



<b>Project:</b>	<b>Audit Engagement-related Disclosures</b>	<b>Meeting</b>	AASB June 2021 (M181)
<b>Topic:</b>	<b>Project update and next steps</b>	<b>Agenda Item:</b>	9.0
		<b>Date:</b>	7 June 2021
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		<b>Decision-Making:</b>	High
		<b>Project Status:</b>	Decide on the next steps

## Objective of this agenda item

- 1 The objectives of this agenda item are for the Board to:
  - (a) receive an update on progress on relevant related projects and discussions, including recent AUASB, ASIC, CA ANZ, CPA, AICD and APESB meetings (see paragraphs 1-22);
  - (b) consider options for disclosing the audit tenure and decide on next steps (see Agenda paper 9.1);
  - (c) consider the comparison of the auditor remuneration categories recommended by RR15 with those suggested by ASIC and APESB and decide whether to define audit services within each category (see Agenda paper 9.2);
  - (d) decide whether to recommend the IASB to add a project on audit engagement-related disclosures to its work program (see Agenda paper 9.2); and
  - (e) provide views on further project direction (see paragraphs 23-29).

## Attachments

Agenda paper 9.1	Staff Paper: Audit Tenure
Agenda paper 9.2	Staff Paper: Auditor remuneration
Agenda paper 9.3	Letter from ASIC ( <b>Board Only – included in the supplementary folder</b> )
Agenda paper 9.4	APESB ED 03/21 <i>Proposed Amendments to Fee-related provisions of APES 110 Code of Ethics for Professional Accountants (including Independence Standards)</i> ( <b>included in the supplementary folder</b> )

## Background

- 1 The [final report](#) of the PJC Inquiry into the Regulation of Auditing in Australia (PJC report) was issued in November 2020 and is awaiting a formal government response. The two key recommendations relevant for the AASB relate to audit tenure and auditor remuneration were:

### **PJC Recommendation 3a**

*The FRC and ASIC by the end of the 2020-21 financial year, oversee consultation, development and introduction under Australian Standards of defined categories and associated fee disclosure requirements in relation to audit and non-audit services.*

### **PJC Recommendation 6**

*The committee recommends that the Financial Reporting Council, by the end of the 2020–21 financial year, oversee the revision and implementation of Australian standards to require audited entities to disclose auditor tenure in annual financial reports. Such disclosure should include both the length of tenure of the entity's external auditor, and of the lead audit partner.*

- 2 At its February 2021 meeting, the Board directed staff to develop an Exposure Draft amending the current disclosures on auditor remuneration in AASB 1054 *Australian Additional Disclosures* (the ED) based on the recommendations in the AASB Research Report 15 [Review of Auditor Remuneration Disclosure Requirements](#) (RR15). An extract from the minutes is noted below:

#### **Audit Engagement-related Disclosures**

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The Board directed staff to develop a draft Exposure Draft for the April meeting with proposed revised auditor remuneration disclosures based on the work presented in AASB Research Report 15 *Review of Auditor Remuneration Disclosure Requirements* and other outreach and research activities. However, issuance of the ED may be subject to the International Ethics Standards Board for Accountants (IESBA) finalising its projects on fees and non-assurance services and the Government's response to the recommendations in the Parliamentary Joint Committee on Corporations and Financial Services' report on the *Regulation of Auditing in Australia*.

Staff will undertake further research on disclosures about auditor tenure and consult the Auditing and Assurance Standards Board (AUASB) whether such disclosures would be better addressed in auditing standards. To promote international consistency, the Board will further recommend that the IASB considers adding a project on audit engagement-related disclosures as part of the IASB's forthcoming Agenda Consultation.

Action:

Staff

## Project update

- 3 Following the February 2021 AASB meeting, AASB staff have continued liaising with the representatives from relevant parties, including the FRC, ASIC, AUASB, APESB, AICD and professional bodies to help ensure there is a coordinated approach to addressing the PJC recommendations. A summary of progress on relevant related projects and discussions is noted below.

### IESBA/APESB projects on fees and non-assurance services

- 4 The Accounting Professional and Ethical Standards Board (APESB) progressed work on the revision of APES 110 *Code of Ethics for Professional Accountants (including Independence*

*Standards*) (the Code). The review is driven by proposed amendments to *the International Code of Ethics for Professional Accountants (including International Independence Standards)* (the IESBA Code) and by recommendations of the PJC report.

- 5 While the IESBA Code changes focus mainly on addressing the issues of threats to auditors' independence arising from the fee charged and the provision of non-assurance services, the APESB Exposure Draft addresses PJC recommendation 3<sup>1</sup> and recommendation 5<sup>2</sup>.
- 6 APESB has been part of the FRC working group that have been considering how to address the recommendations from the PJC Inquiry.
- 7 APESB had concluded that these two recommendations of the PJC Inquiry can be addressed through inclusions in the proposed amendments to the Code.
- 8 The APESB Board discussed the preliminary draft of the APESB ED at the March 2021 meeting (See [Meeting Highlights](#)) and the APESB ED was subsequently approved by the APESB Board at the May 2021 meeting (See [Meeting Highlights](#)). Related APESB staff papers for both these meeting can be found on the [APESB website](#).
- 9 On 28 May 2021, the APESB issued ED 03/21 [Proposed Amendments to Fee-related provisions of APES 110 Code of Ethics for Professional Accountants \(including Independence Standards\)](#) (the APESB ED). Among other proposals, the APESB ED propose that the Code should incorporate guidance on categories of audit services and the description of those services. These amendments result from APESB's attempt to address PJC recommendations 3 and 5 as the IESBA code does not include or propose any guidance on the categories of audit services or the definition of services within each category<sup>3</sup>.
- 10 The key proposed amendments to the Code include:
  - (a) amendments to the current version of the fee-related provisions of the Code based on the IESBA amendments;
  - (b) providing information on the different categories of services that may be provided by an auditor;
  - (c) broadening the requirement for audit partners not to be incentivised, either directly or indirectly, for selling non-assurance services to their audit clients to now prohibit incentivisation for sales of non-assurance services to any audit clients of the Firm; and

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1 Recommendation 3: The committee recommends that the Financial Reporting Council, in partnership with ASIC, by the end of the 2020-21 financial year, oversee consultation, development and introduction under Australian standards of:

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

2 Recommendation 5: The committee recommends that the APESB consider revising the Code to include a safeguard that no audit partner can be incentivised, through remuneration advancement or any other means or practice, for selling non-audit services to an audited entity.

3 However, other countries such as the UK and USA have these within their equivalent standards.

(d) addition of a threshold to assess fee dependency on a referral source that refers multiple audit clients to a firm, an individual partner or an office within the Firm.<sup>4</sup>

11 These APESB proposals in item (b) in paragraph 10 are considered in detail in Agenda Paper 9.2.

#### AICD project on audit tenure

12 The Australian Institute of Company Directors (AICD) is currently working on guidance for the Board of Directors on disclosing the information on audit tenure as a response to the PJC recommendation 6. The AICD plans to publish this guidance in the next financial year and suggests listed entities (say ASX200) voluntarily adopt it for 2022/23. Staff will continue to liaise with AICD as they progress with this project.

13 Staff have met with a representative from AICD. Even though the PJC recommendation 6 is directed to FRC, the AICD representative has expressed the view that the AICD has a responsibility towards the industry to reflect on these recommendations and issue appropriate guidance to enhance audit quality.

14 The AICD representative expressed the view that the audit tenure should be disclosed in the directors' report due to the following reasons:

(a) The Directors' Report appears appropriate for the disclosure of audit tenure as the directors are considered responsible for the auditor's independence assessment. The Audit Committee's role is to oversee the audit process and raise any audit quality concerns with the board of directors.

(b) Disclosure of audit tenure is similar to auditor's independence declaration currently disclosed in the directors' report.

(c) This disclosure will mostly be applicable for entities with public interest (i.e large listed companies with an audit committee).

(d) Director taking responsibility for all audit quality relating issues would be beneficial in terms of good governance practices.

15 The AICD representative also expressed the view that this guidance could be incorporated into the ASX Corporate Governance Principles subject to the decisions by the ASX Corporate Governance Council and pending any Government decision on an amendment to the Corporations Act 2001 (the Act).

#### CAANZ and CPA discussion

16 Staff have met with the CAANZ and CPA representatives. The CAANZ is supportive of a director-led approach on disclosure of auditor tenure rather than mandating the disclosure in the financial statements. CAANZ representative believes that it will provide the right context for

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<sup>4</sup> However, item (d) is not related to the PJC recommendations. It is based on regulatory concerns in the SMSF sector and it is an Australian specific issue.

the information as it relates to audit quality, and it will emphasise that overseeing auditor appointments is an important role of those charged with governance.

- 17 The CPA Australia representatives indicated that they had not formed a view on the most appropriate location of the disclosures in the long term, however transparency was supported which prioritised user needs. Currently, auditor related disclosures are made both in the directors' report (listed companies) and in the financial statements (AASB 1054). The CPA Australia representatives acknowledged that disclosing auditor tenure in the financial statements could have certain advantages, as it would supplement the auditor related information currently disclosed in the financial statements. Whilst this could provide for the reporting of auditor tenure on a consistent basis, they acknowledge that the directors' report may provide greater scope for narrative disclosure, which could be complemented by the Board's broader evaluation of audit quality. They support exploration of how audit tenure, both quantitative and relevant narrative, can best be disclosed in the medium to long term. In the short term, they support guidance to encourage transparency of audit tenure in annual reports whilst a more holistic approach to audit related disclosures is developed and implemented.

#### Discussion with UAC members

- 18 Staff asked for views from the members of the AASB User Advisory Committee (UAC) as to where the audit tenure should be disclosed (i.e in the financial statements or directors' report). There were mixed views expressed by UAC members:
- (a) One member supported the disclosure in Directors' Report as it is responsibility of the directors.
  - (b) Two other members preferred disclosure in the financial statements as it would accompany audit fee disclosures and result in information of similar nature being disclosed in one place.
  - (c) Number of others agreed while the audit tenure disclosure is important, it does not matter where it sits as long as the information is disclosed.

#### AUASB project/board meeting discussions

- 19 The AUASB met on 20 April 2021 and received an update on the preliminary work being done in response to the PJC recommendations, including how recommendations relating to auditor remuneration and auditor tenure are classified and disclosed. The minutes of the meeting are not yet available; however, the AUSB Highlights publication noted that the AUASB Technical Staff have been and will continue to work closely with the FRC, AASB, ASIC, APESB and AICD on this issue.<sup>5</sup>
- 20 At the meeting, the AUASB staff presented the options and analysis on how to address the PJC recommendation on audit tenure disclosure. The AUASB discussed the following possibilities for audit tenure disclosure:<sup>6</sup>
- (a) Financial report
  - (b) Directors' report

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<sup>5</sup> [https://www.auasb.gov.au/admin/file/content102/c3/AUASB\\_Highlights\\_Mtg124\\_Apr21.pdf](https://www.auasb.gov.au/admin/file/content102/c3/AUASB_Highlights_Mtg124_Apr21.pdf) (accessed 26/5/2021)

<sup>6</sup> <https://www.auasb.gov.au/admin/file/content102/c3/AUASBMTG124PublicPapers.pdf> (accessed 26/5/2021)

- (c) Auditor's independence declaration required by S 307C
  - (d) Audit Committee Report or other Corporate Governance reporting within the Annual Report
  - (e) Auditor's report
- 21 From discussions with AUASB staff, AASB staff understand that at the meeting, the AUASB agreed that disclosure of audit tenure in the directors' report would require an amendment to the Corporation Act 2001 (the Act) and then would be mandatory only for entities preparing audited financial statements under the Act. The AUASB noted that amending the Act may not be achievable on a timely basis and, therefore, agreed that including the disclosure requirement in the financial statements and amending the Accounting Standards would also be acceptable. This would need to be considered by the AASB.
- 22 The AUASB further noted that mandating the disclosure requirements by the Accounting Standard would have a broader impact as it would affect all entities preparing their financial statements under the Accounting Standards. For the non-Corporations Act 2001 entities in this population, there is likely to be fewer if any independence disclosures and requirements, such as those related to auditor independence declarations, partner rotation, or long association. In the absence of in-context independence disclosures, the AUASB discussed the risks of users misunderstanding the tenure disclosures.

## **Next Steps**

### Future project direction

- 23 Staff considered whether the Board should wait for a Government response on the PJC report before issuing an ED with the proposed amendment to AASB 1054 (subject to Board's deliberations at this meeting). The timing of the government response to the PJC report is unknown.
- 24 Staff acknowledge that the project direction and next steps for the audit tenure and auditor remuneration disclosures<sup>7</sup> are dependent on the Board's decisions at this meeting.
- 25 The government response (when it is issued) may impact the Board's response in addressing the PJC recommendations directed to FRC. If the Board proceeds ahead of Government and subsequently the Government response is not in line with Board's expectations, the Board might have to change the decisions previously made. Those changes would result in additional communication to the public.

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<sup>7</sup> However, as indicated in the PJC report, clearly defining categories of fees paid for non-audit services may increase transparency of an entity's use of non-audit services provided by their auditor and consequently allow stakeholders to better evaluate the independence of the auditor. Furthermore, recommendations of RR15, results of UAC survey, ASIC letter and the work already carrying out by the APESB are sufficient to demonstrate the need for further action by the AASB.

**Question to Board members**

Q1. Do Board members have a view as to whether to wait for a Government response before issuing an ED, or whether to proceed ahead of government response and progress to issuing the ED considering the staff comments in paragraphs 23-25?

Timeline for the project

26 Staff consider that the next immediate step is to draft the ED and present it at the September meeting. While the timing of the issue of the ED is subject to Board's decision on whether to wait for the government response, the Board can continue deliberating the proposals to amend AASB 1054.

27 Staff would like to present the below short-term timeline for Board's consideration:

Date	Project timeline and milestones
At this meeting	<ul style="list-style-type: none"> <li>• project status update</li> <li>• Board consideration and decision on next steps</li> </ul>
June - August	<ul style="list-style-type: none"> <li>• Staff to draft the ED</li> </ul>
August	<ul style="list-style-type: none"> <li>• Staff to draft comment letter to the APESB and approve the comment letter out of session by Chair (subject to decisions at this meeting)</li> </ul>
31 August	<ul style="list-style-type: none"> <li>• comment period for APESB ED closes</li> </ul>
September 2021 meeting	<ul style="list-style-type: none"> <li>• Board to deliberate the proposed disclosure requirements including review of a working draft of the ED (subject to decisions at this meeting)</li> </ul>
November 2021 meeting	<ul style="list-style-type: none"> <li>• Board to consider final draft of the ED (subject to decisions at this meeting)</li> <li>• Board to receive update on the feedback received for the APESB ED and their project direction</li> </ul>

28 As the timing of the issuance of the ED is subject to the Board's decisions at this meeting and timing of the government response, staff will provide an updated timeline for Board's consideration at September meeting.

29 Staff will monitor any changes to the fee related provisions in the APESB ED and provide update to the Board as appropriate.

**Question to Board members**

Q2. Do Board members agree with staff comments in paragraphs 26-29?

**AASB submission to the IASB Agenda Consultation**

30 To promote international consistency, the Board decided at its February meeting to recommend the IASB to add a project on audit engagement-related disclosures to its work

program. The recommendation would be part of the AASB submission to IASB's Agenda Consultation issued in March 2021, which is open for comment until 27 September 2021.

- 31 However, as the disclosures relating to audit tenure and audit remuneration are to be addressed locally, staff recommend the Board to reconsider the need for the IASB to add this project to its work plan.

**Question to Board members**

Q3. Do Board members wish to recommend the IASB to add a project on audit engagement-related disclosures to its work program as part of the AASB submission to IASB's Agenda Consultation?