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Periodic Comprehensive Review of the External Auditor

Guide for Audit Committees

Australian Institute of Company Directors

Australian Government
Auditing and Assurance Standards Board

About the Australian Institute of Company Directors

The Australian Institute of Company Directors (AICD) is committed to strengthening society through world-class governance. We aim to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. Our membership of more than 45,000 includes directors and senior leaders from business, government and the not-for-profit sectors. For more information about the AICD see the AICD website.

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About the Auditing and Assurance Standards Board

The Auditing and Assurance Standards Board (AUASB) is an independent, non-corporate Commonwealth entity of the Australian Government, responsible for developing, issuing and maintaining auditing and assurance standards. Sound public interest-oriented auditing and assurance standards are necessary to reinforce the credibility of the auditing and assurance processes for those who use financial and other information. The AUASB standards are legally enforceable for audits or reviews of financial reports required under the ***Corporations Act 2001***. For more information about the AUASB see the AUASB website.

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Contents

Foreword

Audit quality is vitally important to stakeholder and investor confidence in financial reporting and the operation of capital markets.

Whilst auditors have the primary responsibility for audit quality, it is best achieved in an environment where there is strong support from other participants in the financial reporting chain. The importance of directors, and in particular audit committees, in supporting and promoting audit quality is emphasised in Australian Securities and Investment Commission's (**ASIC**) Information Sheet 196 - *Audit quality – The role of directors and audit committees*.

A key responsibility of audit committees is to oversee the quality and effectiveness of their auditor. This assessment should be performed continuously and on an annual basis. ASIC Information Sheet 196 provides comprehensive guidance to directors and audit committees about supporting audit quality on an ongoing basis. To complement this, we recommend that audit committees periodically prepare a formal report to the board on the quality of the audit by the incumbent auditor over a number of years. This publication is a tool which includes guidance to perform a periodic comprehensive review and to communicate a well-informed conclusion to the board on whether to retain the auditor or remove them.

We believe stakeholder and investor confidence can be enhanced by transparency of the process audit committees have in place to assess the quality of their auditor. Therefore, we encourage appropriate transparency and public disclosure of that process.

The AICD and AUASB support all parties in the financial reporting chain working together to maintain audit quality and high-quality financial reporting. We believe this publication will assist audit committees to fulfill their responsibilities including supporting their auditor in the achievement of high audit quality, and providing directors with greater confidence in the accuracy of their corporate reporting.

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Introduction to the guide

The guide complements the Australian Securities and Investment Commission's (**ASIC**) Information Sheet 196 - ***Audit quality – The role of directors and audit committees*** which includes an annual assessment of the auditor by the audit committee.

This guide is based upon a similar guide, ***Periodic comprehensive review of the external auditor: Tool for audit committees***, prepared by the Chartered Professional Accountants of Canada (CPA Canada), the Canadian Public Accountability Board (CPAB) and the Canadian Institute of Corporate Directors (ICD). The authors wish to acknowledge the work of CPA Canada, the CPAD and the ICD and thank them for allowing us to use their tool as a basis for this document.

The role of directors and audit committees in supporting audit quality

Audit quality supports high quality financial reporting and is vital to stakeholder and investor confidence.

Directors have primary responsibility for the quality of financial reporting, which is supported by high quality audits. Whilst auditors have the primary responsibility for audit quality, it is best achieved in an environment where there is strong support from other participants in the financial reporting chain. Directors and in particular, audit committees, have key roles to play.

Directors and audit committees should continually assess the quality and effectiveness of the auditor. ASIC Information Sheet 196 provides a comprehensive guide for directors and audit committees including the features of audit committees that may help in promoting and supporting audit quality. In addition, matters communicated to directors and audit committees from ASIC audit inspection program (see *ASIC Regulatory Guide RG 260 Communicating audit findings to directors, audit committee and senior managers*) and ASIC's audit inspection reports, provides relevant information for audit committees.

One of the roles of the audit committee is to assist the board to fulfill its corporate governance and oversight responsibilities in areas including annual financial reporting and oversight of the external auditor. The ***ASX Corporate Governance Principles and Recommendations*** also state the role of the audit committee is usually to review and make recommendations to the board in relation to:

- the appointment or removal of the external auditor
- the fees payable to the auditor for audit and non-audit work
- the rotation of the audit engagement partner
- the scope and adequacy of the external audit
- the independence and performance of the external auditor
- any proposal for the external auditor to provide non-audit services and whether it might compromise independence of the external auditor.[1]

1. Recommendation 4.1, ASX Corporate Governance Council, Corporate Governance Principles and Recommendations (4th ed.)

What is the purpose and who is this guide for?

This guide has been prepared to provide supplementary guidance on process matters where a formal review on audit quality by an incumbent auditor is prepared (for example every five years). This guide is for the purposes of assisting audit committees of primarily listed companies in Australia, to fulfill their responsibilities in assessing the quality and effectiveness of their auditor and deciding whether to retain the auditor or remove them.

It is the responsibility of the board, and the audit committee, to make the assessment outlined in this guide. While management would be expected to provide input, it is possible that they may have interests that are not fully aligned with the conduct of quality audits (for example they may have incentives which may lead to setting low audit fee). Therefore, the responsibility for the assessment of the auditor cannot be delegated.

Areas for the audit committee to consider and assess

This periodic comprehensive review guide focuses on three key areas relevant to audit quality for the audit committee to consider and assess:

1. **Independence, objectivity and professional scepticism** — Does the auditor approach their work with objectivity to ensure they appropriately question and challenge management's assertions in preparing the financial statements?
2. **Quality of the engagement team** — Does the audit firm put forward team members with the appropriate industry and technical skills to perform an effective audit?
3. **Quality of communications and interactions with the auditor** — Are the communications with the auditor (written and oral) clear, concise and free of boilerplate language? Is the auditor open and frank, particularly in areas of significant judgments and estimates or when initial views differ from management?

Within each of these factors, a number of sub-questions are listed as possible indicators of audit quality. The audit committee needs to determine which of these indicators are most relevant in its circumstances and what information is available to assist them in the assessment.

The periodic comprehensive review guide does not require the audit committee to come to an overall measure or a final score trying to measure audit quality. Rather, it helps the audit committees review the relationship. As a result of the findings the audit committee may be entirely satisfied with the auditor's performance. The audit committee may identify potential areas for improvement for the audit firm (and for the audit committee's own processes). Alternatively, the review might raise significant concerns in which case the audit committee may consider recommending to the full board that the audit should be put out for tender.

The guide is not fixed and may be adapted to meet the entity's specific circumstances. The audit committee may identify questions that are particularly relevant to its circumstances on which it needs to focus and ignore those that are less relevant. The guide allows space for the addition of other questions and points to consider as necessary.

Although it is not strictly part of the comprehensive review, as part of its process the audit committee may wish to review its policies on what non-audit services may be provided by the auditor and the processes the audit committee has in place for approving these services and related fees. Where there is an internal audit function that the audit committee wishes to review, then some of the questions might also be applied to that function.

Annual/ongoing assessment vs comprehensive assessment

The periodic comprehensive review is not a substitute for annual/ongoing reviews of audit quality using ASIC Information Sheet 196. They may also wish to utilise, ***Audit Committees: A Guide to Good Practice*** which is produced by the AUASB, AICD and the Institute of Internal Auditors-Australia.

Absent any concerns, the annual/ongoing assessment would be expected to be a less time-consuming process than the periodic comprehensive review. An annual assessment will also likely focus on the most recent audit, whereas the comprehensive review encourages audit committees to step back and consider issues in a broader light.

Directors should also consider transparency of their process to support audit quality as detailed in ASIC Information Sheet 196:

> "Directors might wish to consider whether to comment publicly on the role of the directors and audit committee in supporting audit quality. For example, they might discuss how the directors and audit committee supported audit quality when recommending the appointment of auditors, assessing the auditor's ongoing performance or reviewing audit fees. These comments could, for example, accompany the annual financial report or be made available in a statement on the company's website."

When and how frequently should the comprehensive review be undertaken?

The frequency is dependent on the specific circumstances of the entity, however it is recommended that a five year period and resultant disclosure may be appropriate. Audit committees may consider timing around engagement partner rotation as a comprehensive review may be most effective once the current engagement partner has had a year or two to establish their own approach or style of working with the audit committee. Timing might also be influenced by whether membership of the audit committee has changed recently and should consider factors such as the tenure of the audit committee chair.

Assuming annual/ongoing reviews have been conducted, the periodic comprehensive review guide focuses on the results of prior annual assessments (including from the most recent audit) and the incremental work over and above annual/ongoing assessments required of an audit committee. If the audit committee has not conducted or has no record of annual/ongoing assessments, the audit committee may need additional background information or may need to set in place a process of annual/ongoing reviews prior to undertaking a comprehensive review.

Comprehensive Periodic Review Process

The periodic comprehensive periodic review process is detailed below. Appendix A sets out details of the steps 1 to 4, including the questions that audit committees might like to ask at each stage of the process and documents and information that they might require. The matters outlined in Appendix A may also be part of an ongoing or annual review.

STEP 1

Determine the scope, timing, process and any areas of focus.

STEP 2

Obtain input from entity personnel.

STEP 3

Obtain audit firm input.

STEP 4

Assess areas for the audit committee to consider.

STEP 5

Conclude on the comprehensive review and communicate the results.

STEP 6

Disclosure of results.

STEP 1

Determine the scope, timing, process and any areas of focus

The audit committee determines the scope, timing and process of the periodic comprehensive review. This includes determining what period of time should be covered, what information is required from entity personnel, and what input is required from the audit firm. It also includes determining what questions the audit committee needs to consider in conducting the review. The appropriate sections of the guide are amended by the audit committee chair to reflect these determinations.

The audit committee responsibilities for determining the scope, timing and process for the comprehensive review cannot be delegated to, or influenced by, either management or the auditor. While management and the auditor each have a supportive role to play in a comprehensive review, overall responsibility resides with the audit committee.

STEP 2

Obtain Input from entity personnel

The audit committee obtains information from management, with potential questions for the Chief Executive Officer, the Chief Financial Officer, internal auditors and others as considered necessary. The audit committee will need to determine from whom input is required, the specific questions to be addressed and whether the audit committee wishes to obtain input in writing or through discussions.

STEP 3

Obtain input from the auditor

The audit committee obtains information from the external audit firm. Note that, dependent on the time and work involved, the external audit firm might quite reasonably charge for the time taken to provide this information.

When gathering information from the audit firm, the audit committee might seek the involvement of senior members of the audit firm, including the engagement partner and senior audit firm partners with firm leadership responsibilities including quality control and audit quality.

STEP 4

Assess areas for the audit committee to consider

This section of the tool sets out the areas to be addressed and considered by the audit committee. The audit committee should have been supplied with the input from entity personnel and the external audit firm. Ideally, audit committee members would consider the questions posed to them in Step 4 individually before coming together in a meeting and sharing their views and comparing them with those of entity personnel and the audit firm. This is the most detailed part of the process and audit committee members will need to set aside sufficient time to undertake it.

STEP 5

Conclude on the comprehensive review and communicate the results

The audit committee now makes conclusions from conducting the review and decides how the audit committee will record and communicate the results to the board.

If the preliminary results of the comprehensive review are unsatisfactory, the audit committee may need to perform further work to determine whether its preliminary conclusions are justified and to consult with those affected by its recommendations including the audit firm and management.

When the audit committee has completed the comprehensive review process, it will be able to form an opinion on the performance of the auditor. A number of possibilities arise from that consideration:

- If there are no significant concerns, then the audit committee might recommend to the board that the entity should retain the current audit firm.
- The audit committee may identify some concerns with the auditor or its own processes and might require that there be some adjustments made to current arrangements. It might require certain assurances from the auditor. Finalisation of the comprehensive review might await a satisfactory outcome of those matters.
- If serious concerns have arisen (or for other reasons the audit committee wishes to test the market) the audit committee may recommend to the board that the audit be put out for tender. The current auditor may be invited to participate in that tender.

The audit committee may also recommend other actions to the board. For example, the audit committee may decide that the next comprehensive review should be performed earlier than normal or that the next annual assessment of the auditor should focus on evaluating the effectiveness of planned remedial actions. The audit committee may also recommend changes to entity policies dealing with matters such as the hiring of audit firm staff or the provision of non-audit services. The audit committee may also identify ways that they and/or management may further support the auditor to enhance the quality and effectiveness of the audit.

Once the board has reviewed and approved the outcomes of the comprehensive review, the board should determine the nature and extent to which the results are to be communicated to management, the audit firm, and any other parties it believes should be informed as well as any public disclosure.

Having completed its process, the audit committee may seek the input of others involved in the review process to help identify potential improvements to the comprehensive review process. Changes to the review's scope, timing and process may be appropriate. For example, the audit committee may identify information for the upcoming review period that is useful to capture on an ongoing basis rather than at the end of the period.

STEP 6

Disclosure of results

Public disclosure by the board informs stakeholders that the audit committee has conducted a periodic comprehensive review of the auditor in arriving at its recommendation to the board. Public disclosure may improve confidence in the board's processes relevant to supporting audit quality and the quality of financial reporting. Such disclosure should include some or all of the following information:

- background and context to the external audit, including such items as:
  - the number of years audited (tenure) by the incumbent auditor[2]
  - the audit firms involved and their location
  - analysis of the total services provided over the review period with explanations of significant fluctuations
  - overview of the audit approach, including locations visited and use of specialists
- the time period covered by the review
- outline of the process followed
- conclusions from the review and decision whether to retain the auditor.

Where the board has followed the process set out in this guide then they may wish to disclose that fact.

Boards might also wish to disclose how they review auditor independence, for example, they approve the auditor providing non-audit services to the entity where that occurs. The directors will already have made a statement that the provision of non-audit services by the auditor is compatible with independence, so this provides for the board to set out the basis on which they make that declaration.

The board should inform the auditor of the matters that they will be disclosing and may need to seek legal advice on when, how and where in the entity's regulatory and other document to communicate the results of the review. When the audit committee's conclusion is to retain the auditor, public disclosure could be incorporated into existing reports such as the Operating and Financial Review or the directors' report. Alternatively, the board might choose to issue a stand-alone report outlining the results of the comprehensive review.

When the board's decision is to put the audit out to tender, the nature and timing of the public disclosure will depend on the circumstances. For example, if the incumbent is permitted to bid, it may be appropriate to publicly disclose the comprehensive review only once the tendering process is complete. In this circumstance, the conclusion from the comprehensive review may indicate whether the incumbent auditor has been retained or a new auditor appointed. In other circumstances, such as where the incumbent auditor is not invited to bid, the audit committee may need to consider more timely public disclosure. Legal advice should be obtained in either circumstance.

2. How tenure is defined is a matter for the board taking into account the history of the entity and any changes or mergers of the external auditor during the period in which it has audited the entity. The disclosure should include this information so the board's defnition of tenure is clear to users.

Appendix A - Detailed Process

STEP 1

Determine the scope, timing, process and any areas of focus

Consider the scope, timing and process for the comprehensive review. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:

1. Does the timing of the review make sense given audit committee composition, engagement partner rotation or other entity issues?[3]
2. What is the appropriate timing of the comprehensive review in relation to the audit committee's planned meeting agendas? What additional resources might be needed and what additional time will audit committee members need to devote to the review?
3. Do the results of prior annual assessments indicate areas that require particular attention in this comprehensive review?
4. Have there been any red flags or areas of concern such as significant reporting issues that will need to be addressed in the comprehensive review (e.g. emerging audit risks, the results of ASIC's audit inspection program, restatements, significant financial reporting criticisms related to the entity made by ASIC or in the media).
5. Is there any additional information or questions that are not already set out in the guide that the audit committee may require to assist them in their evaluation?

3. Note that it may be appropriate to conduct a comprehensive review before having five years' experience of annual assessments of the external auditor, for example, when applying this publication's guidance for the first time, when the audit firm's tenure is already long, if problems have been identified, or if another triggering event has occurred, such as a change in the entity's corporate structure.

STEP 2

Obtain input from entity personnel

Consider having entity personnel obtain the following information for the period under review.

1. Tenure of the auditor including whether this takes into account antecedent firms.
2. Analysis of total services provided by the audit firm, covering audit and non-audit services and related fees, since the last comprehensive review[4]. The audit committee might consider having the entity provide an analysis of other auditors' fees for similar services to comparable entities, where available, to allow some benchmarking to take place.
3. Relevant audit committee meeting minutes and written results of annual assessments (where available).
4. Company policies for awarding non-audit work and any reports by management on how ithe company has complied with those policies.
5. Company hiring and director appointment policies regarding former audit firm staff and analysis of key entity personnel that were previously employed by the audit firm. Hospitality and/or gifts provided by the external audit firm to entity staff or the board or by the entity to the auditor.
6. Information about any significant financial reporting matters that have been questioned by regulators or media reports that may have relevance for the relationship with the audit firm.
7. Summary of auditor's reports (e.g., consolidated financial statements, subsidiary financial statements, reports to regulators, special reports).
8. Summary of reports issued by the auditor to the audit committee, including the planned scope of the audit and significant findings.
9. Summary of communications by the auditor of relationships and other matters bearing on independence.[5]
10. Summary of reports by the auditor to management.
11. Transparency reports of the audit firm.[6]
12. Annual reports of the audit firm (if available).
13. ASIC's audit firm inspection report/s[7] and the results of any disciplinary actions from the Accounting Professional Bodies.
14. Where operations are conducted in another jurisdiction, any major or significant findings by an auditor or security regulator in relation to the firm in that jurisdiction.

4. Corporations Act 2001 s 300(11B) This information is disclosed in the directors' report of listed entities as well as a statement whether the directors are satisfied the non-audit services did not compromise the auditor's independence

5. Auditing Standard ASA 260 requires the auditor to communicate a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and all relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgement, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial report for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and the related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level.

6. Section 322 of the Corporations Act provides that an auditor must publish a transparency report on its website if it has conducted audits of any combination of 10 more bodies such as listed companies or authorised deposit-taking institutions.

7. ASIC's audit firm inspections cover the largest six national firms, and other firms that audit the financial reports of listed entities and other public interest entities. The relevant reports are published on ASIC's website.

INPUT FROM CEO/CFO

Audit quality considerations

Request the CEO and/or CFO and potentially the CRO, COO or Head of Internal Audit provide their input in the following areas, noting any significant observations or trends they have identified during the period of the comprehensive review, including for the most recent audit:

1. How do you regard on the **independence, objectivity and professional scepticism** of the auditor?[8] In particular:
   a. In your opinion, how does the auditor demonstrate integrity and objectivity, for example, by maintaining a respectful but questioning approach throughout the audit?
   b. From your perspective, did the auditor exhibit sufficient professional scepticism in challenging estimates and accounting policy choices?
   c. How forthright is the auditor in dealing with difficult situations, for example, by proactively identifying, communicating and resolving judgment or technical issues?
2. Has the auditor maintained the **quality of the engagement team** throughout the review period? In particular:
   a. How would you assess the technical competence and ability of the auditor (partner and across the audit team) to apply knowledge in practice, for example by using technical knowledge and independent judgment to provide appropriate analysis of issue?
   b. How would you assess the auditor's understanding of the business, the industry and environment in which it operates, risk areas and key issues relevant to the financial report; for example, by demonstrating an understanding of the entity's specific business risks, processes, systems and operations?
   c. How sufficient are resources assigned by the auditor to complete work to a high standard and in a timely manner, for example, by providing access to specialised expertise during the audit and assigning additional resources to the audit as necessary to complete work effectively and in a timely manner?
   d. To what extent has the audit engagement team consulted and used specialists on complex technical matters (e.g. for complex asset and financial instrument valuations, or using specialists such as geologists or actuaries, or information technology system experts)?
   e. Are the firm's arrangements for supervising and reviewing the audit, and internal firm quality reviews and controls, adequate (including in connection with foreign and domestic component audits)?
   f. To what extent has the engagement partner maintained quality control over work performed in domestic and any foreign locations?
   g. Has the audit firm maintained an innovative approach applying new work methods and technologies to enhance the effectiveness of the audit?

8. Note that clearly it may be difficult for management to provide an impartial view of the independence, objectivity and professional scepticism of the external auditor so its perspectives should be weighed accordingly.

3. How do you regard the **communication and interaction with the auditor** throughout the review period? In particular:
   a. How candid and complete was the dialogue between the engagement partner and management? How well did the engagement partner explain their views on management's accounting positions as well as auditing issues?
   b. How effectively does the auditor provide timely and informative communications about accounting and other relevant developments?
   c. How does the auditor communicate about matters affecting the firm or its reputation, for example, by advising management on significant matters pertaining to the firm while respecting the confidentiality of other clients' information and by complying with professional standards and legal requirements?
   d. Did the auditor raise relevant and useful comments in their management letters?
4. Provide your overall views on how your relationship with the auditor contributed to your ability to produce reliable financial reporting throughout the comprehensive review period.

Quality of service considerations

Request the CEO and/or CFO provide input in the following areas, noting any significant observations or trends they have identified during the period of the comprehensive review, including for the most recent audit:

1. To what extent is the auditor effective in completing the audit on a timely basis?
2. To what extent does the auditor keep management informed about the progress of the audit and difficulties encountered?
3. To what extent has the engagement team maintained a respectful and professional attitude during the audit?
4. Did the auditor raise key issues affecting the financial report in a timely manner? To what extent was the auditor proactive in identifying information requirements and timely in requesting information from management?
5. Did the auditor identify audit adjustments as a result of the audit process? If yes, what was their nature and materiality?

INPUT FROM INTERNAL AUDIT

Request internal audit staff (where relevant) provide input in the following areas, noting any significant observations or trends they have identified during the period of the comprehensive review, including for the most recent audit:

1. Did the auditor liaise with internal audit to understand the scope, timing and extent of work conducted by the internal auditor that may inform the auditor's assessment of risk?
2. Any other observations on the work of the external auditor?

STEP 3

Obtain input from the auditor

Audit quality considerations

Please answer the following questions:

1. What are the key elements of the firm's quality control processes and how have they been applied to the entity's audit?
2. What steps have been taken to address possible institutional familiarity threats?
3. Can the audit firm explain the basis for its independence declaration?
4. What are the firm's plans for the training and development of the engagement team?
5. What are the firm's expectations as to future partner rotation or other changes to senior engagement team personnel?
6. How are the size, resources and geographical coverage of the audit firm changing?
7. How significant is the entity's size and the fees paid by the entity to the audit firm? Does the audit firm believe that the size of those fees represents any challenge to independence?
8. How has the engagement team addressed potential risks of material fraud (for example, incorporating an element of unpredictability into audit procedures during the period)?
9. What efforts are being made to enhance audit quality within the audit firm generally and the external audit of the entity specifically?
10. How is the audit firm innovating and dealing with areas of emerging risk?
11. To what extent are audit activities performed through offshoring arrangements? How did the engagement partner maintain quality control over the parties performing the activities?
12. If portions of the audit were performed by other teams in various domestic and foreign locations, by the firm's global network or other audit firms, was the engagement partner sufficiently and appropriately involved throughout the engagement, including assessing their technical skills, experience and professional objectivity and maintaining quality control over their work?
13. Is the audit firm's relevant expertise in the industries and markets in which the entity operates adequate and how has it been evolving?
14. What are the audit firm's future plans to serve the entity with an engagement team with appropriate expertise?
15. How have overall public aggregate thematic findings from ASIC's inspections or surveillances that are common across many audits and firms been addressed by the auditor?
16. If the audit firm is subject to ASIC's audit firm inspection process or the Accounting Professional Bodies, what findings have been made about the audit firm over the review period?
17. What comments does the audit firm have to make on any findings by ASIC or a professional accounting body about the audit firm, including how these findings have been addressed by the audit firm?
18. What reputational challenges, if any, are facing the audit firm or its affiliate firms and how are these being addressed?
19. Are there any significant re-statements that the audit firm has been involved in that the firm wishes to address with the auditor?

STEP 4

Assess areas for the audit committee to consider

REVIEW FOR SIGNIFICANT OBSERVATIONS AND TRENDS DURING THE REVIEW PERIOD, INCLUDING THE MOST RECENT AUDIT

The audit committee now considers the information gathered through steps 2 and 3 and their own observations and experiences of the auditor. If the audit committee has been using Information Sheet 196 on an ongoing/annual basis they may elect to use and collate the results when considering the following. Whilst this appendix includes many of the questions from Information Sheet 196, Audit Committees may also have regard to the answers to other relevant questions in Information Sheet 196.

Audit quality considerations

Audit quality considerations are of primary importance because they reflect whether the audit can take place in an environment that promotes a quality audit.

1. Assess the **independence, objectivity and professional scepticism** of the auditor throughout the review period. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:
   a. How does the auditor demonstrate integrity, objectivity and professional scepticism?
   b. Has the auditor explained the basis for their independence declaration?
   c. How does the auditor inform the audit committee about matters that might reasonably be thought to bear on the firm's independence, including exceptions to its compliance with independence requirements and its safeguards in place to detect independence issues?
   d. Have audit team members avoided becoming too close to company management, which can affect independence and objectivity?
   e. In obtaining the audit committee's pre-approval for non-audit services, what safeguards were in place to protect the auditor's independence?
   f. How did the auditor adjust the audit plan to respond to changing risks and circumstances?
   g. How were significant differences in views, if any, between management and the auditor resolved?
   h. What evidence is there that the engagement team challenges significant judgements made by management in preparing the financial statements?
   i. How would you assess the quality of the significant professional judgements made by the engagement team during the audits?
   j. Which of the entity's accounting policies or disclosures, if any, have been questioned by regulators such that the auditor's independence, professional scepticism or judgement has been questioned?
   k. Are the audit fees appropriate in relation to costs incurred to enable the performance of a quality audit? Is audit quality likely to be compromised by reduced audit fees that might result in the audit being inadequately resourced or insufficient work being performed?[9]
2. Assess the quality of the engagement team provided by the auditor throughout the review period. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:
   a. What is your overall judgement of the quality of the insights provided to the audit committee by the auditor, including the quality of the reports presented to the audit committee by the auditor on the conduct and findings from the audit?
   b. How did the engagement partner and audit team ensure that the necessary knowledge and skills (entity-specific, industry, accounting, auditing) were dedicated to the audit?
   c. How would you assess the technical competence and ability of the auditor to translate knowledge into practice, for example by using technical knowledge and independent judgement to provide realistic analyses of issues and by providing appropriate levels of competence across the team?

9. As already noted it might be appropriate for the audit committee to benchmark fees at this stage.

d. How would you assess the auditor's understanding of the business, the industry and environment in which it operates, risk areas and key issues relevant to the financial report; for example, by demonstrating an understanding of the entity's specific business risks, processes, systems and operations?

e. How sufficient are resources assigned by the auditor to complete work in a timely manner, for example, by providing access to specialised expertise during the audit and assigning additional resources to the audit as necessary to complete work in a timely manner?

f. To what extent has the engagement team consulted and used specialists on complex technical matters (e.g. for complex asset and financial instrument valuations, or using specialists such as geologists or actuaries, or information technology system experts)?

g. Did the engagement partner take overall responsibility for, and was sufficiently and appropriately involved throughout the audit engagement?

h. If portions of the audit were performed by other teams in various domestic locations, or abroad by the firm's global network or other audit firms, how satisfied were you with how the engagement partner and the audit firm maintained quality control over that work?

i. How does the audit firm provide appropriate continuity of team members and perform an orderly transition when key members of the engagement team change?

3. Assess the **communication and interaction** with the auditor throughout the review period. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:

a. How candid and complete was the dialogue between the engagement partner, the audit committee and the audit committee chair? How well did the engagement partner explain their view of accounting and auditing issues? How effective was the resolution of issues?

b. How would you assess the auditor's independent assessment on the quality of the entity's financial reporting, including the reasonableness of accounting estimates and judgements, appropriateness of the accounting policies and adequacy of the disclosures?

c. How are Key Audit Matters (KAMs) communicated to the audit committee?

d. During in camera sessions, what is your assessment of how the auditor discussed sensitive issues (for example, were concerns about management's reporting processes, internal control over financial reporting or the quality of the entity's financial management team discussed in a timely, candid and professional manner)?

e. How promptly did the audit engagement partner alert the audit committee if the engagement team did not receive sufficient cooperation?

f. How well did the auditor inform the audit committee of the potential impact on the audit due to current developments in accounting and auditing standards relevant to the entity's financial statements?

Quality of service considerations

Quality of service considerations focus primarily on how the external audit, in terms of being a professional service, was conducted. Although treated separately from audit quality considerations, quality of service considerations can also influence audit quality. For example, if the auditor's behaviour creates unnecessary friction with management, the behaviour may affect the open and constructive relationship between the auditor and management needed to enhance audit quality.

Assess the quality of service provided by the auditor throughout the review period. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:

1. During the audit, how well did the auditor meet the agreed upon performance criteria, such as the engagement letter and audit scope? How well did the auditor meet its commitments, for example, by meeting agreed-upon performance delivery dates and multiple reporting deadlines and by being available and accessible to management and the audit committee?
2. How would you assess the professionalism of the audit partner and the engagement team?
3. How responsive and communicative is the auditor, for example, in soliciting input relative to business risks or issues that might impact the audit plan?
4. How proactive is the auditor in identifying opportunities and risks, for example, by anticipating and providing insights and improving internal controls?
5. Do the audit fees fairly reflect the cost of the services provided given the size, complexity and risks of the entity and a cost effective quality audit?[10]
6. Has the auditor communicated the reasons for any changes to fees (for example, change in scope of work) to the audit committee?

SAFEGUARDS AGAINST INSTITUTIONAL INDEPENDENCE FAMILIARITY THREATS

As part of the comprehensive review, the auditor should identify any significant institutional **threats to independence** and describe the **safeguards** they have put in place to mitigate these threats.

Assess whether there are any significant institutional familiarity threats and, if so, the related safeguards. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:

1. What institutional familiarity threats has the audit firm identified? What steps have been taken to address them?
2. To what extent has the entity employed former audit firm staff in key financial reporting positions?
3. What corporate hospitality including gifts, has been provided to the audit firm/management by management/the audit firm that could bring the auditor's independence into question?
4. What reputational damage or regulatory action, if any, has the audit firm suffered that could bring into question its professionalism, independence, or financial stability?
5. To what extent does the policy for non-audit work by the auditor adequately assure the auditor does not: audit its own work, involve itself in management decisions, act in an advocacy role or create conflicts of interest? Has the policy been complied with?

10. Note the audit committee needs to consider whether audit fees are appropriate to ensure quality.

RESULTS OF ASIC INSPECTION FINDINGS AND THE ACCOUNTING PROFESSIONAL BODIES REVIEWS SINCE THE PREVIOUS REVIEW AND HOW THE AUDIT FIRM HAS RESPONDED

Assess the appropriateness of the auditor's response to suggestions for improvements in audit quality arising from ASIC inspection findings or the Accounting Professional Bodies. Some or all of the following questions may be relevant in the circumstances of the entity and the audit:

1. Have any overall public aggregate thematic findings from ASIC's inspections or surveillances that are common across many audits and firms been addressed by the auditor?
2. If ASIC (or other regulators) inspected the entity's audit and made findings during the review what was the cause of these findings? How did the external audit firm respond?
3. Were there any major or significant issues raised by foreign regulators that raised questions about the external audit firm, especially when work is performed in that jurisdiction?

We welcome feedback on this Guide and how it has been used by boards and audit committees.
Any comments can be shared via email.

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