>Break</b>		
10.30 am	<b>4. GS 001 Concise Financial Reports Review and Comment First Draft</b>	E	RH
11.00 am	<b>5. International Update</b>		
	(a) IAASB Emerging External Reporting – AUASB Draft Submission	F	MM
	(b) IAASB meeting papers	F	All
<b>12.30 pm</b>	<b>Lunch</b>		
1.30 pm	<b>5. International Update continued</b>		
	(b) IAASB meeting papers (continued)	F	All
2.30 pm	<b>6. NOCLAR Consider timing and exposure drafts</b>	E	MD
3.00 pm	<b>7. Auditor Reporting FAQs</b>	F	AW
	(a) Approval of FAQs	F	AW
	(b) Future FAQs	F	AW
	(c) Post implementation review project with Canada	F	AW
	(d) Interim Reviews	F	AW



Time	Agenda Item No.	Type	Resp.
	(e) Feedback from recent AGM	F	AW
3.40 pm	<b>Break</b>		
3.50 pm	<b>8. Other</b>		
	(a) Jim Sylph visit	V	MK
	(b) Data Analytics Roundtables	V	AW
4.10 pm	<b>9. Board Review* (closed session)</b>	V	MK
5.00 p.m.	<b>Close</b>		



## AUASB DECLARATION OF INTERESTS

as 16 November 2016

AUASB Member	Professional Affiliations	Listed Entity Affiliations	Other Relevant Matters
Ms Merran Kelsall (Chairman)	FCA FAIM FAICD FCPA	Nil	Member, IAASB IAASB Activities: Member - Steering Committee Member - Innovation Working Group Chair - Integrated Reporting Working Group Leader - Audit Quality Member, NZAuASB Part time member, Financial Reporting Council (FRC) Director, RACV Ltd Chairman, Australian Health Service Alliance Ltd Director, Melbourne Water Corporation Board member, TarraWarra Art Museum Director, VicSuper
Ms Robin Low (Deputy Chairman)	FCA GAICD	Director, AUB Group Limited Director, CSG Limited (CSV) Director, IPH Limited (IPH) Director, Appen Limited (APX)	Director, Public Education Foundation Ltd Director, Primary Ethics Ltd Deputy President and Treasurer, Sydney Medical School Foundation Member, CA ANZ Professional Conduct Committee

<b>AUASB Member</b>	<b>Professional Affiliations</b>	<b>Listed Entity Affiliations</b>	<b>Other Relevant Matters</b>
Mr Robert Buchanan	Barrister and Solicitor of the High Court of New Zealand Member of the Institute of Directors in New Zealand	Nil	Chairman, NZAuASB Principal, Robert Buchanan Public Law and Governance (Wellington, New Zealand) Member, Governance Advisory Board of the Privacy Commissioner (New Zealand) Member, Risk and Assurance Committee of the Parliamentary Service (New Zealand) Trustee of a family trust
Ms Jo Cain	GAICD	Nil	Executive Director, Materiality Counts Non-Executive Director, Australasian Reporting Awards (ARA) Non-Executive Director, Banksia Environmental Foundation Member, Workways Australia Audit and Risk Committee
Mr Chris George	FCA FCPA MAICD	Nil	Partner, Ernst & Young Member Salvation Army Eastern Territory Audit Advisory Committee
Professor Nonna Martinov-Bennie	FCA FCPA Member, AAA Member, AFAANZ Member, AICD Honorary Member, Business and Professional Ethics Group (BPEG), USYD	Nil	Professor of Accounting and Director of International Governance and Performance Research Centre (IGAP), Macquarie University
Ms Caithlin Mc Cabe	Member, CA ANZ Fellow, Institute of Chartered Accountants in Ireland		Partner, Deloitte Touche Tohmatsu Member of the Australian Public Policy Committee

<b>AUASB Member</b>	<b>Professional Affiliations</b>	<b>Listed Entity Affiliations</b>	<b>Other Relevant Matters</b>
Ms Jane Meade	FCA	Nil	Group Executive Director, Australian National Audit office Former partner RSM Australia
Mr Colin Murphy	FCPA FCA FCSA	Nil	Auditor General for Western Australia
Ms Carolyn Ralph	Member, CA ANZ		Partner, KPMG
Mr Ashley Wood	Member, CA ANZ;  Fellow of the Institute of Chartered Accountants of England & Wales		Partner, PricewaterhouseCoopers Australia



**Subject:** Minutes of the 85<sup>th</sup> meeting of the Auditing and Assurance Standards Board (AUASB)  
**Venue:** Ken Spencer Meeting Room, Tower Level 14, 530 Collins Street, Melbourne  
Teleconference  
**Date:** 25 October 2016 from 10.30 a.m. to 12.00 p.m.

#### **Attendance**

AUASB Members:

- Ms Merran Kelsall (Chairman)
- Mr Robert Buchanan
- Ms Jo Cain
- Prof. Nonna Martinov-Bennie
- Ms Caithlin Mc Cabe
- Ms Jane Meade
- Ms Carolyn Ralph
- Mr Ashley Wood

AUASB Technical Group:

- Mr Mark Dowling
- Ms Rene Herman
- Ms Marina Michaelides
- Ms Anne Waters

Apologies:

- Ms Robin Low (Deputy Chairman)
- Mr Chris George
- Mr Colin Murphy

#### **Welcome and Declarations of Interest**

##### **(Agenda Item 1 – Minute 1064)**

“Declaration of Interests” forms for members were tabled and confirmed. Members have adopted a standing policy in respect of declarations of interests that a specific declaration will be made where there is a particular interest in an issue before the AUASB.

#### **Minutes**

##### **(Agenda Item 1 – Minute 1065)**

Subsequent to some minor editorials, the AUASB approved the minutes of the 84<sup>th</sup> meeting held on 13 September 2016.

#### **Matters Arising and Action List**

##### **(Agenda Item 1 – Minute 1066)**

The status of matters arising and action items brought forward from the previous AUASB meeting was noted. The AUASB requested that the topics of group audits, audit quality and professional scepticism remain as open projects on the matters arising and action list.



## **ASAE 3500 *Performance Engagements* Project Update**

### **(Agenda Item 2 – Minute 1067)**

The AUASB received an update on the progress of ED XX ASAE 3500 *Performance Engagements*, which included a brief overview of the discussion at the 15 September 2016 project advisory group (PAG) meeting.

The PAG discussed the terminology in the draft ED which includes the term 'outputs' and 'outcomes' in relation to the performance activity. The PAG's view is that this terminology is over complicating the ED for direct performance engagements, as although such terminology is used in Service Performance Reporting engagements, these are of a different nature. The AUASB commented that when the assurance practitioner undertakes a performance engagement and identifies the appropriate criteria to apply in the engagement circumstances, the outputs and outcomes of the performance activity would usually be considered. It was agreed that this terminology may need to be addressed in the application material in the draft ED XX ASAE 3500.

## **ASAE 3100 *Compliance Engagements* Project Update**

### **(Agenda Item 3 – Minute 1068)**

The AUASB received an update on the progress of ASAE 3100 *Compliance Engagements* project. A disposition of comments received paper will be brought to the 29 November 2016 AUASB meeting.

## **Auditor Reporting Frequently Asked Questions approval**

### **(Agenda Item 4 – Minute 1069)**

The AUASB discussed the latest draft of the *Auditor Reporting Frequently Asked Questions (FAQ)* and approved the document for issue subject to internal processes and editorial amendments.

The first release will not include a series of questions relating to Stapled Securities, the definition of a listed entity (including Aqua funds), and the treatment of financial reports containing parent and consolidated information (i.e. four column financial report). These questions will be included in a subsequent additional release, after input from external stakeholders.



## **ASA 250 Consideration of Laws and Regulations in an Audit of a Financial Report**

### **(Agenda Item 5 – Minute 1070)**

The AUASB received an update on ED XX ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* to be based on the recently released ISA 250 (revised) that was issued by the IAASB on 5 October 2016.

ISA 250 (revised) aligns with the recent changes to the IESBA code. These changes are yet to be exposed in Australia by the Accounting Professional and Ethical Standards Board (APESB).

The AUASB technical group will co-ordinate with the APESB so that engagement with our respective stakeholders is conducted in a synchronised manner. The AUASB will receive an update in relation to the progress of the APESB exposure draft process at the 29 November 2016 AUASB meeting.

## **Audit Committees Guide**

### **(Agenda Item 6 – Minute 1071)**

The AUASB received an update on the joint project to revise the Audit Committees Guide. Comments were received on the draft amendments to the AUASB section of the document. A first draft of the revision including input from all parties will be discussed at the 29 November 2016 AUASB meeting.

## **Other Matters**

### **(Agenda Item 7 – Minute 1072)**

(a) International Update (for noting)

The AUASB noted the International Update.

(b) AUASB response to the IAASB *Survey on Work Plan for 2017-2018 and the Continuing Relevance for Its Strategic Objectives* (for noting)

The AUASB noted the survey response that was provided to the IAASB on 5 October 2016.

### **Other matters**

The AUASB discussed the approach to strategic planning including agreeing to hold a two hour session on the eve of the AUASB meeting on 29 November 2016 followed by a more comprehensive session at the 1 March 2017 AUASB meeting.

## **Next Meeting**

The next regular meeting of the AUASB will be held in the TEQSA Boardroom, Level 14, 530 Collins Street, Melbourne, on Tuesday, 29 November 2016, commencing at 9.00 a.m.

## **Close of Meeting**

The Chairman closed the meeting at 12.00 p.m.



## Approval

Signed as a true and correct record.

M H Kelsall  
*Chairman*

Date: 29 November 2016



## Matters Arising from Previous Meetings and Action List

### Current Projects

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
1.	Presentations at AUASB meetings		Chairman	
		<ul style="list-style-type: none"> <li>14 June meeting</li> <li>26 July meeting</li> <li>13 September meeting</li> <li>25 October meeting</li> <li>29 November meeting</li> <li>Future meeting considerations: ACNC, BRLF/IIRC/AICD/NZ Company Directors/ G100</li> </ul>		<ul style="list-style-type: none"> <li>CPA – Emma Sweet, John Purcell, Claire Grayston</li> <li>IIAA – Peter Jones and Tony Rasman</li> <li>Rutgers University – Prof Miklos Vasarhelyi</li> <li>To be rescheduled: CAANZ – Liz Stamford</li> <li>To be rescheduled FRC Chairman – Bill Edge</li> </ul>
2.	Compliance Engagements	Revision of ASAE 3100 <i>Compliance Engagements</i> .	M Michaelides	The ED was issued 22 August 2016 for a 60 day exposure period that ended on 19 October 2016. Refer Agenda Item x for comments on disposition and final revised standard for approval.
3.	GS 001 Concise Financial Reports	Project to revise Guidance on Concise Report.	R Herman	Refer Agenda Item x.
4.	Auditor Reporting-FAQ	Prepare plain English FAQ in relation to auditor reporting.	A Waters/ M Dowling	First tranche FAQ issued. Refer Agenda Item x.
5.	ASA 700	The 2013 compiled ASA 700 included para Aus 40.1, <i>The auditor's report shall be dated as of the date the auditor signs that report</i> . When the revised ASA 700 was reissued in December 2015, this Aus paragraph was removed as it had	R Herman	The intention is to include this insertion within the amending standard arising from the NOCLAR amendments.

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
		not passed the compelling reasons test, however the AUASB agreed to include these words as a footnote next to the [DATE] section of all example auditor's reports. This has however not flowed through into the example ASA 700 auditor's reports.		
6.	NOCLAR	The IAASB at the June 2016 meeting approved for issue the revised ISA 250 and consequential amendments to several other standards. These approved standards are subject to PIOB approval – expected at the September 2016 meeting.	R Herman	Refer Agenda Item x. Expected delay in issuance of Australian ED's pending the revision to the APESB Code. APESB expect to issue ED on NOCLAR amendments back end of 2016.
7.	Audit committees Guide	Project plan to update the Revision of <i>Audit Committees – A Guide to Good Practice – 2nd edition</i> . This project is a joint initiative between the Australian Institute of Company Directors, The Institute of Internal Auditors Australia and the AUASB.	R Herman	Refer Agenda Item x.
8.	ISA 540/IFRS 9	The AUASB to consider whether to form an early PAG, to provide input into the IAASB ED. Item to be added to the AUASB September 2016 meeting agenda.	A Waters	IAASB ED may be delayed until March 2017 – timing to be determined after IAASB meeting in early December 2016..

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
9.	Integrated Reporting	AUASB monitoring progress on integrated reporting project and assurance implications.	M Michaelides	<ul style="list-style-type: none"> <li>• August 2016: IAASB Discussion Paper (DP) issued: Supporting Credibility and Trust in Emerging Forms of External Reporting (EER): 10 Key Challenges for Assurance Engagements. To inform the IAASB re: when and how to respond to EER in the public interest.</li> <li>• Two AUASB/Business Reporting Leaders Forum (BRLF) joint roundtables took place on 3 October 2016 in Melbourne and 14 October 2016 in Sydney.</li> <li>• Refer Agenda Item x for draft submission.</li> </ul>
10.	Performance Engagements	Project Plan for revision of ASAE 3500 approved, research underway and Project Advisory Group being formed to advice on revisions.	M Michaelides	This project has been recommenced with a PAG meeting held in September 2016. A further project update will come to the 1 March 2017 meeting.—.
11.	GS 001 Concise Reports	To revise GS 001 in light of the revisions to ASA 810.	R Herman	Refer Agenda Item x.

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
12.	ITC areas: <ul style="list-style-type: none"> <li>• group audits;</li> <li>• professional scepticism;</li> <li>• audit quality</li> </ul>	Monitor IAASB developments in this area	R Herman A Waters	Monitoring international.

## Watching Brief Matters

No.	Reference	Technical matter for monitoring	Responsibility	Status as at 9 November 2016
1	Financial Reporting Framework Project	<p>A research project on the financial reporting framework is being conducted by the AASB, the AUASB will monitor this project for issues that may impact on the AUASB and action as required.</p> <p>[Incorporates the AASB's Differential Reporting Project RDR].</p>	TBD	This project is ongoing and the AUASB will continue to liaise with the AASB on the progress. The RDR ED is expected to be presented to the AASB at the December 2016 AASB meeting.
2	National Greenhouse and Energy Reporting (NGERS)	On-going liaison activities with the Clean Energy Regulator (CER) and the Department of Environment with respect to assurance under the National Greenhouse and Energy Reporting Scheme and Emissions Reduction Fund.	M Michaelides	Further updates on ERF will be provided on a needs basis.
3	Assurance project on Statements of Service Performance	Monitor AASB Reporting Project and jointly participate in NZAuASB assurance project.	M Dowling	<p>AUASB actively monitoring NZAuASB activities. The NZ accounting standard is underway as is the auditing exposure draft. NZ is currently considering submissions received on the accounting ED and expect to finalise the accounting standard by early 2017. Timing of the the auditing ED is dependent upon the finalisation of the accounting standard.</p> <p>The AASB will take feedback from the Australian ED to their December 2016 AASB meeting with a view to seek Board direction on the project.</p>
4	National Frameworks	The FRC has undertaken to lead and provide oversight to a multi-faceted initiative to rationalise the numerous financial reporting frameworks and associated audit/assurance frameworks that currently exist in the Australian environment. Initially the AUASB's objective will be to meet with relevant legislators and regulators to advocate the AUASB Pronouncements and Frameworks.	R Herman/ M Dowling	First meeting held 19 August 2015, no further update.

## Projects on hold

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
1.	Managed Investment Schemes	Revise Guidance Statement GS 013.	R Herman	As confirmed by Doug Niven at the ASIC/AUASB quarterly meeting on 12 January 2015, owing to the government's deregulation agenda, ASIC will not be revising Regulatory Guides in relation to Compliance Plans. Accordingly, this project is on hold.
2.	Value of Audit (Joint with NZ)	A thought piece on how audits and assurance engagements can provide value to organisations.	TBD	This project is currently on hold.
3.	AASB Disclosures Project	Monitoring of, and ongoing liaison with, the AASB on the Disclosures Project (as well as related IASB project) for any audit related issues/consequences.	M Dowling	This project is progressing with an IASBPOD discussion paper expected December 2016
4.	GS 010 <i>Responding to Questions at an AGM</i>	<p>Revised guidance statement.</p> <p>Key action items:</p> <ul style="list-style-type: none"> <li>• revision not to be limited to KAM</li> <li>• GS re-structured to differentiate written questions received prior to the AGM from answering questions during the AGM</li> <li>• GS should be informed by questions actually asked at AGMs</li> <li>• questions asked in advance of AGMs.</li> <li>• guidance on how engagement partner delegates are selected when the engagement partner is not able to attend the AGM.</li> <li>• appendix comprising examples of questions.</li> </ul>	M Dowling	As per discussion at the 18 April AUASB meeting, on hold until later in 2016 after next round of AGMs.

No.	Project	Brief technical description of ongoing project	Responsibility	Status as at 9 November 2016
5.	SBR	Standard Business Reporting (Including XBRL)	M Dowling	There have been no further developments in this area.



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO.      **2**

Meeting Date:                      29 November 2016

Subject:                              ASAE 3100 Compliance Engagements – Comments on Disposition and Approval of revised ASAE 3100

Date Prepared:                      15 November 2016

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☒ Action Required

☐ For Information Purposes Only

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## Agenda Item Objectives

AUASB to consider:

- comments received and proposed disposition paper on ED 04/16 ASAE 3100 and recommended changes; and
- approval of revised ASAE 3100 (marked up) subject to internal QA processes being completed and final review by the Chair.

## Background

1. ASAE 3100 was issued in 2008 and a post-implementation survey was conducted in 2012. The results of that survey identified some matters to be addressed in any future revisions to ASAE 3100.
2. The NZAuASB also completed a post-implementation survey for SAE 3100 in April 2015 and any matters raised will be addressed by the NZAuASB in their revision of SAE 3100 and considered by the AUASB in the revision of ASAE 3100 to ensure consistency.
3. The AUASB approved a project plan to revise ASAE 3100 at the AUASB meeting in February 2015.
4. A project advisory group (PAG) was formed in March 2015 to advise the AUASB TCG specifically on the subject matter and issues encountered in practice with compliance engagements. Four project advisory (PAG) meetings were held in the 2015 calendar year.
5. A PAG meeting was held on 22 March 2016 to discuss with the PAG suggested changes made by the Board to ED ASAE 3100 at the December 2015 and February 2016 meetings.
6. A PAG meeting was held on 14 July 2016 to discuss the outcomes of the June AUASB board meeting and to seek input on the final draft of the ED XX ASAE 3100. The feedback from this PAG meeting is reflected in the final draft ED that was presented to 26 July 2016 meeting.
7. The OBPR process was completed on 15 August 2016 and clearance from OBPR that no RIS was required was received on 17 August 2016.

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*This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.*

8. ED 04/16 ASAE 3100 was further discussed and considered at the 26 July AUASB meeting and further suggested changes were agreed by the Board. ED 04/16 ASAE 3100 was approved for exposure at an out of session vote by the Board on 16 August 2016. ED 04/16 was exposed on 22 August for a 60 day comment period ending on 19 October 2016. The AUASB received a high level update on progress of submissions at the 25 October 2016 meeting.
9. Seven submissions were received on ED 04/16 from the firms, the accounting bodies and ACAG. Detailed comments on disposition and submission letters are included as attachments to this BMSP.

## **Matters to Consider**

### ***Part A – General***

1. Key comments for Board consideration:

#### **1.1 CPA Point 1 – Use of the Term Compliance Framework**

We consider that the term “compliance framework” is not appropriate for the proposed definition provided and will be misunderstood. A plain English understanding of the term “compliance framework” would typically be a reference to the legislation, regulation and other requirements which make up the compliance requirements, effectively the criteria in a compliance engagement. This meaning does not align with the definition of compliance framework in ED 04/16 being: *“A framework adopted by the entity, which is designed to ensure that the entity achieves compliance, and includes governance structures, programs, processes, systems, controls and procedures”*.....

#### **AUASB Technical Group (ATG) Comments on Disposition**

The term ‘compliance framework’ is used and applied in extant ASAE 3100 and the glossary, and is adequately defined for the purposes of this ASAE to be clear as to its meaning and application in revised ASAE 3100.

The use of this definition within the context of this ASAE is much broader than just “controls” or “systems of controls”. It encapsulates a broad understanding by the assurance practitioner of the compliance culture/environment of the entity which includes governance structures, programs, processes, systems and controls which the assurance practitioner.

On this basis the ATG recommend retaining the term “compliance framework” in the revised ASAE 3100.

#### **The Board to advise whether they agree with the proposed disposition on this matter?**

#### **1.2 CPA Point 2 - Compliance Framework as a Subject Matter**

The manner in which the term compliance framework, meaning controls as discussed above, is used in the standard suggests that controls are included in the subject matter of compliance engagements. However the subject matter in these engagements is the compliance activities to meet the compliance requirements, not the controls over those compliance activities. We consider that the subject matter of a compliance engagement relates to compliance with requirements only and not controls over compliance.....

#### **ATG Comments on Disposition**

The concept of a “Compliance Framework’ is applied primarily in a compliance engagement in the planning phase and when obtaining an understanding of the compliance activity and other engagement circumstances. By understanding the compliance framework and its key elements: governance structures, programs, processes, systems, controls and procedures the assurance practitioner has a more in depth understanding of areas where the risks of non-compliance are likely to arise (para 32L(b) and 32R(b)) and respond to these appropriately. The ‘compliance framework’

refers to the broader governance/control environment an entity has around compliance activities and is therefore important to the assurance practitioners understanding of the entity and the environment under which compliance activities are undertaken. This understanding is required for the assurance practitioner to perform their risk assessment as they would under any assurance engagement. This concept is currently applied in extant ASAE 3100 and there does not appear to have been any issues raised previously with its application in practice. The extant ASAE 3100 is not 'broken' and the objective of the revision was primarily to clarify the standard and bring it into line with revised ASAE 3000.

On this basis the ATG recommend retaining the concept of "Compliance Framework" in revised ASAE 3100.

**The Board to advise whether they agree with the proposed disposition on this matter?**

### **1.3 CPA Point 3 - Suitable Criteria**

We do not consider that the phrase "evaluated by the suitable criteria" which is used throughout ED 04/16, after compliance requirements, is useful or communicates any useful meaning, as paragraph 9 states "the criteria may be the compliance requirements, or a subset thereof" anyway. Consequently, we consider that it simply serves to complicate the proposed standard. Compliance requirements are the criteria for a compliance engagement and whilst they may be broken down into greater detail in order to test the compliance activities, we do not see how repeated use of this phrase aids clarity.....

#### **ATG Comments on Disposition**

The concepts of 'compliance requirements' and suitable 'criteria' were discussed at length by the Board throughout the development of ED 04/16. The draft ED 04/16 presented to the Board in Dec 15 was drafted excluding the phrase "evaluated by the suitable criteria" and the Board made a decision to reinstate this terminology as both concepts of "compliance requirements" and "criteria" are relevant in a compliance engagement. This position was also supported by the PAG and is consistent with extant ASAE 3100. A final decision was made by the Board at the February 2016 meeting to retain both terms in the ED 04/16 to provide a clearer understanding as to the application and objective of a compliance engagement.

This reflected that the "compliance requirements" being what the entity has to comply with and the criteria as the subset, (or may be the same as the compliance requirements or even processes or procedures) of the requirements being what the assurance practitioner needs to consider in making their determination and drawing their conclusion about the entities compliance.

Para 9 states "the criteria may be the compliance requirements, or a subset thereof" however this may not always be the case therefore the need to retain both terms in the revised ASAE 3100.

On this basis the ATG recommend retaining the wording "evaluated by the suitable criteria" in revised ASAE 3100.

**The Board to advise whether they agree with the proposed disposition on this matter?**

### **2. All other comments received and proposed disposition**

The AUASB Technical Group has considered all other comments in the detailed comments received and proposed disposition paper as attached.

#### *In Progress*

1. The final internal quality assurance process needs to be completed and ongoing liaison with NZAuASB to ensure consistency in the underlying ASAE 3100 and SAE 3100 standards is maintained.

#### **Part B – NZAuASB**

1. Draft ED SAE 3100 (Revised) is based on ED 04/16 ASAE 3100, with amendments for New Zealand examples and ethical references. The New Zealand revised SAE 3100 does not include the

equivalent of para 38 prohibiting direct assistance (this is consistent with harmonisation differences across the suite of New Zealand and Australian standards).

2. The NZAuASB ED comment period closes on 22 November 2016. Proposed comments on disposition will go to the 8 December 2016 meeting for consideration. The AUASB will be in attendance at this meeting so as to understand the Boards view on any comments or suggested changes.
3. The AUASB will continue to liaise with the NZAuASB on the outcomes from both Board meetings, and any impacts on the final revised standards ASAE 3100 / SAE 3100 to ensure in so far as is practical they are consistent.

### **AUASB Technical Group Recommendations**

The AUASB to consider:

- comments received and proposed disposition paper on ED 04/16 ASAE 3100 and recommended changes; and
- approval of revised ASAE 3100 (marked up) subject to internal QA processes being completed and final review by the Chair.

### **Material Presented**

Agenda Item 2	AUASB Board Meeting Summary Paper
Agenda Item 2(a)	ASAE 3100 Comments Received and Proposed Disposition
Agenda Item 2(b)	ASAE 3100 <i>Compliance Engagements</i> (marked up)
Agenda Item 2.1	KPMG
Agenda Item 2.2	Ernst & Young
Agenda Item 2.3	Australasian Council of Auditors-General
Agenda Item 2.4	CPA Australia Ltd
Agenda Item 2.5	Chartered Accountants Australia New Zealand
Agenda Item 2.6	PWC
Agenda Item 2.7	Deloitte

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### **Action Required**

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	Consider and approve comments on disposition and final revised ASAE 3100.	Feedback and approval of revised ASAE 3100.	AUASB	29 Nov 2016	Pending

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# AUASB Comments Received and Proposed Disposition Paper

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**AGENDA ITEM NO.**      **2a**

**Meeting Date:**            29 November 2016

**Subject:**                  ED 04/16 Compliance Engagements

**Date Prepared:**          8 November 2016

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**Document Type:**        Exposure Draft

**Document Number:**    ED 04/16

**Proposed Type & No:**   ASAE 3100

**Proposed Title:**        ASAE 3100 Compliance Engagements

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**EXHIBIT 1:**              ED 04/16 Compliance Engagements

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## LISTING OF RESPONDENTS

Short Form Name	Name	Date Received
KPMG	KPMG	19/10/16
EY	Ernst & Young	20/10/16
ACAG	Australasian Council of Auditors-General	19/10/16
CPA	CPA Australia Ltd	24/10/16
CAANZ	Chartered Accountants Australia New Zealand	25/10/16
PWC	PWC	27/10/16
Deloitte	Deloitte	2/11/16

ATG = AUASB Technical Group

**EXHIBIT 1: ED 04/16 Compliance Engagements****1. Have applicable laws and regulations been appropriately addressed in the proposed standard**

<b>Respondent Comment</b>		<b>Commentary</b>	<b>Change to be made to Doc? Y/N</b>	<b>Para No.</b>
KPMG	We believe applicable laws and regulations have been appropriately addressed.	Comment noted by ATG	N	
EY	As far as we can see, applicable laws and regulations have been appropriately addressed in the proposal standard.	Comment noted by ATG	N	
ACAG	ACAG makes no comment on this matter.	Comment noted by ATG	N	
CPA	Yes.	Comment noted by ATG	N	
CAANZ	We believe they are adequately addressed.	Comment noted by ATG	N	
PWC	Yes	Comment noted by ATG	N	
Deloitte	Yes, it appears that all the relevant applicable laws and regulations have been appropriately addressed.	Comment noted by ATG	N	

**Summary—Question - Have applicable laws and regulations been appropriately addressed in the proposed standard?**

<b>No. of Respondents</b>	<b>NO</b>	<b>YES</b>
7		7

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****2. Are there any references to relevant laws or regulations that have been omitted?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
KPMG	We are not aware of any references to relevant laws or regulations that have been omitted.	Comment noted by ATG	N	
EY	We are not aware of any references to relevant laws or regulations that have been omitted.	Comment noted by ATG	N	
ACAG	ACAG makes no comment on this matter.	Comment noted by ATG	N	
CPA	No.	Comment noted by ATG	N	
CAANZ	We do not believe so. The inclusion of some common kinds of Australian regulatory compliance engagements in Appendix 3 is useful. It may also be useful to include an example in this Appendix which is not regulation driven, such as compliance with the requirements of a bank covenant to reinforce the point that compliance engagements may be requested by a client due to requirements other than regulation or legislation	Comment noted by ATG. Consideration will be given to further example in Appendix 3.	Y	App 3
PWC	None noted.	Comment noted by ATG	N	
Deloitte	No, we have not identified any omitted references to relevant laws and regulations.	Comment noted by ATG	N	

**Summary—Question - Are there any references to relevant laws or regulations that have been omitted?**

No. of Respondents	NO	YES
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No. of Respondents	NO	YES
7	7	

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
KPMG	We are not aware of any laws or regulations that may prevent or impede application of the proposed standard or may conflict with the proposed standard.	Comment noted by ATG	N	
EY	We are not aware of any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard.	Comment noted by ATG	N	
ACAG	ACAG is not aware of any such laws or regulations.	Comment noted by ATG	N	
CPA	No.	Comment noted by ATG	N	
CAANZ	Not that we are aware of.	Comment noted by ATG	N	
PWC	None noted. However, there are a number of Guidance Statements that include references to the requirements of ASAE 3100. These will need to be reviewed and revised where necessary.	Comment noted by ATG	N	
Deloitte	We are not aware of any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard.	Comment noted by ATG	N	

**Summary—Question - Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

No. of Respondents	NO	YES
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No. of Respondents	NO	YES
7	7	

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****4. Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?**

<b>Respondent Comment</b>		<b>Commentary</b>	<b>Change to be made to Doc? Y/N</b>	<b>Para No.</b>
KPMG	We believe the considerations for conducting a direct engagement are adequately differentiated from an attestation engagement. It would be useful to have one of the attestation examples in the appendices illustrate the alternative conclusion as suggested in paragraph 16 (a), even if by footnote.	Comment noted by ATG. A footnote will be included in Appendix 6 – Example 3 attestation Engagement to reflect the alternative wording.	Y	App 6 Exp 3 - Footnote
EY	In our view, the considerations for conducting a direct engagement are adequately differentiated from an attestation engagement.	Comment noted by ATG	N	
ACAG	Generally, yes.  The considerations in paragraph A4 for differentiating the conduct of a direct engagement from an attestation engagement could better emphasise that in a direct engagement the assurance practitioner directly evaluates compliance with the compliance requirements and in an attestation engagement this evaluation is conducted by the responsible party.	Comment noted by ATG  Emphasis of the distinction between direct and attestation engagement will be made to para A4	Y	A3
CPA	Yes.  In addition, we suggest that the requirements reflect direct engagements by ensuring that non-compliance is included as well as misstatements, which are only relevant to attestation engagements where a Statement is provided. For example in paragraphs 17(u) and 50 insert, after “possible misstatement”, “or non-compliance”.	Comment noted by ATG  Agree change will be made to include non-compliance for direct engagement.	Y	17(U), 50
CAANZ	We understand direct engagements are more prevalent in practice, but we agree there is a need for the proposed	Comment noted by ATG	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>standard to address both direct and attestation engagements.</p> <p>In our view the differentiation between a direct and an attestation engagement could be clearer. We recommend an overarching statement to the effect of “If this ASAE makes reference to a requirement, that requirement shall be applied to both attestation and direct engagements, unless specified otherwise” similar to the statement regarding ASAE 3000 in paragraph 18. Furthermore, we recommend the removal of the following superfluous statements:</p> <ul style="list-style-type: none"> <li>• Paragraph 17(s) [definition of ‘non-compliance’] - “for both attestation and direct engagements on compliance...”</li> <li>• Paragraph 56 - “for attestation engagements and shall also apply those requirements for direct engagements”</li> <li>• Paragraph 57 - “For both attestation and direct engagements”</li> </ul>	ATG believe that the current distinction between direct and attestation engagements in the revised ASAE 3100 provides more clarity would addressed at the requirement level rather than in an overarching statement in the introduction section.		
PWC	Yes.	Comment noted by ATG	N	
Deloitte	Yes, the considerations for conducting a direct engagement adequately differentiated from an attestation engagement.	Comment noted by ATG	N	

**Summary—Question - Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?**

No. of Respondents	NO	YES
7		7

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****5. Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?**

<b>Respondent Comment</b>		<b>Commentary</b>	<b>Change to be made to Doc? Y/N</b>	<b>Para No.</b>
KPMG	We believe the procedures required for limited and reasonable assurance are appropriate and adequately distinguished.	Comment noted by ATG	N	
EY	The procedures required for limited and reasonable assurance engagements are appropriately and adequately distinguished.	Comment noted by ATG	N	
ACAG	The procedures required for limited and reasonable assurance engagements are appropriate and adequately distinguished. We support the use of the tabular approach at paragraphs 32 and 43 to describe the required procedures.	Comment noted by ATG	N	
CPA	Yes.	Comment noted by ATG	N	
CAANZ	We support the approach taken in this aspect of the ED. We recognise there are challenges involved in articulating requirements to achieve a meaningful level of assurance in a limited assurance compliance engagement, while still differentiating appropriately from a reasonable assurance compliance engagement. However, we believe that the proposed standard is a useful starting point.	Comment noted by ATG	N	
PWC	Yes, the procedures are adequately distinguished.	Comment noted by ATG	N	
Deloitte	Yes, the procedures required for limited and reasonable assurance are appropriate and adequately distinguished.	Comment noted by ATG	N	

**Summary—Question - Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?**

No. of Respondents	NO	YES
7		7

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)**

- 6. What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
KPMG	<p>We do not anticipate any significant incremental costs to auditors and the business community arising from compliance with the revised requirements of this proposed standard.</p> <p>There is however an impact with respect to liaising with regulators who issue “prescribed” reporting templates that do not apply the principles and terminology of the ASAEs. It is challenging for practitioners when a report prepared under the requirements of the Standards is rejected. Negotiations are required with regulators to amend their prescribed reports to achieve compliance with the Standards.</p> <p>We encourage the Board to consider how the changes to these Standards can be communicated to regulatory bodies, such that their prescribed reports can be adjusted to comply with the requirements of the revised Standards.</p>	<p>Comment noted by ATG</p> <p>The AUASB through liaison with regulatory bodies will communicate changes to prescribed reports to ensure compliance with the revised standard.</p>	N	
EY	We do not believe that there are any additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard.	Comment noted by ATG	N	
ACAG	ACAG makes no comment on this matter.	Comment noted by ATG	N	
CPA	We have not identified any significant additional costs in complying with the proposed standard. Benefits may not be realised in terms of cost savings but the standard provides greater clarity about how to conduct compliance engagements.	Comment noted by ATG	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
CAANZ	We have not assessed the cost implications of the proposed standard. However, it is likely that there will be additional costs in complying with revised standard when compared to the extant standard due to the revised approach and greater detail in the requirements. However, the quality of the compliance engagement is likely to increase as a result of applying the enhanced requirements in the proposed standard. Therefore, we believe that the benefits outweigh the costs.	Comment noted by ATG	N	
PWC	No significant additional costs expected.	Comment noted by ATG	N	
Deloitte	We are not aware of any additional costs to/benefits for assurance practitioners and business community.	Comment noted by ATG	N	

**Summary—Question - What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?**

No. of Respondents	NO	YES
7	7	

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****7. Are there any other significant public interest matters that constituents wish to raise?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
KPMG	No, there are no other significant public interest matters we wish to raise.	Comment noted by ATG	N	
EY	We have no significant public interest matters that we would like to raise in relation to the proposed standard.	Comment noted by ATG	N	
ACAG	None.	Comment noted by ATG	N	
CPA	No.	Comment noted by ATG	N	
CAANZ	<p>We have no other significant public interest matters to raise. However, we do have the following minor drafting points we wish to raise for your consideration:</p> <p>a) The definition of ‘misstatement’ in paragraph 17(r) only refers to attestation engagements and differences between the statement and the assurance practitioner’s evaluation of compliance with the compliance requirements. However, paragraph 49 includes a statement that a misstatements are “instances of non-compliance with the compliance requirements”. Therefore there is a conflict in the definition between the two paragraphs. We recommend that the definition in 17(r) be expanded to define misstatement in the context of both a direct and an attestation engagement. The sentence defining misstatements in paragraph 49 could then be removed or amended to refer to the definitions in 17(r).</p>	<p>Comment noted by ATG</p> <p>ATG agrees with the comments. This point was also raised by NZAuASB. NZAuASB has suggested that the last sentence in para 49 be removed and replaced with .... <i>Under this ASAE misstatements are only applicable in an attestation engagement on compliance. In a direct assurance engagement on compliance the assurance practitioner shall accumulate identified matters of non-compliance other than those that are already trivial.</i></p>	Y	49, 50

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	b) Paragraph 61 on modified conclusions and paragraph 62 on scope limitation may be better placed under Forming the Assurance Conclusion with paragraphs 54-55.	Retain the current order of para 61 and 62 to maintain consistency with ASAE 3000.	N	
PWC	None noted.	Comment noted by ATG	N	
Deloitte	No, there are no other significant public interest matters we wish to raise.	Comment noted by ATG	N	

**Summary—Question - Are there any other significant public interest matters that constituents wish to raise?**

No. of Respondents	NO	YES
7	7	

**EXHIBIT 1: ED 04/16 Compliance Engagements (cont'd)****8. GENERAL COMMENTS**

<b>Respondent Comment</b>		<b>Commentary</b>	<b>Change to be made to Doc? Y/N</b>	<b>Para No.</b>
EY	We have supported and continue to support the AUASB's initiatives to improve assurance engagement quality and believe that the proposals enhance clarity on how to scope, conduct and report in an assurance engagement on compliance. We agree with the Board's effort to facilitate conformity with current AUASB standards and revised ASAE 3000 <i>Assurance Engagements Other than Audits or Reviews of Historical Financial Information</i> , which will be achieved by the proposals.	Comment noted by ATG	N	
ACAG	Overall, we support the proposed Standard. Although the existing ASAE 3100 Compliance Engagements is used sparingly by Australian audit offices, we have responded to the specific questions in the Exposure Draft and also provide comment on materiality.	Comment noted by ATG	N	
KPMG	Overall, KPMG Australia is very supportive of the revised requirements and additional application and other explanatory material in the Exposure Draft. The key comments we wish to highlight to the AUASB are shown below.	Comment noted by ATG	N	
KPMG	<p><b>Definitions: the term "criteria" Paragraph 17 (g)</b></p> <p>The term <b>criteria</b> isn't clearly differentiated from <b>compliance requirement</b>. Criteria is presented as similar to compliance requirement: <i>the specific requirements established in law versus the legislation used to evaluate whether compliance requirements have been met</i>. Appendix 3 "Examples: Nature of Assurance Engagements on Compliance" makes it easier to understand by illustrating with an</p>	<p>Comments noted by ATG</p> <p>ATG agree with the comments. The definition of the terms 'Compliance Requirement' and 'Criteria' will be tightened to further clarify revised ASAE 3100 and include the compliance requirement as being the overarching.....and criteria as being specific.....</p>	Y	17(f), 17(g)

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[illegible]

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>examples. We do however suggest you include a sentence in the guidance paragraphs to indicate that the AUASB had considered whether this was a technical application of the fair presentation framework and although it is not a strict technical application, you are comfortable to use it with respect to the responsible party's "Statement" to achieve understandability. This will avoid each practitioner challenging whether it's an appropriate use of this phrase; and/or</p> <p>2. Use alternative wording such as "properly prepared and presented".</p>	<p>ATG to adopt the suggested wording of "properly prepared and presented" as it provides greater clarity and understanding as to the conclusion the assurance practitioner will provide over the Statement.</p>	Y	App5 – Exp 1 and 2, App 6 – Exp 3
KPMG	<p>Paragraph</p> <p>17 (c)</p> <p>Issue(s) noted</p> <p>Definition inconsistent with AUASB glossary (Glossary) definition of 'Compliance engagement'. The fuller definition in the Glossary states that its source is ASAE3100.</p> <p>Recommendation/suggestion on wordings to add or remove</p> <p>We suggest retaining the fuller definition from the Glossary in ASAE 3100, or updating the Glossary section for consistency. Alternatively if the fuller description is not included in ASAE 3100, we suggest to delete the reference to ASAE 3100 as the source of the definition in the Glossary.</p>	<p>Comments noted by ATG</p> <p>The Glossary has not been updated since 2009, so there are inconsistencies throughout. Once the revised ASAE 3100 is issued the terms in the Glossary will need to be updated to reflect any new definitions so the references are correct.</p>	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
KPMG	<p>Paragraph(s)</p> <p>23, 24 (b) and A15</p> <p>A16</p> <p>Issue(s) noted</p> <ul style="list-style-type: none"> <li>The practitioner identifies, selects or develops the criteria</li> <li>Criteria may need to be amended during the engagement.</li> </ul> <p>Recommendation/suggestion on wordings to add or remove</p> <ul style="list-style-type: none"> <li>If we're <i>developing</i> the criteria at the time of the engagement, we query how the responsible party can demonstrate compliance with the criteria over the period subject to assurance and therefore meet the overall compliance requirement? How could the responsible party have designed an appropriate compliance activity to meet the criteria if the criteria were not known?</li> <li>Similar concept if we amend the criteria during the engagement per A16. How could the overall compliance requirement be met?</li> </ul>	<p>Comments noted by ATG.</p> <p>ATG agrees to remove references in para 23, 24(b), A15 and A16 to the assurance practitioner developing criteria or amending criteria during the engagement.</p>	Y	23, 24 (b), A15 and A16
KPMG	<p>Paragraph</p> <p>A6</p> <p>Issue noted</p> <p>Independence – A6 implies consulting services with respect to the compliance framework are <b>likely to</b> impact the practitioner's independence and <b>likely to</b> preclude acceptance. There are safeguards that can be applied to be able to deliver an engagement such as pre-assurance work like gap analysis that is an advisory style service that</p>	Comments noted by ATG		

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>provides suggestions or observations. This type of engagement would not contemplate designing or implementing the compliance framework or making management decisions and therefore should not impact independence.</p> <p>Recommendation/suggestion on wordings to add or remove</p> <p>Change to “<b>may</b> impact on the audit practitioner’s independence and <b>may</b> preclude acceptance of the engagement”. This allows the practitioner to evaluate their independence and whether application of a safeguard would manage the risk to an acceptable level.</p>	ATG agree with the suggested changes to A6.	Y	A6
KPMG	<p>Paragraph</p> <p>A33</p> <p>Issue noted</p> <p>Third party outsourced service providers.</p> <p>Recommendation/suggestion on wordings to add or remove</p> <p>We recommend more discussion about how to obtain evidence on compliance with obligations when the responsible party uses an external third party outsourced service provider, as this is a common scenario.</p>	<p>Comments noted by ATG</p> <p>ATG agree there should be a footnote referencing both <i>ASA 402 Audit Considerations Relating to an Entity Using a Service Organisation</i> and <i>GS013 Special Considerations in the Audit of Compliance Plans of Managed Investment Schemes</i> paragraphs 36 and 37 for further guidance on this area.</p>	Y	A33 – New Foot Note
KPMG	<p>Paragraph(s)</p> <p>Appendix 5 Engagement letters – Examples 1 to 3</p> <p>Issue</p>	Comments note by ATG		

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>Missing practitioners' responsibility to apply ASQC 1.</p> <p>Recommendation/suggestion on wordings to add or remove</p> <p>We recommend reference to ASQC 1 in the practitioner's responsibilities section to be consistent with ASAE 3150 and 3402.</p>	ATG agree with comments to include a reference to ASQC1 in the engagement letter examples to be consistent with the example reports in Appendix 6.	Y	App 5 – Exp 1 to 3
KPMG	<p>Paragraph(s)</p> <p>Appendix 6 Assurance reports on compliance – Examples 1 to 3</p> <p>Issue(s)</p> <ul style="list-style-type: none"> <li>Inconsistent with new report format in ASA 700 <i>Forming an opinion and reporting on a financial report</i>.</li> <li>Repeated statement in the inherent limitation section.</li> </ul> <p>We recommend:</p> <ul style="list-style-type: none"> <li>A header "<i>Basis for conclusion</i>" after the '<i>Conclusion</i>' paragraph.</li> <li>To move the following statements from <i>Assurance Practitioner's Responsibilities</i> to the new header "<i>Basis for conclusion</i>".</li> </ul> <p>"We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 <i>Compliance Engagements</i> issued by the Auditing and Assurance Standards Board. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.</p> <ul style="list-style-type: none"> <li>To remove the following statement in the inherent limitation section to make it simple.</li> </ul>	<p>Comments noted by ATG</p> <p>ATG agrees with suggestions made for the Example Reports I Appendix 6 to be more consistent with the format of new ASA 700 reports.</p>	Y	App 6 – Exp 1 to 3

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<ul style="list-style-type: none"> <li>“...on ABC’s compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], at a specified date...”</li> </ul>			
KPMG	<p>Paragraph(s)</p> <p>Appendix 7 Modified assurance reports on compliance – example 3</p> <p>Issue</p> <p>Inconsistent Disclaimer of Opinion with ASA 705 <i>Modifications to the Opinion in the Independence Auditor’s Report</i>.</p> <p>Recommendation/suggestion on wordings to add or remove</p> <p>We suggest below wording in <u>underline</u></p> <p><u>“We do not express an opinion on ABC’s compliance with the [compliance requirements] because of...”</u></p>	<p>Comments noted by ATG</p> <p>ATG agrees with the suggested changes to App 7 – Exp 3 to clarify the wording in the disclaimer of opinion paragraph.</p>	Y	App 7 – Exp 3
ACAG	<p><b>Materiality</b></p> <p>ACAG acknowledges that the definition of “Material in the context of a compliance engagement” at paragraph 17(q) is similar to the definition in the existing ASAE 3100. However, this definition is not easy to understand and interpret, and we suggest that the definition be removed.</p> <p>ACAG considers the materiality requirements at paragraph 31 and the explanatory material at paragraphs A25 to A30 are sufficient, subject to an addition to paragraph 31 requiring the assurance practitioner to consider materiality when evaluating whether the underlying subject matter (compliance activity) meets the compliance requirements.</p>	<p>Comments noted by ATG</p> <p>ATG considers the definition of “Material in the context of a compliance engagement para 17(q) to be useful and it is currently used and applied in extant ASAE 3100.</p> <p>ATG believe that this requirement regarding considering materiality when evaluating whether the underlying subject matter (compliance activity) meets the compliance requirement is adequately covered in the application material A26, A28 and</p>	<p>N</p> <p>N</p>	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	This approach is consistent with the approach in ASAE 3000 <i>Assurance Engagements Other than Audits or Reviews of Historical Financial Information</i> .	A29. ATG made a decision in December 2015 to remove this requirement and cover it in the application material.		
CPA	<p>1. <u>Use of the Term Compliance Framework</u></p> <p>We consider that the term “compliance framework” is not appropriate for the proposed definition provided and will be misunderstood. A plain English understanding of the term “compliance framework” would typically be a reference to the legislation, regulation and other requirements which make up the compliance requirements, effectively the criteria in a compliance engagement. This meaning does not align with the definition of compliance framework in ED 04/16 being: “A <i>framework adopted by the entity, which is designed to ensure that the entity achieves compliance, and includes governance structures, programs, processes, systems, controls and procedures</i>”. This definition encompasses controls to mitigate the risk of non-compliance with the compliance requirements. Consequently, we consider that the term “compliance framework” should be replaced with a term such as “controls”, “system of controls” or “controls relevant to compliance” And the term chosen should be consistent with other AUASB Standards, including ASAE 3150 <i>Assurance Engagements on Controls</i>. We do not suggest use of the term control framework as this is the framework (such as COSO or COBIT), including the control components, used to design the controls, rather the</p>	<p>Comments noted by ATG</p> <p>The term ‘compliance framework’ is used and applied in extant ASAE 3100 and the glossary and is adequately defined for the purposes of this ASAE and to be clear as to its meaning and application in revised ASAE 3100.</p> <p>The use of this definition within the context of this ASAE is much broader than just “controls” or “systems of controls”. It encapsulates a broader understanding by the assurance practitioner of the compliance culture/environment of the entity which includes governance structures, programs, processes, systems and controls which the assurance practitioner</p> <p>On this basis the ATG recommend retaining the term “compliance framework” in the revised ASAE 3100.</p> <p>Refer further comments on ‘Compliance framework’ below at Point 2.</p>	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	controls themselves.			
CPA	<p>2. <u>Compliance Framework as a Subject Matter</u></p> <p>The manner in which the term compliance framework, meaning controls as discussed above, is used in the standard suggests that controls are included in the subject matter of compliance engagements. However the subject matter in these engagements is the compliance activities to meet the compliance requirements, not the controls over those compliance activities. We consider that the subject matter of a compliance engagement relates to compliance with requirements only and not controls over compliance. The objective of a compliance engagement is to obtain assurance “about whether the entity has complied in all material respects with compliance requirements as evaluated by the suitable criteria”. However ED 04/16 repeatedly makes reference to “material deficiency in the compliance framework”, implying that the objective of the engagement also includes identification of material deficiencies in the “compliance framework”, that is the controls relating to compliance. We do not consider that the objective of the engagement includes concluding on the “compliance framework” as defined or controls therein. Even if maintenance of effective controls to ensure compliance with requirements is a compliance requirement itself, reference to controls as part of the subject matter is still not necessary in the proposed standard.</p>	<p>Comments noted by ATG</p> <p>The concept of a “Compliance Framework’ is applied primarily in a compliance engagement in the planning phase and when obtaining an understanding of the compliance activity and other engagement circumstances. By understanding the compliance framework and its key elements: governance structures, programs, processes, systems, controls and procedures the assurance practitioner has a more in depth understanding of areas where the risks of non-compliance are likely to arise (para 32L(b) and 32R(b)) and respond to these appropriately. The ‘compliance framework’ refers to the broader governance/control environment an entity has around compliance activities and is therefore important to the assurance practitioners understanding of the entity and the environment under which compliance activities are undertaken. This understanding is required for the assurance practitioner to perform their risk assessment as they would under any assurance engagement.</p> <p>This concept is currently applied in extant ASAE 3100 and there does not appear to have been any issues raised previously with its application in practice. The extant ASAE 3100 is not ‘broken’ and the objective of the revision was primarily to clarify the standard and bring it into line with</p>	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>In order to remove reference to compliance framework as part of the subject matter of the proposed standard, we suggest that:</p> <ol style="list-style-type: none"> <li>Reference to compliance framework is removed from the definition of materiality and that materiality is applied directly to compliance activities and identified deficiencies and not to deficiencies in the compliance framework/controls.</li> <li>Deficiencies in compliance framework/controls would not normally be accumulated as such, only deficiencies in compliance.</li> <li>If the assurance practitioner believes that there are deficiencies in the compliance framework/controls, they would not necessarily need to investigate those deficiencies, but would instead no longer rely on those controls and conduct further substantive testing directly on compliance.</li> <li>Even though the effectiveness of controls at mitigating the risks of non-compliance need to be evaluated in determining which controls the assurance practitioner intends to rely upon to reduced substantive testing, we consider that additional procedures which the assurance practitioner performs are responsive to the risks of non-compliance and not the risks relating to deficiencies in compliance framework/controls.</li> <li>The engagement letter examples and modified report examples should not refer to material deficiencies in compliance framework/controls.</li> </ol>	<p>revised ASAE 3000.</p> <p>On this basis the ATG will retain the concept of “Compliance Framework” in revised ASAE 3100.</p>		
CPA	3. <u>Suitable criteria</u>	Comments noted by the ATG.	N	

Respondent Comment	Commentary	Change to be made to Doc? Y/N	Para No.
<p>We do not consider that the phrase “evaluated by the suitable criteria” which is used throughout ED 04/16, after compliance requirements, is useful or communicates any useful meaning, as paragraph 9 states “the criteria may be the compliance requirements, or a subset thereof” anyway. Consequently, we consider that it simply serves to complicate the proposed standard. Compliance requirements are the criteria for a compliance engagement and whilst they may be broken down into greater detail in order to test the compliance activities, we do not see how repeated use of this phrase aids clarity. In addition, the example engagement letters and reports include “[compliance requirements] evaluated by the [suitable criteria]” requiring both terms to be specified or described. We consider that this would be unnecessarily onerous and in many cases not be possible. For example for a compliance engagement on a SMSF the “compliance requirements” are: SIS Act Sections 17A, 35AE, 35B, 35C(2), 62, 65, 66, 67,67A, 67B, 82-85, 103, 104, 104A, 105, 109 and 126K and SIS Regulations 1.06(9A), 4.09, 4.09A, 5.03, 5.08, 6.17, 7.04, 8.02B, 13.12, 13.13, 13.14 and 13.18AA. We are not clear how the “suitable criteria” could be described in addition to these compliance requirements or add any value to the assurance report on a SMSF.</p> <p>We suggest that the phrase “evaluated by the suitable criteria” and “using the criteria” should be deleted throughout ED 04/16.</p>	<p>The concepts of ‘compliance requirements’ and suitable ‘criteria’ were discussed at length by the Board throughout the development of ED 04/16. The draft ED 04/16 presented to the Board in Dec 15 was drafted excluding the phrase “evaluated by the suitable criteria” and the Board made a decision to reinstate this terminology as both concepts of “compliance requirements” and “criteria” are relevant in a compliance engagement. This position was also supported by the PAG and is consistent with extant ASAE 3100. A final decision was made by the Board at the February 2016 meeting to retain both terms in the ED 04/16 to provide a clearer understanding as to the application and objective of a compliance engagement.</p> <p>This reflected that the “compliance requirements” being what the entity has to comply with and the criteria as the subset, (or may be the same as the compliance requirements or even processes or procedures) of the requirements being what the assurance practitioner needs to consider in making their determination and drawing their conclusion about the entities compliance.</p> <p>Para 9 states “the criteria may be the compliance requirements, or a subset there of” however this may not always be the case therefore the need to retain both terms in the revised ASAE 3100.</p> <p>On this basis the ATG recommend retaining the wording “evaluated by the suitable criteria” in revised ASAE 3100.</p>		

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
CPA	Para. 3: We suggest that the phrase <i>“using the criteria”</i> is unnecessary. Likewise it should be deleted from paragraphs 9 and 17(e).	Comment noted by ATG  Refer comments at CPA – Point 3 – Suitable Criteria above.	N	
CPA	Sub-para. 17(q)(i) The use of “matter of”, “matters of” or “matter(s) of” non-compliance is unnecessary and does not aid clarity nor will it be well understood. We suggest the words “matter/s of” are deleted or, if necessary, replaced with “instances of” in this sub-paragraph and throughout ED 04/16, including paragraphs 25(h), 29, 40, 44L, 45R, 51, 54, 55, 63, A27, A28, A29, A30, A33, A45, A46, A49 and Appendix 7 Example 1.	Comments noted by ATG  AUASB made a decision in July 16 Board meeting to use the words ‘matters of’ where appropriate. On this basis retain the current wording.	N	
CPA	Sub-para. 17(q)(ii) We consider that materiality is relevant to non-compliance only in a compliance engagement and not to the controls in place to address the risk of non-compliance. We suggest deleting this sub-paragraph: Material in the context of a compliance engagement -  (ii) <i>“in relation to the compliance framework and controls – instance(s) of deficiency that are significant in the context of the entity’s control environment and that may raise the compliance engagement risk</i>	Comments noted by ATG  Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<i>sufficiently to affect the assurance practitioner's conclusion."</i>			
CPA	<p>Para. 32:</p> <p>We understand that this paragraph is equivalent to ASAE 3000, paragraphs 46 and 47, and so we consider that the title to this section needs to be amended. We do not consider that this section does nor should relate primarily to understanding the compliance framework (controls) or compliance requirements. Understanding of the compliance requirements should have been gained in assessing the suitability of the criteria which is addressed in paragraph 23. Understanding of controls is addressed for reasonable assurance engagements but controls do not need to be evaluated necessarily in a limited assurance engagement. Consequently, we suggest that this section should be titled "Obtaining an understanding of the compliance activities and other engagement circumstances".</p> <p>We consider that the wording of this paragraph, both 32L and 32R, should reflect the need to understand the compliance activities. The phrase "entity's compliance framework and its key elements, the compliance requirements" should be replaced with "entity's compliance activities to meet the compliance requirements".</p> <p>We do not consider that it is usually necessary in a</p>	<p>Comments noted by ATG</p> <p>ATG do not agree with this suggested change as reference to the understanding of the compliance framework in para 32 would encompass the compliance activity as it is a broad definition.</p> <p>As above</p>	<p>N</p> <p>N</p> <p>Y</p>	<p>32L(a),</p>

Respondent Comment			Commentary	Change to be made to Doc? Y/N	Para No.
		<p>compliance engagement to select or develop further suitable criteria, so we suggest that sub-paragraphs 32L(a) and 32R(a) are deleted. This requirement is necessary in a controls engagement where identification of the controls which meet the control objectives maybe an involved process.</p> <p>It may be necessary to develop a requirement for limited assurance engagements equivalent to paragraph 32R(c), which could be drawn from ASAE 3000 paragraph 47L.</p>	<p>ATG agree with the suggested change.</p> <p>ATG do not agree with the suggested change as the processes over the compliance outcome would be covered by the requirement in para 32L.</p>	N	32R(a)
CPA	Para. 40:	To remove implied objective regarding controls delete: <i>“material deficiency in the compliance framework”</i> .	<p>Comments noted by ATG</p> <p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p>	N	
CPA	Para. A3:	We suggest deleting this paragraph as it does not add any further information, and maybe misleading. We do not consider that compliance engagements particularly address “risks, compliance requirements and related controls”. As consideration of risk and controls are simply part of the assurance process not matters addressed in their own right in the same way as a controls engagement must consider them. In addition, the definition of compliance requirements already covers the sources of requirements listed in this paragraph, so there is no need to repeat	<p>Comments noted by ATG</p> <p>ATG agree with comments and will delete Para A3.</p>	Y	A3

Respondent Comment			Commentary	Change to be made to Doc? Y/N	Para No.
		compliance with these as the “subject matter”.			
CPA	Para. A4:	We suggest that this paragraph is redundant and so should be deleted. We note that this paragraph is included in ASAE 3150, but controls engagements are quite different to compliance engagements. In a controls engagement identifying the relevant control objectives and controls may be an involved process in a direct engagement where there is no description of the system. A “description” is mentioned in this paragraph but it is not relevant to a compliance engagement and identification of the compliance requirements in an attestation versus a direct compliance engagement is not typically significantly different.	<p>Comments noted by ATG</p> <p>ATG believe this paragraph is relevant to compliance engagements and the distinction between the work effort for a direct and attestation compliance engagement and therefore will retain para A4.</p> <p>Could have a description of the compliance framework??</p>	N	
CPA	Para. A9(b):	This sub-paragraph does not fit grammatically after “An appropriate subject matter is:”, so we suggest deleting “Such that the information about it can” and replace with “Able to”.	<p>Comment noted by ATG</p> <p>ATG agree with comment and suggested change to Para A9(b).</p>	Y	A9(b)
CPA	Para. A26	To remove implied objective regarding controls delete: “deficiencies in the compliance framework”.	<p>Comments noted by ATG</p> <p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p>	N	

Respondent Comment			Commentary	Change to be made to Doc? Y/N	Para No.
CPA	Para. A28	To remove implied objective regarding controls delete: <i>“deficiencies in the compliance framework”</i> and <i>“deficiencies or matters of”</i> .	Comments noted by ATG  Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.	N	
CPA	Para. A33:	The term compliance requirements should be used consistently throughout ASAE 3100. However, in paragraph A33 the term “obligations” has been used several times in place of “requirements”. We suggest that it is replaced.	Comments note by ATG  ATG agree with comment and suggested change to Para A33.	Y	A33
CPA	Para. A35:	Sub-paragraphs (a) and (b) would benefit from linking more directly to the compliance requirements, by using terms such as “controls over compliance”, “fraud with respect to compliance” or “ethical behaviour with respect to compliance”.	Comments note by ATG  ATG agree with comment and will set Para A35(a) and (b) more clearly “with respect to compliance “	Y	A35
CPA	Para. A38:	We suggest deleting the last sentence: <i>“In the case of an attestation engagement, such procedures may include asking the responsible party to examine the matter identified by the assurance practitioner, and to make amendments to the description or Statement, if appropriate.”</i> We consider that this sentence is not relevant as a description is not normally prepared in a compliance engagement and the Statement does not	Comments note by ATG  ATG agree with comment and suggested change to Para A38.	Y	A38

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	normally include a level of detail about the compliance activities which would necessitate amendments.			
CPA	Para. A39: To remove implied objective regarding controls delete: <i>“deficiencies in the compliance framework”</i> .	Comments noted by ATG  Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.	N	
CPA	Para. A42(b) To remove implied objective regarding controls delete: <i>“material deficiency in the compliance framework”</i> .	Comments noted by ATG  Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.	N	
CPA	Sub-para. A59(b)(iii) We suggest deleting this sub-paragraph as it states that an adverse conclusion may be issued if there is a material and pervasive <i>“Systemic deficiency in the compliance framework”</i> . We do not consider that deficiencies in the compliance framework (controls) can directly impact the assurance practitioner’s conclusion. If there are deficiencies in the controls which the assurance practitioner intended to rely upon, then the assurance practitioner cannot rely on those controls and will need to instead conduct further substantive testing sufficient to conclude as to whether or not material non-compliance exists, regardless of the adequacy or inadequacy of controls.	Comments noted by ATG  ATG agree with the comment and suggested removal of para 59(b)(iii) as deficiencies in the compliance framework won’t affect the opinion on compliance with compliance requirements only the risk assessment.	Y	A59(b)(iii)
CPA	<u>Appendix 1:</u> We suggest that this diagram could reflect the information more accurately and clearly by: <ul style="list-style-type: none"> <li>Replacing “Compliance activity to meet the Compliance Requirements” with simply “Compliance Activities”.</li> </ul>	Comments noted by ATG  Direct engagements still have a ‘compliance outcome’ on which the assurance practitioner	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<ul style="list-style-type: none"> <li>Deleting the box for “Attestation Statement” and renaming the box “Compliance outcome” as “Statement” with the arrow to it labelled “attestation engagement”.</li> <li>Deleting the box for “Direct Conclusion”, as this is already represented by the box “Compliance Assurance Report”, and inserting a new arrow from the Criteria box to Compliance Assurance Report box labelled “direct engagement”.</li> </ul> <p>We suggest that the phrase “using the criteria” as it is unnecessary.</p>	<p>concludes on in the ‘Compliance Assurance Report’. The difference being the compliance outcome is determined by the assurance practitioner not the responsible party.</p> <p>On this basis the ATG to retain the current diagram in App 1.</p> <p>Refer comments at CPA – Point 3 – Suitable Criteria above.</p>		
CPA	<p><u>Appendix 2:</u> Delete “(a)” after “objective”. We suggest deleting the row “Compliance requirements” as this is not a term used in ASAE 3000 there is no need to explain the equivalent term in ASAE 3100 and it is already defined in paragraph 17(f).</p> <p>We suggest moving the terms “compliance outcome” and “compliance activity” from column 1 to column 3 to make it clear which terms relate to the definitions provided.</p> <p>We suggest deleting the phrase “using the criteria” from the row subject matter information vs compliance outcome and column ASAE 3100, as it is</p>	<p>Comments noted by ATG.</p> <p>ATG agree to delete (a) after objective. By including the term ‘compliance requirements in the Table at App 2 it serves to highlight the differences between ASAE 3000 and revised ASAE 3100.</p> <p>ATG agree with this suggested change.</p> <p>Refer comments at CPA – Point 3 – Suitable Criteria above.</p>	<p>Y</p> <p>N</p> <p>Y</p> <p>N</p>	App 2

Respondent Comment			Commentary	Change to be made to Doc? Y/N	Para No.
		unnecessary.			
CPA	<u>Appendix 4:</u>	We suggest deleting the rows 4 and 5 as we do not see the relevance of service organisation's controls and controls over economy, efficiency or effectiveness to compliance engagements nor the need to explain that ASAE 3100 is not relevant.	Comments noted by ATG  ATG agrees to the suggested changes to App 4 as row 4 and 5 are not relevant to the subject matter of a compliance engagement.	Y	App 4
CPA	<u>Appendix 5:</u>	<p>The assurance practitioner's conclusion in an attestation engagement may be phrased not only in terms of the responsible party's Statement, but alternatively it may be phrased in terms of the underlying subject matter and the applicable criteria. Therefore, we suggest that it would be helpful to provide the alternative wording in the engagement letter. For example, alternative wording could be added to the phrases:</p> <ul style="list-style-type: none"> <li>• "ABC's Statement is fairly stated" add alternative "/ABC complied with the [compliance requirements]".</li> <li>• "Misstatements in ABC's Statement" add alternative "/non-compliance with the [compliance requirements]".</li> </ul> <p>Paragraph 2, page 45; paragraph 5, page 47 and paragraph 5, page 49 discuss inherent limitations of the engagement, however as this is not a controls</p>	<p>Comments noted by ATG</p> <p>ATG agrees with comments.</p> <p>Further clarification will be provided in footnote 41 – Exp 1 and footnote 44 – Exp 2 to reflect the alternative wording in the example engagement letters for attestation engagements that refer specifically to the compliance requirements being met.</p> <p>Internal controls and the compliance framework as a whole do influence the likelihood of non-compliance or material non-compliance with the</p>	Y	App 5 – Exp 1 and 2

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>engagement we consider that references to internal controls should be deleted including: <i>“together with the inherent limitations of any system of internal control”</i>, <i>“deficiencies in the compliance framework”</i> (already raised above) and <i>“Therefore no opinion will be expressed as to the effectiveness of the system of control as a whole”</i>. In addition, with respect to example 1, we note that in a limited assurance engagement the assurance practitioner is not required to evaluate controls as they are required to do in a reasonable assurance engagement.</p> <p>Paragraph 4, page 45; paragraph 6, page 47 and paragraph 1, page 50 - We suggest deleting or truncating sub-paragraphs (c) and (d) as these are matters which the responsible party has to address in an attestation controls engagement in order to prepare a description of the system of controls, but we do not consider that these need to be detailed to such an extent in a compliance engagement.</p> <p>Paragraph 2, page 46 &amp; paragraph 4, page 48 - The bracketed section on period and date do not flow grammatically and could be amended to: <i>“[the specified period or will be as at a specified date]”</i></p> <p>Paragraph 3, page 46 - States that the assurance</p>	<p>compliance requirements. As such the assurance practitioner needs to obtain an understanding of both these areas in undertaking their risk assessment in planning the engagement.</p> <p>Reference to inherent limitations meets requirement 57(h) Assurance Report content and is consistent with ASAE 3000 and extant ASAE 3100.</p> <p>The wording to be clarified and consistent with other ASAEs regarding inherent limitations in App 5 – Exp 1-3.</p> <p>ATG agree with this comment and suggested changes to App 5 by merging sub-paragraphs (c) and (d) in relation to what the responsible party has to address in relation to controls.</p> <p>ATG agree with this comment and suggested changes to App 5 to include <i>“[the specified period or will be as at a specified date]”</i></p>	<p>Y</p> <p>Y</p> <p>Y</p>	<p>App 5 – Exp 1, 2 and 3</p> <p>App 5 – Exp 1, 2 and 3</p> <p>App 5 – Exp 1</p>

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	report will be attached to ABC's Statement but in sub-paragraph 4(a), page 45, it states the opposite, that the Statement will be attached to the assurance report. Likewise paragraph 5, page 48 is inconsistent with paragraph 6(a), page 47. We do not have a preference but it needs to be amended to be consistent.	ATG agree with this comment and suggested changes to App 5 to reflect the Statement being attached to the Auditor's report.	Y	App 5 – Exp 1 and 2
	Paragraphs 4 and 5, page 46; paragraphs 6 and 7, page 48 and paragraphs 4 and 5, page 50 - we suggest using the future tense as the report will be prepared in the future.	ATG agree with this comment and suggested changes to App 5.	Y	App 5 – Exp 1, 2 and 3
	Example 1: Paragraph 4, page 44 - The description of the procedures which the assurance practitioner will perform in should align with the procedures described in the requirements, specifically paragraph 43L. Paragraph 43L lists discussion, observation and walk-through but does not include examination of documentation nor uses the term enquiries.	Terminology referring to procedures will be reviewed to ensure consistent with requirements in 43L.	Y	43L, App 5 – Exp 1
	Paragraphs 1 & 2, Page 45 - To remove implied objective regarding controls delete: <i>"deficiencies in the compliance framework"</i> .	Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.	N	
	Paragraph 3, page 45 - We suggest deleting the phrase			

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p><i>“any material deficiencies in the compliance framework and relevant controls that exist may not be revealed by the engagement” as this is not the objective of the engagement and replace with “non-compliance may not be detected” or “misstatements in the Statement may not be detected”.</i></p> <p>Paragraph 3, page 45 - we query the need for the last sentence <i>“In expressing our conclusion, our report on ABC’s Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria] will expressly disclaim any reasonable assurance conclusion on the compliance framework and relevant controls.”</i> And suggest it could be deleted.</p> <p>Paragraph 3, page 45 - <i>To remove implied objective regarding controls delete: “any material deficiencies in the compliance framework and relevant controls”</i> and replace with the objective of a compliance engagement being “non-compliance with the compliance requirements”.</p>	<p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p> <p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p> <p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p>	<p>N</p> <p>N</p> <p>N</p>	
Example 2:	<p>Paragraph 4, page 47 - We suggest deleting the words <i>“and controls implemented”</i> in as this is not the objective of a compliance engagement.</p> <p>Paragraphs 4 &amp; 5 page 47 - To remove implied</p>	<p>ATG do not agree with the suggested change as a requirement for reasonable assurance under Para 32R(c).</p>	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>objective regarding controls delete: <i>“deficiencies in the compliance framework”</i>.</p> <p>Example 3: Paragraphs 4 &amp; 5, page 49 - To remove implied objective regarding controls delete: <i>“deficiencies in the compliance framework”</i>.</p>	<p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p> <p>Refer comments at CPA Point 2 – Compliance Framework as a Subject Matter above.</p>	<p>N</p> <p>N</p>	
CPA	<p><u>Appendix 6:</u> Paragraphs 1, page 53; paragraph 4, page 55 &amp; paragraph 4, page 57 - As noted above for the engagement letters, we suggest deleting or truncating sub-paragraphs (c) and (d) as these are matters which the responsible party has to address in an attestation controls engagement in order to prepare a description of the system of controls, but we do not consider that these need to be detailed to such an extent in a compliance engagement, particularly for direct compliance engagements.</p> <p>Paragraph 3, page 54; paragraph 4, page 56 and paragraph 4, page 58 - We suggest using the term compliance requirements rather than laws and regulations for consistency with the requirements.</p> <p>Paragraph 4, page 54, paragraph 5, page 56 and paragraph 5, page 58 – These examples need to allow for engagements which cover a specified period not only a specified date by including the phrase</p>	<p>Comments noted by ATG</p> <p>ATG agree with this comment and suggested changes to the responsibilities of the entity to make it clearer as to their responsibilities in relation to risks and controls.</p> <p>ATG agree with these comments and suggested changes to ensure App 6 has consistent wording to the requirements.</p> <p>ATG agree with these comments and suggested changes as this statement applies to both scenarios “at a specified date and throughout the specified</p>	<p>Y</p> <p>Y</p> <p>Y</p>	<p>App 6 – Exp 1</p> <p>App 6 – Exp 1, 2 and 3</p> <p>App 6 – Exp 1, 2 and 3</p>

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>Example 1: <i>“throughout the period/”.</i></p> <p>Paragraph 4 and 6, page 53 - As noted above for example 1 of the engagement letters, the description of the procedures which the assurance practitioner performed should align with the procedures described in the requirements, specifically paragraph 43L. Paragraph 43L lists discussion, observation and walk-through but does not include examination of documentation or inspection nor uses the term enquiries.</p>	<p>period.</p> <p>Terminology referring to procedures will be reviewed to ensure consistent with requirements in 43L.</p>	Y	App 6 – Exp 1
CPA	<p><u>Appendix 7:</u> The explanation prior to the examples states that they are based on Appendix 6 but they do not seem to be in the same order and so it is not clear how they relate. We suggest deleting this statement or aligning the examples.</p> <p>Example 1: The title requires amendment as it is not possible for non-compliance to be identified with ABC’s Statement. We suggest the title either state that material non-compliance by ABC with the compliance requirements was identified or ABC’s Statement was materially misstated.</p> <p>Under the basis for qualified opinion it states that “We are unable to satisfy ourselves by alternative procedures”, which suggests that the assurance practitioner was unable to obtain sufficient</p>	<p>Comments noted by ATG</p> <p>ATG agree with this comment and will delete this statement in App 7.</p> <p>ATG agree with this comment and the title will be changed to suggestion 2: Material misstatement in ABC’s Statement on the entity’s compliance with the compliance requirements....</p> <p>ATG agree with this comment. The wording in the qualified opinion will be changed to...”We were unable to satisfy ourselves as to ABC’s compliance with this requirement, therefore qualify our opinion</p>	<p>Y</p> <p>Y</p> <p>Y</p>	<p>App 7</p> <p>App 7 – Exp 1</p> <p>App 7 – Exp 1</p>

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>appropriate evidence. However the title says it is an example of material non-compliance, in which case the “trustee bank account and cash book procedures” presumably required by the compliance requirements were not complied with. The basis for qualified opinion needs to be amended to reflect this conclusion.</p> <p>Example 2: This title requires amendment as compliance requirements cannot be non-compliant. Instead ABC could be non-compliant.</p> <p>We do not see that specifying “RSE” in this example is necessary, especially without defining this acronym, and so we suggest using ABC as in the other examples.</p> <p>Example 4: The title suggest that this example seems to be seeking to illustrate when the assurance practitioner could not obtain sufficient appropriate evidence, however this is not clear from the basis for qualified conclusion paragraph. That paragraph states that material non-compliance was identified. The paragraph needs to be redrafted to address the intended reason for the qualification and needs to include the words “We were unable to obtain sufficient appropriate audit evidence about”.</p>	<p>in this regard”.</p> <p>ATG agree with this comment. The title will change to .....”ABC non-compliant with the compliance requirements throughout the specified period.....”</p> <p>ATG agrees with this comment. RSE will be changed to ABC for consistency.</p> <p>ATG agrees with this comment. The Basis for Qualified Conclusion first sentence will change to: “We were unable to obtain sufficient appropriate audit evidence regarding ABC’s compliance with [sXX of Act/regulation XX].</p>	<p>Y</p> <p>Y</p> <p>Y</p>	<p>App 7 – Exp 2</p> <p>App 7 – Exp 2</p> <p>App 7 – Exp 4</p>
CAANZ	<b>Materiality</b>	Comments noted by ATG.		

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p>One of the most challenging aspects of a compliance engagement in practice is materiality, both in the planning stages to determine what a material instance of non-compliance is and in evaluating the instances of non-compliance to determine whether the assurance practitioner's conclusion should be modified. The assurance practitioner must apply professional judgement to understand the needs of the intended users and what is material to them, to consider largely qualitative factors to determine materiality and to evaluate when instances of non-compliance should be considered to be pervasive when determining the nature of a modification to their conclusion.</p> <p>Because compliance engagements are becoming increasingly prevalent in areas such as the not-for-profit sector where compliance requirements may be included in grant agreements, these engagements may be performed by a range of assurance practitioners and their experience considering materiality in non-financial assurance potentially varies widely.</p> <p>The revised ASAE appears to have slightly less material on materiality than extant ASAE 3100. Given that the correct application of materiality is key to these engagements and challenging for practitioners, we encourage the board to consider whether further material to assist practitioner's with applying materiality in compliance engagements can be included either in the standard or provided as guidance material in another format.</p>	<p>The ATG acknowledge the general comments regarding materiality.</p> <p>The ATG have used the application material in the extant ASAE 3100 as a base for the materiality guidance included in revised ASAE 3100 and have adapted it as necessary to include current engagement circumstances and to ensure consistency with ASAE 3000.</p> <p>The ATG does not consider this guidance to be any less in nature or form than the extant ASAE 3100 and coupled with that in ASAE 3000 believe that it is sufficient.</p>	N	
CAANZ	<p><b>Terminology</b></p> <p>We note that the ED introduces several new terms to describe</p>	<p>Comments noted by ATG.</p> <p>Appendix 1, 2 and 3 have been included in ED</p>	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	the various aspects of a compliance engagement. While we understand that these are useful concepts to assist the assurance practitioners to perform the engagements, we found the definitions to be somewhat confusing when reading the standard. The guidance in the Appendices assists in clarifying the differences between the compliance activity, the compliance outcome, the compliance requirements and the criteria, however, we believe it would be useful for practitioners if an additional appendix (in diagram format) was included that demonstrates how all these aspects of a compliance engagement, as well the compliance framework fit together.	04/16 to endeavour to better illustrate the terminology adopted in this subject matter specific ASAE.  Therefore the ATG doesn't believe adding an additional Appendix in this regard would be useful and may actually be more confusing.		
Deloitte	We have an overall concern that the standard may not achieve the desired outcome and the simplicity of the current standard achieves this. In addition, we question whether there is sufficient clarification as to what is required when reporting on compliance at a specific date versus when you are performing an engagement to report on compliance throughout the period.	Comments noted by ATG.  Refer detailed comments below.	N	
Deloitte	<b>Para – 17 (u)</b> Proposed definition of Professional scepticism reads <i>“An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement, and a critical assessment of evidence.”</i>  This is inconsistent with the definition in ASA 200 which reads “Professional scepticism means an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement <u>due to error or fraud</u> , and a critical assessment	Comments noted by ATG.  The Professional scepticism definition in para 17(u) is consistent with ASAE 3000 definition and on this basis will be retained with no change.	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	of audit evidence.			
Deloitte	<b>Para – 39</b> We recommend that paragraph 39 is redrafted as follows “ <i>The assurance practitioner shall design and perform further procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement, having regard to the level of assurance, reasonable or limited, as appropriate</i> ”. This construct is consistent with that used in paragraph 36 of ASAE 3410.	Comments noted by ATG.  The current wording used in Para 39 is consistent with that used in ASAE 3150 para 45.  On this basis the current wording will be retained.	N	
Deloitte	<b>Para – 42</b> As noted in our overall comments we believe that paragraph 42 needs to better distinguish, for the assurance practitioner, the differences in evidence required when reporting on compliance throughout the period versus when reporting on compliance at a specific date. We do not believe that the application material in paragraph A38 achieves this.	Comments noted by ATG.  An additional application material para A38 has been included with regard to .....evidence required when reporting on compliance throughout the period versus when reporting on compliance at a specific date. This is consistent with wording used in ASAE 3150 and ASAE 3402 para A32.	Y	New A38
Deloitte	<b>Para 43L and 43R</b> This tabular information contains the words “ <i>shall ordinarily</i> ”. The use of the word ordinarily is not appropriate in a requirement paragraph.  In addition, the procedures listed which are currently separated by a comma could be better displayed as per ASAE 3150 par 54R.	Comments noted by ATG.  Suggested change to remove the term ‘ordinarily’ will be adopted for consistent wording in the requirements.  Suggested change to layout in para 43L and 43R will be adopted for clarity.	Y	43L, 43R
Deloitte	<b>Para – 49</b> “ASAE 3000 requires the assurance practitioner to accumulate uncorrected misstatements identified during the engagement other	Comments noted by ATG.	N	

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	<p><i>than those that are clearly trivial. Misstatements in a compliance engagement are instances of non-compliance with the compliance requirements."</i></p> <p>We recommend inserting the words "qualitative and quantitative" after uncorrected misstatements in the paragraph. However we understand this is the exact wording per ASAE 3000.</p>	ATG to retain the current wording in Para 49 as consistent with ASAE 3000 para 51.		
Deloitte	<p><b>Para – 50</b>  <i>"Evaluation of evidence obtained by the assurance practitioner shall include any impact of corrected misstatements identified during the compliance engagement."</i></p> <p>We believe that an application guidance paragraph is needed to explain to the practitioner that the overall opinion is based on not only the uncorrected misstatements but also on the extent of corrected misstatements. The extent of corrected misstatements may lead a practitioner to conclude that compliance has not been achieved.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment. An additional application material paragraph with the suggested wording will be added.....</p>	Y	New A46
Deloitte	<p><b>Para - A17(c)</b>  <i>This paragraph states "It is more cost effective for the entity to identify the specific compliance activities, requirements and related controls, evaluate the compliance outcome as the basis for an attestation engagement, rather than it being necessary for the assurance practitioner to do so in a direct engagement."</i></p> <p>We question why this an assurance practitioner's consideration? We believe that it is more the engaging party's consideration. We recommend that this sentence is re-written to clarify its purpose.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggestion on para 17(c). This paragraph does not add anything to the clarity of the engagement letter and will be deleted.</p>	Y	A17(c)

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
Deloitte	<p><b>Para - A20</b> We believe that this paragraph could be simplified if it was redrafted as follows:</p> <p><i>Where relevant, the terms of the engagement could also include a reference to, and description of, the auditor's responsibility in accordance with;</i></p> <ul style="list-style-type: none"> <li>• <i>applicable law,</i></li> <li>• <i>regulation or relevant ethical requirements, and</i></li> <li>• <i>reporting obligations to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is required or appropriate in the circumstances.</i></li> </ul>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to para A20.</p>	Y	A20
Deloitte	<p><b>Para – A22</b> “An example engagement letter is contained in Appendix 5.”</p> <p>As there is more than one engagement letter, we propose the following: Example engagement letter(s) are contained in Appendix 5.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to para A22.</p>	Y	A22
Deloitte	<p><b>Para – A29</b> “...the evaluation of compliance with the compliance requirements, and the interests of the intended users...”</p> <p>The comma after the word requirements should be removed so that the sentence reads, ‘the evaluation of compliance with the compliance requirements and the interests of the intended users’.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to para A29.</p>	Y	A29

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
Deloitte	<p><b>Para – A35 (d)</b> This paragraph states ‘...and the internal control that management has established to mitigate these risks as far as they relate to the compliance requirements...’</p> <p>The paragraph appears to assume that management has only one internal control to mitigate the risks related to the compliance requirements.</p> <p>We propose that it is amended as follows “... and the internal controls that management have established to mitigate these risks as far as they relate to the compliance requirements;</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to para A35(d).</p>	Y	A35(d)
Deloitte	<p><b>Para – A45</b> Within the text there is the following - <i>Error in reference (Ref: Para. 49-Error! Reference source not found.)</i> This needs to be corrected.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to para A45.</p>	Y	A45
Deloitte	<p><b>Para – A46</b> Reference to paragraph 44 is incorrect as the content of paragraph A46 only relates to paragraph 44 L</p>	<p>Comments noted by ATG.</p> <p>The reference to para 44 is correct as the AM para A46 refers to both reasonable and limited assurance material.</p>	N	A46
Deloitte	<p><b>Appendix 2</b> <b>Objective (a)</b> – the ‘(a)’ should be deleted.</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change to Appendix 2.</p>	Y	App 2
Deloitte	<p><b>Appendix 3</b> Under the heading there is a description stated ‘<b>Scope of the Engagement</b>’ which is already included in the table, therefore we</p>	<p>Comments noted by ATG.</p> <p>ATG agree with the comment and suggested change</p>	Y	App 3

Respondent Comment		Commentary	Change to be made to Doc? Y/N	Para No.
	recommend removing.	to Appendix 3.		
Deloitte	<b>Appendix 3</b> Page 42 is missing Appendix number and headers.	Comments noted by ATG.  ATG agree with the comment and suggested change to Appendix 3.	Y	App 3
Deloitte	<b>Appendix 5</b> Page 49 –“To [the appropriate addressee]:” should be in italics to be consistent with the other engagement letters.	Comments noted by ATG.  ATG agree with the comment and suggested change to Appendix 5.	Y	App 5

\* \* \*

**ASAE 3100**  
(December 2016)

**Standard on Assurance Engagements**  
**ASAE 3100**  
*Compliance Engagements*

Issued by the **Auditing and Assurance Standards Board**



**Australian Government**  
**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Standard on Assurance Engagements**

This Standard on Assurance Engagements is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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***Compliance Engagements***

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## PREFACE

### **Reasons for Issuing ASAE 3100**

The AUASB issues Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* pursuant to the requirements of the legislative provisions explained below.

The AUASB is an Australian Government agency established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 227B of the ASIC Act, the AUASB may formulate assurance standards for other purposes.

### **Main Features**

This Standard on Assurance Engagements establishes requirements and provides application and other explanatory material regarding the conduct of and reporting on assurance engagements on compliance. The standard replaces Standard on Assurance Engagements ASAE 3100 *Compliance Engagements*, issued by the AUASB in July 2008 and last revised in October 2008.

This Standard on Assurance Engagements facilitates conformity with current AUASB Standards and revised ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* issued in June 2014. The standard reflects best practice in compliance engagements and clarifies how to scope, conduct and report on an assurance engagement on compliance, to ensure that assurance engagement quality is maintained and where necessary improved.

**AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates this Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*.

This Standard on Assurance Engagements is to be read in conjunction with ASA 100 *Preamble to AUASB Standards*, which sets out the intentions of the AUASB on how the AUASB Standards are to be understood, interpreted and applied and ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, which provides the overarching requirements for all assurance engagements other than those engagements relating to historical financial information.

Dated: <TypeHere>

M H Kelsall  
Chairman - AUASB

**Conformity with International Standards on Assurance Engagements**

This Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* has been formulated for Australian public interest purposes and there is no equivalent International Standard on Assurance Engagements (ISAE), issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

This Standard does, however, reflect certain aspects of other Australian ASAEs, which reproduce substantial parts of the equivalent ISAEs issued by the IAASB and published by IFAC, including ISAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.

# STANDARD ON ASSURANCE ENGAGEMENTS ASAE 3100

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## *Compliance Engagements*

### **Application**

1. This Standard on Assurance Engagements applies to limited and reasonable assurance engagements to provide an assurance report on an entity's compliance with the compliance requirements as evaluated by the suitable criteria. (Ref: Para. A1)

### **Operative Date**

2. This Standard on Assurance Engagements is operative for assurance engagements commencing on or after 1 January 2018, with early adoption permitted prior to this date.

### **Introduction**

#### **Scope of this Standard on Assurance Engagements**

3. This Standard on Assurance Engagements (ASAE) deals with assurance engagements to provide an assurance report on whether the entity has complied in all material respects with the compliance requirements, throughout the specified period or as at a specified date, using the criteria.
4. This ASAE addresses assurance engagements on compliance: (Ref: Para. A2-A5)
  - (a) With the compliance requirements;
  - (b) Providing a limited or reasonable assurance conclusion;
  - (c) For either restricted use, by those charged with governance of the entity or specified third parties, or to be publicly available; and
  - (d) Either based on an attestation engagement or a direct engagement. (Ref: Para. 17(a), 17(h), A4).
5. Agreed-upon procedures engagements, where procedures are conducted and factual findings are reported but no conclusion is provided, and consulting engagements, for the purpose of providing advice, on compliance are not assurance engagements and are not dealt with in this ASAE. Agreed-upon procedures engagements are addressed under Standard on Related Services, ASRS 4400.<sup>1</sup>

#### *Nature of a Compliance Engagement*

6. Compliance engagements are conducted in both the private and public sector, in either case the engaging party will usually be the entity responsible for meeting the compliance requirements which are subject to the compliance engagement. In these circumstances terms of engagement are agreed with the engaging party.
7. An entity may have an obligation to comply with externally and/or internally established compliance requirements. These compliance requirements may be established through law and regulation, contractual arrangements or internally established requirements, for example company policies. A table showing the nature of assurance engagements on compliance is contained in Appendix 3.

<sup>1</sup> See ASRS 4400 Agreed upon Procedures Engagements to Report Factual Findings.

## Standard on Assurance Engagements ASAE 3100

### Compliance Engagements

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#### *Relationship with ASAE 3000, Other Pronouncements and Other Requirements*

8. The assurance practitioner is required to comply with ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (ASAE 3000) and this ASAE when performing compliance engagements. This ASAE supplements, but does not replace ASAE 3000, and expands on how ASAE 3000 is to be applied in a compliance engagement. This ASAE applies the requirements in ASAE 3000 to attestation engagements and adapts those requirements, as necessary, to direct engagements on compliance. ASAE 3000 includes requirements in relation to such topics as engagement acceptance, planning, obtaining evidence and documentation that apply to all assurance engagements, including engagements conducted in accordance with this ASAE. *Framework for Assurance Engagements*, which defines and describes the elements and objectives of an assurance engagement, provides the context for understanding this ASAE and ASAE 3000.
9. An assurance engagement performed in accordance with ASAE 3000 measures or evaluates the underlying subject matter against suitable criteria. In a compliance engagement the assurance practitioner determines whether compliance requirements have been met by evaluating the subject matter against the compliance requirements, using the criteria. The criteria may be the compliance requirements, or a subset thereof. A table explaining the terminology applied in this ASAE is contained in Appendix 2.
10. This ASAE requires the assurance practitioner to apply the ASAE 3000 requirement to comply with relevant ethical requirements related to assurance engagements. It also requires the lead assurance practitioner to be a member of a firm that applies ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Financial Information, Other Assurance Engagements and Related Services Engagements*.
11. An assurance engagement performed under this ASAE may be part of a larger engagement. In such circumstances, this ASAE is relevant only to the portion of the engagement relating to assurance on compliance.
12. If multiple standards are applicable to the assurance engagement, the assurance practitioner applies, in addition to ASAE 3000, either:
  - (a) If the engagement can be separated into parts, the standard relevant to each part of the engagement, including this ASAE for the part on compliance; or
  - (b) If the engagement cannot be separated into parts, the standard which is most directly relevant to the subject matter.
13. Assurance conclusions on compliance may be required by Regulators, Government or other users in conjunction with assurance conclusions on financial reports, other historical financial information, and compliance with other requirements, controls and/or other subject matters. In these engagements the subject matter and criteria against which that subject matter is evaluated and the level of assurance sought may vary, in which case different standards will apply. Assurance reports can include separate sections for each subject matter, criteria or level of assurance in order that the different matters concluded upon are clearly differentiated.
14. A table showing the AUASB Standards to apply to compliance engagements depending on the subject matter and engagement circumstances is contained in Appendix 4. (Ref: Para. A1)

### Objectives

15. In conducting a compliance engagement, the objectives of the assurance practitioner are:
  - (a) To obtain reasonable or limited assurance, about whether the entity has complied in all material respects, with compliance requirements as evaluated by the suitable criteria;

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**Compliance Engagements**

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- (b) To express a conclusion<sup>2</sup> through a written report on the matters in (a) above which expresses either a reasonable or limited assurance conclusion and describes the basis for the conclusion; and/or
  - (c) To communicate further as required by this ASAE and any other relevant ASAEs.
16. In conducting the assurance engagement, the objectives of the assurance practitioner under ASAE 3000<sup>3</sup> include: “to obtain either reasonable or limited assurance, as appropriate, about whether the subject matter information is free from material misstatement”. The subject matter information in a compliance engagement is the outcome of the evaluation<sup>4</sup> of compliance with the compliance requirements, as evaluated by the criteria. The evaluation is conducted:
- (a) In an attestation engagement on compliance, by the responsible party or evaluator, and presented in a Statement<sup>5</sup>, which addresses whether the compliance requirements have been met. The objective of the assurance practitioner is to obtain reasonable or limited assurance about whether the Statement is free from material misstatement, although the assurance practitioner’s conclusion may be expressed in terms of whether the compliance requirements have been met; or
  - (b) In a direct engagement on compliance, by the assurance practitioner and presented in the assurance conclusion, therefore, no Statement is prepared by the responsible party. The objective of the assurance practitioner is to obtain reasonable or limited assurance about whether the compliance requirements have been met.

**Definitions**

17. For the purposes of this Standard on Assurance Engagements, the following terms have the meanings attributed below:
- (a) Attestation engagement on compliance—A reasonable or limited assurance engagement in which a party other than the assurance practitioner, being the responsible party or evaluator evaluates compliance with the compliance requirements. The outcome of that evaluation is provided in a Statement, which may either be available to the intended users or may be presented by the assurance practitioner in the assurance report. In an attestation engagement on compliance, the assurance practitioner’s conclusion addresses whether the Statement is free from material misstatement. The assurance practitioner’s conclusion may be phrased in terms of: (Ref: Para. 4(d), A4)
    - (i) The compliance outcome and the criteria; or
    - (ii) A Statement made by the appropriate party.
  - (b) Compliance activity (subject matter or underlying subject matter)—The activity that is undertaken to meet the compliance requirement(s).
  - (c) Compliance engagement—An assurance engagement in which an assurance practitioner expresses a conclusion after evaluating an entity’s compliance with the compliance requirements.
  - (d) Compliance framework—A framework adopted by the entity, which is designed to ensure that the entity achieves compliance, and includes governance structures, programs, processes, systems, controls and procedures.

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<sup>2</sup> The term conclusion also extends to include an opinion expressed in a reasonable assurance engagement.

<sup>3</sup> See ASAE 3000, paragraph 10.

<sup>4</sup> The term evaluation includes the concept of measurement for quantification aspects of a compliance engagement.

<sup>5</sup> See ASAE 3100, paragraph 17(z) for definition of the term Statement.

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**Compliance Engagements**

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- (e) Compliance outcome (subject matter information)—The outcome of the evaluation of the underlying subject matter (compliance activity) against the compliance requirements, using the criteria. The compliance outcome is the Statement of the responsible party or evaluator in an attestation engagement on compliance, or the assurance practitioner's conclusion in a direct engagement on compliance, providing the outcome of their evaluation.
- (f) Compliance requirement(s)—The ~~overarching~~<sup>specific</sup> requirements established in law, regulations, other statutory requirements (e.g. ASIC Class Orders and Regulatory Guides and APRA Prudential Standards), contractual arrangements, ministerial directives, industry or professional obligations or internally via entity policies, procedures and frameworks. (Ref: Appendix 1)
- (g) Criteria—The <sup>specific</sup> benchmark, framework or legislation used to evaluate whether the compliance requirements have been met. The “applicable criteria” are the criteria used for the particular engagement. (Ref: Para. 23, A13, Appendix 1)
- (h) Direct engagement on compliance—A reasonable or limited assurance engagement in which the assurance practitioner evaluates whether the compliance requirements have been met. The compliance outcome of the assurance practitioner's evaluation (the subject matter information) is expressed in the assurance practitioner's conclusion.
- (i) Engaging party—The party(ies) that engages the assurance practitioner to perform the assurance engagement.
- (j) Entity—The legal entity, economic entity, or the identifiable portion of a legal or economic entity, or combination of legal or other entities or portions of those entities (for example, a joint venture) to which the compliance requirements relate.
- (k) Evaluator—The party(ies) who evaluates the underlying subject matter (compliance activities) against the criteria. The evaluator possesses expertise in the underlying subject matter.
- (l) Firm—A sole assurance practitioner, partnership or corporation or other entity of individual assurance practitioners. “Firm” should be read as referring to its public sector equivalents where relevant.
- (m) Intended users—The individual(s) or organisation(s), or group(s) thereof that the assurance practitioner expects will use the assurance report. In some cases, there may be intended users other than those to whom the assurance report is addressed.
- (n) Internal audit function—A function of an entity that performs assurance and consulting activities designed to evaluate and improve the effectiveness of the entity's governance, risk management and internal control processes.
- (o) Limited assurance engagement—An assurance engagement in which the assurance practitioner reduces engagement risk to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for expressing a conclusion in a form that conveys whether, based on the procedures performed and evidence obtained, a matter(s) has come to the assurance practitioner's attention to cause the assurance practitioner to believe the compliance requirements have not been met, in all material respects. The nature, timing and extent of procedures performed in a limited assurance engagement is limited compared with that necessary in a reasonable assurance engagement but is planned to obtain a level of assurance that is, in the assurance practitioner's professional judgement, meaningful. To be meaningful, the level of assurance obtained by the assurance practitioner is likely to enhance the intended users' confidence about the compliance outcome to a degree that is clearly more than inconsequential.

- (p) Long-form report—Assurance report including other information and explanations that are intended to meet the information needs of users but not to affect the assurance practitioner's conclusion. In addition to the matters required to be contained in the assurance practitioner's report, as set out in paragraph 58, long-form reports may describe in detail matters such as:
- (i) the terms of the engagement;
  - (ii) the criteria being used and the specific compliance activities designed to meet each compliance requirement;
  - (iii) descriptions of the procedures that were performed;
  - (iv) findings relating to the procedures that were performed or particular aspects of the engagement;
  - (v) details of the qualifications and experience of the assurance practitioner and others involved with the engagement;
  - (vi) disclosure of materiality levels; or
  - (vii) recommendations.

The assurance practitioner may find it helpful to consider the significance of providing such information to meet the needs of the intended users. As required by paragraph 59, additional information is clearly separated from the assurance practitioner's conclusion and worded in such a manner as to make it clear that it is not intended to alter or detract from that conclusion.

- (q) Material in the context of a compliance engagement—
- (i) in relation to potential (for risk assessment purposes) or detected (for evaluation purposes) matter(s) of non-compliance – instance(s) of non-compliance that are significant, individually or collectively, in the context of the entity's compliance with compliance requirements, and that might influence relevant decisions of intended users or affect the assurance practitioner's conclusion; and/or
  - (ii) in relation to the compliance framework and controls – instance(s) of deficiency that are significant in the context of the entity's control environment and that may raise the compliance engagement risk sufficiently to affect the assurance practitioner's conclusion.
- (r) Misstatement—For attestation engagements on compliance, a difference between the Statement and the assurance practitioner's evaluation of compliance with the compliance requirements. Misstatements can be intentional or unintentional, qualitative or quantitative, and include omissions.
- (s) Non-compliance—For both attestation and direct engagements on compliance, a failure to meet a compliance requirement in whole or in part.
- (t) Professional judgement—The application of relevant training, knowledge and experience, within the context provided by assurance and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the engagement.
- (u) Professional scepticism—An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement or non-compliance, and a critical assessment of evidence.

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- (v) Reasonable assurance engagement—An assurance engagement in which the assurance practitioner reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the assurance practitioner's conclusion. The assurance practitioner's conclusion is expressed in a form that conveys the assurance practitioner's opinion on the outcome of the evaluation of the compliance activities against compliance requirements.
- (w) Representation—Statement by the responsible party, either oral or written, provided to the assurance practitioner to confirm certain matters or to support other evidence. A representation is additional to but may be provided in combination with the responsible party's or evaluator's Statement provided in an attestation engagement, as set out in paragraph 16(a).
- (x) Responsible party—The party(ies) responsible for the underlying subject matter, being the compliance activity(ies) in a compliance engagement.
- (y) Short-form report—Assurance report including only the matters required under paragraph 57 of this ASAE.
- (z) Statement—The outcome in writing of the responsible party or evaluator's evaluation of compliance with the compliance requirements, provided to the assurance practitioner in an attestation engagement. A Statement is the subject matter information in an attestation engagement on compliance.

## **Requirements**

### **Applicability of ASAE 3000**

18. The assurance practitioner shall not represent compliance with this ASAE unless the assurance practitioner has complied with the requirements of this ASAE and ASAE 3000, adapted as necessary in the case of direct engagements. ASAE 3000 contains requirements and application and other explanatory material specific to attestation assurance engagements but it also applies to direct assurance engagements, adapted as necessary in the engagement circumstances.<sup>6</sup> If this ASAE makes reference to a requirement in ASAE 3000, that requirement shall be applied to both attestation and direct engagements, unless specified otherwise. (Ref: Para. A1, Appendix 4)

### **Ethical Requirements**

19. As required by ASAE 3000, the assurance practitioner shall comply with relevant ethical requirements related to assurance engagements.<sup>7</sup> (Ref: Para. A6)

### **Acceptance and Continuance**

#### *Preconditions for the Assurance Engagement*

20. The assurance practitioner shall accept or continue a compliance engagement only in the circumstances required by ASAE 3000, including that the preconditions for an assurance engagement are present, unless required to accept the engagement by law or regulation.

#### *Appropriateness of the Subject Matter*

21. When establishing whether the preconditions for an assurance engagement as required by ASAE 3000 are present, the assurance practitioner is required to assess the appropriateness of the subject matter.<sup>8</sup> In doing so, the assurance practitioner shall determine whether the

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<sup>6</sup> See ASAE 3000, paragraph 2.

<sup>7</sup> See ASAE 3000, paragraphs Aus 20.1 and ASA 102 Compliance with Ethical Requirements when Performing Audits, Reviews and Other assurance Engagements.

<sup>8</sup> See ASAE 3000, paragraph 24(b)(i).

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### Compliance Engagements

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compliance activities which are to be evaluated are appropriate in addressing the needs of users, that is whether the performance of those activities determines whether the compliance requirements have been met. (Ref: Para. A9-A11)

22. If the subject matter is not appropriate, the assurance practitioner shall not accept the engagement or, if this is determined after accepting the engagement, either withdraw from the engagement or issue a modified conclusion.

#### *Assessing the Suitability of the Criteria*

23. When establishing whether the preconditions for an assurance engagement as required by ASAE 3000 are present, the assurance practitioner shall determine the suitability of the criteria expected to be applied, whether the criteria are provided by the engaging party, as in an attestation engagement, or are to be identified ~~or~~, selected ~~or developed~~ by the assurance practitioner, as in a direct engagement, including that they exhibit the characteristics set out in ASAE 3000.<sup>9</sup> (Ref: Para. 17(g), A12-~~g~~).

#### *Agreeing on the Terms of the Engagement*

24. ASAE 3000<sup>10</sup> requires the parties to the engagement to agree on the terms of the assurance engagement in writing. The assurance practitioner shall obtain the agreement of the responsible party, that it acknowledges and understands its responsibility:
- (a) In an attestation engagement, for evaluating the compliance activity against the compliance requirements and providing a written Statement regarding the outcome of that evaluation and for having a reasonable basis for the written Statement;
  - (b) For identifying suitable compliance requirements and whether they were specified by law, regulation, contract, another party (for example, a user group or a professional body) or developed by the responsible party ~~or assurance practitioner~~;
  - (c) For providing the assurance practitioner with:
    - (i) Access to all information, such as records, documentation and other matters of which the responsible party is aware are relevant to the compliance engagement;
    - (ii) Additional information that the assurance practitioner may request from the responsible party for the purposes of the assurance engagement; and
    - (iii) Unrestricted access to persons within the entity from whom the assurance practitioner determines it necessary to obtain evidence.
25. The terms of engagement shall identify:
- (a) The scope of the engagement;
  - (b) Whether the engagement is a reasonable or limited assurance engagement;
  - (c) Whether the engagement is an attestation or direct engagement and, in the case of an attestation engagement, the form of the responsible party's or evaluator's evaluation of the compliance activity or Statement and whether that Statement will be available to intended users or only referenced in the assurance report; (Ref: Para. A16,A20)
  - (d) The specified period or specified date to be covered by the engagement; (Ref: Para. A17)
  - (e) The compliance requirements against which the compliance activity will be evaluated;

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<sup>9</sup> See ASAE 3000, paragraph 24(b).

<sup>10</sup> See ASAE 3000, paragraph 27.

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- (f) The intended users of the assurance report;
- (g) The content of the assurance report, including whether it will be a short-form or long form report, including additional information such as the compliance requirements, procedures conducted, detailed findings and recommendations to meet the needs of the intended users; and (Ref: Para. A20)
- (h) Any other matters required by law or regulation (e.g. reporting all matters of non-compliance identified to the regulator<sup>11</sup>) to be included in the terms of engagement. (Ref: Para. 27)

#### ***Acceptance of a Change in the Terms of the Engagement***

26. If the engaging party requests a change in the terms of the engagement before the completion of the engagement, the assurance practitioner shall be satisfied that there is a reasonable justification for the change as required by ASAE 3000.<sup>12</sup> (Ref: Para. 0)

#### ***Assurance Report Prescribed by Law or Regulation***

27. If law or regulation prescribe the compliance requirements for evaluation or the form and content of the assurance report, the assurance practitioner evaluates the compliance requirements and form and content of the assurance report. If the compliance requirements are unsuitable or if intended users might misunderstand the assurance report, the assurance practitioner shall: (Ref: Para. A16, A53)
- (a) Not accept the engagement unless additional explanation in the assurance report mitigates these circumstances; or
  - (b) Not include any reference within the assurance report to the engagement having been conducted in accordance with ASAE 3000 or this ASAE, if required to accept the engagement by law or regulation.

#### **Quality Control**

28. The assurance practitioner shall implement quality control procedures as required by ASAE 3000.<sup>13</sup>

#### **Professional Scepticism, Professional Judgement and Assurance Skills and Techniques**

29. The assurance practitioner shall apply professional scepticism, exercise professional judgement and apply assurance skills and techniques in planning and performing an assurance engagement on compliance as required by ASAE 3000.<sup>14</sup> In applying professional scepticism, the assurance practitioner shall recognise the possibility that matters of non-compliance due to fraud could exist, notwithstanding the assurance practitioner's past experience of the honesty and integrity of the entity's management and those charged with governance.

#### **Planning and Performing the Engagement**

##### ***Planning***

30. The assurance practitioner shall plan the engagement so that it will be performed in an effective manner as required by ASAE 3000.<sup>15</sup> (Ref: Para. A22)

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<sup>11</sup> An example of where this would apply is the compliance component of an AFSL Licensee FS 71 engagement where the Australian Securities and Investments Commission (ASIC) require reporting of all breaches.

<sup>12</sup> See ASAE 3000, paragraph 29.

<sup>13</sup> See ASAE 3000, paragraphs 31-36.

<sup>14</sup> See ASAE 3000, paragraphs 37-39.

<sup>15</sup> See ASAE 3000, paragraph 40.

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*Materiality*

31. The assurance practitioner shall consider materiality, as required by ASAE 3000,<sup>16</sup> when determining the nature, timing and extent of procedures. (Ref: Para. A24-A29)

*Obtaining an Understanding of the Compliance Framework and Compliance Requirements*

Limited Assurance	Reasonable Assurance
<p>32L. The assurance practitioner shall obtain an understanding of the entity's compliance framework and its key elements, the compliance requirements which are included in the scope of the engagement, and other engagement circumstances, and on the basis of that understanding, the assurance practitioner shall: (Ref: Para. A30-A32)</p> <p>(a) For a direct engagement, consider whether the identification <del>or</del> selection <del>or development</del> of criteria is appropriate, <del>and/or select or develop further suitable criteria;</del></p> <p>(b) For both attestation and direct engagements:</p> <p>(i) Identify areas where the risks that may cause non-compliance with each of the compliance requirements to be concluded upon are likely to arise; and</p> <p>(ii) Respond to the risks identified in paragraph 32L(b)(i) and use as a basis for designing and performing assurance procedures.</p>	<p>32R. The assurance practitioner shall obtain an understanding of the entity's compliance framework and its key elements, the compliance requirements which are included in the scope of the engagement, and other engagement circumstances, and on the basis of that understanding, the assurance practitioner shall: (Ref: Para. A30-A32)</p> <p>(a) For a direct engagement, consider whether the identification <del>or</del> selection <del>or development</del> of criteria is appropriate, <del>and/or select or develop further suitable criteria;</del></p> <p>(b) For both attestation and direct engagements:</p> <p>(i) Identify and assess the risks that may cause non-compliance with each of the compliance requirements to be concluded upon; and</p> <p>(ii) Respond to the risks identified in paragraph 32R(b)(i) and use as a basis for designing and performing assurance procedures; and</p> <p>(c) Obtain an understanding of the relevant internal controls over the compliance activity to meet the compliance requirements, evaluate the design of those controls and determine whether they have been implemented.</p>

*Identifying Risks of Fraud*

33. When performing risk assessment procedures and related activities to obtain an understanding of the compliance framework and other engagement circumstances, the assurance practitioner shall obtain sufficient information for use in identifying the risks of the compliance requirements not being met due to fraud. (Ref: Para. A33-A34)

<sup>16</sup> See ASAE 3000, paragraph 44.

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*Obtaining an Understanding of the Internal Audit Function*

34. The assurance practitioner shall determine whether the entity has an internal audit function and, if so, makes further enquiries to obtain an understanding of the activities and main findings of the internal audit function with respect to the compliance engagement. (Ref: Para. A35)
35. The assurance practitioner shall consider based on the compliance engagement circumstances whether it is appropriate to use the work of the internal audit function.
36. If the assurance practitioner plans to use the work of the internal audit function in accordance with paragraph 37, the assurance practitioner shall evaluate it as required by ASAE 3000.<sup>17</sup>

*Using the Work of the Internal Audit Function*

37. If the assurance practitioner's evaluation of the internal audit function confirms that the work of the internal audit function can be used for purposes of the compliance engagement, then the assurance practitioner shall determine the planned effect of the work of the internal audit function on the nature, timing or extent of the assurance practitioner's procedures and in doing so, shall consider: (Ref: Para. A36, A43-A44)
- (a) The nature and scope of work performed, or to be performed, on the compliance framework by the internal audit function;
  - (b) The significance of that work to the assurance practitioner's conclusions;
  - (c) The degree of subjectivity involved in the evaluation of the evidence obtained in support of those conclusions; and
  - (d) Re-performing some of the work of the internal audit function that is planned to be used.
38. The use of internal auditors to provide direct assistance is prohibited in an assurance engagement conducted in accordance with this ASAE. Direct assistance is the performance of assurance procedures under the direction, supervision and review of the assurance practitioner.<sup>18</sup> This prohibition does not preclude reliance on the work of the internal audit function to modify the nature or timing, or reduce the extent, of assurance procedures to be performed directly by the assurance practitioner. (Ref: Para. A36)

**Obtaining Evidence**

39. Based on the assurance practitioner's understanding obtained under paragraph 32L and 32R, the assurance practitioner shall perform assurance procedures to respond to identified or assessed risks in paragraph 32L(b) to obtain limited or 32R(b) to obtain reasonable assurance to support the assurance practitioner's conclusion. (Ref: Para. A37-A39)
40. The assurance practitioner shall design and perform additional procedures, the nature, timing and extent of which are responsive to the risks of material deficiency in the compliance framework or matters of non-compliance with compliance requirements, having regard to the level of assurance required, reasonable or limited, as appropriate. (Ref: Para. A40)

*Responses to Assessed Risks of Fraud*

41. The assurance practitioner shall treat those assessed risks of compliance requirements not being met due to fraud as significant risks. Accordingly, the assurance practitioner shall design and perform procedures, on controls designed to mitigate such risks, and whose nature, timing and extent are responsive to those assessed risks. In doing this the assurance

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<sup>17</sup> See ASAE 3000, paragraph 55.

<sup>18</sup> See ASAE 3000, paragraphs 3 and Aus 20.1.

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practitioner shall have regard to the level of assurance required, reasonable or limited, as appropriate. (Ref: Para. A34)

*Obtaining Evidence Regarding the Compliance Activity*

42. When reporting on compliance throughout the specified period or as at a specified date, the assurance practitioner shall evaluate those compliance activities that the assurance practitioner has determined are necessary to meet the compliance requirements identified, and assess their compliance throughout the specified period or as at a specified date. (Ref: Para. A37)

Limited Assurance	Reasonable Assurance
<p>43L. The nature, timing and extent of evaluation of compliance activities, shall <del>ordinarily</del> be limited to:</p> <p>(a) <del>-</del>discussion <u>and enquiries</u> with entity personnel; <u>and</u></p> <p>(b) <del>-</del>observation of the activity in operation for compliance; <u>and</u></p> <p>(c) <del>-</del>walk-through for an appropriate number <del>of instances</del> of material compliance activities to identify any instances of non-compliance.</p> <p><del>-</del>Alternatively, the results of exception reporting, monitoring or other management controls may be examined to provide evidence about the operation of the compliance activity rather than directly testing it. <del>-</del>(Ref: Para. A37)</p>	<p>43R. The nature, timing and extent of testing and evaluation of compliance activities, shall <del>ordinarily</del> include:</p> <p>(a) <del>- in addition to</del> discussion <u>and enquiries</u> with entity personnel; <u>and</u></p> <p>(b) observation of the activity in operation for compliance; <u>and</u></p> <p>(c) <del>-</del>re-performance of a sample of compliance activities; <u>or</u></p> <p>(d) <del>-or</del> other examination and follow up of the application of compliance activities, on a test basis to provide sufficient appropriate evidence on which to base a conclusion.</p> <p>The results of exception reporting, monitoring or other management controls may be examined to reduce the extent of direct testing and evaluation of the operation of the compliance activity but shall not eliminate it entirely. (Ref: Para. A37)</p>
<p>44L. The assurance practitioner shall apply professional judgement in determining the specific nature, timing and extent of procedures to be conducted, which will depend on the assessed risks of material non-compliance with the compliance requirements. If the assurance practitioner determines that additional assurance procedures are required to dispel or confirm a suspicion that a material matter of non-compliance exists, the performance of such additional procedures shall not convert the engagement to a reasonable assurance engagement as they relate to the reduction of risk to an acceptable level with respect to that matter alone. (Ref: Para. A39-A40)</p>	<p>44R. The assurance practitioner shall apply professional judgement in determining the specific nature, timing and extent of procedures to be conducted, which will depend on the assessed risks of material non-compliance with the compliance requirements. (Ref: Para. A39)</p>

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Limited Assurance	Reasonable Assurance
	<p>45R. When determining the extent of testing and evaluation of compliance activities, the assurance practitioner shall consider matters including the characteristics of the population to be tested and evaluated, which includes the nature of the compliance activity, the frequency of their occurrence (for example, monthly, daily, a number of times per day), and the expected rate of matter(s) of non-compliance. Some compliance activities operate continuously, while others operate only at particular times, so the testing and evaluation of compliance shall be performed throughout the specified period of time that is sufficient to allow the practitioner to conclude. (Ref: Para. A40)</p>

**Sampling**

46. When the assurance practitioner uses sampling to test compliance, the assurance practitioner shall: (Ref: Para. 45R)
- (a) Consider the purpose of the procedure and the characteristics of the compliance activity from which the sample will be drawn when designing the sample;
  - (b) Determine a sample size sufficient to reduce sampling risk to an acceptably low level;
  - (c) Select items for the sample in such a way that each sampling unit in the population has a chance of selection and the sample is representative of the population; and
  - (d) If unable to apply the designed procedures, or suitable alternative procedures, to a selected item, treat that item as a deviation.

**Work Performed by an Assurance Practitioner's Expert**

47. When the assurance practitioner plans to use the work of an assurance practitioner's expert, the assurance practitioner shall comply with the requirements in ASAE 3000.<sup>19</sup> (Ref: Para. A41)

**Work Performed by Another Assurance Practitioner or a Responsible Party's or Evaluator's Expert**

48. If the assurance practitioner plans to use information prepared using the work of another assurance practitioner or a responsible party's or evaluator's expert, as evidence, the assurance practitioner shall comply with the requirements of ASAE 3000.<sup>20</sup> (Ref: Para. A42-A43)

**Evaluation of Evidence**

49. ASAE 3000<sup>21</sup> requires the assurance practitioner to accumulate uncorrected misstatements identified during the engagement other than those that are clearly trivial. **Misstatements in a**

<sup>19</sup> See ASAE 3000, paragraph 52.

<sup>20</sup> See ASAE 3000, paragraphs 53-54.

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~~compliance engagement are instances of non-compliance with the compliance requirements. Under this ASAE misstatements are only applicable in an attestation engagement on compliance. In a direct assurance engagement on compliance the assurance practitioner shall accumulate identified matters of non-compliance other than those that are clearly trivial.~~

50. Evaluation of evidence obtained by the assurance practitioner shall include any impact of corrected misstatements or non-compliance identified during the compliance engagement.
51. The assurance practitioner shall evaluate individually and in aggregate, whether the matter of non-compliance with the compliance requirements is material. (Ref: Para. A45)

**Written Representations**

52. The assurance practitioner shall request the responsible party, or other relevant person(s) within the entity to provide written representations, in addition to those required by ASAE 3000,<sup>22</sup> that the responsible party: (Ref: Para. A47)
- (a) In the case of an attestation engagement, reaffirms their Statement regarding the outcome of the responsible party's evaluation of the compliance activity against the compliance requirements throughout the specified period or as at a specified date;
  - (b) Acknowledges its responsibility for the compliance activity, including identifying the risks that threaten the compliance requirements being met, and designing, implementing and maintaining internal controls to mitigate those risks, including the risk of fraud, so that those risks will not prevent achievement of the compliance requirements;
  - (c) Has provided the assurance practitioner with all relevant information and access agreed to, as set out in paragraph 24(c)(i);
  - (d) Has disclosed to the assurance practitioner any of the following of which it is aware may be relevant to the engagement:
    - (i) Instances of non-compliance with the compliance requirements; or
    - (ii) Any events subsequent to the specified period or as at the specified date covered by the assurance practitioner's conclusion up to the date of the assurance report that could have a significant effect on the assurance practitioner's conclusion.

The assurance practitioner shall evaluate written representations in accordance with ASAE 3000. (Ref: Para. A48)

**Subsequent Events**

53. When relevant to the compliance engagement, the assurance practitioner shall consider the effect on the compliance outcome of events up to the date of the assurance report, and shall respond appropriately to facts that become known to the assurance practitioner after the date of the assurance conclusion, that had they been known to the assurance practitioner at that date, may have caused the assurance practitioner to amend the assurance conclusion. The extent of consideration of subsequent events depends on the potential for such events to impact the assurance practitioner's conclusion. The assurance practitioner has no responsibility to perform any procedures regarding the compliance outcome after the date of the assurance report. (Ref: Para. A50-A51)

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<sup>21</sup> See ASAE 3000, paragraph 51.

<sup>22</sup> See ASAE 3000, paragraph 56.

**Forming the Assurance Conclusion**

54. The assurance practitioner shall evaluate the sufficiency and appropriateness of the evidence obtained in the context of the engagement and, if necessary, attempt to obtain further evidence. If the assurance practitioner is unable to obtain necessary further evidence, the assurance practitioner shall consider the implications for the assurance practitioner's conclusion in accordance with ASAE 3000.<sup>23</sup> The assurance practitioner shall qualify their conclusion if the possible effects of undetected matters of non-compliance with the compliance requirements due to an inability to obtain sufficient appropriate evidence could be material, and shall disclaim their conclusion if the possible effects could be both material and pervasive.
55. When the assurance practitioner forms a conclusion in accordance with ASAE 3000,<sup>24</sup> the assurance practitioner shall evaluate the materiality, individually and in aggregate whether due to fraud or error, of any matter(s) of non-compliance with the compliance requirements. If the matters of non-compliance identified are: (Ref: Para. A45-A47)
- (a) Material but not pervasive, the assurance practitioner shall qualify their assurance conclusion with respect to the relevant matter; or
  - (b) Material and pervasive, the assurance practitioner shall issue an adverse conclusion.

**Preparing the Assurance Report**

56. The assurance practitioner shall prepare the assurance report in accordance with ASAE 3000<sup>25</sup> for attestation engagements and shall also apply those requirements for direct engagements.

*Assurance Report Content*

57. For both attestation and direct engagements, the assurance practitioner shall include in the assurance report the basic elements required by ASAE 3000,<sup>26</sup> which are at a minimum:
- (a) A title, indicating that it is an independent assurance report;
  - (b) An addressee;
  - (c) An identification of whether reasonable or limited assurance has been obtained by the assurance practitioner;
  - (d) Identification of the compliance requirements;
  - (e) Whether the assurance practitioner is reporting on compliance throughout the specified period or as at a specified date;
  - (f) In the case of an attestation engagement, reference to the responsible party's Statement as required by paragraph 24(a) and whether that Statement is available to intended users by accompanying the assurance report, reproduction in the assurance report or another identified source;
  - (g) Identification of the overall and/or specific criteria used for evaluating the compliance activity;
  - (h) If appropriate, a description of any significant inherent limitations associated with the evaluation of the compliance activity against the compliance requirements;

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<sup>23</sup> See ASAE 3000, paragraph 66.

<sup>24</sup> See ASAE 3000, paragraphs 64-65.

<sup>25</sup> See ASAE 3000, paragraphs 67-69.

<sup>26</sup> See ASAE 3000, paragraph 69.

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- (i) A statement that the responsible party or evaluator is responsible for:
  - (i) In an attestation engagement:
    - a. Providing a Statement with respect to the outcome of the evaluation of the compliance activity against the compliance requirements;
    - b. Identifying the compliance requirements (where not identified by Parliament, the Government, law or regulation, or another party, for example, a user group or a professional body); and
  - (ii) In both an attestation and a direct engagement:
    - a. The compliance activity covered by the assurance practitioner's report;
    - b. Identifying, designing and implementing controls to enable the compliance requirements to be met and to monitor ongoing compliance;
- (j) A statement that the assurance practitioner's responsibility is to express a conclusion on whether the compliance requirements have, in all material respects, been met;
- (k) A statement that the engagement was performed in accordance with ASAE 3100 *Compliance Engagements*;
- (l) A statement that the firm of which the assurance practitioner is a member applies ASQC 1;
- (m) A statement that the assurance practitioner complies with the independence and other relevant ethical requirements related to assurance engagements;
- (n) An informative summary of the work performed as a basis for the assurance practitioner's conclusion. In the case of a limited assurance engagement, an appreciation of the nature, timing, and extent of procedures performed is essential to understanding the assurance practitioner's conclusion. In a limited assurance engagement, the summary of the work performed shall state that: (Ref: Para. A54-A58)
  - (i) The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement; and
  - (ii) Consequently, the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed;
- (o) When the criteria used to evaluate the compliance requirements are available only to specific intended users, or are relevant only for a specific purpose, a statement restricting the use of the assurance report to those intended users or that purpose; (Ref: Para. A59)
- (p) Either, the assurance practitioner's opinion for a reasonable assurance engagement or the assurance practitioner's conclusion for a limited assurance engagement about whether, in all material respects the entity complied with the compliance requirements throughout the specified period or as at a specified date;
- (q) When the assurance practitioner expresses a modified conclusion, the assurance report shall contain:

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- (i) A section (entitled: Basis for Qualified/Adverse/Disclaimer of Conclusion/Opinion) that provides a description of the matter(s) giving rise to the modification; and
  - (ii) A section that contains the assurance practitioner's modified conclusion;
  - (r) The assurance practitioner's signature, the date of the assurance report and the location in the jurisdiction where the assurance practitioner practices.
58. If the assurance practitioner provides a long-form assurance report to meet the information needs of users, as agreed in the terms of engagement, or as required by law or regulation, the assurance practitioner's report shall include a separate section, or an attachment, containing any other information and explanations that are not intended to affect the assurance practitioner's conclusion and are clearly identified as such. (Ref: Para. A52)
59. If the assurance practitioner is required to conclude on other subject matters under different AUASB standards in conjunction with an engagement to report under this ASAE, the assurance report shall include a separate section for each subject matter in the assurance report, clearly differentiated by appropriate section headings.

*Emphasis of Matter and Other Matter Paragraphs*

60. The assurance practitioner shall include an Emphasis of Matter or Other Matter paragraph in the circumstances provided for in ASAE 3000<sup>27</sup> for an attestation engagement. In a direct engagement, if the assurance practitioner considers it necessary to communicate a matter that, in the assurance practitioner's judgement, is relevant to intended users' understanding of the engagement, the assurance practitioner's responsibilities or the assurance report, the assurance practitioner shall include in the assurance report an Other Matter paragraph, with an appropriate heading, that clearly indicates the assurance practitioner's conclusion is not modified in respect of the matter.

*Modified Conclusions*

61. If the assurance practitioner concludes that the compliance activity has not met the compliance requirements throughout the specified period or as at a specified date; or the assurance practitioner is unable to obtain sufficient appropriate evidence, the assurance practitioner's conclusion shall be modified, and the assurance practitioner's report shall include a section with a clear description of all the reasons for the modification. (Ref: Para. A60-A62)

*Scope Limitation*

62. When a scope limitation is imposed by the circumstances of the particular engagement, the assurance practitioner shall attempt to perform alternative procedures to overcome the limitation. When a scope limitation exists and remains unresolved, the wording of the assurance practitioner's conclusion shall indicate that it is qualified as to the effects of any instances of non-compliance with the compliance requirements, which might have been identified had the limitation not existed. If the effect of the unresolved scope limitation is both material and pervasive, the assurance practitioner shall express a disclaimer of conclusion. (Ref: Para. A63)

**Other Communication Responsibilities**

63. The assurance practitioner shall consider whether, pursuant to the terms of the engagement, if applicable, and other engagement circumstances, any matter has come to the attention of the assurance practitioner that is to be communicated with the responsible party, the evaluator, the engaging party, those charged with governance or others, as required by ASAE 3000.<sup>28</sup> If

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<sup>27</sup> See ASAE 3000, paragraph 73.

<sup>28</sup> See ASAE 3000, paragraph 78.

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during the course of the engagement the assurance practitioner identifies any matters of non-compliance with the entity's compliance requirements other than those which are clearly trivial, the assurance practitioner shall report to an appropriate level of management those matters of non-compliance or those charged with governance on a timely basis those matters of material non-compliance. (Ref: Para. A65)

64. In limited circumstances the assurance practitioner may be required by law or regulation and the terms of the engagement to report all instances of non-compliance with the compliance requirements to the regulator<sup>29</sup>.
65. If the assurance practitioner has identified a fraud or has obtained information that indicates that a fraud may exist, the assurance practitioner shall communicate these matters on a timely basis to the appropriate level of management or those charged with governance in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities. The assurance practitioner shall determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity. (Ref: Para. A64)
66. The assurance practitioner shall design engagement procedures to gather sufficient appropriate evidence to form a conclusion in accordance with the terms of the engagement. In the absence of a specific requirement in the terms of engagement the assurance practitioner does not have a responsibility to design procedures to identify matters outside the scope of the engagement that may be appropriate to report to management or those charged with governance.

**Documentation**

67. The assurance practitioner shall prepare documentation in accordance with ASAE 3000.<sup>30</sup> In documenting the nature, timing and extent of procedures performed as required by ASAE 3000, the assurance practitioner shall record (Ref: Para. A66):
  - (a) The identifying characteristics of the compliance activity being tested;
  - (b) Who performed the work and the date such work was completed; and
  - (c) Who reviewed the work performed and the date and extent of such review.
68. If the assurance practitioner uses specific work of the internal audit function, the assurance practitioner shall document the conclusions reached regarding the evaluation of the adequacy of the work of the internal audit function, and the procedures performed by the assurance practitioner on that work.

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<sup>29</sup> As an example where this would apply is the compliance component of an AFSL Licensee FS 71 engagement where ASIC require reporting of all breaches.

<sup>30</sup> See ASAE 3000, paragraphs 79-83.

## Application and Other Explanatory Material

### Application (Ref: Para. 1)

- A1. Engagements which are covered by this ASAE and those that are covered by other subject matter specific ASAEs have been further illustrated at Appendix 4.

### Introduction (Ref: Para. 3-14)

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- A2. The primary purpose of an assurance engagement is the conduct of assurance procedures to provide an assurance conclusion. However, the assurance practitioner is not precluded from providing recommendations for improvements to the compliance framework or compliance activities in conjunction with or as a result of conducting an assurance engagement to report on compliance.
- ~~A3. The risks, compliance requirements and related controls addressed in an engagement under this ASAE may relate to a broad range of subject matter relevant to the entity. The subject matter can be any activity of the entity, such as: compliance with legislation or regulation; contractual arrangements or policy and procedures.~~ Under a direct engagement, the ~~a~~Assurance ~~p~~Practitioner evaluates the compliance activity conducted by the responsible party to meet the compliance requirement.
- ~~A4.~~A3. Under an attestation engagement, the ~~r~~Responsible ~~p~~Party evaluates the compliance activity against the compliance requirements and provides a statement on the compliance outcome.
- ~~A5.~~A4. The primary practical difference for the assurance practitioner between an attestation and a direct engagement is the additional work effort for a direct engagement when planning the engagement and understanding the compliance framework and other engagement circumstances e.g. criteria to be applied. In a direct engagement the assurance practitioner selects, or is required to use, the criteria which address the purpose or overall objective of the compliance engagement. This difference affects the assurance practitioner's work effort in planning a direct engagement if the compliance requirements have not been identified or documented and in understanding the entity's compliance framework where a description is not available.
- ~~A6.~~A5. In a three party relationship, which is an element of an assurance engagement,<sup>31</sup> the responsible party may or may not be the engaging party, but is responsible for the compliance activities which are the underlying subject matter of the engagement and is a separate party from the intended users. The responsible party and the intended users may both be internal to the entity, for example if the responsible party is at an operational level of management and the intended users are at the level of those charged with governance, such as the Board or Audit Committee. See Appendix 1 for a discussion of how each of these roles relate to an assurance engagement on compliance.

### Ethical Requirements (Ref: Para. 19)

- ~~A7.~~A6. In accepting an assurance engagement on compliance, the assurance practitioner, in order to comply with relevant ethical requirements, considers whether the assurance practitioner has provided internal audit or consulting services with respect to the compliance framework or implementation of controls at the entity, as any such past or current engagements ~~may~~are likely to impact on the assurance practitioner's independence and are likely to preclude acceptance of the engagement.

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<sup>31</sup> See Framework for Assurance Engagements.

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#### Acceptance and Continuance

##### *Competence and Capabilities to Perform the Engagement*

- | ~~A8:~~A7. Relevant competence and capabilities to perform the compliance engagement, as required by ASAE 3000<sup>32</sup> by persons who are to perform the engagement, include matters such as the following:
- Knowledge of the relevant industry, compliance frameworks, the nature of the overall compliance requirements (for example: emissions quantification or regulatory compliance).
  - An understanding of controls, IT and systems.
  - Experience in evaluating risks as they relate to the compliance requirements.
  - Experience in the design and execution of tests of compliance and the evaluation of the results.

##### *Rational Purpose*

- | ~~A9:~~A8. When considering the acceptance of a limited assurance engagement on compliance, ASAE 3000 requires the assurance practitioner to determine whether a meaningful level of assurance is expected to be able to be obtained,<sup>33</sup> which may include whether a limited assurance engagement is likely to be meaningful to users. In making this assessment, the assurance practitioner considers the intended users of the assurance report and whether they are likely to understand the limitations of a limited assurance engagement, including the need to read the assurance report in detail to understand the assurance procedures performed and the assurance obtained.

##### *Assessing the Appropriateness of the Subject Matter (Ref: Para. 21)*

- | ~~A10:~~A9. An appropriate subject matter is:
- (a) Identifiable, and capable of consistent evaluation against the identified criteria; and
- | (b) ~~Able to~~ ~~Such that the information about it can~~ be subjected to procedures for gathering sufficient appropriate evidence to support a reasonable assurance or limited assurance conclusion, as appropriate.
- | ~~A11:~~A10. Examples of subject matters that may be appropriate for a compliance engagement include compliance with the following:
- General Insurers and Insurance Groups - Risk Management Strategy & Reinsurance Management Strategy (RMS/REMS).
  - Treasurer's Instructions.
  - Managed Investment Schemes – Compliance Plan.
  - Registered Superannuation Entity – SIS Act requirements (SPS 310).
  - Financial Services Licensee – Corporations Act 2001 requirements.

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<sup>32</sup> See ASAE 3000, paragraph 32.

<sup>33</sup> See ASAE 3000, paragraph 24(b)(vi).

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~~A12.~~A11. For further guidance on assessing the appropriateness of the subject matter refer to Appendix 3 and ASAE 3000<sup>34</sup>.

*Assessing the Suitability of the Criteria (Ref: Para. 23)*

~~A13.~~A12. Where the criteria are prescribed by legislation or regulation the criteria will ordinarily be deemed to be suitable for the purposes of the compliance engagement. In limited circumstances where this is not the case, the assurance practitioner needs to assess the suitability of the criteria.

~~A14.~~A13. In the context of a compliance engagement, examples of criteria include:

- Externally imposed criteria under law or directives, including:
  - Legislation.
  - Regulation.
  - Other statutory requirements (e.g. ASIC Regulatory Guides and Practice Notes or APRA Prudential Standards).
  - Ministerial directives.
  - Industry or professional obligations (professional standards or guidance, codes of practice or conduct).
  - Enforceable contractual obligations.
  - Enforceable undertakings.
- Internally imposed criteria, as determined by management, including:
  - Organisational policies and procedures.
  - Frameworks, for example, compliance framework based on ISO 19600 – Compliance Management Systems

~~A15.~~A14. Criteria need to be identified by the parties to the engagement and agreed by the engaging party and the assurance practitioner. The assurance practitioner may need to discuss the criteria to be used with those charged with governance, management and the intended users of the report. Criteria can be either established or specifically developed. The assurance practitioner normally concludes that established criteria embodied in laws or regulations or issued by professional bodies, associations or other recognised authorities that follow due process are suitable when the criteria are consistent with the objective. Other criteria may be agreed to by the intended users of the assurance practitioner's report, or a party entitled to act on their behalf, and may also be specifically developed for the engagement.

~~A16.~~A15. In situations where the criteria have been specifically developed for the engagement, ~~including where the assurance practitioner develops or assists in developing criteria,~~ the assurance practitioner obtains from the intended users or a party entitled to act on their behalf, acknowledgment that the specifically developed criteria are sufficient for the user's purposes. (Ref: Para. 23)

~~A17.~~ ~~The criteria may need to be amended during the engagement, if for example more information becomes available or the circumstances of the entity change. Any changes in the criteria are discussed with the engaging party and, if appropriate the intended users.~~

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<sup>34</sup> See ASAE 3000, paragraph 24(b)(i).

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### *Agreeing on the Terms of the Engagement (Ref: Para. 24-25)*

- ~~A18.~~A16. When agreeing whether the engagement is to be conducted as an attestation or direct engagement, the assurance practitioner considers factors such as whether:
- (a) There is a regulatory requirement or users need an evaluation of the compliance activity by the responsible party or evaluator (Ref: Para. 27); or
  - (b) The entity has the resources and expertise to prepare a suitable description or documentation of the compliance activity, compliance requirements and related controls and conduct a meaningful evaluation of the compliance outcome; ~~or~~
  - ~~(c) It is more cost effective for the entity to identify the specific compliance activities, requirements and related controls, evaluate the compliance outcome as the basis for an attestation engagement, rather than it being necessary for the assurance practitioner to do so in a direct engagement.~~
- ~~A19.~~A17. The assurance practitioner considers the needs of users and the period in which the compliance activity has been in place in agreeing the specified date or the specified period to be covered by the assurance engagement, so that the report is not likely to be misleading.
- ~~A20.~~A18. If the criteria are available when agreeing the terms of engagement, they may be listed or attached to the engagement letter or other written terms.
- A19. Where relevant, the terms of the engagement could also include a reference to, and description of, the auditor's responsibility ~~to~~, in accordance with:
- ~~the~~ applicable law;
  - ~~the~~ regulation or relevant ethical requirements, and
  - obligations to determine whether, reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is required or appropriate in the circumstances.
- ~~A21.~~A20. When agreeing whether the report will be in long-form, including matters such as evaluation of compliance procedures and detailed findings, the assurance practitioner considers both the needs of users and the risks of users misunderstanding the context of the procedures conducted or the findings reported. Reporting evaluation of compliance procedures and findings may be appropriate where the users are knowledgeable with respect to assurance and the compliance requirements and, therefore, not likely to misinterpret those findings.
- ~~A22.~~A21. An example engagement letter (s) is contained in Appendix 5.

### **Planning and Performing the Engagement**

#### *Planning (Ref: Para. 30)*

- ~~A23.~~A22. The nature and extent of planning activities will vary with the compliance engagement circumstances, for example the size and complexity of the compliance activity and requirements, the assurance practitioner's previous experience with this area and the entity as a whole. Examples of the main matters to be considered when developing the engagement plan include:
- (a) Matters affecting the industry in which the entity operates, for example economic conditions, laws and regulations, and technology;

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- (b) Risks to which the entity is exposed that are relevant to the compliance activity being examined;
- (c) The quality of the control environment within the entity and the role of the governing body, audit committee and internal audit function;
- (d) Knowledge of the entity's internal control structure obtained during other engagements;
- (e) The extent of recent changes if any, in the entity, its operations or its compliance framework;
- (f) Methods adopted by management to evaluate the effectiveness of the compliance framework;
- (g) Preliminary judgements about significant risk;
- (h) The nature and extent of evidence likely to be available;
- (i) The nature of control procedures relevant to the compliance activity and their relationship to the compliance framework taken as a whole;
- (j) The assurance practitioner's preliminary judgement about the effectiveness of the compliance framework taken as a whole and of the control procedures within the framework;
- (k) The terms of the compliance engagement;
- (l) The characteristics of the compliance activity and the identified criteria;
- (m) Identification of intended users and their needs, and consideration of materiality and the components of compliance engagement risk; and
- (n) Personnel and expertise requirements, including the nature and extent of involvement by experts.

| ~~A24.~~A23. The assurance practitioner may decide to discuss elements of planning with management or other appropriate party when determining the scope of the engagement or to facilitate the conduct and management of the engagement (for example, to co-ordinate some of the planned procedures with the work of the entity's personnel). Although these discussions often occur, the overall engagement strategy and the engagement plan remain the assurance practitioner's responsibility. When discussing matters included in the overall engagement strategy or engagement plan, care is required in order not to compromise the effectiveness of the engagement. For example, discussing the nature and timing of detailed procedures with the entity may compromise the effectiveness of the engagement by making the procedures too predictable.

*Materiality (Ref: Para.31)*

| ~~A25.~~A24. The assurance practitioner applies the same considerations in both limited and reasonable assurance engagements regarding what represents a material compliance requirement, since such judgements are not affected by the level of assurance being obtained.

| ~~A26.~~A25. The assurance practitioner considers materiality of the compliance requirements at the planning stage, reassesses materiality during the engagement based on the findings, and considers the materiality of any identified deficiencies in the compliance framework and/or non-compliance with compliance requirements.

| ~~A27.~~A26. The assurance practitioner considers materiality when determining the nature, timing and extent of evidence-gathering procedures, and when evaluating whether a matter of

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non-compliance is material. In considering materiality, the assurance practitioner understands and assesses what factors might influence the decisions of the intended users.

~~A28:~~A27. The assurance practitioner shall also consider materiality when evaluating the effect of accumulated deficiencies in the compliance framework or matters of non-compliance with the compliance requirements. Material deficiencies or matters of non-compliance are those which could significantly impact the compliance requirements being met and reasonably be expected to influence relevant decisions of the intended users.

~~A29:~~A28. The assurance practitioner considers materiality in the context of quantitative and qualitative factors, such as relative magnitude of instances of detected or suspected matter(s) of non-compliance, the nature and extent of the effect of these factors on the evaluation of compliance with the compliance requirements, and the interests of the intended users. The assessment of materiality and the relative importance of quantitative and qualitative factors in a particular engagement are matters for the assurance practitioner's professional judgement, taking into account specific regulatory reporting requirements.

~~A30:~~A29. Quantitative and qualitative factors which the assurance practitioner may considers when assessing materiality include:

- The magnitude of the instances of detected or suspected matter(s) of non-compliance with the compliance requirements.
- The financial impact of the matter(s) of non-compliance on the entity as a whole.
- The nature of the matter(s) of non-compliance – one off or systemic.
- Evidence of a robust compliance framework in place to detect, rectify and report matter(s) of non-compliance.
- Commonly accepted practices within the relevant industry.
- The nature of relevant transactions, whether they involve high volumes, large dollar values and complex transactions relative to the compliance activity as a whole.
- The extent of interest shown in particular aspects of the compliance activity by, for example, governing body, regulatory authorities and agencies or the public.

#### *Obtaining an Understanding of the Compliance Framework and Compliance Requirements* (Ref: Para. 32)

~~A31:~~A30. The assurance practitioner's understanding of the compliance framework and compliance requirements, ordinarily, has a lesser depth for a limited assurance engagement than for a reasonable assurance engagement. The assurance practitioner's procedures to obtain this understanding may include:

- Review and understand the relevant compliance requirements.
- Enquiring of those within the entity who, in the assurance practitioner's judgement, may have relevant information.
- Observing operations.
- Inspecting documents, reports, printed and electronic records.
- Re-performing compliance procedures.

~~A32:~~A31. The nature and extent of procedures to gain this understanding are a matter for the assurance practitioner's professional judgement and will depend on factors such as:

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- (a) The entity's size and complexity;
- (b) The nature of the activity to be examined, including the compliance requirement(s) to which the compliance procedures are directed and the risk that those compliance requirements will not be met;
- (c) The extent to which IT is used; and
- (d) The documentation available.

~~A33.~~A32. The nature and extent of planning and subsequent evidence-gathering procedures will vary with the engagement circumstances, and the maturity of the entity's compliance framework.

Elements of an entity's compliance framework ordinarily include the following:

- Procedures for identifying and updating compliance requirements.
- Staff training and awareness programs.
- Procedures for assessing the impact of compliance ~~requirements~~obligations on the entity's key business activities.
- Controls embedded within key business processes designed to ensure compliance with ~~requirements~~obligations.
- Processes to identify and monitor the implementation of further mitigating actions required to ensure that compliance ~~requirements~~obligations are met.
- A monitoring plan to test key compliance controls on a periodic basis and report exceptions.
- Procedures for identifying, assessing, rectifying and reporting matters of non-compliance.
- Periodic sign off by management and/or external third party outsourced service providers<sup>35</sup> as to compliance with ~~requirements~~obligations.
- A compliance governance structure that establishes responsibility for the oversight of compliance control activities with those charged with governance, typically a Board Audit, Risk Management or Compliance Committee.

*Identifying Risks of Fraud (Ref: Para. 33,41)*

~~A34.~~A33. Management is in a unique position to perpetrate fraud because of their ability to manipulate the entity's records or prepare fraudulent reports by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk that compliance requirements will not be met due to fraud and thus is a significant risk.

~~A35.~~A34. The assurance practitioner may consider undertaking the following procedures to obtain sufficient appropriate evidence of the risk of fraud in relation to the compliance requirements:

- (a) Make enquiries of management with respect to compliance regarding:

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<sup>35</sup> Refer to *ASA 402 Audit Considerations Relating to an Entity Using a Service Organisation* and *GS013 Special Considerations in the Audit of Compliance Plans of Managed Investment Schemes* paragraphs 36 and 37 for further guidance.

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- (i) Management's assessment of the risk that controls may be circumvented due to fraud, including the nature, extent and frequency of such assessment;
  - (ii) Management's process for identifying and responding to the risks of fraud;
  - (iii) Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud; and
  - (iv) Management's communication, if any, to employees regarding its views on corrupt or fraudulent business practices and unethical behaviour;
- (b) Make enquiries of those charged with governance, management, and others within the entity as appropriate, to determine whether they have knowledge of any actual, suspected or alleged fraud with respect to compliance affecting the entity;
- (c) Make enquiries of the internal audit function, where it exists, to determine whether it has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risks of fraud;
- ~~(d)~~(c) Obtain an understanding of how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal controls that management has established to mitigate these risks as far as they relate to the compliance requirements;
- ~~(e)~~(d) Consider whether other information obtained by the assurance practitioner indicates risks of compliance requirements not being met due to fraud, for which mitigating controls are necessary;
- ~~(f)~~(e) Evaluate whether the information obtained from the other risk assessment procedures and related activities performed indicates that one or more fraud risk factors are present; and
- ~~(g)~~(f) Identify controls over matters for which decisions or actions are not routine, such as adjustments to records, development of estimates and activities outside the normal course of business.

*Obtaining an Understanding of the Internal Audit Function* (Ref: Para. 34-38)

- ~~A36~~A35. In obtaining an understanding of the compliance framework, including controls, the assurance practitioner determines whether the entity has an internal audit function and its effect on the controls within the compliance framework. The internal audit function ordinarily forms part of the entity's internal control and governance structures. The responsibilities of the internal audit function may include, for example, monitoring of internal control, risk management, and review of compliance with laws and regulations, and is considered as part of the assurance practitioner's assessment of risk.
- ~~A37~~A36. An effective internal audit function may enable the assurance practitioner to modify the nature and/or timing, and/or reduce the extent of assurance procedures performed, but cannot eliminate them entirely.

**Obtaining Evidence** (Ref: Para. 42-46)

- A37. Compliance engagements require the application of assurance skills and techniques to gather sufficient appropriate evidence as part of an iterative, systematic assurance engagement process. As the assurance practitioner performs planned procedures, the evidence obtained may differ significantly from that on which the planned procedures were based and cause the assurance practitioner to perform additional procedures.

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- A38. ~~When compliance requirements apply throughout a specified period, the assurance practitioner considers the extent of evaluation and/or testing required, and considers the nature and frequency of the compliance activities undertaken, so that sufficient and appropriate evidence is obtained. Sufficient appropriate evidence about compliance during the current period is required for the assurance practitioner to provide a conclusion. Knowledge of non-compliance observed in prior periods may, however, lead the assurance practitioner to increase the extent of evaluation and/or testing during the current period. In the case of an attestation engagement, such procedures may include asking the responsible party to examine the matter identified by the assurance practitioner, and to make amendments to the description or Statement, if appropriate.~~
- A39. The assurance practitioner may become aware of a matter(s) that causes the assurance practitioner to believe that there are deficiencies in the compliance framework or the compliance activity is not compliant with the compliance requirements. In such cases, the assurance practitioner may investigate such differences by, for example, inquiring of the appropriate party(ies) or performing other procedures as appropriate in the circumstances.

**Limited and Reasonable Assurance Engagements (Ref: Para. 43)**

- A40. The level of assurance obtained in a limited assurance engagement is lower than in a reasonable assurance engagement, therefore the procedures the assurance practitioner performs in a limited assurance engagement are different in nature and timing from, and are less in extent than for, a reasonable assurance engagement. The primary differences between the assurance practitioner's overall responses to assessed risks and further procedures conducted in a reasonable assurance engagement and a limited assurance engagement on compliance include:
- (a) The emphasis placed on the nature of various procedures as a source of evidence will likely differ, depending on the engagement circumstances. For example, the assurance practitioner may judge it to be appropriate in the circumstances of a particular limited assurance engagement to place relatively greater emphasis on indirect evaluation of compliance activities, such as enquiries of the entity's personnel, and relatively less emphasis, on evaluation of compliance activities, such as observation, re-performance or inspection, than may be the case for a reasonable assurance engagement.
  - (b) In a limited assurance engagement, the further procedures performed are less in extent than in a reasonable assurance engagement in that those procedures may involve:
    - (i) Selecting fewer items for examination;
    - (ii) Performing fewer types of procedures; or
    - (iii) Performing procedures at fewer locations.

**Work Performed by an Assurance Practitioner's Expert (Ref: Para. 47)**

- A41. ASAE 3000<sup>36</sup> provides application material for the circumstances where an assurance practitioner's expert is involved in the engagement. This material may also be used as guidance when using the work of another assurance practitioner or a responsible party's or evaluator's expert.

**Work Performed by Another Assurance Practitioner or a Responsible Party's or Evaluator's Expert (Ref: Para. 48)**

- A42. When information on compliance activities to be used as evidence has been prepared using the work of a responsible party's or evaluator's expert, the nature, timing and extent of procedures

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<sup>36</sup> See ASAE 3000, paragraphs A120-A134.

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with respect to the work of the responsible party's or evaluator's expert may be affected by such matters as:

- (a) The nature and complexity of the compliance activity to which the expert's work relates;
- (b) The risks of a material deficiency in the compliance framework or non-compliance with the compliance requirements throughout the specified period or as at a specified date;
- (c) The availability of alternative sources of evidence or mitigating controls;
- (d) The nature, scope and objectives of the expert's work;
- (e) Whether the expert is employed by the entity, or is a party engaged by it to provide relevant services;
- (f) The extent to which the responsible party or evaluator can exercise control or influence over the work of the expert;
- (g) Whether the expert is subject to technical performance standards or other professional or industry requirements;
- (h) The nature and extent of any controls within the entity over the expert's work;
- (i) The assurance practitioner's knowledge and experience of the expert's field of expertise; and
- (j) The assurance practitioner's previous experience of the work of that expert.

*Work Performed by the Internal Audit Function (Ref: Para. 34-38)*

A43. The nature, timing and extent of the assurance practitioner's procedures on specific work of the internal auditors will depend on the assurance practitioner's assessment of the significance of that work to the assurance practitioner's conclusions, the evaluation of the internal audit function and the evaluation of the specific work of the internal auditors. Such procedures may include:

- (a) Examination of evidence of the operation of the compliance activity already examined by the internal auditors;
- (b) Examination of evidence of the operation of other instances of the same compliance activity;
- (c) Examination of the outcomes of monitoring of controls by internal auditors; and
- (d) Observation of procedures performed by the internal auditors.

A44. Irrespective of the degree of autonomy and objectivity of the internal audit function, such a function is not independent of the entity as is required of the assurance practitioner when performing the compliance engagement. The assurance practitioner has sole responsibility for the conclusion expressed in the assurance report, and that responsibility is not reduced by the assurance practitioner's use of the work of the internal auditors.

**Evaluation of Evidence**

- | A45. In evaluating any matter(s) of non-compliance (corrected or un-corrected) with the compliance requirements the assurance practitioner considers materiality as specified in the terms of the engagement where relevant, any relevant legislative, regulatory or other (e.g. contractual) requirements which may apply and the effect on the decisions of the intended users of the

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assurance report and the assurance practitioner's conclusion. (Ref: Para. 49-51 ~~Error! Reference source not found.~~)

~~A46.~~ In evaluating the overall evidence obtained during the compliance engagement, includes both corrected or un-corrected misstatements or matters of non-compliance identified. The extent of corrected misstatements or matters of non-compliance may lead the assurance practitioner to conclude that compliance with the compliance requirements have not been met. The assurance practitioner applies their professional judgement in determining if any additional procedures are required to be performed under paragraph 44L or 44R to assist in forming their conclusion.

~~A45.~~ —

~~A46.~~~~A47.~~ For both reasonable and limited assurance engagements, if the assurance practitioner becomes aware of a matter that leads the assurance practitioner to question whether a material matter of non-compliance exists, the assurance practitioner would ordinarily pursue the matter by performing other evidence gathering procedures sufficient to enable the assurance practitioner to form a conclusion. (Ref: Para. 44) ~~44~~

#### Written Representations (Ref: Para. 52)

~~A47.~~~~A48.~~ For application material on using written representations refer to ASAE 3000.<sup>37</sup>

~~A48.~~~~A49.~~ The person(s) from whom the assurance practitioner requests written representations will ordinarily be a member of senior management or those charged with governance. However, because management and governance structures vary by entity, reflecting influences such as different cultural and legal backgrounds, and size and ownership characteristics, it is not possible for this ASAE to specify for all engagements the appropriate person(s) from whom to request written representations. The process to identify the appropriate person(s) from whom to request written representations requires the exercise of professional judgement.

#### Subsequent Events (Ref: Para 53)

~~A49.~~~~A50.~~ Assurance procedures with respect to the identification of subsequent events after period end are limited to examination of relevant reports, for example reports on compliance procedures, minutes of relevant committees and enquiry of management or other personnel as to significant matter(s) of non-compliance with compliance requirements.

~~A50.~~~~A51.~~ The assurance practitioner does not have any responsibility to perform procedures or make any enquiry after the date of the report. If however, after the date of the report, the assurance practitioner becomes aware of a matter identified, the assurance practitioner considers re-issuing the report. In an attestation engagement where the report has already been issued, the new report includes an Emphasis of Matter discussing the reason for the new report. In a direct engagement, the new report discusses the reason for the new report under a heading "Subsequent Events".

#### Preparing the Assurance Report (Ref: Para. 56-59)

##### *Assurance Report Content*

~~A51.~~~~A52.~~ The assurance practitioner may expand the report to include other information not intended as a qualification of the assurance practitioner's conclusion. If the report includes other information it is a long-form report as the information is additional to the basic elements required in paragraph 58 for a short-form report. This additional information may be required by regulation or agreed in the terms of the engagement to meet the needs of users. When considering whether to include any such information the assurance practitioner assesses the materiality of that information in the context of the objectives of the engagement. Other

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<sup>37</sup> See ASAE 3000, paragraphs A136-A139.

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information is not to be worded in such a manner that it may be regarded as a qualification of the assurance practitioner's conclusion and may include for example:

- Relevant background information and historical context.
- The assurance approach.
- Underlying facts and criteria applied.
- Disclosure of materiality levels.
- Findings relating to particular aspects of the compliance engagement.
- Analysis of the causes of non-compliance with the compliance requirements.
- Recommendations for improvements to address identified compliance framework deficiencies.

| ~~A52:~~A53. In some circumstances, the form and/or content of the assurance report is prescribed by law or regulation. In such cases, the assurance practitioner compares the prescribed report with the reporting requirements under this ASAE to ensure the minimum basic elements have been met. (Ref: Para. 27)

*Summary of the Work Performed (Ref: Para 57(n))*

| ~~A53:~~A54. The summary of the work performed helps the intended users understand the nature of the assurance conveyed by the assurance report. For many assurance engagements, infinite variations in procedures are possible in theory. It may be appropriate to include in the summary a statement that the work performed included evaluating the suitability of the criteria and the compliance requirements and the risks that threaten those compliance requirements not being met. ASAE 3000 provides application material on reporting on the applicable criteria.

| ~~A54:~~A55. In a limited assurance engagement an appreciation of the nature, timing, and extent of procedures performed is essential to understanding the assurance conveyed by the conclusion, therefore the summary of the work performed is ordinarily more detailed than for a reasonable assurance engagement and identifies the limitations on the nature, timing, and extent of procedures. It also may be appropriate to indicate certain procedures that were not performed that would ordinarily be performed in a reasonable assurance engagement. However, a complete identification of all such procedures may not be possible because the assurance practitioner's required understanding and consideration of engagement risk is less than in a reasonable assurance engagement.

| ~~A55:~~A56. Factors to consider in determining the level of detail to be provided in the summary of the work performed include:

- (a) Circumstances specific to the entity (e.g. the maturity of the entity's compliance framework compared to those typical in the industry sector);
- (b) Specific engagement circumstances affecting the nature and extent of the procedures performed; and
- (c) The intended users' expectations of the level of detail to be provided in the report, based on market practice, or applicable law or regulation.

| ~~A56:~~A57. It is important that the summary be written in an objective way that allows intended users to understand the work done as the basis for the assurance practitioner's conclusion. In most cases this will not involve relating the entire work plan, but on the other hand it is important for it not to be so summarised as to be ambiguous, nor written in a way that is overstated or embellished.

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~~A57-A58.~~ Illustrative examples of assurance practitioner's reports are contained in Appendix 6.

*Intended Users and Specific Purpose of the Assurance Report (Ref: Para. 57(o))*

~~A58-A59.~~ If the assurance practitioner's report on compliance has been prepared for a specific purpose and is only relevant to the intended users, this is stated in the assurance practitioner's report. In addition, the assurance practitioner may consider it appropriate to include wording that specifically restricts distribution of the assurance report other than to intended users, its use by others, or its use for other purposes.

*Modified Conclusions (Ref: Para. 61-62)*

~~A59-A60.~~ Modifications to the assurance report may be made in the following circumstances:

- (a) A qualified conclusion may be issued if the following matters are material but not pervasive:
  - (i) Unsuitable criteria mandated by legislation or regulation where the assurance practitioner is unable to resign from the engagement;
  - (ii) Scope limitation;
  - (iii) Non-compliance with the compliance requirements;
  - (iv) Misstatement in the Statement;
- (b) An adverse conclusion may be issued if the following matters are both material and pervasive:
  - (i) Unsuitable criteria mandated by legislation or regulation where the assurance practitioner is unable to resign from the engagement;
  - (ii) Non-compliance with the compliance requirements;
  - ~~(iii) Systemic deficiency in the compliance framework;~~
  - ~~(iv)~~ (iii) Misstatement in the Statement;
- (c) A disclaimer may be issued if there is a limitation of scope which is both material and pervasive.

~~A60-A61.~~ Illustrative examples of elements of modified assurance practitioner's reports are contained in Appendix 7.

~~A61-A62.~~ Even if the assurance practitioner has expressed an adverse conclusion or a disclaimer of conclusion, it may be appropriate to describe in the basis for modification paragraph the reasons for any other matters of which the assurance practitioner is aware that would have required a modification to the conclusion, and the effects thereof.

~~A62-A63.~~ When expressing a disclaimer of conclusion, because of a scope limitation, it is not ordinarily appropriate to identify the procedures that were performed nor include statements describing the characteristics of the assurance practitioner's engagement; to do so might overshadow the disclaimer of conclusion.

**Other Communication Responsibilities (Ref: Para. 63-66)**

~~A63-A64.~~ Appropriate actions to respond to the circumstances identified in paragraph 65 may include:

- Obtaining legal advice about the consequences of different courses of action.

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- Communicating with those charged with governance of the entity.
- Communicating with third parties (for example, a regulator) when required to do so.
- Modifying the assurance practitioner's conclusion, or adding an Other Matter paragraph.
- Withdrawing from the engagement.

| ~~A64.~~A65. Certain matters identified during the course of the engagement may be of such importance that they would be communicated to those charged with governance. Unless stated otherwise in the terms of engagement, less important matters would be reported to a level of management that has the authority to take appropriate action.

**Documentation (Ref: Para. 67-68)**

| ~~A65.~~A66. For application material on preparing and maintaining documentation refer ASAE 3000.<sup>38</sup>

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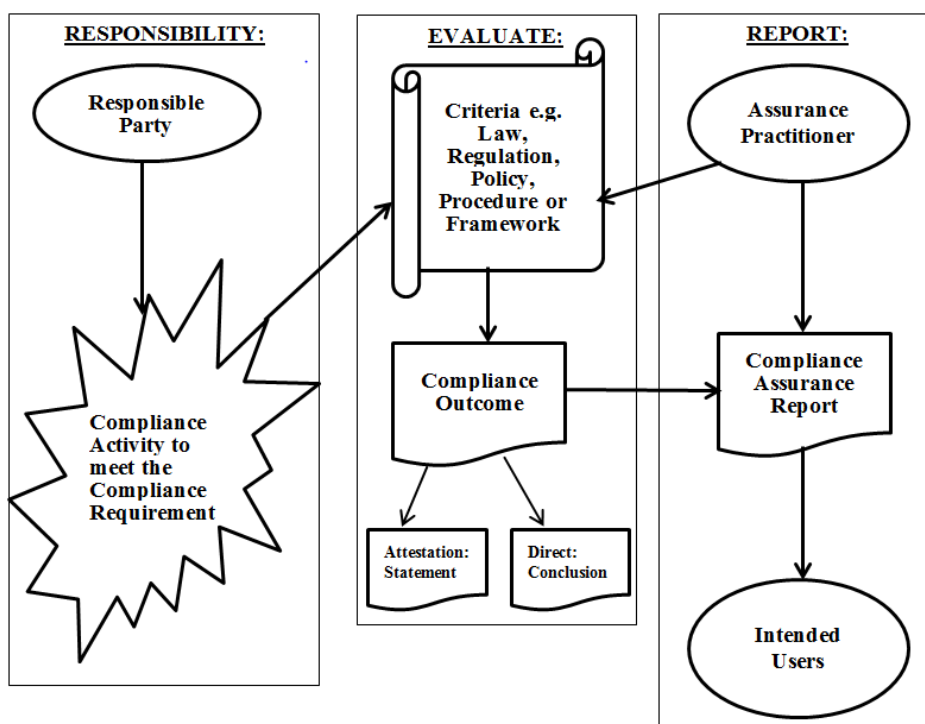
| <sup>38</sup> See ASAE 3000, paragraphs A193-A200.

## Appendix 1

(Ref: Para. A5)

### ROLES AND RESPONSIBILITIES – DIRECT AND ATTESTATION COMPLIANCE ENGAGEMENTS

The diagram below illustrates the relationships in a direct and attestation compliance engagement conducted by an Assurance Practitioner.



Under a direct engagement, the Assurance Practitioner evaluates the compliance activity conducted by the responsible party to meet the compliance requirement.

Under an attestation engagement, the Responsible Party evaluates the compliance activity against the compliance requirements and provides a statement on the compliance outcome.

In both attestation and direct engagements the Assurance Practitioner evaluates the compliance activity against the compliance requirement(s) using the criteria, and obtains assurance on which to base their -assurance conclusion. The compliance assurance report is provided to the intended users.

## Appendix 2

(Ref: Para. 9)

### TERMINOLOGY TABLE - ASAE 3000 AND ASAE 3100

Terminology as applied in ASAEs	ASAE 3000	ASAE 3100
<b>Objective <del>(a)</del></b>	To obtain either reasonable assurance or limited assurance, as appropriate, about whether the subject matter information is free from material misstatement.....;	To obtain reasonable or limited assurance, about whether the entity has complied in all material respects, with compliance requirements as evaluated by the suitable criteria.
<b>Criteria</b>	The benchmarks used to measure or evaluate the underlying subject matter. The “applicable criteria” are the criteria used for the particular engagement.	The benchmark, framework or legislation used to evaluate whether the compliance requirements have been met. The “applicable criteria” are the criteria used for the particular engagement.
<b>Compliance Requirement(s)</b>	No equivalent term.	The specific requirements established in law, regulations, other statutory requirements (e.g. ASIC Class Orders and Regulatory Guides and APRA Prudential Standards), contractual arrangements, ministerial directives, industry or professional obligations or internally via company policies, procedures and frameworks.
<b>Subject Matter Information <del>vs</del> <del>Compliance Outcome</del></b>	The outcome of the measurement or evaluation of the underlying subject matter against the criteria, i.e., the information that results from applying the criteria to the underlying subject matter.	<b><u>Compliance Outcome:</u></b> The outcome of the evaluation of the compliance activity (underlying subject matter) against the compliance requirements, using the criteria. The compliance outcome is the Statement of the responsible party or evaluator in an attestation compliance engagement, or the assurance practitioner’s conclusion in a direct compliance engagement, providing the outcome of their evaluation.
<b>Underlying Subject Matter <del>vs</del> <del>Compliance Activity</del></b>	The phenomenon that is measured or evaluated by applying criteria.	<b><u>Compliance Activity:</u></b> The activity that is undertaken to meet the

Standard on Assurance Engagements ASAE 3100  
*Compliance Engagements*

Terminology as applied in ASAEs	ASAE 3000	ASAE 3100
		compliance requirement(s)

## EXAMPLES: NATURE OF ASSURANCE ENGAGEMENTS ON COMPLIANCE

### Scope of the Engagement

Example scopes of assurance engagements which may be conducted with respect to compliance is set out in the following table:

Scope of Engagement	Compliance Requirement	Criteria for Evaluating Compliance Activity	Subject Matter / Compliance Activity	Compliance Outcome of the Evaluation (Subject Matter Information)	Assurance Conclusion
Compliance of the Real Estate Trust with the requirements of s407 of the <i>Property Agents and Motor dealers Act 2000</i> (the “Act”)	<i>s407 of the Property Agents and Motor Dealers Act 2000</i>	Applicable criteria as specified under s407 of the Act. As an example: maintenance and controls over the Trustee Bank Account.	Trustee Account procedures: Trustee Bank Account and cash book procedures.	Evaluator’s Statement or assurance practitioner’s conclusion whether the Trust has complied in all material respects with s407 of the Act.	Reasonable Assurance – complied in all material respects with s407 of the Act.
Compliance of the Registered Superannuation Entity (RSE) with the applicable provisions of the <i>Superannuation Industry (Supervision) Act 1993</i> (SIS Act), <i>Superannuation Industry (Supervision) Regulations</i> , FSCODA Reporting Standards, <i>Corporations Act 2001</i> (Corporations Act) and <i>Corporations Regulation 2001</i> (Corporation Regulations)	Applicable sections of: SIS Act; SIS Regulations; Corporations Act; Corporation Regulations; FSCODA Reporting Standards; and Conditions C1, C5 <sup>39</sup> , E1, F1 and G1 imposed under s29EA of the SIS Act.	Example: Conditions imposed under C5 <sup>34</sup> of SIS Act: <ul style="list-style-type: none"> <li>all assets of RSE, including all bank accounts are ‘custodially held’ as defined in trustee’s RSE licence</li> </ul>	As an example: RSE procedures and controls covering: <ul style="list-style-type: none"> <li>bank accounts</li> <li>other assets</li> </ul>	Evaluator’s Statement or assurance practitioner’s conclusion whether the RSE has complied in all material respects with the requirements of the applicable SIS Act, SIS Regulations, FSCODA Reporting Standards, Corporations Act and Corporations Regulations, conditions imposed under s29EA of the SIS Act.	Reasonable Assurance – complied in all material respects with Condition C5 imposed under s 29EA of the SIS Act.....and the applicable provisions of the SIS Act, SIS Regulations, FSCODA Reporting Standards, Corporations Act and Corporations Regulations, other conditions imposed under s29EA of the SIS Act.

<sup>39</sup> Condition C5 under s29EA of the SIS Act has been selected as one example of a compliance requirement.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

Scope of Engagement	Compliance Requirement	Criteria for Evaluating Compliance Activity	Subject Matter / Compliance Activity	Compliance Outcome of the Evaluation (Subject Matter Information)	Assurance Conclusion
Compliance of a General Insurer or Insurance Group with the requirements of Prudential Standard GPS 220 <i>Risk Management</i> to maintain a Risk Management Strategy (RMS) and Prudential Standard GPS 230 <i>Reinsurance Management</i> to maintain a Reinsurance Management Strategy (REMS)	GPS 220 <i>Risk Management</i> (RMS) and GPS 230 <i>Reinsurance Management</i> (REMS)	Applicable criteria as specified in GPS 220 and GPS 230. Example: GPS 220 <ul style="list-style-type: none"> <li>General Insurer must have a documented Risk Management Strategy (RMS) which includes specified elements</li> </ul>	General Insurers or Insurance Groups maintenance of an RMS and a REMS.	Evaluator's Statement or assurance practitioner's conclusion whether the General Insurer or Insurance Group has complied in all material respects with its RMS and REMS.	Limited Assurance – nothing has come to our attention that causes us to believe that [throughout the specified period] the General Insurer or Insurance Group did not comply in all material respects with its RMS and REMS.
<u>Compliance of an entity with the requirements of a Bank Covenant agreement.</u>	<u>Bank Covenant Agreement</u> <sup>40</sup>	<u>Applicable criteria as specified in the Bank Covenant agreement.</u> Example: Maintaining specified ratio's of liquid assets to liabilities at a point in time.	<u>Procedures and monitoring controls:</u> <ul style="list-style-type: none"> <li><u>bank accounts</u></li> <li><u>other liquid assets</u></li> <li><u>liabilities</u></li> </ul>	Evaluator's Statement or assurance practitioner's conclusion whether the <u>entity</u> has complied in all material respects with the <u>Bank Covenant Agreement</u> .	<u>Reasonable Assurance – complied in all material respects with the Bank Covenant Agreement.</u>

<sup>40</sup> This example is where the Bank Covenants are based on Historical Financial Information.

STANDARDS APPLICABLE TO EXAMPLE ENGAGEMENTS ON COMPLIANCE

		APPLICABLE AUASB STANDARDS				
		ASAE 3000 Assurance Engagements (not Historical Financial Info)	ASAE 3100 Assurance Engagements on Compliance (This ASAE)	ASAE 3402 Controls at a Service Organisation	ASAE 3150 Controls Engagements	ASRS 4400 Agreed-upon Procedures
Subject Matter of Compliance Assurance Engagement	1. Entity's compliance with:					
	- Laws and regulation	✓	✓			
	- Contractual obligations	✓	✓			
	- Policies and procedures	✓	✓			
	2. Entity's controls <sup>41</sup> over compliance with requirements <sup>42</sup>	✓			✓	
	3. Entity's compliance <sup>39</sup> with requirements specifying controls	✓	✓			
	<del>4. Service Organisation's controls:</del>					
	<del>- Relevant to user entities' non-financial reporting, services or functions</del>	✗			✗	
	<del>- Relevant to user entities' financial reporting</del>	✗		✗		
	<del>Controls over economy, efficiency or effectiveness</del>	✗			✗	
	5.4 Procedures restricted to those specified by engaging party					✓

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<sup>41</sup> The subject matter of the assurance engagement determines which ASAE to apply.

<sup>42</sup> Where controls not specified in law, regulation or quasi-regulation.

## Appendix 5

(Ref: Para. A21)

### EXAMPLE ENGAGEMENT LETTERS

Example 1: Engagement Letter for an Attestation Engagement for Limited Assurance on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria]

Example 2: Engagement Letter for an Attestation Engagement for Reasonable Assurance on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria]

Example 3: Engagement Letter for a Direct Engagement for Reasonable Assurance on ABC's compliance with the [compliance requirements] as evaluated by the [suitable criteria]

*The following examples of assurance practitioner's engagement letters are for guidance only and are not intended to be exhaustive or applicable to all situations.*

#### **Example 1: Engagement Letter for an Attestation Engagement for Limited Assurance on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria]**

To [the appropriate representative of management or those charged with governance of ABC or the engaging party]:

##### *[Objective and scope of the engagement]*

You have requested that we undertake a limited assurance engagement on ABC's Statement [which will accompany our report] of compliance with the [compliance requirements], in all material respects, as evaluated by the [suitable criteria], which you will provide and which will accompany our report, [throughout the specified period or as at a specified date] for the purpose of reporting to [identify intended users: the Board of Directors/Regulator/Customers of ABC].

We are pleased to confirm our acceptance and our understanding of this limited assurance engagement by means of this letter. Our assurance engagement will be conducted with the objective of reaching a conclusion on whether [ABC's Statement]<sup>43</sup> of compliance with the [compliance requirements] is, in all material respects, ~~properly prepared and presented~~~~fairly stated~~ as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

##### *[Our Independence and Quality Control]*

We will comply with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

##### *[Responsibilities of the assurance practitioner]*

We will conduct our assurance engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements*. That standard requires that we comply with ethical requirements applicable to assurance engagements and plan and perform procedures to obtain limited assurance about whether anything has come to our attention that causes us to believe that [ABC's Statement] is not ~~properly prepared and presented~~~~fairly stated~~ in that ~~-~~compliance with the [compliance requirements] as evaluated by the [suitable criteria] have not been met, in all material respects.

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<sup>43</sup> Insert if the assurance report is expressed in terms of the responsible party's or evaluator's Statement rather than the ~~assurance practitioner's conclusion being expressed in terms of whether the compliance requirements have been met~~~~underlying subject matter~~.

## Standard on Assurance Engagements ASAE 3100

### Compliance Engagements

An assurance engagement on compliance involves performing procedures to obtain evidence about the compliance with the [compliance requirements] as measured by the [suitable criteria]. The procedures selected depend on the assurance practitioner's professional judgement, including identifying areas where the risk of material deficiencies in the compliance framework or misstatements in ABC's Statement are likely to arise. We will perform procedures primarily consisting of discussion and making enquiries of management and others within the entity, as appropriate, observation and walkthroughs of compliance activities ~~examination of documentation~~ and evaluation of the evidence obtained about compliance with the [compliance requirements] as evaluated by the [suitable criteria] as provided in ABC's Statement. We will also perform additional procedures if we become aware of matters that cause us to believe there are deficiencies in the compliance framework or misstatements in ABC's Statement. The procedures selected depend on what we consider necessary applying our professional judgement, including the assessment of risks of material deficiencies in the compliance framework or misstatements in ABC's Statement.

Because of the inherent limitations of an assurance engagement, together with the inherent limitations of any system of internal control there is an unavoidable risk that some deficiencies in the compliance framework or misstatements in ABC's Statement may not be detected, even though the engagement is properly planned and performed in accordance with Standards on Assurance Engagements. ~~Therefore no opinion will be expressed as to the effectiveness of the system of internal control as a whole.~~

The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement and consequently the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed. Therefore there is a higher risk than there would be in a reasonable assurance engagement, that any material deficiencies in the compliance framework and relevant controls that exist may not be revealed by the engagement, even though the engagement is properly performed in accordance with ASAE 3100. In expressing our conclusion, our report on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria] will expressly disclaim any reasonable assurance conclusion on the compliance framework and relevant controls.

*[Responsibilities of the responsible party/ management/ those charged with governance]*

Our assurance engagement will be conducted on the basis that [the responsible party/ management/ those charged with governance] acknowledge and understand that they have responsibility:

- (a) For the preparation of a written Statement [which will be attached to our report] that ABC has complied [throughout the specified period or at a specified date], in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria];
- ~~(b)~~ For identification of the [compliance requirements] if not identified by law or regulation.
- ~~(b)~~

For the identification of risks that threaten the [compliance requirements] identified above not being met, ÷

- (c) ~~For the identification, design and implementation of~~ controls which will mitigate those risks ~~so that those risks will not prevent the [compliance requirements] being met~~ and ~~to~~ monitor ongoing compliance; and
- (d) To provide us with:
  - (i) Access to all information of which those charged with governance and management are aware that is relevant to ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria];

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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- (ii) Additional information that we may request from those charged with governance and management for the purposes of this assurance engagement; and
- (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain evidence.

As part of our engagement, we will request from [the responsible party/ management/ those charged with governance] written confirmation concerning representations made to us in connection with the engagement.

*[Assurance Report]*

The format of the report will be in accordance with ASAE 3100 with respect to limited assurance engagements [and will be in long-form, including assurance procedures, findings and recommendations]. An example of the proposed report is contained in the appendix to this letter.

[Our report will be issued [frequency] and will cover ~~[throughout the specified period or will be as at a specified date reported on]~~.<sup>44</sup>

~~The limited assurance report will be attached to~~ [ABC's Statement] will be attached to the limited assurance report and our conclusion will be phrased in terms of whether anything has come to our attention that causes us to believe that [ABC's Statement] is not properly prepared and presented fairly stated and compliance with the [compliance requirements] as evaluated by the [suitable criteria] have not been met, in all material respects [throughout the specified period or as at specified date].

*[Use of the Assurance Report]<sup>45</sup>*

[Our report will be prepared for the use of ABC and [intended users] for [purpose] and may not be suitable for any other purpose].

The assurance report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report to any person other than ABC and [intended users], or for any purpose other than that for which it was prepared.]

We look forward to full cooperation from your staff during our assurance engagement.

*[Other relevant information]*

*[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]*

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our assurance engagement to report on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria], including our respective responsibilities.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of [engaging party]

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<sup>44</sup> Insert this sentence for recurring engagements.

<sup>45</sup> Insert this section if the report is to be for restricted use only.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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(signed)

.....  
Name and Title

Date

**Example 2: Engagement Letter for an Attestation Engagement for Reasonable Assurance on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria]**

*To [the appropriate representative of management or those charged with governance of ABC or the engaging party]:*

*[Objective and scope of the engagement]*

You have requested that we undertake a reasonable assurance engagement on ABC's Statement [which will accompany our report] of compliance with the [compliance requirements] as evaluated by the [suitable criteria], in all material respects, which you will provide and which will accompany our report, [throughout the specified period or as at a specified date] for the purpose of reporting to [identify intended users: the Board of Directors/Regulator/Customers of ABC].

We are pleased to confirm our acceptance and our understanding of this reasonable assurance engagement by means of this letter. Our assurance engagement will be conducted with the objective of expressing an opinion on whether [ABC's Statement]<sup>46</sup> that the entity has complied with the [compliance requirements] is, in all material respects, ~~properly prepared and presented~~ **fairly stated** as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

*[Our Independence and Quality Control]*

We **will** comply with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

*[Responsibilities of the assurance practitioner]*

We will conduct our assurance engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements*. That standard requires that we comply with ethical requirements applicable to assurance engagements and plan and perform procedures to obtain reasonable assurance about whether, [ABC's Statement] is fairly stated, in all material respects.

An assurance engagement on compliance involves performing procedures to obtain evidence about ABC's Statement of compliance with the [compliance requirements] as measured by the [suitable criteria]. We will perform procedures to obtain evidence about compliance activities and controls implemented to meet the [compliance requirements]. The procedures selected depend on the assurance practitioner's professional judgement, including the identification and assessment of risks of material deficiencies in the compliance framework or misstatements in ABC's Statement.

Because of the inherent limitations of an assurance engagement, together with the inherent limitations of any system of internal control there is an unavoidable risk that some deficiencies in the compliance framework or misstatements in ABC's Statement may not be detected, even though the engagement is properly planned and performed in accordance with Standards on Assurance Engagements. ~~Therefore no opinion will be expressed as to the effectiveness of the system of internal control as a whole.~~

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<sup>46</sup> Insert if the assurance report is expressed in terms of the responsible party's or evaluator's Statement rather than the ~~assurance practitioner's conclusion being expressed in terms of whether the compliance requirements have been met~~ underlying subject matter.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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*[Responsibilities of the responsible party /management / those charged with governance]*

Our assurance engagement will be conducted on the basis that [the responsible party/management/those charged with governance] acknowledge and understand that they have responsibility:

- (a) For the preparation of a written Statement [which will be attached to our report] that ABC has complied [throughout the specified period or as at a specified date], in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria].
- (b) Identification of the [compliance requirements] if not identified by law or regulation.
- ~~(c)~~ For the identification of risks that threaten the [compliance requirements] identified above being met and;
- ~~(d)~~(c) ~~For the identification, design and implementation of~~ controls which will mitigate those risks ~~so that those risks will not prevent the [compliance requirements] being met~~ and ~~to~~ monitor ongoing compliance; and
- ~~(e)~~(d) To provide us with:
  - (i) Access to all information of which those charged with governance and management are aware that is relevant to ABC's Statement of compliance with the [compliance requirements] as measured by the [suitable criteria];
  - (ii) Additional information that we may request from those charged with governance and management for the purposes of this assurance engagement; and
  - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain evidence.

As part of our engagement, we will request from [the responsible party/ management/ those charged with governance] written confirmation concerning representations made to us in connection with the engagement.

*[Assurance Report]*

The format of the report will be in accordance with ASAE 3100 with respect to reasonable assurance engagements [and will be in long-form, including assurance procedures, findings and recommendations]. An example of the proposed report is contained in the appendix to this letter.

[Our report will be issued [frequency] and will cover ~~[throughout the specified period or~~ will be as at a specified date].<sup>47</sup>

~~The reasonable assurance report will be attached to~~ [ABC's Statement] will be attached to the reasonable assurance report and our opinion will be phrased in terms of whether [ABC's Statement] that the entity has complied with the [compliance requirements] is, in all material respects, properly prepared and presented~~fairly stated~~ as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

*[Use of the Assurance Report]*<sup>48</sup>

[Our report will be as prepared for the use of ABC and [intended users] for [purpose] and may not be suitable for any other purpose].

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<sup>47</sup> Insert this sentence for recurring engagements.

<sup>48</sup> Insert this section if the report is to be for restricted use only.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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The assurance report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report to any person other than ABC and [intended users], or for any purpose other than that for which it was prepared.]

We look forward to full cooperation from your staff during our assurance engagement.

*[Other relevant information]*

*[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]*

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our assurance engagement to report on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria], including our respective responsibilities.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of [ABC/engaging party]

(signed)

.....

Name and Title

Date

**Example 3: Engagement Letter for a Direct Engagement for Reasonable Assurance on ABC's compliance with the [compliance requirements] as evaluated by the [suitable criteria]**

*To [the appropriate representative of management or those charged with governance of ABC or the engaging partyaddressee]:*

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*[Objective and scope of the engagement]*

You have requested that we undertake a reasonable assurance engagement to report on ABC's compliance with the [compliance requirements] as evaluated by the [suitable criteria], in all material respects, [throughout the specified period or as at a specified date] for the purpose of reporting to [identify intended users: the Board of Directors/Regulator/Customers of ABC].

We are pleased to confirm our acceptance and our understanding of this reasonable assurance engagement by means of this letter. Our assurance engagement will be conducted with the objective of expressing an opinion on ABC's compliance with the [compliance requirements], in all material respects, as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

*[Our Independence and Quality Control]*

We will comply with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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*[Responsibilities of the assurance practitioner]*

We will conduct our assurance engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements*. That standard requires that we comply with ethical requirements applicable to assurance engagements and plan and perform procedures to obtain reasonable assurance about whether ABC has complied with the [compliance requirements], in all material respects, as evaluated by the [suitable criteria].

An assurance engagement on compliance involves performing procedures to obtain evidence about ABC's compliance with the [compliance requirements] as evaluated by the [suitable criteria]. We will perform procedures to obtain evidence about compliance activities and controls implemented to meet the [compliance requirements]. The procedures selected depend on the assurance practitioner's professional judgement, including the identification and assessment of risks of material deficiencies in the compliance framework or material non-compliance with the [compliance requirements] as evaluated by the [suitable criteria].

Because of the inherent limitations of an assurance engagement, together with the inherent limitations of any system of internal control there is an unavoidable risk that some deficiencies in the compliance framework or non-compliance by ABC with the [compliance requirements] may not be detected, even though the engagement is properly planned and performed in accordance with Standards on Assurance Engagements. ~~Therefore no opinion will be expressed as to the effectiveness of the system of internal control as a whole.~~

*[Responsibilities of the responsible party/ management/ those charged with governance]*

Our assurance engagement will be conducted on the basis that [the responsible party/management/those charged with governance] acknowledge and understand that they have responsibility:

- (a) For compliance with the [compliance requirements] as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].
- ~~(b)~~ For the identification of risks that threaten the [compliance requirements] identified above being met ~~and~~;
- ~~(c)~~~~(b)~~ ~~For the identification, design and implementation of~~ controls which will mitigate those risks ~~so that those risks will not prevent the [compliance requirements] being met~~ and ~~to~~ monitor ongoing compliance; and
- ~~(d)~~~~(c)~~ To provide us with:
  - (i) Access to all information of which those charged with governance and management are aware that is relevant to ABC's compliance with the [compliance requirements] as measured by the [suitable criteria];
  - (ii) Additional information that we may request from those charged with governance and management for the purposes of this assurance engagement; and
  - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain evidence.

As part of our engagement, we will request from [the responsible party/ management/ those charged with governance] written confirmation concerning representations made to us in connection with the engagement.

*[Assurance Report]*

The format of the report will be in accordance with ASAE 3100 with respect to reasonable assurance engagements [and will be in long-form, including assurance procedures, findings and recommendations]. An example of the proposed report is contained in the appendix to this letter.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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*[Use of the Assurance Report]<sup>49</sup>*

| [Our report will be prepared for the use of ABC and *[intended users]* for *[purpose]*, and may not be suitable for any other purpose].

The assurance report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report to any person other than ABC and *[intended users]*, or for any purpose other than that for which it was prepared].

We look forward to full cooperation from your staff during our assurance engagement.

*[Other relevant information]*

*[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate]*

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our assurance engagement to report on ABC's compliance with the *[compliance requirements]* as evaluated by the *[suitable criteria]*, including our respective responsibilities.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of *[engaging party]*

(signed).....

Name and Title

Date

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<sup>49</sup> Insert this section if the report is to be for restricted use only.

## Appendix 6

(Ref: Para. A58)

### EXAMPLE ASSURANCE REPORTS ON COMPLIANCE

- Example 1: Limited Assurance Report on compliance with the [compliance requirements] as evaluated by the [suitable criteria] (Direct engagement)
- Example 2: Reasonable Assurance Report on compliance with the [compliance requirements] as evaluated by the [suitable criteria] (Direct engagement)
- Example 3: Reasonable Assurance Report on ABC's Statement of Compliance with the [compliance requirements] as evaluated by the [suitable criteria] (Attestation engagement)

*The following examples of reports are for guidance only and are not intended to be exhaustive or applicable to all situations. They can be applied to both attestation and direct engagements. These examples are short-form reports but may be converted to long-form reports by inclusion of additional information as indicated.*

#### **Example 1: Limited Assurance Report on compliance with the [compliance requirements] as evaluated by the suitable criteria (Direct engagement)**

Independent Assurance Report

[Appropriate Addressee]

##### *Conclusion*

We have undertaken a limited assurance engagement on ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that ABC, has not complied in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

[For a long-form report include a separate section, under an appropriate heading, or reference to an attachment for any additional information agreed in the terms of engagement to be provided to users, for example:

- Terms of the engagement.
- Criteria and compliance requirements being used.
- Descriptions of the tests of compliance that were performed.
- Findings relating to the tests of compliance that were performed or particular aspects of the engagement.
- Details of the qualifications and experience of the assurance practitioner and others involved with the engagement.
- Disclosure of materiality levels.
- Recommendations for improvements to the compliance framework or processes around particular compliance activities].

## Standard on Assurance Engagements ASAE 3100 Compliance Engagements

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### Basis for Conclusion

We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* issued by the Auditing and Assurance Standards Board.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.<sup>50</sup>

### *ABC's Responsibilities*

ABC is responsible for:

- (a) The compliance activity undertaken to meet the [compliance requirements];
- ~~(b) Identification of risks that threaten the [compliance requirements] identified above being met; and~~
- ~~(c) Identification, design and implementation of controls which will mitigate those risks so that those risks will not prevent the [compliance requirements] being met and to monitor ongoing compliance.~~

### *Our Independence and Quality Control*

We have complied with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

### *Assurance Practitioner's Responsibilities*

Our responsibility is to express a limited assurance conclusion on ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date]. ~~We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* issued by the Auditing and Assurance Standards Board. ASAE 3100 That standard requires that we comply with relevant ethical requirements~~ and plan and perform our procedures to obtain limited assurance about whether anything has come to our attention that, ABC has not complied, in all material respects, with the [compliance requirements], as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

In a limited assurance engagement, the assurance practitioner performs procedures, primarily consisting of ~~discussion and making~~ enquiries of management and others within the entity, as appropriate, and ~~observation and walk-through examination of documentation~~, and evaluates the evidence obtained. The procedures selected depend on our judgement, including identifying areas where the risk of material non-compliance with the [compliance requirements] is likely to arise.

*[Insert an informative summary of the nature, timing and extent of procedures performed that, in the assurance practitioner's judgement, provides additional information that may be relevant to the users' understanding of the basis for the assurance practitioner's conclusion. The following section has been provided as guidance, and the example procedures are not an exhaustive list of either the type, or extent, of the procedures which may be important for the users' understanding of the work performed].<sup>50</sup>*

<sup>50</sup> The procedures are to be summarised but not to the extent that they are ambiguous, nor described in a way that is overstated or embellished or that implies that reasonable assurance has been obtained. It is important that the description of the procedures does not give the impression that an agreed-upon procedures engagement has been undertaken, and in most cases will not detail the entire work plan.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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Given the circumstances of the engagement, in performing the procedures listed above we:

- Through discussion, enquiries and observation, obtained an understanding of ABC's compliance framework and internal control environment to meet the [compliance requirements], as evaluated by the [suitable criteria].
- Through discussion, enquiries, ~~observation~~inspection and walk-throughs, obtained an understanding of relevant [compliance activities] that are undertaken to meet the [compliance requirements], as evaluated by the [suitable criteria].

The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement and consequently the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed. Accordingly, we do not express a reasonable assurance opinion on compliance with the [compliance requirements].

~~We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.~~

*Inherent Limitations*

Because of the inherent limitations of an assurance engagement, together with the internal control structure it is possible that fraud, error, or non-compliance with compliance requirements~~laws and regulations~~ may occur and not be detected.

A limited assurance engagement ~~on ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], at a [throughout the specified period or as at specified date]~~<sup>51</sup> does not provide assurance on whether compliance with the [compliance requirements] will continue in the future.

*[Restricted Use]*<sup>52</sup>

[This report has been prepared for use by [intended users] for the purpose of [explain purpose]. We disclaim any assumption of responsibility for any reliance on this report to any person other than [intended users], or for any other purpose other than that for which it was prepared.]

*[Assurance practitioner's signature]*<sup>53</sup>

*[Date of the assurance practitioner's assurance report]*

*[Assurance practitioner's location]*<sup>54</sup>

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<sup>51</sup> ~~Insert only for compliance engagements performed at a date in time.~~

<sup>52</sup> Insert section if the report is restricted use.

<sup>53</sup> The assurance practitioner's report needs to be signed in one or more of the following ways: name of the assurance practitioner's firm, name of the assurance practitioner's company or the personal name of the assurance practitioner as appropriate.

<sup>54</sup> The assurance practitioner's address includes the location in the jurisdiction where the assurance practitioner practices.

**Standard on Assurance Engagements ASAE 3100**  
**Compliance Engagements**

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**Example 2: Reasonable Assurance Report on compliance with the [compliance requirements] as evaluated by the [suitable criteria] (Direct engagement)**

Independent Assurance Report

[Appropriate Addressee]

*Opinion*

We have undertaken a reasonable assurance engagement on ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

In our opinion, ABC has complied, in all material respects with the [compliance requirements] as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

[For a long-form report, include a separate section, under an appropriate heading, or reference to an attachment for any additional information agreed in the terms of engagement to be provided to users, for example:

- Terms of the engagement.
- Criteria and compliance requirements being used.
- Descriptions of the tests of compliance that were performed.
- Findings relating to the tests of compliance that were performed or particular aspects of the engagement.
- Details of the qualifications and experience of the assurance practitioner and others involved with the engagement.
- Disclosure of materiality levels.
- Recommendations for improvements to the compliance framework or processes around particular compliance activities].

*Basis for Opinion*

We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* issued by the Auditing and Assurance Standards Board.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion ~~conclusion~~.

*ABC's Responsibilities*

ABC is responsible for:

- (a) The compliance activity undertaken to meet the [compliance requirements];
- ~~(b)~~ Identification of risks that threaten the [compliance requirements] identified above being met; ~~and~~
- ~~(c)~~ ~~(b)~~ ~~Identification, design and implementation of~~ controls which will mitigate those risks ~~so that those risks will not prevent the [compliance requirements] being met and to~~ monitor ongoing compliance.

## Standard on Assurance Engagements ASAE 3100 Compliance Engagements

---

### *Our Independence and Quality Control*

We have complied with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

### *Assurance Practitioner's Responsibilities*

Our responsibility is to express an opinion on ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date]. ~~We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 Compliance Engagements issued by the Auditing and Assurance Standards Board. That standard ASAE 3100 requires that we comply with relevant ethical requirements and~~ plan and perform our procedures to obtain reasonable assurance about whether, ABC has complied, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date].

An assurance engagement to report on ABC's compliance with the [compliance requirements] involves performing procedures to obtain evidence about the compliance activity and controls implemented to meet the [compliance requirements]. The procedures selected depend on our judgement, including the identification and assessment of risks of material non-compliance with the [compliance requirements], as evaluated by the [suitable criteria].

~~We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

### *Inherent Limitations*

Because of the inherent limitations of an assurance engagement, together with the internal control structure it is possible that fraud, error, or non-compliance with ~~compliance requirements~~ ~~laws and regulations~~ may occur and not be detected.

A reasonable assurance engagement ~~[throughout the specified period or as at ABC's compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], at a specified date]~~<sup>55</sup> does not provide assurance on whether compliance with the [compliance requirements] will continue in the future.

### *[Restricted Use]*<sup>56</sup>

[This report has been prepared for use by [intended users] for the purpose of [explain purpose]. We disclaim any assumption of responsibility for any reliance on this report to any person other than [intended users], or for any other purpose other than that for which it was prepared.]

*[Assurance practitioner's signature]*<sup>57</sup>

*[Date of the assurance practitioner's assurance report]*

*[Assurance practitioner's location]*<sup>58</sup>

---

<sup>55</sup> ~~Insert only for compliance engagements performed at a date in time.~~

<sup>56</sup> Insert section if the report is restricted use.

<sup>57</sup> The assurance practitioner's report needs to be signed in one or more of the following ways: name of the assurance practitioner's firm, name of the assurance practitioner's company or the personal name of the assurance practitioner as appropriate.

<sup>58</sup> The assurance practitioner's address includes the location in the jurisdiction where the assurance practitioner practices.

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**Example 3: Reasonable Assurance Report on ABC's Statement of Compliance with the [compliance requirements] as evaluated by the [suitable criteria] (Attestation engagement)**

Independent Assurance Report

[Appropriate Addressee]

*Opinion*

We have undertaken a reasonable assurance engagement on ABC's Statement of compliance, in all material respects, with the [compliance requirements], as evaluated by the [suitable criteria], [throughout the specified period or as at a specified date]. This Statement will accompany our report, for the purpose of reporting to [identify intended users].

In our opinion, ABC's Statement<sup>59</sup> that the entity has complied with the [compliance requirements] is, in all material respects, properly prepared and presented~~fairly stated~~ as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

*[For a long-form report, include a separate section, under an appropriate heading, or reference to an attachment for any additional information agreed in the terms of engagement to be provided to users, for example:*

- Terms of the engagement.
- Criteria and compliance requirements being used.
- Descriptions of the tests of compliance that were performed.
- Findings relating to the tests of compliance that were performed or particular aspects of the engagement.
- Details of the qualifications and experience of the assurance practitioner and others involved with the engagement.
- Disclosure of materiality levels.
- Recommendations for improvements to the compliance framework or processes around particular compliance activities].

*Basis for Opinion*

We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 *Compliance Engagements* issued by the Auditing and Assurance Standards Board.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our ~~opinion~~conclusion.

*ABC's Responsibilities*

ABC is responsible for:

- (a) Providing a Statement with respect to the outcome of the evaluation of the compliance activity against the [compliance requirements], which accompanies this independent assurance report.
- (b) Identification of the [compliance requirements] if not identified by law and regulation.
- (c) The compliance activity undertaken to meet the [compliance requirements]; and

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<sup>59</sup> This attestation example report assumes the responsible party provides a Statement of Compliance, if this is not provided the assurance practitioner's conclusion would be expressed in terms of whether the compliance requirements have been met.

- (d) Identification, ~~design and implementation of~~ implementation of controls which will mitigate those risks ~~so that those risks will not prevent~~ prevent the [compliance requirements] being met and ~~to~~ monitor ongoing compliance.

#### *Our Independence and Quality Control*

We have complied with the independence and other relevant ethical requirements relating to assurance engagements, and apply Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* in undertaking this assurance engagement.

#### *Assurance Practitioner's Responsibilities*

Our responsibility is to express an opinion, on ABC's Statement of compliance with the [compliance requirements], in all material respects as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date]. ~~We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 Compliance Engagements issued by the Auditing and Assurance Standards Board. ASAE 3100~~ That standard requires that ~~we comply with relevant ethical requirements and we~~ plan and perform our procedures to obtain reasonable assurance about whether, ABC's Statement that the entity has complied with the [compliance requirements] is, in all material respects, ~~properly prepared and presented fairly stated~~ as evaluated by the [suitable criteria] [throughout the specified period or as at a specified date].

An assurance engagement to report on ABC's Statement of the entity's compliance with the [compliance requirements] involves performing procedures to obtain evidence about the compliance activity and controls implemented to meet the [compliance requirements]. The procedures selected depend on our judgement, including the identification and assessment of risks of material misstatements in ABC's Statement are likely to arise.

~~We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.~~

#### *Inherent Limitations*

Because of the inherent limitations of an assurance engagement, together with the internal control structure it is possible that fraud, error, or non-compliance with ~~compliance requirements~~ laws and regulations may occur and not be detected.

A reasonable assurance engagement ~~on ABC's Statement of compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], at a [throughout the specified period or as at a specified date]~~<sup>60</sup> does not provide assurance on whether compliance with the [compliance requirements] will continue in the future.

#### *[Restricted Use]*<sup>61</sup>

[This report has been prepared for use by [intended users] for the purpose of [explain purpose]. We disclaim any assumption of responsibility for any reliance on this report to any person other than [intended users], or for any other purpose other than that for which it was prepared.]

*[Assurance practitioner's signature]*<sup>62</sup>

*[Date of the assurance practitioner's assurance report]*

*[Assurance practitioner's location]*<sup>63</sup>

<sup>60</sup> ~~Insert only for compliance engagements performed at a date in time.~~

<sup>61</sup> Insert section if the report is restricted use.

<sup>62</sup> The assurance practitioner's report needs to be signed in one or more of the following ways: name of the assurance practitioner's firm, name of the assurance practitioner's company or the personal name of the assurance practitioner as appropriate.

<sup>63</sup> The assurance practitioner's address includes the location in the jurisdiction where the assurance practitioner practices.

## Appendix 7

(Ref: Para. A61)

### EXAMPLE MODIFIED ASSURANCE REPORTS ON COMPLIANCE

- Example 1: Qualified reasonable assurance opinion – a material (but not pervasive) ~~misstatement~~ ~~matter of non-compliance was identified with~~in ABC's Statement on the entity's compliance with the [compliance requirements] (Attestation engagement)
- Example 2: Adverse reasonable assurance opinion – ~~ABC non-compliant with~~ the [compliance requirements] ~~were non-compliant~~ throughout the specified period (Direct engagement)
- Example 3: Disclaimer of reasonable assurance opinion – the assurance practitioner is unable to obtain sufficient appropriate evidence of compliance with the [compliance requirements] (Direct engagement)
- Example 4: Qualified limited assurance conclusion – the assurance practitioner is unable to obtain sufficient appropriate evidence of compliance with the [compliance requirements] (Direct engagement)

*The following examples of modified reasonable and limited assurance reports are for guidance only and are not intended to be exhaustive or applicable to all situations. ~~They are based on the example reports in Appendix 6 and may be adapted as appropriate to the engagement circumstances.~~*

**Example 1: Qualified reasonable assurance opinion – a material (but not pervasive)**  
~~misstatement in matter of non-compliance was identified with~~ABC's Statement on the entity's compliance with the [compliance requirements] (Attestation engagement)

...

#### *Qualified Opinion*

In our opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion paragraph, the Statement by ABC that the entity has complied with the [compliance requirements] is, in all material respects, ~~properly prepared and presented~~~~fairly stated~~ as evaluated by the [suitable criteria] [as at [date]/ throughout the specified period from [date] to [date]].

...

#### *Basis for Qualified Opinion*

We identified a material matter in ABC's Statement in relation to [non-compliance with sXX of Act/Regulation XX]. This has the effect of the [Trustee bank account and cash book procedures not being completed throughout the specified period] as required. We were unable to satisfy ourselves ~~as to ABC's compliance with this requirement~~~~by alternate procedures~~, therefore qualify our opinion in this regard.

...

#### *Assurance Practitioner's Responsibilities*

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

---

**Example 2: Adverse reasonable assurance opinion – ABC non-compliant with the compliance requirements ~~were non-compliant~~ throughout the specified period (Direct engagement)**

...

*Adverse Opinion*

In our opinion, ABC has not complied, in all material respects, with the [compliance requirements], as evaluated by the [suitable criteria], throughout the specified period from [date] to [date].

...

*Basis for Adverse Opinion*

We have identified a material matter in relation to [sXX of Act/Regulation XX] with regard to that the procedures and controls regarding ~~ABC's RSE~~ bank accounts and other assets were not completed and effective throughout the specified period [date] to [date]. This has the effect of ~~ABC the RSE~~ not meeting the [conditions imposed under sXX of Act/Regulation XX] and being non-compliant in this regard.

...

*Assurance Practitioner's Responsibilities*

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our adverse opinion.

...

**Example 3: Disclaimer of reasonable assurance opinion – the assurance practitioner is unable to obtain sufficient appropriate evidence of compliance with the [compliance requirements] (Direct engagement)**

...

*Disclaimer of Opinion*

Because of the significance of the matter described in the Basis for Disclaimer of Opinion section of our report, we ~~do not express an opinion have not been able to obtain sufficient appropriate evidence to provide the basis for an opinion~~ on ABC's compliance with [compliance requirements], as evaluated by the [suitable criteria] throughout the specified period.

...

*Basis for Disclaimer of Opinion*

ABC's computer systems were subject to a cyber-attack on [date] in which a substantial amount of ABC's data was destroyed and no back up data retrievable, throughout the period from [date] to [date]. Due to this event we were unable to conduct testing of compliance activities or walk-throughs relevant to [compliance requirements] throughout the specified period, which would be necessary to form an opinion on whether ABC was complaint with [compliance requirements] throughout the period.

...

*Assurance Practitioner's Responsibilities*

Because of the matter described in the Basis for Disclaimer of Opinion paragraph, we are not able to obtain sufficient appropriate evidence to provide a basis for a reasonable assurance opinion on ABC's compliance with the [compliance requirements], as evaluated by the [suitable criteria].

...

---

**Example 4: Qualified limited assurance conclusion – the assurance practitioner is unable to obtain sufficient appropriate evidence of compliance with the [compliance requirements] (Direct engagement)**

...

*Qualified Conclusion*

Based on the procedures we have performed and the evidence we have obtained, except for the effects of the matter described in the Basis for Qualified Conclusion paragraph, nothing has come to our attention that causes us to believe that, ABC has not complied, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria] throughout the specified period from [date] to [date].

...

*Basis for Qualified Conclusion*

We ~~were unable to obtain sufficient appropriate audit evidence about ABC's compliance with identified a material matter in relation to [non-compliance with~~ sXX of Act/Regulation XX]. This has the effect of [the Trustee bank account and cash book procedures not being completed in relation to sXX of Act/Regulation XX] throughout the specified period as required. We were unable to satisfy ourselves by alternate procedures, therefore qualify our conclusion in this regard.

...

*Assurance Practitioner's Responsibilities*

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified conclusion.

The Chairman  
Auditing and Assurance Standards Board  
PO Box 204,  
Collins Street West  
Melbourne Victoria 8007  
Australia

Our ref KPMG submission ED 3100  
Compliance Engagements.  
docx

17 October 2016

Dear Chairman

**AUASB Exposure Draft (ED), 04/16 on ASAE 3100 *Compliance Engagements***

We are pleased to have the opportunity to respond to the ED 04/16, ASAE 3100 *Compliance Engagements* issued by the Australian Auditing and Assurance Standards Board (AUASB).

This letter represents KPMG Australia's views.

**Overarching comments**

Overall, KPMG Australia is very supportive of the revised requirements and additional application and other explanatory material in the Exposure Draft. The key comments we wish to highlight to the AUASB are shown below.

**1. Definitions: the term "criteria" Paragraph 17 (g)**

The term **criteria** isn't clearly differentiated from **compliance requirement**. Criteria is presented as similar to compliance requirement: *the specific requirements established in law versus the legislation used to evaluate whether compliance requirements have been met*. Appendix 3 "Examples: Nature of Assurance Engagements on Compliance" makes it easier to understand by illustrating with an example. We recommend that **compliance requirement** be phrased as the overarching Act, Standard, Regulation, or Section and the **criteria** is the specific requirements contained or listed in the Act, Standard, Regulation or Section.

**2. Use of the term "Fairly stated" in an attestation engagement assurance report**

We note that Appendix 6: Example 3 Reasonable Assurance Report on ABC's Statement of Compliance (Attestation Engagement) uses the term "fairly stated" when concluding on ABC's Statement. The term "fairly stated" relates to the "fair presentation framework" and the use in this example is not a technical application but rather applied as a commonly understood plain English phrase such as in the meaning of "adequately" or "reasonably".

We suggest one of the following two options:

1. Retain the example wording of "*fairly stated*" because we believe that intended users are able to understand the assurance practitioner's conclusion when phrased in this manner and ASAE 3150 uses a similar phrase "*fairly presented*" in its assurance report examples. We do however suggest you include a sentence in the guidance paragraphs to indicate that the AUASB had considered whether this was a technical application of the fair presentation



framework and although it is not a strict technical application, you are comfortable to use it with respect to the responsible party's "Statement" to achieve understandability. This will avoid each practitioner challenging whether it's an appropriate use of this phrase; and/or

2. Use alternative wording such as "properly prepared and presented".

**Other comments**

We provide further detailed observations as follows:

- Appendix 1: other comments for the AUASB's consideration.
- Appendix 2: responses to the specific questions listed in the AUASB Exposure Draft.

Please contact me on (02) 9335 7630 if you wish to discuss any of the comments in this letter.

Yours faithfully

A handwritten signature in dark ink, appearing to read 'M McGrath'.

Martin McGrath  
Partner  
KPMG

## Appendix 1 – Other comments for AUASB’s further consideration

	Paragraph(s)	Issue(s) noted	Recommendation / suggestion on wordings to add and remove.
1	17 (c)	Definition inconsistent with AUASB glossary (Glossary) definition of ‘Compliance engagement’. The fuller definition in the Glossary states that its source is ASAE3100.	We suggest retaining the fuller definition from the Glossary in ASAE 3100, or updating the Glossary section for consistency. Alternatively if the fuller description is not included in ASAE 3100, we suggest to delete the reference to ASAE 3100 as the source of the definition in the Glossary.
3	23, 24 (b) and A15 A16	<ul style="list-style-type: none"> <li>The practitioner identifies, selects or develops the criteria</li> <li>Criteria may need to be amended during the engagement.</li> </ul>	<ul style="list-style-type: none"> <li>If we’re <i>developing</i> the criteria at the time of the engagement, we query how the responsible party can demonstrate compliance with the criteria over the period subject to assurance and therefore meet the overall compliance requirement? How could the responsible party have designed an appropriate compliance activity to meet the criteria if the criteria were not known?</li> <li>Similar concept if we amend the criteria during the engagement per A16. How could the overall compliance requirement be met?</li> </ul>
5	A6	Independence – A6 implies consulting services with respect to the compliance framework are <b>likely to</b> impact the practitioner’s independence and <b>likely to</b> preclude acceptance. There are safeguards that can be applied to be able to deliver an engagement such as pre-assurance work like gap analysis that is an advisory style service that provides suggestions or observations. This type of engagement would not contemplate designing or implementing the compliance framework or making management decisions and therefore should not impact independence.	Change to “ <b>may</b> impact on the audit practitioner’s independence and <b>may</b> preclude acceptance of the engagement”. This allows the practitioner to evaluate their independence and whether application of a safeguard would manage the risk to an acceptable level.
6	A33	Third party outsourced service providers.	We recommend more discussion about how to obtain evidence on compliance with obligations when the responsible party uses an external third party outsourced service provider, as this is a common scenario.
7	Appendix 5	Missing practitioners’ responsibility to apply	We recommend reference to ASQC 1 in the practitioner’s responsibilities

	Engagement letters – Examples 1 to 3	ASQC 1.	section to be consistent with ASAE 3150 and 3402.
8	Appendix 6 Assurance reports on compliance – Examples 1 to 3	<ul style="list-style-type: none"> <li>• Inconsistent with new report format in ASA 700 <i>Forming an opinion and reporting on a financial report</i>.</li> <li>• Repeated statement in the inherent limitation section.</li> </ul>	<p>We recommend:</p> <ul style="list-style-type: none"> <li>• A header “<i>Basis for conclusion</i>” after the ‘<i>Conclusion</i>’ paragraph.</li> <li>• To move the following statements from <i>Assurance Practitioner’s Responsibilities</i> to the new header “<i>Basis for conclusion</i>”.</li> </ul> <p>“We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3100 <i>Compliance Engagements</i> issued by the Auditing and Assurance Standards Board. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.</p> <ul style="list-style-type: none"> <li>• To remove the following statement in the inherent limitation section to make it simple.</li> </ul> <p>“...on ABC’s compliance, in all material respects, with the [compliance requirements] as evaluated by the [suitable criteria], at a specified date...”</p>
9	Appendix 7 Modified assurance reports on compliance – example 3	Inconsistent Disclaimer of Opinion with ASA 705 <i>Modifications to the Opinion in the Independence Auditor’s Report</i> .	<p>We suggest below wording in <u>underline</u></p> <p><u>“We do not express an opinion on ABC’s compliance with the [compliance requirements] because of....”</u></p>

## **Appendix 2 – KPMG responses to the specific questions listed in the AUASB Exposure Draft**

1. *Have applicable laws and regulations been appropriately addressed in the proposed standard?*  
  
We believe applicable laws and regulations have been appropriately addressed.
2. *Are there any references to relevant laws or regulations that have been omitted?*  
  
We are not aware of any references to relevant laws or regulations that have been omitted.
3. *Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?*  
  
We are not aware of any laws or regulations that may prevent or impede application of the proposed standard or may conflict with the proposed standard.
4. *Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?*  
  
We believe the considerations for conducting a direct engagement are adequately differentiated from an attestation engagement. It would be useful to have one of the attestation examples in the appendices illustrate the alternative conclusion as suggested in paragraph 16 (a), even if by footnote.
5. *Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?*  
  
We believe the procedures required for limited and reasonable assurance are appropriate and adequately distinguished.
6. *What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?*  
  
We do not anticipate any significant incremental costs to auditors and the business community arising from compliance with the revised requirements of this proposed standard.  
  
There is however an impact with respect to liaising with regulators who issue “prescribed” reporting templates that do not apply the principles and terminology of the ASAEs. It is challenging for practitioners when a report prepared under the requirements of the Standards is rejected. Negotiations are required with regulators to amend their prescribed reports to achieve compliance with the Standards.  
  
We encourage the Board to consider how the changes to these Standards can be communicated to regulatory bodies, such that their prescribed reports can be adjusted to comply with the requirements of the revised Standards.
7. *Are there any other significant public interest matters that constituents wish to raise?*  
  
No, there are no other significant public interest matters we wish to raise.

The Chairman  
Auditing and Assurance Standards Board  
PO Box 204, Collins Street West  
Melbourne Victoria 8007

11 October 2016

## **ED 04/16 Proposed Standard on Assurance Engagements ASAE 3100 *Compliance Engagements***

Dear Merran

On behalf of Ernst & Young I am writing to support the proposals contained within Exposure Draft 04/16 which is designed to update ASAE 3100 *Compliance Engagements* to establish requirements and provides application and other explanatory material regarding the conduct of and reporting on assurance engagements on compliance.

We have supported and continue to support the AUASB's initiatives to improve assurance engagement quality and believe that the proposals enhance clarity on how to scope, conduct and report in an assurance engagement on compliance. We agree with the Board's effort to facilitate conformity with current AUASB standards and revised ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, which will be achieved by the proposals.

We also note the following, as requested:

1. As far as we can see, applicable laws and regulations have been appropriately addressed in the proposal standard;
2. We are not aware of any references to relevant laws or regulations that have been omitted;
3. We are not aware of any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard;
4. In our view, the considerations for conducting a direct engagement are adequately differentiated from an attestation engagement;
5. The procedures required for limited and reasonable assurance engagements are appropriately and adequately distinguished;
6. We do not believe that there are any additional significant costs to/ benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard; and
7. We have no significant public interest matters that we would like to raise in relation to the proposed standard.

Please contact me if you would like to discuss this submission further.

Denis Thorn  
Partner  
Ernest & Young



Copy to: Kathy Parsons, Oceania Professional Practice Director

19 October 2016

Ms Merran Kelsall  
Chairman  
Auditing and Assurance Standards Board  
PO Box 204, Collins Street West  
MELBOURNE VICTORIA 8007

Dear Ms Kelsall

**ACAG SUBMISSION ON EXPOSURE DRAFT 04/16 - PROPOSED STANDARD ON  
ASSURANCE ENGAGEMENTS ASAE 3100 COMPLIANCE ENGAGEMENTS**

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on the above Exposure Draft. The views expressed in this submission represent those of all Australian members of ACAG.

Overall, we support the proposed Standard. Although the existing ASAE 3100 *Compliance Engagements* is used sparingly by Australian audit offices, we have responded to the specific questions in the Exposure Draft and also provide comment on materiality.

We appreciate the opportunity to respond and trust you will find our comments useful.

Yours sincerely



Andrew Greaves  
**Chairman**

**ACAG Financial Reporting and Auditing Committee**

**Exposure Draft 04/16 - Proposed Standard on Assurance Engagements ASAE 3100  
Compliance Engagements**

**Specific Questions for Comment**

- 1. Have applicable laws and regulations been appropriately addressed in the proposed standard?**

ACAG makes no comment on this matter.

- 2. Are there any references to relevant laws or regulations that have been omitted?**

ACAG makes no comment on this matter.

- 3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

ACAG is not aware of any such laws or regulations.

- 4. Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?**

Generally, yes.

The considerations in paragraph A4 for differentiating the conduct of a direct engagement from an attestation engagement could better emphasise that in a direct engagement the assurance practitioner directly evaluates compliance with the compliance requirements and in an attestation engagement this evaluation is conducted by the responsible party.

- 5. Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?**

The procedures required for limited and reasonable assurance engagements are appropriate and adequately distinguished. We support the use of the tabular approach at paragraphs 32 and 43 to describe the required procedures.

- 6. What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?**

ACAG makes no comment on this matter.

- 7. Are there any other significant public interest matters that constituents wish to raise?**

None.

## **Comment on other matters**

### **Materiality**

ACAG acknowledges that the definition of “Material in the context of a compliance engagement” at paragraph 17(q) is similar to the definition in the existing ASAE 3100. However, this definition is not easy to understand and interpret, and we suggest that the definition be removed.

ACAG considers the materiality requirements at paragraph 31 and the explanatory material at paragraphs A25 to A30 are sufficient, subject to an addition to paragraph 31 requiring the assurance practitioner to consider materiality when evaluating whether the underlying subject matter (compliance activity) meets the compliance requirements.

This approach is consistent with the approach in ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.



24 October 2016

Merran Kelsall  
The Chairman  
Auditing and Assurance Standards Board  
PO Box 204, Collins St West  
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Australia

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Dear Merran

**ED 04/16 Proposed Standard on Assurance Engagements ASAE 3100 *Compliance Engagements***

CPA Australia welcomes the opportunity to respond to ED 04/16. CPA Australia represents the diverse interests of more than 155,000 members in 118 countries. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders. We make this submission on behalf of our members and in the broader public interest.

We support the AUASB's revision of ASAE 3100 as well as the scope and the overall approach of the proposed standard. Nevertheless, we consider that there are a number of matters which need to be addressed prior to finalisation of the standard. Our overall comments on ED 04/16 are set out below and further detailed comments are included as attachments.

**1. Use of the Term Compliance Framework**

We consider that the term "compliance framework" is not appropriate for the proposed definition provided and will be misunderstood. A plain English understanding of the term "compliance framework" would typically be a reference to the legislation, regulation and other requirements which make up the compliance requirements, effectively the criteria in a compliance engagement. This meaning does not align with the definition of compliance framework in ED 04/16 being: *"A framework adopted by the entity, which is designed to ensure that the entity achieves compliance, and includes governance structures, programs, processes, systems, controls and procedures"*. This definition encompasses controls to mitigate the risk of non-compliance with the compliance requirements.

Consequently, we consider that the term "compliance framework" should be replaced with a term such as "controls", "system of controls" or "controls relevant to compliance". And the term chosen should be consistent with other AUASB Standards, including ASAE 3150 *Assurance Engagements on Controls*. We do not suggest use of the term control framework as this is the framework (such as COSO or COBIT), including the control components, used to design the controls, rather the controls themselves.

## 2. Compliance Framework as a Subject Matter

The manner in which the term compliance framework, meaning controls as discussed above, is used in the standard suggests that controls are included in the subject matter of compliance engagements. However the subject matter in these engagements is the compliance activities to meet the compliance requirements, not the controls over those compliance activities. We consider that the subject matter of a compliance engagement relates to compliance with requirements only and not controls over compliance.

The objective of a compliance engagement is to obtain assurance “about whether the entity has complied in all material respects with compliance requirements as evaluated by the suitable criteria”. However ED 04/16 repeatedly makes reference to “material deficiency in the compliance framework”, implying that the objective of the engagement also includes identification of material deficiencies in the “compliance framework”, that is the controls relating to compliance. We do not consider that the objective of the engagement includes concluding on the “compliance framework” as defined or controls therein. Even if maintenance of effective controls to ensure compliance with requirements is a compliance requirement itself, reference to controls as part of the subject matter is still not necessary in the proposed standard.

In order to remove reference to compliance framework as part of the subject matter of the proposed standard, we suggest that:

- a. Reference to compliance framework is removed from the definition of materiality and that materiality is applied directly to compliance activities and identified deficiencies and not to deficiencies in the compliance framework/controls.
- b. Deficiencies in compliance framework/controls would not normally be accumulated as such, only deficiencies in compliance.
- c. If the assurance practitioner believes that there are deficiencies in the compliance framework/controls, they would not necessarily need to investigate those deficiencies, but would instead no longer rely on those controls and conduct further substantive testing directly on compliance.
- d. Even though the effectiveness of controls at mitigating the risks of non-compliance need to be evaluated in determining which controls the assurance practitioner intends to rely upon to reduced substantive testing, we consider that additional procedures which the assurance practitioner performs are responsive to the risks of non-compliance and not the risks relating to deficiencies in compliance framework/controls.
- e. The engagement letter examples and modified report examples should not refer to material deficiencies in compliance framework/controls.

## 3. Suitable criteria

We do not consider that the phrase “evaluated by the suitable criteria” which is used throughout ED 04/16, after compliance requirements, is useful or communicates any useful meaning, as paragraph 9 states “the criteria may be the compliance requirements, or a subset thereof” anyway. Consequently, we consider that it simply serves to complicate the proposed standard. Compliance requirements are the criteria for a compliance engagement and whilst they may be broken down into greater detail in order to test the compliance activities, we do not see how repeated use of this phrase aids clarity. In addition, the example engagement letters and reports include “[compliance requirements] evaluated by the [suitable criteria]” requiring both terms to be specified or described. We consider that this would be unnecessarily onerous and in many cases not be possible. For example for a compliance engagement on a SMSF the “compliance requirements” are: SIS Act Sections 17A, 35AE, 35B, 35C(2), 62, 65, 66, 67,67A, 67B, 82-85, 103, 104, 104A, 105, 109 and 126K and SIS Regulations 1.06(9A), 4.09, 4.09A, 5.03, 5.08, 6.17, 7.04, 8.02B, 13.12, 13.13, 13.14 and 13.18AA. We are not clear how the “suitable criteria” could be described in addition to these compliance requirements or add any value to the assurance report on a SMSF.

We suggest that the phrase “evaluated by the suitable criteria” and “using the criteria” should be deleted throughout ED 04/16.

For our comments on specific questions raised in the ED please see Attachment 1, specific paragraphs of ED 04/16 please see Attachment 2 and for our comments on specific Appendices please see Attachment 3.

If you require further information on our views expressed in this submission please contact Claire Grayston on (03) 9606 5183 or at [claire.grayston@cpaaustralia.com.au](mailto:claire.grayston@cpaaustralia.com.au).

Yours sincerely

A handwritten signature in black ink, appearing to be 'Stuart Dignam', with a stylized flourish at the end.

Stuart Dignam  
General Manager, Policy & Corporate Affairs

## **Attachment 1: Response to Specific Questions Raised**

1. *Have applicable laws and regulations been appropriately addressed in the proposed standard?*

Yes.

2. *Are there any references to relevant laws or regulations that have been omitted?*

No.

3. *Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?*

No.

4. *Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?*

Yes.

In addition, we suggest that the requirements reflect direct engagements by ensuring that non-compliance is included as well as misstatements, which are only relevant to attestation engagements where a Statement is provided. For example in paragraphs 17(u) and 50 insert, after “possible misstatement”, “or non-compliance”.

5. *Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?*

Yes.

6. *What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?*

We have not identified any significant additional costs in complying with the proposed standard. Benefits may not be realised in terms of cost savings but the standard provides greater clarity about how to conduct compliance engagements.

7. *Are there any other significant public interest matters that constituents wish to raise?*

No.

## Attachment 2: Comments on Specific Paragraphs

- Para. 3: We suggest that the phrase “*using the criteria*” is unnecessary. Likewise it should be deleted from paragraphs 9 and 17(e).
- Sub-para. 17(q)(i) The use of “matter of”, “matters of” or “matter(s) of” non-compliance is unnecessary and does not aid clarity nor will it be well understood. We suggest the words “matter/s of” are deleted or, if necessary, replaced with “instances of” in this sub-paragraph and throughout ED 04/16, including paragraphs 25(h), 29, 40, 44L, 45R, 51, 54, 55, 63, A27, A28, A29, A30, A33, A45, A46, A49 and Appendix 7 Example 1.
- Sub-para. 17(q)(ii) We consider that materiality is relevant to non-compliance only in a compliance engagement and not to the controls in place to address the risk of non-compliance. We suggest deleting this sub-paragraph: Material in the context of a compliance engagement -
- (ii) *“in relation to the compliance framework and controls – instance(s) of deficiency that are significant in the context of the entity’s control environment and that may raise the compliance engagement risk sufficiently to affect the assurance practitioner’s conclusion.”*
- Para. 32: We understand that this paragraph is equivalent to ASAE 3000, paragraphs 46 and 47, and so we consider that the title to this section needs to be amended. We do not consider that this section does nor should relate primarily to understanding the compliance framework (controls) or compliance requirements. Understanding of the compliance requirements should have been gained in assessing the suitability of the criteria which is addressed in paragraph 23. Understanding of controls is addressed for reasonable assurance engagements but controls do not need to be evaluated necessarily in a limited assurance engagement. Consequently, we suggest that this section should be titled “Obtaining an understanding of the compliance activities and other engagement circumstances”.
- We consider that the wording of this paragraph, both 32L and 32R, should reflect the need to understand the compliance activities. The phrase “entity’s compliance framework and its key elements, the compliance requirements” should be replaced with “entity’s compliance activities to meet the compliance requirements”.
- We do not consider that it is usually necessary in a compliance engagement to select or develop further suitable criteria, so we suggest that sub-paragraphs 32L(a) and 32R(a) are deleted. This requirement is necessary in a controls engagement where identification of the controls which meet the control objectives maybe an involved process.
- It may be necessary to develop a requirement for limited assurance engagements equivalent to paragraph 32R(c), which could be drawn from ASAE 3000 paragraph 47L.
- Para. 40: To remove implied objective regarding controls delete: “*material deficiency in the compliance framework*”.
- Para. A3: We suggest deleting this paragraph as it does not add any further information, and maybe misleading. We do not consider that compliance engagements particularly address “risks, compliance requirements and related controls”. As consideration of risk and controls are simply part of the assurance process not matters addressed in their own right in the same way as a controls engagement must consider them. In addition, the definition of compliance requirements already covers the sources of requirements listed in this paragraph, so there is no need to repeat compliance with these as the “subject matter”.
- Para. A4: We suggest that this paragraph is redundant and so should be deleted. We note that this paragraph is included in ASAE 3150, but controls engagements are quite different to compliance engagements. In a controls engagement identifying the relevant control objectives and controls may be an involved process in a direct engagement where there

is no description of the system. A “description” is mentioned in this paragraph but it is not relevant to a compliance engagement and identification of the compliance requirements in an attestation versus a direct compliance engagement is not typically significantly different.

- Para. A9(b): This sub-paragraph does not fit grammatically after “An appropriate subject matter is:”, so we suggest deleting “Such that the information about it can” and replace with “Able to”.
- Para. A26 To remove implied objective regarding controls delete: “*deficiencies in the compliance framework*”.
- Para. A28 To remove implied objective regarding controls delete: “*deficiencies in the compliance framework*” and “*deficiencies or matters of*”.
- Para. A33: The term compliance requirements should be used consistently throughout ASAE 3100. However, in paragraph A33 the term “obligations” has been used several times in place of “requirements”. We suggest that it is replaced.
- Para. A35: Sub-paragraphs (a) and (b) would benefit from linking more directly to the compliance requirements, by using terms such as “controls over compliance”, “fraud with respect to compliance” or “ethical behaviour with respect to compliance”.
- Para. A38: We suggest deleting the last sentence: “*In the case of an attestation engagement, such procedures may include asking the responsible party to examine the matter identified by the assurance practitioner, and to make amendments to the description or Statement, if appropriate.*” We consider that this sentence is not relevant as a description is not normally prepared in a compliance engagement and the Statement does not normally include a level of detail about the compliance activities which would necessitate amendments.
- Para. A39: To remove implied objective regarding controls delete: “*deficiencies in the compliance framework*”.
- Para. A42(b) To remove implied objective regarding controls delete: “*material deficiency in the compliance framework*”.
- Sub-para. A59(b)(iii) We suggest deleting this sub-paragraph as it states that an adverse conclusion may be issued if there is a material and pervasive “*Systemic deficiency in the compliance framework*”. We do not consider that deficiencies in the compliance framework (controls) can directly impact the assurance practitioner’s conclusion. If there are deficiencies in the controls which the assurance practitioner intended to rely upon, then the assurance practitioner cannot rely on those controls and will need to instead conduct further substantive testing sufficient to conclude as to whether or not material non-compliance exists, regardless of the adequacy or inadequacy of controls.

### Attachment 3: Comments on Specific Appendices

Appendix 1: We suggest that this diagram could reflect the information more accurately and clearly by:

- Replacing “Compliance activity to meet the Compliance Requirements” with simply “Compliance Activities”.
- Deleting the box for “Attestation Statement” and renaming the box “Compliance outcome” as “Statement” with the arrow to it labelled “attestation engagement”.
- Deleting the box for “Direct Conclusion”, as this is already represented by the box “Compliance Assurance Report”, and inserting a new arrow from the Criteria box to Compliance Assurance Report box labelled “direct engagement”.

We suggest that the phrase “using the criteria” as it is unnecessary.

Appendix 2: Delete “(a)” after “objective”.

We suggest deleting the row “Compliance requirements” as this is not a term used in ASAE 3000 there is no need to explain the equivalent term in ASAE 3100 and it is already defined in paragraph 17(f).

We suggest moving the terms “compliance outcome” and “compliance activity” from column 1 to column 3 to make it clear which terms relate to the definitions provided.

We suggest deleting the phrase “*using the criteria*” from the row subject matter information vs compliance outcome and column ASAE 3100, as it is unnecessary.

Appendix 4: We suggest deleting the rows 4 and 5 as we do not see the relevance of service organisation’s controls and controls over economy, efficiency or effectiveness to compliance engagements nor the need to explain that ASAE 3100 is not relevant.

Appendix 5: The assurance practitioner’s conclusion in an attestation engagement may be phrased not only in terms of the responsible party’s Statement, but alternatively it may be phrased in terms of the underlying subject matter and the applicable criteria. Therefore, we suggest that it would be helpful to provide the alternative wording in the engagement letter. For example, alternative wording could be added to the phrases:

- “ABC’s Statement is fairly stated” add alternative “/ABC complied with the [compliance requirements]”.
- “Misstatements in ABC’s Statement” add alternative “/non-compliance with the [compliance requirements]”.

Paragraph 2, page 45; paragraph 5, page 47 and paragraph 5, page 49 discuss inherent limitations of the engagement, however as this is not a controls engagement we consider that references to internal controls should be deleted including: “*together with the inherent limitations of any system of internal control*”, “*deficiencies in the compliance framework*” (already raised above) and “*Therefore no opinion will be expressed as to the effectiveness of the system of control as a whole*”. In addition, with respect to example 1, we note that in a limited assurance engagement the assurance practitioner is not required to evaluate controls as they are required to do in a reasonable assurance engagement.

Paragraph 4, page 45; paragraph 6, page 47 and paragraph 1, page 50 - We suggest deleting or truncating sub-paragraphs (c) and (d) as these are matters which the responsible party has to address in an attestation controls engagement in order to prepare a description of the system of controls, but we do not consider that these need to be detailed to such an extent in a compliance engagement.

Paragraph 2, page 46 & paragraph 4, page 48 - The bracketed section on period and date do not flow grammatically and could be amended to: “*[the specified period or will be as at a specified date]*”

Paragraph 3, page 46 - States that the assurance report will be attached to ABC's Statement but in sub-paragraph 4(a), page 45, it states the opposite, that the Statement will be attached to the assurance report. Likewise paragraph 5, page 48 is inconsistent with paragraph 6(a), page 47. We do not have a preference but it needs to be amended to be consistent.

Paragraphs 4 and 5, page 46; paragraphs 6 and 7, page 48 and paragraphs 4 and 5, page 50 - we suggest using the future tense as the report will be prepared in the future.

Example 1: Paragraph 4, page 44 - The description of the procedures which the assurance practitioner will perform in should align with the procedures described in the requirements, specifically paragraph 43L. Paragraph 43L lists discussion, observation and walk-through but does not include examination of documentation nor uses the term enquiries.

Paragraphs 1 & 2, Page 45 - To remove implied objective regarding controls delete: *"deficiencies in the compliance framework"*.

Paragraph 3, page 45 - We suggest deleting the phrase *"any material deficiencies in the compliance framework and relevant controls that exist may not be revealed by the engagement"* as this is not the objective of the engagement and replace with *"non-compliance may not be detected"* or *"misstatements in the Statement may not be detected"*.

Paragraph 3, page 45 - we query the need for the last sentence *"In expressing our conclusion, our report on ABC's Statement of compliance with the [compliance requirements] as evaluated by the [suitable criteria] will expressly disclaim any reasonable assurance conclusion on the compliance framework and relevant controls."* And suggest it could be deleted.

Paragraph 3, page 45 - To remove implied objective regarding controls delete: *"any material deficiencies in the compliance framework and relevant controls"* and replace with the objective of a compliance engagement being *"non-compliance with the compliance requirements"*.

Example 2: Paragraph 4, page 47 - We suggest deleting the words *"and controls implemented"* in as this is not the objective of a compliance engagement.

Paragraphs 4 & 5 page 47 - To remove implied objective regarding controls delete: *"deficiencies in the compliance framework"*.

Example 3: Paragraphs 4 & 5, page 49 - To remove implied objective regarding controls delete: *"deficiencies in the compliance framework"*.

Appendix 6: Paragraphs 1, page 53; paragraph 4, page 55 & paragraph 4, page 57 - As noted above for the engagement letters, we suggest deleting or truncating sub-paragraphs (c) and (d) as these are matters which the responsible party has to address in an attestation controls engagement in order to prepare a description of the system of controls, but we do not consider that these need to be detailed to such an extent in a compliance engagement, particularly for direct compliance engagements.

Paragraph 3, page 54; paragraph 4, page 56 and paragraph 4, page 58 - We suggest using the term compliance requirements rather than laws and regulations for consistency with the requirements.

Paragraph 4, page 54, paragraph 5, page 56 and paragraph 5, page 58 – These examples need to allow for engagements which cover a specified period not only a specified date by including the phrase *"throughout the period/".*

Example 1: Paragraph 4 and 6, page 53 - As noted above for example 1 of the engagement letters, the description of the procedures which the assurance practitioner performed should align with the procedures described in the requirements, specifically paragraph 43L.

Paragraph 43L lists discussion, observation and walk-through but does not include examination of documentation or inspection nor uses the term enquiries.

Appendix 7: The explanation prior to the examples states that they are based on Appendix 6 but they do not seem to be in the same order and so it is not clear how they relate. We suggest deleting this statement or aligning the examples.

Example 1: The title requires amendment as it is not possible for non-compliance to be identified with ABC's Statement. We suggest the title either state that material non-compliance by ABC with the compliance requirements was identified or ABC's Statement was materially misstated.

Under the basis for qualified opinion it states that "We are unable to satisfy ourselves by alternative procedures", which suggests that the assurance practitioner was unable to obtain sufficient appropriate evidence. However the title says it is an example of material non-compliance, in which case the "trustee bank account and cash book procedures" presumably required by the compliance requirements were not complied with. The basis for qualified opinion needs to be amended to reflect this conclusion.

Example 2: This title requires amendment as compliance requirements cannot be non-compliant. Instead ABC could be non-compliant.

We do not see that specifying "RSE" in this example is necessary, especially without defining this acronym, and so we suggest using ABC as in the other examples.

Example 4: The title suggest that this example seems to be seeking to illustrate when the assurance practitioner could not obtain sufficient appropriate evidence, however this is not clear from the basis for qualified conclusion paragraph. That paragraph states that material non-compliance was identified. The paragraph needs to be redrafted to address the intended reason for the qualification and needs to include the words "We were unable to obtain sufficient appropriate audit evidence about".



26 October 2016

Merran Kelsall FCA  
 The Chairman  
 Australian Auditing and Assurance Standards Board  
 PO Box 204  
 Collins Street West  
 Melbourne 8007

*Submission via website*

Dear Merran

## **Submission on Exposure Draft 04/16: Proposed Standard on Assurance Engagements ASAE 3100 Compliance Engagements**

Chartered Accountants Australia and New Zealand (CA ANZ) welcomes the opportunity to comment on the Exposure Draft ("the ED"). We commend the Australian Auditing and Assurance Standards Board (AUASB) for taking this opportunity to work with the New Zealand Auditing and Assurance Standards Board (NZAuASB) to jointly develop this proposed standard. Our responses to the specific questions raised in the paper are set out in Appendix A. Appendix B includes more information about CA ANZ.

### **General Comments**

We recognise the increasing prevalence of, and demand for, compliance engagements and support the collaborative efforts to establish requirements and provide application and other explanatory material in this regard. We note that while there are requirements for compliance engagements in some jurisdictions, there is no similar comprehensive pronouncement internationally. Given that the increasing importance of compliance engagements is an international trend, we recommend and support the promotion of the final standard with international standard setters.

### **Materiality**

One of the most challenging aspects of a compliance engagement in practice is materiality, both in the planning stages to determine what a material instance of non-compliance is and in evaluating the instances of non-compliance to determine whether the assurance practitioner's conclusion should be modified. The assurance practitioner must apply professional judgement to understand the needs of the intended users and what is material to them, to consider largely qualitative factors to determine materiality and to evaluate when instances of non-compliance should be considered to be pervasive when determining the nature of a modification to their conclusion.

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Because compliance engagements are becoming increasingly prevalent in areas such as the not-for-profit sector where compliance requirements may be included in grant agreements, these engagements may be performed by a range of assurance practitioners and their experience considering materiality in non-financial assurance potentially varies widely.

The revised ASAE appears to have slightly less material on materiality than extant ASAE 3100. Given that the correct application of materiality is key to these engagements and challenging for practitioners, we encourage the board to consider whether further material to assist practitioner's with applying materiality in compliance engagements can be included either in the standard or provided as guidance material in another format.

## **Terminology**

We note that the ED introduces several new terms to describe the various aspects of a compliance engagement. While we understand that these are useful concepts to assist the assurance practitioners to perform the engagements, we found the definitions to be somewhat confusing when reading the standard. The guidance in the Appendices assists in clarifying the differences between the compliance activity, the compliance outcome, the compliance requirements and the criteria, however, we believe it would be useful for practitioners if an additional appendix (in diagram format) was included that demonstrates how all these aspects of a compliance engagement, as well the compliance framework fit together.

Should you have any queries concerning the matters in this submission, or wish to discuss them in further detail, please contact Geraldine Magarey (Acting Audit and Insolvency Leader) via email at [geraldine.magarey@charteredaccountantsanz.com](mailto:geraldine.magarey@charteredaccountantsanz.com) or phone 02 9290 5597.

Yours sincerely

**Rob Ward FCA AM**

Head of Leadership and Advocacy

## **Appendix A: Responses to specific questions**

### **1. Have applicable laws and regulations been appropriately addressed in the proposed standard?**

We believe they are adequately addressed.

### **2. Are there any references to relevant laws or regulations that have been omitted?**

We do not believe so. The inclusion of some common kinds of Australian regulatory compliance engagements in Appendix 3 is useful. It may also be useful to include an example in this Appendix which is not regulation driven, such as compliance with the requirements of a bank covenant to reinforce the point that compliance engagements may be requested by a client due to requirements other than regulation or legislation

### **3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

Not that we are aware of.

### **4. Is there a need for the proposed standard to address both direct and attestation engagements? If yes, are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?**

We understand direct engagements are more prevalent in practice, but we agree there is a need for the proposed standard to address both direct and attestation engagements.

In our view the differentiation between a direct and an attestation engagement could be clearer. We recommend an overarching statement to the effect of “If this ASAE makes reference to a requirement, that requirement shall be applied to both attestation and direct engagements, unless specified otherwise” similar to the statement regarding ASAE 3000 in paragraph 18. Furthermore, we recommend the removal of the following superfluous statements:

- Paragraph 17(s) [definition of ‘non-compliance’] - “for both attestation and direct engagements on compliance...”
- Paragraph 56 - “for attestation engagements and shall also apply those requirements for direct engagements”
- Paragraph 57 - “For both attestation and direct engagements”

### **5. Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?**

We support the approach taken in this aspect of the ED. We recognise there are challenges involved in articulating requirements to achieve a meaningful level of assurance in a limited assurance compliance engagement, while still differentiating appropriately from a reasonable assurance compliance engagement. However, we believe that the proposed standard is a useful starting point.

**6. What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?**

We have not assessed the cost implications of the proposed standard. However, it is likely that there will be additional costs in complying with revised standard when compared to the extant standard due to the revised approach and greater detail in the requirements. However, the quality of the compliance engagement is likely to increase as a result of applying the enhanced requirements in the proposed standard. Therefore, we believe that the benefits outweigh the costs.

**7. Are there any other significant public interest matters that constituents wish to raise?**

We have no other significant public interest matters to raise. However, we do have the following minor drafting points we wish to raise for your consideration:

- a) The definition of 'misstatement' in paragraph 17(r) only refers to attestation engagements and differences between the statement and the assurance practitioner's evaluation of compliance with the compliance requirements. However, paragraph 49 includes a statement that a misstatements are "instances of non-compliance with the compliance requirements". Therefore there is a conflict in the definition between the two paragraphs. We recommend that the definition in 17(r) be expanded to define misstatement in the context of both a direct and an attestation engagement. The sentence defining misstatements in paragraph 49 could then be removed or amended to refer to the definitions in 17(r).
- b) Paragraph 61 on modified conclusions and paragraph 62 on scope limitation may be better placed under Forming the Assurance Conclusion with paragraphs 54-55.

## **Appendix B: About Chartered Accountants Australia and New Zealand**

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations. We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation accounting professionals across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.



Merran Kelsall  
The Chairman  
Auditing and Assurance Standards Board  
PO Box 204  
Collins Street West  
Melbourne VIC 8007

24 October 2016

Dear Ms Kelsall

**Exposure Draft 04/16: Proposed Standard on Assurance Engagements ASAE 3100  
Compliance Engagements**

We appreciate the opportunity to comment on the above mentioned Exposure Draft.

We have included our responses to the specific questions included in the Request for Comment in the Appendix to this letter.

We would be pleased to discuss our comments with you. Please contact Avril Trent on (02) 8266 8097 should you require any further information.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Valerie Clifford', with a large, stylized flourish at the end.

Valerie Clifford  
Assurance Risk & Quality Leader



## Appendix

### Response to the Request for Comments questions: ED 04/16

- 1. Have applicable laws and regulations been appropriately addressed in the proposed standard?**

Yes

- 2. Are there any references to relevant laws or regulations that have been omitted?**

None noted.

- 3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

None noted. However, there are a number of Guidance Statements that include references to the requirements of ASAE 3100. These will need to be reviewed and revised where necessary.

- 4. Are the considerations for conduction a direct engagement adequately differentiated from an attestation engagement?**

Yes.

- 5. Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?**

Yes, the procedures are adequately distinguished.

- 6. What, if any are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the e requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?**

No significant additional costs expected.

- 7. Are there any other significant public interest matters that constituents wish to raise?**

None noted.

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The Chairman  
Auditing and Assurance Standards Board  
PO Box 204  
Collins Street West  
Melbourne Victoria 8007

2 November 2016

Dear Ms Kelsall,

**Re: Exposure Draft ED 04/16 Proposed Standard on Assurance Engagements ASAE 3100  
*Compliance Engagements.***

Deloitte Touche Tohmatsu (Deloitte) is pleased to respond to the Australian Auditing and Assurance Standards Board (AUASB) on Exposure Draft ED 04/16 Proposed Standard on Assurance Engagements ASAE 3100 *Compliance Engagements (ED 04/16)*.

We support the issuance of an updated standard to replace the current ASAE 3100 in order to align and be consistent with ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* standards issued by the AUASB as well as provide clear and useful guidance to users.

We have an overall concern that the standard may not achieve the desired outcome and the simplicity of the current standard achieves this. In addition, we question whether there is sufficient clarification as to what is required when reporting on compliance at a specific date versus when you are performing an engagement to report on compliance throughout the period.

We have responded to the specific questions posed in ED 04/16 below and Appendix 1 contains our detailed comments with respect to ED 04/16.

**Specific questions posed in ED 04/16**

1. *Have applicable laws and regulations been appropriately addressed in the proposed standard?*

Yes, it appears that all the relevant applicable laws and regulations have been appropriately addressed.

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Member of Deloitte Touche Tohmatsu Limited

2. *Are there any references to relevant laws or regulations that have been omitted?*

No, we have not identified any omitted references to relevant laws and regulations.

3. *Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?*

We are not aware of any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard.

4. *Are the considerations for conducting a direct engagement adequately differentiated from an attestation engagement?*

Yes, the considerations for conducting a direct engagement adequately differentiated from an attestation engagement.

5. *Are the procedures required for limited and reasonable assurance appropriate and adequately distinguished?*

Yes, the procedures required for limited and reasonable assurance are appropriate and adequately distinguished.

6. *What, if any, are the additional significant costs to/benefits for assurance practitioners and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of compliance engagements?*

We are not aware of any additional costs to/benefits for assurance practitioners and business community.

7. *Are there any other significant public interest matters that constituents wish to raise?*

No, there are no other significant public interest matters we wish to raise.

We would be pleased to discuss our comments with members of the Board or its staff. If you wish to do so, please do not hesitate to contact me on 02 9322 3434.

Yours sincerely,



Gareth Bird

Partner

Deloitte Touche Tohmatsu

## APPENDIX 1: Proposed Additional Editorial Amendments

ED 04/16 Paragraph	Amendment
17 (u)	<p>Proposed definition of Professional scepticism reads <i>“An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement, and a critical assessment of evidence.”</i></p> <p>This is inconsistent with the definition in ASA 200 which reads “Professional scepticism means an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement <u>due to error or fraud</u>, and a critical assessment of audit evidence.</p>
39	<p>We recommend that paragraph 39 is redrafted as follows <i>“The assurance practitioner shall design and perform further procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement, having regard to the level of assurance, reasonable or limited, as appropriate”</i>. This construct is consistent with that used in paragraph 36 of ASAE 3410.</p>
42	<p>As noted in our overall comments we believe that paragraph 42 needs to better distinguish, for the assurance practitioner, the differences in evidence required when reporting on compliance throughout the period versus when reporting on compliance at a specific date. We do not believe that the application material in paragraph A38 achieves this.</p>
43L and 43R	<p>This tabular information contains the words <i>“shall ordinarily”</i>. The use of the word ordinarily is not appropriate in a requirement paragraph.</p> <p>In addition, the procedures listed which are currently separated by a comma could be better displayed as per ASAE 3150 par 54R.</p>
49	<p><i>“ASAE 3000 requires the assurance practitioner to accumulate uncorrected misstatements identified during the engagement other than those that are clearly trivial. Misstatements in a compliance engagement are instances of non-compliance with the compliance requirements.”</i></p> <p>We recommend inserting the words “qualitative and quantitative” after uncorrected misstatements in the paragraph. However we understand this is the exact wording per ASAE 3000.</p>
50	<p><i>“Evaluation of evidence obtained by the assurance practitioner shall include any impact of corrected misstatements identified during the compliance engagement.”</i></p> <p>We believe that an application guidance paragraph is needed to explain to the practitioner that the overall opinion is based on not only the uncorrected misstatements but also on the extent of corrected misstatements. The extent of corrected misstatements may lead a practitioner to conclude that compliance has not been achieved.</p>
A17 (c)	<p>This paragraph states <i>“It is more cost effective for the entity to identify the specific compliance activities, requirements and related controls, evaluate the compliance outcome as the basis for an attestation engagement, rather than it being necessary for the assurance practitioner to do so in a direct engagement.”</i></p>

	<p>We question why this an assurance practitioner's consideration? We believe that it is more the engaging party's consideration. We recommend that this sentence is re-written to clarify its purpose.</p>
A20	<p>We believe that this paragraph could be simplified if it was redrafted as follows:</p> <p><i>Where relevant, the terms of the engagement could also include a reference to, and description of, the auditor's responsibility in accordance with;</i></p> <ul style="list-style-type: none"> <li>· <i>applicable law,</i></li> <li>· <i>regulation or relevant ethical requirements, and</i></li> <li>· <i>reporting obligations to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is required or appropriate in the circumstances.</i></li> </ul>
A22	<p>"An example engagement letter is contained in Appendix 5."</p> <p>As there is more than one engagement letter, we propose the following: Example engagement letter(s) are contained in Appendix 5.</p>
A29	<p>"...the evaluation of compliance with the compliance requirements, and the interests of the intended users..."</p> <p>The comma after the word requirements should be removed so that the sentence reads, 'the evaluation of compliance with the compliance requirements and the interests of the intended users'.</p>
A35 (d)	<p>This paragraph states '...and the internal control that management has established to mitigate these risks as far as they relate to the compliance requirements...'.</p> <p>The paragraph appears to assume that management has only one internal control to mitigate the risks related to the compliance requirements.</p> <p>We propose that it is amended as follows "... and the internal controls that management have established to mitigate these risks as far as they relate to the compliance requirements;</p>
A45	<p>Within the text there is the following - <i>Error in reference (Ref: Para. 49-<b>Error! Reference source not found.</b>)</i> This needs to be corrected.</p>
A46	<p>Reference to paragraph 44 is incorrect as the content of paragraph A46 only relates to paragraph 44 L</p>
Appendix 2	<p><b>Objective (a)</b> – the '(a)' should be deleted.</p>
Appendix 3	<p>Under the heading there is a description stated "<b>Scope of the Engagement</b>" which is already included in the table, therefore we recommend removing.</p>
Appendix 3	<p>Page 42 is missing Appendix number and headers</p>
Appendix 5	<p>Page 49 – "To [the appropriate addressee]:" should be in italics to be consistent with the other engagement letters.</p>



# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **3**

Meeting Date: 29 November 2016  
Subject: Audit Committee Guide Revision  
Date Prepared: 15 November 2016

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☒ Action Required

☐ For Information Purposes Only

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## Objective:

To present to the AUASB, and to receive AUASB input on the first draft of the Audit Committee Guide Revision as prepared by the three authors, the Australian Institute of Company Directors (AICD), the Institute of Internal Auditors Australia (IIA) and the Australian Auditing and Assurance Standards Board (AUASB).

## Background:

At the 26 July 2016 AUASB meeting, the AUASB approved a project plan for all three authors, AICD, IIA and the AUASB, to work jointly, to take into account changes in the regulation and operation of audit committees since the guide was last issued in February 2012.

This project is a high level update/revision only – the project is not intended to be a re-write.

The colour coded table of contents (Agenda Item x.1) has been provided and sections highlighted yellow are the AUASB allocated work areas.

## Extract of timetable – AUASB input/timing:

August – October 16: Working group members complete each section as noted above.

**AUASB: 25 October AUASB meeting – AUASB allocated sections only presented to AUASB**

Nov – Dec 2016: Draft sent out for review and review comments received by mid-December

**AUASB: 29 November AUASB meeting – First Draft of full revision**

February 2017 Review comments incorporated and Draft 2 sent out for review (including ASIC review)

**AUASB: 1 March AUASB meeting – Second Draft of full revision**

### **AUASB Technical Group Comments**

Bearing in mind that the target audience is audit committees, and that content needs to be appropriate for that audience, there are several issues that will need resolution in relation to 4 particular sections: Responsibilities of the Audit Committee (except for the piece on external audit); Internal Auditor role and responsibilities, Glossary and new Appendix 4. These matters relate to:

1. general: granularity of content and appropriateness to target audience;
2. potential confusion around the usage of the term “assurance” under the responsibilities of the audit committee section (pages 14/15 clean, page 17 in mark up);
3. granularity and content used in the controls risk management section (pages 21-24 clean, pages 27-30 mark up);
4. content and relevance to audit committees of appendix 4 (page 54 clean, page 63 mark up)

### **Material Presented**

Agenda Item 3	AUASB Board Meeting Summary Paper
Agenda Item 3.1	Colour coded table of contents
Agenda Item 3.2	Draft 1 Audit Committee Guide (mark up)
Agenda Item 3.3	Draft 1 Audit Committee Guide (clean)

---

### **Action Required**

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	Input	Input	AUASB	29 November 2016	

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**BLUE: AICD**  
**GREEN: IIA**  
**YELLOW: AUASB**

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**AUDIT COMMITTEES**  
**A GUIDE TO GOOD PRACTICE**  
~~23rd~~ Edition

A joint publication from the Auditing and Assurance Standards Board, Australian Institute of  
Company Directors and The Institute of Internal Auditors-Australia

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### Related publications:

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## Introduction

An audit committee is a committee of a board of directors (board), operating under delegation of authority from the board. Its objectives are clearly defined and documented in its charter and its efficiency and effectiveness is measured by reference to its objectives.

An independent audit committee is a fundamental component of good corporate governance.<sup>1</sup>

Typically, an audit committee:

1. focuses on issues relevant to the integrity of an entity's financial reporting
2. oversees external audit, internal audit, risk management, internal control and compliance
3. liaises with the board, internal and external auditors<sup>2</sup> and management.

Some entities establish one committee with the responsibility for all of these tasks, such as an audit and risk management committee. Other entities may establish more than one committee, such as an audit committee, together with a risk and compliance committee, health and safety committee, environmental management committee and other committees. This depends on the nature of the entity, but is more common in larger entities due to the increased work load.

## Who should use this guide?

This guide is primarily for directors and audit committees of Australian listed companies. Directors, boards of management and audit committees of not-for-profit, public sector<sup>3</sup>, and other private sector entities, may also find this guide to be a useful reference.

There is no "one size fits all" good practice solution for audit committees. The nature of the business, the regulatory environment, ownership structure, legal requirements, and audit committee membership influence the objectives and activities of an audit committee. Smaller entities with limited resources might find it impractical to meet all of the practices outlined in this guide. They may use this guide to assess the elements of good practice that are relevant for their financial reporting, corporate governance, risk management and internal control and exercise them at the board or committee level.

## Purpose of this guide

This guide provides a practical introduction to the role and responsibilities of an audit committee. It explains the context in which an audit committee typically operates and outlines good practice.

While the guide assists the board and audit committee members, it may also be helpful to risk and compliance managers, internal auditors, external auditors and senior management, as it demonstrates the interactions between the audit committee and these other parties.

Clarifying the roles and responsibilities between the audit committee, risk and compliance managers and auditors (both internal and external) assists their communication, efficiency and effectiveness. Using this guide assists audit committees in assessing an entity's external

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<sup>1</sup> See Principle 4 *Safeguard Integrity in ~~Financial Corporate~~ Reporting*, Recommendation 4.1 of the ~~3<sup>rd</sup> edition of the~~ ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*, ~~with 2010 Amendments~~.

<sup>2</sup> See glossary for definitions.

<sup>3</sup> Federal and state bodies should also consider their own specific guidance relating to the operation of their audit committees.

financial and other internal and external reporting requirements. It also assists in assessing the effectiveness of an entity's risk management and internal control systems.

This ~~second-third~~ edition of the guide reflects developments in audit committee practice, legislation and guidance from regulatory bodies and in leading global board practices since the previous edition was published in 2012~~08~~. It has been produced by the Auditing and Assurance Standards Board, the Australian Institute of Company Directors and the Institute of Internal Auditors—Australia.

The guide does not attempt to advise directors or members of audit committees about their legal duties. For a general discussion of directors' duties refer to *Duties and Responsibilities of Directors and Officers 21~~st~~0th* Edition by Professor Robert Baxt AO, published by the Australian Institute of Company Directors in 2016~~2~~.

### Recent developments regarding audit committees

Since the previous edition of this guide was published in 2012~~08~~, some of the key developments in Australia include:

- ~~November 2009—the Australian Prudential Regulation Authority (APRA)<sup>4</sup> issued revised Prudential Standards on governance for APRA-regulated institutions. These standards outline the governance arrangements for authorised deposit-taking institutions and for life and general insurance entities and include requirements for board audit committees and board risk committees.~~
- ~~January-December 2016~~—revised Australian Auditing Standards came into effect, some of which impact the operation of audit committees as they change the requirement in relation to the auditor reporting to the board. For example, Auditing Standard ASA 700 series, including the new ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report* ~~260~~ and related consequential changes to other relevant audit standards, such as ASA260 *Communication with Those Charged with Governance* and ASA 570 *Going Concern*. introduced new requirements for auditor reporting to the board, including the audit committee.
- ~~March-June 2014~~—the ASX Corporate Governance Council<sup>5</sup> released the 3<sup>rd</sup> edition of the ASX Corporate Governance Principles and Recommendations-with 2010 Amendments. These revised guidelines came into effect from 1 ~~January-July 2014~~.
- October 2010—The Institute of Internal Auditors Inc. (IIA) issued a revised International Professional Practices Framework (IPPF). The IPPF has been adopted by the Institute of Internal Auditors-Australia (IIA-A) and was effective from 1 January 2011.
- ~~August 2011—the Australian National Audit Office (ANAO) published its revised better practice guide, *Public Sector Audit Committees*.~~
- ~~September-January 2014~~—APRA released a new revised consolidated Prudential Standard CPS 510 *Governance*, which came into effect on 1 ~~July-January 2015~~ and replaces the previous prudential standard on governance. was introduced along with the new CPS 220 *Risk Management*.
- ~~June 2012—the Corporations Legislation Amendment (Audit Enhancement) Act 2012 made changes to the Corporations Act 2001 and the Australian Securities and Investments Commission Act 2001 (ASIC Act) that are relevant to audit committees.~~

<sup>4</sup> APRA Prudential Standards on governance for regulated institutions are available through APRA's website [www.apra.gov.au](http://www.apra.gov.au).

<sup>5</sup> The ASX Corporate Governance Council was formed in August 2002 and brings together various business, shareholder and industry groups to enhance corporate governance practices in Australia. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be a practical guide for listed entities, their investors and the wider Australian community.

~~The new provisions relate to extending the rotation period for the external audit engagement partner, subject to certain requirements; annual transparency reports to be published by external auditors in certain circumstances; audit deficiency reports that may be published by the Australian Securities and Investments Commission (ASIC) in certain circumstances; and new powers for ASIC to communicate directly with the audit committee, the board or senior management of an entity in certain circumstances.~~

~~Mainly due~~ Since the ~~ongoing~~ global financial crisis, there has been continuing focus on corporate governance around the world. This has resulted in the review of existing governance frameworks, including accounting and auditing frameworks and regulatory reforms, to strengthen corporate governance.

Businesses, regulators, investors and the members of the public have increasingly called for more transparency in corporate reporting.

The audit committee plays a pivotal role in assisting the board in fulfilling its corporate governance obligations and enhancing the integrity and transparency of corporate reporting, particularly financial reporting, and consequently, some of the proposed reforms relate to clarifying and expanding the role of the audit committee.

## The board and board committees

Under the *Corporations Act 2001* in section 201A, every company must have at least one director and public companies must have at least three directors.<sup>6</sup> Collectively, the directors are known as the board of directors (board) and its overriding responsibility is to supervise the company on behalf of shareholders and other stakeholders.

The boards of larger entities often establish committees of directors to better use their time and to help deal with complex or specialised areas, such as financial reporting and audit, compliance, risk management, sustainability or health and safety.

Committees make recommendations for action to the full board, which retains collective responsibility for decision-making.

Involvement in committees allows directors to deepen their knowledge of the organisation, become more actively engaged and fully utilise their experience. Additionally, the existence of committee can indicate to investors that the board is taking particular issues seriously.

Examples of committees include audit, risk, remuneration, nomination and investment committees. The nature and type of committees will vary from industry to industry and according to the size of the organisation. For example, a resources company may have an environmental committee, an airline may a safety committee, a charity may have a fundraising committee.

Committees may be ongoing in nature like the audit committee, usually referred to as standing committees, or may be formed for a specific short term project or goal.

Section 198D of the Corporations Act 2001 allows boards to delegate some of their powers to a committee of directors unless the company's constitution disallows it. The delegation must be recorded in the minute book.

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<sup>6</sup> This requirement does not include alternative directors, and two of the three directors (one for proprietary companies) need to ordinarily reside in Australia.

Section 190 provides that, when directors delegate a power under s198D of the Corporations Act 2001 they remain responsible for the exercise of the power by the delegate as if it had been exercised by the directors themselves. There is a limited exception where the director who delegates will not be held responsible if that director believed:

- On reasonable grounds at all times that the delegate would exercise the power in conformity with the duties imposed by the Act and the company's constitution; and
- On reasonable grounds and in good faith (and after making proper inquiries if circumstances so required) that the delegate was reliable and competent in relation to the power delegated.

Section 189 gives authority for the rest of the board to reasonably rely on the information or advice given by a committee so long as it is independently assessed by the board and is relied upon in good faith. However, this delegation of authority does not lessen the board's overall duties and responsibilities.

The 3<sup>rd</sup> edition of the ASX Corporate Governance Council's Principles and Recommendations recommends that the board establish three committees – audit, remuneration and nomination. In addition it recommends that boards should have a committee or committees to oversee risk. In some cases this function is combined with the audit committee. In other cases it is a standalone committee of the board.

Similarly, APRA's prudential standards include the establishment of the audit committee and a remuneration committee. These requirements are imposed on authorised deposit taking institutions (or example banks, building societies and credit unions) and general and life insurers as well as regulated superannuation funds.

~~The audit committee plays a key role in assisting the board to fulfil its corporate governance and oversight responsibilities. These responsibilities can include an entity's financial reporting, risk management and internal control, compliance, the internal audit activity<sup>7</sup> and external audit. For example, the audit committee may assist the board in achieving the following objectives of the entity:~~

~~Facilitating well-informed, efficient and effective decision making, particularly by the board~~

~~Promoting and monitoring an ethical culture throughout the entity~~

~~Ensuring a code of conduct is appropriately designed and implemented and compliance with the code is monitored~~

~~Implementing an effective system of risk oversight and management, which may typically include:~~

~~policies dealing with material business risks, clearly describing the roles and responsibilities~~

~~of the board, audit committee, management and internal audit activity~~

~~documenting the entity's risk profile and the risk appetite of the board~~

~~effective reporting of material business risks~~

~~ongoing monitoring of the entity's risk profile~~

~~risk-based internal audit plans~~

~~Implementing an effective and efficient internal control system, including:~~

~~a strong control environment, commensurate with the risk appetite of the board~~

~~identification and management of risk~~

~~adequate design and operation of business policies and procedures to safeguard assets,~~

~~protect against fraud and comply with applicable laws, regulations and standards~~

~~ongoing monitoring of internal controls~~

~~an independent, internal audit activity to provide assurance over the internal control systems~~

~~timely responsiveness to internal and external audit recommendations to enhance the~~

~~internal control environment~~

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<sup>7</sup>See glossary.

~~Ensuring high quality internal and external reporting (financial and non-financial), including:  
 complete, timely, accurate and useful information  
 appropriate accounting policies and procedures  
 reasonable judgements and estimates  
 Obtaining an independent, effective and efficient external audit  
 Promoting effective communication between the board and the internal and external auditors, and providing timely and appropriate responses to matters arising from audits.~~

## Role of the audit committee

The audit committee plays a key role in assisting the board to fulfil its corporate governance and oversight responsibilities in areas such as:

- corporate reporting, including external financial reporting, the directors report and annual report
- external audit
- internal audit
- risk management and internal control
- compliance and ethics
- activities to prevent, deter, detect and report on fraud.

These responsibilities can include an entity's financial reporting, risk management and internal control, compliance, the internal audit activity<sup>8</sup> and external audit.

The main objectives of an appropriately established and effective audit committee may include assisting the board to discharge its responsibility to exercise due care, diligence and skill in relation to the following areas:

- Facilitating well-informed, efficient and effective decision making, particularly by the board
- Promoting and monitoring an ethical culture throughout the entity
- Ensuring a code of conduct is appropriately designed and implemented and compliance with the code is monitored
- Implementing an effective system of risk oversight and management, which may typically include:
  - policies dealing with material business risks, clearly describing the roles and responsibilities of the board, audit committee, management and internal audit activity
  - documenting the entity's risk profile and the risk appetite of the board
  - effective reporting of material business risks
  - ongoing monitoring of the entity's risk profile
- risk-based internal audit plans
- Implementing an effective and efficient internal control system
  - a strong control environment, commensurate with the risk appetite of the board
  - identification and management of risk
  - adequate design and operation of business policies and procedures to safeguard assets, protect against fraud and comply with applicable laws, regulations and standards
  - ongoing monitoring of internal controls
  - an independent, internal audit activity to provide assurance over the internal control systems
  - timely responsiveness to internal and external audit recommendations to enhance the internal control environment

- Ensuring the existence of business policies and practices and appropriate financial management
- Ensuring protection of an entity's assets
- Ensuring high quality internal and external reporting (financial and non-financial) to users of financial reports;
- Ensuring compliance with applicable laws, regulations, standards and best practice guidelines
- ~~including~~ appropriate accounting policies and procedures
- Providing a formal forum for communication between the board and senior financial management
- Obtaining an independent, effective and efficient external audit, including assessing audit quality and recommendations in respect of auditor rotation for listed entities
- Facilitating effective communication between the board and the internal and external auditors, and providing timely and appropriate responses to matters arising from audits
- Consideration of significant matters that were raised during the audit process.

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~~Under the Corporations Act 2001, directors are required to declare that the financial statements and notes comply with accounting standards and give a true and fair view of the financial position and performance of the company. Overall responsibility for the content of the annual financial statements and notes sits with the board.~~

~~The board determines the audit committee's role, which may include oversight and monitoring of:~~

- ~~○ corporate reporting, including external financial reporting~~
- ~~○ external audit~~
- ~~○ internal audit~~
- ~~○ risk management and internal control~~
- ~~○ compliance and ethics~~
- ~~○ activities to prevent, deter, detect and report on fraud.~~

~~For example, the audit committee may assist the board in achieving the following objectives of the entity:~~

- ~~— Facilitating well informed, efficient and effective decision making, particularly by the board~~
- ~~— Promoting and monitoring an ethical culture throughout the entity~~
- ~~— Ensuring a code of conduct is appropriately designed and implemented and compliance with the code is monitored~~
- ~~— Implementing an effective system of risk oversight and management, which may typically include:~~
  - ~~— policies dealing with material business risks, clearly describing the roles and responsibilities of the board, audit committee, management and internal audit activity~~
  - ~~— documenting the entity's risk profile and the risk appetite of the board~~
  - ~~— effective reporting of material business risks~~
  - ~~— ongoing monitoring of the entity's risk profile~~
- ~~— risk based internal audit plans~~
- ~~— Implementing an effective and efficient internal control system, including:~~
  - ~~— a strong control environment, commensurate with the risk appetite of the board~~
  - ~~— identification and management of risk~~
  - ~~— adequate design and operation of business policies and procedures to safeguard assets, protect against fraud and comply with applicable laws, regulations and standards~~
  - ~~— ongoing monitoring of internal controls~~

~~an independent, internal audit activity to provide assurance over the internal control systems~~  
~~timely responsiveness to internal and external audit recommendations to enhance the internal control environment~~  
~~Ensuring high quality internal and external reporting (financial and non-financial), including:~~  
~~complete, timely, accurate and useful information~~  
~~appropriate accounting policies and procedures~~  
~~reasonable judgements and estimates~~  
~~Obtaining an independent, effective and efficient external audit~~  
~~Promoting effective communication between the board and the internal and external auditors, and providing timely and appropriate responses to matters arising from audits.~~

The audit committee's responsibilities are typically documented in its charter. Ideally, the audit committee's annual work plan is cross-referenced to its charter to ensure that the committee fulfils its responsibilities.

~~The board and its individual directors cannot abrogate or delegate their responsibilities to the audit committee (see page 15, 16 for more detail).~~

Under the *Corporations Act 2001*, directors are required to declare that the financial statements and notes comply with accounting standards and give a true and fair view of the financial position and performance of the company. Overall responsibility for the content of the annual financial statements and notes sits with the board.

The audit committee can assist directors to fulfil their responsibilities and facilitate decision making by:

- facilitating open communication between board members and senior management, risk and compliance managers, internal and external auditors
- focusing on matters within the audit committee's charter, thereby allowing the full board to spend more time on other matters.

To be effective, the audit committee must be independent from management and free from any undue influence. Members of the audit committee should not have any executive powers, management functions, or delegated financial responsibility of the entity.

## Regulatory context

Audit committee members need to be aware of legislation, regulatory requirements, standards and guidance that are relevant to the operation of the audit committee, either directly, by establishing requirements for boards and audit committees, or indirectly, by establishing requirements for other parties reporting to, or working with, the audit committee, such as the internal and external auditors.

For those entities that operate in multiple jurisdictions, the audit committee would also need to consider the relevant legislation and regulations in those jurisdictions.

The legislation, regulatory bodies and the accompanying regulation, standards and guidance listed below may be relevant.

## Corporations Act 2001

The *Corporations Act 2001* is the principal legislation regulating companies in Australia. It covers matters such as the formation and operation of companies, duties of officers, takeovers and fundraising. It is a key point of reference for the audit committee on financial reporting and external audit requirements.

## Australian Securities Exchange Listing Rules and Corporate Governance Guidelines

The ASX Listing Rules require entities included in the S&P/ASX All Ordinaries Index at the beginning of their financial year to have an audit committee.<sup>9</sup> They also require the S&P/ASX 300 listed entities to comply with the 3<sup>rd</sup> edition of the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations with 2010 Amendments (Corporate Governance Principles and Recommendations) on the composition, operation and responsibility of the audit committee.

Principle 4 of the Corporate Governance Principles and Recommendations states that:

~~Companies should have a structure to independently verify and safeguard the integrity of their financial reporting. A listed entity should have the formal and rigorous processes that independently verify and safeguard the integrity of its corporate reporting.~~

### ASX Listing rule 12.7

An entity which was included in the S&P All Ordinaries Index at the beginning of its financial year must have an audit committee during that year. If the entity was included in the S&P/ASX 300 Index at the beginning of its financial year it must also comply with the best practice recommendations set out in the ASX Corporate Governance Council in relation to composition ~~and~~, operation ~~and responsibility~~ of the audit committee for the whole of that financial year, unless it had been included in that for the first time less than three months before the beginning of that financial year. An entity that is included in the S&P/ASX 300 Index for the first time less than three months before the first day of its financial year but did not comply with the ~~best practice~~ recommendations set by the ASX Corporate Governance Council in relation to composition ~~and~~, operation ~~and responsibility~~ of the audit committee at that date must take steps so that it complies within three months of the beginning of the financial year.

The supporting recommendations for a listed entity for that principle<sup>10</sup> are:

#### Recommendation 4.1

~~(a) 4.1: The board should establish have an audit committee which:~~

~~4.2: The audit committee should be structured so that it:~~

- consists only of non-executive directors
- consists of a majority of independent directors
- is chaired by an independent chair, who is not the chair of the board
- has at least three members; ~~and~~

~~4.3: The audit board committee should disclose the:~~

- charter of the audit committee
  - relevant qualifications and experience of the audit committee
  - number of times the committee met during the period and the individual attendances of the members at those meetings; or
- ~~have a formal charter~~

~~(b): If the board does not have an audit committee, this is disclosed as well as the processes that the board employs that independently verifies and safeguards the integrity of the corporate reporting function~~ 4.4: Companies should provide the information indicated in the Guide to reporting on Principle 4.

#### Recommendation 4.2

<sup>9</sup> See ASX Listing Rule 12.7.

<sup>10</sup> These recommendations came into effect from 1 January 2008.

The board should, before it approves the entity's financial statements for a financial period, receive from its CEO and CFO a declaration that, in their opinion, the financial records of the entity have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively. This declaration is required under section 295A of the *Corporations Act 2001*.

#### Recommendation 4.3

Where the entity has an AGM, the external auditor should attend and be available to answer questions relevant to the audit. Section 250RA of the *Corporations Act 2001* requires a listed company's auditor to be represented at the company's AGM by a suitably qualified member of the audit team who is in a position to answer questions about the audit.

Where a listed entity does not have a stand-alone risk committee, then the audit committee may be charged with the responsibilities of a risk committee, the responsibilities of whom are set out in Principle 7 of the ASX Corporate Governance Principles and Recommendations that states *A listed entity should establish a sound risk management framework and periodically review the effectiveness of the framework*. The commentary under Recommendation 4.3 states that the audit committee should report to the board on the results of the committee's review of risk management and internal control systems. Further guidance on the recognition and management of risk is provided under Principle 7 of the Corporate Governance Principles and Recommendations.<sup>11</sup>

### **AASB Accounting Standards**

The *Corporations Act 2001* requires the entity's financial report to comply with the Accounting Standards made by the Australian Accounting Standards Board (AASB). Compliance with these standards underpins the audit committee's monitoring and oversight of the entity's financial reporting. The Act also requires that financial reports present a "true and fair view". Since July 2005 the standards made by the AASB incorporate the equivalent International Financial Reporting Standards (IFRS).<sup>12 13</sup>

### **AUASB Auditing Standards**

The *Corporations Act 2001* requires the entity's financial report to be audited in accordance with the Auditing Standards made by the Auditing and Assurance Standards Board (AUASB).<sup>14</sup> While not creating obligations for the entity itself, the Australian Auditing Standards establish the mandatory requirements and provide application and other explanatory material for the external auditor of the entity.

This includes requirements for the external auditor to:

- agree with the entity the terms of the audit engagement

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<sup>11</sup> ~~*Corporate Governance Principles and Recommendations with 2010 Amendments, Principle 7 Recognise and manage risk, ASX Corporate Governance Council.*~~

<sup>12</sup> International Financial Reporting Standards (IFRS) are issued by the International Accounting Standards Board.

<sup>13</sup> Australian Accounting Standards may include additional paragraphs that do not appear in the equivalent IFRS. They are identified by the prefix "Aus" and generally relate to identifying the entities required to apply the standard and to matters affecting not-for-profit entities.

<sup>14</sup> Auditing Standards made by the AUASB conform with equivalent International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). Australian Auditing Standards may include additional paragraphs that do not appear in the equivalent ISA. Such paragraphs are identified by the prefix "Aus" and generally relate to Australian-specific legislative requirements and established audit practices.

- communicate with the entity:
  - the auditor's responsibility for forming and expressing an opinion on the financial report prepared by management
  - an overview of the planned scope and timing of the audit
  - significant qualitative aspects of the entity's accounting practices
  - significant difficulties, if any, encountered during the audit
  - significant matters arising during the audit that were discussed or subject to correspondence with management, including significant deficiencies in internal control identified during the audit
  - circumstances that affect the form and content of the auditor's report including where:
    - the auditor expects to modify the opinion;
    - a material uncertainty related to going concern is reported;
    - a key audit matter is communicated;
    - an emphasis of matter or other matter is included; and
    - there is an uncorrected material misstatement of the other information
  - any other matters that are significant to the oversight of the financial reporting process
  - independence statements
- seek representations from management (refer Appendix 3).

The audit committee can expect to interact with the external auditor on these matters and plays a key role in establishing an appropriate relationship with the external auditor.

### International Professional Practices Framework

The *International Professional Practices Framework* (IPPF) is promulgated by the IIA to provide consistent standards for the internal auditing profession. Members of the IIA agree to conform with the *Definition of Internal Auditing*, the *Code of Ethics* and the *International Standards for the Professional Practice of Internal Auditing* (Standards).

The Standards are principles-based requirements consisting of:

- Statements of basic requirements for the professional practice of internal auditing and for evaluating the effectiveness of its performance, which are internationally applicable at organisational and individual levels.
- Interpretations, which clarify terms or concepts within the statements.

### Accounting Professional and Ethical Standards Board

The Accounting Professional and Ethical Standards Board (APESB) is an independent, national body that sets the code of ethics and professional standards by which members of Australia's three professional accounting bodies abide.

Audit committee members who are members of an Australian professional accounting body must comply with the standards issued by the APESB and, in particular, APES 110 *Code of Ethics for Professional Accountants* (the Code), which includes the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

Audit committee members should be aware that auditors and other advisers that deal with the audit committee, who are members of an Australian professional accounting body, must comply with the Code, including the requirements to be independent and to comply with Australian Auditing Standards issued by the AUASB, where relevant.

### **Australian Securities and Investments Commission**

The Australian Securities and Investment Commission (ASIC) is Australia's corporate, markets and financial services regulator, established under the *Australian Securities and Investment Commission Act 2001*. Its role includes maintaining, facilitating and improving the performance of the Australian financial system and entities in that system, thereby promoting confident and informed participation by investors and consumers in the financial system.

ASIC has responsibility for the surveillance, investigation and enforcement of the financial reporting requirements of the *Corporations Act 2001*, including the enforcement of auditor independence and audit quality requirements, as well as audit inspection and information gathering powers under the ASIC Act.

The *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, further enhances ASIC's audit inspection and reporting powers by allowing ASIC to issue an audit deficiency report about specified failures by an individual audit firm and to communicate directly with the audit committee (or board or senior management), subject to certain requirements.

### **Australian Prudential Regulatory Authority**

The Australian Prudential Regulatory Authority (APRA) is the prudential regulator that oversees banks, credit unions, building societies, life and general insurance and reinsurance companies, friendly societies and superannuation funds (excluding self-managed funds).

APRA formulates, promulgates and enforces prudential policy and practice through Prudential Standards, which are supported by law, and Guidance Notes.

Audit committees of APRA-regulated entities will need to have regard to applicable APRA prudential requirements, for example, for risk management, governance, internal control systems and annual reporting requirements.

### **Australian Charities and Not-for-profits Commission**

The Australian Charities and Not-for-profits Commission (ACNC) is established under the ACNC Act and is the independent national regulator of charities.

The ACNC has responsibility for:

- registering organisations as charities
- helping charities understand and meet their obligations through information, guidance, advice and other support
- helping the public understand the work of the not-for profit sector through information, guidance, advice and other support
- maintaining a free and searchable public register so that anyone can look up information about registered charities, and
- working with state and territory governments (as well as individual federal, state and territory government agencies) to develop a 'report-once, use-often' reporting framework for charities.

### **Standards Australia**

Where audit committees are responsible for overseeing and monitoring risk management and compliance, joint Australian/New Zealand Standards such as AS/NZS ISO 31000: 2009 *Risk Management – Principles and guidelines* and AS 3806-2006 *Compliance programs*, developed by Standards Australia, might be useful.

AS/NZS ISO 31000: 2009 provides principles and generic guidance for the design and implementation of risk management plans and frameworks which can be used by any public, private or community enterprise, association, group or individual.

AS 3806-2006 provides principles and guidance for designing, developing, implementing, maintaining and improving a flexible, responsive, effective and measurable compliance program within an organisation.

## Responsibilities of the audit committee

It is important to clearly define the responsibilities of the audit committee in its charter, formally approved by the board and communicated to shareholders. Ideally, the audit committee's annual work plan is cross-referenced to its charter.

Over time, audit committee responsibilities have expanded from a financial focus to an approach focused on entity risks. This has broadened the audit committee mandate and overage to reflect the expanding scope of audit work, including their need to keep abreast of new risks driven by technology, economic instability, health threats, cybercrime, terrorism, increased regulation, and other factors that are involving faster than ever. There is also an increasing focus on corporate culture. Therefore, audit committees need to stay attuned to its responsibilities which may need to be revised or expanded by the Board of Directors from time-to-time.

The role of audit committees is to seek assurance, which can be defined as a process to provide a level of confidence that objectives will be achieved within an acceptable level of risk. Assurance is a positive declaration intended to give confidence. It is designed to improve the quality of information to aid informed decision-making. Assurance should be built-in to an entity's established processes.

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With increased outsourcing of non-critical operations to third parties and the adoption of combined assurance reporting concepts, audit committees need to consider the entity's overarching governance arrangements for assurance purposes. This includes an understanding of all assurance providers, awareness of what is being assured, nature of reporting within the entity's discrete governance structures, alignment between assurance and high-level risk exposures, consolidated risk and assurance profiles and co-ordinated reporting of assurance activities.

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The IIA lists the four pillars of governance as the audit committee, executive management, internal audit and external audit. With this perspective in mind, the audit committee has an active role to play to satisfy itself there is a strong governance environment covering their entity.

The combined assurance 3 Lines of Defence model is used by many entities to define their control and risk management environment to provide assurance to the board of directors, audit committee, chief executive officer, senior executives and stakeholders about effective governance:

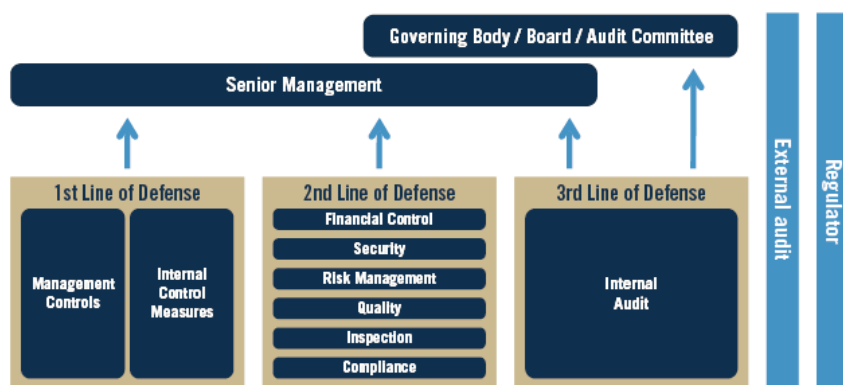
- The 1st line of defence *owns and manages risk*. It initiates risk and is responsible for managing the risks, together with making sure there are mechanisms in place to demonstrate controls are working effectively.
- The 2nd line of defence *monitors risk*. It monitors reviews and tests effectiveness of first line controls and management of risks. It is a form of assurance.

- The 3rd line of defence assures risk is managed. It independently evaluates and gives an opinion on the adequacy and effectiveness of both the 1st line and 2nd line risk management approaches. It is a form of assurance independent of management.

While the approach will be different for every entity, the concept can generally be illustrated as shown in the following diagram.

If the 3 Lines of Defence are assessed as operating effectively, the audit committee can have a higher level of confidence the entity is well-governed.

### The Three Lines of Defense Model



Adapted from ECIIA/FERMA Guidance on the 8th EU Company Law Directive, article 41

As previously set out, the key responsibilities of the audit committee, which are focused on assurance, are discussed in more detail below.

## Financial-Corporate reporting

### Financial reporting

The audit committee plays a key role in reviewing financial information before it is presented to the board for approval and publication, including the financial report and other financial information in an entity's financial reporting cycle, namely the concise financial report (if applicable), half year review and the annual report.

The audit committee may also report to the board on profit announcements, analyst briefings, investor presentations, announcements made under continuous disclosure obligations and other media releases containing financial information about the entity.

It is important to note that the board retains ultimate responsibility for financial reporting and cannot delegate that responsibility to the audit committee, or to management or external advisers. The audit committee will make use of knowledge gained from considering risk management, internal control and compliance activities, and from discussing matters with management, the internal auditor and the external auditor.

In the ~~recent~~ court case *ASIC v Healey* (2011) 196 FCR 291 at 339 and 298, Justice Middleton held that:

“... whilst an audit committee has an important role of monitoring and oversight, this is not to the exclusion of the role of a director to consider the financial accounts for him or herself in the way I have attempted to explain. This does not involve a director being familiar with every accounting standard, but sufficiently aware and knowledgeable to understand what is being approved or adopted.”

Justice Middleton further held that:

“... What each director is expected to do is to take a diligent and intelligent interest in the information available to him or her, to understand that information, and apply an enquiring mind to the responsibilities placed upon him or her. Such a responsibility arises in this proceeding in adopting and approving the financial statements. Because of their nature and importance, the directors must understand and focus upon the content of financial statements, and if necessary, make further enquiries if matters revealed in the financial statements call for such enquiries.”

### **Accounting policies**

The audit committee may require management to advise and provide representation on:

- How they selected and applied critical accounting policies and any changes in significant accounting policies, or their application, during the reporting period
- Whether they made a specific assessment of the entity's ability to continue as a going concern and how they made that assessment; if not, the basis for using the going concern assumption in preparing the financial statements and note disclosures
- The methods used to account for significant, complex or unusual transactions, or transactions in emerging areas for which there may be no specific accounting standard, including management's reasoning in determining the appropriateness of those methods
- The process used to determine that all relevant information has been brought to the attention of senior management to enable consideration of whether disclosure is required in the financial report
- Significant estimates and judgements in the financial report and the processes used by management in making those estimates and judgements. Management should comment on the impact of different assumptions, where these could have a significant impact on the financial report
- Other significant matters that do, or may, impact on the financial position of the entity and management's decision on disclosure or otherwise in the financial report
- The processes for identifying related party transactions and the nature, extent and reasonableness of related party transactions identified
- The processes for ensuring and monitoring compliance with laws, regulations and other requirements on external reporting by the entity of financial and non-financial information. Requirements include IFRS, the Corporations Act 2001, the ASX listing rules, APRA and, where applicable, the legislation and regulations of other countries in which the entity operates.

The audit committee may require the external auditor and, where appropriate, the internal auditor, to advise on:

- The appropriateness of the entity's accounting policies and procedures
- Areas of subjectivity in the financial report, including significant estimates and areas where judgement was involved

- Actual and potential material audit adjustments
- The materiality threshold used in the performance of the audit
- Other areas that may affect the quality of the financial report, for example:
  - non-compliance with laws and regulations, and actions taken by the entity in response to non-compliance
  - internal control issues.
- The auditor's view on management's:
  - technical competence and compliance with accounting standards
  - use of the going concern basis in preparing the financial statements and note disclosures
  - proper application of accounting principles
  - clarity in financial disclosure practices.

### Annual financial report

Regarding the annual financial report,<sup>15</sup> the audit committee needs to consider whether:

- The financial report complies with applicable legislation and accounting standards
- The financial statements and note disclosures present a true and fair view of the entity's financial position and performance, if not, additional disclosures are required
- The financial statements and note disclosures have been prepared on the basis that the entity is a going concern, and, if not, that they appropriately reflect the entity's inability to continue as a going concern
- Other information in the annual report is consistent with the financial report and other information known to the audit committee. For example, information in the directors' report or other management report/s relating to the entity's operations, financial position, business strategies and future prospects
- There is any information known to them gained in their role as a director of the entity that should be disclosed.

In light of the above, the audit committee may consider whether it is appropriate to make a recommendation to the board regarding approval of the directors' declaration.<sup>16</sup>

To fulfil this role the audit committee needs to have a good understanding of:

- the entity's financial reporting framework, which in most cases for Australian listed entities will be the Corporations Act 2001 and the Australian Accounting Standards
- the appropriateness of the entity's accounting policies and procedures, and whether they are consistent with the stated financial reporting framework
- the nature of the underlying transactions, assets and liabilities.

~~The audit committee will make use of knowledge gained from considering risk management, internal control and compliance activities, and from discussing matters with management, the internal auditor and the external auditor.~~

~~The audit committee may require management to advise and provide representation on:~~

- ~~• How they selected and applied critical accounting policies and any changes in significant accounting policies, or their application, during the reporting period~~
- ~~• Whether they made a specific assessment of the entity's ability to continue as a going concern and how they made that assessment; if not, the basis for using the going concern assumption in preparing the financial statements and note disclosures~~

<sup>15</sup> The audit committee may also review the concise financial report, if any, and the interim financial statements, and make similar considerations to those discussed for the annual financial report.

<sup>16</sup> The *Corporations Act 2001* in section 295(4) sets out the requirements of the directors' declaration regarding the financial report.

- ~~The methods used to account for significant, complex or unusual transactions, or transactions in emerging areas for which there may be no specific accounting standard, including management's reasoning in determining the appropriateness of those methods~~
- ~~The process used to determine that all relevant information has been brought to the attention of senior management to enable consideration of whether disclosure is required in the financial report~~
- ~~Significant estimates and judgements in the financial report and the processes used by management in making those estimates and judgements. Management should comment on the impact of different assumptions, where these could have a significant impact on the financial report~~
- ~~Other significant matters that do, or may, impact on the financial position of the entity and management's decision on disclosure or otherwise in the financial report~~
- ~~The processes for identifying related party transactions and the nature, extent and reasonableness of related party transactions identified~~
- ~~The processes for ensuring and monitoring compliance with laws, regulations and other requirements on external reporting by the entity of financial and non-financial information. Requirements include IFRS, the Corporations Act 2001, the ASX listing rules, APRA and, where applicable, the legislation and regulations of other countries in which the entity operates.~~

~~The audit committee may require the external auditor and, where appropriate, the internal auditor, to advise on:~~

- ~~The appropriateness of the entity's accounting policies and procedures~~
- ~~Areas of subjectivity in the financial report, including significant estimates and areas where judgement was involved~~
- ~~Actual and potential material audit adjustments~~
- ~~The materiality threshold used in the performance of the audit~~
- ~~Other areas that may affect the quality of the financial report, for example:~~
  - ~~non-compliance with laws and regulations, and actions taken by the entity in response to non-compliance~~
  - ~~internal control issues.~~
- ~~The auditor's view on management's:~~
  - ~~technical competence and compliance with accounting standards~~
  - ~~use of the going concern basis in preparing the financial statements and note disclosures~~
  - ~~proper application of accounting principles~~
  - ~~clarity in financial disclosure practices.~~

### **Reporting to the audit committee and the board**

Ideally, the audit committee reviews all representation letters signed by management to assess whether information provided appears complete and appropriate.

The audit committee may review the chief executive officer (CEO) and chief financial officer (CFO) declarations in respect of the financial report and financial records, provided in accordance with section 295(A) of the *Corporations Act 2001*.

The audit committee also reviews the letter, if any, provided by the external auditor to the audit committee at the end of the audit of the financial report, which may include, for example, a discussion of audit materiality, the appropriateness of accounting policies adopted by the entity and information about changes to accounting standards, both current and proposed, that may be relevant to the entity's financial report.

Based on its review and consideration of the financial statements and note disclosures, and other information, the audit committee should recommend to the board whether the financial report should be approved.

### Other external reporting

In relation to other external reporting,<sup>17</sup> the audit committee should ideally:

- Review documents and reports to regulators for consistency with the financial report and other information known to the audit committee
- Review the reporting of the entity's main corporate governance practices as required under the ASX listing rules for completeness and accuracy
- Review any non-IFRS financial information,<sup>18</sup> including the reconciliation between the underlying profit and statutory profit, if applicable
- Review any analyst briefings, investor presentations and media releases for consistency with the financial report
- Review the processes established for the purposes of continuous disclosure reporting to the ASX.

Based on its review and consideration of the other external reports, the audit committee should recommend to the board whether the reports should be approved.

### Other reporting

Entity performance encompasses both financial and non-financial performance, with the value of an entity driven by its bottom-line, but also by non-financial business drivers.

The audit committee should be appraised of entity performance from the perspective of whether performance measures are fit-for-purpose and whether they are being achieved. This should ideally relate to both financial and non-financial performance.

Performance measures need to be specific (clear and concise), measurable (quantifiable), achievable (practical and reasonable), relevant (to uses), and timed (within a range or time limit).

The purpose of management reporting is to aid decision-making and promote action. Management should provide the audit committee with relevant, integrated, timely, comparable, reliable and clear reports.

The focus of management reports to the audit committee should be on matters relevant to a clear picture of the overall state of entity assurance. In this way, an audit committee can achieve comfort the entity control and assurance environment is operating effectively.

### External audit

The audit committee has a key role in the entity's relationship with the external auditor and in promoting audit quality. The importance of this role is emphasised in the IAASB publication *A Framework for Audit Quality*. In addition, ASIC information sheet 196<sup>19</sup> provides guidance to assist directors and audit committees in their role in ensuring the quality of the external audit of a financial report.

<sup>17</sup> Other external reporting may include corporate social responsibility (CSR), sustainability, greenhouse gas and energy and occupational health and safety reporting.

<sup>18</sup> See ASIC Regulatory Guide 230 *Disclosing non-IFRS financial information and Underlying Profit: Principles for reporting of non-statutory profit information*, a joint publication between the Australian Institute of Company Directors and the Financial Services Institute of Australasia (Finsia).

<sup>19</sup> ASIC information sheet 196 *Audit Quality: The Role of Directors and Audit Committees*

The audit committee's responsibilities typically include:

- Recommending the appointment of an auditor to the board or assessing potential and continuing auditors including understanding the:
  - audit tender or selection process;
  - auditor's commitment to audit quality;
  - auditor's resources devoted to the audit;
  - auditor's reliance on experts and other auditors, (including using the work of other auditors, coverage of components within a group and reliance on internal auditors); and
  - accountability for audit quality by the auditor's engagement partner, review partner, specialists and audit team members.

The audit committee may agree the audit fee or make a recommendation thereon to the board. In addition, the audit committee may recommend to the board, if appropriate, the extension of the rotation period of the external audit engagement partner subject to certain requirements<sup>20</sup>.

- Facilitating the audit process by supporting the audit and ensuring company management and staff are accountable, supportive and helpful of the audit process.

Supporting the audit includes understanding that a high quality and comprehensive audit can be conducted for the agreed fee and that financial reporting and audit processes have been planned to ensure that an effective quality audit can be conducted within the financial reporting timeframes.

- Establishing ongoing communications with the auditor so as to:

- address any risk or areas of concern; and
- ensure access to directors and audit committees

Ensuring access includes the auditor attending all appropriate audit committee meetings and the auditor meeting with the audit committee separately from management without discussions being shared with management<sup>21</sup>.

- Maintaining and reviewing auditor independence and objectivity by considering whether the external auditor's relationships and services with the entity and other relevant organisations might impair, or appear to impair, the external auditor's independence. Under the *Corporations Act 2001*, the audit committee of a listed entity must provide written advice to the board regarding the provision of non-audit services by the external auditor.<sup>22</sup> Some audit committees may establish policies on the extent to which the external auditor can provide other assurance, or non-assurance, services and monitor the application of the policies to consider the possible implications for the auditor's independence

- Assessing the quality of audits conducted and evaluating of the performance of the auditor including considering:

- the auditor's internal quality and standards (reference may be made to the audit firms transparency report lodged with ASIC);
- the audit process (including the auditor's demonstration of professional scepticism);
- the timeliness of communications and usefulness and relevance of issues;
- other information (including firms audit transparency reports);
- findings from ASIC's audit inspections and surveillances.

The audit committee has a key role in the entity's relationship with the external auditor:

<sup>20</sup> Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, the audit committee of a listed entity may recommend to the board that the rotation period of the audit engagement partner be extended from five up to a maximum of seven years. The recommendation may be endorsed by a resolution passed by members of the audit committee and be in writing, stating the audit committee is satisfied that approval of the extension is consistent with maintaining the quality of the audit and would not give rise to a conflict of interest.

<sup>21</sup> The IAASB Publication *A Framework for Audit Quality*, suggests at least one meeting annually.

<sup>22</sup> See *Corporations Act 2001*, section 300 (11B) – (11E).

The audit committee's responsibilities typically include:

- Making recommendations to the board on the appointment of the external auditor. The audit committee may agree the audit fee or make a recommendation thereon to the board. The audit committee needs to be satisfied that a high quality and comprehensive audit can be conducted for the agreed fee
- Recommending to the board, if appropriate, the extension of the rotation period of the external audit engagement partner subject to certain requirements<sup>23</sup>
- Carefully examining any recommendations by management that the external auditor needs to be replaced, or that the audit needs to be put out to tender. The audit committee reports to the board on its examination before any decision is made by the board
- Agreeing on the terms of the audit engagement with the external auditor at the start of each audit
- Reviewing the independence of the external auditor. The audit committee considers whether the external auditor's relationships and services with the entity and other relevant organisations might impair, or appear to impair, the external auditor's independence. Under the Corporations Act 2001, the audit committee of a listed entity must provide written advice to the board regarding the provision of non-audit services by the external auditor.<sup>24</sup> Some audit committees may establish policies on the extent to which the external auditor can provide other assurance, or non-assurance, services and monitor the application of the policies to consider the possible implications for the auditor's independence
- Inviting the external auditor to attend audit committee meetings throughout the financial year, as a minimum to coincide with the reporting and audit cycles. For example, meetings to review the external audit plan, including proposed audit strategies, particularly in areas of identified audit risk, to discuss audit results and to consider the implications of the external audit findings for the control environment
- Meeting privately with the external auditor, at least once each year without management, to facilitate free and open communication. For example, the audit committee may ask the external auditor if there are any significant resolved or unresolved issues arising from the audit or whether senior management imposed any restrictions on the conduct of the audit
- Evaluating the performance of the external auditor
- Monitoring the relationship between the internal and external auditors.

Australian Auditing Standards include requirements for the external auditor to communicate certain matters to the audit committee.<sup>25</sup> Audit committee members may wish to familiarise themselves with these requirements and may expect to be informed by the external auditor of important matters related to the audit.

## Internal audit

Internal audit activities within entities are a key expression of their attitude towards an effective control environment.<sup>26</sup>

<sup>23</sup> Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, the audit committee of a listed entity may recommend to the board that the rotation period of the audit engagement partner be extended from five up to a maximum of seven years. The recommendation may be endorsed by a resolution passed by members of the audit committee and be in writing, stating the audit committee is satisfied that approval of the extension is consistent with maintaining the quality of the audit and would not give rise to a conflict of interest.

<sup>24</sup> See *Corporations Act 2001*, section 300 (11B) – (11E).

<sup>25</sup> See *Relationships – External Auditor* on page 30 of this guide.

<sup>26</sup> Not all entities will have an internal audit function.

The IIA defines the mission of internal audit as:

*“To enhance and protect organisational value by providing risk-based and objective assurance, advice, and insight.”<sup>27</sup>*

Internal audit provides the board of directors, audit committee, chief executive officer, senior executives and stakeholders with an independent view on whether an entity has an appropriate risk and control environment, while acting as a catalyst for a strong risk and compliance culture.

Good practice reporting arrangements for internal audit are: audit committee practices in overseeing internal audit activities typically include:

- Functionally for operations to the audit committee through the chair
- Administratively to the chief executive officer.

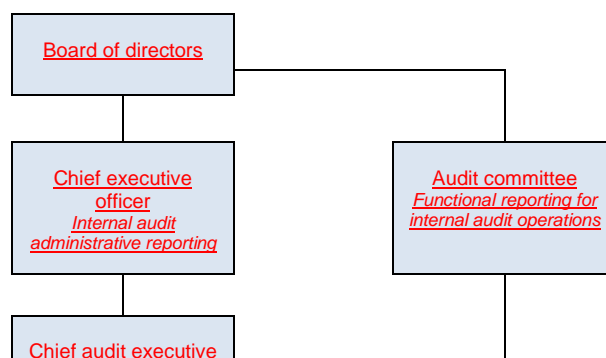
Functional reporting generally involves the audit committee:

- Reviewing and approving the internal audit charter
- ~~Making~~ Approving decisions regarding recommendations to the board on the appointment, remuneration and dismissal and removal of the chief audit executive (CAE)
- Reviewing and approving the strategic internal audit plan, often for a 2-3 year period
- Reviewing and approving the annual internal audit plan
- Approving any changes to the annual internal audit plan
- Reviewing reports on the results of internal audit engagements, audit-related activities, audit team capability, audit performance and other important matters
- Monitoring compliance with standards, together with quality and improvement arrangements
- Meeting privately with the CAE at least once a year without the chief executive officer or other management present
- Making enquiries of the CAE to determine any scope of budget limitations that may impede the execution of internal audit responsibilities.

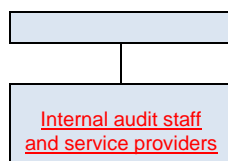
Administrative reporting to the chief executive officer generally includes:

- ~~the~~ internal audit resources and annual budget
- Provision of corporate services to internal audit including office accommodation, computers and equipment
- Human resource administration.

This can be shown diagrammatically as:



<sup>27</sup> Source: the 'International Professional Practices Framework issued by the Institute of Internal Auditors.



Internal audit work is risk-based and encompasses both financial and non-financial operations.

Appendix 4 contains a table identifying the fundamental differences between the work of internal audit and external audit.

- ~~activity's mission, charter, resources and budget to determine whether these maintain and enforce internal audit's independence from management. This is achieved through its reporting structures and the right to access all levels of management and relevant information<sup>28</sup>~~
- ~~Maintaining the independence of the internal audit activity<sup>29</sup>~~
- ~~Ensuring that the CAE reports to the audit committee for functional purposes, and to the CEO (or equivalent) for administrative purposes, and has access to all levels of management with the right to seek information and explanations relevant to their operations~~

~~The IPPF, Standard 1100 provides examples of functional reporting to the board, where the board is involved in:~~

- ~~approving the internal audit charter~~
- ~~approving the risk based internal audit plan~~
- ~~receiving communications from the CAE on the internal audit activity's performance relative to its plan and other matters~~
- ~~approving decisions regarding the appointment and removal of the CAE making appropriate enquiries of management and the CAE to determine whether there are inappropriate scope or resource limitations.~~

- ~~Monitoring the internal audit activity's participation in non-assurance roles to assess whether it impairs their independence and it aligns with the internal audit program~~
- ~~Reviewing the internal audit plan to assess whether it is risk-based and addresses the material business risks of the entity~~
- ~~Reviewing and approving the scope of the internal audit plan and work program~~
- ~~Meeting privately with the internal auditor at least once each year, without management, to facilitate free and open communication. For example, the audit committee may ask the internal auditor if there are any significant resolved or unresolved issues arising from the internal audit reviews, or whether senior management imposed any restrictions on the conduct of the internal audit activity~~
- ~~Receiving and reviewing reports prepared by the internal audit activity in terms of quality, timeliness and results of engagements~~
- ~~Monitoring the progress of the internal audit plan and work program~~
- ~~Noting and discussing the implications of internal audit findings on the internal control framework and business environment~~
- ~~Monitoring the implementation of internal audit activity's findings and recommendations~~

<sup>28</sup> ~~The Privacy Act 1988 may be a consideration in determining access to information.~~

<sup>29</sup> ~~The IPPF, Standard 1110 states that, "Organisational independence is effectively achieved when the CAE reports functionally to the board".~~

- ~~Monitoring and reviewing the quality of internal audit services delivered~~
- ~~Evaluating the process the entity has in place for monitoring and assessing the effectiveness of the internal audit activity~~
- ~~Overseeing the coordination of the planned activities of internal and external audit, risk and compliance management, and any other assurance providers.~~

## Risk management and internal control

Risk occurs when entity's try to achieve objectives in an uncertain environment. It is usually measured in terms of likelihood and consequence.

Risk management is an inherent part of the management process and incorporates the principles of corporate governance, accountability, communication and strategic alignment.

This requires co-ordinated and economical application of resources to:

- Address the uncertainty found in the entity environment, including uncertainty associated with assumptions.
- Minimise, monitor and control the probability (likelihood) or impact (consequence) of unforeseen events (threats).
- Maximise opportunities (good outcomes).

Risk management should be applied at all levels of an entity including:

- Enterprise-wide (strategic).
- Business unit (operational).
- Project-specific (tactical).
- Internal audit (planning, objectives and scoping).

A control is any action taken by management to enhance the likelihood that objectives will be achieved. These may be:

- Preventive – to deter undesirable events from occurring.
- Detective – to detect and correct undesirable events that have happened.
- Directive – to cause or encourage a desirable event to occur.

There are two types of controls – 'hard controls' and 'soft controls'.

- Hard controls are formal controls such as policies and procedures, reconciliations of accounting records, management sign-offs, a documented business plan, written code of conduct, separation of duties, and safety procedures.
- Soft controls are informal and include competency, knowledge and understanding of employees, ethical behaviour of management and staff, relationship building, and employee understanding of procedures.

Soft controls are more difficult to audit than hard controls because they generally do not have clear and definitive methods of testing the controls.

To manage identified hazards and risks, organisations apply both hard and soft controls that typically fall into three layers:

- Systems and processes (IT risk, business continuity, security).
- Capability.
- Culture (leadership, behaviour, attitudes).

The risk management and internal control framework within an entity is a key expression of its attitude to the control environment. While the board retains overall responsibility for risk management and internal control, it typically delegates elements of this responsibility to the

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audit committee (or the audit and risk management committee or a separate risk management committee, as applicable).

The three most commonly used sources of guidance on the elements of an effective risk management and internal control framework are the:

- Australia/New Zealand Standard on Risk Management (AS/NZS ISO 31000:2009) and accompanying handbooks published by Standards Australia
- Enterprise Risk Management Conceptual Framework (published by the Committee of Sponsoring Organisations of the Treadway Commission (COSO))
- Internal control – Integrated Framework (also published by COSO).

For example, the board retains responsibility for establishing an appropriate “tone at the top” - the corporate environment or culture, which disseminates throughout the entity and may be seen by some as equal to the internal control environment. This tone can be the most important factor contributing to the integrity of the entity’s key business processes, including financial reporting.

The board is also responsible for agreeing on the entity’s risk appetite and monitoring the strategic risks ~~facing the entity~~~~faced~~. This should be formally documented in a risk appetite statement from the board that clearly outlines the risks the entity is willing to take or accept in pursuit of its strategic objectives. The purpose of a risk appetite statement is to convey to the CEO what the board expectations are on how risk is to be managed within the entity.

A risk appetite statement explicitly outlines the risks to be avoided and for which the board has no tolerance. It considers the entity’s risk universe across all risk categories, with all business decisions to be made in the context of the approved risk appetite statement.

The board may delegate the following responsibilities to the audit committee:

- Reviewing whether the entity has an effective risk management system and that material business risks to the entity are appropriately reflected in the risk profile reported at least annually to the board
- Understanding the processes for determining and managing material business risks in accordance with the entity’s identified tolerance for risk, particularly risks in the following areas:
  - significant business risks, recognising that responsibility for general or specific risk areas for example, environmental risk, occupational health and safety, might be assigned to other board committees
  - breakdown of key business processes
  - non-compliance with laws, regulations and standards, and entity policy
  - fraud and theft
  - business continuity and disaster preparedness
- Monitoring the effectiveness of the entity’s processes for identification and control of material business risks, including operational, financial, legal, compliance and strategic risks. This might include oversight of the entity’s risk management framework and activities conducted by internal audit and external audit, together with -and any other assurance providers, to give-provide a holistic picture of assurance over that framework across the entity
- Receiving summary reports from management on all suspected and actual frauds, thefts and material breaches of laws, ensuring such events are reported to the board and/or relevant authorities
- Assessing adequacy of entity processes to manage insurable risks and the adequacy of insurance cover, and if applicable, the level of self-insurance
- Monitoring the effectiveness of the entity’s internal control system through discussions with management, ~~and the~~ internal auditors and external auditors

- Assessing whether management has controls in place for unusual types of transactions and/or any potential transactions that might carry more than an acceptable degree of risk
- Meeting periodically with key management, internal audit and external auditors, and compliance staff, to understand and discuss any changes in the entity's control environment
- Liaising with other board committees.

## Compliance and ethics

Within entities, compliance and ethics programs are a key expression of an entity's values. Non-compliance and unethical behaviour can have potential financial, non-financial or reputational impacts on an entity.

Compliance encompasses adherence to policies, plans, procedures, laws, regulations, contracts or other requirements.

Organisations need to comply with obligations associated with their establishing legislation or constitution, as well as broader legislative and regulatory obligations on how they operate, account and report.

Compliance continues to be a primary concern for the boards, audit committees and senior management of most entities, with reputation risk pushed to new levels as a consequence of the complexity and pace of legislative and regulatory change, coupled with an increase in regulatory scrutiny and enforcement.

Internal auditors are expected to assess the effectiveness of the entity's compliance framework including identification, risk assessment, awareness, monitoring, handling breaches, continuous improvement, the compliance register, reporting, and cross-border obligations.

The international standard for compliance management AS/ISO19600 was rolled-out in 2014 and is intended to serve as a global standard and benchmark for compliance management programs.

Part of compliance, is adherence to work health safety legislation. This legislation imposes a framework to secure the health and safety of workers and workplaces by protecting workers and other persons against harm to their health, safety and welfare through the elimination of risks arising from work. This is in accordance with the principle that workers and other persons should, as reasonably practicable, be given the highest level of protection against harm to their health, safety and welfare from hazards and risks arising from work. This requires the entity to:

- Eliminate risks to health and safety so far as is reasonably practicable
- If elimination is not reasonably practicable, minimise the risks so far as is reasonably practicable.

Accordingly, good audit committee practices will often include ~~some level of~~ oversight of compliance and ethics programs, including:

- Staying informed about the entity's processes for monitoring compliance with laws and regulations, industry codes, internal policies, standards of good corporate governance and other community expectations, ensuring they are aligned with the compliance culture expectations of the board. This will normally involve receiving

reports and briefings from key senior management, and meeting periodically with them.<sup>30</sup>

- Ensuring a code of conduct is in place, there is an effective implementation process to support its adoption, and the entity has a program for monitoring compliance with the code
- Approving and reviewing the policies, processes and framework for identifying, analysing and addressing complaints relating to the entity's compliance and ethical obligations. This includes both whistleblowing procedures for employees and customer complaint handling processes
- Staying informed on significant compliance and ethical issues, as well as independent investigations and disciplinary action in relation to non-compliance or unethical behaviour
- Receiving information from the external auditor on matters involving non-compliance with laws and regulations that were identified during the audit<sup>31</sup>
- Identifying and recognising adverse trends within the entity and reviewing management's plans to deal with them
- Reviewing management disclosures in the financial reports of the effect of significant compliance issues
- Ensuring the internal audit activity considers assessing compliance and ethics risks in their audit plan.

## Fraud and corruption control

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The audit committee may be responsible for overseeing the systems and programs implemented by management for fraud and corruption prevention, deterrence and detection, particularly in the context of financial accounting and reporting.

The existence of fraud and corruption prevention systems and programs ~~to prevent, deter and detect fraud within entities~~ is a key expression of the attitude of the board, audit committee and management to minimising fraud and corruption.

Good audit committee practices in overseeing fraud ~~minimisation and corruption prevention and detection programs~~ typically include:

- Ascertaining whether fraud risks have been included in the assessment of the risk profile of the entity
- Reviewing management's efforts to create and maintain a strong internal control environment, including the design and implementation of anti-fraud and corruption strategies and programs
- Reviewing management's communications, if any, to employees regarding its views on business practices and ethical behaviour
- Enquiring of management, ~~the internal auditor~~ and the external auditor<sup>32</sup> regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments
- Enquiring of management, the internal auditor and the external auditor whether they have knowledge of any actual, suspected or alleged fraud or corruption affecting the

<sup>30</sup> In this context, senior management might include the compliance officer, legal counsel, chief financial officer, head of human resources or tax manager.

<sup>31</sup> See Auditing Standard ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*.

<sup>32</sup> See Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*. Although intended for external auditors, this auditing standard contains information in its appendices that may be helpful for audit committee members. For example, it provides an extensive list of factors that indicate an incentive, pressure or opportunity to commit fraud, and examples of circumstances that indicate the possibility of fraud.

entity, and how the entity responded to such instances, including changes made to the control environment

- Monitoring remedial actions implemented by management, where **control** weaknesses were identified
- Obtaining representations from management that all known instances of actual, suspected or alleged fraud **or corruption** affecting the entity have been disclosed to the audit committee
- Ensuring the entity has fulfilled its fraud **and corruption** reporting obligations, if any, in accordance with relevant laws, regulations or other authority.

Audit committees need to be aware of their entity's operations and whether it may be in conflict with anti-corruption legislation, including in the internal arena.

## Relationships

### Board

#### Role

The audit committee assists in the discharge of the board's oversight and corporate governance responsibilities, whereas the role of the board is that of a constituting and governing body.

#### Responsibilities

The board:

- Establishes the audit committee with an appropriate charter, membership and level of resources to effectively carry out its activities
- Ensures that there is an appropriate reporting mechanism in place between it and the audit committee
- Periodically reviews the performance of the audit committee as a whole, and of each audit committee member. The audit committee performance review can be (and often is) by self-assessment (see the self-assessment tool in Appendix 2), but should preferably be part of a whole of board review.

It is important for the members of the audit committee and the board to recognise that delegation of activities to the audit committee does not absolve individual directors from their responsibilities. Individual directors are obliged to reach their own decisions based on a proper assessment of the information, which includes audit committee reports.

General responsibilities of directors, which extend to audit committee interaction and involvement, typically include:

- Duty to act in good faith in the best interests of the entity
- Duty to act with care and diligence
- Duty to avoid a conflict in the position of a director and/or any interest that a director may have
- A range of duties that prohibit the misuse of information obtained by directors.<sup>33</sup>

<sup>33</sup> See *Duties and Responsibilities of Directors and Officers 21<sup>st</sup> Edition* by Professor Robert Baxt AO, Australian Institute of Company Directors, 2016<sup>2</sup>.

## External Auditor

### Role

The scope of the external auditor's engagement usually emanates from a regulatory requirement, such as a requirement under the *Corporations Act 2001*, or other relevant legislation, to audit or review the entity's financial report.<sup>34</sup>

The external auditor must be independent from the entity's governance, internal control and ownership structures. The external auditor gains an understanding of the entity, its environment and its internal controls, makes risk assessments about the financial report and obtains sufficient appropriate audit evidence to support the auditor's report on the financial report.

As an independent party with knowledge of the entity's financial affairs, the external auditor can provide the audit committee with valuable, objective insight into aspects of the entity's governance and internal control, including its risk management. In turn, the audit committee aids the effectiveness of the external auditor. The importance of effective two-way communication in the promotion of audit quality is emphasised in the IAASB's publication, *A Framework for Audit Quality*.

For the external auditor, communication and consultation with the audit committee helps to facilitate an effective and efficient audit and the communication of matters arising from the audit. External auditors seek a constructive relationship with the audit committee while maintaining their independence, objectivity and an attitude of professional scepticism.

External auditors are required to respond to questions relating to certain aspects of the audit raised by the members of a listed entity at the entity's annual general meeting (AGM).<sup>35</sup> The relevant matters that members may query include the content of the auditor's report, the conduct of the audit, the accounting policies adopted by the entity and the independence of the auditor. As such, the external auditor fulfils an important role in providing independent information to members.

### Responsibilities

As set out in Australian Auditing Standards the external auditor has responsibilities for effective communication with those charged with governance (which may include the audit committee) in an audit of a financial report.

#### Promoting effective two-way communication

Effective two-way communication<sup>36</sup> assists:

- The audit committee in fulfilling its responsibility to oversee the financial reporting process
- The auditor in obtaining information relevant to the audit from the audit committee
- Both the audit committee and the auditor in establishing a constructive working relationship.

Auditing Standard ASA 260 *Communication with Those Charged with Governance* provides an overarching framework for the external auditor's communication with those charged with governance and identifies some specific matters to be communicated with them.

<sup>34</sup> Sections 307, 308, 309 and 314(2)(c) of the *Corporations Act 2001*.

<sup>35</sup> Not all listed entities are required to hold an annual general meeting, such as listed trusts.

<sup>36</sup> See ASA 260 *Communication With Those Charged With Governance*.

Additional matters to be communicated are identified in other auditing standards.<sup>37</sup> The key requirements are listed below:

### ***Promoting effective two-way communication***

~~Effective two-way communication<sup>38</sup> assists:~~

- ~~• The audit committee in fulfilling its responsibility to oversee the financial reporting process~~
- ~~• The auditor in obtaining information relevant to the audit from the audit committee~~
- ~~• Both the audit committee and the auditor in establishing a constructive working relationship.~~

### ***Establishing whether the preconditions for an audit are present***

In establishing whether the preconditions for an audit are present<sup>39</sup> discussions are needed with management and the audit committee to assist the auditor in:

- Determining whether the financial reporting framework to be applied by management in the preparation of the financial report is acceptable
- Obtaining the agreement of management that it acknowledges and understands its responsibility for preparation of the financial report, for the internal control system related to preparation of the financial report and for providing access by the auditor to all relevant information and persons for the purposes of obtaining audit evidence.

### ***Agreeing the terms of the audit engagement***

- Discussing and agreeing the terms of the audit engagement,<sup>40</sup> including who to communicate with, when and how to communicate
- Communicating the auditor's responsibilities in relation to the audit.

### ***Establishing and maintaining independence***

- Confirming their independence<sup>41</sup> in accordance with ethical and regulatory requirements
- Communicating any relationships that might have a bearing on their independence, including the provision of other assurance, and non-assurance, services to the entity and relevant external organisations and disclosing a categorised fee breakdown in both the reporting to the audit committee as well as within the financial report
- Notifying the audit committee of any contraventions to the auditor's independence requirements
- Communicating the safeguards applied to eliminate threats to their independence.

### ***Discussing elements of audit planning***

- Discussing the overall audit strategy, scope and timing,<sup>42</sup> including any limitations – based on the auditor's consideration of materiality, high risk areas affecting the financial report and their plans to examine the effectiveness of internal controls
- Discussing proposed co-ordination with the internal audit activity, including any planned use of internal audit work.

<sup>37</sup> See ASA 260, Appendix 1, which lists other auditing standards that require specific matters to be communicated to those charged with governance.

<sup>38</sup> ~~See ASA 260.~~

<sup>39</sup> See ASA 210 *Agreeing the Terms of Audit Engagements*.

<sup>40</sup> See ASA 210 *Agreeing the Terms of Audit Engagements*.

<sup>41</sup> See ASA 260 *Communication With Those Charged With Governance*.

<sup>42</sup> See ASA 300 *Planning and Audit of a Financial Report*.

- Discussing the nature and extent of specialised skill or knowledge needed, including the use of auditor's or management's experts
- Discussing the auditor's preliminary views about matters that may require significant auditor's attention and therefore may be key audit matters that are required to be included in the auditor's report.

### ***Requiring significant auditor's attention***

- Key audit matters (KAM) are those matters that in the auditor's professional judgement were of most significance in the audit of the financial report of the current period. Reporting of KAM is only required for general purpose financial reports of listed entities or where required by law or regulation.<sup>43</sup>
- The auditor is required to communicate with those charged with governance those matters that the auditor has determined to be key audit matters. Communication with those charged with governance recognises their important role in overseeing the financial reporting process, and provides the opportunity for those charged with governance to understand the auditor's decisions in relation to KAM and how those matters will be described in the auditor's report. It also enables those charged with governance to consider whether new or enhanced disclosures may be useful in light of the fact that these matters will be communicated in the auditor's report.

### ***Communicating considerations of group audits***

- The group engagement team communicates the following with the audit committee:
  - an overview of the work to be done on the financial information of components and an overview of the group engagement teams planned involvement in that work
  - concerns over the quality of component auditor's work
  - limitations on the group audit for example access to information restrictions
  - fraud or suspected fraud involving group or component management or where a fraud resulted in a material misstatement of the group financial report

### ***Discussing significant related party relationships and transactions***

- Discussing with the audit committee the nature, extent and business rationale of significant related party relationships and transactions,<sup>44</sup> including those involving actual conflicts of interests.

### ***Enquiring about fraud***

- The auditor is required to obtain an understanding of how management and others within the entity, including the audit committee, exercise oversight of management's processes for identifying and responding to the risks of fraud and the internal controls that management has established to mitigate these risks
- The auditor is required to enquire of management and others within the entity, including the audit committee and internal audit, to determine if they have any knowledge of actual, suspected or alleged fraud<sup>45</sup> affecting the entity.
- The auditor communicates fraud or suspected fraud involving group or component management or employees to the audit committee.

<sup>43</sup> See ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*.

<sup>44</sup> See ASA 550 *Related Parties*.

<sup>45</sup> See ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*.

### *Communicating significant findings from the audit*

- Determining, based on professional judgement, when significant findings from the audit<sup>46</sup> should be communicated to management, the audit committee and/or directly to the board<sup>47</sup>
- Communicating the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial report disclosures
- Discussing significant difficulties, if any, encountered during the audit
- Discussing significant matters raised with management during the audit, including any disagreements with management, whether resolved or unresolved, relating to the financial report
- Communicating circumstances that affect the form and content of the auditor's report including:
  - a modification of the opinion in the auditor's report
  - a material uncertainty related to going concern
  - key audit matters
  - an Emphasis of Matter paragraph or Other Matters paragraph
  - an uncorrected material misstatement of the other information
- Advising on representations the auditor is seeking from management<sup>48</sup>
- Communicating significant deficiencies in internal controls identified during the audit<sup>49</sup>
- Communicating identified fraud, information that indicates a fraud might exist, or weaknesses in the design or implementation of internal control to prevent, deter, detect and report on fraud
- Communicating significant matters of non-compliance with laws and regulations and the appropriate remedies<sup>50</sup>
- Communicating uncorrected misstatements identified by the auditor, ~~including corrected and uncorrected misstatements~~<sup>51</sup>
- Communicating events or conditions identified by the auditor that may cast doubt on the entity's ability to continue as a going concern<sup>52</sup>
- Communicating matters of governance interest that arose during the audit of the financial report that are relevant to the oversight of financial reporting. Such matters typically include:
  - modifications in audit strategy based on a revised consideration of risks
  - material risks and exposures regarding the financial report
  - industry, regulatory, or other external factors
  - material misstatements of fact or material inconsistencies in information accompanying the audited financial report

### ~~Discussing expected modifications to the auditor's report.~~

It is highly desirable that the external auditor discuss all issues to be raised at the audit committee meeting with the CEO, ~~and the CFO~~ and the audit committee chair before the

<sup>46</sup> See ASA 260 Communication With Those Charged With Governance.

<sup>47</sup> While the auditor may agree with the entity on preferred lines and forms of communications, the auditor should continue to use judgement to determine whether communication with the audit committee is sufficient and appropriate. The auditor should take into account such things as the nature of the matters, the governance structure, legal requirements and the composition of the audit committee (for example, the extent to which the members of the board are represented on the audit committee).

<sup>48</sup> See ASA 580 *Written Representations*.

<sup>49</sup> See ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*.

<sup>50</sup> See ASA 250 Consideration of Laws and Regulations in an Audit of a Financial Report.

<sup>51</sup> See ASA 450 *Evaluation of Misstatements Identified during the Audit*.

<sup>52</sup> See ASA 570 *Going Concern*.

meeting. This ensures that all relevant information has been obtained and is done as a courtesy to these executives.

### Responding to questions

- Responding in a timely manner to reasonable audit committee questions and communications.

## Internal Auditor

### Role

~~The~~ internal audit ~~activity~~, where it exists, acts as an agent for the audit committee and provides independent and objective assurance to the audit committee on governance, risk management and ~~internal~~ control processes.

~~Internal audit activities~~ should be conducted in a manner consistent with the IPPF, including the *Definition of Internal Auditing*, the *Code of Ethics* and the *Standards*. Internal audit ~~activity~~ requires professionals with an appropriate level of understanding of the business culture, systems and processes to provide assurance ~~that the internal~~ controls in place are sufficient to manage ~~the risks, that the~~ governance processes are adequate and ~~that~~ organisational ~~goals and~~ objectives are met.

Ultimately, the internal audit ~~activity~~ assists the audit committee in its role with monitoring and oversight ~~and which~~ typically falls into two distinct categories:

1. **Assurance services:** involves the internal auditor's objective examination of evidence for the purpose of providing an independent assessment on governance, risk management and control processes for the organisation.
2. **Consulting services:** providing advisory and related client service activities, the nature and scope of which are agreed with management. When performing consulting services, ~~the internal audit activity~~ must not assume management responsibility.

Internal auditors must communicate the results of engagements, and include their objectives and scope, as well as applicable conclusions, recommendations and action plans.

### Responsibilities

~~The Internal audit~~ responsibilities ~~of the internal audit activity~~ typically include:

#### Discussing elements of internal audit planning

- Providing a draft of the risk-based internal audit plan for input and formal approval. In developing the draft internal audit plan, the CAE should consider all ~~entity risks to the organisation,~~ including operational, financial, compliance and strategic risks. The draft plan should detail ~~the internal audit activity's~~ objectives, work schedules, staffing requirements, budgets and a description of any limitations placed on ~~the internal audit's activity's~~ scope of work
- The internal audit plan might also include financial or compliance audits, operational reviews, risk and control self-assessments, system-based audits, performance audits, IT audits and so on, and/or specific one-off assignments. It should evaluate and monitor the adequacy and effectiveness of the internal control systems. The plan should:
  - Provide details of the internal audit staff structure, including staff skills, experience and qualifications
  - Consider the activities of other assurance providers, both internal and external to the entity

- Advise on the coordination of the internal audit plan with the external audit plan.
- Discussing any changes to the internal audit plan
- Holding periodic discussions with the chair, and with all audit committee members, without the presence of management.

#### **Communicating on independence**

- Advising on ~~internal audit the~~ independence ~~of the internal audit activity~~
- Reporting any non-~~assurance audit~~ activities ~~provided by of the~~ internal audit activity.

#### **Communicating matters arising from ~~an~~ internal audit work**

- Submitting activity reports, highlighting significant findings, their effect, or potential effect, and recommendations (particularly regarding the entity's risk management plan), and advising ~~on~~ the actions taken, or proposed, by management
- Submitting reports on any major variances from ~~the~~ internal audit objectives, activity goals, work schedule and budget
- Providing activity reports on any major fraud
- Reporting on any identified conflicts of interest ~~or identified conflict of interest~~
- Advising changes to the risk profile of the entity and the implications of these for the audit plan.

#### **Responding to requests**

- Providing ~~Performing~~ audits that may be requested by the audit committee
- Providing any other information requested by the audit committee
- Providing assurance to management on the adequacy in the areas of internal corporate governance, risk management, ~~internal~~ control and compliance, and being available to management ~~for consultation~~ to assist with the improvement of ~~these~~ processes and control activities.

#### **Engaging with the audit committee on matters associated with governance, risk management, internal control and other matters**

- ~~The~~ Internal audit activity provides a key source of information for members of the audit committee on governance, risk management and internal control, and other matters affecting the entity's operations.

#### **Annual reporting**

- Provides an annual report of its work to the audit committee, including an assessment on the effectiveness of the organisation's control system.
- Advising the audit committee and management of patterns, trends and systemic issues identified from its work.

### **Developing an effective charter**

The charter is the audit committee's blueprint for its operations, and should be developed to meet the needs of the entity, allowing for the entity's objectives, culture and the industry in which it operates.

The charter should cover all key aspects of the audit committee's operations while remaining flexible to enable the committee to respond appropriately to issues that arise.

The audit committee charter is developed and approved by the board.

A wide range of sample audit committee charters are available in the public domain including some issued by professional bodies.<sup>53</sup> One size cannot fit all in respect of audit committees, so each audit committee should evolve and develop its own guidelines suited to itself and the organisation.

Commonly the charter defines and/or outlines the following<sup>54</sup>:

- The audit committee's purpose and objectives
- The audit committee's responsibilities, including:
  - its duty to carry out, or to arrange, investigations requested by the board
  - the scope of its activities for:
    - financial reporting oversight
    - internal and external audit evaluation
    - risk management and internal control
    - compliance with laws, regulations, internal policies and industry standards
    - fraud control
    - continuous disclosure
  - its responsibility for ensuring procedures are in place for the receipt, retention and treatment of complaints received by the entity regarding accounting, internal accounting controls or auditing matters
- The authority delegated from the board to the audit committee, which might include the committee's right to:
  - obtain outside legal or independent professional advice at the entity's expense
  - institute special investigations
  - recommend the appointment and retention of the external auditor
  - approve the external audit fee and oversee the work of the external auditor
  - ~~Audit committee membership, which may:~~
  - ~~cover the number of independent, non-executive directors and non-director committee members, if applicable~~
  - ~~the process for their appointment and replacement by the board~~
  - ~~their terms of office~~
  - ~~the process for reviewing the independent, non-executive status of committee members and appointment~~
- ~~The appointment and role of the chair (see page — for more detail).~~
- ~~The method of identifying and declaring actual or potential conflicts of interest by audit committee members~~
- ~~The arrangements for meetings, including flexibility for the audit committee to invite non-members such as external auditors, internal auditors and members of management who may call a meeting, the frequency and timing of meetings and what constitutes a quorum~~
- The audit committee's responsibility for reporting on its activity
- ~~The need to prepare a meeting agenda, minutes of meetings and other records, if any, of significant decisions made by the audit committee~~
- ~~Attendance at audit committee meetings by non-member invitees, including board members (who should be entitled to attend but not vote)~~
- ~~The parties with whom the audit committee should meet privately, without management, and the frequency of such meetings~~
- ~~The audit committee's responsibilities, including:~~

<sup>53</sup> See Appendix 1 for a sample audit committee charter.

<sup>54</sup> Note that protocols applicable to all committees are not included here – such as appointment, conflicts of interest, preparation of agenda, minutes, attendance at meetings, etc.

- ~~its duty to carry out, or to arrange, investigations requested by the board~~
- ~~the scope of its activities for:~~
  - ~~— financial reporting oversight~~
  - ~~— internal and external audit evaluation~~
  - ~~— risk management and internal control~~
  - ~~— compliance with laws, regulations, internal policies and industry standards~~
  - ~~— fraud control~~
  - ~~— continuous disclosure~~
- ~~its responsibility for ensuring procedures are in place for the receipt, retention and treatment of complaints received by the entity regarding accounting, internal accounting controls or auditing matters~~
- ~~The audit committee's obligations to report on its activities to the board, regulators and/or members~~
- ~~The process for assessing the audit committee's performance, including compliance with its charter~~
- ~~The process for periodic review of the audit committee charter~~
- ~~The extent of liaison expected between the audit committee and other board committees.~~ How the audit committee performance will be assessed

Audit committee members, the board, management and internal and external auditors need to understand the audit committee's charter, including the audit committee's scope of activities and communication and reporting arrangements.

The charter should be regularly monitored, and reviewed annually to ensure it remains relevant to the entity's needs (for instance, revising reporting requirements to cover board needs for additional information) and reflects current regulatory requirements and audit committee good practice.

## Membership

The membership of the audit committee is a key determinant of its success.

### Audit committee composition

The composition of the audit committee should include a balance of professional skills, knowledge and technical experience, as well as sufficient capacity, independence and objectivity, to discharge its responsibilities as defined in its charter.

The ASX Corporate Governance Council recommends the audit committee should be structured so that it:<sup>55</sup>

- consists only of non-executive directors
- consists of a majority of independent directors
- is chaired by an independent chair, who is not the chair of the board
- has at least three members.

S&P/ASX 300 entities are required to comply with these recommendations regarding the structure of the audit committee.<sup>56</sup>

<sup>55</sup> See Recommendation 4.12 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* with 2010 Amendments.

<sup>56</sup> See ASX Listing Rule 12.7.

The CEO (or managing director) should not be a member of the audit committee, although it is not uncommon for the CEO to be invited to attend audit committee meetings (see *Attendance* on page 54).

The board might appoint a person who is not a director of the entity to the audit committee to provide particular expertise.

### **Selection of audit committee members**

Not only is it important to maintain audit committee continuity, but also provide a fresh perspective through succession planning and the selection process.

The following key qualities are desirable when appointing members:

- Individuals should have:
  - an understanding of the industry, the entity, its business and its products and/or services
  - a mindset that is independent of the entity's management
  - strong communication skills, including an ability to offer different perspectives and constructive suggestions
  - high levels of personal integrity and ethics
  - sufficient time available to devote to executing responsibilities
  - financial literacy, including an ability to read or understand financial statements, ask pertinent questions about them, and interpret and evaluate answers.
- The audit committee as a whole should have:
  - at least one member with financial expertise, which may be interpreted broadly as being "a qualified accountant or other financial professional with experience of financial and accounting matters."
  - a mix of skills and experience relevant to discharging responsibilities, including experience in business, financial and legal compliance, risk management and international commercial background and experience, if applicable.

Committee members and the audit committee chair should be appointed by the board. A board nomination committee should be convened with the power to interview candidates considered to have the skills, experience and interest in being a member of the audit committee and recommend their appointment.

### **Independent and non-executive members**

It is recommended that the majority of members of the audit committee are independent and non-executive members. However, if the entity is in the S&P/ASX 300 at the beginning of the year, it is a requirement under the Listing Rules that the committee consist solely of non-executive directors, a majority of whom are "independent".

Independent, non-executive directors are individuals free from any management, business or other relationship that could reasonably be perceived to materially interfere with their ability to act in the best interests of the entity. The "independence" of audit committee members should always be considered in relation to any applicable legislation, or regulation, that defines the requirements of independence for audit committee membership.

Independence is arguably a state of mind, and cannot necessarily be assessed by a person's relationship with the entity. It is commonplace to examine an audit committee member's past and current relationships with the entity as indicators of independence, or otherwise.

The ASX Corporate Governance Council<sup>57</sup> identifies the following relationships which may affect the independent status of a director if the director:

- Is a substantial shareholder of the entity or an officer of, or otherwise associated directly with, a substantial shareholder of the entity
- Is employed, or has previously been employed, in an executive capacity by the entity or another group member, and there has not been a period of at least three years between ceasing this employment and serving on the board
- Has, within the last three years, been a principal of a material professional adviser or a material consultant to the entity or another group member, or an employee materially associated with the service provided
- Is, or has been within the last three years, a material supplier or customer of the entity or other group member, or an officer of, or otherwise associated directly or indirectly with, a material supplier or customer
- Has a material, contractual relationship with the entity or another group member other than as a director
- Has close family ties with any person falling within any of the categories described above
- Has been a director of the entity for such a period that his or her independence may have been compromised.-

This list is not exhaustive and if one or more of the above is exhibited by a director it is possible that their status as an independent director might be compromised. However in relation to the last point, the guidelines indicate that the mere fact a director has served on the board for a substantial period of time does not mean that he or she has become too close to management to be considered independent. It indicates that the board should regularly assess whether that might be the case for any directors who has served in that position for more than 10 years.

Members and potential members of the audit committee need to exercise care to ensure they disclose to the board for its consideration any relationships that could be viewed by other parties as impairing either the individual's, or the audit committee's actual or perceived independence. When deciding what is significant, consider the significance of the relationship to both the entity and to the individual.

The board might choose to appoint an individual to the audit committee, despite the existence of relationships identified above, because of the individual's business or other expertise but only after the Board has considered the materiality of the interest, position, association or relationship to determine whether it might interfere, or might reasonably be seen to interfere with the directors capacity to bring an independent judgement to bear on issues before the board and to act in the best interests of the entity and its security holders generally.-

The ASX Corporate Governance Council recommends<sup>58</sup> that the listed entity should disclose:

- The names of the directors considered by the board to be independent directors
- If a director has an interest, position, association or relationship of the type described in the listing above [box 2.3] but the board is of the opinion that it does not compromise the independence of the director; this existence of such relationships should be disclosed in the corporate governance statement along with the reasons for considering such a director to be independent
- The length of service of each director.

<sup>57</sup> See Box 2.34 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* ~~with 2010 Amendments~~.

<sup>58</sup> See Recommendation 2.3 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*

~~suggests that the board should state its reasons for considering such a director to be independent, and the corporate governance statement should disclose the existence of any such relationships.<sup>59</sup> It is important for the board to consider materiality thresholds from the perspective of both the entity and its directors, and to disclose these.~~

## Audit committee chair

The chair of the audit committee plays a pivotal role in the overall effectiveness of the audit committee. The chair of the audit committee is preferably independent and not ~~be~~ the chair of the board.<sup>60</sup> <sup>61</sup> However, if the entity is in the S&P/ASX 300 at the beginning of its financial year, then this is actually a requirement under the Listing Rules.

The chair is responsible for:

- Promoting effective communications between the audit committee and the board, CEO, CFO, CAE, internal audit, other senior management and the external auditor
- Ensuring audit committee meetings run smoothly so, that the views of all audit committee members are heard, that adequate time is allowed for discussion of each issue and that the agenda and meeting papers properly reflect proceedings.

The board should select an audit committee chair who:

- Has demonstrated strong leadership qualities
- Is knowledgeable of the duties and responsibilities of the position as outlined in the charter
- Has skills and knowledge about the industry, the entity's business, and financial reporting and auditing requirements
- Has strong communication skills, including the ability to promote effective working relationships among audit committee members and with others, such as management and the internal and external auditors

The chair's own term of appointment should be specified by the board and should relate to the director's term of appointment to the audit committee. The board may also appoint a deputy chair in the same manner.

## Induction of new members

The audit committee's knowledge and proficiency are enhanced when new members are appropriately acquainted with the audit committee's objectives and practices. All new members and existing directors need to be well briefed. Induction can be undertaken in many different ways, ranging from formal orientation programs to informal discussions.

A new member needs to understand the audit committee's role, objectives and responsibilities, be familiar with its relationships with management and the internal and external auditors, and have a sound knowledge of the entity's operations and the environment in which it operates, including the entity's code of conduct. They also need to understand the time and effort they will need to devote to their audit committee membership additional to the time and effort they devote to each board meeting.

Relevant information may be provided to new audit committee members, including:

- The audit committee charter

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<sup>59</sup> ~~See Recommendation 2.1 of the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations with 2010 Amendments.~~

<sup>60</sup> See Recommendation 4. ~~12~~ of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's Corporate Governance Principles and Recommendations ~~with 2010 Amendments.~~

<sup>61</sup> ASX Listing Rule 12.7.

- An overview of business operations and the industry in which the entity operates
- All material previously provided to audit committee members on matters still before the audit committee, including current audit plans and outstanding corrective action from previous audit reports (both external and internal)
- Papers from recent audit committee meetings
- Internal audit charter
- Financial performance information
- Risk profile of the entity and a list of material business risks
- Risk appetite of the board
- Risk management framework and processes
- Internal control framework and processes
- Key financial reporting policies, including any related party issues
- Legal and regulatory requirements, including external reporting and compliance responsibilities
- Code of conduct for the entity, board and/or the audit committee
- Estimates of the time members need to commit to their audit committee role
- Fraud control framework (and high level details on previous fraud issues/allegations, if any).

All new members should meet with the chair, other audit committee members, senior management, and external and internal auditors as soon as practicable after being appointed.

### **Ongoing training**

It is important that audit committee members keep abreast of current developments in matters that affect their capacity to effectively discharge their duties. Audit committee members may routinely receive focussed information on:

- Important relevant industry issues, trends and developments
- Key financial, and other performance indicators, of the entity detailing the level of achievement of the entity's objectives
- Significant proposed changes in financial reporting and regulatory requirements
- Other matters that might have a significant impact on the risk profile of the entity.

Audit committee members should be encouraged to attend relevant third-party training, conferences and seminars and share information at subsequent audit committee meetings.

### **Rotation**

Periodic rotation of audit committee members is encouraged as it enhances the perception of audit committee independence.

Rotation will generally depend on the size of the board from which audit committee members are drawn, and the availability of suitable candidates from within and outside the entity.

### **Conducting meetings**

How audit committee meetings are conducted will greatly influence the ability of audit committee members to achieve the audit committee's objectives.

## Frequency of meetings

A regular schedule of meetings should be designed to enable the audit committee to effectively discharge its responsibilities.

While the number and duration of audit committee meetings will depend on the size and complexity of the audit committee's responsibilities, it is common for the following to occur:

- Audit committees typically meet at least four times a year to coincide with key dates within the financial reporting and audit cycles, and to plan the year and review performance
- There may be a separate meeting to consider the annual financial report and half year review, which may be covered within the normal meeting schedule or in an additional meeting, where necessary. This meeting should allow ample time for detailed consideration of the report,<sup>62</sup> with the agenda tailored accordingly and not overburdened with other items. For example, important accounting judgements, key audit matters and related decisions may be determined ahead of the year end and at an earlier meeting than the one that considers the annual financial report
- When possible, meetings are arranged so that all audit committee members can attend. The proposed schedule of audit committee meetings may be discussed and agreed well in advance. In planning the schedule of meetings, reference should be made to the meeting schedule of the full board, allowing sufficient time between audit committee and board meetings to action any items and prepare papers and reports to be tabled at the board meeting
- The audit committee charter normally empowers the chair to convene a special meeting at the request of the board, an audit committee member, senior management, the external or internal auditor.

## Structure of meetings

Normal business practices for committee meetings apply to audit committees.

Well-run audit committee meetings typically include:

- The preparation of a formal, well-structured agenda with reference to the audit committee charter to ensure that the agenda and meeting papers are appropriate
- The internal and external auditors are invited to contribute to the agenda
- The chair reviews and approves the agenda, and relevant meeting papers, before issuing them to audit committee members and other parties authorised by the audit committee
- The agenda and meeting papers are distributed before the meeting, allowing sufficient time for members to read them carefully. As a guide, papers should be distributed at least one week before the meeting. However, where there is a large volume of papers, or papers involve complex matters, the audit committee may require them to be distributed more than one week before the meeting to enable members to carefully review and understand the content of papers

In ASIC v Healey (2011) 196 FCR 291, notwithstanding a complex corporate reporting structure, multiple sets of financial statements requiring approval and reporting deadlines, the ruling confirmed the proposition that members of the audit committee and other directors have a duty to read the financial statements and check them. Timing issues and information overload cannot be used as defences in avoiding this responsibility.

<sup>62</sup> Time should be allowed for the audit committee to consider any changes that have been made to the financial report since the audit committee papers were distributed. Management may provide the audit committee with a detailed list of all such changes.

- Inclusion of the annual work plan or calendar of events, cross-referenced to the charter, in meeting papers may be useful in providing audit committee members with an overview and ensuring compliance with the charter
- Efficient running of the meeting is assisted by:
  - Ensuring the meeting starts and finishes on time, while taking as long as necessary to adequately consider agenda items
  - Members agreeing to the priority of, and the time to be devoted to, each item at the commencement of each meeting
  - Meeting processes requiring members to declare any actual, perceived or potential conflicts of interest each year, and at the beginning of each meeting to strengthen the audit committee's independence. Members consider past employment, consultancy arrangements and related party issues when considering conflicts of interest
  - Establishing clear decision-making processes and voting protocols.
- The minutes are usually administered as follows:
  - Minutes are complete, clear and concise, providing a record of proceedings, including the issues, outcomes and actions with clear responsibilities and timelines attached
  - Draft minutes are provided to the chair within a week of the meeting for clearance and distributed to audit committee members within two weeks of the meeting
  - Within two weeks of the meeting, the audit committee secretariat provides senior management with a brief summary of issues dealt with at each meeting, including details of actions to be taken with assigned responsibilities and timelines
  - The minutes are circulated to the board with the papers of the next board meeting after the audit committee meeting
  - The chair should brief the board on significant issues
  - The minutes are signed by the chair at the subsequent audit committee meeting.

## Attendance

Regarding attendance at audit committee meetings, the following matters should be considered:

- Attendance of non-members is by invitation only. Audit committees should always reserve this right to meet alone, without non-members, including management, in attendance. This enables the audit committee to approach its tasks objectively and to maintain both actual and perceived independence
- The CEO, CFO and other relevant staff are generally invited to attend meetings to participate in discussion of particular agenda items. Their presence can provide an opportunity to resolve issues swiftly and efficiently
- The internal auditor and external auditor are generally invited to attend relevant parts of each meeting. Where necessary, the chair might decide that they should not attend for certain agenda items
- The audit committee should meet separately, at least annually, with both the internal auditor and the external auditor to discuss issues of mutual interest, without management present.

The chair of the audit committee is likely to have meetings with key executives and advisors outside the audit committee meetings to ensure ongoing awareness of issues and activities as they arise.

## Reporting by the audit committee

### To the board

The formality, detail and frequency of audit committee reports to the board vary. The audit committee refers to its charter when preparing a report.

Ideally, the audit committee should formally report to the board at the board meeting following each audit committee meeting, providing a summary of the audit committee's work and results.

The report should typically cover areas such as:

- The audit committee minutes<sup>63</sup>, including details of members present
- Any formal resolutions of the audit committee
- Assessment of management processes supporting external reporting
- Procedures for selection and appointment / removal of external auditor
- Information about the audit processes and the results of work completed by the internal and external auditors as well as an assessment thereof
- Any determination by the audit committee about the external auditor's independence
- The annual review of the audit committee charter and whether the audit committee has achieved the responsibilities set out in the charter
- Any recommendations requiring board actions and/or approval
- Audit recommendations for corrective action and status report
- Information about instances of actual, suspected or alleged fraud, if any
- Information about whistleblowing by employees or other parties, if any
- Any concerns about the entity's ability to continue as a going concern
- Recommendations on whether to extend the rotation period for the external audit engagement partner beyond five years to a maximum of seven years<sup>64</sup>
- Information about the annual transparency report published by the external auditor, if applicable<sup>65</sup>
- Information about an audit deficiency report published by ASIC on its website, if applicable

Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012* an audit deficiency is where ASIC reasonably believes that there is a significant weakness, in the auditor's quality control system or a significant weakness in the conduct of the audit that may be detrimental to the overall quality of the audit as a result of a failure by the auditor to comply with:

- auditing standards
- the auditor independence requirements of the *Corporations Act 2001*
- any applicable code of professional conduct
- provisions of the *Corporations Act 2001* dealing with the conduct of audits.

- Information about any communications received directly from ASIC regarding significant matters (such as an audit client's accounting or disclosure practices)

<sup>63</sup> APES GN 41 Management Representations prepared and issued by the Accounting Professional and Ethical Standards Board, provides guidance that a Member in Business who is at the audit committee level should consider taking reasonable steps to ensure that key decisions made at those meetings are appropriately reflected in the minutes of the applicable meeting.

<sup>64</sup> See footnote 18

<sup>65</sup> Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, an individual auditor, an audit firm or an authorised audit company conducting audits of ten or more entities of certain specified categories is required to publish an annual transparency report. The disclosures in the transparency report will include the names of relevant entities audited, information about the auditor's governance structure and independence practices, and other information.

identified while exercising its functions and powers in relation to audit (mainly its surveillance and inspection activities)<sup>66</sup>

- Information about correspondence from other regulators or stakeholders, if any (for example, from APRA in relation to APRA-regulated entities)
- Other matters the audit committee believes need to be reported to the board.

### To the shareholders

The annual report would typically include information on the audit committee's role and responsibilities, structure and membership, and its principal activities during the year. This information would be included as part of the wider corporate governance information in the annual report.

Improving the communication channels to investors highlights the importance of the active role that audit committees play in promoting greater transparency in reporting.

The following material would typically be included in the corporate governance section of the annual report:

- A summary of the role of the audit committee
- Details of the names and qualifications of those appointed to the audit committee, or, where the audit committee has not been formed, those who fulfil the functions of an audit committee
- The number of meetings of the audit committee and the names of the attendees.

### To other stakeholders

The following information may be publicly available on an entity's website in a clearly marked corporate governance section:

- The audit committee charter
- Description of the role and responsibilities of the audit committee
- A description of the audit committee's oversight role for the entity's governance, risk management and internal control
- Names of audit committee members, professional background and qualifications
- Information on procedures for the selection and appointment of the external auditor, and for the rotation of external audit engagement partner
- Information on procedures for the selection and appointment of the internal auditor.

## Assessing performance

### Assessing the audit committee's performance

Recent pronouncements on corporate governance have emphasised the need for boards and board committees to demonstrate a high level of professionalism, including a regular assessment of ways in which their performance can be improved. ~~The board may annually review the performance of the audit committee, preferably as part of the whole of board review.~~

An assessment of audit committee performance by the board should be undertaken as part of any periodic review of overall board performance, although a high performing audit

<sup>66</sup> The *Corporations Legislation Amendment (Audit Enhancement) Act 2012* gives ASIC the power to communicate directly with the audit committee, other directors or senior management of an entity in relation to significant matters identified by ASIC during the course of the exercise of its statutory functions in relation to audit.

committee is also likely to consider on an annual basis how it can improve its performance in the year to come.

Matters for consideration ~~by the board~~ in any review of performance include:

- Identifying and agreeing to the criteria by which the performance of the audit committee will be assessed
- Assessing the effectiveness of the audit committee as a whole and the performance of individual audit committee members
- Identifying the process for implementing action plans developed in response to areas identified for improvement
- Assessing compliance with the audit committee's charter.

~~The~~ A performance assessment may be carried out by a third part of the board ~~may require the or an~~ audit committee may elect to utilise to a self-assessment approach to its performance, with findings reported and report its findings to the board. A self-assessment guide for audit committees is provided in Appendix 2.

Audit committees ~~should~~ may also wish to take advantage of opportunities to benchmark their organisational procedures and activities with audit committees in similar entities.

### **Evaluation of individual audit committee members**

Evaluation of individual audit committee member performance may be carried out by a third party, by the chair of the audit committee (possibly in conjunction with the board chair) or by self-assessment by individual committee members.

~~The chair of the audit committee may undertake an annual performance assessment of individual audit committee members as part of the board review process.~~

~~The~~ Any assessment would typically cover issues such as whether the member has ~~displayed~~ demonstrated:

- A good understanding of, and commitment to, the audit committee's role and responsibilities
- Objectivity and independence
- An ability and willingness to take difficult but constructive stands at meetings when necessary
- A good understanding of the entity's business
- A sound understanding of the entity's financial reporting issues and obligations
- A good understanding of the entity's risk management and internal control processes
- ~~P~~Their participation in activities to keep their business, industry, financial and regulatory knowledge current
- ~~P~~Their preparation for, and participation in, audit committee meetings.

~~A~~ udit committees can use tools such as a self-assessment questionnaire to assist with the evaluation of a member's performance and contribution to the audit committee. ~~A self-assessment guide for audit committees~~ is included at Appendix 2.

Areas of additional focus arising out ~~Results~~ of performance assessments should be formally communicated to the board.

### **Further reading**

*Corporate Governance Principles and Recommendations- 3<sup>rd</sup> edition* ~~with 2010 Amendments, June 2010~~ 2014, ASX Corporate Governance Council, Australia

*Audit Committee Effectiveness—What Works Best*, 4th ed., June 2011, sponsored by The Institute of Internal Auditors Research Foundation and prepared by PricewaterhouseCoopers LLP

*The Audit Committee Handbook*, 5th ed., March 2010, Louis Braiotta, Jr., R. Trent Gazzaway, Robert Colson, Sridhar Ramamoorti, USA

*International Professional Practices Framework*, 2011, The Institute of Internal Auditors Inc.

*Walk the line: Discussion and insights with leading audit committee members*, February 2012, The Institute of Chartered Accountants Australia, Financial Reporting Council (UK) and The Institute of Chartered Accountants of Scotland

~~*Going Concern Issues in Financial Reporting A Guide for Companies and Directors*, 2009, Auditing and Assurance Standards Board and the Australian Institute of Company Directors.~~

~~*Underlying Profit: Principles for reporting of non-statutory profit information*, 2009, the Australian Institute of Company Directors and the Financial Services Institute of Australasia~~  
~~*Public Sector Audit Committees*, March 2015, Australian National Audit Office~~

~~*Governance in focus: Audit Committee Effectiveness*, February 2015, The Deloitte Academy~~

## Appendix 1

### Sample audit committee charter

The following is one example of an audit committee charter and captures many of the good practices used today. No sample charter encompasses all activities that might be appropriate to a particular audit committee, nor will all activities identified in a sample charter be relevant to every committee. Each committee should tailor this charter to their needs and governing rules.

The audit committee's annual work plan may be developed having regard to, and being cross-referenced to, its charter to ensure that the audit committee acts according to its authority and fulfils its responsibilities.

### Sample audit committee charter

#### Purpose

The audit committee is appointed by the board of directors to assist the board in discharging its responsibilities to oversee corporate reporting processes, including the financial reporting process, risk management and internal control, external audit, internal audit and compliance with laws, regulations, internal policies (including the code of conduct) and industry standards.

#### Authority

The board authorises the audit committee, within its scope of responsibilities, to:

- Perform the activities identified within this charter
- ~~Make recommendations to the board on the appointment, compensation and retention of the external auditor~~

- ~~Approve the terms of the external audit engagement (other than the audit fee, although some audit committee charters may allow the audit committee to approve the fee or may make provision for the audit committee to recommend the audit fee to the board)~~
- ~~Oversee the work of the external auditor~~
- ~~Consider any disagreements between management and the external auditor related to financial reporting~~
- ~~Require the attendance of management at meetings as appropriate~~
- ~~Have unrestricted access to employees and relevant entity information~~
- ~~Meet with external auditors, independent legal counsel and other external advisers as necessary~~
- ~~Engage independent legal counsel, accountants and other external advisers as it considers necessary to carry out its duties.~~

### **Composition**

~~The audit committee will consist of [insert number (at least three)] non-executive members of the board of directors, the majority being independent.~~

~~The board, on the recommendation of its nominating committee (where applicable), will appoint audit committee members and the audit committee chair.~~

~~Each audit committee member should have skills, knowledge and experience appropriate to the entity's business.~~

~~The committee, as a whole, should have a mix and balance of relevant skills, knowledge and experience.~~

~~Each audit committee member must be financially literate. At least one member must have accounting or related financial expertise.~~

### **Chair**

~~Preferably, the chair of the audit committee should be independent and not be the chair of the board. (If the entity is in the S&P/ASX 300 at the beginning of its financial year, then this is a requirement.)~~

~~The chair will carry out the following responsibilities:~~

- ~~Promote effective communications between the audit committee and the board, CEO, CFO, CAE, other senior management and the external auditor~~
- ~~Ensure audit committee meetings run smoothly, that the views of all audit committee members are heard, that adequate time is allowed for discussion of each issue and that the agenda and meeting papers properly reflect proceedings.~~

### **Meetings**

~~The audit committee will typically meet at least four times a year, with authority to convene additional meetings, if necessary to fulfil the audit committee charter. All audit committee members are expected to attend each meeting, in person or via teleconference or video conference.~~

~~Only audit committee members are entitled to attend meetings. The audit committee may invite other people (such as the other board members, CEO, CFO, CAE, internal legal counsel and the external auditor) to its meetings as it considers necessary.~~

~~An agenda and meeting papers will be prepared and provided in advance to members, along with appropriate briefing materials.~~

~~Agreed decision-making processes and voting protocols will be followed.~~

~~Minutes of meetings will be prepared and circulated to audit committee members and to the board at its next meeting.~~

## Responsibilities

The audit committee will carry out the following responsibilities:

### ***Financial Corporate Reporting***

- Gain an understanding of the current areas of greatest financial risk and how they are managed
- Review significant accounting and reporting issues, including recent professional and regulatory pronouncements, and understand their impact on financial reports
- Review complex or unusual financial transactions and highly judgemental areas, and understand their effect on the financial report
- Oversee the periodic financial reporting process implemented by management and review the interim financial statements, annual financial statements, concise financial report, if any, and preliminary announcements before their release
- Meet with management and the external auditor to review the financial statements, key accounting policies and decisions, and the results of the audit, including significant adjustments, unadjusted differences and any difficulties encountered or unresolved disagreements with management
- Review all representation letters signed by management and assess for completeness and appropriateness
- With management and the external auditor, review all matters required to be communicated to the audit committee under Australian Auditing Standards, such as key audit matters for listed companies.
- Review the CEO and CFO declarations regarding the financial report and financial records, prepared in accordance with the requirements of the Corporations Act 2001
- Based on its review of the financial statements, note disclosures and other information, provide a recommendation to the board whether the financial report should be approved
- Review the other sections of the annual report before its release and consider whether the information is understandable and consistent with members' knowledge about the entity and its operations, and is unbiased
- Review management's process for ensuring that information contained in analyst briefings, investor presentations and press announcements is consistent with published financial information, and is balanced and transparent.

### ***Working with the external auditor***

- Provide a recommendation to the board on the appointment of the external auditor or the assessment of potential and continuing auditors, reappointment or termination of the appointment of the external auditor
- ~~Where appropriate, provide a recommendation to the board on extending the rotation period of the external audit engagement partner from five years up to a maximum of seven years~~
- ~~Annually review the performance of the external auditor~~ Assess the quality of the audit conducted and evaluate performance of the auditor

- Consider the independence of the external auditor and any potential conflicts of interest. Maintaining and reviewing auditor independence and objectivity by considering the external auditor's relationships and services with the entity and other relevant organisations
- Review the external auditor's proposed audit scope and approach for the current year in light of the entity's circumstances and changes in regulatory and other requirements
- Establishing ongoing communications with the auditors so as to address any risk or areas of concerns and ensure access to directors and the audit committee. Discuss with the external auditor any difficulties encountered in the audit, including any restriction on audit scope, access to information and any significant resolved or unresolved disagreements with management
- Discuss with the external auditor the appropriateness of the accounting policies applied by management in the entity's financial reports
- Facilitating the audit process by supporting the audit and ensuring company management are accountable, supportive and helpful to the audit process. Discuss with the external auditor, and assess the appropriateness of, management's responses to significant findings and recommendations made by the external auditor
- At least once a year meet separately with the external auditor to discuss matters that the audit committee or auditor believes should be discussed privately. Ensure the external auditor has access to the chair of the audit committee when required.
- Develop policies for the provision of non-audit services by the external auditor, including other assurance engagements, and, where applicable, pre-approve such services
- Monitor the relationship between internal and external auditors.

#### **Working with ~~the~~ internal audit activity**

- Recommend to the board on the appointment, ~~promotion and/or dismissal~~ removal of the CAE
- Review ~~and approve the internal audit the~~ charter, activities, resources and organisational structure of the internal audit activity and ensure there are no unjustified restrictions or limitations
- Ensure the internal auditor reports to the audit committee for functional purposes and to the CEO for administrative purposes, and has access to all levels of management with the right to seek information relevant to the internal audit activity
- Review ~~and approve~~ the ~~strategic~~ internal audit plan, ~~often for a 2-3 year period~~ to assess whether it addresses the material business risks of the entity
- ~~Review and approve the annual internal audit plan and any significant changes made to the plan and that there is appropriate coordination with the external auditor~~
- ~~Review and approve the scope of the internal audit plan and work program~~ Review reports of results of internal audit engagements, audit-related activities, team capability, audit performance and other important matters
- Monitor ~~the progress of the internal audit plan and work program, and the implementation of the findings and recommendations of the internal audit activity~~ compliance with standards, together with quality and improvement arrangements
- ~~Consider the processes implemented by the entity for monitoring and assessing the effectiveness of the internal audit activity~~
- ~~Without management being present, meet periodically with the CAE to discuss matters that the audit committee or internal auditor believes should be discussed privately~~
- ~~Make enquiries of the CAE to determine any scope or budget limitations that may impede the execution of internal audit responsibilities.~~

### ***Risk management and internal control***

- Consider whether the entity has an appropriate attitude towards controls and communicate the importance of risk management and internal control
- Ensure that management has appropriate processes for identifying, assessing and responding to risks in a manner that is in accordance with the entity's risk appetite, and that those processes are operating effectively
- Ensure that material business risks, including operational, financial, legal and compliance risks, are appropriately reflected in the risk profile and reported to the board at least annually
- Evaluate the overall effectiveness of the risk management and internal control framework, including activities undertaken by internal **audit** and external audit, **and together with any other assurance providers, related to the framework to provide a holistic picture of assurance across the entity**
- Understand the internal control systems implemented by management for the approval of transactions, the recording and processing of financial data, and ensuring that financial statements comply with relevant standards and requirements, and are subject to appropriate management review
- Understand the internal control systems implemented by management for the security of computer systems and applications, and the contingency plans for processing financial information in the event of a systems breakdown, or to protect against computer fraud or misuse
- Understand the processes management has implemented for managing insurable risks and, if applicable, self-insurance, including assessing the adequacy of insurance cover
- Meet periodically with the head of risk management without other management being present.

### ***Compliance with laws, regulations, ethical requirements, internal policies and industry standards***

- Review the effectiveness of the entity's systems for monitoring compliance with laws, regulations, internal policies and industry standards, and the results of management's investigation and follow-up (including disciplinary action) of any instances of non-compliance
- Obtain regular updates from management and the head of compliance about compliance matters that may have a material impact on the entity's financial statements, strategy, operations or reputation, including material breaches of laws, regulations, standards and company policies
- Review and liaise with management and/or regulators, as appropriate about the findings of any examinations by regulators
- Review and, where applicable, approve the policies, processes and framework for identifying, analysing and addressing complaints (including whistleblowing) and review material complaints and their resolution
- Review the entity's process for communicating the code of conduct to staff and assess the effectiveness of, and compliance with the code
- Discuss with management whether all regulatory compliance matters of the entity have been considered in the preparation of the financial statements
- Meet periodically with the head of compliance and legal counsel without other management being present.

### ***Fraud and Corruption***

- Ascertain whether fraud/corruption-risks have been included in the assessment of the risk profile of the entity
- Review management's anti-fraud/corruption -strategies and programs
- Enquire of management, ~~the internal auditor~~ and the external auditor regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments
- Enquire of management, the internal auditor and the external auditor whether they are aware of any actual, suspected or alleged fraud or corruption affecting the entity and how they responded to such instances, including any changes made to the internal control environment
- Obtain representations from management that all known instances of actual, suspected or alleged fraud or corruption, have been disclosed to the audit committee
- Ensure the entity has fulfilled its fraud or corruption reporting obligations, if any.

### ***Reporting responsibilities***

- Report regularly to the board about audit committee activities and make appropriate recommendations
- ~~• Ensure the board is aware of matters that may significantly affect the financial condition or affairs of the entity~~
- ~~• Prepare any reports requested by the board, such as a report on the audit committee's responsibilities and activities to be included in the corporate governance section in the annual report~~
- ~~• Facilitate open communication between internal auditor, the external auditor and the board.~~

### ***Evaluating performance***

- Evaluate the audit committee's own performance (that of individual members and collectively) on a regular basis
- ~~• Assess the committee's achievement of responsibilities specified in this charter and report the findings to the board.~~

### ***Review the audit committee charter***

- ~~• Annually review the audit committee charter and discuss required changes with the board~~
- ~~• Ensure that the charter is approved or re-approved by the board.~~

### ***Other responsibilities***

- Perform other activities related to this charter as requested by the board.

### ***-Membership***

The audit committee will consist of [insert number (at least three)] non-executive members of the board of directors, the majority being independent.

The board, on the recommendation of its nominating committee (where applicable), will appoint audit committee members and the audit committee chair who will be an independent and not the chair of the Board.

Each audit committee member should have skills, knowledge and experience appropriate to the entity's business.

The committee, as a whole, should have a mix and balance of relevant skills, knowledge and experience.

Each audit committee member must be financially literate. At least one member must have accounting or related financial expertise.

### **Meetings**

The audit committee will typically meet at least four times a year, with authority to convene additional meetings, if necessary to fulfil the audit committee charter. All audit committee members are expected to attend each meeting, in person or via teleconference or video conference.

- Only audit committee members are entitled to attend meetings. The audit committee may invite other people (such as the other board members, CEO, CFO, CAE, internal legal counsel and the external auditor) to its meetings as it considers necessary.

An agenda and meeting papers will be prepared and provided in advance to members, along with appropriate briefing materials.

Agreed decision-making processes and voting protocols will be followed.

Minutes of meetings will be prepared and circulated to audit committee members and to the board at its next meeting.

## **Appendix 2**

### **Self-assessment guide for audit committees**

This guide has been provided to illustrate the types of considerations against which the audit committee might assess its performance collectively. Similar considerations may be applied to the assessment of the performance of individual members of the audit committee.

The guide includes a large number of considerations and should be tailored by each audit committee to meet its own requirements. The audit committee may complete the guide as a whole or individually, and then collate individual responses. The chair of the audit committee and members may decide to weight certain aspects of the self-assessment guide more than others. The audit committee may also seek input from non-member attendees and separately assess the information received.

The results of the self-assessment should be used by the audit committee for discussion to identify areas for improvement and a summary of agreed action items should be provided to the chair of the board.

We suggest the responses to the statements below are rated using a rating scale, such as the Likert Scale. A Likert-type scale assumes that the strength/intensity of experience is linear, i.e. on a continuum from strongly agree to strong disagree, and makes the assumption that attitudes can be measured.

Likert scale examples include the following:

- Agreement – Strongly agree/Agree/Undecided/Disagree/Strongly disagree

- Frequency – Very frequently/Frequently/Occasionally/Rarely/Never
- Importance – Very important/Important/Moderately important/Of little importance/Unimportant
- Likelihood – About always true/Usually true/Occasionally true/Usually not true/Almost never true

The audit committee's self-assessment approach should be consistent with the committee's charter. For this reason, the considerations listed below reflect the structure and content of the sample charter provided in Appendix 1.

## Assessing Audit Committee Performance

In evaluating the performance of the audit committee, the following would typically be considered.

### Authority

- Has the Audit Committee has obtained authority from the board to perform the activities in its charter
- ~~Has been able to require the attendance of management at audit committee meetings, as necessary~~
- ~~Has had unrestricted access to management, employees and relevant information~~
- ~~Has been able to meet with independent legal counsel and other external advisers as necessary~~
- ~~Has been able to engage independent legal counsel, accountants and other external advisers as it considers necessary.~~

### Composition

- ~~The size of the audit committee is appropriate to the entity and the responsibilities in the audit committee charter~~
- ~~All audit committee members are non-executive directors~~
- ~~The majority of audit committee members are independent~~
- ~~The mix of skills, knowledge and experience of the audit committee as a whole has been reviewed and is appropriate~~
- ~~All audit committee members have skills, knowledge and experience appropriate to the entity's business~~
- ~~All audit committee members are financially literate and able to understand financial statements; at least one member has accounting or related financial expertise.~~

### Chair

- ~~The chair of the audit committee is preferably independent and not the chair of the board (for S&P/ASX 300 entities, this is a requirement).~~

### Meetings

- ~~The audit committee meets regularly throughout the year and the number of meetings is appropriate for the nature of the entity and the responsibilities of the audit committee~~
- ~~Only audit committee members are entitled to attend meetings. The CEO, CFO, CAE, internal legal counsel, other senior management and the external auditor are invited to attend meetings as necessary~~
- ~~Audit committee members attended every meeting or provided input, if unable to attend~~

- ~~Decisions were made by the audit committee in accordance with agreed decision-making processes and voting protocols.~~

### ***Agenda, meeting papers and minutes***

- ~~The agenda and meeting papers are provided in advance of meetings, with sufficient time allowed for members to prepare for meetings~~
- ~~Minutes of meetings are prepared and circulated promptly to audit committee members, to the board at its next meeting and to internal and external auditors, as necessary.~~

## **Responsibilities**

### ***Financial reporting***

- ~~CC~~ained an understanding of the current areas of greatest financial risk and how they are being managed
- ~~RR~~viewed significant accounting and reporting issues, including recent professional and regulatory pronouncements, and gained an understanding of their impact on the financial report
- ~~RR~~viewed complex or unusual financial transactions and highly judgemental areas, and understood their effect on the financial report
- ~~Provided an oversight role of the periodic financial reporting process implemented by management and reviewed interim financial statements, annual financial statements, concise financial report, if any and preliminary announcements before their release~~
- ~~The Audit Committee has met~~Met with management and the external auditor to review and understand the interim financial statements, annual financial statements, concise financial report, if any, and preliminary announcements prior to their release. In particular, reviewed key accounting policies and decisions, and the results of the audit, including significant adjustments, unadjusted differences and any difficulties encountered or unresolved disagreements with management?
- Reviewed all representation letters signed by management, for completeness and appropriateness
- ~~RR~~viewed with management and the external auditor all matters required to be communicated to the audit committee under Australian Auditing Standards, including key audit matters when appropriate
- Reviewed the CEO and CFO declarations in respect of the financial report and financial records
- ~~RR~~viewed the financial statements, note disclosures and other information and recommended to the board whether the financial report should be approved
- ~~RR~~viewed other sections of the annual report before its release, for consistency with members' knowledge about the entity and its operations, is unbiased
- ~~RR~~viewed management's process for ensuring that information contained in analyst briefings, investor presentations and press announcements was consistent with published financial information, and was balanced and transparent.

### ***Working with the external auditor***

- Recommended to the board on the appointment of the external auditor or the assessment or potential and continuing auditors, ~~reappointment or termination of the appointment of the external auditor~~
- ~~Where appropriate, provided a recommendation to the board on extending the rotation period of the external audit engagement partner from five years to a maximum of seven years~~

- ~~Considered the quality of the audit conducted and evaluated the performance of the auditor independence of the external auditor and any potential conflicts of interest~~
- ~~Reviewed the external auditor's proposed audit scope and approach auditor independence and objectivity by considering the external auditor's relationships and services with the entity and other relevant organisations~~
- ~~Discussed with the external auditor any difficulties encountered in the audit, including any restriction on audit scope, access to information and any disagreements with management (resolved or unresolved) Established effective ongoing communications with the auditors so as to address any risk or areas of concerns and ensure access to directors and the audit committee.~~
- ~~Facilitated the audit process by supporting the audit and ensuring company management are accountable, supportive and helpful to the audit process~~
- ~~Discussed with the external auditor the appropriateness of the accounting policies applied by management in the entity's financial reports~~
- ~~Discussed with the external auditor the results of the audit and management's responses to significant findings~~
- ~~The Audit Committee has mMet privately with the external auditor at least once a year without management present and ensured that the external auditor had access to the chair of the audit committee when required~~
- ~~Developed and reviewed the policies for the provision of non-audit services by the external auditor, including other assurance engagements and where applicable, pre-approved such services~~
- ~~Monitored the relationship between the internal and external auditors.~~

#### **Working with the internal audit activity**

- Where appropriate ~~the Audit Committee~~ provided recommendations to the board on the appointment, ~~promotion and dismissal removal~~ of the CAE
- ~~Review and approved ed the internal audit charter, resources and the organisational structure of the internal audit activity and ensured there were no unjustified restrictions or limitations~~
- ~~Ensured the internal auditor reports to the audit committee for functional purposes and to the CEO for administrative purposes~~
- ~~Reviewed and approved the strategic internal audit plan~~
- ~~Reviewed and approved the annual internal audit plan and any significant changes~~
- ~~Reviewed reports on the results of internal audit engagements, audit-related activities, audit team capability, audit performance and other important matters~~
- ~~Monitored compliance with standards, together with quality and improvement arrangements~~
- ~~Discussed with the internal auditor any difficulties encountered in the internal audit process, including any restrictions on access to information and any disagreements with management (resolved or unresolved)~~
- ~~Ensured the internal audit plan is risk-based, addressing the material business risks of the entity~~
- ~~Reviewed and approved the scope of the internal audit plan and work program, and monitored its progress throughout the year~~
- ~~Considered the processes the entity had implemented for monitoring and assessing the effectiveness of the internal audit activity~~
- ~~The Audit Committee has mMet privately with the internal auditor at least once a year without management present~~
- ~~Made enquiries of the CAE to determine the scope of budget limitations that could impede the execution of internal audit responsibilities.-~~

### ***Risk management and internal control***

- ~~AA~~ssessed the entity's attitude towards controls and promoted the importance of risk management and internal control
- ~~Ensured management has appropriate processes~~ ~~Reviewed and assessed the effectiveness of management's processes~~ for identifying, assessing and responding to risks, ensuring that they are appropriate to the entity's risk appetite and these processes were operating effectively
- ~~EE~~nsured the material business risks, including operational, financial, legal and compliance risks, are appropriately reflected in the risk profile and reported at least annually to the board
- ~~EE~~valuated the overall effectiveness of the risk management and internal control framework, including activities undertaken by internal and external audit, ~~and together with any~~ other assurance providers, ~~related to the framework~~ to provide a holistic picture of assurance across the entity
- ~~OO~~btained an understanding of the internal control systems implemented by management for the approval of transactions, the recording and processing of financial data, and ensuring that financial statements complied with relevant standards and requirements, and ~~were ensured they are~~ subject to appropriate management review
- ~~RR~~viewed the adequacy of controls for the security of computer systems and applications, and the contingency plans for processing financial information in the event of systems breakdown, or computer fraud or misuse
- Reviewed the processes management has implemented for managing insurable risks and, where applicable, self-assurance, and assessed the adequacy of insurance cover
- ~~The Audit Committee has m~~et privately with the head of risk management without management being present:-

### ***Compliance and ethics***

- ~~RR~~viewed the effectiveness of management's systems for monitoring compliance with law, regulations, internal policies and industry standards, and the results of management's investigations and follow-up of any instances of non-compliance
- ~~OO~~btained regular updates from management and the head of compliance about compliance matters that may have a material impact on the entity's financial statements, strategy, operations or reputation, including material breaches of laws, regulations, standards and company policies
- ~~LL~~iaised with management and/or regulators, as appropriate, about the findings of any examinations by regulators
- ~~RR~~viewed and approved (where applicable) the policies, processes and framework for identifying, analysing and addressing complaints (including whistleblowing) and reviewed material complaints and their resolution?
- ~~RR~~viewed the entity's process for communicating the code of conduct to staff and assessed the effectiveness of, and compliance with, the code
- ~~DD~~iscussed with management whether all regulatory compliance matters of the entity were considered in the preparation of the financial statements
- ~~Met~~ ~~The Audit Committee met~~ privately with the head of compliance and legal counsel, without management being present:-

### ***Fraud and Corruption***

- Ensured fraud risks have been included in the assessment of the risk profile of the entity
- ~~RR~~viewed management's anti-fraud and corruption strategies and programs

- ~~EE~~ Enquired of management, ~~the internal auditor~~ and the external auditor regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments
- ~~EE~~ Enquired of management, the internal auditor and the external auditor whether they have any knowledge of actual, suspected or alleged fraud or corruption affecting the entity and how they responded, including any changes made to the internal control environment
- ~~OO~~ Obtained representations from management that all known instances of actual, suspected or alleged fraud or corruption have been disclosed to the audit committee
- ~~EE~~ Ensured that management has fulfilled the entity's fraud and corruption reporting obligations, if any:-

### **Reporting by the audit committee**

- ~~The Audit Committee r~~ Report ~~sed~~ regularly to the board on the audit committee's activities and made recommendations where appropriate
- ~~Ensured the board was aware of matters that may significantly affect the financial condition or affairs of the entity~~
- ~~Prepared reports requested by the board~~
- ~~Facilitated open communication between internal audit activity, the external auditor and the board:-~~

### **Evaluating performance**

- ~~The Audit Committee e~~ Evaluate ~~d~~ the audit committee's performance, as a whole and for each member, at least once a year, ~~including its achievement of the responsibilities specified in the audit committee charter~~
- ~~Reported on the results of the evaluation of the audit committee's performance to the board:-~~

### **Review of the audit committee charter**

- ~~Reviewed the charter to ensure it articulates the audit committee's responsibilities~~
- ~~Ascertained that the charter facilitates and supports the effective operation of the audit committee:-~~

### **Other responsibilities**

- ~~The Audit Committee has satisfactorily p~~ Performed other activities, as requested by the board:-

### **Composition**

- T ~~The~~ size of the audit committee is appropriate to the entity and the responsibilities in the audit committee charter
- A ~~All~~ audit committee members are non-executive directors
- T ~~The~~ majority of audit committee members are independent
- T ~~The~~ mix of skills, knowledge and experience of the audit committee as a whole ~~has been reviewed and is appropriate~~
- A ~~All~~ audit committee members have skills, knowledge and experience appropriate to the entity's business
- A ~~All~~ audit committee members ~~are financially literate and able to understand financial statements; with at least one member has~~ with accounting or related financial expertise:-

### Meetings

- The audit committee meets regularly throughout the year and the number of meetings is appropriate for the nature of the entity and the responsibilities of the audit committee
- Only audit committee members are entitled to attend meetings, with the CEO, CFO, CAE, internal legal counsel, other senior management and the external auditor are invited to attend meetings as necessary
- Audit committee members attended every meeting or provided input, if unable to attend
- The agenda and meeting papers are provided well in advance of meetings
- Decisions were made by the audit committee in accordance with agreed decision-making processes and voting protocols
- Minutes are taken and appropriately circulated to committee members in a timely manner, and to the Board at its next meeting

### Overall

- What has been done well on the Audit Committee this year?
- What has not been done well on the Audit Committee this year?
- What are three areas for improvement for the Audit Committee operations and processes going forward?

## Appendix 3

### Management representation letter

#### **Internal management representations to those charged with governance** **Matters commonly included in management representation letter**

Representation letters are commonly used by those charged with governance to assist them in discharging their obligations to external parties. Such representations may include:

- Financial Reporting Certifications including Internal Control Questionnaires;
- Declarations provided to the board or audit committee of local or foreign jurisdictions in accordance with the respective jurisdiction's regulations; or
- Representations in respect of continuous disclosure obligations to enable disclosures to the market may be requested by the external auditor, the board or the audit committee in relation to the audit of the financial report.

Section 8 of APES GN 41 *Management Representations* prepared and issued by the Accounting Professional and Ethical Standards Board provides guidance in relation to management representation considerations at the audit committee level.

## **External management representations to the external auditor**

The external auditor requests written representations from management with appropriate responsibilities for the financial report<sup>67</sup>. The following list is provided to assist audit committees to understand the types of representations included in a representation letter prepared and signed by management. It includes selected matters that are commonly included and may not include all representations provided by management to the external auditor. It is provided for information purposes only and is not definitive.

Management would ordinarily represent, or confirm, to the external auditor that:

### **Regarding the financial report**

- Management has fulfilled its responsibilities for the preparation of the financial report in accordance with [the applicable reporting framework]
- All transactions have been recorded in the accounting records and are reflected in the financial report
- Significant assumptions used by management in making accounting estimates, including those measured at fair value, are reasonable
- Related party relationships and transactions have been appropriately accounted for and disclosed
- All events subsequent to the date of the financial report required to be adjusted or disclosed have been adjusted or disclosed
- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial report as a whole. (A list of the uncorrected misstatements may be attached to the representation letter)

### **Regarding the information provided**

- Management has provided the auditor with:
  - access to all information of which they are aware that is relevant to the preparation of the financial report such as records, documentation and other matters
  - additional information that the auditor has requested from them for the purpose of the audit
  - unrestricted access to persons within the entity from whom the auditor determined it necessary to obtain audit evidence
  - all information required to be provided by the law or regulations.
- Management has disclosed to the auditor:
  - the results of their assessment of the risk that the financial report may be materially misstated as a result of fraud
  - all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial report communicated by employees, former employees, analysts, regulators or others
  - all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial report
  - all known actual or possible litigation and claims whose effects should be considered when preparing the financial report; and accounted for and disclosed in accordance with [the applicable financial reporting framework]
  - the identity of the entity's related parties and all the related party relationships and transactions of which we are aware
  - all the documents that they expect to issue that may comprise other information.

<sup>67</sup> See Auditing and Assurance Standards Board ASA 580 *Written Representations*

### Regarding other matters

- Management acknowledges its responsibility for the design, implementation and maintenance of internal control to prevent, deter, detect and report on fraud.

## Appendix 4

### External audit versus internal audit

There are fundamental differences between the work of external audit and internal audit which are shown in the following table:

External Audit		Internal Audit
Appointed from outside the organisation (independently appointed in the public sector)	Status	Employees of the organisation, or can be an independent entity through outsourced or co-sourced arrangement
Independent of management and the governing body (including board of directors)	Independence	Independent of activities audited, but able to respond to the needs of management and the audit committee
Serves third parties that need reliable financial information, including shareholders (corporate sector) and parliament (public sector)	Serving	Serves the needs of the organisation
Shareholders and board of directors	Reports to	Audit committee functionally for operations and chief executive officer for administration
True and fair view of financial statements	Objective	Varies according to the audit – focused on evaluating controls designed to assure the accomplishment of the organisation's goals and objectives
Historical events as expressed in financial statements	Focus	Forward-looking
Reviews records supporting the financial statements (periodically, usually annually)	Coverage	Reviews governance, risk management, and control processes according to risk-based need
Opinion on financial statements	Outcome	Helps organisation to enhance and protect organisation value and accomplish their objectives
Incidentally concerned with prevention and detection of fraud and corruption in general, but is directly concerned when financial statements may be materially affected	Fraud and Corruption	Is directly concerned with the prevention of fraud and corruption in any activity reviewed
Shareholders, regulators, board of directors and audit committee	Reports go to	Management and audit committee
External audit standards	Standards	Internal audit standards
Mandatory	Qualifications	Not mandatory, though there is a recent shift in some jurisdictions to require the chief audit executive to have appropriate certifications and qualifications, or

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<u>External Audit</u>	<u>Internal Audit</u>
	demonstrated high-level experience

## Glossary

### APRA-regulated entities

Entities that are regulated by the Australian Prudential Regulation Authority (APRA), including banks, building societies and credit unions (authorised deposit-taking institutions), life and general insurance and reinsurance companies, friendly societies and superannuation funds (excluding self-managed funds).

### Audit adjustments

Corrections made to misstatements in financial information or disclosures identified by the auditor in conducting an audit of the financial report.

### Audit engagement partner

The partner or other person in the audit firm who is responsible for the audit engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

### Business risks

All risks to the organisation including operational, financial, compliance and strategic risks.

### Chief audit executive (CAE)

A person in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and the *International Professional Practices Framework* (IPPF), which includes the *Definition of Internal Auditing*, the *Code of Ethics* and the *International Standards for the Professional Practice of Internal Auditing*.

### Concise financial report

A report for a financial year prepared under Chapter 2M of the *Corporations Act 2001* in accordance with Australian Accounting Standard AASB 1039 *Concise Financial Reports*.

### Continuous disclosure obligations

Continuous disclosure is the timely advising of information to keep the market informed of events and developments as they occur. Under the ASX Listing Rules, once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities, the entity must immediately tell the ASX that information.

### Corruption

Corruption can be defined as abuse of entrusted power for private gain.

### External auditor

An individual auditor, an audit firm or an authorised audit company providing external audit services.

### **Financial report (as set out in the Corporations Act 2001)**

An annual financial report or a half-year financial report prepared under Chapter 2M of the *Corporations Act 2001*. An annual financial report contains the financial statements, notes to the financial statements and the directors' declaration about the financial statements and notes. The half-year financial report contains the financial statements and notes to the financial statements.

### **Financial statements**

A complete set of financial statements comprises:

1. A statement of financial position as at the end of the period
2. A statement of comprehensive income for the period
3. A statement of changes in equity for the period
4. A statement of cash flows for the period
5. Notes, comprising a summary of significant accounting policies and other explanatory information
6. A statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

### **Fraud**

Fraud can be defined as wrongful or criminal deception intended to result in financial or personal gain.

### **Internal audit**

Internal audit as defined by the International Professional Practices Framework (IPPF) issued by the Institute of Internal Auditors (IIA): "Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes."

### **Internal audit activity**

The function, as defined by the *International Standards for the Professional Practice of Internal Auditing*, that is: "A department, division, team of consultants or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organisation's operations. The internal audit activity helps an organisation accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes".

### **Internal auditor**

The individual/s who perform the internal audit services as part of the internal audit activity

### **International Financial Reporting Standards (IFRS)**

Standards for accounting and financial reporting issued by the International Accounting Standards Board (IASB).

### **Risk appetite**

The level of risk that the entity is prepared to accept

### **Risk profile**

The description of the entity's set of risks.

### **Representation letter**

A written statement provided by management of an entity to confirm certain matters represented by them in the financial report, or in relation to the preparation of the financial report, or to support other audit evidence. Representation letters may be requested by those charged with governance, including the audit committee, or the external auditor.

### **Those charged with governance**

The person/s or organisation/s (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process and therefore may include the audit committee.

## **List of Acronyms**

AASB	Australian Accounting Standards Board
AICD	Australian Institute of Company Directors
ANAO	Australian National Audit Office
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ASX	Australian Stock Exchange
AUASB	Australian Auditing and Assurance Standards Board
CAE	Chief Audit Executive
CEO	Chief Executive Officer
CFO	Chief Financial Officer
COSO	Committee of Sponsoring Organisations of the Treadway Commission
Finsia	Financial Services Institute of Australasia
FRC	Financial Reporting Council
IFRS	International Financial Reporting Standards
IIA	The Institute of Internal Auditors Inc.
IIA-A	Institute of Internal Auditors-Australia
IPPF	International Professional Practices Framework

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**AUDIT COMMITTEES**  
**A GUIDE TO GOOD PRACTICE**  
3rd Edition

A joint publication from the Auditing and Assurance Standards Board, Australian Institute of  
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## Introduction

An audit committee is a committee of a board of directors (board), operating under delegation of authority from the board. Its objectives are clearly defined and documented in its charter and its efficiency and effectiveness is measured by reference to its objectives.

An independent audit committee is a fundamental component of good corporate governance.<sup>1</sup>

Typically, an audit committee:

1. focuses on issues relevant to the integrity of an entity's financial reporting
2. oversees external audit, internal audit, risk management, internal control and compliance
3. liaises with the board, internal and external auditors<sup>2</sup> and management.

Some entities establish one committee with the responsibility for all of these tasks, such as an audit and risk management committee. Other entities may establish more than one committee, such as an audit committee, together with a risk and compliance committee, health and safety committee, environmental management committee and other committees. This depends on the nature of the entity, but is more common in larger entities due to the increased work load.

## Who should use this guide?

This guide is primarily for directors and audit committees of Australian listed companies. Directors, boards of management and audit committees of not-for-profit, public sector<sup>3</sup>, and other private sector entities, may also find this guide to be a useful reference.

There is no "one size fits all" good practice solution for audit committees. The nature of the business, the regulatory environment, ownership structure, legal requirements, and audit committee membership influence the objectives and activities of an audit committee. Smaller entities with limited resources might find it impractical to meet all of the practices outlined in this guide. They may use this guide to assess the elements of good practice that are relevant for their financial reporting, corporate governance, risk management and internal control and exercise them at the board or committee level.

## Purpose of this guide

This guide provides a practical introduction to the role and responsibilities of an audit committee. It explains the context in which an audit committee typically operates and outlines good practice.

While the guide assists the board and audit committee members, it may also be helpful to risk and compliance managers, internal auditors, external auditors and senior management, as it demonstrates the interactions between the audit committee and these other parties.

Clarifying the roles and responsibilities between the audit committee, risk and compliance managers and auditors (both internal and external) assists their communication, efficiency and effectiveness. Using this guide assists audit committees in assessing an entity's external

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<sup>1</sup> See Principle 4 *Safeguard Integrity in Corporate Reporting*, Recommendation 4.1 of the 3<sup>rd</sup> edition of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

<sup>2</sup> See glossary for definitions.

<sup>3</sup> Federal and state bodies should also consider their own specific guidance relating to the operation of their audit committees.

financial and other internal and external reporting requirements. It also assists in assessing the effectiveness of an entity's risk management and internal control systems.

This third edition of the guide reflects developments in audit committee practice, legislation and guidance from regulatory bodies and in leading global board practices since the previous edition was published in 2012. It has been produced by the Auditing and Assurance Standards Board, the Australian Institute of Company Directors and the Institute of Internal Auditors-Australia.

The guide does not attempt to advise directors or members of audit committees about their legal duties. For a general discussion of directors' duties refer to *Duties and Responsibilities of Directors and Officers 21st Edition* by Professor Robert Baxt AO, published by the Australian Institute of Company Directors in 2016.

### Recent developments regarding audit committees

Since the previous edition of this guide was published in 2012, some of the key developments in Australia include:

- December 2016—revised Australian Auditing Standards came into effect, some of which impact the operation of audit committees as they change the requirement in relation to the auditor reporting to the board. For example, Auditing Standard ASA 700 series, including the new ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report* and related consequential changes to other relevant audit standards, such as ASA260 *Communication with Those Charged with Governance* and ASA 570 *Going Concern*.
- March 2014—the ASX Corporate Governance Council<sup>4</sup> released the 3<sup>rd</sup> edition of the *ASX Corporate Governance Principles and Recommendations*. These revised guidelines came into effect from 1 July 2014.
- October 2010—The Institute of Internal Auditors Inc. (IIA) issued a revised *International Professional Practices Framework (IPPF)*. The IPPF has been adopted by the Institute of Internal Auditors-Australia (IIA-A) and was effective from 1 January 2011.
- January 2014—APRA released a revised Prudential Standard CPS 510 *Governance*, which came into effect on 1 January 2015 and was introduced along with the new CPS 220 *Risk Management*.

Since the global financial crisis, there has been continuing focus on corporate governance around the world. This has resulted in the review of existing governance frameworks, including accounting and auditing frameworks and regulatory reforms, to strengthen corporate governance.

Businesses, regulators, investors and the members of the public have increasingly called for more transparency in corporate reporting.

The audit committee plays a pivotal role in assisting the board in fulfilling its corporate governance obligations and enhancing the integrity and transparency of corporate reporting, particularly financial reporting, and consequently, some of the proposed reforms relate to clarifying and expanding the role of the audit committee.

---

<sup>4</sup> The ASX Corporate Governance Council was formed in August 2002 and brings together various business, shareholder and industry groups to enhance corporate governance practices in Australia. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be a practical guide for listed entities, their investors and the wider Australian community.

## The board and board committees

Under the *Corporations Act 2001* in section 201A, every company must have at least one director and public companies must have at least three directors.<sup>5</sup> Collectively, the directors are known as the board of directors (board) and its overriding responsibility is to supervise the company on behalf of shareholders and other stakeholders.

The boards of larger entities often establish committees of directors to better use their time and to help deal with complex or specialised areas, such as financial reporting and audit, compliance, risk management, sustainability or health and safety.

Committees make recommendations for action to the full board, which retains collective responsibility for decision-making.

Involvement in committees allows directors to deepen their knowledge of the organisation, become more actively engaged and fully utilise their experience. Additionally, the existence of committee can indicate to investors that the board is taking particular issues seriously.

Examples of committees include audit, risk, remuneration, nomination and investment committees. The nature and type of committees will vary from industry to industry and according to the size of the organisation. For example, a resources company may have an environmental committee, an airline may a safety committee, a charity may have a fundraising committee.

Committees may be ongoing in nature like the audit committee, usually referred to as standing committees, or may be formed for a specific short term project or goal.

Section 198D of the *Corporations Act 2001* allows boards to delegate some of their powers to a committee of directors unless the company's constitution disallows it. The delegation must be recorded in the minute book.

Section 190 provides that, when directors delegate a power under s198D of the *Corporations Act 2001* they remain responsible for the exercise of the power by the delegate as if it had been exercised by the directors themselves. There is a limited exception where the director who delegates will not be held responsible if that director believed:

- On reasonable grounds at all times that the delegate would exercise the power in conformity with the duties imposed by the Act and the company's constitution; and
- On reasonable grounds and in good faith (and after making proper inquiries if circumstances so required) that the delegate was reliable and competent in relation to the power delegated.

Section 189 gives authority for the rest of the board to reasonably rely on the information or advice given by a committee so long as it is independently assessed by the board and is relied upon in good faith. However, this delegation of authority does not lessen the board's overall duties and responsibilities.

The 3<sup>rd</sup> edition of the ASX Corporate Governance Council's Principles and Recommendations recommends that the board establish three committees – audit, remuneration and nomination. In addition it recommends that boards should have a committee or committees to oversee risk. In some cases this function is combined with the audit committee. In other cases it is a standalone committee of the board.

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<sup>5</sup> This requirement does not include alternative directors, and two of the three directors (one for proprietary companies) need to ordinarily reside in Australia.

Similarly, APRA's prudential standards include the establishment of the audit committee and a remuneration committee. These requirements are imposed on authorised deposit taking institutions (or example banks, building societies and credit unions) and general and life insurers as well as regulated superannuation funds.

### **Role of the audit committee**

The audit committee plays a key role in assisting the board to fulfil its corporate governance and oversight responsibilities in areas such as:

- corporate reporting, including external financial reporting, the directors report and annual report
- external audit
- internal audit
- risk management and internal control
- compliance and ethics
- activities to prevent, deter, detect and report on fraud.

The main objectives of an appropriately established and effective audit committee may include assisting the board to discharge its responsibility to exercise due care, diligence and skill in relation to the following areas:

- Facilitating well-informed, efficient and effective decision making, particularly by the board
- Promoting and monitoring an ethical culture throughout the entity
- Ensuring a code of conduct is appropriately designed and implemented and compliance with the code is monitored
- Implementing an effective system of risk oversight and management
- Implementing an effective and efficient internal control system
- Ensuring the existence of business policies and practices and appropriate financial management
- Ensuring protection of an entity's assets
- Ensuring high quality internal and external reporting (financial and non-financial) to users of financial reports
- Ensuring compliance with applicable laws, regulations, standards and best practice guidelines
- Providing a formal forum for communication between the board and senior financial management
- Obtaining an independent, effective and efficient external audit, including assessing audit quality and recommendations in respect of auditor rotation for listed entities
- Facilitating effective communication between the board and the internal and external auditors, and providing timely and appropriate responses to matters arising from audits
- Consideration of significant matters that were raised during the audit process.

The audit committee's responsibilities are typically documented in its charter. Ideally, the audit committee's annual work plan is cross-referenced to its charter to ensure that the committee fulfils its responsibilities.

Under the *Corporations Act 2001*, directors are required to declare that the financial statements and notes comply with accounting standards and give a true and fair view of the financial position and performance of the company. Overall responsibility for the content of the annual financial statements and notes sits with the board.

The audit committee can assist directors to fulfil their responsibilities and facilitate decision making by:

- facilitating open communication between board members and senior management, risk and compliance managers, internal and external auditors
- focusing on matters within the audit committee's charter, thereby allowing the full board to spend more time on other matters.

To be effective, the audit committee must be independent from management and free from any undue influence. Members of the audit committee should not have any executive powers, management functions, or delegated financial responsibility of the entity.

## Regulatory context

Audit committee members need to be aware of legislation, regulatory requirements, standards and guidance that are relevant to the operation of the audit committee, either directly, by establishing requirements for boards and audit committees, or indirectly, by establishing requirements for other parties reporting to, or working with, the audit committee, such as the internal and external auditors.

For those entities that operate in multiple jurisdictions, the audit committee would also need to consider the relevant legislation and regulations in those jurisdictions.

The legislation, regulatory bodies and the accompanying regulation, standards and guidance listed below may be relevant.

## Corporations Act 2001

The *Corporations Act 2001* is the principal legislation regulating companies in Australia. It covers matters such as the formation and operation of companies, duties of officers, takeovers and fundraising. It is a key point of reference for the audit committee on financial reporting and external audit requirements.

## Australian Securities Exchange Listing Rules and Corporate Governance Guidelines

The ASX Listing Rules require entities included in the S&P/ASX All Ordinaries Index at the beginning of their financial year to have an audit committee.<sup>6</sup> They also require the S&P/ASX 300 listed entities to comply with the 3<sup>rd</sup> edition of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* (Corporate Governance Principles and Recommendations) on the composition, operation and responsibility of the audit committee.

Principle 4 of the Corporate Governance Principles and Recommendations states that:

*A listed entity should have the formal and rigorous processes that independently verify and safeguard the integrity of its corporate reporting.*

### ASX Listing rule 12.7

An entity which was included in the S&P All Ordinaries Index at the beginning of its financial year must have an audit committee during that year. If the entity was included in the S&P/ASX 300 Index at the beginning of its financial year it must also comply with the best practice recommendations set out in the ASX Corporate Governance Council in relation to composition and operation of the audit committee for the whole of that financial year, unless it had been included in that for the first time less than three months before the beginning of

<sup>6</sup> See ASX Listing Rule 12.7.

that financial year. An entity that is included in the S&P/ ASX 300 Index for the first time less than three months before the first day of its financial year but did not comply with the recommendations set by the ASX Corporate Governance Council in relation to composition and operation of the audit committee at that date must take steps so that it complies within three months of the beginning of the financial year.

The supporting recommendations for a listed entity for that principle<sup>7</sup> are:

**Recommendation 4.1**

(a) The board should have an audit committee which:

- consists only of non-executive directors
- consists of a majority of independent directors
- is chaired by an independent chair, who is not the chair of the board
- has at least three members; and

The board should disclose the:

- charter of the audit committee
- relevant qualifications and experience of the audit committee
- number of times the committee met during the period and the individual attendances of the members at those meetings; or

(b): If the board does not have an audit committee, this is disclosed as well as the processes that the board employs that independently verifies and safeguards the integrity of the corporate reporting function

**Recommendation 4.2**

The board should, before it approves the entity's financial statements for a financial period, receive from its CEO and CFO a declaration that, in their opinion, the financial records of the entity have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively. This declaration is required under section 295A of the *Corporations Act 2001*.

**Recommendation 4.3**

Where the entity has an AGM, the external auditor should attend and be available to answer questions relevant to the audit. Section 250RA of the *Corporations Act 2001* requires a listed company's auditor to be represented at the company's AGM by a suitably qualified member of the audit team who is in a position to answer questions about the audit.

Where a listed entity does not have a stand-alone risk committee, then the audit committee may be charged with the responsibilities of a risk committee, the responsibilities of whom are set out in Principle 7 of the ASX Corporate Governance Principles and Recommendations that states *A listed entity should establish a sound risk management framework and periodically review the effectiveness of the framework*.

## **AASB Accounting Standards**

The *Corporations Act 2001* requires the entity's financial report to comply with the Accounting Standards made by the Australian Accounting Standards Board (AASB). Compliance with these standards underpins the audit committee's monitoring and oversight of the entity's financial reporting. The Act also requires that financial reports present a "true and fair view". Since July 2005 the standards made by the AASB incorporate the equivalent International Financial Reporting Standards (IFRS).<sup>8 9</sup>

<sup>7</sup> These recommendations came into effect from 1 January 2008.

<sup>8</sup> International Financial Reporting Standards (IFRS) are issued by the International Accounting Standards Board.

## AUASB Auditing Standards

The *Corporations Act 2001* requires the entity's financial report to be audited in accordance with the Auditing Standards made by the Auditing and Assurance Standards Board (AUASB).<sup>10</sup> While not creating obligations for the entity itself, the Australian Auditing Standards establish the mandatory requirements and provide application and other explanatory material for the external auditor of the entity.

This includes requirements for the external auditor to:

- agree with the entity the terms of the audit engagement
- communicate with the entity:
  - the auditor's responsibility for forming and expressing an opinion on the financial report prepared by management
  - an overview of the planned scope and timing of the audit
  - significant qualitative aspects of the entity's accounting practices
  - significant difficulties, if any, encountered during the audit
  - significant matters arising during the audit that were discussed or subject to correspondence with management, including significant deficiencies in internal control identified during the audit
  - circumstances that affect the form and content of the auditor's report including where:
    - the auditor expects to modify the opinion;
    - a material uncertainty related to going concern is reported;
    - a key audit matter is communicated;
    - an emphasis of matter or other matter is included; and
  - there is an uncorrected material misstatement of the other information any other matters that are significant to the oversight of the financial reporting process
  - independence statements
- seek representations from management (refer Appendix 3).

The audit committee can expect to interact with the external auditor on these matters and plays a key role in establishing an appropriate relationship with the external auditor.

## International Professional Practices Framework

The *International Professional Practices Framework* (IPPF) is promulgated by the IIA to provide consistent standards for the internal auditing profession. Members of the IIA agree to conform with the *Definition of Internal Auditing*, the *Code of Ethics* and the *International Standards for the Professional Practice of Internal Auditing* (Standards).

The Standards are principles-based requirements consisting of:

- Statements of basic requirements for the professional practice of internal auditing and for evaluating the effectiveness of its performance, which are internationally applicable at organisational and individual levels.
- Interpretations, which clarify terms or concepts within the statements.

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<sup>9</sup> Australian Accounting Standards may include additional paragraphs that do not appear in the equivalent IFRS. They are identified by the prefix "Aus" and generally relate to identifying the entities required to apply the standard and to matters affecting not-for-profit entities.

<sup>10</sup> Auditing Standards made by the AUASB conform with equivalent International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). Australian Auditing Standards may include additional paragraphs that do not appear in the equivalent ISA. Such paragraphs are identified by the prefix "Aus" and generally relate to Australian-specific legislative requirements and established audit practices.

### **Accounting Professional and Ethical Standards Board**

The Accounting Professional and Ethical Standards Board (APESB) is an independent, national body that sets the code of ethics and professional standards by which members of Australia's three professional accounting bodies abide.

Audit committee members who are members of an Australian professional accounting body must comply with the standards issued by the APESB and, in particular, APES 110 *Code of Ethics for Professional Accountants* (the Code), which includes the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

Audit committee members should be aware that auditors and other advisers that deal with the audit committee, who are members of an Australian professional accounting body, must comply with the Code, including the requirements to be independent and to comply with Australian Auditing Standards issued by the AUASB, where relevant.

### **Australian Securities and Investments Commission**

The Australian Securities and Investment Commission (ASIC) is Australia's corporate, markets and financial services regulator, established under the *Australian Securities and Investment Commission Act 2001*. Its role includes maintaining, facilitating and improving the performance of the Australian financial system and entities in that system, thereby promoting confident and informed participation by investors and consumers in the financial system.

ASIC has responsibility for the surveillance, investigation and enforcement of the financial reporting requirements of the *Corporations Act 2001*, including the enforcement of auditor independence and audit quality requirements, as well as audit inspection and information gathering powers under the ASIC Act.

The *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, further enhances ASIC's audit inspection and reporting powers by allowing ASIC to issue an audit deficiency report about specified failures by an individual audit firm and to communicate directly with the audit committee (or board or senior management), subject to certain requirements.

### **Australian Prudential Regulatory Authority**

The Australian Prudential Regulatory Authority (APRA) is the prudential regulator that oversees banks, credit unions, building societies, life and general insurance and reinsurance companies, friendly societies and superannuation funds (excluding self-managed funds).

APRA formulates, promulgates and enforces prudential policy and practice through Prudential Standards, which are supported by law, and Guidance Notes.

Audit committees of APRA-regulated entities will need to have regard to applicable APRA prudential requirements, for example, for risk management, governance, internal control systems and annual reporting requirements.

### **Australian Charities and Not-for-profits Commission**

The Australian Charities and Not-for-profits Commission (ACNC) is established under the ACNC Act and is the independent national regulator of charities.

The ACNC has responsibility for:

- registering organisations as charities
- helping charities understand and meet their obligations through information, guidance, advice and other support
- helping the public understand the work of the not-for profit sector through information, guidance, advice and other support
- maintaining a free and searchable public register so that anyone can look up information about registered charities, and
- working with state and territory governments (as well as individual federal, state and territory government agencies) to develop a 'report-once, use-often' reporting framework for charities.

### Standards Australia

Where audit committees are responsible for overseeing and monitoring risk management and compliance, joint Australian/New Zealand Standards such as AS/NZS ISO 31000: 2009 *Risk Management – Principles and guidelines* and AS 3806-2006 *Compliance programs*, developed by Standards Australia, might be useful.

AS/NZS ISO 31000: 2009 provides principles and generic guidance for the design and implementation of risk management plans and frameworks which can be used by any public, private or community enterprise, association, group or individual.

AS 3806-2006 provides principles and guidance for designing, developing, implementing, maintaining and improving a flexible, responsive, effective and measurable compliance program within an organisation.

### Responsibilities of the audit committee

It is important to clearly define the responsibilities of the audit committee in its charter, formally approved by the board and communicated to shareholders. Ideally, the audit committee's annual work plan is cross-referenced to its charter.

Over time, audit committee responsibilities have expanded from a financial focus to an approach focused on entity risks. This has broadened the audit committee mandate and coverage to reflect the expanding scope of audit work, including their need to keep abreast of new risks driven by technology, economic instability, health threats, cybercrime, terrorism, increased regulation, and other factors that are involving faster than ever. There is also an increasing focus on corporate culture. Therefore, audit committees need to stay attuned to its responsibilities which may need to be revised or expanded by the Board of Directors from time-to-time.

The role of audit committees is to seek assurance, which can be defined as a process to provide a level of confidence that objectives will be achieved within an acceptable level of risk. Assurance is a positive declaration intended to give confidence. It is designed to improve the quality of information to aid informed decision-making. Assurance should be built-in to an entity's established processes.

With increased outsourcing of non-critical operations to third parties and the adoption of combined assurance reporting concepts, audit committees need to consider the entity's overarching governance arrangements for assurance purposes. This includes an understanding of all assurance providers, awareness of what is being assured, nature of reporting within the entity's discrete governance structures, alignment between assurance

and high-level risk exposures, consolidated risk and assurance profiles and co-ordinated reporting of assurance activities.

The IIA lists the four pillars of governance as the audit committee, executive management, internal audit and external audit. With this perspective in mind, the audit committee has an active role to play to satisfy itself there is a strong governance environment covering their entity.

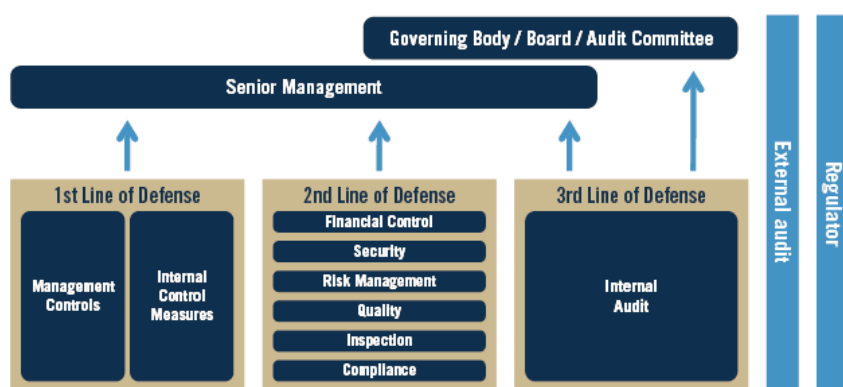
The combined assurance 3 Lines of Defence model is used by many entities to define their control and risk management environment to provide assurance to the board of directors, audit committee, chief executive officer, senior executives and stakeholders about effective governance:

- The 1st line of defence *owns and manages risk*. It initiates risk and is responsible for managing the risks, together with making sure there are mechanisms in place to demonstrate controls are working effectively.
- The 2nd line of defence *monitors risk*. It monitors reviews and tests effectiveness of first line controls and management of risks. It is a form of assurance.
- The 3rd line of defence *assures risk is managed*. It independently evaluates and gives an opinion on the adequacy and effectiveness of both the 1st line and 2nd line risk management approaches. It is a form of assurance independent of management.

While the approach will be different for every entity, the concept can generally be illustrated as shown in the following diagram.

If the 3 Lines of Defence are assessed as operating effectively, the audit committee can have a higher level of confidence the entity is well-governed.

### The Three Lines of Defense Model



Adapted from ECIIA/FERMA Guidance on the 8th EU Company Law Directive, article 41

As previously set out, the key responsibilities of the audit committee, which are focused on assurance, are discussed in more detail below.

**Comment [HR1]:** Suggest content too granular and technical. Suggest confusion over the usage of the generic term "assurance" – usage does not fit in with AUASB standards and is being used here in a different context.

**Comment [HR2]:** see above

**Comment [HR3]:** see above – used throughout this section

## Corporate reporting

### Financial reporting

The audit committee plays a key role in reviewing financial information before it is presented to the board for approval and publication, including the financial report and other financial information in an entity's financial reporting cycle, namely the concise financial report (if applicable), half year review and the annual report.

The audit committee may also report to the board on profit announcements, analyst briefings, investor presentations, announcements made under continuous disclosure obligations and other media releases containing financial information about the entity.

It is important to note that the board retains ultimate responsibility for financial reporting and cannot delegate that responsibility to the audit committee, or to management or external advisers. The audit committee will make use of knowledge gained from considering risk management, internal control and compliance activities, and from discussing matters with management, the internal auditor and the external auditor.

In the court case *ASIC v Healey* (2011) 196 FCR 291 at 339 and 298, Justice Middleton held that:

“... whilst an audit committee has an important role of monitoring and oversight, this is not to the exclusion of the role of a director to consider the financial accounts for him or herself in the way I have attempted to explain. This does not involve a director being familiar with every accounting standard, but sufficiently aware and knowledgeable to understand what is being approved or adopted.”

Justice Middleton further held that:

“... What each director is expected to do is to take a diligent and intelligent interest in the information available to him or her, to understand that information, and apply an enquiring mind to the responsibilities placed upon him or her. Such a responsibility arises in this proceeding in adopting and approving the financial statements. Because of their nature and importance, the directors must understand and focus upon the content of financial statements, and if necessary, make further enquiries if matters revealed in the financial statements call for such enquiries.”

### Accounting policies

The audit committee may require management to advise and provide representation on:

- How they selected and applied critical accounting policies and any changes in significant accounting policies, or their application, during the reporting period
- Whether they made a specific assessment of the entity's ability to continue as a going concern and how they made that assessment; if not, the basis for using the going concern assumption in preparing the financial statements and note disclosures
- The methods used to account for significant, complex or unusual transactions, or transactions in emerging areas for which there may be no specific accounting standard, including management's reasoning in determining the appropriateness of those methods
- The process used to determine that all relevant information has been brought to the attention of senior management to enable consideration of whether disclosure is required in the financial report

- Significant estimates and judgements in the financial report and the processes used by management in making those estimates and judgements. Management should comment on the impact of different assumptions, where these could have a significant impact on the financial report
- Other significant matters that do, or may, impact on the financial position of the entity and management's decision on disclosure or otherwise in the financial report
- The processes for identifying related party transactions and the nature, extent and reasonableness of related party transactions identified
- The processes for ensuring and monitoring compliance with laws, regulations and other requirements on external reporting by the entity of financial and non-financial information. Requirements include IFRS, the Corporations Act 2001, the ASX listing rules, APRA and, where applicable, the legislation and regulations of other countries in which the entity operates.

The audit committee may require the external auditor and, where appropriate, the internal auditor, to advise on:

- The appropriateness of the entity's accounting policies and procedures
- Areas of subjectivity in the financial report, including significant estimates and areas where judgement was involved
- Actual and potential material audit adjustments
- The materiality threshold used in the performance of the audit
- Other areas that may affect the quality of the financial report, for example:
  - non-compliance with laws and regulations, and actions taken by the entity in response to non-compliance
  - internal control issues.
- The auditor's view on management's:
  - technical competence and compliance with accounting standards
  - use of the going concern basis in preparing the financial statements and note disclosures
  - proper application of accounting principles
  - clarity in financial disclosure practices.

### Annual financial report

Regarding the annual financial report,<sup>11</sup> the audit committee needs to consider whether:

- The financial report complies with applicable legislation and accounting standards
- The financial statements and note disclosures present a true and fair view of the entity's financial position and performance, if not, additional disclosures are required
- The financial statements and note disclosures have been prepared on the basis that the entity is a going concern, and, if not, that they appropriately reflect the entity's inability to continue as a going concern
- Other information in the annual report is consistent with the financial report and other information known to the audit committee. For example, information in the directors' report or other management report/s relating to the entity's operations, financial position, business strategies and future prospects
- There is any information known to them gained in their role as a director of the entity that should be disclosed.

In light of the above, the audit committee may consider whether it is appropriate to make a recommendation to the board regarding approval of the directors' declaration.<sup>12</sup>

<sup>11</sup> The audit committee may also review the concise financial report, if any, and the interim financial statements, and make similar considerations to those discussed for the annual financial report.

<sup>12</sup> The *Corporations Act 2001* in section 295(4) sets out the requirements of the directors' declaration regarding the financial report.

To fulfil this role the audit committee needs to have a good understanding of:

- the entity's financial reporting framework, which in most cases for Australian listed entities will be the Corporations Act 2001 and the Australian Accounting Standards
- the appropriateness of the entity's accounting policies and procedures, and whether they are consistent with the stated financial reporting framework
- the nature of the underlying transactions, assets and liabilities.

### Reporting to the audit committee and the board

Ideally, the audit committee reviews all representation letters signed by management to assess whether information provided appears complete and appropriate.

The audit committee may review the chief executive officer (CEO) and chief financial officer (CFO) declarations in respect of the financial report and financial records, provided in accordance with section 295(A) of the *Corporations Act 2001*.

The audit committee also reviews the letter, if any, provided by the external auditor to the audit committee at the end of the audit of the financial report, which may include, for example, a discussion of audit materiality, the appropriateness of accounting policies adopted by the entity and information about changes to accounting standards, both current and proposed, that may be relevant to the entity's financial report.

Based on its review and consideration of the financial statements and note disclosures, and other information, the audit committee should recommend to the board whether the financial report should be approved.

### Other external reporting

In relation to other external reporting,<sup>13</sup> the audit committee should ideally:

- Review documents and reports to regulators for consistency with the financial report and other information known to the audit committee
- Review the reporting of the entity's main corporate governance practices as required under the ASX listing rules for completeness and accuracy
- Review any non-IFRS financial information,<sup>14</sup> including the reconciliation between the underlying profit and statutory profit, if applicable
- Review any analyst briefings, investor presentations and media releases for consistency with the financial report
- Review the processes established for the purposes of continuous disclosure reporting to the ASX.

Based on its review and consideration of the other external reports, the audit committee should recommend to the board whether the reports should be approved.

### Other reporting

Entity performance encompasses both financial and non-financial performance, with the value of an entity driven by its bottom-line, but also by non-financial business drivers.

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<sup>13</sup> Other external reporting may include corporate social responsibility (CSR), sustainability, greenhouse gas and energy and occupational health and safety reporting.

<sup>14</sup> See ASIC Regulatory Guide 230 *Disclosing non-IFRS financial information*

The audit committee should be appraised of entity performance from the perspective of whether performance measures are fit-for-purpose and whether they are being achieved. This should ideally relate to both financial and non-financial performance.

Performance measures need to be specific (clear and concise), measurable (quantifiable), achievable (practical and reasonable), relevant (to uses), and timed (within a range or time limit).

The purpose of management reporting is to aid decision-making and promote action. Management should provide the audit committee with relevant, integrated, timely, comparable, reliable and clear reports.

The focus of management reports to the audit committee should be on matters relevant to a clear picture of the overall state of entity assurance. In this way, an audit committee can achieve comfort the entity control and assurance environment is operating effectively.

## External audit

The audit committee has a key role in the entity's relationship with the external auditor and in promoting audit quality. The importance of this role is emphasised in the IAASB publication *A Framework for Audit Quality*. In addition, ASIC information sheet 196<sup>15</sup> provides guidance to assist directors and audit committees in their role in ensuring the quality of the external audit of a financial report.

The audit committee's responsibilities typically include:

- Recommending the appointment of an auditor to the board or assessing potential and continuing auditors including understanding the:
  - audit tender or selection process;
  - auditor's commitment to audit quality;
  - auditor's resources devoted to the audit;
  - auditor's reliance on experts and other auditors, (including using the work of other auditors, coverage of components within a group and reliance on internal auditors); and
  - accountability for audit quality by the auditor's engagement partner, review partner, specialists and audit team members.

The audit committee may agree the audit fee or make a recommendation thereon to the board. In addition, the audit committee may recommend to the board, if appropriate, the extension of the rotation period of the external audit engagement partner subject to certain requirements<sup>16</sup>.

- Facilitating the audit process by supporting the audit and ensuring company management and staff are accountable, supportive and helpful of the audit process.

Supporting the audit includes understanding that a high quality and comprehensive audit can be conducted for the agreed fee and that financial reporting and audit processes have been planned to ensure that an effective quality audit can be conducted within the financial reporting timeframes.

- Establishing ongoing communications with the auditor so as to:
  - address any risk or areas of concern; and
  - ensure access to directors and audit committees

<sup>15</sup> ASIC information sheet 196 *Audit Quality: The Role of Directors and Audit Committees*

<sup>16</sup> Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, the audit committee of a listed entity may recommend to the board that the rotation period of the audit engagement partner be extended from five up to a maximum of seven years. The recommendation may be endorsed by a resolution passed by members of the audit committee and be in writing, stating the audit committee is satisfied that approval of the extension is consistent with maintaining the quality of the audit and would not give rise to a conflict of interest.

Ensuring access includes the auditor attending all appropriate audit committee meetings and the auditor meeting with the audit committee separately from management without discussions being shared with management<sup>17</sup>.

- Maintaining and reviewing auditor independence and objectivity by considering whether the external auditor's relationships and services with the entity and other relevant organisations might impair, or appear to impair, the external auditor's independence. Under the *Corporations Act 2001*, the audit committee of a listed entity must provide written advice to the board regarding the provision of non-audit services by the external auditor.<sup>18</sup> Some audit committees may establish policies on the extent to which the external auditor can provide other assurance, or non-assurance, services and monitor the application of the policies to consider the possible implications for the auditor's independence
- Assessing the quality of audits conducted and evaluating the performance of the auditor including considering:
  - the auditor's internal quality and standards (reference may be made to the audit firms transparency report lodged with ASIC);
  - the audit process (including the auditor's demonstration of professional scepticism);
  - the timeliness of communications and usefulness and relevance of issues;
  - other information (including firms audit transparency reports);
  - findings from ASIC's audit inspections and surveillances.

Australian Auditing Standards include requirements for the external auditor to communicate certain matters to the audit committee.<sup>19</sup> Audit committee members may wish to familiarise themselves with these requirements and may expect to be informed by the external auditor of important matters related to the audit.

## Internal audit

Internal audit activities within entities are a key expression of their attitude towards an effective control environment.<sup>20</sup>

The IIA defines the mission of internal audit as:

*"To enhance and protect organisational value by providing risk-based and objective assurance, advice, and insight."*<sup>21</sup>

Internal audit provides the board of directors, audit committee, chief executive officer, senior executives and stakeholders with an independent view on whether an entity has an appropriate risk and control environment, while acting as a catalyst for a strong risk and compliance culture.

Good practice reporting arrangements for internal audit are:

- Functionally for operations to the audit committee through the chair
- Administratively to the chief executive officer.

Functional reporting generally involves the audit committee:

- Reviewing and approving the internal audit charter

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<sup>17</sup> The IAASB Publication *A Framework for Audit Quality*, suggests at least one meeting annually.

<sup>18</sup> See *Corporations Act 2001*, section 300 (11B) – (11E).

<sup>19</sup> See *Relationships – External Auditor* on page 30 of this guide.

<sup>20</sup> Not all entities will have an internal audit function.

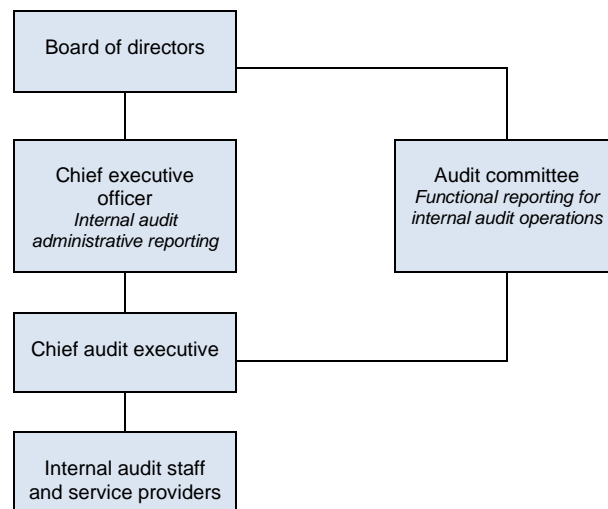
<sup>21</sup> Source: the 'International Professional Practices Framework' issued by the Institute of Internal Auditors.

- Approving decisions regarding appointment and removal of the chief audit executive (CAE)
- Reviewing and approving the strategic internal audit plan, often for a 2-3 year period
- Reviewing and approving the annual internal audit plan
- Approving any changes to the annual internal audit plan
- Reviewing reports on the results of internal audit engagements, audit-related activities, audit team capability, audit performance and other important matters
- Monitoring compliance with standards, together with quality and improvement arrangements
- Meeting privately with the CAE at least once a year without the chief executive officer or other management present
- Making enquiries of the CAE to determine any scope of budget limitations that may impede the execution of internal audit responsibilities.

Administrative reporting to the chief executive officer generally includes:

- Internal audit resources and annual budget
- Provision of corporate services to internal audit including office accommodation, computers and equipment
- Human resource administration.

This can be shown diagrammatically as:



Internal audit work is risk-based and encompasses both financial and non-financial operations.

Appendix 4 contains a table identifying the fundamental differences between the work of internal audit and external audit.

## Risk management and internal control

Risk occurs when entity's try to achieve objectives in an uncertain environment. It is usually measured in terms of likelihood and consequence.

Risk management is an inherent part of the management process and incorporates the principles of corporate governance, accountability, communication and strategic alignment.

Comment [HR4]: IIAA are thinking about separating these sections out – which may cause further granularity concerns.

Comment [HR5]: what risk/defined?

This requires co-ordinated and economical application of resources to:

- Address the uncertainty found in the entity environment, including uncertainty associated with assumptions.
- Minimise, monitor and control the probability (likelihood) or impact (consequence) of unforeseen events (threats).
- Maximise opportunities (good outcomes).

Risk management should be applied at all levels of an entity including:

- Enterprise-wide (strategic).
- Business unit (operational).
- Project-specific (tactical).
- Internal audit (planning, objectives and scoping).

A control is any action taken by management to enhance the likelihood that objectives will be achieved. These may be:

- Preventive – to deter undesirable events from occurring.
- Detective – to detect and correct undesirable events that have happened.
- Directive – to cause or encourage a desirable event to occur.

There are two types of controls – ‘hard controls’ and ‘soft controls’.

- Hard controls are formal controls such as policies and procedures, reconciliations of accounting records, management sign-offs, a documented business plan, written code of conduct, separation of duties, and safety procedures.
- Soft controls are informal and include competency, knowledge and understanding of employees, ethical behaviour of management and staff, relationship building, and employee understanding of procedures.

Soft controls are more difficult to audit than hard controls because they generally do not have clear and definitive methods of testing the controls.

To manage identified hazards and risks, organisations apply both hard and soft controls that typically fall into three layers:

- Systems and processes (IT risk, business continuity, security).
- Capability.
- Culture (leadership, behaviour, attitudes).

The risk management and internal control framework within an entity is a key expression of its attitude to the control environment. While the board retains overall responsibility for risk management and internal control, it typically delegates elements of this responsibility to the audit committee (or the audit and risk management committee or a separate risk management committee, as applicable).

The three most commonly used sources of guidance on the elements of an effective risk management and internal control framework are the:

- Australia/New Zealand Standard on Risk Management (AS/NZS ISO 31000:2009) and accompanying handbooks published by Standards Australia
- Enterprise Risk Management Conceptual Framework (published by the Committee of Sponsoring Organisations of the Treadway Commission (COSO))
- Internal control – Integrated Framework (also published by COSO).

For example, the board retains responsibility for establishing an appropriate “tone at the top” - the corporate environment or culture, which disseminates throughout the entity and may be seen by some as equal to the internal control environment. This tone can be the most

**Comment [HR6]:** Suggest granular and technical, ? Relevance to target audience. Terminology not consistent with AUASB standards.

important factor contributing to the integrity of the entity's key business processes, including financial reporting.

The board is also responsible for agreeing on the entity's risk appetite and monitoring the strategic risks faced. This should be formally documented in a risk appetite statement from the board that clearly outlines the risks the entity is willing to take or accept in pursuit of its strategic objectives. The purpose of a risk appetite statement is to convey to the CEO what the board expectations are on how risk is to be managed within the entity.

A risk appetite statement explicitly outlines the risks to be avoided and for which the board has no tolerance. It considers the entity's risk universe across all risk categories, with all business decisions to be made in the context of the approved risk appetite statement.

Comment [HR7]: is this defined anywhere?

The board may delegate the following responsibilities to the audit committee:

- Reviewing whether the entity has an effective risk management system and that material business risks to the entity are appropriately reflected in the risk profile reported at least annually to the board
- Understanding the processes for determining and managing material business risks in accordance with the entity's identified tolerance for risk, particularly risks in the following areas:
  - significant business risks, recognising that responsibility for general or specific risk areas for example, environmental risk, occupational health and safety, might be assigned to other board committees
  - breakdown of key business processes
  - non-compliance with laws, regulations and standards, and entity policy
  - fraud and theft
  - business continuity and disaster preparedness
- Monitoring the effectiveness of the entity's processes for identification and control of material business risks, including operational, financial, legal, compliance and strategic risks. This might include oversight of the entity's risk management framework and activities conducted by internal audit and external audit, together with other assurance providers, to provide a holistic picture of assurance across the entity
- Receiving summary reports from management on all suspected and actual frauds, thefts and material breaches of laws, ensuring such events are reported to the board and/or relevant authorities
- Assessing adequacy of entity processes to manage insurable risks and the adequacy of insurance cover, and if applicable, the level of self-insurance
- Monitoring the effectiveness of the entity's internal control system through discussions with management, internal auditors and external auditors
- Assessing whether management has controls in place for unusual types of transactions and/or any potential transactions that might carry more than an acceptable degree of risk
- Meeting periodically with key management, internal audit and external audit, and compliance staff, to understand and discuss any changes in the entity's control environment
- Liaising with other board committees.

### Compliance and ethics

Within entities, compliance and ethics programs are a key expression of an entity's values. Non-compliance and unethical behaviour can have potential financial, non-financial or reputational impacts on an entity.

Comment [HR8]: IIAA are thinking about separating these sections out – which may cause further granularity concerns.

Compliance encompasses adherence to policies, plans, procedures, laws, regulations, contracts or other requirements.

Organisations need to comply with obligations associated with their establishing legislation or constitution, as well as broader legislative and regulatory obligations on how they operate, account and report.

Compliance continues to be a primary concern for the boards, audit committees and senior management of most entities, with reputation risk pushed to new levels as a consequence of the complexity and pace of legislative and regulatory change, coupled with an increase in regulatory scrutiny and enforcement.

Internal auditors are expected to assess the effectiveness of the entity's compliance framework including identification, risk assessment, awareness, monitoring, handling breaches, continuous improvement, the compliance register, reporting, and cross-border obligations.

The international standard for compliance management AS/ISO19600 was rolled-out in 2014 and is intended to serve as a global standard and benchmark for compliance management programs.

Part of compliance, is adherence to work health safety legislation. This legislation imposes a framework to secure the health and safety of workers and workplaces by protecting workers and other persons against harm to their health, safety and welfare through the elimination of risks arising from work. This is in accordance with the principle that workers and other persons should, as reasonably practicable, be given the highest level of protection against harm to their health, safety and welfare from hazards and risks arising from work. This requires the entity to:

- Eliminate risks to health and safety so far as is reasonably practicable
- If elimination is not reasonably practicable, minimise the risks so far as is reasonably practicable.

Comment [HR9]: Suggest too granular/too specific

Accordingly, good audit committee practices will often include oversight of compliance and ethics programs, including:

- Staying informed about the entity's processes for monitoring compliance with laws and regulations, industry codes, internal policies, standards of good corporate governance and other community expectations, ensuring they are aligned with the compliance culture expectations of the board. This will normally involve receiving reports and briefings from key senior management, and meeting periodically with them.<sup>22</sup>
- Ensuring a code of conduct is in place, there is an effective implementation process to support its adoption, and the entity has a program for monitoring compliance with the code
- Approving and reviewing the policies, processes and framework for identifying, analysing and addressing complaints relating to the entity's compliance and ethical obligations. This includes both whistleblowing procedures for employees and customer complaint handling processes
- Staying informed on significant compliance and ethical issues, as well as independent investigations and disciplinary action in relation to non-compliance or unethical behaviour

<sup>22</sup> In this context, senior management might include the compliance officer, legal counsel, chief financial officer, head of human resources or tax manager.

- Receiving information from the external auditor on matters involving non-compliance with laws and regulations that were identified during the audit<sup>23</sup>
- Identifying and recognising adverse trends within the entity and reviewing management's plans to deal with them
- Reviewing management disclosures in the financial reports of the effect of significant compliance issues
- Ensuring the internal audit activity considers assessing compliance and ethics risks in their audit plan.

## Fraud and corruption control

The audit committee may be responsible for overseeing the systems and programs implemented by management for fraud and corruption prevention, deterrence and detection, particularly in the context of financial accounting and reporting.

The existence of fraud and corruption prevention systems and programs is a key expression of the attitude of the board, audit committee and management to minimising fraud and corruption.

Good audit committee practices in overseeing fraud and corruption prevention typically include:

- Ascertaining whether fraud risks have been included in the assessment of the risk profile of the entity
- Reviewing management's efforts to create and maintain a strong internal control environment, including the design and implementation of anti-fraud and corruption strategies and programs
- Reviewing management's communications, if any, to employees regarding its views on business practices and ethical behaviour
- Enquiring of management, and the external auditor<sup>24</sup> regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments
- Enquiring of management, the internal auditor and the external auditor whether they have knowledge of any actual, suspected or alleged fraud or corruption affecting the entity, and how the entity responded to such instances, including changes made to the control environment
- Monitoring remedial actions implemented by management, where control weaknesses were identified
- Obtaining representations from management that all known instances of actual, suspected or alleged fraud or corruption affecting the entity have been disclosed to the audit committee
- Ensuring the entity has fulfilled its fraud and corruption reporting obligations, if any, in accordance with relevant laws, regulations or other authority.

Audit committees need to be aware of their entity's operations and whether it may be in conflict with anti-corruption legislation, including in the internal arena.

Comment [HR10]: AUASB standards don't use this word or define it.

<sup>23</sup> See Auditing Standard ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*.

<sup>24</sup> See Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*. Although intended for external auditors, this auditing standard contains information in its appendices that may be helpful for audit committee members. For example, it provides an extensive list of factors that indicate an incentive, pressure or opportunity to commit fraud, and examples of circumstances that indicate the possibility of fraud.

## Relationships

### Board

#### Role

The audit committee assists in the discharge of the board's oversight and corporate governance responsibilities, whereas the role of the board is that of a constituting and governing body.

#### Responsibilities

The board:

- Establishes the audit committee with an appropriate charter, membership and level of resources to effectively carry out its activities
- Ensures that there is an appropriate reporting mechanism in place between it and the audit committee
- Periodically reviews the performance of the audit committee as a whole, and of each audit committee member. The audit committee performance review can be (and often is) by self-assessment (see the self-assessment tool in Appendix 2), but should preferably be part of a whole of board review.

It is important for the members of the audit committee and the board to recognise that delegation of activities to the audit committee does not absolve individual directors from their responsibilities. Individual directors are obliged to reach their own decisions based on a proper assessment of the information, which includes audit committee reports.

General responsibilities of directors, which extend to audit committee interaction and involvement, typically include:

- Duty to act in good faith in the best interests of the entity
- Duty to act with care and diligence
- Duty to avoid a conflict in the position of a director and/or any interest that a director may have
- A range of duties that prohibit the misuse of information obtained by directors.<sup>25</sup>

### External Auditor

#### Role

The scope of the external auditor's engagement usually emanates from a regulatory requirement, such as a requirement under the *Corporations Act 2001*, or other relevant legislation, to audit or review the entity's financial report.<sup>26</sup>

The external auditor must be independent from the entity's governance, internal control and ownership structures. The external auditor gains an understanding of the entity, its environment and its internal controls, makes risk assessments about the financial report and obtains sufficient appropriate audit evidence to support the auditor's report on the financial report.

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<sup>25</sup> See *Duties and Responsibilities of Directors and Officers 21<sup>st</sup> Edition* by Professor Robert Baxt AO, Australian Institute of Company Directors, 2016.

<sup>26</sup> Sections 307, 308, 309 and 314(2)(c) of the *Corporations Act 2001*.

As an independent party with knowledge of the entity's financial affairs, the external auditor can provide the audit committee with valuable, objective insight into aspects of the entity's governance and internal control, including its risk management. In turn, the audit committee aids the effectiveness of the external auditor. The importance of effective two-way communication in the promotion of audit quality is emphasised in the IAASB's publication, *A Framework for Audit Quality*.

For the external auditor, communication and consultation with the audit committee helps to facilitate an effective and efficient audit and the communication of matters arising from the audit. External auditors seek a constructive relationship with the audit committee while maintaining their independence, objectivity and an attitude of professional scepticism.

External auditors are required to respond to questions relating to certain aspects of the audit raised by the members of a listed entity at the entity's annual general meeting (AGM).<sup>27</sup> The relevant matters that members may query include the content of the auditor's report, the conduct of the audit, the accounting policies adopted by the entity and the independence of the auditor. As such, the external auditor fulfils an important role in providing independent information to members.

### **Responsibilities**

As set out in Australian Auditing Standards the external auditor has responsibilities for effective communication with those charged with governance (which may include the audit committee) in an audit of a financial report.

### **Promoting effective two-way communication**

Effective two-way communication<sup>28</sup> assists:

- The audit committee in fulfilling its responsibility to oversee the financial reporting process
- The auditor in obtaining information relevant to the audit from the audit committee
- Both the audit committee and the auditor in establishing a constructive working relationship.

Auditing Standard ASA 260 *Communication with Those Charged with Governance* provides an overarching framework for the external auditor's communication with those charged with governance and identifies some specific matters to be communicated with them.

Additional matters to be communicated are identified in other auditing standards.<sup>29</sup> The key requirements are listed below:

### **Establishing whether the preconditions for an audit are present**

In establishing whether the preconditions for an audit are present<sup>30</sup> discussions are needed with management and the audit committee to assist the auditor in:

- Determining whether the financial reporting framework to be applied by management in the preparation of the financial report is acceptable
- Obtaining the agreement of management that it acknowledges and understands its responsibility for preparation of the financial report, for the internal control system

<sup>27</sup> Not all listed entities are required to hold an annual general meeting, such as listed trusts.

<sup>28</sup> See ASA 260 *Communication With Those Charged With Governance*.

<sup>29</sup> See ASA 260, Appendix 1, which lists other auditing standards that require specific matters to be communicated to those charged with governance.

<sup>30</sup> See ASA 210 *Agreeing the Terms of Audit Engagements*.

related to preparation of the financial report and for providing access by the auditor to all relevant information and persons for the purposes of obtaining audit evidence.

### ***Agreeing the terms of the audit engagement***

- Discussing and agreeing the terms of the audit engagement,<sup>31</sup> including who to communicate with, when and how to communicate
- Communicating the auditor's responsibilities in relation to the audit.

### ***Establishing and maintaining independence***

- Confirming their independence<sup>32</sup> in accordance with ethical and regulatory requirements
- Communicating any relationships that might have a bearing on their independence, including the provision of other assurance, and non-assurance, services to the entity and relevant external organisations and disclosing a categorised fee breakdown in both the reporting to the audit committee as well as within the financial report)
- Notifying the audit committee of any contraventions to the auditor's independence requirements
- Communicating the safeguards applied to eliminate threats to their independence.

### ***Discussing elements of audit planning***

- Discussing the overall audit strategy, scope and timing,<sup>33</sup> including any limitations – based on the auditor's consideration of materiality, high risk areas affecting the financial report and their plans to examine the effectiveness of internal controls
- Discussing proposed co-ordination with the internal audit activity, including any planned use of internal audit work.
- Discussing the nature and extent of specialised skill or knowledge needed, including the use of auditor's or management's experts  
Discussing the auditor's preliminary views about matters that may require significant auditor's attention and therefore may be key audit matters that are required to be included in the auditor's report.

### ***Requiring significant auditor's attention***

- Key audit matters (KAM) are those matters that in the auditor's professional judgement were of most significance in the audit of the financial report of the current period. Reporting of KAM is only required for general purpose financial reports of listed entities or where required by law or regulation.<sup>34</sup>
- The auditor is required to communicate with those charged with governance those matters that the auditor has determined to be key audit matters. Communication with those charged with governance recognises their important role in overseeing the financial reporting process, and provides the opportunity for those charged with governance to understand the auditor's decisions in relation to KAM and how those matters will be described in the auditor's report. It also enables those charged with governance to consider whether new or enhanced disclosures may be useful in light of the fact that these matters will be communicated in the auditor's report.

### ***Communicating considerations of group audits***

- The group engagement team communicates the following with the audit committee:

<sup>31</sup> See ASA 210 *Agreeing the Terms of Audit Engagements*.

<sup>32</sup> See ASA 260 *Communication With Those Charged With Governance*.

<sup>33</sup> See ASA 300 *Planning and Audit of a Financial Report*.

<sup>34</sup> See ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*.

- an overview of the work to be done on the financial information of components and an overview of the group engagement teams planned involvement in that work
- concerns over the quality of component auditor's work
- limitations on the group audit for example access to information restrictions
- fraud or suspected fraud involving group or component management or where a fraud resulted in a material misstatement of the group financial report

### ***Discussing significant related party relationships and transactions***

- Discussing with the audit committee the nature, extent and business rationale of significant related party relationships and transactions,<sup>35</sup> including those involving actual conflicts of interests.

### ***Enquiring about fraud***

- The auditor is required to obtain an understanding of how management and others within the entity, including the audit committee, exercise oversight of management's processes for identifying and responding to the risks of fraud and the internal controls that management has established to mitigate these risks
- The auditor is required to enquire of management and others within the entity, including the audit committee and internal audit, to determine if they have any knowledge of actual, suspected or alleged fraud<sup>36</sup> affecting the entity.
- The auditor communicates fraud or suspected fraud involving group or component management or employees to the audit committee.

### ***Communicating significant findings from the audit***

- Determining, based on professional judgement, when significant findings from the audit<sup>37</sup> should be communicated to management, the audit committee and/or directly to the board<sup>38</sup>
- Communicating the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial report disclosures
- Discussing significant difficulties, if any, encountered during the audit
- Discussing significant matters raised with management during the audit, including any disagreements with management, whether resolved or unresolved, relating to the financial report
- Communicating circumstances that affect the form and content of the auditor's report including:
  - a modification of the opinion in the auditor's report
  - a material uncertainty related to going concern
  - key audit matters
  - an Emphasis of Matter paragraph or Other Matters paragraph
  - an uncorrected material misstatement of the other information

<sup>35</sup> See ASA 550 *Related Parties*.

<sup>36</sup> See ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*.

<sup>37</sup> See ASA 260 *Communication With Those Charged With Governance*.

<sup>38</sup> While the auditor may agree with the entity on preferred lines and forms of communications, the auditor should continue to use judgement to determine whether communication with the audit committee is sufficient and appropriate. The auditor should take into account such things as the nature of the matters, the governance structure, legal requirements and the composition of the audit committee (for example, the extent to which the members of the board are represented on the audit committee).

- Advising on representations the auditor is seeking from management<sup>39</sup>
- Communicating significant deficiencies in internal controls identified during the audit<sup>40</sup>
- Communicating identified fraud, information that indicates a fraud might exist, or weaknesses in the design or implementation of internal control to prevent, deter, detect and report on fraud
- Communicating significant matters of non-compliance with laws and regulations and the appropriate remedies<sup>41</sup>
- Communicating uncorrected misstatements identified by the auditor<sup>42</sup>
- Communicating events or conditions identified by the auditor that may cast doubt on the entity's ability to continue as a going concern<sup>43</sup>
- Communicating matters of governance interest that arose during the audit of the financial report that are relevant to the oversight of financial reporting. Such matters typically include:
  - modifications in audit strategy based on a revised consideration of risks
  - material risks and exposures regarding the financial report
  - industry, regulatory, or other external factors
  - material misstatements of fact or material inconsistencies in information accompanying the audited financial report

It is highly desirable that the external auditor discuss all issues to be raised at the audit committee meeting with the CEO, CFO and the audit committee chair before the meeting. This ensures that all relevant information has been obtained and is done as a courtesy to these executives.

### **Responding to questions**

- Responding in a timely manner to reasonable audit committee questions and communications.

## **Internal Auditor**

### **Role**

Internal audit, where it exists, acts as an agent for the audit committee and provides independent and objective assurance to the audit committee on governance, risk management and control processes.

Internal audit activities should be conducted in a manner consistent with the IPPF, including the *Definition of Internal Auditing*, the *Code of Ethics* and the *Standards*. Internal audit requires professionals with an appropriate level of understanding of the business culture, systems and processes to provide assurance the controls in place are sufficient to manage risks, governance processes are adequate and organisational objectives are met.

Ultimately, the internal audit assists the audit committee in its role with monitoring and oversight which typically falls into two distinct categories:

<sup>39</sup> See ASA 580 *Written Representations*.

<sup>40</sup> See ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*.

<sup>41</sup> See ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*.

<sup>42</sup> See ASA 450 *Evaluation of Misstatements Identified during the Audit*.

<sup>43</sup> See ASA 570 *Going Concern*.

1. **Assurance services:** involves the internal auditor's objective examination of evidence for the purpose of providing an independent assessment on governance, risk management and control processes for the organisation.
2. **Consulting services:** providing advisory and related client service activities, the nature and scope of which are agreed with management. When performing consulting services, internal audit must not assume management responsibility.

Internal auditors must communicate the results of engagements, and include their objectives and scope, as well as applicable conclusions, recommendations and action plans.

## **Responsibilities**

Internal audit responsibilities typically include:

### ***Discussing elements of internal audit planning***

- Providing a draft of the risk-based internal audit plan for input and formal approval. In developing the draft internal audit plan, the CAE should consider all entity including operational, financial, compliance and strategic risks. The draft plan should detail internal audit objectives, work schedules, staffing requirements, budgets and a description of any limitations placed on internal audit's scope of work
- The internal audit plan might also include financial or compliance audits, operational reviews, risk and control self-assessments, system-based audits, performance audits, IT audits and so on, and/or specific one-off assignments. It should evaluate and monitor the adequacy and effectiveness of the internal control systems. The plan should:
  - Provide details of the internal audit staff structure, including staff skills, experience and qualifications
  - Consider the activities of other assurance providers, both internal and external to the entity
  - Advise on the coordination of the internal audit plan with the external audit plan.
- Discussing any changes to the internal audit plan
- Holding periodic discussions with the chair, and with all audit committee members, without the presence of management.

### ***Communicating on independence***

- Advising on internal audit independence
- Reporting any non-audit activities provided by internal audit.

### ***Communicating matters arising from internal audit work***

- Submitting activity reports, highlighting significant findings, their effect, or potential effect, and recommendations (particularly regarding the entity's risk management plan), and advising the actions taken, or proposed, by management
- Submitting reports on any major variances from internal audit objectives, work schedule and budget
- Providing activity reports on any major fraud
- Reporting on any identified conflicts of interest
- Advising changes to the risk profile of the entity and the implications of these for the audit plan.

### ***Responding to requests***

- Performing audits that may be requested by the audit committee

- Providing any other information requested by the audit committee
- Providing assurance to management on the adequacy governance, risk management, control and compliance, and being available to management to assist with the improvement of processes and control activities.

#### ***Engaging with the audit committee on matters associated with governance, risk management, control and other matters***

- Internal audit provides a key source of information for members of the audit committee on governance, risk management and internal control, and other matters affecting the entity's operations.

#### ***Annual reporting***

- Provides an annual report of its work to the audit committee, including an assessment on the effectiveness of the organisation's control system.
- Advising the audit committee and management of patterns, trends and systemic issues identified from its work.

### **Developing an effective charter**

The charter is the audit committee's blueprint for its operations, and should be developed to meet the needs of the entity, allowing for the entity's objectives, culture and the industry in which it operates.

The charter should cover all key aspects of the audit committee's operations while remaining flexible to enable the committee to respond appropriately to issues that arise.

The audit committee charter is developed and approved by the board.

A wide range of sample audit committee charters are available in the public domain including some issued by professional bodies.<sup>44</sup> One size cannot fit all in respect of audit committees, so each audit committee should evolve and develop its own guidelines suited to itself and the organisation.

Commonly the charter defines and/or outlines the following<sup>45</sup>:

- The audit committee's purpose and objectives
- The audit committee's responsibilities, including:
  - its duty to carry out, or to arrange, investigations requested by the board
  - the scope of its activities for:
    - financial reporting oversight
    - internal and external audit evaluation
    - risk management and internal control
    - compliance with laws, regulations, internal policies and industry standards
    - fraud control
    - continuous disclosure
  - its responsibility for ensuring procedures are in place for the receipt, retention and treatment of complaints received by the entity regarding accounting, internal accounting controls or auditing matters

<sup>44</sup> See Appendix 1 for a sample audit committee charter.

<sup>45</sup> Note that protocols applicable to all committees are not included here – such as appointment, conflicts of interest, preparation of agenda, minutes, attendance at meetings, etc.

- The authority delegated from the board to the audit committee, which might include the committee's right to:
  - obtain outside legal or independent professional advice at the entity's expense
  - institute special investigations
  - recommend the appointment and retention of the external auditor
  - approve the external audit fee and oversee the work of the external auditor
  - Audit committee membership and appointment
- Arrangements for meetings, including flexibility for the audit committee to invite non-members such as external auditors, internal auditors and members of management
- The audit committee's responsibility for reporting on its activity
- How the audit committee performance will be assessed

Audit committee members, the board, management and internal and external auditors need to understand the audit committee's charter, including the audit committee's scope of activities and communication and reporting arrangements.

The charter should be regularly monitored, and reviewed annually to ensure it remains relevant to the entity's needs (for instance, revising reporting requirements to cover board needs for additional information) and reflects current regulatory requirements and audit committee good practice.

## Membership

The membership of the audit committee is a key determinant of its success.

### Audit committee composition

The composition of the audit committee should include a balance of professional skills, knowledge and technical experience, as well as sufficient capacity, independence and objectivity, to discharge its responsibilities as defined in its charter.

The ASX Corporate Governance Council recommends the audit committee should be structured so that it:<sup>46</sup>

- consists only of non-executive directors
- consists of a majority of independent directors
- is chaired by an independent chair, who is not the chair of the board
- has at least three members.

S&P/ASX 300 entities are required to comply with these recommendations regarding the structure of the audit committee.<sup>47</sup>

The CEO (or managing director) should not be a member of the audit committee, although it is not uncommon for the CEO to be invited to attend audit committee meetings (see *Attendance* on page 54).

The board might appoint a person who is not a director of the entity to the audit committee to provide particular expertise.

<sup>46</sup> See Recommendation 4.1 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

<sup>47</sup> See ASX Listing Rule 12.7.

## Selection of audit committee members

Not only is it important to maintain audit committee continuity, but also provide a fresh perspective through succession planning and the selection process.

The following key qualities are desirable when appointing members:

- Individuals should have:
  - an understanding of the industry, the entity, its business and its products and/or services
  - a mindset that is independent of the entity's management
  - strong communication skills, including an ability to offer different perspectives and constructive suggestions
  - high levels of personal integrity and ethics
  - sufficient time available to devote to executing responsibilities
  - financial literacy, including an ability to read or understand financial statements, ask pertinent questions about them, and interpret and evaluate answers.
- The audit committee as a whole should have:
  - at least one member with financial expertise, which may be interpreted broadly as being “a qualified accountant or other financial professional with experience of financial and accounting matters.”
  - a mix of skills and experience relevant to discharging responsibilities, including experience in business, financial and legal compliance, risk management and international commercial background and experience, if applicable.

Committee members and the audit committee chair should be appointed by the board. A board nomination committee should be convened with the power to interview candidates considered to have the skills, experience and interest in being a member of the audit committee and recommend their appointment.

## Independent and non-executive members

It is recommended that the majority of members of the audit committee are independent and non-executive members. However, if the entity is in the S&P/ASX 300 at the beginning of the year, it is a requirement under the Listing Rules that the committee consist solely of non-executive directors, a majority of whom are “independent”.

Independent, non-executive directors are individuals free from any management, business or other relationship that could reasonably be perceived to materially interfere with their ability to act in the best interests of the entity. The “independence” of audit committee members should always be considered in relation to any applicable legislation, or regulation, that defines the requirements of independence for audit committee membership.

Independence is arguably a state of mind, and cannot necessarily be assessed by a person's relationship with the entity. It is commonplace to examine an audit committee member's past and current relationships with the entity as indicators of independence, or otherwise.

The ASX Corporate Governance Council<sup>48</sup> identifies the following relationships which may affect the independent status of a director if the director:

- Is a substantial shareholder of the entity or an officer of, or otherwise associated directly with, a substantial shareholder of the entity

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<sup>48</sup> See Box 2.3 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

- Is employed, or has previously been employed, in an executive capacity by the entity or another group member, and there has not been a period of at least three years between ceasing this employment and serving on the board
- Has, within the last three years, been a principal of a material professional adviser or a material consultant to the entity or another group member, or an employee materially associated with the service provided
- Is, or has been within the last three years, a material supplier or customer of the entity or other group member, or an officer of, or otherwise associated directly or indirectly with, a material supplier or customer
- Has a material, contractual relationship with the entity or another group member other than as a director
- Has close family ties with any person falling within any of the categories described above
- Has been a director of the entity for such a period that his or her independence may have been compromised.

This list is not exhaustive and if one or more of the above is exhibited by a director it is possible that their status as an independent director might be compromised. However in relation to the last point, the guidelines indicate that the mere fact a director has served on the board for a substantial period of time does not mean that he or she has become too close to management to be considered independent. It indicates that the board should regularly assess whether that might be the case for any directors who has served in that position for more than 10 years.

Members and potential members of the audit committee need to exercise care to ensure they disclose to the board for its consideration any relationships that could be viewed by other parties as impairing either the individual's, or the audit committee's actual or perceived independence. When deciding what is significant, consider the significance of the relationship to both the entity and to the individual.

The board might choose to appoint an individual to the audit committee, despite the existence of relationships identified above, because of the individual's business or other expertise but only after the Board has considered the materiality of the interest, position, association or relationship to determine whether it might interfere, or might reasonably be seen to interfere with the directors capacity to bring an independent judgement to bear on issues before the board and to act in the best interests of the entity and its security holders generally.

The ASX Corporate Governance Council recommends<sup>49</sup> that the listed entity should disclose:

- The names of the directors considered by the board to be independent directors
- If a director has an interest, position, association or relationship of the type described in the listing above [box 2.3] but the board is of the opinion that it does not compromise the independence of the director; this existence of such relationships should be disclosed in the corporate governance statement along with the reasons for considering such a director to be independent
- The length of service of each director.

### **Audit committee chair**

The chair of the audit committee plays a pivotal role in the overall effectiveness of the audit committee. The chair of the audit committee is preferably independent and not the chair of

<sup>49</sup> See Recommendation 2.3 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*

the board.<sup>50 51</sup> However, if the entity is in the S&P/ASX 300 at the beginning of its financial year, then this is actually a requirement under the Listing Rules.

The chair is responsible for:

- Promoting effective communications between the audit committee and the board, CEO, CFO, CAE, internal audit, other senior management and the external auditor
- Ensuring audit committee meetings run smoothly so that the views of all audit committee members are heard, that adequate time is allowed for discussion of each issue and that the agenda and meeting papers properly reflect proceedings.

The board should select an audit committee chair who:

- Has demonstrated strong leadership qualities
- Is knowledgeable of the duties and responsibilities of the position as outlined in the charter
- Has skills and knowledge about the industry, the entity's business, and financial reporting and auditing requirements
- Has strong communication skills, including the ability to promote effective working relationships among audit committee members and with others, such as management and the internal and external auditors

The chair's own term of appointment should be specified by the board and should relate to the director's term of appointment to the audit committee. The board may also appoint a deputy chair in the same manner.

### Induction of new members

The audit committee's knowledge and proficiency are enhanced when new members are appropriately acquainted with the audit committee's objectives and practices. All new members and existing directors need to be well briefed. Induction can be undertaken in many different ways, ranging from formal orientation programs to informal discussions.

A new member needs to understand the audit committee's role, objectives and responsibilities, be familiar with its relationships with management and the internal and external auditors, and have a sound knowledge of the entity's operations and the environment in which it operates, including the entity's code of conduct. They also need to understand the time and effort they will need to devote to their audit committee membership additional to the time and effort they devote to each board meeting.

Relevant information may be provided to new audit committee members, including:

- The audit committee charter
- An overview of business operations and the industry in which the entity operates
- All material previously provided to audit committee members on matters still before the audit committee, including current audit plans and outstanding corrective action from previous audit reports (both external and internal)
- Papers from recent audit committee meetings
- Internal audit charter
- Financial performance information
- Risk profile of the entity and a list of material business risks
- Risk appetite of the board
- Risk management framework and processes

<sup>50</sup> See Recommendation 4.1 of the 3<sup>rd</sup> edition of ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

<sup>51</sup> ASX Listing Rule 12.7.

- Internal control framework and processes
- Key financial reporting policies, including any related party issues
- Legal and regulatory requirements, including external reporting and compliance responsibilities
- Code of conduct for the entity, board and/or the audit committee
- Estimates of the time members need to commit to their audit committee role
- Fraud control framework (and high level details on previous fraud issues/allegations, if any).

All new members should meet with the chair, other audit committee members, senior management, and external and internal auditors as soon as practicable after being appointed.

### **Ongoing training**

It is important that audit committee members keep abreast of current developments in matters that affect their capacity to effectively discharge their duties. Audit committee members may routinely receive focussed information on:

- Important relevant industry issues, trends and developments
- Key financial, and other performance indicators, of the entity detailing the level of achievement of the entity's objectives
- Significant proposed changes in financial reporting and regulatory requirements
- Other matters that might have a significant impact on the risk profile of the entity.

Audit committee members should be encouraged to attend relevant third-party training, conferences and seminars and share information at subsequent audit committee meetings.

### **Rotation**

Periodic rotation of audit committee members is encouraged as it enhances the perception of audit committee independence.

Rotation will generally depend on the size of the board from which audit committee members are drawn, and the availability of suitable candidates from within and outside the entity.

### **Conducting meetings**

How audit committee meetings are conducted will greatly influence the ability of audit committee members to achieve the audit committee's objectives.

### **Frequency of meetings**

A regular schedule of meetings should be designed to enable the audit committee to effectively discharge its responsibilities.

While the number and duration of audit committee meetings will depend on the size and complexity of the audit committee's responsibilities, it is common for the following to occur:

- Audit committees typically meet at least four times a year to coincide with key dates within the financial reporting and audit cycles, and to plan the year and review performance
- There may be a separate meeting to consider the annual financial report and half year review, which may be covered within the normal meeting schedule or in an additional

meeting, where necessary. This meeting should allow ample time for detailed consideration of the report,<sup>52</sup> with the agenda tailored accordingly and not overburdened with other items. For example, important accounting judgements, key audit matters and related decisions may be determined ahead of the year end and at an earlier meeting than the one that considers the annual financial report

- When possible, meetings are arranged so that all audit committee members can attend. The proposed schedule of audit committee meetings may be discussed and agreed well in advance. In planning the schedule of meetings, reference should be made to the meeting schedule of the full board, allowing sufficient time between audit committee and board meetings to action any items and prepare papers and reports to be tabled at the board meeting
- The audit committee charter normally empowers the chair to convene a special meeting at the request of the board, an audit committee member, senior management, the external or internal auditor.

### Structure of meetings

Normal business practices for committee meetings apply to audit committees.

Well-run audit committee meetings typically include:

- The preparation of a formal, well-structured agenda with reference to the audit committee charter to ensure that the agenda and meeting papers are appropriate
- The internal and external auditors are invited to contribute to the agenda
- The chair reviews and approves the agenda, and relevant meeting papers, before issuing them to audit committee members and other parties authorised by the audit committee
- The agenda and meeting papers are distributed before the meeting, allowing sufficient time for members to read them carefully. As a guide, papers should be distributed at least one week before the meeting. However, where there is a large volume of papers, or papers involve complex matters, the audit committee may require them to be distributed more than one week before the meeting to enable members to carefully review and understand the content of papers

In ASIC v Healey (2011) 196 FCR 291, notwithstanding a complex corporate reporting structure, multiple sets of financial statements requiring approval and reporting deadlines, the ruling confirmed the proposition that members of the audit committee and other directors have a duty to read the financial statements and check them. Timing issues and information overload cannot be used as defences in avoiding this responsibility.

- Inclusion of the annual work plan or calendar of events, cross-referenced to the charter, in meeting papers may be useful in providing audit committee members with an overview and ensuring compliance with the charter
- Efficient running of the meeting is assisted by:
  - Ensuring the meeting starts and finishes on time, while taking as long as necessary to adequately consider agenda items
  - Members agreeing to the priority of, and the time to be devoted to, each item at the commencement of each meeting
  - Meeting processes requiring members to declare any actual, perceived or potential conflicts of interest each year, and at the beginning of each meeting to strengthen the audit committee's independence. Members consider past

<sup>52</sup> Time should be allowed for the audit committee to consider any changes that have been made to the financial report since the audit committee papers were distributed. Management may provide the audit committee with a detailed list of all such changes.

- employment, consultancy arrangements and related party issues when considering conflicts of interest
  - Establishing clear decision-making processes and voting protocols.
- The minutes are usually administered as follows:
  - Minutes are complete, clear and concise, providing a record of proceedings, including the issues, outcomes and actions with clear responsibilities and timelines attached
  - Draft minutes are provided to the chair within a week of the meeting for clearance and distributed to audit committee members within two weeks of the meeting
  - Within two weeks of the meeting, the audit committee secretariat provides senior management with a brief summary of issues dealt with at each meeting, including details of actions to be taken with assigned responsibilities and timelines
  - The minutes are circulated to the board with the papers of the next board meeting after the audit committee meeting
  - The chair should brief the board on significant issues
  - The minutes are signed by the chair at the subsequent audit committee meeting.

## Attendance

Regarding attendance at audit committee meetings, the following matters should be considered:

- Attendance of non-members is by invitation only. Audit committees should always reserve this right to meet alone, without non-members, including management, in attendance. This enables the audit committee to approach its tasks objectively and to maintain both actual and perceived independence
- The CEO, CFO and other relevant staff are generally invited to attend meetings to participate in discussion of particular agenda items. Their presence can provide an opportunity to resolve issues swiftly and efficiently
- The internal auditor and external auditor are generally invited to attend relevant parts of each meeting. Where necessary, the chair might decide that they should not attend for certain agenda items
- The audit committee should meet separately, at least annually, with both the internal auditor and the external auditor to discuss issues of mutual interest, without management present.

The chair of the audit committee is likely to have meetings with key executives and advisors outside the audit committee meetings to ensure ongoing awareness of issues and activities as they arise.

## Reporting by the audit committee

### To the board

The formality, detail and frequency of audit committee reports to the board vary. The audit committee refers to its charter when preparing a report.

Ideally, the audit committee should formally report to the board at the board meeting following each audit committee meeting, providing a summary of the audit committee's work and results.

The report should typically cover areas such as:

- The audit committee minutes<sup>53</sup>, including details of members present
- Any formal resolutions of the audit committee
- Assessment of management processes supporting external reporting
- Procedures for selection and appointment / removal of external auditor
- Information about the audit processes and the results of work completed by the internal and external auditors as well as an assessment thereof
- Any determination by the audit committee about the external auditor's independence
- The annual review of the audit committee charter and whether the audit committee has achieved the responsibilities set out in the charter
- Any recommendations requiring board actions and/or approval
- Audit recommendations for corrective action and status report
- Information about instances of actual, suspected or alleged fraud, if any
- Information about whistleblowing by employees or other parties, if any
- Any concerns about the entity's ability to continue as a going concern
- Recommendations on whether to extend the rotation period for the external audit engagement partner beyond five years to a maximum of seven years<sup>54</sup>
- Information about the annual transparency report published by the external auditor, if applicable<sup>55</sup>
- Information about an audit deficiency report published by ASIC on its website, if applicable

Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012* an audit deficiency is where ASIC reasonably believes that there is a significant weakness, in the auditor's quality control system or a significant weakness in the conduct of the audit that may be detrimental to the overall quality of the audit as a result of a failure by the auditor to comply with:

- auditing standards
- the auditor independence requirements of the *Corporations Act 2001*
- any applicable code of professional conduct
- provisions of the *Corporations Act 2001* dealing with the conduct of audits.

- Information about any communications received directly from ASIC regarding significant matters (such as an audit client's accounting or disclosure practices) identified while exercising its functions and powers in relation to audit (mainly its surveillance and inspection activities)<sup>56</sup>
- Information about correspondence from other regulators or stakeholders, if any (for example, from APRA in relation to APRA-regulated entities)
- Other matters the audit committee believes need to be reported to the board.

<sup>53</sup> APES GN 41 Management Representations prepared and issued by the Accounting Professional and Ethical Standards Board, provides guidance that a Member in Business who is at the audit committee level should consider taking reasonable steps to ensure that key decisions made at those meetings are appropriately reflected in the minutes of the applicable meeting.

<sup>54</sup> See footnote 18

<sup>55</sup> Under the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, an individual auditor, an audit firm or an authorised audit company conducting audits of ten or more entities of certain specified categories is required to publish an annual transparency report. The disclosures in the transparency report will include the names of relevant entities audited, information about the auditor's governance structure and independence practices, and other information.

<sup>56</sup> The *Corporations Legislation Amendment (Audit Enhancement) Act 2012* gives ASIC the power to communicate directly with the audit committee, other directors or senior management of an entity in relation to significant matters identified by ASIC during the course of the exercise of its statutory functions in relation to audit.

## **To the shareholders**

The annual report would typically include information on the audit committee's role and responsibilities, structure and membership, and its principal activities during the year. This information would be included as part of the wider corporate governance information in the annual report.

Improving the communication channels to investors highlights the importance of the active role that audit committees play in promoting greater transparency in reporting.

The following material would typically be included in the corporate governance section of the annual report:

- A summary of the role of the audit committee
- Details of the names and qualifications of those appointed to the audit committee, or, where the audit committee has not been formed, those who fulfil the functions of an audit committee
- The number of meetings of the audit committee and the names of the attendees.

## **To other stakeholders**

The following information may be publicly available on an entity's website in a clearly marked corporate governance section:

- The audit committee charter
- Description of the role and responsibilities of the audit committee
- A description of the audit committee's oversight role for the entity's governance, risk management and internal control
- Names of audit committee members, professional background and qualifications
- Information on procedures for the selection and appointment of the external auditor, and for the rotation of external audit engagement partner
- Information on procedures for the selection and appointment of the internal auditor.

## **Assessing performance**

### **Assessing the audit committee's performance**

Recent pronouncements on corporate governance have emphasised the need for boards and board committees to demonstrate a high level of professionalism, including a regular assessment of ways in which their performance can be improved.

An assessment of audit committee performance by the board should be undertaken as part of any periodic review of overall board performance, although a high performing audit committee is also likely to consider on an annual basis how it can improve its performance in the year to come.

Matters for consideration in any review of performance include:

- Identifying and agreeing to the criteria by which the performance of the audit committee will be assessed
- Assessing the effectiveness of the audit committee as a whole and the performance of individual audit committee members
- Identifying the process for implementing action plans developed in response to areas identified for improvement
- Assessing compliance with the audit committee's charter.

A performance assessment may be carried out by a third part of the board or an audit committee may elect to utilise a self-assessment approach to performance, with findings reported to the board. A self-assessment guide for audit committees is provided in Appendix 2.

Audit committees may also wish to take advantage of opportunities to benchmark their organisational procedures and activities with audit committees in similar entities.

### **Evaluation of individual audit committee members**

Evaluation of individual audit committee member performance may be carried out by a third party, by the chair of the audit committee (possibly in conjunction with the board chair) or by self-assessment by individual committee members.

Any assessment would typically cover issues such as whether the member has demonstrated:

- A good understanding of, and commitment to, the audit committee's role and responsibilities
- Objectivity and independence
- An ability and willingness to take difficult but constructive stands at meetings when necessary
- A good understanding of the entity's business
- A sound understanding of the entity's financial reporting issues and obligations
- A good understanding of the entity's risk management and internal control processes
- Participation in activities to keep their business, industry, financial and regulatory knowledge current
- Preparation for, and participation in, audit committee meetings.

A self-assessment questionnaire to assist with the evaluation of a member's performance and contribution to the audit committee is included at Appendix 2.

Areas of additional focus arising out of performance assessments should be formally communicated to the board.

### **Further reading**

*Corporate Governance Principles and Recommendations 3<sup>rd</sup> edition* 2014, ASX Corporate Governance Council, Australia

*Audit Committee Effectiveness—What Works Best*, 4th ed., June 2011, sponsored by The Institute of Internal Auditors Research Foundation and prepared by PricewaterhouseCoopers LLP

*The Audit Committee Handbook*, 5th ed., March 2010, Louis Braiotta, Jr., R. Trent Gazzaway, Robert Colson, Sridhar Ramamoorti, USA

*International Professional Practices Framework*, 2011, The Institute of Internal Auditors Inc.

*Walk the line: Discussion and insights with leading audit committee members*, February 2012, The Institute of Chartered Accountants Australia, Financial Reporting Council (UK) and The Institute of Chartered Accountants of Scotland

*Public Sector Audit Committees*, March 2015, Australian National Audit Office

## Appendix 1

### Sample audit committee charter

The following is one example of an audit committee charter and captures many of the good practices used today. No sample charter encompasses all activities that might be appropriate to a particular audit committee, nor will all activities identified in a sample charter be relevant to every committee. Each committee should tailor this charter to their needs and governing rules.

The audit committee's annual work plan may be developed having regard to, and being cross-referenced to, its charter to ensure that the audit committee acts according to its authority and fulfils its responsibilities.

### Sample audit committee charter

#### Purpose

The audit committee is appointed by the board of directors to assist the board in discharging its responsibilities to oversee corporate reporting processes, including the financial reporting process, risk management and internal control, external audit, internal audit and compliance with laws, regulations, internal policies (including the code of conduct) and industry standards.

#### Authority

The board authorises the audit committee, within its scope of responsibilities, to:

- Perform the activities identified within this charter

#### Responsibilities

The audit committee will carry out the following responsibilities:

##### Corporate Reporting

- Gain an understanding of the current areas of greatest financial risk and how they are managed
- Review significant accounting and reporting issues, including recent professional and regulatory pronouncements, and understand their impact on financial reports
- Review complex or unusual financial transactions and highly judgemental areas, and understand their effect on the financial report
- Oversee the periodic financial reporting process implemented by management and review the interim financial statements, annual financial statements, concise financial report, if any, and preliminary announcements before their release
- Meet with management and the external auditor to review the financial statements, key accounting policies and decisions, and the results of the audit, including significant adjustments, unadjusted differences and any difficulties encountered or unresolved disagreements with management
- Review all representation letters signed by management and assess for completeness and appropriateness

- With management and the external auditor, review all matters required to be communicated to the audit committee under Australian Auditing Standards, such as key audit matters for listed companies.
- Review the CEO and CFO declarations regarding the financial report and financial records, prepared in accordance with the requirements of the Corporations Act 2001
- Based on its review of the financial statements, note disclosures and other information, provide a recommendation to the board whether the financial report should be approved
- Review the other sections of the annual report before its release and consider whether the information is understandable and consistent with members' knowledge about the entity and its operations, and is unbiased
- Review management's process for ensuring that information contained in analyst briefings, investor presentations and press announcements is consistent with published financial information, and is balanced and transparent.

#### ***Working with the external auditor***

- Provide a recommendation to the board on the appointment of the external auditor or the assessment of potential and continuing auditors
- Assess the quality of the audit conducted and evaluate performance of the auditor
- Maintaining and reviewing auditor independence and objectivity by considering the external auditor's relationships and services with the entity and other relevant organisations
- Establishing ongoing communications with the auditors so as to address any risk or areas of concerns and ensure access to directors and the audit committee.
- Facilitating the audit process by supporting the audit and ensuring company management are accountable, supportive and helpful to the audit process
- At least once a year meet separately with the external auditor to discuss matters that the audit committee or auditor believes should be discussed privately. Ensure the external auditor has access to the chair of the audit committee when required.

#### ***Working with internal audit***

- Recommend to the board on the appointment and removal of the CAE
- Review and approve the internal audit charter
- Ensure the internal auditor reports to the audit committee for functional purposes and to the CEO for administrative purposes, and has access to all levels of management with the right to seek information relevant to the internal audit activity
- Review and approve the strategic internal audit plan, often for a 2-3 year period to assess whether it addresses the material business risks of the entity
- Review and approve the annual internal audit plan and any significant changes made to the plan
- Review reports of results of internal audit engagements, audit-related activities, team capability, audit performance and other important matters
- Monitor compliance with standards, together with quality and improvement arrangements
- Without management being present, meet periodically with the CAE to discuss matters that the audit committee or internal auditor believes should be discussed privately
- Make enquiries of the CAE to determine any scope or budget limitations that may impede the execution of internal audit responsibilities.

#### ***Risk management and internal control***

- Consider whether the entity has an appropriate attitude towards controls and communicate the importance of risk management and internal control

- Ensure that management has appropriate processes for identifying, assessing and responding to risks in a manner that is in accordance with the entity's risk appetite, and that those processes are operating effectively
- Ensure that material business risks, including operational, financial, legal and compliance risks, are appropriately reflected in the risk profile and reported to the board at least annually
- Evaluate the overall effectiveness of the risk management and internal control framework, including activities undertaken by internal audit and external audit, together with other assurance providers, to provide a holistic picture of assurance across the entity
- Understand the internal control systems implemented by management for the approval of transactions, the recording and processing of financial data, and ensuring that financial statements comply with relevant standards and requirements, and are subject to appropriate management review
- Understand the internal control systems implemented by management for the security of computer systems and applications, and the contingency plans for processing financial information in the event of a systems breakdown, or to protect against computer fraud or misuse
- Understand the processes management has implemented for managing insurable risks and, if applicable, self-insurance, including assessing the adequacy of insurance cover
- Meet periodically with the head of risk management without other management being present.

#### ***Compliance with laws, regulations, ethical requirements, internal policies and industry standards***

- Review the effectiveness of the entity's systems for monitoring compliance with laws, regulations, internal policies and industry standards, and the results of management's investigation and follow-up (including disciplinary action) of any instances of non-compliance
- Obtain regular updates from management and the head of compliance about compliance matters that may have a material impact on the entity's financial statements, strategy, operations or reputation, including material breaches of laws, regulations, standards and company policies
- Review and liaise with management and/or regulators, as appropriate about the findings of any examinations by regulators
- Review and, where applicable, approve the policies, processes and framework for identifying, analysing and addressing complaints (including whistleblowing) and review material complaints and their resolution
- Review the entity's process for communicating the code of conduct to staff and assess the effectiveness of, and compliance with the code
- Discuss with management whether all regulatory compliance matters of the entity have been considered in the preparation of the financial statements
- Meet periodically with the head of compliance and legal counsel without other management being present.

#### ***Fraud and Corruption***

- Ascertain whether fraud/corruption risks have been included in the assessment of the risk profile of the entity
- Review management's anti-fraud/corruption strategies and programs
- Enquire of management and the external auditor regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments

- Enquire of management, the internal auditor and the external auditor whether they are aware of any actual, suspected or alleged fraud or corruption affecting the entity and how they responded to such instances, including any changes made to the internal control environment
- Obtain representations from management that all known instances of actual, suspected or alleged fraud or corruption, have been disclosed to the audit committee
- Ensure the entity has fulfilled its fraud or corruption reporting obligations, if any.

#### **Reporting responsibilities**

- Report regularly to the board about audit committee activities and make appropriate recommendations

#### **Evaluating performance**

- Evaluate the audit committee's own performance (that of individual members and collectively) on a regular basis

#### **Other responsibilities**

- Perform other activities related to this charter as requested by the board.

#### **Membership**

The audit committee will consist of [insert number (at least three)] non-executive members of the board of directors, the majority being independent.

The board, on the recommendation of its nominating committee (where applicable), will appoint audit committee members and the audit committee chair who will be an independent and not the chair of the Board.

Each audit committee member should have skills, knowledge and experience appropriate to the entity's business.

The committee, as a whole, should have a mix and balance of relevant skills, knowledge and experience.

Each audit committee member must be financially literate. At least one member must have accounting or related financial expertise.

#### **Meetings**

The audit committee will typically meet at least four times a year, with authority to convene additional meetings, if necessary to fulfil the audit committee charter. All audit committee members are expected to attend each meeting, in person or via teleconference or video conference.

- Only audit committee members are entitled to attend meetings. The audit committee may invite other people (such as the other board members, CEO, CFO, CAE, internal legal counsel and the external auditor) to its meetings as it considers necessary.

An agenda and meeting papers will be prepared and provided in advance to members, along with appropriate briefing materials.

Agreed decision-making processes and voting protocols will be followed.

Minutes of meetings will be prepared and circulated to audit committee members and to the board at its next meeting.

## Appendix 2

### Self-assessment guide for audit committees

This guide has been provided to illustrate the types of considerations against which the audit committee might assess its performance collectively. Similar considerations may be applied to the assessment of the performance of individual members of the audit committee.

The guide includes a large number of considerations and should be tailored by each audit committee to meet its own requirements. The audit committee may complete the guide as a whole or individually, and then collate individual responses. The chair of the audit committee and members may decide to weight certain aspects of the self-assessment guide more than others. The audit committee may also seek input from non-member attendees and separately assess the information received.

The results of the self-assessment should be used by the audit committee for discussion to identify areas for improvement and a summary of agreed action items should be provided to the chair of the board.

We suggest the responses to the statements below are rated using a rating scale, such as the Likert Scale. A Likert-type scale assumes that the strength/intensity of experience is linear, i.e. on a continuum from strongly agree to strong disagree, and makes the assumption that attitudes can be measured.

Likert scale examples include the following:

- Agreement – Strongly agree/Agree/Undecided/Disagree/Strongly disagree
- Frequency – Very frequently/Frequently/Occasionally/Rarely/Never
- Importance – Very important/Important/Moderately important/Of little importance/Unimportant
- Likelihood – About always true/Usually true/Occasionally true/Usually not true/Almost never true

The audit committee's self-assessment approach should be consistent with the committee's charter. For this reason, the considerations listed below reflect the structure and content of the sample charter provided in Appendix 1.

### Assessing Audit Committee Performance

In evaluating the performance of the audit committee, the following would typically be considered.

#### Authority

- The Audit Committee has obtained authority from the board to perform the activities in its charter

## **Responsibilities**

### ***Financial reporting***

- Gained an understanding of the current areas of greatest financial risk and how they are being managed
- Reviewed significant accounting and reporting issues, including recent professional and regulatory pronouncements, and gained an understanding of their impact on the financial report
- Reviewed complex or unusual financial transactions and highly judgemental areas, and understood their effect on the financial report
- Provided an oversight role of the periodic financial reporting process implemented by management and reviewed interim financial statements, annual financial statements, concise financial report, if any and preliminary announcements before their release
- The Audit Committee has met with management and the external auditor to review and understand the interim financial statements, annual financial statements, concise financial report, if any, and preliminary announcements prior to their release. In particular, reviewed key accounting policies and decisions, and the results of the audit, including significant adjustments, unadjusted differences and any difficulties encountered or unresolved disagreements with management?
- Reviewed all representation letters signed by management, for completeness and appropriateness
- Reviewed with management and the external auditor all matters required to be communicated to the audit committee under Australian Auditing Standards, including key audit matters when appropriate
- Reviewed the CEO and CFO declarations in respect of the financial report and financial records
- Reviewed the financial statements, note disclosures and other information and recommended to the board whether the financial report should be approved
- Reviewed other sections of the annual report before its release, for consistency with members' knowledge about the entity and its operations, is unbiased
- Reviewed management's process for ensuring that information contained in analyst briefings, investor presentations and press announcements was consistent with published financial information, and was balanced and transparent

### ***Working with the external auditor***

- Recommended to the board on the appointment of the external auditor or the assessment or potential and continuing auditors
- Considered the quality of the audit conducted and evaluated the performance of the auditor
- Reviewed auditor independence and objectivity by considering the external auditor's relationships and services with the entity and other relevant organisations
- Established effective ongoing communications with the auditors so as to address any risk or areas of concerns and ensure access to directors and the audit committee.
- Facilitated the audit process by supporting the audit and ensuring company management are accountable, supportive and helpful to the audit process
- The Audit Committee has met privately with the external auditor at least once a year without management present and ensured that the external auditor had access to the chair of the audit committee when required

### ***Working with the internal audit activity***

- Where appropriate the Audit Committee provided recommendations to the board on the appointment and removal of the CAE
- Review and approved the internal audit charterEnsured the internal auditor reports to the audit committee for functional purposes and to the CEO for administrative purposes
- Reviewed and approved the strategic internal audit plan
- Reviewed and approved the annual internal audit plan and any significant changes
- Reviewed reports on the results of internal audit engagements, audit-related activities, audit team capability, audit performance and other important matters
- Monitored compliance with standards, together with quality and improvement arrangements
- The Audit Committee has met privately with the internal auditor at least once a year without management present
- Made enquiries of the CAE to determine the scope of budget limitations that could impede the execution of internal audit responsibilities.

### ***Risk management and internal control***

- Assessed the entity's attitude towards controls and promoted the importance of risk management and internal control
- Ensured management has appropriate processes for identifying, assessing and responding to risks, ensuring that they are appropriate to the entity's risk appetite and these processes were operating effectively
- Ensured the material business risks, including operational, financial, legal and compliance risks, are appropriately reflected in the risk profile and reported at least annually to the board
- Evaluated the overall effectiveness of the risk management and internal control framework, including activities undertaken by internal and external audit, together with other assurance providers, to provide a holistic picture of assurance across the entity
- Obtained an understanding of the internal control systems implemented by management for the approval of transactions, the recording and processing of financial data, and ensuring that financial statements complied with relevant standards and requirements, and ensured they are subject to appropriate management review
- Reviewed the adequacy of controls for the security of computer systems and applications, and the contingency plans for processing financial information in the event of systems breakdown, or computer fraud or misuse
- Reviewed the processes management has implemented for managing insurable risks and, where applicable, self-assurance, and assessed the adequacy of insurance cover
- The Audit Committee has met privately with the head of risk management without management being present

### ***Compliance and ethics***

- Reviewed the effectiveness of management's systems for monitoring compliance with law, regulations, internal policies and industry standards, and the results of management's investigations and follow-up of any instances of non-compliance
- Obtained regular updates from management and the head of compliance about compliance matters that may have a material impact on the entity's financial statements, strategy, operations or reputation, including material breaches of laws, regulations, standards and company policies
- Liaised with management and/or regulators, as appropriate, about the findings of any examinations by regulators

- Reviewed and approved (where applicable) the policies, processes and framework for identifying, analysing and addressing complaints (including whistleblowing) and reviewed material complaints and their resolution?
- Reviewed the entity's process for communicating the code of conduct to staff and assessed the effectiveness of, and compliance with, the code
- Discussed with management whether all regulatory compliance matters of the entity were considered in the preparation of the financial statements
- The Audit Committee met privately with the head of compliance and legal counsel, without management being present.

### ***Fraud and Corruption***

- Ensured fraud risks have been included in the assessment of the risk profile of the entity
- Reviewed management's anti-fraud and corruption strategies and programs
- Enquired of management and the external auditor regarding their assessments of the risk of material misstatement in the financial report due to fraud, including the nature, extent and frequency of such assessments
- Enquired of management, the internal auditor and the external auditor whether they have any knowledge of actual, suspected or alleged fraud or corruption affecting the entity and how they responded, including any changes made to the internal control environment
- Obtained representations from management that all known instances of actual, suspected or alleged fraud or corruption have been disclosed to the audit committee
- Ensured that management has fulfilled the entity's fraud and corruption reporting obligations, if any

### ***Reporting by the audit committee***

- The Audit Committee reports regularly to the board on the audit committee's activities and made recommendations where appropriate

### ***Evaluating performance***

- The Audit Committee evaluates the audit committee's performance, as a whole and for each member, at least once a year

### ***Other responsibilities***

- The Audit Committee has satisfactorily performed other activities, as requested by the board

### ***Composition***

- The size of the audit committee is appropriate to the entity and the responsibilities in the audit committee charter
- All audit committee members are non-executive directors
- The majority of audit committee members are independent
- The mix of skills, knowledge and experience of the audit committee as a whole been reviewed and is appropriate
- All audit committee members have skills, knowledge and experience appropriate to the entity's business
- All audit committee members financially literate and able to understand financial statements; with at least one member with accounting or related financial expertise

### Meetings

- The audit committee meet regularly throughout the year and the number of meetings is appropriate for the nature of the entity and the responsibilities of the audit committee
- Only audit committee members attend meetings, with the CEO, CFO, CAE, internal legal counsel, other senior management and the external auditor invited to attend meetings as necessary
- Audit committee members attend every meeting or provided input, if unable to attend
- The agenda and meeting papers are provided well in advance of meetings
- Decisions were made by the audit committee in accordance with agreed decision-making processes and voting protocols
- Minutes are taken and appropriately circulated to committee members in a timely manner, and to the Board at its next meeting

### Overall

- What has been done well on the Audit Committee this year?
- What has not been done well on the Audit Committee this year?
- What are three areas for improvement for the Audit Committee operations and processes going forward?

## Appendix 3

### Management representation letter

Internal management representations to those charged with governance  
Management Representation letters are commonly used by those charged with governance to assist them in discharging their obligations to external parties. Such representations may include:

- Financial Reporting Certifications including Internal Control Questionnaires;
- Declarations provided to the board or audit committee of local or foreign jurisdictions in accordance with the respective jurisdiction's regulations; or
- Representations in respect of continuous disclosure obligations to enable disclosures to the market.

Section 8 of APES GN 41 *Management Representations* prepared and issued by the Accounting Professional and Ethical Standards Board provides guidance in relation to management representation considerations at the audit committee level.

### External management representations to the external auditor

The external auditor requests written representations from management with appropriate responsibilities for the financial report<sup>57</sup>. The following list is provided to assist audit committees to understand the types of representations included in a representation letter prepared and signed by management. It includes selected matters that are commonly included and may not include all representations provided by management to the external auditor. It is provided for information purposes only and is not definitive.

Management would ordinarily represent, or confirm, to the external auditor that:

#### Regarding the financial report

- Management has fulfilled its responsibilities for the preparation of the financial report in accordance with [the applicable reporting framework]
- All transactions have been recorded in the accounting records and are reflected in the financial report
- Significant assumptions used by management in making accounting estimates, including those measured at fair value, are reasonable
- Related party relationships and transactions have been appropriately accounted for and disclosed
- All events subsequent to the date of the financial report required to be adjusted or disclosed have been adjusted or disclosed
- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial report as a whole. (A list of the uncorrected misstatements may be attached to the representation letter)

#### Regarding the information provided

- Management has provided the auditor with:
  - access to all information of which they are aware that is relevant to the preparation of the financial report such as records, documentation and other matters
  - additional information that the auditor has requested from them for the purpose of the audit

<sup>57</sup> See Auditing and Assurance Standards Board ASA 580 *Written Representations*

- unrestricted access to persons within the entity from whom the auditor determined it necessary to obtain audit evidence
- all information required to be provided by the law or regulations.
- Management has disclosed to the auditor:
  - the results of their assessment of the risk that the financial report may be materially misstated as a result of fraud
  - all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial report communicated by employees, former employees, analysts, regulators or others
  - all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial report
  - all known actual or possible litigation and claims whose effects should be considered when preparing the financial report; and accounted for and disclosed in accordance with [the applicable financial reporting framework]
  - the identity of the entity's related parties and all the related party relationships and transactions of which we are aware
  - all the documents that they expect to issue that may comprise other information.

#### **Regarding other matters**

- Management acknowledges its responsibility for the design, implementation and maintenance of internal control to prevent, deter, detect and report on fraud.

## Appendix 4

### External audit versus internal audit

There are fundamental differences between the work of external audit and internal audit which are shown in the following table:

External Audit		Internal Audit
Appointed from outside the organisation (independently appointed in the public sector)	<b>Status</b>	Employees of the organisation, or can be an independent entity through outsourced or co-sourced arrangement
Independent of management and the governing body (including board of directors)	<b>Independence</b>	Independent of activities audited, but able to respond to the needs of management and the audit committee
Serves third parties that need reliable financial information, including shareholders (corporate sector) and parliament (public sector)	<b>Serving</b>	Serves the needs of the organisation
Shareholders and board of directors	<b>Reports to</b>	Audit committee functionally for operations and chief executive officer for administration
True and fair view of financial statements	<b>Objective</b>	Varies according to the audit – focused on evaluating controls designed to assure the accomplishment of the organisation's goals and objectives
Historical events as expressed in financial statements	<b>Focus</b>	Forward-looking
Reviews records supporting the financial statements (periodically, usually annually)	<b>Coverage</b>	Reviews governance, risk management, and control processes according to risk-based need
Opinion on financial statements	<b>Outcome</b>	Helps organisation to enhance and protect organisation value and accomplish their objectives
Incidentally concerned with prevention and detection of fraud and corruption in general, but is directly concerned when financial statements may be materially affected	<b>Fraud and Corruption</b>	Is directly concerned with the prevention of fraud and corruption in any activity reviewed
Shareholders, regulators, board of directors and audit committee	<b>Reports go to</b>	Management and audit committee
External audit standards	<b>Standards</b>	Internal audit standards
Mandatory	<b>Qualifications</b>	Not mandatory, though there is a recent shift in some jurisdictions to require the chief audit executive to have appropriate certifications and qualifications, or demonstrated high-level experience

**Comment [HR12]:** Several concerns with this table and the content. Suggest remove table. Too granular, content not wide enough to cover all scenarios Wording issues.

## Glossary

### APRA-regulated entities

Entities that are regulated by the Australian Prudential Regulation Authority (APRA), including banks, building societies and credit unions (authorised deposit-taking institutions), life and general insurance and reinsurance companies, friendly societies and superannuation funds (excluding self-managed funds).

### Audit adjustments

Corrections made to misstatements in financial information or disclosures identified by the auditor in conducting an audit of the financial report.

### Audit engagement partner

The partner or other person in the audit firm who is responsible for the audit engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

### Business risks

All risks to the organisation including operational, financial, compliance and strategic risks.

### Chief audit executive (CAE)

A person in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and the *International Professional Practices Framework* (IPPF), which includes the *Definition of Internal Auditing*, the *Code of Ethics* and the *International Standards for the Professional Practice of Internal Auditing*.

### Concise financial report

A report for a financial year prepared under Chapter 2M of the *Corporations Act 2001* in accordance with Australian Accounting Standard AASB 1039 *Concise Financial Reports*.

### Continuous disclosure obligations

Continuous disclosure is the timely advising of information to keep the market informed of events and developments as they occur. Under the ASX Listing Rules, once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities, the entity must immediately tell the ASX that information.

### Corruption

Corruption can be defined as abuse of entrusted power for private gain.

### External auditor

An individual auditor, an audit firm or an authorised audit company providing external audit services.

### Financial report (as set out in the Corporations Act 2001)

An annual financial report or a half-year financial report prepared under Chapter 2M of the *Corporations Act 2001*. An annual financial report contains the financial statements, notes to the financial statements and the directors' declaration about the financial statements and

notes. The half-year financial report contains the financial statements and notes to the financial statements.

### Financial statements

A complete set of financial statements comprises:

1. A statement of financial position as at the end of the period
2. A statement of comprehensive income for the period
3. A statement of changes in equity for the period
4. A statement of cash flows for the period
5. Notes, comprising a summary of significant accounting policies and other explanatory information
6. A statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

### Fraud

Fraud can be defined as wrongful or criminal deception intended to result in financial or personal gain.

Comment [HR13]: different to ASA

### Internal audit

Internal audit as defined by the International Professional Practices Framework (IPPF) issued by the Institute of Internal Auditors (IIA): "Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes."

### Internal audit activity

The function, as defined by the *International Standards for the Professional Practice of Internal Auditing*, that is: "A department, division, team of consultants or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organisation's operations. The internal audit activity helps an organisation accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes".

### Internal auditor

The individual/s who perform the internal audit services as part of the internal audit activity

### International Financial Reporting Standards (IFRS)

Standards for accounting and financial reporting issued by the International Accounting Standards Board (IASB).

### Risk appetite

The level of risk that the entity is prepared to accept

### Risk profile

The description of the entity's set of risks.

### Representation letter

A written statement provided by management of an entity to confirm certain matters represented by them in the financial report, or in relation to the preparation of the financial report, or to support other audit evidence. Representation letters may be requested by those charged with governance, including the audit committee, or the external auditor.

### Those charged with governance

The person/s or organisation/s (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process and therefore may include the audit committee.

## List of Acronyms

AASB	Australian Accounting Standards Board
AICD	Australian Institute of Company Directors
ANAO	Australian National Audit Office
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ASX	Australian Stock Exchange
AUASB	Australian Auditing and Assurance Standards Board
CAE	Chief Audit Executive
CEO	Chief Executive Officer
CFO	Chief Financial Officer
COSO	Committee of Sponsoring Organisations of the Treadway Commission
Finsia	Financial Services Institute of Australasia
FRC	Financial Reporting Council
IFRS	International Financial Reporting Standards
IIA	The Institute of Internal Auditors Inc.
IIA-A	Institute of Internal Auditors-Australia
IPPF	International Professional Practices Framework

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# AUASB Board Meeting Summary Paper

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AGENDA ITEM NO. **4**

Meeting Date: 29 November 2016

Subject: GS 001 *Concise Financial Reports under the Corporations Act 2001*

Date Prepared: 14 November 2016

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☒ Action Required

☐ For Information Purposes Only

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## Agenda Item Objectives

1. To approve the project plan as presented at AI x.1.
2. To review and provide input into the draft revised GS 001 *Concise Financial Reports Under the Corporations Act 2001* to take into account the changes to ASA 810 *Engagements to Report on Summary Financial Statements* arising from the new suite of auditor reporting standards.

## Background

GS 001 was first issued in 2007, revised in 2008 and again in 2010. At the time of revising ASA 810 in September 2016, the AUASB agreed to revise GS 001 on the basis that even though concise reports were not used widely in Australia, they were still prepared and accordingly we need to retain guidance on this specific area of the Corporations Act.

## Matters to Consider

### *Part A – General*

Key areas of change in the revision to GS 001 for the AUASB to consider:

1. Modifications to the Opinion, Emphasis of Matter Paragraph, Other Matter Paragraph and Material Uncertainty Related to Going Concern Section: paragraph 35
2. KAM: paragraphs 38-39
3. Other Information: paragraphs 40-45
4. Illustrative auditor's reports: illustrative examples 1-4

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*This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.*

**Part B – NZAuASB**

1. N/A

**Part C – “Compelling Reasons” Assessment**

1. N/A

**AUASB Technical Group Recommendations**

1. N/A – objective is to receive input into the draft.

**Material Presented**

Agenda Item 4	AUASB Board Meeting Summary Paper
Agenda Item 4.1	Project Plan GS 001
Agenda Item .4.2	GS 001 <i>Concise Financial Reports under the Corporations Act 2001</i> (mark up)
Agenda Item .4.3	GS 001 <i>Concise Financial Reports under the Corporations Act 2001</i> (clean)

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**Action Required**

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	Input	Input	AUASB	29 November 2016	

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# Project Plan

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<b>Project Title:</b>	Revision of GS 001 <i>Concise Financial Reports Under the Corporations Act 2001</i>
<b>Project ID:</b>	2016
<b>Project Objective(s):</b>	To revise GS 001 <i>Concise Financial Reports Under the Corporations Act 2001</i> to take into account the changes to ASA 810 Engagements to Report on Summary Financial Statements arising from the new suite of auditor reporting standards
<b>Priority:</b>	Medium
<b>Issue/Reason:</b>	The revision of GS 001 is required to reflect the changes to ASA 810 arising from recent enhancements to auditor reporting developed by the International Auditing and Assurance Standards Board.
<b>Date Prepared:</b>	14 November 2016
<b>Date To Be Approved:</b>	29 November 2016
<b>Date Updated: (if applicable)</b>	

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## Project Objectives

To revise GS 001 *Concise Financial Reports Under the Corporations Act 2001* to take into account the changes to ASA 810 *Engagements to Report on Summary Financial Statements* arising from the new suite of auditor reporting standards.

## Stakeholders

1. Auditors of Concise Financial Reports
2. Relevant regulatory bodies:
  - (i) Australian Securities and Investment Commission (ASIC)
3. Accounting bodies – ICAA, CPA Australia & IPA – representing practitioners.

## Background

GS 001 was first issued in 2007, revised in 2008 and again in 2010. At the time of revising ASA 810 in September 2016, the AUASB agreed to revise GS 001 on the basis that even though concise reports were not used widely in Australia, they were still prepared and accordingly we need to retain guidance on this specific area of the Corporations Act.

## **Scope**

To revise the guidance statement that provides guidance to auditors reporting on a concise financial report prepared under the *Corporations Act 2001* and in accordance with accounting standard AASB 1039 *Concise Financial Reports*.

## **Risks/Issues**

To ensure that the changes to GS 001 are minimised so that no unnecessary costs are incurred by practitioners in modifying the engagement approach to address any amendments

## **Action Plan**

1. Develop a project plan and obtain AUASB approval
1. Revise guidance statement in light of the project objectives.
2. Obtain OBPR clearance
3. Obtain AUASB approval for revised GS 001
4. Issue GS 001

## **Resources**

1 Senior Project Manager

## **Timing**

29 November AUASB meeting: Project Plan approval and Review and Input into First Draft

Jan/Feb 2017: Further revisions to draft/OBPR clearance

March 2017 AUASB meeting: Review and Approve Final Draft

March 2017: Issue GS 001

## Timetable

Date	Description
25 October 2016	Present Project Plan and obtain AUASB approval
October 2016	Research amendments to GS 001
	Revise GS 001 and prepare 1 <sup>st</sup> draft
29 November 2016	AUASB Meeting – present 1 <sup>st</sup> draft GS 001 for consideration
December/January 2016	Further revisions of GS 001
	QA GS 001
	Obtain OBPR clearance
February 2017	AUASB Meeting – present 2nd draft GS 001 for review and approval

**GS 001**  
(November 2016)

# **Guidance Statement GS 001**

## ***Concise Financial Reports Under the Corporations Act 2001***

Issued by the **Auditing and Assurance Standards Board**



**Australian Government**  
**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Guidance Statement**

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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*Important Note*

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement *Concise Financial Reports Under the Corporations Act 2001* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

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Appendix 1: Illustrative Examples of the Auditor's Report on a Concise Financial Report

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 001 *Concise Financial Reports Under the Corporations Act 2001* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

This Guidance Statement provides guidance to assist the auditor to fulfil the objectives of the audit or assurance engagement. It includes explanatory material on specific matters for the purposes of understanding and complying with AUASB Standards. The auditor exercises professional judgement when using this Guidance Statement.

This Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

M H Kelsall  
Chairman - AUASB

## GUIDANCE STATEMENT GS 001

### *Concise Financial Reports Under the Corporations Act 2001*

#### Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors reporting on a concise financial report prepared under the *Corporations Act 2001* ("the Act") and in accordance with Accounting Standard AASB 1039 *Concise Financial Reports* (as amended ~~June 2009~~ [April 2015](#)) (AASB 1039).
2. For audits of other concise financial reports, the auditor complies with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.
3. This Guidance Statement should be used when an auditor conducts an audit under the Australian Auditing Standards .

#### Issuance Date

4. This Guidance Statement is issued on 1 February 2017 by the AUASB and replaces GS 001-*Concise Financial Reports Under the Corporations Act 2001*, issued in March 2010.

#### Introduction

5. The auditor's objective in respect of a concise financial report prepared under the Act, is to express an opinion:
  - (a) whether the concise financial report complies with AASB 1039; and
  - (b) when included, whether the discussion and analysis complies with the requirements of AASB 1039.

#### Regulatory Requirements

6. The annual financial reporting requirements of a company, registered scheme and disclosing entity are found in section 314(1) of the Act.
7. Section 314(2) of the Act states:

A concise report for a financial year consists of:

  - (a) a concise financial report for the year drawn up in accordance with accounting standards made for the purpose of this paragraph; and
  - (b) the directors' report for the year (see sections 298-300A); and
  - (c) a statement by the auditor:
    - (i) that the financial report has been audited; and
    - (ii) whether, in the auditor's opinion, the concise financial report complies with the accounting standards made for the purpose of paragraph (a); and
  - (d) a copy of any qualification in, and of any statements included in the emphasis of matter section of, the auditor's report on the financial report; and
  - (e) a statement that the report is a concise report and that the full financial report and auditor's report will be sent to the member free of charge if the member asks for them.

8. Section 314 of the Act does not require a concise report to include the directors' declaration made under section 295(4) of the Act in respect of the (full) financial report for the year. Consequently, where the directors of an entity decide to include the directors' declaration as part of the concise report, the auditor, under *ASA 720 The Auditor's Responsibilities Relating to Other Information in Documents Containing an Audited Financial Report*, needs to read the declaration, along with other documents comprising the concise report, to identify material inconsistencies with the concise financial report and material misstatements of fact.
9. Section 314(3) of the Act requires the auditor to report on whether the discussion and analysis, if required by the Accounting Standard to be included in the concise financial report<sup>1</sup>, complies with the requirements laid down by the Accounting Standard. Furthermore, section 314(3)(b) specifies that the auditor need not otherwise audit the statements made in the discussion and analysis.
10. The requirements of the Act relating to concise financial reports are based on the view that a concise financial report can provide members with information relevant to evaluating the business, without giving them fully detailed accounting disclosures. The concise report will, in many cases, be the only report that is sent to members<sup>2</sup>. The provision, to some members, of less detailed information is expected to be sufficient to meet their needs for an understanding of the financial performance, financial position and financing and investing activities of the company, registered scheme or disclosing entity.

#### Accounting Standard AASB 1039

11. The Australian Accounting Standards Board issued Accounting Standard AASB 1039 *Concise Financial Reports*, the latest revision of which, dated ~~June 2009~~ April 2015, is operative for financial reporting periods beginning on or after 1 January 2009.

#### Discussion and Analysis

12. The Accounting Standard, inter alia, specifies the minimum content of a concise financial report, including a requirement that the financial statements forming part of the concise financial report, other than those of a listed company, be accompanied by discussion and analysis to assist the understanding of members.
13. AASB 1039 adopts the view that the information reported in the financial statements forming part of the concise financial report will be enhanced by discussion and analysis of the principal factors which affect the financial performance, financial position and financing and investing activities of an entity. According to AASB 1039, the extent of discussion and analysis which is required to be provided in concise financial reports will vary from entity to entity, and from year to year, as is necessary in the circumstances to compensate for the brevity of the concise financial report, compared with the (full) financial report for the year.
14. AASB 1039 does not require the financial statements, forming part of the concise financial report of listed companies, to be accompanied by discussion and analysis. This is so as to avoid repetition of information required to be included in the directors' report by section 299A of the Act.
15. Whilst AASB 1039 does not mandate specific discussion and analysis disclosures, paragraph 27 of the Standard provides examples of the types of disclosures that may, at least, be expected to accompany the financial statements.

---

<sup>1</sup> *Discussion and analysis* are not required for listed companies – see AASB 1039 paragraph 24. This is because, unlike other entities, listed companies are required by section 299A of the Act to provide an operational and financial report in the directors' report (which is included in the concise report).

<sup>2</sup> Unless members request a copy of the full financial report (annual financial report) – see section 314(2)(e) of the Act.

## Materiality

- ~~16.~~ AASB 1039 paragraph 5 specifies that the requirements in AASB 1039 are subject to the requirements of AASB 1031 *Materiality*.

## Audit Activities

### Engagement Acceptance

- ~~17.~~16. Given that the concise financial report is an alternative form of reporting to members under the Act, and that the Act prescribes the auditor's reporting requirements, the AUASB takes the view that the audit of the concise financial report is treated, by auditors, as a separate engagement from the audit of the (full) financial report for the year. This view has been taken also because procedures, additional to those performed on the (full) financial report for the year, will be necessary when undertaking the audit of the concise financial report, particularly given that AASB 1039 requires, in certain circumstances, the inclusion of other information not found in the (full) financial report for the year, such as discussion and analysis.
- ~~18.~~17. In order to avoid any misunderstandings in relation to the audit of the concise financial report, the auditor complies with the engagement acceptance requirements in *ASA 810 Engagements to Report on Summary Financial Statements*. The auditor agrees the terms of the audit engagement with the appropriate person(s) within the entity's governance structure. The prudent auditor records the terms of engagement in writing and obtains written acceptance from the appropriate person representing the entity. These terms may be included in the written terms of the audit engagement for the (full) financial report. On recurring audits, the terms of the engagement are revised and re-confirmed as appropriate
- ~~19.~~18. In addition to the specific requirements in ASA 810, the terms of engagement ordinarily include the objective and scope of the audit of the concise financial report (including the audit of discussion and analysis disclosures in that report). Such inclusions differentiate the engagement to audit the concise report from the engagement to audit the (full) financial report.

### Audit Procedures

#### *Auditing Standards*

- ~~20.~~19. AASB 1039 requires the concise financial report to be derived from the (full) financial report for the year and each financial statement to be presented as it is in the (full) financial report for the year. Consequently, the audit procedures performed under the Auditing Standards by the auditor when auditing the (full) financial report for the year are effectively performed on that information in the concise financial report that has been derived from the (full) financial report for the year. Accordingly, there is no expectation that such audit procedures need be repeated on the relevant information in the concise financial report.
- ~~21.~~20. Reference to "audit" and "audit procedures" in the illustrative examples of an auditor's report on the concise financial report (see Appendix 1) relate to all procedures that have been performed by the auditor (i.e. regarding both the (full) financial report and the concise financial report).
- ~~22.~~21. When selecting and applying procedures in addition to those performed in relation to the (full) financial report for the year, the auditor complies with ASA 810.
- ~~23.~~22. Under ASA 810, paragraph 8, the auditor is required to perform specified procedures. Furthermore, the auditor is required to perform additional procedures that the auditor considers necessary as the basis for the auditor's opinion (on the concise financial report), for example, procedures addressing discussion and analysis.

*Discussion and Analysis*

- | ~~24-23.~~ As the inclusion of discussion and analysis is not required in the (full) financial report for the year of some entities reporting under the Act, the audit of a concise financial report will include procedures to enable the auditor to reach a conclusion on the discussion and analysis, as part of forming an opinion on the concise financial report.
- | ~~25-24.~~ These procedures may include, a recalculation of ratios and/or trend analyses which have been included in the discussion and analysis; and ensuring that these disclosures are consistent with the information in the (full) financial report for the year.
- | ~~26-25.~~ Whilst AASB 1039 requires that the financial statements and the specific disclosures in a concise financial report be consistent with the (full) financial report for the year of the entity, it is recognised that because of the nature of discussion and analysis, such information (for example, a discussion and analysis of the main influences on the costs of the operations of the entity) goes beyond the type of disclosure which is included normally in the audited (full) financial report for the year.
- | ~~27-26.~~ In such circumstances, the auditor selects and applies appropriate procedures to be able to reach a conclusion on the discussion and analysis and evaluates the results of such procedures when forming an opinion on whether the discussion and analysis complies with the requirements of AASB 1039. In selecting and applying procedures and evaluating results, the auditor exercises professional judgement in accordance with *ASA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.
- | ~~28-27.~~ Where information of a subjective and/or prospective nature is included in the discussion and analysis, either to comment on, or to augment the entity's financial statements forming part of the concise financial report (for example, a discussion of the impact of significant economic or other events on the operations of the entity), the auditor assesses whether the inclusion of such information in the audited concise financial report has the potential to mislead users.
- | ~~29-28.~~ Under ASA 200, the auditor exercises professional judgement in assessing the inclusion of such information in the discussion and analysis. If the auditor considers that this information is overly subjective and/or prospective in nature, and/or that it is information which cannot be quantified or verified, then the auditor refers to Auditing Standard *ASA 705 Modifications to the Opinion in the Independent Auditor's Report*, for requirements and guidance on modifying the auditor's report. Depending on the circumstances, the modification to the auditor's report may be as a result of a disagreement with the directors (those charged with governance) on the adequacy or appropriateness of disclosures in the concise financial report or may be as a result of a limitation in scope.
- | ~~30-29.~~ In view of the matters discussed above, it is generally important that the auditor ascertains from the directors (those charged with governance), at an early stage in the audit, the extent and nature of the discussion and analysis that they intend to include in the concise financial report.
- | ~~31-30.~~ In ascertaining the extent and nature of the discussion and analysis at an early stage the auditor seeks to avert any difficulties which might otherwise arise with regard to the inclusion of such information. The directors (those charged with governance) are thus informed at that stage if, in the auditor's opinion, there is any possibility that users of the concise financial report might be misled by the inclusion of overly subjective and/or prospective terminology and information in the discussion and analysis which forms part of the concise financial report.

*Representations*

- | ~~32-31.~~ Given that the Act does not require a directors' declaration to be included in the concise report, prior to issuing the auditor's report, it would be prudent for the auditor, under *ASA 580 Written Representations*, to obtain a written representation from the entity's directors which

attests that the concise financial report (including, when applicable, discussion and analysis disclosures) complies with the requirements of AASB 1039 and the Act.

### The Auditor's Report

~~33.~~32. When reporting on a concise financial report, the auditor complies with the Act and ASA 810. As section 314 of the Act prescribes the auditor's reporting obligations, the auditor adheres to the requirements in ASA 810, paragraph 10 in respect of the prescribed reporting obligations.

~~34.~~33. Under ASA 810, paragraph 10(b), the auditor evaluates whether the users of a concise financial report might misunderstand the auditor's opinion. Due to the precision of wording recommended in this Guidance Statement; and the requirements of the Act, an auditor ordinarily concludes that users will not misunderstand the auditor's opinion.

~~35.~~34. ASA 810, paragraph ~~44~~16 lists the elements required to be included in an auditor's report.

*Modifications to the Opinion, Emphasis of Matter Paragraph, ~~and~~ Other Matter Paragraph and Material Uncertainty Related to Going Concern Section*

~~35.~~ Under ASA 810, paragraph ~~47~~19, where the auditor's report on the (full) financial report includes a qualified opinion, an emphasis of matter or other matter paragraph or a material uncertainty related to going concern, all modifications to the auditor's report on the (full) financial report are to be included in the auditor's report on the concise financial report. The form of inclusion is dependent on whether the modification to the opinion, emphasis of matter paragraph or other matter paragraph contained in the auditor's report on the (full) financial report is applicable, or not applicable, to the concise financial report the auditor's report on the concise financial report states that. In addition the auditor's report on the concise financial report describes:

(a) the basis for the qualified opinion on the (full) financial report, and the effect thereof on the concise financial report;

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~~36.~~(b) the matter referred to in the emphasis of matter or other matter paragraph or the material uncertainty related to going concern section in the (full) financial report, and the effect thereof on the concise financial report.

~~37.~~36. Examples:

- (a) AASB 1039 requires the concise financial report to be derived from, and consistent with, the (full) financial report for the year. Accordingly, modifications to the auditor's opinion on the (full) financial report for the year will commonly be applicable to the auditor's opinion on the concise financial report. Certain modifications to the auditor's opinion on the (full) financial report for the year, however, may not be applicable to the auditor's opinion on the concise financial report, such as those relating solely to disclosures in the notes to the (full) financial report for the year.
- (b) The auditor may modify the auditor's report relating to the concise financial report only. An example is when an auditor is of the opinion that the discussion and analysis does not comply with the requirements of AASB 1039.

~~38.~~37. Where the auditor's report on the (full) financial report contains an adverse or disclaimer of opinion, the auditor's report on the concise financial report must, under ASA 810, paragraph ~~48~~20:

- (a) state that the auditor's report on the ~~audited financial report~~(full) financial report contains an adverse opinion or disclaimer of opinion;
- (b) describe the basis for that adverse opinion or disclaimer of opinion; and

- (c) state that, as a result of the adverse opinion or disclaimer of opinion, it is inappropriate to express an opinion on the concise financial report.

Key Audit Matters

38. Where an auditor's report on the (full) financial report includes communication of key audit matters in accordance with ASA 701<sup>3</sup> and the auditor is satisfied that the concise financial report is materially consistent with the (full) financial report, the auditor's report on the concise financial report states that the auditor's report on the (full) financial report includes communication of key audit matters.
39. The auditor is not required to describe the individual key audit matters in the auditor's report on the concise financial report. However, the auditor, using professional judgement, may determine whether or not to include more detailed reference to key audit matters, either generically or specifically (ie by providing subheadings or descriptions). In making this determination, the auditor considers whether such inclusions are beneficial to the users understanding of the audit of the concise financial report, or whether such inclusions could be misleading if the underlying issues are not relevant to or disclosed in a similar manner in the concise financial report.

Other Information

40. Where an auditor's report on the (full) financial report includes a statement that describes an uncorrected material misstatement of the other information in accordance with ASA 720<sup>4</sup> and the auditor is satisfied that the concise financial report is materially consistent with the (full) financial report, the auditor's report on the concise financial report states that the auditor's report on the (full) financial report includes a statement that describes an uncorrected material misstatement of other information; and describes the uncorrected material misstatement of other information and the effect thereof, if any, on the information included in a document containing the concise financial report.
41. A document that includes a concise financial report may contain some or all of the same matters dealt with in the other information included in the audited annual report or may include matters that are not dealt with in the other information included in the annual report.
42. The auditor reads the information included in a document containing the concise financial report, and considers whether there is a material inconsistency between that information and the concise financial report. Where a material inconsistency is identified, the auditor discusses the inconsistency with management and determines what revisions are required and considers the implications, if any, on the auditor's report on the concise financial report.
43. Where information is included in a document that includes a concise financial report and that information deals with some or all of the matters as the other information in the annual report, the work already performed on that other information in accordance with ASA 720 may be sufficient.
44. When an uncorrected material misstatement of the other information has been identified in the auditor's report on the (full) financial report and that uncorrected material misstatement relates to a matter that is dealt with in the information in a document containing the concise financial report, a material inconsistency between the concise financial report and that information may exist or the information may be misleading. The auditor discusses the inconsistency with management and determines what revisions are required and considers the implications, if any, on the auditor's report on the concise financial report.

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<sup>3</sup> See ASA 701 Key Audit Matters.

<sup>4</sup> See ASA 720 The Auditor's Responsibilities Relating to Other Information.

45. Where information is included in a document that includes a concise financial report and that information deals with matters not dealt with in other information in the annual report, the auditor may still find ASA 720 helpful and follows the guidance contained in paragraph 42 of this guidance statement.

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#### *Remuneration Report<sup>5</sup>*

39-46. Where a company includes a Remuneration Report in the annual directors' report, the auditor reports thereon to members. Whilst there is no legal requirement to do so, it is in the public interest that a copy of the auditor's report on the Remuneration Report is included with the auditor's report on the concise financial report.

#### *Illustrative Examples*

40. The illustrative reports in Appendix 1 provide examples of an auditor's report on a concise financial report covering:

- an unmodified opinion;
- modified opinions; and
- an Emphasis of Matter paragraph.

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### **Conformity with International Pronouncements**

41-48. As this Guidance Statement relates to Australian legislative requirements under the Act, there is no equivalent International Standard on Auditing or International Auditing Practice Statement to this Guidance Statement.

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<sup>5</sup> See Guidance Statement GS 008 *The Auditor's Report on a Remuneration Report Pursuant to Under Section 300A of the Corporations Act 2001*.

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## Appendix 1

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### ILLUSTRATIVE EXAMPLES OF THE AUDITOR'S REPORT ON A CONCISE FINANCIAL REPORT

#### Introduction

##### A. Examples Provided in this Appendix

Consideration of the examples in this Appendix is as follows:

- (a) Illustration 1: Unmodified report—consider Example 1. Concise financial report derived from a (full) financial report of an *unlisted entity* where the auditor's report thereon includes a *material uncertainty related to going concern*.
- (b) Illustration 2: Modified report—qualification on (full) financial report that does not affect the opinion on the concise financial report—consider Example 2. Concise financial report derived from a (full) financial report of a *listed entity* where the auditor's report thereon includes a *material uncertainty related to going concern and key audit matters*.
- (c) Modified report—qualification on either:
  - (i) the concise financial report only; or
  - (ii) both the (full) financial report and the concise financial report—i.e. qualification on (full) financial report that *does* affect the opinion on the concise financial report—consider Example 3.
- (d) Modified report—Emphasis of Matter Paragraph relating to either:
  - (i) the concise financial report only; or
  - (ii) both the (full) financial report for the year and the concise financial report—consider Example 4.
- Note: Wording used in an auditor's report to describe an auditor's responsibilities will differ according to the circumstances described above.
- (b) A schematic of these illustrative examples is provided at paragraph E. below.
- (c) Illustration 3: Concise financial report derived from a (full) financial report of a *listed entity* where the *auditor's report is qualified* but the *qualification does not affect the auditor's opinion on the concise financial report*.
- (d) Illustration 4: Concise financial report derived from a (full) financial report of an *unlisted entity* where the *auditor's report thereon includes a material uncertainty related to going concern and the auditor's opinion on the concise financial report is qualified*.

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**B.** *Form of Reporting*

AASB 1039 does not specify whether a concise financial report prepared under section 314 of the Act is a “general purpose financial report” within the meaning described in Accounting Standard AASB 101 *Presentation of Financial Statements*. The auditor’s reporting obligations, under section 314, require an opinion on compliance (with AASB 1039), not an expression of opinion on the fair presentation of the financial information. Accordingly, the illustrative example auditor’s reports, contained within this Appendix, are not developed from a classification (general purpose or special purpose) of the concise financial report and are not based on the expression of an opinion on fair presentation.

Instead, the illustrative example auditor’s reports contained within this Appendix are discrete and have been developed from:

- (a) the auditor’s reporting obligations specified in the Act;
- (b) the reporting requirements under ASA 810;
- (c) the principles of auditor’s reporting found in Auditing Standard ASA 700 *Forming an Opinion and Reporting on a Financial Report* in relation to a compliance financial reporting framework;
- (d) consideration of the nature of concise reports, including concise financial reports, prepared under the Act and AASB 1039; and
- (e) recognition of the relationship, prescribed in AASB 1039, of a concise financial report to the audited (full) financial report for the year.

It should be noted that as AASB 1039 does not require parent entity information to be separately disclosed when consolidated financial information is presented in concise financial reports, separate references to the parent entity and consolidated entity are therefore not required in the auditor’s report on a concise financial report.

**C.** *Qualifications*

Section 314(2)(d) of the Act specifies that — “a copy of any qualification in, and of any statements included in the emphasis of matter section of, the auditor’s report on the financial report”—is to be included in a concise report.

At the time section 314 was introduced into the Act, the word “qualification” was a generic term and had the same meaning and expression as used in the then Auditing Standards (AUSs) issued by the former Auditing and Assurance Standards Board (AuASB) of the Australian Accounting Research Foundation. Specifically, AUS 702.25(b) stated that a “qualified” opinion should be expressed as:

- (a) an “except for” opinion;
- (b) an adverse opinion; or
- (c) an inability to form an opinion.

However, under the current Auditing Standard (ASA 705), the term “qualified” has a specific and different meaning—it refers only to an “except for” type modification to the auditor’s opinion. The terminology used in this Guidance Statement is consistent with ASA 705.

The meaning of the term Emphasis of Matter Paragraph does not differ between the Act, the AUSs, the ASAs and this Guidance Statement.

The term “Other Matter Paragraph” has been introduced to the Australian Auditing Standards applicable for financial reporting periods commencing on or after 1 January 2010. Accordingly, the term is not used in the Act but its use has no consequence under the Act.

The term “Material Uncertainty Related to Going Concern” has been introduced to the Australian Auditing Standards applicable for financial reporting periods commencing on or after 15 December 2016. Accordingly, the term is not used in the Act but its use has no consequence under the Act as it does not result in a qualification to the auditor’s report.

The use of differing terminology between the Act and this Guidance Statement, as described above, does not mean that the requirements of section 314 of the Act have changed in so far that only “except for” type modifications are included in a concise report. The requirements of the Act remain unchanged and the term “qualification” in the Act covers all three types of modification to the auditor’s opinion listed above, regardless of how they may be described in this Guidance Statement (or the Auditing Standards).

**D. *Directors’ Obligations under the Act***

This Guidance Statement, including the illustrative auditor’s reports, is prepared to provide guidance to the auditor reporting on a concise financial report prepared under the *Corporations Act 2001*. It is not prepared to provide guidance to directors on their obligations under the Act, especially regarding section 314(2)(d) that requires a copy of any qualification and/or emphasis of matter [from the auditor’s report on the (full) financial report] to be included in the “concise report”.

See “Important Notes” at Example 3 with respect to “appropriately restating” a qualification.

E. Illustrative Auditor's Report

**Illustration 1:**

Circumstances include the following:

- An unmodified opinion is expressed on the (full) financial report of an entity other than a listed entity.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the (full) financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the (full) financial report was not required to communicate key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Opinion**

We have audited the concise financial report of ABC Company which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1 and the discussion and analysis.

In our opinion, the accompanying concise financial report, including the discussion and analysis of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- A Material Uncertainty Related to Going Concern section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, in all material respects, complies with AASB 1039 *Concise Financial Reports* and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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<sup>†</sup> Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the audited financial report for the year.

<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

### **Illustration 2:**

Circumstances include the following:

- An unmodified opinion is expressed on the audited financial report of a listed entity.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the audited financial report includes key audit matters in accordance with ASA 701.

### **Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

#### **Opinion**

We have audited the concise financial report of ABC Company, which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1<sup>§</sup>.

In our opinion, the accompanying concise financial report of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

#### **Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report<sup>\*</sup>.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>§</sup> As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented. Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

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## **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

## **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- A *Material Uncertainty Related to Going Concern* section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.
- The communication of other\* key audit matters. [Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period.]#

## **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

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## **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, complies in all material respects, with AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

## **Report on Other Legal and Regulatory Requirements†**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

## **Report on the Remuneration Report**

The following paragraphs are copies from our Report on the Remuneration Report for the [period] ended 31 December 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 31 December 20X1.]

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\* In the circumstances where there is no material uncertainty related to going concern, inclusion of the word "other" in the statement for the communication of key audit matters would not be necessary.

# The auditor may include additional explanation about key audit matters considered helpful to users of the auditor's report on the concise financial report.

† Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

[\[Auditor's name and signature<sup>§</sup>\]](#)

[\[Auditor's address\]](#)

[\[Date of the auditor's report\]](#)

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<sup>§</sup> [The auditor is required, under the \*Corporations Act 2001\*, to sign the auditor's report in both their own name and the name of their firm \[section 324AB\(3\)\] or the name of the audit company \[section 324AD\(1\)\], as applicable.](#)

### **Illustration 3:**

Circumstances include the following:

- A modified opinion is expressed on the audited financial report of a listed entity that does not affect the auditor's opinion on the concise financial report.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes key audit matters in accordance with ASA 701.

### **Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

#### **Opinion**

We have audited the concise financial report of ABC Company, which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1<sup>§</sup>. We expressed a qualified opinion on the audited financial report. The modification, included below does not qualify our opinion on the concise financial report<sup>‡</sup> because [insert reason(s)].

In our opinion, the accompanying concise financial report of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

#### **Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>§</sup> As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>‡</sup> An example of a modification to the (full) financial report for the year that does not affect the concise financial report is a qualification ("except for") on disclosures in the notes to the financial statements where no such notes are included in the concise financial report. A copy of the modification paragraphs are included in a section of this auditor's report and is clearly identified as not affecting the auditor's opinion on the concise financial report.

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We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report<sup>\*</sup>.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed a qualified audit opinion on the audited financial report in our report dated 15 February 20X2. The following paragraphs are copied from our report on the financial report for the year. The modification to the opinion in that report does not apply to our opinion on the concise financial report for the reason(s) stated above. [Insert the exact wording, including headings, of the basis of modification paragraph(s) and the modified opinion paragraph from the auditor's report on the financial report for the year.]

That report also includes:

- The communication of other<sup>\*</sup> key audit matters. [Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period.]<sup>#</sup>

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

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### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, complies in all material respects, with AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

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<sup>\*</sup> Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

<sup>#</sup> In the circumstances where there is no material uncertainty related to going concern, inclusion of the word "other" in the statement for the communication of key audit matters would not be necessary.

<sup>†</sup> The auditor may include additional explanation about key audit matters considered helpful to users of the auditor's report on the concise financial report.

<sup>†</sup> Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

### **Report on the Remuneration Report**

The following paragraphs are copies from our Report on the Remuneration Report for the [period] ended 31 December 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 31 December 20X1.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

**Illustration 4:**

Circumstances include the following:

- An unmodified opinion is expressed on the audited financial report of an entity other than a listed entity however, a qualified opinion is expressed on the concise financial report.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the audited financial report was not required to communicate key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Qualified Opinion**

We have audited the concise financial report of ABC Company which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1 and the discussion and analysis.

In our opinion, except for the effect on the concise financial report of the matter(s) referred to in the paragraph below, the accompanying concise financial report, including the discussion and analysis of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Qualified Opinion**

[Include a clear description of all the substantive reasons for the qualification and quantification of the effects.]<sup>†</sup>

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>†</sup> The qualification effects the opinion on the concise financial report ONLY – for example, a qualification on the discussion and analysis.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- A Material Uncertainty Related to Going Concern section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, in all material respects, complies with AASB 1039 *Concise Financial Reports* and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

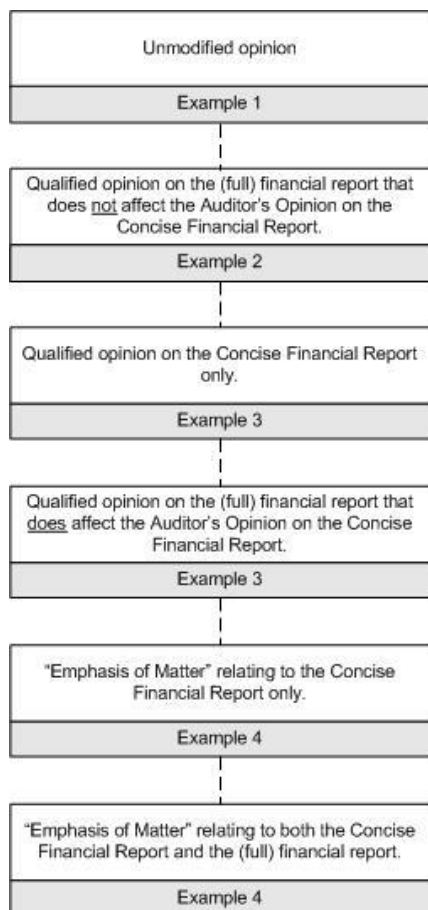
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\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

<sup>†</sup> Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the audited financial report for the year.

<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

*Schematic of Illustrative Examples*



**[HD5]Example 1: Unmodified Report  
Unmodified Auditor's Report on a Concise Financial Report prepared under section 314 of the  
Corporations Act 2001.**

**INDEPENDENT AUDITOR'S REPORT**

To the members of [name of entity]:

**Report on the Concise Financial Report<sup>6</sup>**

We have audited the accompanying concise financial report of [name of entity] which comprises the statement of financial position as at

30 June 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>7</sup> for the year then ended, and related notes, derived from the audited financial report of [name of entity] for the year ended 30 June 20X1 [and the discussion and analysis<sup>8,9</sup>]. The concise financial report does not contain all the disclosures required by the Australian Accounting Standards and accordingly, reading the concise financial report is not a substitute for reading the audited financial report.

**Directors<sup>10</sup> Responsibility for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine are necessary to enable the preparation of the concise financial report.

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<sup>6</sup>—The subheading “Report on the Concise Financial Report” is unnecessary in circumstances when the subheadings “Report on Other Legal and Regulatory Requirements” and “Report on the Remuneration Report” are not applicable.

<sup>7</sup>—The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports* applicable for annual reporting periods beginning on or after 1 January 2009. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>8</sup>—A discussion and analysis is not required for listed companies due to their section 299A reporting requirement (AASB 1039 paragraph 24-25).

<sup>9</sup>—As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>10</sup>—Alternatively, insert the title of those charged with governance.

#### Auditor's Responsibility

~~Our responsibility is to express an opinion on the concise financial report based on our procedures which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*. We have conducted an independent audit, in accordance with Australian Auditing Standards, of the financial report of [name of entity] for the year ended 30 June 20X1. We expressed an unmodified audit opinion on that financial report in our report dated [date]. The Australian Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report for the year is free from material misstatement.~~

~~An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the concise financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the concise financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the concise financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our procedures included testing that the information in the concise financial report is derived from, and is consistent with, the financial report for the year, and examination on a test basis, of audit evidence supporting the amounts [, discussion and analysis,] and other disclosures which were not directly derived from the financial report for the year. These procedures have been undertaken to form an opinion whether, in all material respects, the concise financial report complies with AASB-1039 *Concise Financial Reports* [and whether the discussion and analysis complies with the requirements laid down in AASB-1039 *Concise Financial Reports*]<sup>++</sup>. [The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial report.]<sup>\*</sup> We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.~~

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<sup>++</sup>—Include when a discussion and analysis is required (i.e. other than listed companies)—AASB-1039 paragraph 24.

<sup>\*</sup>—Include if the date of the auditor's report on the concise financial report is later than the date of the auditor's report on the audited financial report.

**Independence**

~~In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of [name of entity] would be in the same terms if given to the directors as at the time of this auditor's report.<sup>\*</sup>~~

**Opinion**

~~In our opinion, the concise financial report [, including the discussion and analysis<sup>12</sup>] of [name of entity] for the year ended 30 June 20X1 complies with Accounting Standard AASB 1039 *Concise Financial Reports*.~~

**Report on Other Legal and Regulatory Requirements<sup>13</sup>**

~~[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]~~

**Report on the Remuneration Report<sup>14</sup>**

~~The following paragraphs are copied from our Report on the Remuneration Report for the [period] ended 30 June 20X1.~~

~~[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 30 June 20X1.]~~

~~[Auditor's signature]<sup>15</sup>~~

~~[Date of the auditor's report]~~

~~[Auditor's address]~~

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<sup>\*</sup>—Or, alternatively, include statements: (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made.

<sup>12</sup>—Include when a discussion and analysis has been included in the concise financial report.

<sup>13</sup>—Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

<sup>14</sup>—Include only when an auditor's Report on the Remuneration Report has been included with the auditor's report on the (full) financial report.

<sup>15</sup>—The auditor's report needs to be signed in one or more of the following ways: the name of the audit firm, the name of the audit company or the personal name of the auditor as appropriate.

**Example 2: Modified Report**

~~Unmodified Auditor's Opinion on a Concise Financial Report prepared under section 314 of the Corporations Act 2001—Qualified Auditor's Opinion on the (full) financial report for the year that does not affect the Auditor's Opinion on the Concise Financial Report.~~

~~INDEPENDENT AUDITOR'S REPORT~~

~~To the members of [name of entity]:~~

~~**Report on the Concise Financial Report**~~<sup>16</sup>

~~We have audited the accompanying concise financial report of [name of entity] which comprises the statement of financial position as at 30 June 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>17</sup> for the year then ended, and related notes, derived from the audited financial report of [name of entity] for the year ended 30 June 20X1 [and the discussion and analysis<sup>18,19</sup>]. The concise financial report does not contain all the disclosures required by the Australian Accounting Standards and accordingly, reading the concise financial report is not a substitute for reading the audited financial report.~~

~~Directors<sup>20</sup> Responsibility for the Concise Financial Report~~

~~The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001* and for such internal control as the directors determine are necessary to enable the preparation of the concise financial report.~~

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<sup>16</sup>—The subheading “Report on the Concise Financial Report” is unnecessary in circumstances when the subheadings “Report on Other Legal and Regulatory Requirements”, “Modification to the Auditor's Report on the Financial Report for the Year” and “Report on the Remuneration Report” are not applicable.

<sup>17</sup>—The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports* applicable for annual reporting periods beginning on or after 1 January 2009. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>18</sup>—A discussion and analysis is not required for listed companies due to their section 299A reporting requirement (see AASB 1039, paragraph 24–25).

<sup>19</sup>—As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>20</sup>—Alternatively, insert the title of those charged with governance.

## Auditor's Responsibility

Our responsibility is to express an opinion on the concise financial report based on our procedures which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*. We have conducted an independent audit, in accordance with Australian Auditing Standards, of the financial report of [name of entity] for the year ended 30 June 20X1. We expressed a modified audit opinion on that financial report in our report dated [date]. The modification, stated below does not qualify our opinion on the concise financial report<sup>21</sup> because [insert reason(s)]. The Australian Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report for the year is free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the concise financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the concise financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the concise financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our procedures included testing that the information in the concise financial report is derived from, and is consistent with, the financial report for the year, and examination on a test basis, of audit evidence supporting the amounts [ , discussion and analysis, ] and other disclosures which were not directly derived from the financial report for the year. These procedures have been undertaken to form an opinion whether, in all material respects, the concise financial report complies with Accounting Standard AASB 1039 *Concise Financial Reports* [and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports*]<sup>22</sup>.

[The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial report.]<sup>\*</sup> We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of [name of entity] would be in the same terms if given to the directors as at the time of this auditor's report.<sup>\*</sup>

## Opinion

In our opinion, the concise financial report [ , including the discussion and analysis<sup>23</sup> ] of [name of entity] for the year ended 30 June 20X1 complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

## Report on Other Legal and Regulatory Requirements<sup>24</sup>

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

## Modification to the Auditor's Report on the Financial Report for the Year

The following paragraphs are copied from our report on the financial report for the year. The modification to the opinion in that report does not apply to our opinion on the Concise Financial Report for the reason(s) stated above.

[Insert the exact wording, including headings, of the basis of modification paragraph(s) and the modified opinion paragraph from the auditor's report on the financial report for the year.]

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<sup>21</sup>—An example of a modification to the (full) financial report for the year that does *not* affect the concise financial report is a qualification ("except for") on disclosures in the notes to the financial statements where no such notes are included in the concise financial report. A copy of the modification paragraphs are included in a section of this auditor's report that follows the opinion and is clearly identified as *not* affecting the auditor's opinion on the concise financial report.

<sup>22</sup>—Include when a discussion and analysis is required (i.e. other than listed companies) — see AASB 1039, paragraph 24.

<sup>\*</sup>—Include if the date of the auditor's report on the concise financial report is later than the date of the auditor's report on the audited financial report.

<sup>\*</sup>—Or, alternatively, include statements: (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made.

<sup>23</sup>—Include when a discussion and analysis has been included in the concise financial report.

<sup>24</sup>—Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

**Report on the Remuneration Report<sup>25</sup>**

The following paragraphs are copied from our Report on the Remuneration Report for the [period] ended 30 June 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 30 June 20X1.]

[Auditor's signature]<sup>26</sup>

[Date of the auditor's report]

[Auditor's address]

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<sup>25</sup>—Include only when an auditors Report on the Remuneration Report has been included with the auditor's report on the (full) financial report.

<sup>26</sup>—The auditor's report needs to be signed in one or more of the following ways: the name of the audit firm, the name of the audit company or the personal name of the auditor as appropriate.

**Example 3: Modified Report**

~~Modified Auditor's Opinion on a Concise Financial Report prepared under section 314 of the Corporations Act 2001—Qualified Auditor's Opinion ("Except for") relating to either: the Concise Financial Report only; or the (full) financial report and the Concise Financial Report—i.e. Qualified Auditor's Opinion on the (full) financial report for the year that does affect the Auditor's Opinion on the Concise Financial Report.~~

**IMPORTANT NOTES:**

1. ~~This example auditor's report (Example 3) illustrates a qualification affecting the opinion on the concise financial report only and a qualification on the (full) financial report for the year that affects the auditor's opinion on the concise financial report.~~
2. ~~Where a qualification on the (full) financial report for the year affects the auditor's opinion on the concise financial report, the following point is important:  
The primary obligation is for the auditor to opine on the concise financial report and accordingly it may not be appropriate to copy the exact wording of the basis for qualification paragraph from the auditor's report on the (full) financial report. For example, the basis for qualification paragraph on the (full) financial report may include reference to a note to the financial statements which note is not present in the concise financial report. In such circumstances, it will be necessary to "appropriately restate" the wording [from the basis for qualification paragraph on the (full) financial report] in the auditor's report on the concise financial report. Any such "restatement" must reflect the meaning of the basis for qualification on the (full) financial report.  
It is important to remember the qualification on the (full) financial report is the basis for qualifying the concise financial report; however, the wording of the qualification(s) may differ.~~

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## INDEPENDENT AUDITOR'S REPORT

To the members of [name of entity]:

### Report on the Concise Financial Report<sup>27</sup>

We have audited the accompanying concise financial report of [name of entity], which comprises the statement of financial position as at 30 June 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>28</sup> for the year then ended and related notes, derived from the audited financial report of [name of entity] for the year ended 30 June 20X1 [and the discussion and analysis<sup>29,30</sup>]. The concise financial report does not contain all the disclosures required by the Australian Accounting Standards and accordingly, reading the concise financial report is not a substitute for reading the audited financial report.

### Directors' Responsibility for the Concise Financial Report<sup>31</sup>

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001* and for such internal control as the directors determine are necessary to enable the preparation of the concise financial report.

### Auditor's Responsibility

Our responsibility is to express an opinion on the concise financial report based on our procedures which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*. We have conducted an independent audit, in accordance with Australian Auditing Standards, of the financial report of [name of entity] for the year ended 30 June 20X1. We expressed a modified audit opinion on that financial report in our report dated [date]. The modification affects our report on the concise financial report and is a modification to our opinion<sup>32</sup> on the concise financial report. The Australian Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report for the year is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the concise financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the concise financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the concise financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our procedures included testing that the information in the concise financial report is derived from and consistent with the financial report for the year, and examination on a test basis, of audit evidence supporting the amounts [, discussion and analysis,] and other disclosures which were not directly derived from the financial report for the year. These procedures have been undertaken to form an opinion whether, in all material respects, the concise financial report complies with Accounting Standard AASB 1039 *Concise Financial Reports* [and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports*]<sup>33</sup>.

[The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial report.]<sup>\*</sup>

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Independence

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<sup>27</sup>—The subheading "Report on the Concise Financial Report" is unnecessary in circumstances when the subheadings "Report on Other Legal and Regulatory Requirements" and "Report on the Remuneration Report" are not applicable.

<sup>28</sup>—The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports* applicable for annual reporting periods beginning on or after 1 January 2009. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>29</sup>—A discussion and analysis is not required for listed companies due to their section 299A reporting requirement (AASB 1039, paragraph 24-25).

<sup>30</sup>—As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>31</sup>—Alternatively, insert the title of those charged with governance.

<sup>32</sup>—An emphasis of matter is not a modification to the auditor's opinion—it is a modification to the auditor's report (see Example 4).

<sup>33</sup>—Include when a discussion and analysis is required (i.e. other than listed companies)—

AASB 1039, paragraph 24.

<sup>\*</sup>—Include if the date of the auditor's report on the concise financial report is later than the date of the auditor's report on the audited financial report.

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of [name of entity] would be in the same terms if given to the directors as at the time of this auditor's report.<sup>\*</sup>

**Basis for Qualified Opinion**

[Include a clear description of all the substantive reasons for the qualification and quantification of the effects.]<sup>34</sup>

[Copy exactly, or appropriately restate, the Basis for Qualified Opinion paragraph(s) from the auditor's report on the financial report for the year.] This basis for qualification to our opinion on the concise financial report is also a basis for qualification to our opinion on the financial report of (name of entity) for the year<sup>35</sup>.

**Qualified Opinion**

In our opinion, except for the effect on the concise financial report of the matter(s) referred to in the preceding paragraph(s), the concise financial report [, including the discussion and analysis<sup>36</sup>] of [name of entity] for the year ended 30 June 20X1 complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Report on Other Legal and Regulatory Requirements<sup>37</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

**Report on the Remuneration Report<sup>38</sup>**

The following paragraphs are copied from our Report on the Remuneration Report for the [period] ended 30 June 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 30 June 20X1.]

[Auditor's signature]<sup>39</sup>

[Date of the auditor's report]

[Auditor's address]

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<sup>\*</sup>—Or, alternatively, include statements: (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made.

<sup>34</sup>—The qualification affects the opinion on the concise financial report ONLY—for example, a qualification on the *discussion and analysis*.

<sup>35</sup>—Copy exactly or appropriately restate the wording from the basis for modification paragraph(s) from the auditor's report on the (full) financial report for the year that affects the opinion on the concise financial report. Ensure the modification is described as a copy or restatement of a qualification to the opinion on the financial report for the year.

<sup>36</sup>—Include when a discussion and analysis has been included in the concise financial report.

<sup>37</sup>—Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the financial report for the year.

<sup>38</sup>—Include only when an auditor's Report on the Remuneration Report has been included with the auditor's report on the (full) financial report.

<sup>39</sup>—The auditor's report needs to be signed in one or more of the following ways: the name of the audit firm, the name of the audit company or the personal name of the auditor as appropriate.

**Example 4: Modified Report**

**Modified Auditor's Report on a Concise Financial Report prepared under section 314 of the Corporations Act 2001—Emphasis of Matter Paragraph relating to either:**

**the Concise Financial Report only; or**

**both the (full) financial report for the year and the Concise Financial Report.**

**INDEPENDENT AUDITOR'S REPORT**

To the members of [name of entity]:

**Report on the Concise Financial Report<sup>40</sup>**

We have audited the accompanying concise financial report of [name of entity] which comprises the statement of financial position as at 30 June 20X1, the statement of comprehensive income, statement of changes in equity (or statement of recognised income and expenses), statement of cash flows<sup>41</sup> for the year then ended, and related notes, derived from the audited financial report of [name of entity] for the year ended 30 June 20X1 [and the discussion and analysis<sup>42,43</sup>]. The concise financial report does not contain all the disclosures required by the Australian Accounting Standards and accordingly, reading the concise financial report is not a substitute for reading the audited financial report.

**Directors' Responsibility for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001* and for such internal control as the directors determine are necessary to enable the preparation of the concise financial report.

**Auditor's Responsibility**

Our responsibility is to express an opinion on the concise financial report based on our procedures which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*. We have conducted an independent audit, in accordance with Australian Auditing Standards, of the financial report of [name of entity] for the year ended 30 June 20X1. We expressed a modified [unmodified<sup>45</sup>] audit opinion on that financial report in our report dated [date]. The modification, an emphasis of matter, affects [does not affect] the concise financial report [because (state reasons)]<sup>46</sup>. The Australian Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report for the year is free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the concise financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the concise financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the concise financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our included testing that the information in the concise financial report is derived from, and is consistent with, the financial report for the year, and examination on a test basis, of audit evidence supporting the amounts [, discussion and analysis,] and other disclosures which were not directly derived from the financial report for the year. These procedures have been undertaken to form an opinion whether, in all material respects, the concise financial report complies with Accounting Standard AASB 1039 *Concise Financial Reports* [and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports*]<sup>47</sup>.

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<sup>40</sup>—The subheading "Report on the Concise Financial Report" is unnecessary in circumstances when the subheadings "Emphasis of Matter in the Auditor's Report on the Financial Report for the Year", "Report on Other Legal and Regulatory Requirements" and "Report on the Remuneration Report" are not applicable.

<sup>41</sup>—The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports* applicable for annual reporting periods beginning on or after 1 January 2009. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>42</sup>—A discussion and analysis is not required for listed companies due to their section 299A reporting requirement (AASB 1039, paragraph 24-25).

<sup>43</sup>—As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>44</sup>—Alternatively, insert the title of those charged with governance.

<sup>45</sup>—Use only when the auditor's report on the (full) financial report is unmodified (i.e. contains no emphasis of matter paragraph and/or no modification to the opinion).

<sup>46</sup>—Use this sentence only when the auditor's report on the (full) financial report for the year is modified.

<sup>47</sup>—Include when a discussion and analysis is required (i.e. other than listed companies)—AASB 1039, paragraph 24.

~~[The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial report.]<sup>\*</sup>~~  
~~We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.~~

#### ~~Independence~~

~~In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of [name of entity] would be in the same terms if given to the directors as at the time of this auditor's report.<sup>#</sup>~~

#### ~~Opinion(s)~~

~~In our opinion, the concise financial report [, including the discussion and analysis<sup>48</sup>] of [name of entity] for the year ended 30 June 20X1 complies with Accounting Standard AASB 1039 *Concise Financial Reports*.~~

#### ~~Description of Emphasis of Matter~~

~~Without qualification (or without further qualification) to the opinion expressed above, attention is drawn to... (include details)<sup>49</sup>. [This emphasis of matter paragraph is included in our auditor's report on the financial report of (name of entity) for the year.]<sup>50</sup>~~

#### ~~Emphasis of Matter in the Auditor's Report on the Financial Report for the Year<sup>51</sup>~~

~~The following paragraph(s) are copied from our report on the financial report for the year. The emphasis of matter paragraph in that report does not apply to the Concise Financial Report for the reason(s) stated above.~~

~~[Insert the exact wording of the Emphasis of Matter paragraph included in the auditor's report on the financial report for the year.]~~

#### ~~Report on Other Legal and Regulatory Requirements<sup>52</sup>~~

~~[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]~~

#### ~~Report on the Remuneration Report<sup>53</sup>~~

~~The following paragraphs are copied from our Report on the Remuneration Report for the [period] ended 30 June 20X1.~~

~~[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 30 June 20X1.]~~

~~[Auditor's signature]<sup>54</sup>~~

~~[Date of the auditor's report]~~

~~[Auditor's address]~~

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<sup>\*</sup>—Include if the date of the auditor's report on the concise financial report is later than the date of the auditor's report on the audited financial report.

<sup>#</sup>—Or, alternatively, include statements: (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made.

<sup>48</sup>—Include when a discussion and analysis has been included in the concise financial report.

<sup>49</sup>—Include when the Emphasis of Matter paragraph relates to either: (a) the concise financial report; or (b) both the concise financial report and the (full) financial report for the year.

<sup>50</sup>—Include only when the Emphasis of Matter paragraph relates to both the concise financial report and the (full) financial report for the year.

<sup>51</sup>—Include only when the Emphasis of Matter paragraph in the auditor's report on the (full) financial report for the year does not relate to the concise financial report.

<sup>52</sup>—Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

<sup>53</sup>—Include only when an auditor's Report on the Remuneration Report has been included with the auditor's report on the (full) financial report.

<sup>54</sup>—The auditor's report needs to be signed in one or more of the following ways: the name of the audit firm, the name of the audit company or the personal name of the auditor as appropriate.

**GS 001**  
(November 2016)

# **Guidance Statement GS 001**

## ***Concise Financial Reports Under the Corporations Act 2001***

Issued by the **Auditing and Assurance Standards Board**



**Australian Government**

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**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Guidance Statement**

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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*Important Note*

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement *Concise Financial Reports Under the Corporations Act 2001* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

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Appendix 1: Illustrative Examples of the Auditor's Report on a Concise Financial Report

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 001 *Concise Financial Reports Under the Corporations Act 2001* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

This Guidance Statement provides guidance to assist the auditor to fulfil the objectives of the audit or assurance engagement. It includes explanatory material on specific matters for the purposes of understanding and complying with AUASB Standards. The auditor exercises professional judgement when using this Guidance Statement.

This Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

M H Kelsall  
Chairman - AUASB

## **GUIDANCE STATEMENT GS 001**

### ***Concise Financial Reports Under the Corporations Act 2001***

#### **Application**

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors reporting on a concise financial report prepared under the *Corporations Act 2001* (“the Act”) and in accordance with Accounting Standard AASB 1039 *Concise Financial Reports* (as amended April 2015) (AASB 1039).
2. For audits of other concise financial reports, the auditor complies with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.
3. This Guidance Statement should be used when an auditor conducts an audit under the Australian Auditing Standards .

#### **Issuance Date**

4. This Guidance Statement is issued on 1 February 2017 by the AUASB and replaces GS 001 *Concise Financial Reports Under the Corporations Act 2001*, issued in March 2010.

#### **Introduction**

5. The auditor’s objective in respect of a concise financial report prepared under the Act, is to express an opinion:
  - (a) whether the concise financial report complies with AASB 1039; and
  - (b) when included, whether the discussion and analysis complies with the requirements of AASB 1039.

#### **Regulatory Requirements**

6. The annual financial reporting requirements of a company, registered scheme and disclosing entity are found in section 314(1) of the Act.
7. Section 314(2) of the Act states:

A concise report for a financial year consists of:

  - (a) a concise financial report for the year drawn up in accordance with accounting standards made for the purpose of this paragraph; and
  - (b) the directors’ report for the year (see sections 298-300A); and
  - (c) a statement by the auditor:
    - (i) that the financial report has been audited; and
    - (ii) whether, in the auditor’s opinion, the concise financial report complies with the accounting standards made for the purpose of paragraph (a); and
  - (d) a copy of any qualification in, and of any statements included in the emphasis of matter section of, the auditor’s report on the financial report; and
  - (e) a statement that the report is a concise report and that the full financial report and auditor’s report will be sent to the member free of charge if the member asks for them.

8. Section 314 of the Act does not require a concise report to include the directors' declaration made under section 295(4) of the Act in respect of the (full) financial report for the year. Consequently, where the directors of an entity decide to include the directors' declaration as part of the concise report, the auditor, under ASA 720 *The Auditor's Responsibilities Relating to Other Information in Documents Containing an Audited Financial Report*, needs to read the declaration, along with other documents comprising the concise report, to identify material inconsistencies with the concise financial report and material misstatements of fact.
9. Section 314(3) of the Act requires the auditor to report on whether the discussion and analysis, if required by the Accounting Standard to be included in the concise financial report<sup>1</sup>, complies with the requirements laid down by the Accounting Standard. Furthermore, section 314(3)(b) specifies that the auditor need not otherwise audit the statements made in the discussion and analysis.
10. The requirements of the Act relating to concise financial reports are based on the view that a concise financial report can provide members with information relevant to evaluating the business, without giving them fully detailed accounting disclosures. The concise report will, in many cases, be the only report that is sent to members<sup>2</sup>. The provision, to some members, of less detailed information is expected to be sufficient to meet their needs for an understanding of the financial performance, financial position and financing and investing activities of the company, registered scheme or disclosing entity.

#### **Accounting Standard AASB 1039**

11. The Australian Accounting Standards Board issued Accounting Standard AASB 1039 *Concise Financial Reports*, the latest revision of which, dated April 2015, is operative for financial reporting periods beginning on or after 1 January 2009.

#### *Discussion and Analysis*

12. The Accounting Standard, inter alia, specifies the minimum content of a concise financial report, including a requirement that the financial statements forming part of the concise financial report, other than those of a listed company, be accompanied by discussion and analysis to assist the understanding of members.
13. AASB 1039 adopts the view that the information reported in the financial statements forming part of the concise financial report will be enhanced by discussion and analysis of the principal factors which affect the financial performance, financial position and financing and investing activities of an entity. According to AASB 1039, the extent of discussion and analysis which is required to be provided in concise financial reports will vary from entity to entity, and from year to year, as is necessary in the circumstances to compensate for the brevity of the concise financial report, compared with the (full) financial report for the year.
14. AASB 1039 does not require the financial statements, forming part of the concise financial report of listed companies, to be accompanied by discussion and analysis. This is so as to avoid repetition of information required to be included in the directors' report by section 299A of the Act.
15. Whilst AASB 1039 does not mandate specific discussion and analysis disclosures, paragraph 27 of the Standard provides examples of the types of disclosures that may, at least, be expected to accompany the financial statements.

---

<sup>1</sup> *Discussion and analysis* are not required for listed companies – see AASB 1039 paragraph 24. This is because, unlike other entities, listed companies are required by section 299A of the Act to provide an operational and financial report in the directors' report (which is included in the concise report).

<sup>2</sup> Unless members request a copy of the full financial report (annual financial report) – see section 314(2)(e) of the Act.

## **Audit Activities**

### **Engagement Acceptance**

16. Given that the concise financial report is an alternative form of reporting to members under the Act, and that the Act prescribes the auditor's reporting requirements, the AUASB takes the view that the audit of the concise financial report is treated, by auditors, as a separate engagement from the audit of the (full) financial report for the year. This view has been taken also because procedures, additional to those performed on the (full) financial report for the year, will be necessary when undertaking the audit of the concise financial report, particularly given that AASB 1039 requires, in certain circumstances, the inclusion of other information not found in the (full) financial report for the year, such as discussion and analysis.
17. In order to avoid any misunderstandings in relation to the audit of the concise financial report, the auditor complies with the engagement acceptance requirements in ASA 810 *Engagements to Report on Summary Financial Statements*. The auditor agrees the terms of the audit engagement with the appropriate person(s) within the entity's governance structure. The prudent auditor records the terms of engagement in writing and obtains written acceptance from the appropriate person representing the entity. These terms may be included in the written terms of the audit engagement for the (full) financial report. On recurring audits, the terms of the engagement are revised and re-confirmed as appropriate.
18. In addition to the specific requirements in ASA 810, the terms of engagement ordinarily include the objective and scope of the audit of the concise financial report (including the audit of discussion and analysis disclosures in that report). Such inclusions differentiate the engagement to audit the concise report from the engagement to audit the (full) financial report.

### **Audit Procedures**

#### *Auditing Standards*

19. AASB 1039 requires the concise financial report to be derived from the (full) financial report for the year and each financial statement to be presented as it is in the (full) financial report for the year. Consequently, the audit procedures performed under the Auditing Standards by the auditor when auditing the (full) financial report for the year are effectively performed on that information in the concise financial report that has been derived from the (full) financial report for the year. Accordingly, there is no expectation that such audit procedures need be repeated on the relevant information in the concise financial report.
20. Reference to "audit" and "audit procedures" in the illustrative examples of an auditor's report on the concise financial report (see Appendix 1) relate to all procedures that have been performed by the auditor (i.e. regarding both the (full) financial report and the concise financial report).
21. When selecting and applying procedures in addition to those performed in relation to the (full) financial report for the year, the auditor complies with ASA 810.
22. Under ASA 810, paragraph 8, the auditor is required to perform specified procedures. Furthermore, the auditor is required to perform additional procedures that the auditor considers necessary as the basis for the auditor's opinion (on the concise financial report), for example, procedures addressing discussion and analysis.

#### *Discussion and Analysis*

23. As the inclusion of discussion and analysis is not required in the (full) financial report for the year of some entities reporting under the Act, the audit of a concise financial report will include procedures to enable the auditor to reach a conclusion on the discussion and analysis, as part of forming an opinion on the concise financial report.

24. These procedures may include, a recalculation of ratios and/or trend analyses which have been included in the discussion and analysis; and ensuring that these disclosures are consistent with the information in the (full) financial report for the year.
25. Whilst AASB 1039 requires that the financial statements and the specific disclosures in a concise financial report be consistent with the (full) financial report for the year of the entity, it is recognised that because of the nature of discussion and analysis, such information (for example, a discussion and analysis of the main influences on the costs of the operations of the entity) goes beyond the type of disclosure which is included normally in the audited (full) financial report for the year.
26. In such circumstances, the auditor selects and applies appropriate procedures to be able to reach a conclusion on the discussion and analysis and evaluates the results of such procedures when forming an opinion on whether the discussion and analysis complies with the requirements of AASB 1039. In selecting and applying procedures and evaluating results, the auditor exercises professional judgement in accordance with *ASA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.
27. Where information of a subjective and/or prospective nature is included in the discussion and analysis, either to comment on, or to augment the entity's financial statements forming part of the concise financial report (for example, a discussion of the impact of significant economic or other events on the operations of the entity), the auditor assesses whether the inclusion of such information in the audited concise financial report has the potential to mislead users.
28. Under ASA 200, the auditor exercises professional judgement in assessing the inclusion of such information in the discussion and analysis. If the auditor considers that this information is overly subjective and/or prospective in nature, and/or that it is information which cannot be quantified or verified, then the auditor refers to Auditing Standard *ASA 705 Modifications to the Opinion in the Independent Auditor's Report*, for requirements and guidance on modifying the auditor's report. Depending on the circumstances, the modification to the auditor's report may be as a result of a disagreement with the directors (those charged with governance) on the adequacy or appropriateness of disclosures in the concise financial report or may be as a result of a limitation in scope.
29. In view of the matters discussed above, it is generally important that the auditor ascertains from the directors (those charged with governance), at an early stage in the audit, the extent and nature of the discussion and analysis that they intend to include in the concise financial report.
30. In ascertaining the extent and nature of the discussion and analysis at an early stage the auditor seeks to avert any difficulties which might otherwise arise with regard to the inclusion of such information. The directors (those charged with governance) are thus informed at that stage if, in the auditor's opinion, there is any possibility that users of the concise financial report might be misled by the inclusion of overly subjective and/or prospective terminology and information in the discussion and analysis which forms part of the concise financial report.

#### *Representations*

31. Given that the Act does not require a directors' declaration to be included in the concise report, prior to issuing the auditor's report, it would be prudent for the auditor, under *ASA 580 Written Representations*, to obtain a written representation from the entity's directors which attests that the concise financial report (including, when applicable, discussion and analysis disclosures) complies with the requirements of AASB 1039 and the Act.

### **The Auditor's Report**

32. When reporting on a concise financial report, the auditor complies with the Act and ASA 810. As section 314 of the Act prescribes the auditor's reporting obligations, the auditor adheres to the requirements in ASA 810, paragraph 10 in respect of the prescribed reporting obligations.
33. Under ASA 810, paragraph 10(b), the auditor evaluates whether the users of a concise financial report might misunderstand the auditor's opinion. Due to the precision of wording recommended in this Guidance Statement; and the requirements of the Act, an auditor ordinarily concludes that users will not misunderstand the auditor's opinion.
34. ASA 810, paragraph 16 lists the elements required to be included in an auditor's report.

#### *Modifications to the Opinion, Emphasis of Matter Paragraph, Other Matter Paragraph and Material Uncertainty Related to Going Concern Section*

35. Under ASA 810, paragraph 19, where the auditor's report on the (full) financial report includes a qualified opinion, an emphasis of matter or other matter paragraph or a material uncertainty related to going concern, the auditor's report on the concise financial report states that. In addition the auditor's report on the concise financial report describes:
  - (a) the basis for the qualified opinion on the (full) financial report, and the effect thereof on the concise financial report;
  - (b) the matter referred to in the emphasis of matter or other matter paragraph or the material uncertainty related to going concern section in the (full) financial report, and the effect thereof on the concise financial report.
36. Examples:
  - (a) AASB 1039 requires the concise financial report to be derived from, and consistent with, the (full) financial report for the year. Accordingly, modifications to the auditor's opinion on the (full) financial report for the year will commonly be applicable to the auditor's opinion on the concise financial report. Certain modifications to the auditor's opinion on the (full) financial report for the year, however, may not be applicable to the auditor's opinion on the concise financial report, such as those relating solely to disclosures in the notes to the (full) financial report for the year.
  - (b) The auditor may modify the auditor's report relating to the concise financial report only. An example is when an auditor is of the opinion that the discussion and analysis does not comply with the requirements of AASB 1039.
37. Where the auditor's report on the (full) financial report contains an adverse or disclaimer of opinion, the auditor's report on the concise financial report must, under ASA 810, paragraph 20:
  - (a) state that the auditor's report on the (full) financial report contains an adverse opinion or disclaimer of opinion;
  - (b) describe the basis for that adverse opinion or disclaimer of opinion; and
  - (c) state that, as a result of the adverse opinion or disclaimer of opinion, it is inappropriate to express an opinion on the concise financial report.

*Key Audit Matters*

38. Where an auditor's report on the (full) financial report includes communication of key audit matters in accordance with ASA 701<sup>3</sup> and the auditor is satisfied that the concise financial report is materially consistent with the (full) financial report, the auditor's report on the concise financial report states that the auditor's report on the (full) financial report includes communication of key audit matters.
39. The auditor is not required to describe the individual key audit matters in the auditor's report on the concise financial report. However, the auditor, using professional judgement, may determine whether or not to include more detailed reference to key audit matters, either generically or specifically (ie by providing subheadings or descriptions). In making this determination, the auditor considers whether such inclusions are beneficial to the users understanding of the audit of the concise financial report, or whether such inclusions could be misleading if the underlying issues are not relevant to or disclosed in a similar manner in the concise financial report.

*Other Information*

40. Where an auditor's report on the (full) financial report includes a statement that describes an uncorrected material misstatement of the other information in accordance with ASA 720<sup>4</sup> and the auditor is satisfied that the concise financial report is materially consistent with the (full) financial report, the auditor's report on the concise financial report states that the auditor's report on the (full) financial report includes a statement that describes an uncorrected material misstatement of other information; and describes the uncorrected material misstatement of other information and the effect thereof, if any, on the information included in a document containing the concise financial report.
41. A document that includes a concise financial report may contain some or all of the same matters dealt with in the other information included in the audited annual report or may include matters that are not dealt with in the other information included in the annual report.
42. The auditor reads the information included in a document containing the concise financial report, and considers whether there is a material inconsistency between that information and the concise financial report. Where a material inconsistency is identified, the auditor discusses the inconsistency with management and determines what revisions are required and considers the implications, if any, on the auditor's report on the concise financial report.
43. Where information is included in a document that includes a concise financial report and that information deals with some or all of the matters as the other information in the annual report, the work already performed on that other information in accordance with ASA 720 may be sufficient.
44. When an uncorrected material misstatement of the other information has been identified in the auditor's report on the (full) financial report and that uncorrected material misstatement relates to a matter that is dealt with in the information in a document containing the concise financial report, a material inconsistency between the concise financial report and that information may exist or the information may be misleading. The auditor discusses the inconsistency with management and determines what revisions are required and considers the implications, if any, on the auditor's report on the concise financial report.
45. Where information is included in a document that includes a concise financial report and that information deals with matters not dealt with in other information in the annual report, the auditor may still find ASA 720 helpful and follows the guidance contained in paragraph 42 of this guidance statement.

---

<sup>3</sup> See ASA 701 *Key Audit Matters*

<sup>4</sup> See ASA 720 *The Auditor's Responsibilities Relating to Other Information*

*Remuneration Report*<sup>5</sup>

46. Where a company includes a Remuneration Report in the annual directors' report, the auditor reports thereon to members. Whilst there is no legal requirement to do so, it is in the public interest that a copy of the auditor's report on the Remuneration Report is included with the auditor's report on the concise financial report.

*Illustrative Examples*

47. The illustrative reports in Appendix 1 provide examples of an auditor's report on a concise financial report.

**Conformity with International Pronouncements**

48. As this Guidance Statement relates to Australian legislative requirements under the Act, there is no equivalent International Standard on Auditing or International Auditing Practice Statement to this Guidance Statement.

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<sup>5</sup> See Guidance Statement GS 008 *The Auditor's Report on a Remuneration Report Under Section 300A of the Corporations Act 2001*.

## Appendix 1

(Ref: Para.45 )

### ILLUSTRATIVE EXAMPLES OF THE AUDITOR'S REPORT ON A CONCISE FINANCIAL REPORT

#### Introduction

A. *Examples Provided in this Appendix*

- (a) Illustration 1: Concise financial report derived from a (full) financial report of an *unlisted entity* where the auditor's report thereon includes a *material uncertainty related to going concern*.
- (b) Illustration 2: Concise financial report derived from a (full) financial report of a *listed entity* where the auditor's report thereon includes a *material uncertainty related to going concern* and *key audit matters*.
- (c) Illustration 3: Concise financial report derived from a (full) financial report of a *listed entity* where the *auditor's report is qualified* but the *qualification does not affect the auditor's opinion on the concise financial report*.
- (d) Illustration 4: Concise financial report derived from a (full) financial report of an *unlisted entity* where the *auditor's report thereon includes a material uncertainty related to going concern* and the *auditor's opinion on the concise financial report is qualified*.

**B. *Form of Reporting***

AASB 1039 does not specify whether a concise financial report prepared under section 314 of the Act is a “general purpose financial report” within the meaning described in Accounting Standard AASB 101 *Presentation of Financial Statements*. The auditor’s reporting obligations, under section 314, require an opinion on compliance (with AASB 1039), not an expression of opinion on the fair presentation of the financial information. Accordingly, the illustrative example auditor’s reports, contained within this Appendix, are not developed from a classification (general purpose or special purpose) of the concise financial report and are not based on the expression of an opinion on fair presentation.

Instead, the illustrative example auditor’s reports contained within this Appendix are discrete and have been developed from:

- (a) the auditor’s reporting obligations specified in the Act;
- (b) the reporting requirements under ASA 810;
- (c) the principles of auditor’s reporting found in Auditing Standard ASA 700 *Forming an Opinion and Reporting on a Financial Report* in relation to a compliance financial reporting framework;
- (d) consideration of the nature of concise reports, including concise financial reports, prepared under the Act and AASB 1039; and
- (e) recognition of the relationship, prescribed in AASB 1039, of a concise financial report to the audited (full) financial report for the year.

It should be noted that as AASB 1039 does not require parent entity information to be separately disclosed when consolidated financial information is presented in concise financial reports, separate references to the parent entity and consolidated entity are therefore not required in the auditor’s report on a concise financial report.

**C. *Qualifications***

Section 314(2)(d) of the Act specifies that — “a copy of any qualification in, and of any statements included in the emphasis of matter section of, the auditor’s report on the financial report”—is to be included in a concise report.

At the time section 314 was introduced into the Act, the word “qualification” was a generic term and had the same meaning and expression as used in the then Auditing Standards (AUSs) issued by the former Auditing and Assurance Standards Board (AuASB) of the Australian Accounting Research Foundation. Specifically, AUS 702.25(b) stated that a “qualified” opinion should be expressed as:

- (a) an “except for” opinion;
- (b) an adverse opinion; or
- (c) an inability to form an opinion.

However, under the current Auditing Standard (ASA 705), the term “qualified” has a specific and different meaning—it refers only to an “except for” type modification to the auditor’s opinion. The terminology used in this Guidance Statement is consistent with ASA 705.

The meaning of the term Emphasis of Matter Paragraph does not differ between the Act, the AUSs, the ASAs and this Guidance Statement.

The term “Other Matter Paragraph” has been introduced to the Australian Auditing Standards applicable for financial reporting periods commencing on or after 1 January 2010. Accordingly, the term is not used in the Act but its use has no consequence under the Act.

The term “Material Uncertainty Related to Going Concern” has been introduced to the Australian Auditing Standards applicable for financial reporting periods commencing on or after 15 December 2016. Accordingly, the term is not used in the Act but its use has no consequence under the Act as it does not result in a qualification to the auditor’s report.

The use of differing terminology between the Act and this Guidance Statement, as described above, does not mean that the requirements of section 314 of the Act have changed in so far that only “except for” type modifications are included in a concise report. The requirements of the Act remain unchanged and the term “qualification” in the Act covers all three types of modification to the auditor’s opinion listed above, regardless of how they may be described in this Guidance Statement (or the Auditing Standards).

**D. *Directors’ Obligations under the Act***

This Guidance Statement, including the illustrative auditor’s reports, is prepared to provide guidance to the auditor reporting on a concise financial report prepared under the *Corporations Act 2001*. It is not prepared to provide guidance to directors on their obligations under the Act, especially regarding section 314(2)(d) that requires a copy of any qualification and/or emphasis of matter [from the auditor’s report on the (full) financial report] to be included in the “concise report”.

E. *Illustrative Auditor's Report*

**Illustration 1:**

Circumstances include the following:

- An unmodified opinion is expressed on the (full) financial report of an entity other than a listed entity.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the (full) financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the (full) financial report was not required to communicate key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Opinion**

We have audited the concise financial report of ABC Company which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1 and the discussion and analysis.

In our opinion, the accompanying concise financial report, including the discussion and analysis of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report\*.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- *A Material Uncertainty Related to Going Concern* section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, in all material respects, complies with AASB 1039 *Concise Financial Reports* and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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<sup>†</sup> Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the audited financial report for the year.

<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

**Illustration 2:**

Circumstances include the following:

- An unmodified opinion is expressed on the audited financial report of a listed entity.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the audited financial report includes key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Opinion**

We have audited the concise financial report of ABC Company, which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1<sup>§</sup>.

In our opinion, the accompanying concise financial report of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report\*.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>§</sup> As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the *Corporations Act 2001*.]

## **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

## **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- A *Material Uncertainty Related to Going Concern* section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.
- The communication of other\* key audit matters. [Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period.]#

## **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

## **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, complies in all material respects, with AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

## **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

## **Report on the Remuneration Report**

The following paragraphs are copies from our Report on the Remuneration Report for the [period] ended 31 December 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 31 December 20X1.]

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\* In the circumstances where there is no material uncertainty related to going concern, inclusion of the word "other" in the statement for the communication of key audit matters would not be necessary.  
# The auditor may include additional explanation about key audit matters considered helpful to users of the auditor's report on the concise financial report.  
† Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

**Illustration 3:**

Circumstances include the following:

- A modified opinion is expressed on the audited financial report of a listed entity that does not affect the auditor's opinion on the concise financial report.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Opinion**

We have audited the concise financial report of ABC Company, which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1<sup>§</sup>. We expressed a qualified opinion on the audited financial report. The modification, included below does not qualify our opinion on the concise financial report<sup>‡</sup> because [insert reason(s)].

In our opinion, the accompanying concise financial report of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Opinion**

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>§</sup> As the concise financial report will be included in a document that contains other information (the concise report), the auditor may consider, if the form of presentation allows, identifying the page numbers on which the audited concise financial report is presented.

<sup>‡</sup> An example of a modification to the (full) financial report for the year that does not affect the concise financial report is a qualification ("except for") on disclosures in the notes to the financial statements where no such notes are included in the concise financial report. A copy of the modification paragraphs are included in a section of this auditor's report and is clearly identified as not affecting the auditor's opinion on the concise financial report.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report\*.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed a qualified audit opinion on the audited financial report in our report dated 15 February 20X2. The following paragraphs are copied from our report on the financial report for the year. The modification to the opinion in that report does not apply to our opinion on the concise financial report for the reason(s) stated above. [Insert the exact wording, including headings, of the basis of modification paragraph(s) and the modified opinion paragraph from the auditor's report on the financial report for the year.]

That report also includes:

- The communication of other\* key audit matters. [Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period.]#

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, complies in all material respects, with AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements†**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

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\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the Corporations Act 2001.]

# In the circumstances where there is no material uncertainty related to going concern, inclusion of the word "other" in the statement for the communication of key audit matters would not be necessary.

† The auditor may include additional explanation about key audit matters considered helpful to users of the auditor's report on the concise financial report.

† Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the (full) financial report for the year.

## **Report on the Remuneration Report**

The following paragraphs are copies from our Report on the Remuneration Report for the [period] ended 31 December 20X1.

[Insert the exact wording, including headings, of the Report on the Remuneration Report for the [period] ended 31 December 20X1.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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<sup>§</sup> The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.

**Illustration 4:**

Circumstances include the following:

- An unmodified opinion is expressed on the audited financial report of an entity other than a listed entity however, a qualified opinion is expressed on the concise financial report.
- The Concise Financial Report is prepared under the *Corporations Act 2001*.
- Established criteria for the preparation of the concise financial report exist.
- The auditor's report on the concise financial report is dated later than the date of the auditor's report on the financial report from which the concise financial report is derived.
- The auditor's report on the audited financial report includes a *Material Uncertainty Related to Going Concern* section.
- The auditor's report on the audited financial report was not required to communicate key audit matters in accordance with ASA 701.

**Report of the Independent Auditor on the Concise Financial Report**

[Appropriate Addressee]

**Qualified Opinion**

We have audited the concise financial report of ABC Company which comprises the statement of financial position as at 31 December 20X1, the statement of comprehensive income, statement of changes in equity, statement of cash flows<sup>#</sup> for the year then ended, and related notes, derived from the audited financial report of ABC Company for the year ended 31 December 20X1 and the discussion and analysis.

In our opinion, except for the effect on the concise financial report of the matter(s) referred to in the paragraph below, the accompanying concise financial report, including the discussion and analysis of ABC Company complies with Accounting Standard AASB 1039 *Concise Financial Reports*.

**Basis for Qualified Opinion**

[Include a clear description of all the substantive reasons for the qualification and quantification of the effects.]<sup>†</sup>

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities* section of our report. We are independent of the Company in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the concise financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report\*.

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<sup>#</sup> The titles used for financial statements in this example are consistent with those used in AASB 101 *Presentation of Financial Statements* and AASB 1039 *Concise Financial Reports*. AASB 101 permits the use of other appropriate titles, and consequently, auditors should ensure consistency of terms used in the auditor's report with those used in the concise financial report.

<sup>†</sup> The qualification effects the opinion on the concise financial report ONLY – for example, a qualification on the discussion and analysis.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

### **Concise Financial Report**

The concise financial report does not contain all the disclosures required by the Australian Accounting Standards. Reading the concise financial report and the auditor's report thereon, therefore, is not a substitute for reading the audited financial report and the auditor's report thereon. The concise financial report and the audited financial report do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial report.

### **The Audited Financial Report and Our Report Thereon**

We expressed an unmodified audit opinion on the audited financial report in our report dated 15 February 20X2. That report also includes:

- A *Material Uncertainty Related to Going Concern* section that draws attention to Note 6 in the audited financial report. Note 6 of the audited financial report indicates that ABC Company incurred a net loss of ZZZ during the year ended 31 December 20X1 and, as of that date, ABC Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note 6 of the audited financial report, indicate that a material uncertainty exists that may cast significant doubt on ABC Company's ability to continue as a going concern. These matters are addressed in Note 5 of the concise financial report.

### **Responsibilities of the Directors for the Concise Financial Report**

The Directors are responsible for the preparation of the concise financial report in accordance with Accounting Standard AASB 1039 *Concise Financial Reports*, and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the concise financial report.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on whether the concise financial report, in all material respects, complies with AASB 1039 *Concise Financial Reports* and whether the discussion and analysis complies with the requirements laid down in AASB 1039 *Concise Financial Reports* based on our procedures, which were conducted in accordance with Auditing Standard ASA 810 *Engagements to Report on Summary Financial Statements*.

### **Report on Other Legal and Regulatory Requirements<sup>†</sup>**

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities.]

[Auditor's name and signature<sup>§</sup>]

[Auditor's address]

[Date of the auditor's report]

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\* Or, alternatively, include statements (a) to the effect that circumstances have changed since the declaration was given to the relevant directors; and (b) setting out how the declaration would differ if it had been given to the relevant directors at the time the auditor's report was made. [Section 307C (5A)(d) of the Corporations Act 2001.]

† Include when applicable, such as when a matter has been reported under this heading in the auditor's report on the audited financial report for the year.

§ The auditor is required, under the *Corporations Act 2001*, to sign the auditor's report in both their own name and the name of their firm [section 324AB(3)] or the name of the audit company [section 324AD(1)], as applicable.





# AUASB Board Meeting Summary Paper

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**AGENDA ITEM NO.** 6  
**Meeting Date:** 29 November 2016  
**Subject:** NOCLAR (ASA 250 and conforming amendments)  
**Date Prepared:** 16 November 2016

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☒ **Action Required**

☐ **For Information Purposes Only**

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## Agenda Item Objectives

1. To consider the timing of the exposure drafts on ASA 250 and the amending standard in light of the APESB adoption of IESBA changes to NOCLAR;
2. To consider and approve the compelling reasons for modifying the ISA's; and
3. To consider and approve the exposure drafts, with timing dependent on resolution of point 1 above.

## Background

The IAASB issued the final revised ISA 250 on 5 October 2016. [Refer Agenda Item 6.3] In summary the changes in ISA 250 relate to:

- Align aspects of ISA 250 (Revised) to the NOCLAR provisions in the IESBA Code, particularly the definition of non-compliance and the examples of laws and regulations within the scope of ISA 250 (Revised) (see paragraphs 12, A6 and A9–A10 of ISA 250 (Revised)).
- Clarify the requirement regarding the auditor's determination of whether to report identified or suspected NOCLAR to an appropriate authority outside the entity and the auditor's duty of confidentiality, in order to recognize the different provisions of laws, regulations, or relevant ethical requirements (see paragraphs 29 and A28–A34 of ISA 250 (Revised)).
- Highlight that the auditor may have additional responsibilities under law, regulation, or relevant ethical requirements regarding identified or suspected NOCLAR. This also includes additional emphasis of the possible documentation requirements contained in law, regulation or relevant ethical requirements (see paragraph 9 of ISA 250 (Revised)).
- Emphasise the requirements in the IESBA Code relating to the communication of identified or suspected NOCLAR to a group engagement partner or an auditor at a component (see paragraph A8 of ISA 250 (Revised)).
- Draw attention to the fact that, in certain cases, communication with management or those charged with governance may be restricted or prohibited by law or regulation, for example law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by

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*This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.*

an appropriate authority into an actual, or suspected, illegal act (see paragraphs 20, 23 and A21 of ISA 250 (Revised)).

- Furthermore, conforming amendments were also made to a number of other International Standards to reflect the matters indicated above or clarify the expected work effort with regard to identified or suspected NOCLAR. These include ISQC 1; ISA 210; ISA 220; ISA 240; ISA 260; ISA 500; ISRE 3000, ISAE 3402; ISAE 3410; and ISRS 4410.
- Subject to the timing of the issuance of the exposure drafts, the AUASB Technical Group have prepared for AUASB approval:
  - ASA 250 ED 05-16 *Consideration of Laws and Regulations in an Audit of a Financial Report*
  - ASA 2016-1 ED 06-16 *Amendments to Australian Auditing Standards*

## **Matters to Consider**

### ***Part A – General***

The AUASB is requested to consider the matters below:

#### **Objective 1: Timing of the adoption by the APESB of IESBA NOCLAR amendments to the Code:**

- Changes to the NOCLAR provisions in the IESBA code were issued on 14 July 2016.
- ISA 250 has been amended to align with changes in the IESBA code. A revised ASA 250 in line with ISA 250 can only be issued once these changes have been adopted by the APESB.

#### ***APESB NOCLAR***

- The APESB approved a project plan for implementation of the IESBA changes in August 2016 with a view to developing an exposure draft for the Board's consideration at the APESB meeting on 29 November 2016.
- The ED is expected to have an extended exposure period of 90 days.
- At the time APESB consulted in Australia in respect of the NOCLAR ED, stakeholders (for example, SMP practices) had divergent views and there is the potential for the APESB to receive a high number of questions/issues which may impact the timing of release of the final standard.
- In addition, IESBA is going through a restructure of the Code which may render section and paragraph references redundant. IESBA is expected to issue the Code's restructure ED in Dec 2016 which will incorporate NOCLAR in the new format with section and paragraph referencing which differs from its July 2016 Standard. The stated intention is that the substance of the requirements will be maintained.
- Based on the above the AUASB and APESB will need to work together where appropriate to ensure that engagement with our stakeholders is conducted in a synchronised manner.
- A member of the AUASB Technical Group will be attending the APESB meeting on 29 November 2016. A report of these discussions will be presented to the AUASB as part of this agenda item.

**Objective 2: Issue arising from AUASB “Aus” additions contained in existing ASA 250 [refer Agenda Item 6.5 for a copy of existing ASA 250]**

<i>ASA 250 Para ref</i>	<i>Extract</i>	<i>Suggestion</i>
Aus A11.1	<p>Review of breach registers and equivalent records (for example, complaints, whistleblower or suspicious matter reports register).</p>	<p>Remove</p> <p>This paragraph was originally included in ASA 250 based on feedback obtained from the 2009 exposure process.</p> <p>Whilst the paragraph provides helpful guidance it does not meet the rationale in the compelling reason test (which requires an inconsistency with Australian regulatory arrangements or principles and practices considered appropriate in Australia).</p>
Aus A18.1	<p>Reporting Non-Compliance in the Auditor’s Report on the Financial Report (Ref: Para. 25)</p> <p>If, in the case of an audit conducted under the Corporations Act 2001, the auditor identifies non-compliance with an Australian Accounting Standard, defects or irregularities in the financial report or deficiencies, failures or shortcomings in respect of sec 307 of the Act, the auditor’s report is to include the information required by the Act.<sup>1</sup> The auditor needs to consider and other relevant laws and regulations. If the auditor is in doubt as to the proper interpretation of laws or regulations, or whether non-compliance has in fact occurred, the auditor ordinarily seeks legal advice before expressing an opinion on the financial report.</p> <p>* See sections 308 (2) and (3) of the <i>Corporations Act 2001</i></p>	<p>Remove</p> <p>This requirement is covered in AUS 700 Aus A58.1 which states:</p> <p>When the audit of a financial report is conducted in accordance with the <i>Corporations Act 2001</i> (the “Act”), section 308(3)(b) of that Act requires the auditor to describe in the auditor’s report and deficiency, failure or shortcoming in respect of certain matters referred to in section 307(b), (c) or (d) of that Act.</p>
Aus A29.1	<p>In certain circumstances, the auditor has a statutory responsibility to report instances of non-compliance with laws and regulations. For example, in certain circumstances, the auditor is required under the <i>Corporations Act 2001</i>, to report to the Australian Securities and Investments Commission (ASIC)*. Establishing the appropriate authority to which such a report would be made in a particular instance will depend on the nature and circumstances of the non-compliance. When in doubt, the auditor would ordinarily seek legal advice.</p> <p>* See ASIC Regulatory Guide 34 Auditors’ obligations: Reporting to ASIC that provides guidance to help auditors comply with their obligations, under sections 311, 601HG and 990K of the Corporations Act 2001, to report contraventions and suspected contraventions of the Act to ASIC.</p>	<p>Retain</p> <p>This Aus paragraph is in the extant and meets the compelling reason test as it results in effective and efficient compliance with a legal framework in Australia (the <i>Corporations Act 2001</i>).</p> <p>Refer compelling reason test, AI 6.6</p>

## ***Part B – NZAuASB***

The NZAuASB approved the IESBA NOCLAR amendments to their Professional and Ethical Standard 1 (PES1) on 25 August 2016.

Following the changes to PES 1, the NZAuASB approved the International Standard on Auditing (New Zealand)(ISA (NZ)) 250 (Revised) and Conforming Amendments to ISAs (NZ) and Other Pronouncements during the NZAuASB meeting held on 27 October 2016.

## ***Part C – “Compelling Reasons” Assessment***

Refer agenda item x.6

### **AUASB Technical Group Comments**

The AUASB has a strategic objective of “contributing to the development of and converging with one set of robust international auditing and assurance standards”. Delays in the implementation of the IESBA NOCLAR changes by the APESB may delay this objective. The status of the APES 110 ED (including the NOCLAR provisions referred to by the ASA 250 ED) is being discussed at the APESB meeting on 29 November 2016. A member of the Technical Group is scheduled to attend for this agenda item and will provide an update to the AUASB.

As a result, the timing of APESB project remains uncertain. The AUASB Technical Group is seeking AUASB approval of the most appropriate course of action in relation the following scenarios:

Scenario 1: If the APESB issues the APES 110 ED in December 2016, the AUASB to issue the AUASB EDs simultaneously with a 90 day comment period (to align with the APESB); or

Scenario 2: If the APESB delays issuance of the APES 110 ED, the AUASB could:

- Release the ASA 250 and amending standard EDs with references to proposed changes to the APESB Code; or
- Delay the release of the ASA 250 and amending standard EDs until the APESB approves the release of APES 110 ED.

### **AUASB Technical Group Recommendation**

1. Timing of the release of exposure drafts on ASA 250 and amending standard:
  - If scenario 1 occurs, the AUASB Technical Group recommends the AUASB approve the release the exposure drafts on ASA 250 and amending standard with references to proposed changes to the APESB Code, subject to internal quality control review.
  - If scenario 2 occurs, the AUASB Technical Group recommends the AUASB delays the release of the ASA 250 and ASA 2016-x EDs until the APESB have confirmed timing of the release of the NOCLAR ED.
2. The AUASB approve the compelling reason test in relation to proposed ASA 250 Aus para. A29.1
3. The AUASB approves the exposure drafts on ASA 250 and amending standard, to be released subject to the decision made above.

## **Material Presented**

Agenda Item 6	AUASB Board Meeting Summary Paper
Agenda Item 6.1	ASA 250 Exposure Draft
Agenda Item 6.2	ASA 2016-1 Exposure Draft
Agenda Item 6.3	Final ISA 250 (marked-up from extant)
Agenda Item 6.4	Basis for Conclusions ISA 250
Agenda Item 6.5	Extant ASA 250
Agenda Item 6.6	Compelling reason test

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## **Action Required**

<b>No.</b>	<b>Action Item</b>	<b>Deliverable</b>	<b>Responsibility</b>	<b>Due Date</b>	<b>Status</b>
1.	Approve the timing of the release of the exposure drafts on ASA 250 and amending standard	Approval in relation to timing	AUASB	29 November 2016	o/s
2.	Approve the compelling reason test in relation to ASA 250 Aus para. A29.1	Approval	AUASB	29 November 2016	o/s
2.	Approve the exposure drafts on ASA 250 and the amending standard	Approval	AUASB	29 November 2016	o/s

EXPOSURE DRAFT

**ED 05-16**  
(November 2016)

# **Proposed Auditing Standard ASA 250** *Consideration of Laws and Regulations in an Audit of a Financial Report*

Issued for Comment by the **Auditing and Assurance Standards Board**

## **DISCLAIMER**

This document contains draft proposals to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions and/or proposals to be contained in a published Exposure Draft or Auditing Standard. No responsibility is taken by the AUASB for the results of reliance, actions or omissions to act on the basis of any information contained in this document (including appendices), or for any errors or omissions in it.



**Australian Government**  

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**Auditing and Assurance Standards Board**

## Commenting on this Exposure Draft

Comments on this Exposure Draft should be received by no later than 1 February 2017. Comments should be addressed to:

The Chairman  
Auditing and Assurance Standards Board  
PO Box 204, Collins Street West  
Melbourne Victoria 8007 AUSTRALIA

## Formal Submissions

Submissions should be lodged online via the “Work in Progress-Open for Comment” page of the Auditing and Assurance Standards Board (AUASB) website ([www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx](http://www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx)) as a PDF document and Word document.

A copy of all non-confidential submissions will be placed on public record on the AUASB website: [www.auasb.gov.au](http://www.auasb.gov.au)

## Obtaining a Copy of this Exposure Draft

This Exposure Draft is available on the AUASB website: [www.auasb.gov.au](http://www.auasb.gov.au)

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## PREFACE

### Reasons for Issuing ED 05-16

### Main Proposals

This proposed Auditing Standard represents the Australian equivalent of revised ISA 250 *Consideration of Laws and Regulations in the Audit of Financial Statements* and will replace the current ASA 250 issued by the AUASB in June 2011.

This proposed Auditing Standard contains differences from the revised ISA 250, which have been made to accord with the Australian legislative environment and to maintain audit quality where the AUASB has considered there are compelling reasons to do so.

### Proposed Operative Date

It is intended that this proposed Auditing Standard will be operative for financial reporting periods commencing on or after December 15 2017.

### Request for Comments

Comments are invited on this Exposure Draft of the proposed re-issuance of *ASA 250 Consideration of Laws and Regulations in the Audit of a Financial Report* by no later than **TBD**. The AUASB is seeking comments from respondents on the following questions:

1. Have applicable laws and regulations been appropriately addressed in the proposed standard?
2. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?
3. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of audit services?
4. Are there any other significant public interest matters that constituents wish to raise?

The AUASB prefers that respondents express a clear opinion on whether the proposed Auditing Standard, as a whole, is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the above matters. The AUASB regards both supportive and critical comments as essential to a balanced review of the proposed Auditing Standard.

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* pursuant to section 227B of the Australian Securities and Investments Commission Act 2001 and section 336 of the Corporations Act 2001.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. This Auditing Standard is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

## **Conformity with International Standards on Auditing**

This Auditing Standard conforms with International Standard on Auditing ISA 250 *Consideration of Laws and Regulations in an Audit of Financial Statements* issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix “Aus”.

This Auditing Standard incorporates terminology and definitions used in Australia.

Compliance with this Auditing Standard enables compliance with ISA 250.

## AUDITING STANDARD ASA 250

### *Consideration of Laws and Regulations in an Audit of a Financial Report*

#### Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 15 December 2017.

#### Introduction

##### Scope of this Auditing Standard

1. This Auditing Standard deals with the auditor's responsibility to consider laws and regulations in an audit of a financial report. This Auditing Standard does not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific laws or regulations.

##### Effect of Laws and Regulations

2. The effect on a financial report of laws and regulations varies considerably. Those laws and regulations to which an entity is subject constitute the legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial report in that they determine the reported amounts and disclosures in an entity's financial report. Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial report. Some entities operate in heavily regulated industries (such as banks and chemical companies). Others are subject only to the many laws and regulations that relate generally to the operating aspects of the business (such as those related to occupational safety and health, and equal employment opportunity). Non-compliance with laws and regulations may result in fines, litigation or other consequences for the entity that may have a material effect on the financial report.

##### Responsibility for Compliance with Laws and Regulations (Ref: Para. A1–A8)

3. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial report.

##### *Responsibility of the Auditor*

4. The requirements in this Auditing Standard are designed to assist the auditor in identifying material misstatement of the financial report due to non-compliance with laws and regulations.

However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

5. The auditor is responsible for obtaining reasonable assurance that the financial report, taken as a whole, is free from material misstatement, whether due to fraud or error.<sup>1</sup> In conducting an audit of financial report, the auditor takes into account the applicable legal and regulatory framework. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial report may not be detected, even though the audit is properly planned and performed in accordance with the Australian Auditing Standards.<sup>2</sup> In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:

- There are many laws and regulations, relating principally to the operating aspects of an entity, that typically do not affect the financial report and are not captured by the entity's information systems relevant to financial reporting.
- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor.
- Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial report, the less likely the auditor is to become aware of it or to recognise the non-compliance.

6. This Auditing Standard distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows: (Ref: Para. A6, A12–A13)
- (a) The provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report such as tax and superannuation laws and regulations (see paragraph 14) (Ref: Para. A12); and
  - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial report, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (e.g., compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial report (see paragraph 15) (Ref: Para. A13).
7. In this Auditing Standard, differing requirements are specified for each of the above categories of laws and regulations. For the category referred to in paragraph 6(a), the auditor's responsibility is to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations. For the category referred to in paragraph 6(b), the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial report.
8. The auditor is required by this Auditing Standard to remain alert to the possibility that other audit procedures applied for the purpose of forming an opinion on the financial report may bring instances of non-compliance to the auditor's attention. Maintaining professional

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<sup>1</sup> See ASA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*, paragraph 5

<sup>2</sup> See ASA 200, paragraphs A51–A52

scepticism throughout the audit, as required by ASA 200,<sup>3</sup> is important in this context, given the extent of laws and regulations that affect the entity.

9. The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond this Auditing Standard, such as: (Ref: Para. A8)
- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;
  - (b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of a group financial report); and
  - (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other Australian Auditing Standards (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

#### **Effective Date**

10. [Deleted by the AUASB. Refer Aus 0.3]

#### **Objectives**

11. The objectives of the auditor are:
- (a) To obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report;
  - (b) To perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial report; and
  - (c) To respond appropriately to identified or suspected non-compliance with laws and regulations identified during the audit.

#### **Definition**

12. For the purposes of this Auditing Standard, the following term has the meaning attributed below:

Non-compliance – Acts of omission or commission, intentional or unintentional, committed by the entity, or by those charged with governance, by management or by other individuals working for or under the direction of the entity, which are contrary to the prevailing laws or regulations. Non-compliance does not include personal misconduct unrelated to the business activities of the entity. (Ref: Para. A9–A10)

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<sup>3</sup> See ASA 200, paragraph 15

## **Requirements**

### **The Auditor's Consideration of Compliance with Laws and Regulations**

13. As part of obtaining an understanding of the entity and its environment in accordance with ASA 315,<sup>4</sup> the auditor shall obtain a general understanding of:
  - (a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and
  - (b) How the entity is complying with that framework. (Ref: Para. A11)
14. The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report. (Ref: Para. A12)
15. The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial report: (Ref: Para. A13–A14)
  - (a) Enquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and
  - (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.
16. During the audit, the auditor shall remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. (Ref: Para. A15)
17. The auditor shall request management and, where appropriate, those charged with governance, to provide written representations that all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial report have been disclosed to the auditor. (Ref: Para. A16)
18. In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than those set out in paragraphs 13–17.

### **Audit Procedures When Non-Compliance Is Identified or Suspected**

19. If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain: (Ref: Para. A17–A18)
  - (a) An understanding of the nature of the act and the circumstances in which it has occurred; and
  - (b) Further information to evaluate the possible effect on the financial report. (Ref: Para. A19)
20. If the auditor suspects there may be non-compliance, the auditor shall discuss the matter, unless prohibited by law or regulation, with the appropriate level of management and, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgement, the effect of the

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<sup>4</sup> See ASA 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 11

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***Consideration of Laws and Regulations in an Audit of a Financial Report***

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suspected non-compliance may be material to the financial report, the auditor shall consider the need to obtain legal advice. (Ref: Para. A20–A22)

21. If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.
22. The auditor shall evaluate the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. (Ref: Para. A23–A25)

**Communicating and Reporting Identified or Suspected Non-Compliance**

*Communicating Identified or Suspected Non-Compliance with Those Charged with Governance*

23. Unless all of those charged with governance are involved in management of the entity, and therefore are aware of matters involving identified or suspected non-compliance already communicated by the auditor,<sup>5</sup> the auditor shall communicate, unless prohibited by law or regulation, with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.
24. If, in the auditor's judgement, the non-compliance referred to in paragraph 23 is believed to be intentional and material, the auditor shall communicate the matter with those charged with governance as soon as practicable.
25. If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

*Potential Implications of Identified or Suspected Non-Compliance for the Auditor's Report*  
(Ref: Para. A26–A27)

26. If the auditor concludes that the identified or suspected non-compliance has a material effect on the financial report, and has not been adequately reflected in the financial report, the auditor shall, in accordance with ASA 705, express a qualified opinion or an adverse opinion on the financial report.<sup>6</sup>
27. If the auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial report has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial report on the basis of a limitation on the scope of the audit in accordance with ASA 705.<sup>7</sup>
28. If the auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance, the auditor shall evaluate the effect on the auditor's opinion in accordance with ASA 705.

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<sup>5</sup> See ASA 260, *Communication with Those Charged with Governance*, paragraph 13

<sup>6</sup> See ASA 705, *Modifications to the Opinion in the Independent Auditor's Report*, paragraphs 7–8

<sup>7</sup> See ASA 705, paragraphs 7 and 9

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*Reporting Identified or Suspected Non-Compliance to an Appropriate Authority outside the Entity*

29. If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether law, regulation or relevant ethical requirements: (Ref: Para. A28–A34)
- (a) Require the auditor to report to an appropriate authority outside the entity.
  - (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

**Documentation**

30. The auditor shall include in the audit documentation<sup>8</sup> identified or suspected non-compliance with laws and regulations and: (Ref: Para. A35–A36)
- (a) The audit procedures performed, the significant professional judgements made and the conclusions reached thereon; and
  - (b) The discussions of significant matters related to the non-compliance with management, those charged with governance and others, including how management and, where applicable, those charged with governance have responded to the matter.

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<sup>8</sup> See ASA 230, *Audit Documentation*, paragraphs 8–11, and A6

## **Application and Other Explanatory Material**

### **Responsibility for Compliance with Laws and Regulations** (Ref: Para. 3–9)

- A1. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with laws and regulations. Laws and regulations may affect an entity's financial report in different ways: for example, most directly, they may affect specific disclosures required of the entity in the financial report or they may prescribe the applicable financial reporting framework. They may also establish certain legal rights and obligations of the entity, some of which will be recognised in the entity's financial report. In addition, laws and regulations may impose penalties in cases of non-compliance.
- A2. The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations:
- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
  - Instituting and operating appropriate systems of internal control.
  - Developing, publicising and following a code of conduct.
  - Ensuring employees are properly trained and understand the code of conduct.
  - Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
  - Engaging legal advisors to assist in monitoring legal requirements.
  - Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to the following:

- An internal audit function.
- An audit committee.
- A compliance function.

### *Responsibility of the Auditor*

- A3. Non-compliance by the entity with laws and regulations may result in a material misstatement of the financial report. Detection of non-compliance, regardless of materiality, may affect other aspects of the audit including, for example, the auditor's consideration of the integrity of management, those charged with governance or employees.
- A4. Whether an act constitutes non-compliance with laws and regulations is a matter to be determined by a court or other appropriate adjudicative body, which is ordinarily beyond the auditor's professional competence to determine. Nevertheless, the auditor's training, experience and understanding of the entity and its industry or sector may provide a basis to recognise that some acts, coming to the auditor's attention, may constitute non-compliance with laws and regulations.
- A5. In accordance with specific statutory requirements, the auditor may be specifically required to report, as part of the audit of the financial report, on whether the entity complies with certain

**Proposed Auditing Standard ASA 250**  
***Consideration of Laws and Regulations in an Audit of a Financial Report***

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provisions of laws or regulations. In these circumstances, ASA 700<sup>9</sup> or ASA 800<sup>10</sup> deal with how these audit responsibilities are addressed in the auditor's report. Furthermore, where there are specific statutory reporting requirements, it may be necessary for the audit plan to include appropriate tests for compliance with these provisions of the laws and regulations.

*Categories of Laws and Regulations (Ref: Para. 6)*

A6. The nature and circumstances of the entity may impact whether relevant laws and regulations are within the categories of laws and regulations described in paragraphs 6(a) or 6(b). Examples of laws and regulations that may be included in the categories described in paragraph 6 include those that deal with:

- Fraud, corruption and bribery.
- Money laundering, terrorist financing and proceeds of crime.
- Securities markets and trading.
- Banking and other financial products and services.
- Data protection.
- Tax and superannuation liabilities and payments.
- Environmental protection.
- Public health and safety.

*Considerations Specific to Public Sector Entities*

A7. In the public sector, there may be additional audit responsibilities with respect to the consideration of laws and regulations which may relate to the audit of the financial report or may extend to other aspects of the entity's operations.

*Additional Responsibilities Established by Law, Regulation or Relevant Ethical Requirements*  
(Ref: Para. 9)

A8. Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the *Code of Ethics for Professional Accountants* issued by the Accounting Professional and Ethical Standards Board (APESB Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial report.<sup>11</sup>

**Definition** (Ref: Para. 12)

- A9. Acts of non-compliance with laws and regulations include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, by management or by other individuals working for or under the direction of the entity.
- A10. Non-compliance also includes personal misconduct related to the business activities of the entity, for example, in circumstances where an individual in a key management position, in a

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<sup>9</sup> See ASA 700, *Forming an Opinion and Reporting on a Financial Report*, paragraph 43

<sup>10</sup> See ASA 800, *Special Considerations—Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks*, paragraph 11

<sup>11</sup> See Sections 225.21–225.22 of the IESBA Code.

personal capacity, has accepted a bribe from a supplier of the entity and in return secures the appointment of the supplier to provide services or contracts to the entity.

### **The Auditor's Consideration of Compliance with Laws and Regulations**

#### *Obtaining an Understanding of the Legal and Regulatory Framework (Ref: Para. 13)*

- A11. To obtain a general understanding of the legal and regulatory framework, and how the entity complies with that framework, the auditor may, for example:
- Use the auditor's existing understanding of the entity's industry, regulatory and other external factors;
  - Update the understanding of those laws and regulations that directly determine the reported amounts and disclosures in the financial report;
  - Enquire of management as to other laws or regulations that may be expected to have a fundamental effect on the operations of the entity;
  - Enquire of management concerning the entity's policies and procedures regarding compliance with laws and regulations; and
  - Enquire of management regarding the policies or procedures adopted for identifying, evaluating and accounting for litigation claims.

#### *Laws and Regulations Generally Recognised to Have a Direct Effect on the Determination of Material Amounts and Disclosures in the Financial Report (Ref: Para. 6, 14)*

- A12. Certain laws and regulations are well-established, known to the entity and within the entity's industry or sector, and relevant to the entity's financial report (as described in paragraph 6(a)). They could include those that relate to, for example:
- The form and content of a financial report;
  - Industry-specific financial reporting issues;
  - Accounting for transactions under government contracts; or
  - The accrual or recognition of expenses for income tax or superannuation costs.

Some provisions in those laws and regulations may be directly relevant to specific assertions in the financial report (e.g., the completeness of income tax provisions), while others may be directly relevant to the financial report as a whole (e.g., the required statements constituting a complete set of financial statements). The aim of the requirement in paragraph 14 is for the auditor to obtain sufficient appropriate audit evidence regarding the determination of amounts and disclosures in the financial report in compliance with the relevant provisions of those laws and regulations.

Non-compliance with other provisions of such laws and regulations and other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for in the financial report, but are not considered to have a direct effect on the financial report as described in paragraph 6(a).

#### *Procedures to Identify Instances of Non-Compliance—Other Laws and Regulations (Ref: Para. 6, 15)*

- A13. Certain other laws and regulations may need particular attention by the auditor because they have a fundamental effect on the operations of the entity (as described in paragraph 6(b)). Non-compliance with laws and regulations that have a fundamental effect on the operations of the entity may cause the entity to cease operations, or call into question the entity's

continuance as a going concern.<sup>12</sup> For example, non-compliance with the requirements of the entity's license or other entitlement to perform its operations could have such an impact (e.g., for a bank, non-compliance with capital or investment requirements). There are also many laws and regulations relating principally to the operating aspects of the entity that typically do not affect the financial report and are not captured by the entity's information systems relevant to financial reporting.

- A14. As the financial reporting consequences of other laws and regulations can vary depending on the entity's operations, the audit procedures required by paragraph 15 are directed to bringing to the auditor's attention instances of non-compliance with laws and regulations that may have a material effect on the financial report.

*Non-Compliance Brought to the Auditor's Attention by Other Audit Procedures (Ref: Para. 16)*

- A15. Audit procedures applied to form an opinion on the financial report may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. For example, such audit procedures may include:

- Reading minutes;
- Enquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, claims and assessments; and
- Performing substantive tests of details of classes of transactions, account balances or disclosures.

*Written Representations (Ref: Para. 17)*

- A16. Because the effect on a financial report of laws and regulations can vary considerably, written representations provide necessary audit evidence about management's knowledge of identified or suspected non-compliance with laws and regulations, whose effects may have a material effect on the financial report. However, written representations do not provide sufficient appropriate audit evidence on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained by the auditor.<sup>13</sup>

**Audit Procedures When Non-Compliance Is Identified or Suspected**

*Indications of Non-Compliance with Laws and Regulations (Ref: Para. 19)*

- A17. The auditor may become aware of information concerning an instance of non-compliance with laws and regulations other than as a result of performing the procedures in paragraphs 13–17 (e.g., when the auditor is alerted to non-compliance by a whistle blower).
- A18. The following matters may be an indication of non-compliance with laws and regulations:
- Investigations by regulatory organisations and government departments or payment of fines or penalties.
  - Payments for unspecified services or loans to consultants, related parties, employees or government employees.
  - Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the entity or in its industry or to the services actually received.
  - Purchasing at prices significantly above or below market price.

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<sup>12</sup> See ASA 570, *Going Concern*.

<sup>13</sup> See ASA 580, *Written Representations*, paragraph 4

- Unusual payments in cash, purchases in the form of cashiers' cheques payable to bearer or transfers to numbered bank accounts.
- Unusual transactions with companies registered in tax havens.
- Payments for goods or services made other than to the country from which the goods or services originated.
- Payments without proper exchange control documentation.
- Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.
- Unauthorised transactions or improperly recorded transactions.
- Adverse media comment.

*Matters Relevant to the Auditor's Evaluation (Ref: Para. 19(b))*

- A19. Matters relevant to the auditor's evaluation of the possible effect on the financial report include:
- The potential financial consequences of identified or suspected non-compliance with laws and regulations on the financial report including, for example, the imposition of fines, penalties, damages, threat of expropriation of assets, enforced discontinuation of operations, and litigation.
  - Whether the potential financial consequences require disclosure.
  - Whether the potential financial consequences are so serious as to call into question the fair presentation of the financial report, or otherwise make the financial report misleading.

*Audit Procedures and Communicating Identified or Suspected Non-Compliance with Management and Those Charged with Governance (Ref: Para. 20)*

- A20. The auditor is required to discuss the suspected non-compliance with the appropriate level of management and, where appropriate, those charged with governance, as they may be able to provide additional audit evidence. For example, the auditor may confirm that management and, where appropriate, those charged with governance have the same understanding of the facts and circumstances relevant to transactions or events that have led to the suspected non-compliance with laws and regulations.
- A21. However, in some jurisdictions, law or regulation may restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice.
- A22. If management or, as appropriate, those charged with governance do not provide sufficient information to the auditor that the entity is in fact in compliance with laws and regulations, the auditor may consider it appropriate to consult with the entity's in-house or external legal counsel about the application of the laws and regulations to the circumstances, including the possibility of fraud, and the possible effects on the financial report. If it is not considered appropriate to consult with the entity's legal counsel or if the auditor is not satisfied with the legal counsel's opinion, the auditor may consider it appropriate to consult on a confidential basis with others within the firm, a network firm, a professional body, or with the auditor's legal counsel as to whether a contravention of a law or regulation is involved, including the

possibility of fraud, the possible legal consequences, and what further action, if any, the auditor would take.

*Evaluating the Implications of Identified or Suspected Non-Compliance (Ref: Para. 22)*

- A23. As required by paragraph 22, the auditor evaluates the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations. The implications of particular identified or suspected non-compliance will depend on the relationship of the perpetration and concealment, if any, of the act to specific control activities and the level of management or individuals working for, or under the direction of, the entity involved, especially implications arising from the involvement of the highest authority within the entity. As noted in paragraph 9, the auditor's compliance with law, regulation or relevant ethical requirements may provide further information that is relevant to the auditor's responsibilities in accordance with paragraph 22.
- A24. Examples of circumstances that may cause the auditor to evaluate the implications of identified or suspected non-compliance on the reliability of written representations received from management and, where applicable, those charged with governance include when:
- The auditor suspects or has evidence of the involvement or intended involvement of management and, where applicable, those charged with governance in any identified or suspected non-compliance.
  - The auditor is aware that management and, where applicable, those charged with governance have knowledge of such non-compliance and, contrary to legal or regulatory requirements, have not reported, or authorised reporting of, the matter to an appropriate authority within a reasonable period.
- A25. In certain circumstances, the auditor may consider withdrawing from the engagement, where permitted by law or regulation, for example when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances or the identified or suspected non-compliance raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial report. The auditor may consider it appropriate to obtain legal advice to determine whether withdrawal from the engagement is appropriate. When the auditor determines that withdrawing from the engagement would be appropriate, doing so would not be a substitute for complying with other responsibilities under law, regulation or relevant ethical requirements to respond to identified or suspected non-compliance. Furthermore, paragraph A8a of ASA 220<sup>14</sup> indicates that some ethical requirements may require the predecessor auditor, upon request by the proposed successor auditor, to provide information regarding non-compliance with laws and regulations to the successor auditor.

**Communicating and Reporting Identified or Suspected Non-Compliance**

*Potential Implications of Identified or Suspected Non-Compliance for the Auditor's Report*  
(Ref: Para. 26–28)

- A26. Identified or suspected non-compliance with laws and regulation is communicated in the auditor's report when the auditor modifies the opinion in accordance with paragraphs 26–28. In certain other circumstances, the auditor may communicate identified or suspected non-compliance in the auditor's report, for example:
- When the auditor has other reporting responsibilities, in addition to the auditor's responsibilities under the Australian Auditing Standards, as contemplated by paragraph 43 of ASA 700;

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<sup>14</sup> See ASA 220, *Quality Control for an Audit of a Financial Report and Other Historical Financial Information*

**Proposed Auditing Standard ASA 250**  
***Consideration of Laws and Regulations in an Audit of a Financial Report***

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- When the auditor determines that the identified or suspected non-compliance is a key audit matter and accordingly communicates the matter in accordance with ASA 701,<sup>15</sup> unless paragraph 14 of that Auditing Standard applies; or
- In exceptional cases when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances and withdrawal from the engagement is not possible (see paragraph A25), the auditor may consider describing the identified or suspected non-compliance in an Other Matter paragraph in accordance with ASA 706.<sup>16</sup>

A27. Law or regulation may preclude public disclosure by either management, those charged with governance or the auditor about a specific matter. For example, law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including a prohibition on alerting the entity. When the auditor intends to communicate identified or suspected non-compliance in the auditor's report under the circumstances set out in paragraph A26 or otherwise, such law or regulation may have implications for the auditor's ability to describe the matter in the auditor's report, or in some circumstances to issue the auditor's report. In such cases, the auditor may consider obtaining legal advice to determine the appropriate course of action.

*Reporting Identified or Suspected Non-Compliance to an Appropriate Authority outside the Entity*  
(Ref: Para. 29)

- A28. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:
- (a) Law, regulation or relevant ethical requirements require the auditor to report (see paragraph A29);
  - (b) The auditor has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements (see paragraph A30); or
  - (c) Law, regulation or relevant ethical requirements provide the auditor with the right to do so (see paragraph A31).
- A29. In some jurisdictions, the auditor may be required by law, regulation or relevant ethical requirements to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity. For example, in some jurisdictions, statutory requirements exist for the auditor of a financial institution to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to a supervisory authority. Also, misstatements may arise from non-compliance with laws or regulations and, in some jurisdictions, the auditor may be required to report misstatements to an appropriate authority in cases where management or those charged with governance fail to take corrective action.

Aus 29.1 In certain circumstances, the auditor has a statutory responsibility to report instances of non-compliance with laws and regulations. For example, in certain circumstances, the auditor is required under the Corporations Act 2001, to report to the Australian Securities and Investments Commission (ASIC).<sup>\*</sup> Establishing the appropriate authority to which such a report would be made in a particular instance will depend on the nature and circumstances of the non-compliance. When in doubt, the auditor would ordinarily seek legal advice.

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<sup>15</sup> See ASA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

<sup>16</sup> See ASA 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

<sup>\*</sup> See ASIC Regulatory Guide 34 *Auditors' obligations: Reporting to ASIC* that provides guidance to help auditors comply with their obligations, under sections 311, 601HG and 990K of the *Corporations Act 2001*, to report contraventions and suspected contraventions of the Act to ASIC.

- A30. In other cases, the relevant ethical requirements may require the auditor to determine whether reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the APESB Code requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed, which may include reporting to an appropriate authority outside the entity.<sup>17</sup> The APESB Code explains that such reporting would not be considered a breach of the duty of confidentiality under the APESB Code.<sup>18</sup>
- A31. Even if law, regulation or relevant ethical requirements do not include requirements that address reporting identified or suspected non-compliance, they may provide the auditor with the right to report identified or suspected non-compliance to an appropriate authority outside the entity. For example, when auditing the financial report of financial institutions, the auditor may have the right under law or regulation to discuss matters such as identified or suspected non-compliance with laws and regulations with a supervisory authority.
- A32. In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the auditor's duty of confidentiality under law, regulation or relevant ethical requirements.
- A33. The determination required by paragraph 29 may involve complex considerations and professional judgements. Accordingly the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular course of action.

*Considerations Specific to Public Sector Entities*

- A34. A public sector auditor may be obliged to report on identified or suspected non-compliance to the legislature or other governing body or to report them in the auditor's report.

**Documentation** (Ref: Para. 30)

- A35. The auditor's documentation of findings regarding identified or suspected non-compliance with laws and regulations may include, for example:
- Copies of records or documents.
  - Minutes of discussions held with management, those charged with governance or parties outside the entity.
- A36. Law, regulation or relevant ethical requirements may also set out additional documentation requirements regarding identified or suspected non-compliance with laws and regulations.<sup>19</sup>

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<sup>17</sup> See, for example, Section 225.29 and Sections 225.33–225.36 of the IESBA Code.

<sup>18</sup> See, for example, Section 140.7 and Section 225.35 of the IESBA Code.

<sup>19</sup> See, for example, Section 225.37 of the IESBA Code.

**Summary of Differences — Proposed Revised ASA 250 and Existing ASA 250*****Summary of Main Differences — ASA 250 and Existing ASA 250***

The summary below outlines the main differences (excluding editorial amendments) between this proposed Auditing Standard and existing ASA 250. *This summary should not be used as a complete list of all changes made.*

- Align aspects of ASA 250 to the NOCLAR provisions in the APESB Code, particularly the definition of non-compliance and the examples of laws and regulations within the scope of ASA 250 (see paragraphs 12, A6 and A9–A10 of ASA 250).
- Clarify the requirement regarding the auditor's determination of whether to report identified or suspected NOCLAR to an appropriate authority outside the entity and the auditor's duty of confidentiality, in order to recognize the different provisions of laws, regulations, or relevant ethical requirements (see paragraphs 29 and A28–A34 of ASA 250).
- Highlight that the auditor may have additional responsibilities under law, regulation, or relevant ethical requirements regarding identified or suspected NOCLAR. This also includes additional emphasis of the possible documentation requirements contained in law, regulation or relevant ethical requirements (see paragraph 9 of ASA 250).
- Highlight the implications of identified or suspected NOCLAR on the audit, for example, the reliability of management's representations, the implications for the auditor's report, and the consideration of whether to withdraw from the engagement (see paragraphs 22 and A23–A27 of ASA 250).
- Emphasise the requirements in the APESB Code relating to the communication of identified or suspected NOCLAR to a group engagement partner or an auditor at a component (see paragraph A8 of ASA 250).
- Draw attention to the fact that, in certain cases, communication with management or those charged with governance may be restricted or prohibited by law or regulation, for example law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act (see paragraphs 20, 23 and A21 of ASA 250).

**EXPOSURE DRAFT**

**ED 06-2016**

(November 2016)

# **Proposed Auditing Standard ASA 2016-1** *Amendments to Australian Auditing Standards*

**Draft**

Issued for Comment by the **Auditing and Assurance Standards Board**

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**Australian Government**

**Auditing and Assurance Standards Board**

## **Commenting on this Exposure Draft**

Comments on this Exposure Draft should be received by no later than 28 February 2017. Comments should be addressed to:

The Chairman  
Auditing and Assurance Standards Board  
PO Box 204, Collins Street West  
Melbourne Victoria 8007 AUSTRALIA

## **Formal Submissions**

Submissions should be lodged online via the “Work in Progress-Open for Comment” page of the Auditing and Assurance Standards Board (AUASB) website ([www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx](http://www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx)) as a PDF document and Word document.

A copy of all non-confidential submissions will be placed on public record on the AUASB website: [www.auasb.gov.au](http://www.auasb.gov.au)

## **Obtaining a Copy of this Exposure Draft**

This Exposure Draft is available on the AUASB website: [www.auasb.gov.au](http://www.auasb.gov.au)

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## PREFACE

### Reasons for Issuing ED 06-2016

The AUASB issues exposure draft ED 06-2016 of proposed Auditing Standard ASA 2016-1 *Amendments to Australian Auditing Standards* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, inter alia, to develop auditing standards that have a clear public interest focus and are of the highest quality.

### Main Proposals

This proposed Auditing Standard makes amendments to the requirements and/or application & other explanatory material of the following Auditing Standards:

ASQC 1	<i>Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements</i> (11 November 2013)
ASA 210	<i>Agreeing the Terms of Audit Engagements</i> (1 December 2015)
ASA 220	<i>Quality Control for an Audit of a Financial Report and Other Historical Information</i> (1 December 2015)
ASA 240	<i>The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report</i> (1 December 2015)
ASA 260	<i>Communication with Those Charged with Governance</i> (11 November 2013)
ASA 450	<i>Evaluation of Misstatements Identified During the Audit</i> (1 December 2015)
ASA 500	<i>Audit Evidence</i> (1 December 2015)
ASRE 2400	<i>Review of a Financial Report Performed by an Assurance Practitioner Who is Not the Auditor of the Entity</i> (26 March 2013)
ASAE 3000	<i>Assurance Engagements Other than Audits or Reviews of Historical Financial Information</i> (24 June 2014)
ASAE 3402	<i>Assurance Reports on Controls at a Service Organisation</i> (24 June 2014)
ASAE 3410	<i>Assurance Engagements on Greenhouse Gas Statements</i> (24 June 2014)

The amendments arise from changes made by the International Auditing and Assurance Standards Board (IAASB) to ISA 250. Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the IAASB for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards.

## **Proposed Operative Date**

It is intended that this proposed Auditing Standard will be operative for financial reporting periods commencing on or after 15 December 2017.

## **Request for Comments**

Comments are invited on this Exposure Draft of the proposed issuance of ASA 2016-1 *Amendments to Australian Auditing Standards* by no later than 28 February 2017. The AUASB is seeking comments from respondents on the following questions:

1. Have applicable laws and regulations been appropriately addressed in the proposed standard?
2. Are there any references to relevant laws or regulations that have been omitted?
3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?
4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of audit services?
5. Are there any other significant public interest matters that constituents wish to raise?

The AUASB prefers that respondents express a clear opinion on whether the proposed Auditing Standard, as a whole, is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the above matters. The AUASB regards both supportive and critical comments as essential to a balanced review of the proposed Auditing Standard.

**AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 2016-1 *Amendments to Australian Auditing Standards* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

Draft

## **Conformity with International Standards on Auditing**

This Auditing Standard has been made for Australian legislative purposes and accordingly there is no equivalent International Standard on Auditing (ISA) issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC). These proposed amendments, in the main, reflect similar amendments made to the equivalent International Standards on Auditing (ISAs).

**Draft**

## **AUDITING STANDARD ASA 2016-1**

### ***Amendments to Australian Auditing Standards***

#### **Application**

1. This Auditing Standard applies to:
  - an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - an audit of a financial report, or a complete set of financial statements, for any other purpose.
2. This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### **Operative Date**

3. This Auditing Standard is operative for financial reporting periods commencing on or after 15 December 2017.

#### **Introduction**

##### **Scope of this Auditing Standard**

4. This Auditing Standard makes amendments to the Australian Auditing Standards arising from changes made by the International Auditing and Assurance Standards Board (IAASB) to ISA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* resulting from enhancements aimed at addressing laws and regulations.

#### **Objective**

5. The objective of this Auditing Standard is to make amendments to the following Auditing Standards:
  - (a) ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements* (11 November 2013)
  - (b) ASA 210 *Agreeing the Terms of Audit Engagements* (1 December 2015)
  - (c) ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Information* (1 December 2015)
  - (d) ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (1 December 2015)
  - (e) ASA 260 *Communication with Those Charged with Governance* (11 November 2013)
  - (f) ASA 450 *Evaluation of Misstatements Identified During the Audit* (1 December 2015)
  - (g) ASA 500 *Audit Evidence* (1 December 2015)
  - (h) ASRE 2400 *Review of a Financial Report Performed by an Assurance Practitioner Who is Not the Auditor of the Entity* (26 March 2013)

- (i) ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (24 June 2014)
- (j) ASAE 3402 *Assurance Reports on Controls at a Service Organisation* (24 June 2014)
- (k) ASAE 3410 *Assurance Engagements on Greenhouse Gas Statements* (24 June 2014)

## **Definition**

6. For the purposes of this Auditing Standard, the meanings of terms are set out in each Auditing Standard and in the *AUASB Glossary*. This Auditing Standard does not introduce new definitions.

## **Amendments to Auditing Standards**

### **Amendments to ASQC 1**

7. A new paragraph A56 is inserted as follows:

Relevant ethical requirements establish an obligation for the firm's personnel to observe at all times the confidentiality of information contained in engagement documentation, unless specific client authority has been given to disclose information, or there are responsibilities under law, regulation or relevant ethical requirements is a legal or professional duty to do so.<sup>1</sup> Specific laws or regulations may impose additional obligations on the firm's personnel to maintain client confidentiality, particularly where data of a personal nature are concerned.

### **Amendments to ASA 210**

8. Paragraph A26 is amended to read as follows:

When relevant, the following points could also be made in the audit engagement letter:

- Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.
- Arrangements concerning the involvement of internal auditors and other staff of the entity.
- Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit.
- A reference to, and description of, the auditor's responsibilities under law, regulation or relevant ethical requirements that address reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
- Any restriction of the auditor's liability when such possibility exists.
- A reference to any further agreements between the auditor and the entity.
- Any obligations to provide audit working papers to other parties.

An example of an audit engagement letter is set out in Appendix 1.

### **Amendments to ASA 220**

9. A new paragraph A8 is inserted as follows:

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<sup>1</sup> See, for example, Section 140.7 and Section 225.35 of the IESBA Code.

Law, regulation, or relevant ethical requirements<sup>2</sup> may require the auditor to request, prior to accepting the engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's judgement, the auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances, the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected non-compliance with laws and regulations to the proposed successor auditor. For example, where the predecessor auditor has withdrawn from the engagement as a result of identified or suspected non-compliance with laws and regulations, the APESB Code requires that the predecessor auditor, on request by a proposed successor auditor, provides all such facts and other information concerning such non-compliance that, in the predecessor auditor's opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.<sup>3</sup>

#### **Amendments to ASA 240**

10. A new paragraph 8 is inserted as follows:

The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this and other Australian Auditing Standards, such as: (Ref: Para. A5a)

- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;
- (b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of a group financial report); and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other Australian Auditing Standards (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

11. Paragraph 40 is amended to read as follows:

If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor shall communicate these matters, unless prohibited by law or regulation, on a timely basis with~~to~~ the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities. (Ref: Para. A59a–A60)

12. Paragraph 41 is amended to read as follows:

Unless all of those charged with governance are involved in managing the entity, if the auditor has identified or suspects fraud involving:

- (a) management;
- (b) employees who have significant roles in internal control; or
- (c) others where the fraud results in a material misstatement in the financial report,

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<sup>2</sup> See, for example, Sections 210.14 of the IESBA Code.  
<sup>3</sup> See, for example, Sections 225.31 of the IESBA Code.

the auditor shall communicate these matters ~~with~~ those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions ~~with~~ those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit. Such communications with those charged with governance are required unless the communication is prohibited by law or regulation. (Ref: Para. A59a, A61–A63)

13. Paragraph 42 is amended to read as follows:

The auditor shall communicate, unless prohibited by law or regulation, with those charged with governance any other matters related to fraud that are, in the auditor's judgement, relevant to their responsibilities. (Ref: Para. A59a, A64)

14. The heading above paragraph 43 is amended to read as follows:

~~Communications to Regulatory and Enforcement Authorities~~ Reporting Fraud to an Appropriate Authority Outside the Entity

15. Paragraph 43 is amended to read as follows:

If the auditor has identified or suspects a fraud, the auditor shall determine whether law, regulation or relevant ethical requirements ~~there is a responsibility to report the occurrence or suspicion to a party outside the entity. Although the auditor's professional duty to maintain the confidentiality of client information may preclude such reporting, the auditor's legal responsibilities may override the duty of confidentiality in some circumstances.~~  
(Ref: Para. A65–A67)

- (a) Require the auditor to report to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

16. A new heading is inserted above paragraph A5 as follows:

**Responsibility for the Prevention and Detection of Fraud**

*Responsibilities of the Auditor* (Ref: Para. 8a)

17. A new paragraph A5 is inserted as follows:

Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the *Code of Ethics for Professional Accountants* issued by the Accounting and Professional and Ethical Standards Board (APESB Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial report.<sup>4</sup>

18. The heading above paragraph A60 is amended to read as follows:

~~Communications to Regulatory and Enforcement Authorities~~ Reporting Fraud to an Appropriate Authority outside the Entity (Ref: Para. 43)

19. A new paragraph A60 is inserted as follows:

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<sup>4</sup> See Sections 225.21–225.22 of the IESBA Code.

In some jurisdictions, law or regulation may restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the fraud to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice.

20. The heading above paragraph A65 is amended to read as follows:

Communications to Regulatory and Enforcement Authorities Reporting Fraud to an Appropriate Authority outside the Entity (Ref: Para. 43)

21. A new paragraph A65 is inserted as follows:

ASA 250 (Revised)<sup>5</sup> provides further guidance with respect to the auditor's determination of whether reporting identified or suspected non-compliance with laws or regulations to an appropriate authority outside the entity is required or appropriate in the circumstances, including consideration of the auditor's duty of confidentiality. The auditor's professional duty to maintain the confidentiality of client information may preclude reporting fraud to a party outside the client entity. However, the auditor's legal responsibilities vary by country and, in certain circumstances, the duty of confidentiality may be overridden by statute, the law or courts of law. In some countries, the auditor of a financial institution has a statutory duty to report the occurrence of fraud to supervisory authorities. Also, in some countries the auditor has a duty to report misstatements to authorities in those cases where management and those charged with governance fail to take corrective action.

22. Paragraph A66 is amended to read as follows:

The determination required by paragraph 43 may involve complex considerations and professional judgements. Accordingly, the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider it appropriate to obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular determine the appropriate course of action in the circumstances, the purpose of which is to ascertain the steps necessary in considering the public interest aspects of identified fraud.

#### **Amendments to ASA 260**

23. Paragraph 7 is amended to read as follows:

In some jurisdictions, Law or regulation may restrict the auditor's communication of certain matters with those charged with governance. For example, Laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report identified or suspected non-compliance with laws and regulations to an appropriate authority pursuant to anti-money laundering legislation. In some these circumstances, the issues considered by the auditor potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, and the auditor may consider it appropriate to obtaining legal advice.

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<sup>5</sup> See ASA 250, Consideration of Laws and Regulations in an Audit of a Financial Report, paragraphs A28–A34

#### **Amendments to ASA 450**

24. Paragraph 8 is amended to read as follows:

The auditor shall communicate, unless prohibited by law or regulation, on a timely basis all misstatements accumulated during the audit with the appropriate level of management, ~~unless prohibited by law or regulation~~.<sup>6</sup> The auditor shall request management to correct those misstatements. (Ref: Para. A7–A9)

25. Paragraph A8 is amended to read as follows:

In some jurisdictions, law or regulation may restrict the auditor's communication of certain misstatements to management, or others, within the entity. For example, laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report identified or suspected non-compliance with law or regulation to an appropriate authority pursuant to anti-money laundering legislation. In some of these circumstances, potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, the issues considered by the auditor may be complex and the auditor may consider seeking appropriate to obtain legal advice

#### **Amendments to ASA 500**

26. Paragraph 7 is amended to read as follows:

When designing and performing audit procedures, the auditor shall consider the relevance and reliability of the information to be used as audit evidence. (Ref: Para. A26–A33a)

27. Paragraph A26 is amended to read as follows:

As noted in paragraph A1, while audit evidence is primarily obtained from audit procedures performed during the course of the audit, it may also include information obtained from other sources such as, for example, previous audits, in certain circumstances, ~~and~~ a firm's quality control procedures for client acceptance and continuance and complying with certain additional responsibilities under law, regulation or relevant ethical requirements (e.g., regarding an entity's non-compliance with laws and regulations). The quality of all audit evidence is affected by the relevance and reliability of the information upon which it is based.

28. A new paragraph A33 is inserted as follows:

ASA 250<sup>7</sup> provides further guidance with respect to the auditor complying with any additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's identified or suspected non-compliance with laws and regulations that may provide further information that is relevant to the auditor's work in accordance with Australian Auditing Standards and evaluating the implications of such non-compliance in relation to other aspects of the audit.

#### **Amendments to ASRE 2400**

29. Paragraph 48 is amended to read as follows:

The practitioner's enquiries of management and others within the entity, as appropriate, shall include the following: (Ref: Para. A84–A87a)

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<sup>6</sup> See ASA 260, Communication with Those Charged with Governance, paragraph 7

<sup>7</sup> See ASA 250, Consideration of Laws and Regulations in an Audit of a Financial Report, paragraph 9

- (d) The existence of any actual, suspected or alleged:
- (i) Fraud or illegal acts affecting the entity; and
  - (ii) Non-compliance with provisions of laws and regulations that are generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report, such as tax and superannuation laws and regulations;
30. The heading above paragraph 52 is amended to read as follows:
- Fraud and non-compliance with laws ~~and~~ regulations
31. Paragraph 52 is amended to read as follows:
- When there is an indication that fraud or non-compliance with laws ~~and~~ regulations, or suspected fraud or non-compliance with laws ~~and~~ regulations, has occurred in the entity, the practitioner shall:
- (a) Communicate that matter, unless prohibited by law or regulation, with to the appropriate level of senior management or those charged with governance as appropriate; (Ref: Para. A91a)
  - (b) Request management's assessment of the effect(s), if any, on the financial report;
  - (c) Consider the effect, if any, of management's assessment of the effects of identified or suspected fraud or non-compliance with laws ~~and~~ regulations communicated to the practitioner on the practitioner's conclusion on the financial report and on the practitioner's report; and
  - (d) Determine whether law, regulation or relevant ethical requirements; ~~there is a responsibility to report the occurrence or suspicion of fraud or illegal acts to a party outside the entity. (Ref: Para. A92–A92d)~~
    - (i) Require the practitioner to report to an appropriate authority outside the entity.
    - (ii) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.
32. A new paragraph A87 is inserted as follows:
- The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this ASRE, such as:
- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;
  - (b) Communicating identified or suspected non-compliance with laws and regulations to an auditor, for example a group engagement partner;<sup>8</sup> and
  - (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

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<sup>8</sup> See, for example, Sections 225.44–225.48 of the IESBA Code.

Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this Assurance Standard (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

33. The heading above paragraph A92 is amended to read as follows:

Fraud and non-compliance with laws ~~or~~and regulations (Ref: Para. 52(a) and (d))

34. A heading is inserted above paragraph A92 as follows:

Communication with management and those charged with governance

35. A new paragraph A92 is inserted as follows:

In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report identified or suspected non-compliance with laws and regulations to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may be complex and the practitioner may consider it appropriate to obtain legal advice.

Reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity

36. Paragraph A92 is amended to read as follows:

~~Under this ISRE, if the practitioner has identified or suspects fraud or illegal acts, the practitioner is required to determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:~~

- (a) Law, regulation or relevant ethical requirements require the practitioner to report;
- (b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements (see paragraph A92a); or
- (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so (see paragraph A92b).

~~Although the practitioner's professional duty to maintain the confidentiality of client information may preclude such reporting, the practitioner's legal responsibilities may override the duty of confidentiality in some circumstances.~~

37. A new paragraph A92a is inserted as follows:

In some cases, the relevant ethical requirements may require the practitioner to report or to consider whether reporting identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the APESB Code requires the practitioner to take steps to respond to identified or suspected non-compliance with laws and regulations, and consider whether further action is needed, which may include reporting to an appropriate authority

outside the entity.<sup>9</sup> The APESB Code explains that such reporting would not be considered a breach of the duty of confidentiality under the APESB Code.<sup>10</sup>

38. A new paragraph A92b is inserted as follows:

Even if law, regulation or relevant ethical requirements do not include requirements that address reporting identified or suspected non-compliance, they may provide the practitioner with the right to report identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity.

39. A new paragraph A92c is inserted as follows:

In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation or relevant ethical requirements.

40. A new paragraph A92d is inserted as follows:

The determination required by paragraph 52(d) may involve complex considerations and professional judgements. Accordingly, the practitioner may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The practitioner may also consider obtaining legal advice to understand the practitioner's options and the professional or legal implications of taking any particular course of action.

#### **Amendments to ASAE 3000**

41. Paragraph 45 is amended to read as follows:

The practitioner shall make enquiries of the appropriate party(ies) regarding:

- (a) Whether they have knowledge of any actual, suspected or alleged intentional misstatement or non-compliance with laws and regulations affecting the subject matter information; (Ref: Para. A101–A101a)
- (b) Whether the responsible party has an internal audit function and, if so, make further enquiries to obtain an understanding of the activities and main findings of the internal audit function with respect to the subject matter information; and
- (c) Whether the responsible party has used any experts in the preparation of the subject matter information.

42. Paragraph A78 is amended to read as follows:

The practitioner shall consider whether, pursuant to the terms of the engagement and other engagement circumstances, any matter has come to the attention of the practitioner that is to be communicated with the responsible party, the measurer or evaluator, the engaging party, those charged with governance or others. (Ref: Para. A192–A192f)

43. A new paragraph A101a is inserted as follows:

The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond the practitioner's responsibilities under this ASAE, such as:

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<sup>9</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.

<sup>10</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.

- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;
- (b) Communicating identified or suspected non-compliance with laws and regulations to an auditor;<sup>11</sup> and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this and any other ASAE (e.g., regarding the integrity of the responsible party or those charged with governance). Paragraphs A192a–A192e further address the practitioner's responsibilities under law, regulation or relevant ethical requirements regarding communicating and reporting identified or suspected non-compliance with laws and regulations.

44. A new heading is inserted above paragraph A192a as follows:

Communication with Management and Those Charged with Governance

45. A new paragraph A192a is inserted as follows:

Relevant ethical requirements may include a requirement to report identified or suspected non-compliance with laws and regulations to an appropriate level of management or those charged with governance. In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with the responsible party, management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may be complex and the practitioner may consider it appropriate to obtain legal advice.

46. A new heading is inserted above paragraph A192b as follows:

Reporting of Identified or Suspected Non-Compliance with Laws and Regulations to an Appropriate Authority outside the Entity

47. A new paragraph A192b is inserted as follows:

Law, regulation or relevant ethical requirements may:

- (a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>12</sup>

48. A new paragraph A192c is inserted as follows:

Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

- (a) Law, regulation or relevant ethical requirements require the practitioner to report;

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<sup>11</sup> See, for example, Sections 225.44–225.48 of the IESBA Code.

<sup>12</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.

- (b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements; or.
- (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.

49. A new paragraph A192d is inserted as follows:

The reporting of identified or suspected non-compliance with laws and regulations in accordance with law, regulation or relevant ethical requirements may include non-compliance with laws and regulations that the practitioner comes across or is made aware of when performing the engagement but which may not affect the subject matter information. Under this ASAE, the practitioner is not expected to have a level of understanding of laws and regulations beyond those affecting the subject matter information. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgement and expertise in responding to such non-compliance. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

50. A new paragraph A192e is inserted as follows:

In some circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation, or relevant ethical requirements. In other cases, reporting identified or suspected non-compliance to an appropriate authority outside the entity would not be considered a breach of the duty of confidentiality under the relevant ethical requirements.<sup>13</sup>

51. A new paragraph A192f is inserted as follows:

The practitioner may consider consulting internally (e.g., within the firm or network firm), obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality).<sup>14</sup>

## **Amendments to ASAE 3402**

52. Paragraph 56 is amended to read as follows:

If the service auditor becomes aware of non-compliance with laws and regulations, fraud, or uncorrected errors attributable to the service organisation that are not clearly trivial and may affect one or more user entities, the service auditor shall determine whether the matter has been communicated appropriately to affected user entities. If the matter has not been so communicated and the service organisation is unwilling to do so, the service auditor shall take appropriate action. (Ref: Para. A53)

53. Paragraph 56 is amended to read as follows:

Appropriate actions to respond to the circumstances identified in paragraph 56, unless prohibited by law or regulation, may include:

- Obtaining legal advice about the consequences of different courses of action.
- Communicating with those charged with governance of the service organisation.

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<sup>13</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.

<sup>14</sup> See, for example, Section 225.55 of the IESBA Code.

- Determining whether to communicate with third parties (e.g., law, regulation or relevant ethical requirements may require the service auditor to report to an appropriate authority outside the entity or the external auditor of the service organisation,<sup>15</sup> or establish responsibilities under which such reporting may be appropriate in the circumstances).~~Communicating with third parties (for example, a regulator) when required to do so.~~
- Modifying the service auditor's opinion, or adding an Other Matter paragraph.
- Withdrawing from the engagement.

**Amendments to ASAE 3410**

54. Paragraph 78 is amended to read as follows:

The practitioner shall communicate, unless prohibited by law or regulation, ~~with~~ those person(s) with oversight responsibilities for the GHG statement the following matters that come to the practitioner's attention during the course of the engagement, and shall determine whether there is a responsibility to report them to another party within or outside the entity:

- (a) Deficiencies in internal control that, in the practitioner's professional judgement, are of sufficient importance to merit attention;
- (b) Identified or suspected fraud; and
- (c) Matters involving identified or suspected non-compliance with laws and~~or~~ regulations, other than when the matters are clearly trivial. (Ref: Para. A87)

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<sup>15</sup> See, for example, Section 225.44 to 225.48 of the IESBA Code.

**Final Pronouncement**  
October 2016

*International Standard on Auditing 250 (Revised)*

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# Consideration of Laws and Regulations in an Audit of Financial Statements

## Including Related Conforming Amendments to Other International Standards



International Auditing  
and Assurance  
Standards Board

## About the IAASB

This document was developed and approved by the International Auditing and Assurance Standards Board.

The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

The IAASB develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the Public Interest Oversight Board, which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance. The structures and processes that support the operations of the IAASB are facilitated by the International Federation of Accountants (IFAC).

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# INTERNATIONAL STANDARD ON AUDITING 250 (REVISED)

## CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS

(Effective for audits of financial statements for periods beginning  
on or after December 15, 2009~~17~~)

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INTERNATIONAL STANDARD ON AUDITING 250 (REVISED)  
CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS

International Standard on Auditing (ISA) 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, should be read in conjunction with ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

ISA 250 (Revised) has received the approval of the Public Interest Oversight Board (PIOB) which concluded that due process was followed in the development of the standard and that proper regard was paid to the public interest.

## Introduction

### Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility to consider laws and regulations in an audit of financial statements. This ISA does not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific laws or regulations.

### Effect of Laws and Regulations

2. The effect on financial statements of laws and regulations varies considerably. Those laws and regulations to which an entity is subject constitute the legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the reported amounts and disclosures in an entity's financial statements. Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial statements. Some entities operate in heavily regulated industries (such as banks and chemical companies). Others are subject only to the many laws and regulations that relate generally to the operating aspects of the business (such as those related to occupational safety and health, and equal employment opportunity). Non-compliance with laws and regulations may result in fines, litigation or other consequences for the entity that may have a material effect on the financial statements.

### Responsibility for Compliance with Laws and Regulations (Ref: Para. A1–A68)

3. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.

### *Responsibility of the Auditor*

4. The requirements in this ISA are designed to assist the auditor in identifying material misstatement of the financial statements due to non-compliance with laws and regulations. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.
5. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether ~~caused by~~ due to fraud or error.<sup>1</sup> In conducting an audit of financial statements, the auditor takes into account the applicable legal and regulatory framework. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs.<sup>2</sup> In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:

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<sup>1</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph 5

<sup>2</sup> ISA 200, paragraphs A51–A52

There are many laws and regulations, relating principally to the operating aspects of an entity, that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting.

- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor.
- Whether an act constitutes non-compliance is ultimately a matter ~~for legal determination~~ to be determined by a court of law or other appropriate adjudicative body.

Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial statements, the less likely the auditor is to become aware of it or to recognize the non-compliance.

6. This ISA distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows: (Ref: Para. A6, A12–A13)
  - (a) The provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and pension laws and regulations (see paragraph ~~4314~~) (Ref: Para. A12); and
  - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties ~~(for example e.g.,~~ compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial statements (see paragraph ~~4415~~) (Ref: Para. A13).
7. In this ISA, differing requirements are specified for each of the above categories of laws and regulations. For the category referred to in paragraph 6(a), the auditor's responsibility is to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations. For the category referred to in paragraph 6(b), the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.
8. The auditor is required by this ISA to remain alert to the possibility that other audit procedures applied for the purpose of forming an opinion on financial statements may bring instances of ~~identified or suspected~~ non-compliance to the auditor's attention. Maintaining professional skepticism throughout the audit, as required by ISA 200,<sup>3</sup> is important in this context, given the extent of laws and regulations that affect the entity.
9. The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond this ISA, such as: (Ref: Para. A8)
  - (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with

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<sup>3</sup> ISA 200, paragraph 15

governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;

- (b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of group financial statements); and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other ISAs (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

### Effective Date

910. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 20092017.

### Objectives

110. The objectives of the auditor are:

- (a) To obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements;
- (b) To perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements; and
- (c) To respond appropriately to non-compliance identified or suspected non-compliance with laws and regulations identified during the audit.

### Definition

124. For the purposes of this ISA, the following term has the meaning attributed below:

Non-compliance – Acts of omission or commission ~~by the entity, either intentional or unintentional, committed by the entity, or by those charged with governance, by management or by other individuals working for or under the direction of the entity, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees.~~ Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) ~~by those charged with governance, management or employees of the entity.~~ (Ref: Para. A9–A10)

### Requirements

#### The Auditor's Consideration of Compliance with Laws and Regulations

132. As part of obtaining an understanding of the entity and its environment in accordance with ISA 315 (Revised),<sup>4</sup> the auditor shall obtain a general understanding of:

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<sup>4</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 11

- (a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and
  - (b) How the entity is complying with that framework. (Ref: Para. A711)
143. The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements. (Ref: Para. A128)
154. The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements: (Ref: Para. A139–A149)
- (a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and
  - (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.
165. During the audit, the auditor shall remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. (Ref: Para. A154)
176. The auditor shall request management and, where appropriate, those charged with governance, to provide written representations that all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor. (Ref: Para. A126)
187. In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than those set out in paragraphs 132–176.

#### **Audit Procedures When Non-Compliance Is Identified or Suspected**

198. If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain: (Ref: Para. A173–A18)
- (a) An understanding of the nature of the act and the circumstances in which it has occurred; and
  - (b) Further information to evaluate the possible effect on the financial statements. (Ref: Para. A194)
1920. If the auditor suspects there may be non-compliance, the auditor shall discuss the matter, unless prohibited by law or regulation, with the appropriate level of management and, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements, the auditor shall consider the need to obtain legal advice. (Ref: Para. A2045–A2246)
210. If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.

224. The auditor shall evaluate the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. (Ref: Para. A2347–A2548)

### **Communicating and Reporting of Identified or Suspected Non-Compliance**

#### **Communicating and Reporting Identified or Suspected Non-Compliance with Those Charged with Governance**

232. Unless all of those charged with governance are involved in management of the entity, and therefore are aware of matters involving identified or suspected non-compliance already communicated by the auditor,<sup>5</sup> the auditor shall communicate, unless prohibited by law or regulation, with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.
234. If, in the auditor's judgment, the non-compliance referred to in paragraph 232 is believed to be intentional and material, the auditor shall communicate the matter with those charged with governance as soon as practicable.
254. If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

#### **Potential Reporting Implications of Identified or Suspected Non-Compliance in the Auditor's Report on the Financial Statements** (Ref: Para. A26–A27)

265. If the auditor concludes that the identified or suspected non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall, in accordance with ISA 705 (Revised), express a qualified opinion or an adverse opinion on the financial statements.<sup>6</sup>
276. If the auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements on the basis of a limitation on the scope of the audit in accordance with ISA 705 (Revised).<sup>7</sup>
287. If the auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance, the auditor shall evaluate the effect on the auditor's opinion in accordance with ISA 705 (Revised).

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<sup>5</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 13

<sup>6</sup> ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*, paragraphs 7–8

<sup>7</sup> ISA 705 (Revised), paragraphs 7 and 9

*Reporting Identified or Suspected Non-Compliance to ~~Regulatory and Enforcement Authorities~~ an  
Appropriate Authority outside the Entity*

298. If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether law, regulation or relevant ethical requirements; ~~the auditor has a responsibility to report the identified or suspected non-compliance to parties outside the entity.~~ (Ref: Para. A2819–A3420)
- (a) Require the auditor to report to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

**Documentation**

2930. The auditor shall include in the audit documentation<sup>8</sup> identified or suspected non-compliance with laws and regulations and; ~~the results of discussion with management and, where applicable, those charged with governance and other parties outside the entity.~~<sup>9</sup> (Ref: Para. A3521–A36)
- (a) The audit procedures performed, the significant professional judgments made and the conclusions reached thereon; and
- (b) The discussions of significant matters related to the non-compliance with management, those charged with governance and others, including how management and, where applicable, those charged with governance have responded to the matter.

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**Application and Other Explanatory Material**

**Responsibility for Compliance with Laws and Regulations** (Ref: Para. 3–89)

- A1. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with laws and regulations. Laws and regulations may affect an entity's financial statements in different ways: for example, most directly, they may affect specific disclosures required of the entity in the financial statements or they may prescribe the applicable financial reporting framework. They may also establish certain legal rights and obligations of the entity, some of which will be recognized in the entity's financial statements. In addition, laws and regulations may impose penalties in cases of non-compliance.
- A2. The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations:
- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
  - Instituting and operating appropriate systems of internal control.
  - Developing, publicizing and following a code of conduct.
  - Ensuring employees are properly trained and understand the code of conduct.

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<sup>8</sup> ISA 230, *Audit Documentation*, paragraphs 8–11, and A6

<sup>9</sup> ISA 230, *Audit Documentation*, paragraphs 8–11, and A6

- Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
- Engaging legal advisors to assist in monitoring legal requirements.
- Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to the following:

- An internal audit function.
- An audit committee.
- A compliance function.

#### *Responsibility of the Auditor*

- A3. Non-compliance by the entity with laws and regulations may result in a material misstatement of the financial statements. Detection of non-compliance, regardless of materiality, may affect other aspects of the audit including, for example, the auditor's consideration of the integrity of management, those charged with governance or employees.
- A4. Whether an act constitutes non-compliance with laws and regulations is a matter ~~for legal determination~~ to be determined by a court or other appropriate adjudicative body, which is ordinarily beyond the auditor's professional competence to determine. Nevertheless, the auditor's training, experience and understanding of the entity and its industry or sector may provide a basis to recognize that some acts, coming to the auditor's attention, may constitute non-compliance with laws and regulations.
- A5. In accordance with specific statutory requirements, the auditor may be specifically required to report, as part of the audit of the financial statements, on whether the entity complies with certain provisions of laws or regulations. In these circumstances, ISA 700 (Revised)<sup>10</sup> or ISA 800 (Revised)<sup>11</sup> deal with how these audit responsibilities are addressed in the auditor's report. Furthermore, where there are specific statutory reporting requirements, it may be necessary for the audit plan to include appropriate tests for compliance with these provisions of the laws and regulations.

#### Categories of Laws and Regulations (Ref: Para. 6)

- A6. The nature and circumstances of the entity may impact whether relevant laws and regulations are within the categories of laws and regulations described in paragraphs 6(a) or 6(b). Examples of laws and regulations that may be included in the categories described in paragraph 6 include those that deal with:
- Fraud, corruption and bribery.
  - Money laundering, terrorist financing and proceeds of crime.
  - Securities markets and trading.

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<sup>10</sup> ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 4243

<sup>11</sup> ISA 800 (Revised), *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*, paragraph 11

- Banking and other financial products and services.
- Data protection.
- Tax and pension liabilities and payments.
- Environmental protection.
- Public health and safety.

#### Considerations Specific to Public Sector Entities

A67. In the public sector, there may be additional audit responsibilities with respect to the consideration of laws and regulations which may relate to the audit of financial statements or may extend to other aspects of the entity's operations.

#### Additional Responsibilities Established by Law, Regulation or Relevant Ethical Requirements (Ref: Para. 9)

A8. Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the *Code of Ethics for Professional Accountants* issued by the International Ethics Standards Board for Accountants (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.<sup>12</sup>

#### **Definition** (Ref: Para. 12)

A9. Acts of non-compliance with laws and regulations include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, by management or by other individuals working for or under the direction of the entity.

A10. Non-compliance also includes personal misconduct related to the business activities of the entity, for example, in circumstances where an individual in a key management position, in a personal capacity, has accepted a bribe from a supplier of the entity and in return secures the appointment of the supplier to provide services or contracts to the entity.

### **The Auditor's Consideration of Compliance with Laws and Regulations**

#### *Obtaining an Understanding of the Legal and Regulatory Framework* (Ref: Para. 132)

A117. To obtain a general understanding of the legal and regulatory framework, and how the entity complies with that framework, the auditor may, for example:

- Use the auditor's existing understanding of the entity's industry, regulatory and other external factors;
- Update the understanding of those laws and regulations that directly determine the reported amounts and disclosures in the financial statements;

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<sup>12</sup> See Sections 225.21–225.22 of the IESBA Code.

- Inquire of management as to other laws or regulations that may be expected to have a fundamental effect on the operations of the entity;
- Inquire of management concerning the entity's policies and procedures regarding compliance with laws and regulations; and
- Inquire of management regarding the policies or procedures adopted for identifying, evaluating and accounting for litigation claims.

*Laws and Regulations Generally Recognized to Have a Direct Effect on the Determination of Material Amounts and Disclosures in the Financial Statements (Ref: Para. ~~436~~, 14)*

A~~8~~12. Certain laws and regulations are well-established, known to the entity and within the entity's industry or sector, and relevant to the entity's financial statements (as described in paragraph 6(a)). They could include those that relate to, for example:

- The form and content of financial statements;
- Industry-specific financial reporting issues;
- Accounting for transactions under government contracts; or
- The accrual or recognition of expenses for income tax or pension costs.

Some provisions in those laws and regulations may be directly relevant to specific assertions in the financial statements (~~for example~~, e.g., the completeness of income tax provisions), while others may be directly relevant to the financial statements as a whole (~~for example~~, e.g., the required statements constituting a complete set of financial statements). The aim of the requirement in paragraph ~~43~~14 is for the auditor to obtain sufficient appropriate audit evidence regarding the determination of amounts and disclosures in the financial statements in compliance with the relevant provisions of those laws and regulations.

Non-compliance with other provisions of such laws and regulations and other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for in the financial statements, but are not considered to have a direct effect on the financial statements as described in paragraph 6(a).

*Procedures to Identify Instances of Non-Compliance—Other Laws and Regulations (Ref: Para. ~~446~~, 15)*

A~~13~~9. Certain other laws and regulations may need particular attention by the auditor because they have a fundamental effect on the operations of the entity (as described in paragraph 6(b)). Non-compliance with laws and regulations that have a fundamental effect on the operations of the entity may cause the entity to cease operations, or call into question the entity's continuance as a going concern.<sup>13</sup> For example, non-compliance with the requirements of the entity's license or other entitlement to perform its operations could have such an impact (~~e.g. for example~~, e.g., for a bank, non-compliance with capital or investment requirements). There are also many laws and regulations relating principally to the operating aspects of the entity that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting.

A~~14~~0. As the financial reporting consequences of other laws and regulations can vary depending on the entity's operations, the audit procedures required by paragraph ~~44~~15 are directed to bringing to the

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<sup>13</sup> See ISA 570 (Revised), *Going Concern*.

auditor's attention instances of non-compliance with laws and regulations that may have a material effect on the financial statements.

*Non-Compliance Brought to the Auditor's Attention by Other Audit Procedures* (Ref: Para. 4516)

A154. Audit procedures applied to form an opinion on the financial statements may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. For example, such audit procedures may include:

- Reading minutes;
- Inquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, claims and assessments; and
- Performing substantive tests of details of classes of transactions, account balances or disclosures.

*Written Representations* (Ref: Para. 4617)

A162. Because the effect on financial statements of laws and regulations can vary considerably, written representations provide necessary audit evidence about management's knowledge of identified or suspected non-compliance with laws and regulations, whose effects may have a material effect on the financial statements. However, written representations do not provide sufficient appropriate audit evidence on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained by the auditor.<sup>14</sup>

**Audit Procedures When Non-Compliance is Identified or Suspected**

*Indications of Non-Compliance with Laws and Regulations* (Ref: Para. 4819)

A17. The auditor may become aware of information concerning an instance of non-compliance with laws and regulations other than as a result of performing the procedures in paragraphs 13–17 (e.g., when the auditor is alerted to non-compliance by a whistle blower).

A183. ~~If the auditor becomes aware of the existence of, or information about,~~ The following matters, it may be an indication of non-compliance with laws and regulations:

- Investigations by regulatory organizations and government departments or payment of fines or penalties.
- Payments for unspecified services or loans to consultants, related parties, employees or government employees.
- Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the entity or in its industry or to the services actually received.
- Purchasing at prices significantly above or below market price.
- Unusual payments in cash, purchases in the form of cashiers' checks payable to bearer or transfers to numbered bank accounts.
- Unusual transactions with companies registered in tax havens.

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<sup>14</sup> ISA 580, *Written Representations*, paragraph 4

- Payments for goods or services made other than to the country from which the goods or services originated.
- Payments without proper exchange control documentation.
- Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.
- Unauthorized transactions or improperly recorded transactions.
- Adverse media comment.

*Matters Relevant to the Auditor's Evaluation (Ref: Para. 4819(b))*

A194. Matters relevant to the auditor's evaluation of the possible effect on the financial statements include:

- The potential financial consequences of identified or suspected non-compliance with laws and regulations on the financial statements including, for example, the imposition of fines, penalties, damages, threat of expropriation of assets, enforced discontinuation of operations, and litigation.
- Whether the potential financial consequences require disclosure.
- Whether the potential financial consequences are so serious as to call into question the fair presentation of the financial statements, or otherwise make the financial statements misleading.

*Audit Procedures and Communicating Identified or Suspected Non-Compliance with Management and Those Charged with Governance (Ref: Para. 4920)*

A2045. The auditor ~~may~~ is required to discuss the findings with suspected non-compliance with the appropriate level of management and, where appropriate, those charged with governance where, as they may be able to provide additional audit evidence. For example, the auditor may confirm that management and, where appropriate, those charged with governance have the same understanding of the facts and circumstances relevant to transactions or events that have led to the possibility of suspected non-compliance with laws and regulations.

A21. However, in some jurisdictions, law or regulation may restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice.

A2246. If management or, as appropriate, those charged with governance do not provide sufficient information to the auditor that the entity is in fact in compliance with laws and regulations, the auditor may consider it appropriate to consult with the entity's in-house ~~legal counsel~~ or external legal counsel about the application of the laws and regulations to the circumstances, including the possibility of fraud, and the possible effects on the financial statements. If it is not considered appropriate to consult with the entity's legal counsel or if the auditor is not satisfied with the legal counsel's opinion, the auditor may consider it appropriate to consult the auditor's own legal counsel on a confidential basis with others within the firm, a network firm, a professional body, or with the auditor's legal counsel as

to whether a contravention of a law or regulation is involved, ~~the possible legal consequences, including the possibility of fraud, the possible legal consequences,~~ and what further action, if any, the auditor would take.

*Evaluating the Implications of Identified or Suspected Non-Compliance (Ref: Para. 2422)*

A2347. As required by paragraph 2422, the auditor evaluates the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations. The implications of particular ~~instances of identified or suspected non-compliance identified by the auditor~~ will depend on the relationship of the perpetration and concealment, if any, of the act to specific control activities and the level of management or ~~employees~~ individuals working for, or under the direction of, the entity involved, especially implications arising from the involvement of the highest authority within the entity. As noted in paragraph 9, the auditor's compliance with law, regulation or relevant ethical requirements may provide further information that is relevant to the auditor's responsibilities in accordance with paragraph 22.

A24. Examples of circumstances that may cause the auditor to evaluate the implications of identified or suspected non-compliance on the reliability of written representations received from management and, where applicable, those charged with governance include when:

- The auditor suspects or has evidence of the involvement or intended involvement of management and, where applicable, those charged with governance in any identified or suspected non-compliance.
- The auditor is aware that management and, where applicable, those charged with governance have knowledge of such non-compliance and, contrary to legal or regulatory requirements, have not reported, or authorized reporting of, the matter to an appropriate authority within a reasonable period.

A4825. In ~~certain circumstances~~ exceptional cases, the auditor may consider ~~whether withdrawing~~ from the engagement, where ~~withdrawal is possible under applicable~~ permitted by law or regulation, for ~~example is necessary~~ when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances, or the identified or suspected non-compliance raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial statements. When deciding whether withdrawal from the engagement is necessary, the auditor may consider it appropriate to obtain seeking legal advice to determine whether withdrawal from the engagement is appropriate. If withdrawal from the engagement is not possible, the auditor may consider alternative actions, including describing the non-compliance in an Other Matter paragraph in the auditor's report.<sup>45</sup> When the auditor determines that withdrawing from the engagement would be appropriate, doing so would not be a substitute for complying with other responsibilities under law, regulation or relevant ethical requirements to respond to identified or suspected non-compliance. Furthermore, paragraph A8a of ISA 220<sup>16</sup> indicates that some ethical requirements may require the predecessor auditor, upon request by the proposed successor auditor, to provide information regarding non-compliance with laws and regulations to the successor auditor.

<sup>45</sup> — ISA 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*, paragraph 8

<sup>16</sup> — ISA 220, *Quality Control for an Audit of Financial Statements*

## **Communicating and Reporting of Identified or Suspected Non-Compliance**

*Potential Implications of Identified or Suspected Non-Compliance for the Auditor's Report* (Ref: Para. 26–28)

A26. Identified or suspected non-compliance with laws and regulation is communicated in the auditor's report when the auditor modifies the opinion in accordance with paragraphs 26–28. In certain other circumstances, the auditor may communicate identified or suspected non-compliance in the auditor's report, for example:

- When the auditor has other reporting responsibilities, in addition to the auditor's responsibilities under the ISAs, as contemplated by paragraph 43 of ISA 700 (Revised);
- When the auditor determines that the identified or suspected non-compliance is a key audit matter and accordingly communicates the matter in accordance with ISA 701,<sup>17</sup> unless paragraph 14 of that ISA applies; or
- In exceptional cases when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances and withdrawal from the engagement is not possible (see paragraph A25), the auditor may consider describing the identified or suspected non-compliance in an Other Matter paragraph in accordance with ISA 706 (Revised).<sup>18</sup>

A27. Law or regulation may preclude public disclosure by either management, those charged with governance or the auditor about a specific matter. For example, law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including a prohibition on alerting the entity. When the auditor intends to communicate identified or suspected non-compliance in the auditor's report under the circumstances set out in paragraph A26 or otherwise, such law or regulation may have implications for the auditor's ability to describe the matter in the auditor's report, or in some circumstances to issue the auditor's report. In such cases, the auditor may consider obtaining legal advice to determine the appropriate course of action.

*Reporting Identified or Suspected Non-Compliance to ~~Regulatory and Enforcement~~ an Appropriate Authority ~~ies~~ outside the Entity* (Ref: Para. 29~~8~~)

~~A19. The auditor's professional duty to maintain the confidentiality of client information may preclude reporting identified or suspected non-compliance with laws and regulations to a party outside the entity. However, the auditor's legal responsibilities vary by jurisdiction and, in certain circumstances, the duty of confidentiality may be overridden by statute, the law or courts of law. In some jurisdictions, the auditor of a financial institution has a statutory duty to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to supervisory authorities. Also, in some jurisdictions, the auditor has a duty to report misstatements to authorities in those cases where management and, where applicable, those charged with governance fail to take corrective action. The auditor may consider it appropriate to obtain legal advice to determine the appropriate course of action.~~

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<sup>17</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

<sup>18</sup> ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

- A28. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:
- (a) Law, regulation or relevant ethical requirements require the auditor to report (see paragraph A29);
  - (b) The auditor has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements (see paragraph A30); or
  - (c) Law, regulation or relevant ethical requirements provide the auditor with the right to do so (see paragraph A31).
- A29. In some jurisdictions, the auditor may be required by law, regulation or relevant ethical requirements to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity. For example, in some jurisdictions, statutory requirements exist for the auditor of a financial institution to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to a supervisory authority. Also, misstatements may arise from non-compliance with laws or regulations and, in some jurisdictions, the auditor may be required to report misstatements to an appropriate authority in cases where management or those charged with governance fail to take corrective action.
- A30. In other cases, the relevant ethical requirements may require the auditor to determine whether reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the IESBA Code requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed, which may include reporting to an appropriate authority outside the entity.<sup>19</sup> The IESBA Code explains that such reporting would not be considered a breach of the duty of confidentiality under the IESBA Code.<sup>20</sup>
- A31. Even if law, regulation or relevant ethical requirements do not include requirements that address reporting identified or suspected non-compliance, they may provide the auditor with the right to report identified or suspected non-compliance to an appropriate authority outside the entity. For example, when auditing the financial statements of financial institutions, the auditor may have the right under law or regulation to discuss matters such as identified or suspected non-compliance with laws and regulations with a supervisory authority.
- A32. In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the auditor's duty of confidentiality under law, regulation or relevant ethical requirements.
- A33. The determination required by paragraph 29 may involve complex considerations and professional judgments. Accordingly the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular course of action.

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<sup>19</sup> See, for example, Section 225.29 and Sections 225.33–225.36 of the IESBA Code.

<sup>20</sup> See, for example, Section 140.7 and Section 225.35 of the IESBA Code.

### Considerations Specific to Public Sector Entities

~~A3420.~~ A public sector auditor may be obliged to report on ~~instances of~~identified or suspected non-compliance to the legislature or other governing body or to report them in the auditor's report.

### **Documentation** (Ref: Para. ~~2930~~)

~~A3524.~~ The auditor's documentation of findings regarding identified or suspected non-compliance with laws and regulations may include, for example:

- Copies of records or documents.
- Minutes of discussions held with management, those charged with governance or parties outside the entity.

A36. Law, regulation or relevant ethical requirements may also set out additional documentation requirements regarding identified or suspected non-compliance with laws and regulations.<sup>21</sup>

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<sup>21</sup> See, for example, Section 225.37 of the IESBA Code.

## CONFORMING AMENDMENTS TO OTHER INTERNATIONAL STANDARDS

**Note:** The following are conforming amendments to other International Standards as a result of the approval of ISA 250 (Revised). These amendments will become effective at the same time as ISA 250 (Revised), and are shown with marked changes from the latest approved versions of the International Standards that are amended. The footnote numbers within these amendments do not align with the International Standards that are amended, and reference should be made to those International Standards. These conforming amendments have received the approval of the PIOB which concluded that due process was followed in the development of the conforming amendments and that proper regard was paid to the public interest.

### ***ISQC 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements***

#### **Application and Other Explanatory Material**

Confidentiality, Safe Custody, Integrity, Accessibility and Retrievability of Engagement Documentation  
(Ref: Para. 46)

A56. Relevant ethical requirements establish an obligation for the firm's personnel to observe at all times the confidentiality of information contained in engagement documentation, unless specific client authority has been given to disclose information, or there are responsibilities under law, regulation or relevant ethical requirements ~~is a legal or professional duty~~ to do so.<sup>22</sup> Specific laws or regulations may impose additional obligations on the firm's personnel to maintain client confidentiality, particularly where data of a personal nature are concerned.

### ***ISA 210, Agreeing the Terms of Audit Engagements***

#### **Application and Other Explanatory Material**

##### **Agreement on Audit Engagement Terms**

A24. When relevant, the following points could also be made in the audit engagement letter:

- Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.
- Arrangements concerning the involvement of internal auditors and other staff of the entity.
- Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit.
- A reference to, and description of, the auditor's responsibilities under law, regulation or relevant ethical requirements that address reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
- Any restriction of the auditor's liability when such possibility exists.
- A reference to any further agreements between the auditor and the entity.
- Any obligations to provide audit working papers to other parties.

An example of an audit engagement letter is set out in Appendix 1.

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<sup>22</sup> See, for example, Section 140.7 and Section 225.35 of the IESBA Code.

## **ISA 220, *Quality Control for an Audit of Financial Statements***

### **Application and Other Explanatory Material**

#### **Acceptance and Continuance of Client Relationships and Audit Engagements (Ref: Para. 12)**

A8a. Law, regulation, or relevant ethical requirements<sup>23</sup> may require the auditor to request, prior to accepting the engagement, the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's judgment, the auditor needs to be aware of before deciding whether to accept the engagement. In some circumstances, the predecessor auditor may be required, on request by the proposed successor auditor, to provide information regarding identified or suspected non-compliance with laws and regulations to the proposed successor auditor. For example, where the predecessor auditor has withdrawn from the engagement as a result of identified or suspected non-compliance with laws and regulations, the IESBA Code requires that the predecessor auditor, on request by a proposed successor auditor, provides all such facts and other information concerning such non-compliance that, in the predecessor auditor's opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.<sup>24</sup>

## **ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements***

### **Introduction**

#### **Responsibility for the Prevention and Detection of Fraud**

##### *Responsibilities of the Auditor*

8a. The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this and other ISAs, such as: (Ref: Para. A5a)

- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;
- (b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of group financial statements); and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other ISAs (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

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<sup>23</sup> See, for example, Sections 210.14 of the IESBA Code.

<sup>24</sup> See, for example, Sections 225.31 of the IESBA Code.

## Requirements

### Communications to Management and with Those Charged with Governance

40. If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor shall communicate these matters, unless prohibited by law or regulation, on a timely basis ~~with~~to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities. (Ref: Para. A59a–A60)
41. Unless all of those charged with governance are involved in managing the entity, if the auditor has identified or suspects fraud involving:
- (a) management;
  - (b) employees who have significant roles in internal control; or
  - (c) others where the fraud results in a material misstatement in the financial statements,
- the auditor shall communicate these matters ~~with~~to those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions ~~with~~to those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit. Such communications with those charged with governance are required unless the communication is prohibited by law or regulation. (Ref: Para. A59a, A61–A63)
42. The auditor shall communicate, unless prohibited by law or regulation, with those charged with governance any other matters related to fraud that are, in the auditor's judgment, relevant to their responsibilities. (Ref: Para. A59a, A64)

### ~~Communications to Regulatory and Enforcement Authorities~~Reporting Fraud to an Appropriate Authority Outside the Entity

43. If the auditor has identified or suspects a fraud, the auditor shall determine whether law, regulation or relevant ethical requirements~~there is a responsibility to report the occurrence or suspicion to a party outside the entity. Although the auditor's professional duty to maintain the confidentiality of client information may preclude such reporting, the auditor's legal responsibilities may override the duty of confidentiality in some circumstances.~~ (Ref: Para. A65–A67)
- (a) Require the auditor to report to an appropriate authority outside the entity.
  - (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

## Application and Other Explanatory Material

### Responsibility for the Prevention and Detection of Fraud

*Responsibilities of the Auditor* (Ref: Para. 8a)

A5a. Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the *Code of Ethics for Professional Accountants* issued by the International Ethics Standards Board for Accountants (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group,

including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.<sup>25</sup>

### **Communications to Management and with Those Charged with Governance (Ref: Para. 40–42)**

A59a. In some jurisdictions, law or regulation may restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the fraud to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice.

### **~~Communications to Regulatory and Enforcement Authorities~~ Reporting Fraud to an Appropriate Authority outside the Entity (Ref: Para. 43)**

A65. ISA 250 (Revised)<sup>26</sup> provides further guidance with respect to the auditor's determination of whether reporting identified or suspected non-compliance with laws or regulations to an appropriate authority outside the entity is required or appropriate in the circumstances, including consideration of the auditor's duty of confidentiality. The auditor's professional duty to maintain the confidentiality of client information may preclude reporting fraud to a party outside the client entity. However, the auditor's legal responsibilities vary by country and, in certain circumstances, the duty of confidentiality may be overridden by statute, the law or courts of law. In some countries, the auditor of a financial institution has a statutory duty to report the occurrence of fraud to supervisory authorities. Also, in some countries the auditor has a duty to report misstatements to authorities in those cases where management and those charged with governance fail to take corrective action.

A66. The determination required by paragraph 43 may involve complex considerations and professional judgments. Accordingly, tThe auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider it appropriate to obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular determine the appropriate course of action in the circumstances, the purpose of which is to ascertain the steps necessary in considering the public interest aspects of identified fraud.

## **ISA 260 (Revised), *Communication with Those Charged with Governance***

### **Introduction**

#### **The Role of Communication**

7. In some jurisdictions, Llaw or regulation may restrict the auditor's communication of certain matters with those charged with governance. For example, lLaws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report identified or suspected non-compliance with laws and regulations to an appropriate

<sup>25</sup> See Sections 225.21–225.22 of the IESBA Code.

<sup>26</sup> ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraphs A28–A34

authority pursuant to anti-money laundering legislation. In some these circumstances, the issues considered by the auditor potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, and the auditor may consider it appropriate to obtaining legal advice.

## **ISA 450, *Evaluation of Misstatements Identified During the Audit***

### **Requirements**

#### **Communication and Correction of Misstatements**

8. The auditor shall communicate, unless prohibited by law or regulation, on a timely basis all misstatements accumulated during the audit with the appropriate level of management, ~~unless prohibited by law or regulation.~~<sup>27</sup> The auditor shall request management to correct those misstatements. (Ref: Para. A7–A9)

### **Application and Other Explanatory Material**

#### **Communication and Correction of Misstatements** (Ref: Para. 8–9)

- A8. In some jurisdictions, Law or regulation may restrict the auditor's communication of certain misstatements to management, or others, within the entity. For example, Laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report identified or suspected non-compliance with law or regulation to an appropriate authority pursuant to anti-money laundering legislation. In some these circumstances, potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, the issues considered by the auditor may be complex and the auditor may consider seeking it appropriate to obtain legal advice.

## **ISA 500, *Audit Evidence***

### **Requirements**

#### **Information to Be Used as Audit Evidence**

7. When designing and performing audit procedures, the auditor shall consider the relevance and reliability of the information to be used as audit evidence. (Ref: Para. A26–A33a)

### **Application and Other Explanatory Material**

#### **Information to Be Used as Audit Evidence**

##### *Relevance and Reliability* (Ref: Para. 7)

- A26. As noted in paragraph A1, while audit evidence is primarily obtained from audit procedures performed during the course of the audit, it may also include information obtained from other sources such as, for example, previous audits, in certain circumstances, ~~and a firm's quality control procedures for client acceptance and continuance~~ and complying with certain additional responsibilities under law, regulation or relevant ethical requirements (e.g., regarding an entity's non-compliance with laws and regulations). The quality of all audit evidence is affected by the relevance and reliability of the information upon which it is based.

<sup>27</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 7

A33a. ISA 250 (Revised)<sup>28</sup> provides further guidance with respect to the auditor complying with any additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's identified or suspected non-compliance with laws and regulations that may provide further information that is relevant to the auditor's work in accordance with ISAs and evaluating the implications of such non-compliance in relation to other aspects of the audit.

## **ISRE 2400 (Revised), *Engagements to Review Historical Financial Statements***

### **Requirements**

#### **Performing the Engagement**

##### *Designing and Performing Procedures*

48. The practitioner's inquiries of management and others within the entity, as appropriate, shall include the following: (Ref: Para. A84–A87a)

...

- (d) The existence of any actual, suspected or alleged:
  - (i) Fraud or illegal acts affecting the entity; and
  - (ii) Non-compliance with provisions of laws and regulations that are generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements, such as tax and pension laws and regulations;

##### Fraud and non-compliance with laws ~~and~~ regulations

52. When there is an indication that fraud or non-compliance with laws ~~and~~ regulations, or suspected fraud or non-compliance with laws ~~and~~ regulations, has occurred in the entity, the practitioner shall:
- (a) Communicate that matter, unless prohibited by law or regulation, with to the appropriate level of senior management or those charged with governance as appropriate; (Ref: Para. A91a)
  - (b) Request management's assessment of the effect(s), if any, on the financial statements;
  - (c) Consider the effect, if any, of management's assessment of the effects of identified or suspected fraud or non-compliance with laws ~~and~~ regulations communicated to the practitioner on the practitioner's conclusion on the financial statements and on the practitioner's report; and
  - (d) Determine whether law, regulation or relevant ethical requirements; there is a responsibility to report the occurrence or suspicion of fraud or illegal acts to a party outside the entity. (Ref: Para. A92–A92d)
    - (i) Require the practitioner to report to an appropriate authority outside the entity.
    - (ii) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

<sup>28</sup> ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraph 9

## Application and Other Explanatory Material

### Performing the Engagement

*Designing and Performing Procedures* (Ref: Para. 47, 55)

*Inquiry* (Ref: Para. 46–48)

A87a. The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, including fraud, which may differ from or go beyond this ISRE, such as:

- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;
- (b) Communicating identified or suspected non-compliance with laws and regulations to an auditor, for example a group engagement partner;<sup>29</sup> and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this ISRE (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

### Procedures to Address Specific Circumstances

*Fraud and non-compliance with laws and regulations* (Ref: Para. 52(a) and (d))

Communication with management and those charged with governance

A91a. In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report identified or suspected non-compliance with laws and regulations to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may be complex and the practitioner may consider it appropriate to obtain legal advice.

Reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity

A92. ~~Under this ISRE, if the practitioner has identified or suspects fraud or illegal acts, the practitioner is required to determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity.~~ Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

- (a) Law, regulation or relevant ethical requirements require the practitioner to report;
- (b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements (see paragraph A92a); or

<sup>29</sup> See, for example, Sections 225.44–225.48 of the IESBA Code.

- (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so (see paragraph A92b).

~~Although the practitioner's professional duty to maintain the confidentiality of client information may preclude such reporting, the practitioner's legal responsibilities may override the duty of confidentiality in some circumstances.~~

A92a. In some cases, the relevant ethical requirements may require the practitioner to report or to consider whether reporting identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the IESBA Code requires the practitioner to take steps to respond to identified or suspected non-compliance with laws and regulations, and consider whether further action is needed, which may include reporting to an appropriate authority outside the entity.<sup>30</sup> The IESBA Code explains that such reporting would not be considered a breach of the duty of confidentiality under the IESBA Code.<sup>31</sup>

A92b. Even if law, regulation or relevant ethical requirements do not include requirements that address reporting identified or suspected non-compliance, they may provide the practitioner with the right to report identified or suspected fraud or non-compliance with laws and regulations to an appropriate authority outside the entity.

A92c. In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation or relevant ethical requirements.

A92d. The determination required by paragraph 52(d) may involve complex considerations and professional judgments. Accordingly, the practitioner may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The practitioner may also consider obtaining legal advice to understand the practitioner's options and the professional or legal implications of taking any particular course of action.

## **ISAE 3000 (Revised), Assurance Engagements other than Audits or Reviews of Historical Financial Information**

### **Requirements**

#### **Planning and Performing the Engagement**

##### *Understanding the Underlying Subject Matter and Other Engagement Circumstances*

45. The practitioner shall make inquiries of the appropriate party(ies) regarding:
- (a) Whether they have knowledge of any actual, suspected or alleged intentional misstatement or non-compliance with laws and regulations affecting the subject matter information; (Ref: Para. A101–A101a)
  - (b) Whether the responsible party has an internal audit function and, if so, make further inquiries to obtain an understanding of the activities and main findings of the internal audit function with respect to the subject matter information; and

<sup>30</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.

<sup>31</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.

- (c) Whether the responsible party has used any experts in the preparation of the subject matter information.

### **Other Communication Responsibilities**

78. The practitioner shall consider whether, pursuant to the terms of the engagement and other engagement circumstances, any matter has come to the attention of the practitioner that is to be communicated with the responsible party, the measurer or evaluator, the engaging party, those charged with governance or others. (Ref: Para. A192–A192f)

## **Application and Other Explanatory Material**

### **Planning and Performing the Engagement**

*Understanding the Engagement Circumstances* (Ref: Para. 45–47R)

A101a. The practitioner may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond the practitioner's responsibilities under this ISAE, such as:

- (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance and considering whether further action is needed;
- (b) Communicating identified or suspected non-compliance with laws and regulations to an auditor;<sup>32</sup> and
- (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

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Complying with any additional responsibilities may provide further information that is relevant to the practitioner's work in accordance with this and any other ISAE (e.g., regarding the integrity of the responsible party or those charged with governance). Paragraphs A192a–A192e further address the practitioner's responsibilities under law, regulation or relevant ethical requirements regarding communicating and reporting identified or suspected non-compliance with laws and regulations.

### **Other Communication Responsibilities** (Ref: Para. 78)

*Communication with Management and Those Charged with Governance*

A192a. Relevant ethical requirements may include a requirement to report identified or suspected non-compliance with laws and regulations to an appropriate level of management or those charged with governance. In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with the responsible party, management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may be complex and the practitioner may consider it appropriate to obtain legal advice.

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<sup>32</sup> See, for example, Sections 225.44–225.48 of the IESBA Code.

Reporting of Identified or Suspected Non-Compliance with Laws and Regulations to an Appropriate Authority outside the Entity

A192b. Law, regulation or relevant ethical requirements may:

- (a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>33</sup>

A192c. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

- (a) Law, regulation or relevant ethical requirements require the practitioner to report;
- (b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements; or,
- (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.

A192d. The reporting of identified or suspected non-compliance with laws and regulations in accordance with law, regulation or relevant ethical requirements may include non-compliance with laws and regulations that the practitioner comes across or is made aware of when performing the engagement but which may not affect the subject matter information. Under this ISAE, the practitioner is not expected to have a level of understanding of laws and regulations beyond those affecting the subject matter information. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgment and expertise in responding to such non-compliance. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

A192e. In some circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation, or relevant ethical requirements. In other cases, reporting identified or suspected non-compliance to an appropriate authority outside the entity would not be considered a breach of the duty of confidentiality under the relevant ethical requirements.<sup>34</sup>

A192f. The practitioner may consider consulting internally (e.g., within the firm or network firm), obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulations or would breach the duty of confidentiality).<sup>35</sup>

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<sup>33</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.

<sup>34</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.

<sup>35</sup> See, for example, Section 225.55 of the IESBA Code.

## **ISAE 3402, *Assurance Reports on Controls at a Service Organization***

### **Requirements**

#### **Other Communication Responsibilities**

56. If the service auditor becomes aware of non-compliance with laws and regulations, fraud, or uncorrected errors attributable to the service organization that are not clearly trivial and may affect one or more user entities, the service auditor shall determine whether the matter has been communicated appropriately to affected user entities. If the matter has not been so communicated and the service organization is unwilling to do so, the service auditor shall take appropriate action. (Ref: Para. A53)

### **Application and Other Explanatory Material**

#### **Other Communication Responsibilities (Ref: Para. 56)**

A53. Appropriate actions to respond to the circumstances identified in paragraph 56, unless prohibited by law or regulation, may include:

- Obtaining legal advice about the consequences of different courses of action.
- Communicating with those charged with governance of the service organization.
- Determining whether to communicate with third parties (e.g., law, regulation or relevant ethical requirements may require the service auditor to report to an appropriate authority outside the entity or the external auditor of the service organization,<sup>36</sup> or establish responsibilities under which such reporting may be appropriate in the circumstances). ~~Communicating with third parties (for example, a regulator) when required to do so.~~
- Modifying the service auditor's opinion, or adding an Other Matter paragraph.
- Withdrawing from the engagement.

## **ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements***

### **Requirements**

#### **Other Communication Responsibilities**

78. The practitioner shall communicate, unless prohibited by law or regulation, ~~with~~ to those person(s) with oversight responsibilities for the GHG statement the following matters that come to the practitioner's attention during the course of the engagement, and shall determine whether there is a responsibility to report them to another party within or outside the entity:
- (a) Deficiencies in internal control that, in the practitioner's professional judgment, are of sufficient importance to merit attention;
  - (b) Identified or suspected fraud; and
  - (c) Matters involving identified or suspected non-compliance with laws and/or regulations, other than when the matters are clearly trivial. (Ref: Para. A87)

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<sup>36</sup> See, for example, Section 225.44 to 225.48 of the IESBA Code.

## ISRS 4410 (Revised), *Compilation Engagements*

### Requirements

#### Ethical Requirements

21. The practitioner shall comply with relevant ethical requirements. (Ref: Para. A19–A21~~e~~)

#### Communication with Management and Those Charged with Governance

27. The practitioner shall communicate with management or those charged with governance, as appropriate, on a timely basis during the course of the compilation engagement, all matters concerning the compilation engagement that, in the practitioner's professional judgment, are of sufficient importance to merit the attention of management or those charged with governance, as appropriate. (Ref: Para. A41–A41~~a~~)

#### Ethical Requirements (Ref: Para. 21)

##### Reporting of Identified or Suspected Non-Compliance with Laws and Regulations to an Appropriate Authority outside the Entity

A21a. Law, regulation or relevant ethical requirements may:

- (a) Require the practitioner to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.<sup>37</sup>

A21b. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

- (a) Law, regulation or relevant ethical requirements require the practitioner to report;
- (b) The practitioner has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements; or
- (c) Law, regulation or relevant ethical requirements provide the practitioner with the right to do so.

A21c. Under paragraph 28 of this ISRS, the practitioner is not expected to have a level of understanding of laws and regulations beyond that necessary to be able to perform the compilation engagement. However, law, regulation or relevant ethical requirements may expect the practitioner to apply knowledge, professional judgment and expertise in responding to identified or suspected non-compliance. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

A21d. In some circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the practitioner's duty of confidentiality under law, regulation or relevant ethical requirements. In other cases, reporting

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<sup>37</sup> See, for example, Section 225.51 to 225.52 of the IESBA Code.

identified or suspected non-compliance to an appropriate authority outside the entity would not be considered a breach of the duty of confidentiality under the relevant ethical requirements.<sup>38</sup>

A21e. The practitioner may consider consulting internally (e.g., within the firm or network firm), obtaining legal advice to understand the professional or legal implications of taking any particular course of action, or consulting on a confidential basis with a regulator or a professional body (unless doing so is prohibited by law or regulations or would breach the duty of confidentiality).<sup>39</sup>

**Communication with Management and Those Charged with Governance (Ref: Para. 27)**

A41a. Relevant ethical requirements may include a requirement to report identified or suspected non-compliance with laws and regulations to an appropriate level of management or those charged with governance. In some jurisdictions, law or regulation may restrict the practitioner's communication of certain matters with management or those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the practitioner is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the practitioner may be complex and the practitioner may consider it appropriate to obtain legal advice.

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<sup>38</sup> See, for example, Section 140.7 and Section 225.53 of the IESBA Code.

<sup>39</sup> See, for example, Section 225.55 of the IESBA Code.



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**Basis for Conclusions**  
**Prepared by the Staff of the IAASB**  
*October 2016*

*International Standard on Auditing 250 (Revised)*

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# Consideration of Laws and Regulations in an Audit of Financial Statements

## Including Related Conforming Amendments to Other International Standards

**IAASB**

International Auditing  
and Assurance  
Standards Board

## About the IAASB

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The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related services standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

The IAASB develops auditing and assurance standards and guidance for use by all professional accountants under a shared standard-setting process involving the Public Interest Oversight Board, which oversees the activities of the IAASB, and the IAASB Consultative Advisory Group, which provides public interest input into the development of the standards and guidance. The structures and processes that support the operations of the IAASB are facilitated by the International Federation of Accountants (IFAC).

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# **BASIS FOR CONCLUSIONS: ISA 250 (REVISED), CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS, INCLUDING RELATED CONFORMING AMENDMENTS TO OTHER INTERNATIONAL STANDARDS<sup>1</sup>**

This Basis for Conclusions has been prepared by Staff of the International Auditing and Assurance Standards Board (IAASB). It relates to, but does not form part of, ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, or the related conforming amendments to other International Standards.

ISA 250 (Revised) was approved with the affirmative votes of 16 out of 18 IAASB members present for the vote at the June 2016 meeting.<sup>2</sup> The related conforming amendments to other International Standards were approved with the affirmative votes of 15 out of 18 IAASB members present for the vote at the June 2016 meeting.<sup>3</sup>

## **Background**

1. This project was initiated in response to the need to make amendments to ISA 250 and certain other International Standards as a result of the International Ethics Standards Board for Accountants (IESBA's) project regarding non-compliance with laws and regulations (NOCLAR). The objective of the project was to address actual or perceived inconsistencies of the approach to identifying and dealing with instances of identified or suspected NOCLAR between the International Standards and the IESBA's *Code of Ethics for Professional Accountants* (the IESBA Code), as it is in the public interest that the International Standards and the IESBA Code are able to operate mutually and without confusion.

## **Background to the IESBA NOCLAR Project**

2. In providing a professional service to an entity, a professional accountant (including an auditor or an assurance practitioner)<sup>4</sup> may come across an act or suspected act of NOCLAR committed (or about to be committed) by the entity, by those charged with governance, by management, or by other individuals working for or under the direction of the entity. The IESBA noted that the professional accountant has a prima facie ethical responsibility not to turn a blind eye to the matter and recognized that such a situation could often be difficult and stressful for the professional accountant. Accordingly, the IESBA approved a project in 2010 to develop enhancements to the IESBA Code to help guide professional accountants in dealing with circumstances when NOCLAR is identified or suspected, and in deciding how best to act in the public interest in these circumstances.

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<sup>1</sup> The IAASB's International Standards comprise the International Standards on Auditing (ISAs), the International Standards on Review Engagements (ISREs), the International Standards on Assurance Engagements (ISAEs), and the International Standards on Related Services (ISRSs).

<sup>2</sup> For a full record of the voting on ISA 250 (Revised), including the rationale of the IAASB members who abstained from the vote, see the [minutes of the June 21–24 2016 IAASB meeting](#).

<sup>3</sup> For a full record of the voting on the conforming amendments, including the rationale of the IAASB members who abstained from the vote or voted against the conforming amendments, see the [minutes of the June 21–24 2016 IAASB meeting](#).

<sup>4</sup> Henceforth, the term "auditor" is used within this Basis for Conclusions to include auditors of financial statements and the term "practitioner" is used to include other assurance practitioners.

3. After two exposure drafts (EDs),<sup>5</sup> and after taking into consideration and responding to stakeholder feedback to the IESBA Re-Exposure Draft (IESBA Re-ED), the IESBA [approved](#) changes to the IESBA Code addressing NOCLAR at its April 2016 meeting, with an effective date of July 15, 2017 (i.e., effective for addressing instances of NOCLAR that come to the professional accountant's attention on or after July 15, 2017).
4. The revised IESBA Code sets out a framework for professional accountants to respond to identified or suspected NOCLAR, including consideration as to whether identified or suspected NOCLAR should be disclosed to an appropriate authority. This framework encompasses many other considerations and actions; these include obtaining an understanding of the matter, discussing the matter with management, and, when appropriate, those charged with governance, and assessing the appropriateness of their response, and determining whether further action is needed in the public interest (e.g., reporting to an appropriate authority or withdrawal from the engagement).

### **Background to the IAASB's NOCLAR Project**

5. The IAASB was kept apprised of developments on the IESBA's NOCLAR project through updates and discussions at IAASB meetings as the IESBA's NOCLAR project progressed. The IAASB considered the IESBA's efforts to address NOCLAR and noted that the changes proposed by the IESBA would represent a fundamental change in the approach to confidentiality under the IESBA Code in this area. Furthermore, the IESBA NOCLAR proposals included examples of laws and regulations that were more diverse than those described in extant ISA 250 and specifically referred to NOCLAR that may occur. Accordingly, the IAASB concluded that certain of the International Standards, in particular ISA 250, could be enhanced to give more attention to the additional responsibilities of the auditor or practitioner under the revised IESBA Code when NOCLAR is identified or suspected. The IAASB also thought it would be helpful within the International Standards to highlight the IESBA's view that, when disclosure of identified or suspected NOCLAR to an appropriate authority is an appropriate course of action in the circumstances, this is not considered a breach of the duty of confidentiality under Section 140 of the IESBA Code.
6. Accordingly, in June 2015 the IAASB [approved a project](#) to address actual or perceived inconsistencies of the approach to identifying and dealing with instances of identified or suspected NOCLAR in complying with ISA 250 and other International Standards when the IESBA Code also applies. While the IAASB believed that failing to address such actual or perceived inconsistencies may raise questions among stakeholders regarding the clarity of the interaction between the International Standards and the IESBA Code; the IAASB concluded that only limited amendments to its standards would be necessary. The IAASB accelerated this work so that its ED would be out for public comment at the same time as the IESBA's re-ED, in order for respondents to consider the implications of both proposals concurrently, and so that the respective Boards could finalize their proposals on a similar timeline. To further facilitate the liaison during this time, the IAASB's NOCLAR Task Force included the Chair of the IESBA NOCLAR project, and the IESBA's NOCLAR Task Force included the Chair of the IAASB NOCLAR project.
7. The IAASB's NOCLAR ED, [Responding to Non-Compliance or Suspected Non-Compliance with Laws and Regulations](#) (ED-ISA 250), was released for public exposure in July 2015 and the comment period closed on October 20, 2015. Forty-five (45) comment letters were received from various

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<sup>5</sup> The IESBA released the first ED, *Responding to a Suspected Illegal Act*, in August 2012, and issued a Re-ED, *Responding to Non-Compliance with Laws & Regulations*, in May 2015.

respondents, including regulators and oversight bodies, national auditing standard setters, accounting firms, public sector organizations, IFAC member bodies, representatives of small and medium practices and other professional organizations. Included in the responses were two responses from Monitoring Group members.<sup>6</sup>

8. The IAASB discussed this project with its Consultative Advisory Group (CAG) on three separate occasions. In addition, the IAASB liaised closely with the IESBA in the finalization of the respective projects.
9. This Basis for Conclusions explains the significant issues raised by respondents to ED-ISA 250, and how the IAASB has addressed them.

## **Significant Matters**

### **Public Interest Issues Addressed by This Project**

10. The IAASB believes that it is in the public interest that its International Standards and the IESBA Code are able to operate mutually and without confusion due to the many jurisdictions that have adopted both. It is also important that the International Standards acknowledge and do not potentially undermine the enhancements to the IESBA Code in respect of NOCLAR — either through being inconsistent or failing to draw appropriate attention to the revised requirements in the IESBA Code. Equally, it would not be in the public interest for auditors and practitioners to be placed in a situation where the IESBA Code requires a response but the International Standards, either in the requirements or the application material, do not support or recognize that response.

### **Nature and Extent of Changes from Extant ISA 250**

11. As recommended in the project proposal, the limited amendments to ISA 250 (Revised) were not intended to explicitly duplicate all the specific requirements in the revised IESBA Code. This approach allows for flexibility when ethical codes other than the IESBA Code are applied and minimizes the amount of material that was necessary to incorporate into ISA 250 (Revised) and other International Standards. This approach is consistent with how reference was made in ISA 260 (Revised)<sup>7</sup> to the requirements in the IESBA Code to communicate with those charged with governance about breaches of independence.
12. In summary, the significant changes to ISA 250 (Revised) included in the final pronouncement are intended to:
  - Align aspects of ISA 250 (Revised) to the NOCLAR provisions in the IESBA Code, particularly the definition of non-compliance and the examples of laws and regulations within the scope of ISA 250 (Revised) (see paragraphs 12, A6 and A9–A10 of ISA 250 (Revised)).
  - Clarify the requirement regarding the auditor's determination of whether to report identified or suspected NOCLAR to an appropriate authority outside the entity and the auditor's duty of

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<sup>6</sup> The Monitoring Group comprises the Basel Committee on Banking Supervision (BCBS), the European Commission (EC), the Financial Stability Board (FSB), the International Association of Insurance Supervisors (IAIS), the International Forum of Independent Audit Regulators (IFIAR), the International Organization of Securities Organizations (IOSCO), and the World Bank. IFIAR and IOSCO responded to the IAASB's ED.

<sup>7</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*

confidentiality, in order to recognize the different provisions of laws, regulations, or relevant ethical requirements (see paragraphs 29 and A28–A34 of ISA 250 (Revised)).

- Highlight that the auditor may have additional responsibilities under law, regulation, or relevant ethical requirements regarding identified or suspected NOCLAR. This also includes additional emphasis of the possible documentation requirements contained in law, regulation or relevant ethical requirements (see paragraph 9 of ISA 250 (Revised)).
  - Highlight the implications of identified or suspected NOCLAR on the audit, for example, the reliability of management's representations, the implications for the auditor's report, and the consideration of whether to withdraw from the engagement (see paragraphs 22 and A23–A27 of ISA 250 (Revised)).
  - Emphasize the requirements in the IESBA Code relating to the communication of identified or suspected NOCLAR to a group engagement partner or an auditor at a component (see paragraph A8 of ISA 250 (Revised)).
  - Draw attention to the fact that, in certain cases, communication with management or those charged with governance may be restricted or prohibited by law or regulation, for example law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act (see paragraphs 20, 23 and A21 of ISA 250 (Revised)).
13. Furthermore, conforming amendments were also made to a number of other International Standards<sup>8</sup> to reflect the matters indicated above or clarify the expected work effort with regard to identified or suspected NOCLAR.
14. For example, new application material has been included in ISA 220 to reflect the communication between predecessor and proposed successor auditors as contemplated in the revised IESBA Code, that is, the requirement that the predecessor auditor, upon request by the proposed successor auditor, will (i) provide known information regarding any facts or circumstances that, in the predecessor auditor's judgment, the successor auditor needs to be aware of before deciding whether to accept the engagement, and (ii) inform the successor auditor of identified or suspected NOCLAR when the predecessor auditor resigns from the engagement as a result of such NOCLAR.

#### *Summary of Overall Comments Received on Exposure*

15. Overall, many respondents were supportive of the IAASB's efforts to address actual or perceived inconsistencies in the approach to responding to identified or suspected NOCLAR between the International Standards and the IESBA NOCLAR Re-ED.

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<sup>8</sup> These include ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*; ISA 210, *Agreeing the Terms of Audit Engagements*; ISA 220, *Quality Control for an Audit of Financial Statements*; ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, ISA 260 (Revised); ISA 450, *Evaluation of Misstatements Identified during the Audit*; ISA 500, *Audit Evidence*; ISRE 2400 (Revised), *Engagements to Review Historical Financial Statements*; ISAE 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*; ISAE 3402, *Assurance Reports on Controls at a Service Organization*; ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements*; and ISRS 4410 (Revised), *Compilation Engagements*.

## Approach to Changes to the International Standards

### Summary of comments received on exposure

16. A few respondents explicitly expressed support for the IAASB's approach in proposing limited amendments to the International Standards that do not explicitly duplicate in detail all of the specific requirements in the IESBA NOCLAR Re-ED, allowing flexibility when other ethical codes are applied and minimizing the amount of material incorporated into ISA 250 (Revised) and other International Standards. Some respondents requested more alignment between the IESBA NOCLAR Re-ED and the International Standards, for example the inclusion of the work effort requirements from the IESBA NOCLAR Re-ED in the International Standards, or an enhanced link to the IESBA NOCLAR Re-ED. One Monitoring Group member specifically questioned whether the IAASB had concluded that certain aspects of the IESBA proposals that were not addressed in the IAASB's proposals did not need to be addressed in ISA 250 (Revised) because they went beyond what is necessary for an audit of financial statements, and suggested that if this was the case that ISA 250 (Revised) should indicate that the amendments made are those necessary for the purposes of an audit.
17. Some respondents emphasized their concerns and comments previously expressed in response to the IESBA NOCLAR Re-ED or expressed hesitation about the timing of ED-ISA 250 and concerns that the IAASB and IESBA needed to be closely aligned in finalizing their respective proposals. In this regard, the importance of ongoing coordination with the IESBA as it finalized the changes to the IESBA Code was stressed. There were also comments that updating the International Standards for minor amendments requires effort in translation and updates to firms' methodologies, at a time when there are other significant changes to deal with.

### IAASB decisions

18. The IAASB believed that, consistent with the IAASB NOCLAR ED, the intent was not to repeat all the requirements of the IESBA NOCLAR Re-ED in the International Standards, as doing so could place additional requirements on auditors and practitioners who are bound by ethical codes other than the IESBA Code and it could be impracticable for such auditors and practitioners to comply with the International Standards if they included these additional requirements. Furthermore, not all of the procedures contemplated by the IESBA NOCLAR Re-ED are designed for the purpose of providing sufficient appropriate audit evidence to support an opinion on the financial statements and are instead intended to support the auditor or practitioner in fulfilling relevant ethical obligations by responding to NOCLAR that the auditor or practitioner comes across or of which the auditor or practitioner is made aware. The IAASB carefully considered the matters addressed in the final IESBA pronouncement and decided it should continue with the limited approach to amendments to the International Standards, but has highlighted in ISA 250 (Revised) that the auditor may have additional responsibilities under law, regulation, or relevant ethical requirements regarding identified or suspected NOCLAR (see further discussion in paragraphs 27–30 of this Basis for Conclusions).

## **The Auditor's Determination of Whether to Report Identified or Suspected NOCLAR to an Appropriate Authority outside the Entity**

### *Background*

19. Extant ISA 250 includes a requirement that the auditor must determine whether the auditor has a responsibility to report identified or suspected NOCLAR to parties outside the entity.

20. In ED-ISA 250, the IAASB proposed updating this requirement to indicate that the auditor has a responsibility to determine whether the auditor has a legal or ethical duty or right to report identified or suspected NOCLAR. The amendments were proposed in order to more clearly recognize that the auditor may have a responsibility to report under law, regulation or relevant ethical requirements, and the expectations of the auditor may differ, for example, an obligation to report (“a duty”) or a general “right” (but not an obligation) to report.
21. Application material to support this amended requirement was also included in ED-ISA 250 to provide guidance to auditors on the considerations that the auditor may apply in reporting identified or suspected NOCLAR to appropriate authorities, including with respect to the auditor’s duty of confidentiality.

#### *Summary of Comments Received on Exposure*

22. Concerns were raised by respondents with the use of the phrase “legal or ethical duty or right”, as it was believed that this did not reflect the underlying decision-making process and evaluation that would take place before exercising a right, and it did not reflect that, in some cases, it is an ethical requirement or responsibility to report. It was also noted that the IESBA NOCLAR Re-ED did not make use of the term “right”. Other respondents were of the view that the phrase was ambiguous and unclear, particularly where laws or regulations prohibit the breach of confidentiality and the auditor is not able to report identified or suspected NOCLAR outside of the entity.
23. Respondents, including Monitoring Group members, provided various suggestions for improvements to ISA 250 and the conforming amendments in this regard, including the nature and extent of how ISA 250 makes reference to the provisions within the IESBA Code. Notably, there were requests to include, similar to the IESBA NOCLAR Re-ED, discussion of the legal and other risks that the auditor would take into account when determining whether to report identified or suspected NOCLAR to an appropriate authority, as well as reference to the “public interest test” included in the IESBA’s NOCLAR re-ED. Some also recommended more prominence be given in the requirements to the possible preclusion of reporting to an appropriate authority outside the entity, for example, due to confidentiality requirements contained in law or regulation that would override or be in conflict with any ethical requirements.

#### *IAASB Decisions*

24. The IAASB explored various alternatives of how to articulate the auditor’s determination of whether to report identified or suspected NOCLAR to an appropriate authority outside the entity. The IAASB recognized that reporting responsibilities under law, regulation or relevant ethical requirements differ, and it is not possible to encapsulate all of these succinctly in a requirement without making it overly complex. Accordingly, the IAASB agreed to retain a simple requirement that generally covers the possible reporting responsibilities that may exist. The IAASB also believed that it should be clear that the ISAs require the auditor to determine what provisions are contained in law, regulation or relevant ethical requirements regarding reporting of identified or suspected NOCLAR, and that any reporting would be in accordance with such law, regulation or relevant ethical requirements (see paragraph 29 of ISA 250 (Revised)). Further, the IAASB was of the view that it is essential for the requirements to be supported by application material that comprehensively addresses the possible scenarios that may exist (see paragraphs A28–A31 of ISA 250 (Revised)).

25. As the objective of the project was to address actual or perceived inconsistencies with the IESBA Code, the IAASB also considered how best to give appropriate prominence within ISA 250 (Revised) to the requirements in the IESBA Code. The IAASB believed that reference to the IESBA Code would be best placed in the application material as an example, as this achieves the effect of highlighting the specific requirements within the IESBA Code, while recognizing not all who apply the ISAs apply the IESBA Code (see paragraph A30 of ISA 250 (Revised)). This approach is consistent with how the IESBA Code is referred to in other ISAs (e.g., ISA 260 (Revised)).
26. The IAASB also debated whether to explain the considerations relating to the duty of confidentiality in the requirement (i.e., that law, regulation or relevant ethical requirements may in some cases preclude reporting to an appropriate authority). The IAASB concluded that including this reference within the requirement could potentially undermine the objective of the project and inhibit the auditor's consideration of whether to report, and would therefore be best placed in application material (see paragraph A32 of ISA 250 (Revised)). Paragraphs A28–A33 of ISA 250 (Revised) are set out in the manner in which the IAASB believes an auditor would likely consider identified or suspected NOCLAR and determine whether reporting was required or appropriate in the circumstances.

### **Additional Responsibilities under Law, Regulation or Relevant Ethical Requirements Regarding Identified or Suspected NOCLAR, Including with Respect to Documentation**

#### *Background*

27. As noted in paragraph 11, the IAASB's approach was to make limited amendments to the International Standards that do not explicitly duplicate in detail all of the specific requirements in the IESBA NOCLAR Re-ED. Accordingly, in paragraph 8a of ED-ISA 250, the IAASB proposed highlighting that the auditor may have additional responsibilities under ethical requirements regarding identified or suspected NOCLAR, and that complying with those additional responsibilities may provide further information that is relevant to the auditor's work in accordance with ISA 250 and other ISAs.

#### *Summary of Comments Received on Exposure*

28. While respondents generally agreed with the IAASB's approach (see paragraph 16), some respondents specifically requested the inclusion of the documentation requirements contained in the IESBA NOCLAR Re-ED in ISA 250, or suggested other ways to alert the auditor to the fact that additional documentation is required for those auditors subject to the IESBA Code, to give this new requirement in the IESBA Code appropriate prominence.

#### *IAASB Decisions*

29. The IAASB believed that clarifying what some of the additional responsibilities under law, regulation or relevant ethical requirements would entail would be useful, and accordingly incorporated additional material highlighting some of the features of the IESBA Code in the introductory section (see paragraph 9 of ISA 250 (Revised)).
30. The IAASB also agreed with respondents that emphasis of the documentation requirements contained in the IESBA Code would be useful. In reconsidering the documentation requirements of ISA 250, the IAASB believed that the existing requirements in ISA 250 were somewhat limited, and may not appropriately guide the auditor in documenting their significant professional judgments, and the discussion of how management have responded to the identified or suspected NOCLAR.

Accordingly, the IAASB has enhanced the documentation requirements (see paragraph 30 of ISA 250 (Revised)) and has brought emphasis to the additional documentation requirements that may exist in law, regulation or relevant ethical requirements (see paragraphs 9 and A36 of ISA 250 (Revised)).

## Group Audits

### *Background and Summary of Comments Received on Exposure*

31. Consistent with the IESBA NOCLAR Re-ED, the ED-ISA 250 did not propose specific changes related to group audits.
32. In responding to the IESBA NOCLAR Re-ED, respondents, including one member of the Monitoring Group, commented that specific consideration should be given to communication of identified or suspected NOCLAR in a group audit situation. The IESBA accepted that there was a need to enhance the provisions in the IESBA Code regarding communication amongst auditors within a group audit as the guidance provided in the IESBA NOCLAR Re-ED lacked sufficient specificity. The IESBA did not believe that it would be appropriate to rely on ISA 600<sup>9</sup> to provide the necessary direction and guidance in this regard, as the IESBA Code serves different objectives compared with the ISAs. The IESBA also recognized that the IESBA Code and the ISAs are independent of each other and jurisdictions do not necessarily adopt them together. Subsequent to the issuance of ED-ISA 250, the IESBA found it necessary to include more specific provisions dealing with the communication of identified or suspected NOCLAR amongst auditors within a group audit in finalizing the changes to the IESBA Code.

### *IAASB Decisions*

33. The IAASB considered the implications of these amendments to the IESBA Code on the ISAs, and explored various alternatives to alerting auditors to the additional responsibilities in respect of group audit situations. These options included making conforming amendments to ISA 600, inserting additional requirements in ISA 250 addressing group audits, or including additional application material in ISA 250. The IAASB noted that the communication requirements in the revised IESBA Code would apply more widely than to those participating directly in a group audit. For example, there are communication requirements for auditors who are performing work at a component (e.g., a statutory audit) who may not be functioning as a component auditor for the purposes of the audit of the group financial statements.
34. The IAASB has a current initiative addressing group audits,<sup>10</sup> and as part of that initiative is exploring the two-way communications that may be necessary between group engagement teams and component auditors at a holistic level. The IAASB noted that there are existing provisions in ISA 600 that, to some extent, address the issues arising from the amendments in the revised IESBA Code. The IAASB<sup>11</sup> therefore did not believe a conforming amendment to ISA 600 would be appropriate at this time.

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<sup>9</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

<sup>10</sup> See the [Invitation to Comment, Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits](#).

<sup>11</sup> The IAASB member who voted against the conforming amendments did so on the basis that, in his view, a conforming amendment to ISA 600 was necessary at this time to give sufficient prominence to the additional communication requirements set out in the IESBA NOCLAR pronouncement.

35. Notwithstanding this view, the IAASB determined that emphasis should be included in ISA 250 regarding the additional responsibilities that may be contained in relevant ethical requirements relating to group audit situations. In order to remain consistent with the IAASB's decisions explained in paragraphs 18 and 29 above, the IAASB agreed to also highlight that the additional responsibilities that may be contained in relevant ethical requirements may include communicating instances of identified or suspected NOCLAR to other auditors (e.g., in an audit of group financial statements) (see paragraph 9 of ISA 250 (Revised)). This has been supported by application material that explains what such communication might entail (see paragraph A8 of ISA 250 (Revised)), with reference to the specific paragraphs in the IESBA Code. This positioning in ISA 250 has the benefit of highlighting the communication requirements in the IESBA Code that may apply in cases where ISA 600 does not apply – for example, to auditors performing statutory audits at a component who are not otherwise involved in the audit of the group financial statements.

### **The Implications of Identified or Suspected NOCLAR on the Audit**

#### *Background*

36. In ED-ISA 250, the IAASB proposed new guidance to clarify how addressing identified or suspected NOCLAR under the IESBA Code may have an effect on the audit being performed under the ISAs. In particular, new introductory material was added to highlight that complying with the additional responsibilities under relevant ethical requirements may provide further information that is relevant to the audit. This was further emphasized in the application material in ED-ISA 250, which explained circumstances that could impact on the reliability of written representations.

#### *Summary of Comments Received on Exposure*

37. Views were expressed that ISA 250 should incorporate more considerations relating to the impact of identified or suspected NOCLAR on the auditor's report, for example key audit matters. Respondents further noted that identified or suspected NOCLAR could qualify as a key audit matter, even if such NOCLAR was completely unrelated to the financial statements. Respondents also indicated that communication of identified or suspected NOCLAR in the auditor's report could be highly sensitive or there may be a circumstance when it should not be communicated as law or regulation may specifically prohibit a communication, or other action that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act.
38. It was also observed by respondents that the requirements of ISA 250 regarding withdrawal from the engagement were not aligned to the IESBA NOCLAR Re-ED, in particular that ISA 250 refers to the possibility of withdrawal as being an "exceptional case", and therefore contemplates withdrawal in more limited circumstances than the IESBA NOCLAR Re-ED.

#### *IAASB Decisions*

39. The IAASB reconsidered the application material in ED-ISA 250 addressing the implications for the auditor's report, including the possible withdrawal from the audit (as extant ISA 250 makes reference to an Other Matter paragraph, in the context of the auditor being unable to withdraw from the engagement).
40. The IAASB introduced new application material to clearly set out the variety of circumstances in which identified or suspected NOCLAR may have implications for the auditor's report (including key audit matters). This material acknowledges that the auditor may determine identified or suspected

NOCLAR to be a key audit matter, but also draws reference to relevant material in ISA 701<sup>12</sup> that addresses circumstances in which the auditor determines a matter to be a key audit matter but decides not to communicate the matter in the auditor's report<sup>13</sup> (see paragraph A26 of ISA 250 (Revised)). The application material also highlights that limitations may exist in relation to referring to identified or suspected NOCLAR in the auditor's report, which may affect the auditor's ability to describe the matter in the auditor's report, or in some circumstances, the auditor's ability to issue the auditor's report (see paragraph A27 of ISA 250 (Revised)).

41. The IAASB noted that, throughout the ISAs, the manner in which withdrawal from the engagement is described or required varies due to the circumstances in which withdrawal is contemplated. The IAASB believes that withdrawal "in exceptional circumstances", as indicated in extant ISA 250, may imply that withdrawal is a last resort, which is inconsistent with the intention of the revised IESBA Code. This is because withdrawal may be appropriate in some scenarios even if management has appropriately dealt with the identified or suspected NOCLAR, for example when there are questions about management's integrity. Accordingly, the IAASB agreed to better align the withdrawal provisions in ISA 250 with the revised IESBA Code (see paragraph A25 of ISA 250 (Revised)). However, the IAASB decided not to include the additional guidance in the revised IESBA Code regarding factors to consider in determining whether withdrawal is appropriate within ISA 250 (Revised), as this would be dissimilar to and more prescriptive than the approach taken in other ISAs in relation to withdrawal.

### **Alignment of the Definition of Non-Compliance and the Scope of Laws and Regulations with the IESBA Code**

#### *Background*

42. ED-ISA 250 included proposed changes to ISA 250 that the IAASB believed would significantly clarify the application of the International Standards in light of the IESBA Code. This largely comprised including in ED-ISA 250 the examples of laws and regulations that were indicated in the IESBA NOCLAR Re-ED as being those which the NOCLAR section of the IESBA Code addresses.

#### *Summary of Comments Received on Exposure*

43. Respondents expressed mixed views regarding the inclusion of the examples in ED-ISA 250. Some believed that it would create more confusion as there is no clear separation between the examples that relate to the two different categories<sup>14</sup> of laws and regulations contemplated in paragraph 6 of

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<sup>12</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

<sup>13</sup> Paragraph 14 of ISA 701 indicates that the auditor shall describe each key audit matter in the auditor's report unless (a) law or regulation precludes public disclosure about the matter; or (b) in extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

<sup>14</sup> ISA 250 (Revised) distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows: (a) the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and pension laws and regulations; and (b) other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (e.g., compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial statements.

ISA 250. Others expressed concern that the examples in the IESBA NOCLAR Re-ED are for a different purpose or application than the ISAs. There was also a view that the examples could increase the expectations gap in terms of how auditors respond in those circumstances versus what the public would expect them to do. Others noted that some of the examples are outside of the auditor's particular expertise, or were included in the IESBA NOCLAR Re-ED for a different purpose, for example to address insider trading.

44. There were suggestions on how to improve the examples, including classifying them between the two categories, combining the examples with other examples referenced in ISA 250, or including appropriate disclaimers to emphasize that the examples are not exhaustive and that the auditor would have to consider what represents relevant laws or regulations in the context of the particular engagement, the entity's industry and the regulatory framework. Respondents also recommended the inclusion of additional examples.
45. Additionally, while no changes were proposed to the definition of non-compliance in ED-ISA 250, respondents highlighted that the definition of non-compliance was not consistent with the IESBA NOCLAR Re-ED, which is explained in paragraph 225.2 of the revised IESBA Code as follows:

Non-compliance with laws and regulations ("non-compliance") comprises acts of omission or commission, intentional or unintentional, committed by a client, or by those charged with governance, by management or by other individuals working for or under the direction of a client which are contrary to the prevailing laws or regulations.

46. There were suggestions that the definition in ISA 250 (Revised) should refer to personal misconduct related to the business activities of the entity, as well as include acts on behalf of the entity by individuals not employed by the entity. However, there was a view from a respondent that the definition in ISA 250 is subtly different from the IESBA NOCLAR Re-ED, in that all instances of personal misconduct are outside the scope of ISA 250.

#### *IAASB Decisions*

47. The IAASB believed that, to the extent possible, the relevant concepts in the ISAs (the scope of laws and regulations, the definition of non-compliance, and the circumstances under which the auditor may withdraw from the engagement) should be aligned to those of the revised IESBA Code, with the recognition that adaptations may be necessary to ensure the provisions remain relevant and appropriate in the context of the an audit of financial statements.

#### *Examples of Laws and Regulations*

48. The IAASB explored the suggestions and recommendations from respondents. While the IAASB acknowledged that it may be helpful to classify the examples between the two categories, the Board thought making a bright line distinction would not be possible, given that the appropriate classification depends on the nature and circumstances of the entity. Instead, the IAASB agreed that additional emphasis should be made in the application material to indicate that the classification of the laws or regulations between the two categories is dependent on the nature and circumstances of the entity (see paragraph A6 of ISA 250 (Revised)).
49. While the IAASB broadly believed that consistency with the revised IESBA Code is important, the Board did not think it necessary in ISA 250 (Revised) to reference the additional examples that were included in the IESBA NOCLAR pronouncement. The IAASB also noted that the examples are not

exhaustive, and therefore would not preclude the additional suggested examples from being within the scope of ISA 250 (Revised).

#### Definition of Non-Compliance

50. In exploring the need for consistency between the ISAs and the IESBA Code, the IAASB debated the meaning of the definition of non-compliance in extant ISA 250 and agreed the following matters:

- The reference to “transactions entered into by, in the name of, or on behalf of the entity” is an example of an act of non-compliance in the context of a financial statement audit.
- Personal misconduct related to the business activities of the entity is, and has always been, included within the scope of ISA 250, since the extant definition only scopes out personal misconduct unrelated to the business activities of the entity.

51. In light of these views, the IAASB evaluated the definition of non-compliance in relation to how non-compliance is described in the revised IESBA Code (see paragraph 225.2 and 225.9 of the revised IESBA Code). The intention of the IESBA was to align the concept of non-compliance with that contained in the ISAs, although the IESBA refined this explanation to ensure the description was relevant in the context of the IESBA Code. The IAASB noted the following key differences between extant ISA 250 and the revised IESBA Code:

- The description in the revised IESBA Code refers to acts committed by “other individuals working for or under the direction of the entity”, in addition to management and those charged with governance. Extant ISA 250 refers to “employees”. The IAASB agreed with how this is described in the revised IESBA Code, since it is possible that others who are not actual employees could be involved with the NOCLAR (such as contractors) and, accordingly, replaced “employees” with “other individuals working for or under the direction of the entity” (see paragraph 12 of ISA 250 (Revised)).
- Extant ISA 250 indicates that “Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees”. The revised IESBA Code does not make reference to this example as the IESBA believed that NOCLAR would not always arise from a transaction, but is rather something that arises from an action or inaction. The IAASB believed that this example should be retained as it is still relevant in the context of the ISAs, but relocated it to the application material supporting the definition (see paragraph A9 of ISA 250 (Revised)).
- The revised IESBA Code explains that the NOCLAR section of the Code does not address personal misconduct unrelated to the business activities of the client; this is located separately (paragraph 225.9 of the Code) from where the Code explains what non-compliance is (paragraph 225.2 of the Code). Extant ISA 250 also indicates that personal misconduct unrelated to the business activities of the entity is not included in the definition of non-compliance. In analyzing the consistency with the revised IESBA Code, the IAASB debated where best this would be placed, i.e., in the definition or in the application material. The IAASB believed that since this is important to the auditor’s understanding of which matters would be excluded from the definition of non-compliance, it should be retained in the definition (see paragraph 12 of ISA 250 (Revised)).
- The IAASB considered, but rejected, including additional explanatory material that was included in the IESBA Code to explain that non-compliance does not include acts committed

by third parties. The IAASB believed the example described in the IESBA Code would be rare, if at all possible, in an audit of financial statements, and concluded that including such a reference purely for consistency may be confusing.

52. The IAASB was further of the view that additional clarity regarding what would constitute personal misconduct related to the business activities would be helpful. Accordingly, an example has been included in the application material (see paragraph A10 of ISA 250 (Revised)).

## **Communication with Management or Those Charged with Governance**

### *Background*

53. New guidance was included in ED-ISA 250 to recognize that laws or regulations may prohibit alerting the entity, for example when the auditor is required to report identified or suspected NOCLAR to an appropriate authority pursuant to money laundering legislation.

### *Summary of Comments Received on Exposure*

54. Respondents raised concern that there is insufficient emphasis in the requirements to alert the auditor to the fact that the auditor may be prohibited from discussing the NOCLAR with management or those charged with governance. It was also noted that it is inconsistently treated within ISA 250 and could be given greater prominence (for example, by adding a statement to the introduction to ISA 250, consistent with paragraph 7 of ISA 260 (Revised)).
55. A Monitoring Group respondent also recommended that paragraphs 40–42 of ISA 240, which address the communication of fraud to management and those charged with governance, should encompass identified or suspected NOCLAR occurring at a component.

### *IAASB Decisions*

56. The IAASB reconsidered how ISA 250 and the conforming amendments address the possible preclusion on communicating with and reporting to management or those charged with governance. The IAASB believed it was important to highlight this possible preclusion in the requirements through the addition of “unless such communication is prohibited by law or regulation” in certain places (see, for example, paragraphs 20 and 23 of ISA 250 (Revised)), supported by an explanation in the application material (see paragraph A21 of ISA 250 (Revised)). The IAASB reviewed ISA 250 and the conforming amendments and included a reference to the preclusion in all cases where communication with management or those charged with governance is indicated.
57. The IAASB noted that both ISA 250 and ISA 240 address communication with management and those charged with governance, and accordingly provisions relating to communicating with group management regarding identified or suspected NOCLAR at a component would need to apply to both. However, as indicated in paragraphs 31–35 above, the IAASB considered revisions to ISA 250 and ISA 600 relating to group audits, and determined that revisions to ISA 600 at this time would not be appropriate, due to the current initiative addressing group audits. Instead, the IAASB has included a general indication that there may be additional responsibilities relating to group audit situations contained in relevant ethical requirements (see paragraphs 9 and A8 of ISA 250 (Revised)).

## **Communication with a Proposed Successor Auditor**

### *Background*

58. The ED proposed a conforming amendment to ISA 220 as application material to highlight a requirement in the IESBA NOCLAR Re-ED that, in the case of an audit of financial statements, an auditor shall request the predecessor auditor to provide known information regarding any facts or circumstances that, in the predecessor auditor's opinion, the auditor needs to be aware of before deciding whether to accept the engagement.

### *Summary of Comments Received on Exposure*

59. There was concern that the predecessor auditor may not be willing to provide the information, or may not have the client's permission to do so, and clarification of this was requested in paragraph A8a of ISA 220. There was also a recommendation to indicate examples of "facts and circumstances" (e.g., identified or suspected NOCLAR), or to reference to the relevant sections of the revised IESBA Code.

### *IAASB Decisions*

60. The IAASB noted that, in finalizing the NOCLAR provisions for the revised IESBA Code, the IESBA made amendments to require that, when withdrawing from the engagement as a result of identified or suspected NOCLAR, the predecessor auditor, on request by the proposed successor auditor, should provide all such facts and other information concerning identified or suspected NOCLAR to the proposed successor auditor that, in the predecessor auditor's opinion, the proposed successor auditor needs to be aware of before deciding whether to accept the audit appointment.
61. The IAASB has accordingly highlighted this requirement of the revised IESBA Code in the application material of ISA 220 (see paragraph A8a of ISA 220).
62. Furthermore, the IAASB agreed that it would be helpful to refer to paragraph 210.14 of the revised IESBA Code in ISA 220 as an example of what may specifically be required by relevant ethical requirements in relation to communications between a predecessor auditor and a proposed successor auditor (see paragraph A8a of ISA 220 (Revised)).

## **Implications for International Standards Other than ISAs**

### *Background*

63. The NOCLAR provisions in the revised IESBA Code apply to all professional accountants, although the responsibilities differ between professional accountants performing audits of financial statements, professional accountants providing professional services other than audits of financial statements and professional accountants in business.
64. In terms of the revised IESBA Code, the laws and regulations to which a professional accountant must respond if the professional accountant is made aware of identified or suspected NOCLAR are the same as the laws and regulations covered by ISA 250 (i.e., laws and regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements or are fundamental to the operating aspects of the entity's business, to its ability to continue as a going concern or to avoid material penalties).
65. In the ED-ISA 250, proposed amendments were only made to ISRE 2400 (Revised), with a minor edit to ISAE 3402.

### *Summary of Comments Received on Exposure*

66. Two respondents highlighted that the scope of laws and regulations in the IESBA NOCLAR Re-ED is inconsistent with the scope of the laws and regulations contemplated by certain of the International Standards, specifically ISRE 2400 (Revised) and ISAE 3000 (Revised). There were also concerns about the inconsistency in work effort relating to identified or suspected NOCLAR between these International Standards and the IESBA NOCLAR Re-ED, since the IESBA NOCLAR Re-ED imposes an obligation on a practitioner beyond the requirements of these International Standards.
67. Three respondents questioned whether the conforming amendments to the International Standards were adequate, as no amendments were proposed in the ED to certain of the International Standards, particularly ISAE 3000 (Revised).

### *IAASB Decisions*

68. The IAASB noted that the practitioner is, under the revised IESBA Code, expected to respond to NOCLAR when it comes to the practitioner's attention. However, the revised IESBA Code does not require the practitioner to perform procedures to identify instances of NOCLAR. The revised IESBA Code explains the practitioner's expected level of knowledge of laws and regulations, as reflected in paragraph 225.40 of the revised IESBA Code:

The professional accountant is expected to apply knowledge, professional judgment and expertise, but is not expected to have a level of understanding of laws and regulations beyond that which is required for the professional service for which the accountant was engaged. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body. Depending on the nature and significance of the matter, the professional accountant may consult on a confidential basis with others within the firm, a network firm or a professional body, or with legal counsel.

69. The IAASB considered whether amendments to the other standards would be appropriate and concluded that:
- It would be appropriate to bring emphasis to the additional responsibilities relating to NOCLAR under the revised IESBA Code in ISAE 3000 (Revised) and ISRS 4410 (Revised).
  - Conforming amendments would not be appropriate for ISRE 2410,<sup>15</sup> as this standard is still in the "pre-clarity" format and has not been recently amended to reflect conforming amendments in respect of other IAASB projects.
  - Conforming amendments would not be appropriate for ISRS 4400,<sup>16</sup> as this standard is the subject of a current IAASB project.

## **Jurisdictions that Do Not Adopt, or Plan to Adopt, the IESBA Code**

### *Background*

70. In issuing ED-ISA 250, the IAASB proposed limited amendments to the International Standards and did not intend on duplicating all the specific requirements in the revised IESBA Code. This approach recognized that, in some jurisdictions, ethical codes other than the IESBA Code may be applied. The

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<sup>15</sup> ISRE 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*

<sup>16</sup> ISRS 4400, *Engagements to Perform Agreed-upon Procedures Regarding Financial Information*

IAASB requested respondents to indicate the impact, if any, of the proposed limited amendments in jurisdictions that have not adopted, or do not plan to adopt, the IESBA Code.

#### *Summary of Comments Received on Exposure*

71. Respondents generally indicated that there is no conflict between the proposed amendments to the International Standards and local jurisdictional codes or laws or regulations in jurisdictions that have not adopted, or do not plan to adopt, the IESBA Code. However, a limited number of respondents expressed the view that a possible conflict could arise, or that future compliance with the International Standards may become difficult, due to the requirement in ISA 200<sup>17</sup> that the auditor comply with “relevant ethical requirements” when conducting an audit in accordance with ISAs. There was also a question raised about how ethical codes applied by auditors and practitioners would be measured to determine their equivalency to the IESBA Code, given a perception of the IESBA Code becoming more explicit and detailed.

#### *IAASB Decisions*

72. The IAASB further discussed these matters, including with the IAASB’s National Auditing Standard Setters Liaison Group, in order to obtain a better understanding of how ISA 200 is interpreted and applied by NSS in their jurisdictions. IAASB staff also consulted with IESBA staff to ascertain the implication of the circumstances where the IESBA Code is in conflict with local laws or regulations. The Board concluded that the concern raised does not appear to have broad relevance internationally at this time, and therefore there is no present need to clarify ISA 200. Nonetheless, this may be a matter for monitoring by the IAASB, taking into account any pertinent findings from the post-implementation review the IESBA intends to undertake in the future regarding the NOCLAR provisions in the revised IESBA Code. It was also acknowledged that the determination of how national ethical requirements (when not the IESBA Code), the IESBA Code, and the ISAs interrelate is a matter for local or jurisdictional consideration, although it was recognized that the relevant ethical requirements applied would need to be high quality.

### **Other Issues Raised by Respondents**

#### *Whether a More Fulsome Review of ISA 250 Is Warranted in Due Course*

73. Prior to undertaking this project, in developing its current Strategy and Work Plan, the IAASB had not identified a need for a fulsome review of ISA 250. However, the IAASB recognized that ED-ISA 250 was an opportunity for the IAASB to solicit stakeholders’ views as to whether there is merit in exploring other aspects of ISA 250 where further improvements may need to be considered in due course (i.e., under a future IAASB Work Plan).
74. There were mixed views from respondents regarding the need for a future project to revise ISA 250 or explore its improvement. Respondents in support of a future revision, including a Monitoring Group member, expressed support for some of the specific aspects highlighted in the ED of matters that may warrant consideration in the future. There were also suggestions and recommendations from respondents of matters that could be considered in a future revision of ISA 250. Respondents who did not support a more fulsome review of ISA 250 cited various reasons, including other higher priority

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<sup>17</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

projects, a lack of observed problems with the current ISA, and concerns about the scope, responsibilities and expectations of the auditor arising from a revision.

#### *IAASB Decisions*

75. Consistent with the proposals in ED-ISA 250, the IAASB continues to believe that an immediate revision of ISA 250 is not warranted in light of other more urgent priorities that were identified in developing the current Work Plan – which continue to be supported by feedback to the December 2015 Invitation to Comment, *Enhancing Audit Quality in the Public Interest*. However, the question of the relative importance of a fulsome review and accordingly whether this should be considered by the IAASB in its next Work Plan for 2017–2018 was included in IAASB's July 2016 survey, [Survey Consultation—The IAASB's Work Plan for 2017–2018 and Continuing Relevance of Its Strategic Objectives](#). The determination of future priorities, including whether to revise ISA 250 more fully in the future, will be made based on feedback from this survey and discussions with the CAG, with oversight from the Public Interest Oversight Board.

#### *Firms' Systems of Quality Control*

76. A Monitoring Group respondent indicated that the IAASB should establish requirements for firms to establish processes internal to the firm that stipulate how the firm should address those instances in which an auditor or practitioner comes across identified or suspected NOCLAR at an entity. It was suggested this could potentially be done as part of the IAASB's current project addressing quality control.
77. ISQC 1 contains a general requirement for firms to establish policies and procedures with regards to compliance with relevant ethical requirements. The IAASB agreed that the establishment of appropriate policies and procedures to address the response to identified or suspected NOCLAR is important, and will consider the need for a specific requirement in ISQC 1 in this regard as part of its quality control project.

#### *Other Conforming Amendments*

78. Respondents recommended that paragraph A24 of ISA 210 should address the inclusion in the engagement letter of the auditor's legal duty or ethical responsibility to report identified or suspected NOCLAR. The IAASB agreed with this suggestion.
79. For the purposes of consistency, respondents suggested revising paragraph A26 of ISA 500 and inserting a new paragraph in ISA 500 (paragraph A33a) to highlight that audit evidence may arise from other sources, such as ethical requirements, and that identified or suspected NOCLAR may provide further information relevant to the audit. The IAASB agreed with the inclusion of this additional guidance.

#### **Effective Date**

80. At the time of exposing ED-ISA 250, the IESBA was targeting approval of the NOCLAR provisions together with the restructured IESBA Code, which was expected to take place by the fourth quarter of 2016. Accordingly, the IAASB anticipated that the effective date of the changes to ISA 250 (Revised) could be aligned with that of the NOCLAR provisions in the revised IESBA Code, and respondents supported this.

81. The IESBA subsequently determined that its NOCLAR provisions should be issued when finalized, instead of waiting for the final restructuring of the IESBA Code, thus moving the timeline for the effective date of the IESBA NOCLAR pronouncement forward. The effective date of the IESBA NOCLAR provisions is July 15, 2017 (i.e., the provisions apply to instances of NOCLAR that come to the professional accountant's attention on or after July 15, 2017).
82. The IAASB debated various options, balancing the aim of trying to achieve alignment with the IESBA's effective date with recognition of the importance of allowing sufficient time for stakeholders to effectively implement ISA 250 (Revised) and the conforming amendments. The IAASB noted that it is not possible to achieve perfect alignment of the effective dates.
83. The IAASB noted that the changes to ISA 250 (Revised) do not change the auditor's work effort, i.e., the auditor's response to identified or suspected NOCLAR would not differ between extant and revised ISA 250. This is because the auditor would still have an obligation in accordance with extant ISA 250 to consider the appropriate action be taken in accordance with the relevant ethical requirements, for example the IESBA Code when this constitutes the relevant ethical requirements. Therefore, the lack of alignment of effective dates would, in practice, not have an effect.
84. Accordingly, the IAASB agreed that the most appropriate effective date is for audits of financial statements for periods beginning on or after December 15, 2017, with early adoption permitted, as this would allow for a sufficient time period for the implementation activities (approximately fifteen months).

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**Compiled Auditing Standard**

**ASA 250**  
(June 2011)

# **Auditing Standard ASA 250**

## ***Consideration of Laws and Regulations in an Audit of a Financial Report***

This compilation was prepared on 27 June 2011 taking into account amendments made by ASA 2011-1

Prepared by the **Auditing and Assurance Standards Board**



**Australian Government**

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**Auditing and Assurance Standards Board**

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#### **Conformity with International Standards on Auditing**

## COMPILATION DETAILS

### ***Auditing Standard ASA 250 Consideration of Laws and Regulations in an Audit of a Financial Report as Amended***

This compilation takes into account amendments made up to and including 27 June 2011 and was prepared on 27 June 2011 by the Auditing and Assurance Standards Board (AUASB).

This compilation is not a separate Auditing Standard made by the AUASB. Instead, it is a representation of ASA 250 (October 2009) as amended by another Auditing Standard which is listed in the Table below.

#### **Table of Standards**

<b>Standard</b>	<b>Date made</b>	<b>Operative date</b>
ASA 250	27 October 2009	1 January 2010
ASA 2011-1	27 June 2011	1 July 2011

#### **Table of Amendments**

<b>Paragraph affected</b>	<b>How affected</b>	<b>By ... [paragraph]</b>
5 Footnote 2	Amended	ASA 2011-1 [24]

**Compiled Auditing Standard ASA 250**  
***Consideration of Laws and Regulations in an Audit of a Financial Report***

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**AUTHORITY STATEMENT**

Auditing Standard ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* (as amended at 27 June 2011) is set out in paragraphs 1 to A21.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. This Auditing Standard is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

Dated: 27 June 2011

M H Kelsall  
Chairman - AUASB

## AUDITING STANDARD ASA 250

The Auditing and Assurance Standards Board (AUASB) made Auditing Standard ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*, pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*, on 27 October 2009.

This compiled version of ASA 250 incorporates subsequent amendments contained in another Auditing Standard made by the AUASB up to and including 27 June 2011 (see Compilation Details).

## AUDITING STANDARD ASA 250

### *Consideration of Laws and Regulations in an Audit of a Financial Report*

#### Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 1 January 2010. [Note: For operative dates of paragraphs changed or added by an amending Standard, see Compilation Details.]

#### Introduction

##### Scope of this Auditing Standard

1. This Auditing Standard deals with the auditor's responsibility to consider laws and regulations in an audit of a financial report. This Auditing Standard does not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific laws or regulations.

##### Effect of Laws and Regulations

2. The effect on a financial report of laws and regulations varies considerably. Those laws and regulations to which an entity is subject constitute the legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the

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financial report in that they determine the reported amounts and disclosures in an entity's financial report. Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial report. Some entities operate in heavily regulated industries (such as banks and chemical companies). Others are subject only to the many laws and regulations that relate generally to the operating aspects of the business (such as those related to occupational safety and health, and equal employment opportunity). Non-compliance with laws and regulations may result in fines, litigation or other consequences for the entity that may have a material effect on the financial report.

**Responsibility for Compliance with Laws and Regulations** (Ref: Para. A1-A6)

3. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial report.

*Responsibility of the Auditor*

4. The requirements in this Auditing Standard are designed to assist the auditor in identifying material misstatement of the financial report due to non-compliance with laws and regulations. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.
5. The auditor is responsible for obtaining reasonable assurance that the financial report, taken as a whole, is free from material misstatement, whether caused by fraud or error.<sup>1</sup> In conducting an audit of a financial report, the auditor takes into account the applicable legal and regulatory framework. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial report may not be detected, even though the audit is properly planned and performed in accordance with the Australian Auditing Standards.<sup>2</sup> In the context of laws and regulations, the potential effects of inherent limitations

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<sup>1</sup> See ASA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*, paragraph 5.

<sup>2</sup> See ASA 200, paragraph A51-A52.

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on the auditor's ability to detect material misstatements are greater for such reasons as the following:

- There are many laws and regulations, relating principally to the operating aspects of an entity, that typically do not affect the financial report and are not captured by the entity's information systems relevant to financial reporting.
- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor.
- Whether an act constitutes non-compliance is ultimately a matter for legal determination by a court of law.

Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial report, the less likely the auditor is to become aware of it or to recognise the non-compliance.

6. This Auditing Standard distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows:
- (a) The provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report such as tax and superannuation laws and regulations (see paragraph 13 of this Auditing Standard); and
  - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial report, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (for example, compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial report (see paragraph 14 of this Auditing Standard).
7. In this Auditing Standard, differing requirements are specified for each of the above categories of laws and regulations. For the

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category referred to in paragraph 6(a) of this Auditing Standard, the auditor's responsibility is to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations. For the category referred to in paragraph 6(b) of this Auditing Standard, the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial report.

8. The auditor is required by this Auditing Standard to remain alert to the possibility that other audit procedures applied for the purpose of forming an opinion on the financial report may bring instances of identified or suspected non-compliance to the auditor's attention. Maintaining professional scepticism throughout the audit, as required by ASA 200,<sup>3</sup> is important in this context, given the extent of laws and regulations that affect the entity.

**Effective Date**

9. [Deleted by the AUASB. Refer Aus 0.3]

**Objectives**

10. The objectives of the auditor are:
- (a) To obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report;
  - (b) To perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial report; and
  - (c) To respond appropriately to non-compliance or suspected non-compliance with laws and regulations identified during the audit.

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<sup>3</sup> See ASA 200, paragraph 15.

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**Definition**

11. For the purposes of this Auditing Standard, the following term has the meaning attributed below:

Non-compliance means acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

**Requirements**

**The Auditor's Consideration of Compliance with Laws and Regulations**

12. As part of obtaining an understanding of the entity and its environment in accordance with ASA 315,<sup>4</sup> the auditor shall obtain a general understanding of:
- (a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and
  - (b) How the entity is complying with that framework.  
(Ref: Para. A7)
13. The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report. (Ref: Para. A8)
14. The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial report:  
(Ref: Para. A9-A10)
- (a) Enquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and

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<sup>4</sup> See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 11.

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- (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.
- 15. During the audit, the auditor shall remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. (Ref: Para. A11-Aus A11.1)
- 16. The auditor shall request management and, where appropriate, those charged with governance, to provide written representations that all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial report have been disclosed to the auditor. (Ref: Para. A12)
- 17. In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than those set out in paragraphs 12-16 of this Auditing Standard.

**Audit Procedures When Non-Compliance Is Identified or Suspected**

- 18. If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain: (Ref: Para. A13)
  - (a) An understanding of the nature of the act and the circumstances in which it has occurred; and
  - (b) Further information to evaluate the possible effect on the financial report. (Ref: Para. A14)
- 19. If the auditor suspects there may be non-compliance, the auditor shall discuss the matter with management and, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgement, the effect of the suspected non-compliance may be material to the financial report, the auditor shall consider the need to obtain legal advice. (Ref: Para. A15-A16)
- 20. If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.

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21. The auditor shall evaluate the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. (Ref: Para. A17-A18)

**Reporting of Identified or Suspected Non-Compliance**

***Reporting Non-Compliance to Those Charged with Governance***

22. Unless all of those charged with governance are involved in management of the entity, and therefore are aware of matters involving identified or suspected non-compliance already communicated by the auditor,<sup>5</sup> the auditor shall communicate with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.
23. If, in the auditor's judgement, the non-compliance referred to in paragraph 22 of this Auditing Standard is believed to be intentional and material, the auditor shall communicate the matter to those charged with governance as soon as practicable.
24. If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

***Reporting Non-Compliance in the Auditor's Report on the Financial Report***

25. If the auditor concludes that the non-compliance has a material effect on the financial report, and has not been adequately reflected in the financial report, the auditor shall, in accordance with ASA 705, express a qualified opinion or an adverse opinion on the financial report.<sup>6</sup> (Ref: Para. A18.1)

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<sup>5</sup> See ASA 260, *Communication with Those Charged with Governance*, paragraph 13.

<sup>6</sup> See ASA 705, *Modifications to the Opinion in the Independent Auditor's Report*, paragraphs 7-8.

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26. If the auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial report has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial report on the basis of a limitation on the scope of the audit in accordance with ASA 705.
27. If the auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance, the auditor shall evaluate the effect on the auditor's opinion in accordance with ASA 705.

***Reporting Non-Compliance to Regulatory and Enforcement Authorities***

28. If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether the auditor has a responsibility to report the identified or suspected non-compliance to parties outside the entity. (Ref: Para. A19-A20)

**Documentation**

29. The auditor shall include in the audit documentation identified or suspected non-compliance with laws and regulations and the results of discussion with management and, where applicable, those charged with governance and other parties outside the entity.<sup>7</sup>  
(Ref: Para. A21)

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<sup>7</sup> See ASA 230 *Audit Documentation*, paragraphs 8-11, and paragraph A6.

## **Application and Other Explanatory Material**

### **Responsibility for Compliance with Laws and Regulations** (Ref: Para. 3-8)

- A1. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with laws and regulations. Laws and regulations may affect an entity's financial report in different ways: for example, most directly, they may affect specific disclosures required of the entity in the financial report or they may prescribe the applicable financial reporting framework. They may also establish certain legal rights and obligations of the entity, some of which will be recognised in the entity's financial report. In addition, laws and regulations may impose penalties in cases of non-compliance.
- A2. The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations:
- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
  - Instituting and operating appropriate systems of internal control.
  - Developing, publicising and following a code of conduct.
  - Ensuring employees are properly trained and understand the code of conduct.
  - Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
  - Engaging legal advisors to assist in monitoring legal requirements.
  - Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

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In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to the following:

- An internal audit function.
- An audit committee.
- A compliance function.

*Responsibility of the Auditor*

- A3. Non-compliance by the entity with laws and regulations may result in a material misstatement of the financial report. Detection of non-compliance, regardless of materiality, may affect other aspects of the audit including, for example, the auditor's consideration of the integrity of management or employees.
- A4. Whether an act constitutes non-compliance with laws and regulations is a matter for legal determination, which is ordinarily beyond the auditor's professional competence to determine. Nevertheless, the auditor's training, experience and understanding of the entity and its industry or sector may provide a basis to recognise that some acts, coming to the auditor's attention, may constitute non-compliance with laws and regulations.
- A5. In accordance with specific statutory requirements, the auditor may be specifically required to report, as part of the audit of the financial report, on whether the entity complies with certain provisions of laws or regulations. In these circumstances, ASA 700<sup>8</sup> or ASA 800<sup>9</sup> deal with how these audit responsibilities are addressed in the auditor's report. Furthermore, where there are specific statutory reporting requirements, it may be necessary for the audit plan to include appropriate tests for compliance with these provisions of the laws and regulations.

*Considerations Specific to Public Sector Entities*

- A6. In the public sector, there may be additional audit responsibilities with respect to the consideration of laws and regulations which may

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<sup>8</sup> See ASA 700 *Forming an Opinion and Reporting on a Financial Report*, paragraph 38.

<sup>9</sup> See ASA 800 *Special Considerations — Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks*, paragraph 11.

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relate to the audit of a financial report or may extend to other aspects of the entity's operations.

**The Auditor's Consideration of Compliance with Laws and Regulations**

*Obtaining an Understanding of the Legal and Regulatory Framework*

(Ref: Para. 12)

- A7. To obtain a general understanding of the legal and regulatory framework, and how the entity complies with that framework, the auditor may, for example:
- Use the auditor's existing understanding of the entity's industry, regulatory and other external factors;
  - Update the understanding of those laws and regulations that directly determine the reported amounts and disclosures in the financial report;
  - Enquire of management as to other laws or regulations that may be expected to have a fundamental effect on the operations of the entity;
  - Enquire of management concerning the entity's policies and procedures regarding compliance with laws and regulations; and
  - Enquire of management regarding the policies or procedures adopted for identifying, evaluating and accounting for litigation claims.

*Laws and Regulations Generally Recognised to Have a Direct Effect on the Determination of Material Amounts and Disclosures in the Financial Report*

(Ref: Para. 13)

- A8. Certain laws and regulations are well-established, known to the entity and within the entity's industry or sector, and relevant to the entity's financial report (as described in paragraph 6(a)). They could include those that relate to, for example:
- The form and content of the financial report;
  - Industry-specific financial reporting issues;
  - Accounting for transactions under government contracts; or

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- The accrual or recognition of expenses for income tax or superannuation costs.

Some provisions in those laws and regulations may be directly relevant to specific assertions in the financial report (for example, the completeness of income tax provisions), while others may be directly relevant to the financial report as a whole (for example, the required statements constituting a complete set of financial statements). The aim of the requirement in paragraph 13 is for the auditor to obtain sufficient appropriate audit evidence regarding the determination of amounts and disclosures in the financial report in compliance with the relevant provisions of those laws and regulations.

Non-compliance with other provisions of such laws and regulations and other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for in the financial report, but are not considered to have a direct effect on the financial report as described in paragraph 6(a).

*Procedures to Identify Instances of Non-Compliance – Other Laws and Regulations* (Ref: Para. 14)

- A9. Certain other laws and regulations may need particular attention by the auditor because they have a fundamental effect on the operations of the entity (as described in paragraph 6(b)). Non-compliance with laws and regulations that have a fundamental effect on the operations of the entity may cause the entity to cease operations, or call into question the entity's continuance as a going concern. For example, non-compliance with the requirements of the entity's license or other entitlement to perform its operations could have such an impact (for example, for a bank, non-compliance with capital or investment requirements). There are also many laws and regulations relating principally to the operating aspects of the entity that typically do not affect the financial report and are not captured by the entity's information systems relevant to financial reporting.
- A10. As the financial reporting consequences of other laws and regulations can vary depending on the entity's operations, the audit procedures required by paragraph 14 are directed to bringing to the auditor's attention instances of non-compliance with laws and regulations that may have a material effect on the financial report.

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*Non-Compliance Brought to the Auditor's Attention by Other Audit Procedures* (Ref: Para. 15)

A11. Audit procedures applied to form an opinion on the financial report may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. For example, such audit procedures may include:

- Reading minutes;
- Enquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, claims and assessments; and
- Performing substantive tests of details of classes of transactions, account balances or disclosures; and

Aus A11.1 Review of breach registers and equivalent records (for example, complaints, whistleblower or suspicious matter reports registers).

*Written Representations* (Ref: Para. 16)

A12. Because the effect on the financial report of laws and regulations can vary considerably, written representations provide necessary audit evidence about management's knowledge of identified or suspected non-compliance with laws and regulations, whose effects may have a material effect on the financial report. However, written representations do not provide sufficient appropriate audit evidence on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained by the auditor.<sup>10</sup>

**Audit Procedures When Non-Compliance Is Identified or Suspected**

*Indications of Non-Compliance with Laws and Regulations* (Ref: Para. 18)

A13. If the auditor becomes aware of the existence of, or information about, the following matters, it may be an indication of non-compliance with laws and regulations:

- Investigations by regulatory organisations and government departments or payment of fines or penalties.

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<sup>10</sup> See ASA 580 *Written Representations*, paragraph 4.

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- Payments for unspecified services or loans to consultants, related parties, employees or government employees.
- Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the entity or in its industry or to the services actually received.
- Purchasing at prices significantly above or below market price.
- Unusual payments in cash, purchases in the form of cashiers' cheques payable to bearer or transfers to numbered bank accounts.
- Unusual transactions with companies or entities registered in tax havens.
- Payments for goods or services made other than to the country from which the goods or services originated.
- Payments without proper exchange control documentation.
- Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.
- Unauthorised transactions or improperly recorded transactions.
- Adverse media comment.

*Matters Relevant to the Auditor's Evaluation* (Ref: Para. 18(b))

- A14. Matters relevant to the auditor's evaluation of the possible effect on the financial report include:
- The potential financial consequences of non-compliance with laws and regulations on the financial report including, for example, the imposition of fines, penalties, damages, threat of expropriation of assets, enforced discontinuation of operations, and litigation.
  - Whether the potential financial consequences require disclosure.

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- Whether the potential financial consequences are so serious as to call into question the fair presentation of the financial report, or otherwise make the financial report misleading.

*Audit Procedures* (Ref: Para. 19)

- A15. The auditor may discuss the findings with those charged with governance where they may be able to provide additional audit evidence. For example, the auditor may confirm that those charged with governance have the same understanding of the facts and circumstances relevant to transactions or events that have led to the possibility of non-compliance with laws and regulations.
- A16. If management or, as appropriate, those charged with governance do not provide sufficient information to the auditor that the entity is in fact in compliance with laws and regulations, the auditor may consider it appropriate to consult with the entity's in-house legal counsel or external legal counsel about the application of the laws and regulations to the circumstances, including the possibility of fraud, and the possible effects on the financial report. If it is not considered appropriate to consult with the entity's legal counsel or if the auditor is not satisfied with the legal counsel's opinion, the auditor may consider it appropriate to consult the auditor's own legal counsel as to whether a contravention of a law or regulation is involved, the possible legal consequences, including the possibility of fraud, and what further action, if any, the auditor would take.

*Evaluating the Implications of Non-Compliance* (Ref: Para. 21)

- A17. As required by paragraph 21, the auditor evaluates the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations. The implications of particular instances of non-compliance identified by the auditor will depend on the relationship of the perpetration and concealment, if any, of the act to specific control activities and the level of management or employees involved, especially implications arising from the involvement of the highest authority within the entity.
- A18. In exceptional cases, the auditor may consider whether withdrawal from the engagement, where withdrawal is possible under applicable law or regulation, is necessary when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances, even when the non-compliance is not material to the financial report. When deciding

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whether withdrawal from the engagement is necessary, the auditor may consider seeking legal advice. If withdrawal from the engagement is not possible, the auditor may consider alternative actions, including describing the non-compliance in an Other Matter(s) paragraph in the auditor's report.<sup>11</sup>

**Reporting of Identified or Suspected Non-Compliance**

*Reporting Non-Compliance in the Auditor's Report on the Financial Report*  
(Ref: Para. 25)

Aus A18.1 If, in the case of an audit conducted under the *Corporations Act 2001*, the auditor identifies non-compliance with an Australian Accounting Standard, defects or irregularities in the financial report or deficiencies, failures or shortcomings in respect of sec 307 of the Act, the auditor's report is to include the information required by the Act.\* The auditor needs to consider any other relevant laws and regulations. If the auditor is in doubt as to the proper interpretation of laws or regulations, or whether non-compliance has in fact occurred, the auditor ordinarily seeks legal advice before expressing an opinion on the financial report.

*Reporting Non-Compliance to Regulatory and Enforcement Authorities*  
(Ref: Para. 28)

A19. The auditor's professional duty to maintain the confidentiality of client information may preclude reporting identified or suspected non-compliance with laws and regulations to a party outside the entity. However, the auditor's legal responsibilities vary by jurisdiction and, in certain circumstances, the duty of confidentiality may be overridden by statute, the law or courts of law. In some jurisdictions, the auditor of a financial institution has a statutory duty to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to supervisory authorities. Also, in some jurisdictions, the auditor has a duty to report misstatements to authorities in those cases where management and, where applicable, those charged with governance fail to take corrective action. The auditor may consider it appropriate to obtain legal advice to determine the appropriate course of action.

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<sup>11</sup> See ASA 706 *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*, paragraphs 8 and Aus 8.1.

\* See sections 308 (2) and (3) of the *Corporations Act 2001*.

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Aus A19.1      In certain circumstances, the auditor has a statutory responsibility to report instances of non-compliance with laws and regulations. For example, in certain circumstances, the auditor is required under the *Corporations Act 2001*, to report to the Australian Securities and Investments Commission (ASIC).<sup>\*</sup> Establishing the appropriate authority to which such a report would be made in a particular instance will depend on the nature and circumstances of the non-compliance. When in doubt, the auditor would ordinarily seek legal advice.

**Considerations Specific to Public Sector Entities**

A20.      A public sector auditor may be obliged to report on instances of non-compliance to the legislature or other governing body or to report them in the auditor's report.

**Documentation** (Ref: Para. 29)

A21.      The auditor's documentation of findings regarding identified or suspected non-compliance with laws and regulations may include, for example:

- Copies of records or documents.
- Minutes of discussions held with management, those charged with governance or parties outside the entity.

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<sup>\*</sup> See ASIC Regulatory Guide 34 *Auditors' obligations: reporting to ASIC* (December 2007) that provides guidance to help auditors comply with their obligations, under sections 311, 601HG and 990K of the *Corporations Act 2001*, to report contraventions and suspected contraventions of the Act to ASIC.

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**Conformity with International Standards on Auditing**

This Auditing Standard conforms with International Standard on Auditing ISA 250 *Consideration of Laws and Regulations in an Audit of Financial Statements* (Redrafted), issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix “Aus”.

Compliance with this Auditing Standard enables compliance with ISA 250.



## Proposed modification (1) to international standard ISA 250

Proposed modification

Include Aus 29.1:

In certain circumstances, the auditor has a statutory responsibility to report instances of non-compliance with laws and regulations. For example, in certain circumstances, the auditor is required under the *Corporations Act 2001*, to report to the Australian Securities and Investments Commission (ASIC)\*. Establishing the appropriate authority to which such a report would be made in a particular instance will depend on the nature and circumstances of the non-compliance. When in doubt, the auditor would ordinarily seek legal advice.

\* See ASIC Regulatory Guide 34 Auditors' obligations: Reporting to ASIC (May 2013) that provides guidance to help auditors comply with their obligations, under sections 311, 601HG and 990K of the *Corporations Act 2001*, to report contraventions and suspected contraventions of the Act to ASIC.

### Rationale for the proposed modification

**The international standard is not consistent with Australian regulatory arrangements.**

The proposed modification is merely to correctly identify the reporting requirements under Australian legislation.

**OR**

**The international standard does not reflect principles and practices that are considered appropriate in Australia.**

NA

### A. Consideration of compelling reason criteria where the international standard is not consistent with Australian regulatory requirements.

#### Compelling reason criteria as per agreed Principles of Convergence

#### Consideration whether the proposed modification meets the criteria

**1. The standard can be modified so as to result in a standard the application of which results in effective and efficient compliance with the legal framework in Australia.**

Yes.

The proposed modifications provides a reference to a requirement under the *Corporations Act 2001*.

**2. The proposed modification does not result in a standard that conflicts with, or results in lesser requirements than the international standard.**

There is no conflict or lessening of the ISA requirements merely adaptations to comply with applicable legislation.

### B. Consideration of compelling reason criteria where the international standard does not reflect principles and practices that are considered appropriate in Australia.

#### Compelling reason criteria as per agreed Principles of Convergence

#### Consideration whether the proposed modification meets the criteria

**1. The application of the proposed modification will result in compliance with**

NA



<b>Proposed modification (1) to international standard ISA 250</b>	
<b>principles and practices considered appropriate by the AUASB.</b>	
<b>2. The proposed modification results in a standard that is clear and that promotes consistent application by all practitioners. (For example, excluding options not relevant in Australia and New Zealand)</b>	NA
<b>3. The proposed modification will promote significant improvement in audit quality in Australia (With improvement in audit quality being linked to one or more of the Applicable Elements in the IAASB's Framework for Audit Quality)</b>	NA
<b>4. The relative benefits of the modification outweigh the cost (with cost being compliance cost and the cost of differing from the international standard, and benefit relating to audit quality).</b>	NA
<b>5. The proposed modification does not conflict with or result in lesser requirements than the international standard.</b>	NA
<b>6. The proposed modification overall does not result in the standard being overly complex and confusing.</b>	NA
<b>7. The proposed modification does not inadvertently change the meaning of the international standard wording by placing more onerous requirements on a practitioner in Australia than necessary to meet the intent of the international standard.</b>	NA
<b>C. Conclusion</b>	
<b>Compelling reasons test met/not met?</b>	The compelling reasons test has been met.
<b>Does the Board agree that the proposed modification meets the compelling reason test, and that ISA 250 should be modified as described above?</b>	