

EXPOSURE DRAFT

ED 34/05
(December 2005)

**Proposed Auditing Standard:
Communication of Audit
Matters With Those Charged
With Governance
(Re-issuance of AUS 710)**

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



Australian Government

Auditing and Assurance Standards Board

Commenting on this Exposure Draft

Comments on this Exposure Draft should be forwarded so as to arrive by 31 January 2006. Comments should be addressed to:

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A copy of all non-confidential submissions will be placed on public record on the AUASB website: www.auasb.gov.au.

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PREFACE

Reasons for Issuing ED 34/05

The Auditing and Assurance Standards Board (AUASB) is proposing to re-issue Auditing Standard (AUS 710) *Communication of Audit Matters With Those Charged With Governance* due to the requirements of the legislative provisions explained below.

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (the CLERP 9 Act) established the AUASB as an independent statutory body under section 227A of the *Australian Securities and Investments Commission Act 2001*, as from 1 July 2004. 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 will be legislative instruments under the *Legislative Instruments Act 2003*.

Main Proposals

This Proposed Auditing Standard establishes mandatory requirements and provides explanatory guidance on communication of audit matters arising from the audit of the financial report between the auditor and those charged with governance of an entity.

Proposed Operative Date

It is intended that this proposed Auditing Standard will be operative for financial reporting periods commencing on or after 1 July 2006.

Main changes from existing AUS 710 (May 1999)

The main differences between this proposed Auditing Standard and the Auditing Standard issued by the former Auditing & Assurance Standards Board of the Australian Accounting Research Foundation that it supersedes, AUS 710 (May 1999), is that in this proposed Auditing Standard:

2. the word 'shall', in the **bold-type** paragraphs, is the terminology used to describe an auditor's mandatory requirements, whereas an auditor's degree of responsibility was previously described by the word 'should';
3. the explanatory paragraphs provide guidance and illustrative examples to assist the auditor in fulfilling the mandatory requirements, whereas previously some obligations were implied within certain explanatory paragraphs. Accordingly, such paragraphs have been redrafted to clarify that the matter forms part of the explanatory guidance;
4. the terminology and overall concepts have been aligned to the Audit Risk Standards. The issue and re-issue of the Audit Risk Standards in February 2004, comprising:
 - AUS 402 *Understanding the Entity and Its Environment and Assessing the Risks of Misstatement*;
 - AUS 406 *The Auditor's Procedures in Response to Assessed Risks*; and
 - AUS 502 *Audit Evidence*gave rise to necessary conforming amendments to certain existing AUSs, including AUS 710;
5. the definition of "governance", "audit matters of governance interest" and "those charged with governance" and the explanatory guidance on "relevant persons" replace the explanatory guidance on the different level of management and the definitions of "report to management" and "operational management" in the existing AUS 710;
6. the mandatory requirement and explanatory guidance paragraphs on "Audit Matters of Governance Interest to be Communicated" replace "Identification of Significant Matters" and "Reporting Significant Matters" in the existing AUS 710 with the following revised and/or additional requirements:

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- (a) The auditor shall consider audit matters of governance interest that arise from the audit of the financial report and communicate them with those charged with governance (paragraph 15).
 - (b) The auditor shall inform those charged with governance of those uncorrected misstatements aggregated by the auditor during the audit that were determined by management to be immaterial, both individually and in the aggregate, to the financial report taken as a whole (paragraph 17);
7. the following additional specific mandatory requirements are included:
- (a) The auditor shall determine the relevant persons who are charged with governance and with whom audit matters of governance interest are communicated (paragraph 9).
 - (b) When the audit is conducted under Part 2M.3 of the *Corporations Act 2001*, the auditor shall communicate directly with those charged with governance:
 - (i) a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms are independent in accordance with relevant ethical requirements and any additional external requirements that apply to the engagement; and
 - (ii) - 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 communication shall include advice of 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

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- related safeguards that have been applied to eliminate threats to independence or reduce them to an acceptable level (paragraph 20);
 - (iii) If a contravention of the *Corporations Act 2001* or relevant ethical requirements as they relate to auditor independence has occurred, the auditor shall, at the earliest practical date, directly communicate with those charged with governance regarding details of the contravention and whether remedial action, if any, has been taken or proposed (paragraph 23);
8. the following mandatory requirement and related explanatory guidance paragraphs on “Format and Presentation” in the existing AUS 710 has been removed in view of the same mandatory requirement included in the proposed AUS 208 *Audit Documentation*:
- The auditor should document the subject matter of oral reports to management regarding significant matters(paragraph .31);
9. the mandatory requirement and related explanatory guidance paragraphs on “Management Response” in the existing AUS 710 has been included as guidance (paragraph 25).

A Table of Proposed Changes is provided as an attachment to the Exposure Draft.

Request for Comments

Comments are invited on this Exposure Draft of the proposed re-issuance of Auditing Standard (AUS 710) *Communication of Audit Matters With Those Charged With Governance* by 31 January 2006. The AUASB would prefer that respondents express a clear overall 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 any matter. The AUASB regards both critical and supportive comments as essential to a balanced review of the proposed Auditing Standard.

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AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes Auditing Standard <<>> *Communication of Audit Matters With Those Charged With Governance* as set out in paragraphs 1 to 39, 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 the *Preamble to AUASB Standards*, which sets out the intentions of the AUASB on how the Auditing Standards are to be understood, interpreted and applied.

The mandatory requirements of this Auditing Standard are set out in **bold-type** paragraphs.

AUDITING STANDARD

Communication of Audit Matters With Those Charged With Governance

Application

- 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 Part 2M.3 of the *Corporations Act 2001*; and**
 - (b) **an audit of a financial report for any other purpose.**
- 2 This Auditing Standard also applies, as appropriate, to an audit of other financial information.

Operative Date

- 3 **This Auditing Standard is operative for financial reporting periods commencing on or after 1 July 2006.**

Introduction

- 4 The purpose of this Auditing Standard is to establish mandatory requirements and to provide explanatory guidance on communication of audit matters arising from the audit of the financial report between the auditor and those charged with governance of an entity. These communications relate to audit matters of governance interest as defined in this Auditing Standard. This Auditing Standard does not provide guidance on communications by the auditor to parties outside the entity, for example, external regulatory agencies.
- 5 **The auditor shall communicate audit matters of governance interest arising from the audit of the financial report with those charged with governance of an entity.**
- 6 For the purposes of this Auditing Standard, “governance” is the term used to describe the role of persons entrusted with the oversight,

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control and direction of an entity¹. “Those charged with governance” comprises those persons accountable for ensuring that the entity achieves its objectives, with regard to reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws, and reporting to interested parties. Those charged with governance include management only when it performs such functions.

- 7 “Management” comprises officers and others who also perform senior managerial functions. Management includes those charged with governance only in those instances when they perform such functions.
- 8 For the purpose of this Auditing Standard, “audit matters of governance interest” are those that arise from the audit of the financial report and, in the opinion of the auditor, are both important and relevant to those charged with governance in overseeing the financial reporting and disclosure process. Audit matters of governance interest include only those matters that have come to the attention of the auditor as a result of the performance of the audit. The auditor is not required, in an audit in accordance with Auditing Standards, to design audit procedures for the specific purpose of identifying matters of governance interest.

Relevant Persons

- 9 **The auditor shall determine the relevant persons who are charged with governance and with whom audit matters of governance interest are communicated.**
- 10 The structures of governance vary according to the size and nature of an entity and from country to country reflecting different cultural and legal contextual backgrounds. In Australia, the audit committee or a governing board is responsible for the oversight function, while

¹ Principles of corporate governance have generally been developed by various countries as a point of reference for the establishment of good corporate behaviour. Such principles generally focus on publicly listed companies; however, they may also serve to improve governance in other forms of entities. As board and governance structures and practices vary from country to country, there is no single model of good corporate governance. A common principle is that the entity has in place a governance structure which enables the board to exercise objective oversight over the business and management of the entity including financial reporting. Internationally, it may be appropriate to refer to the *Principles of Corporate Governance*, as issued from time to time, by the Organisation for Economic Co-operation and Development (OECD). In Australia, it may be appropriate to refer to the *Principles of Good Corporate Governance and Best Practice Recommendations*, as issued from time to time, by the Australian Stock Exchange Ltd.

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senior executives is responsible for the management function. In other countries the oversight and management function may be legally separated into different bodies, such as a supervisory (wholly or mainly non-executive) board and a management (executive) board.

- 11 This diversity makes it difficult to establish a universal identification of the persons who are charged with governance and with whom the auditor communicates audit matters of governance interest. The auditor uses professional judgement to determine those persons with whom audit matters of governance interest are communicated, taking into account the governance structure of the entity, the circumstances of the engagement and any relevant legislation. The auditor also ordinarily considers the legal responsibilities of those persons. For example, in entities with audit committees, the relevant persons may be members of the audit committee. However, in entities where a unitary board has established an audit committee, the auditor may decide to communicate with the audit committee, or with the whole board, depending on the importance of the audit matters of governance interest.
- 12 When the entity's governance structure is not well defined, or those charged with governance are not clearly identified by the circumstances of the engagement, or by legislation, the auditor ordinarily comes to an agreement with the entity about with whom audit matters of governance interest are to be communicated. Examples include some owner-managed entities, some not for profit organizations, and some government agencies.
- 13 To avoid misunderstandings, an audit engagement letter may explain that the auditor will communicate only those matters of governance interest that come to attention as a result of the performance of an audit and that the auditor is not required to design audit procedures for the specific purpose of identifying matters of governance interest. The engagement letter may also:
- describe the form in which any communications on audit matters of governance interest will be made;
 - identify the relevant persons with whom such communications will be made; and
 - identify any specific audit matters of governance interest which it has been agreed are to be communicated.
- 14 The effectiveness of communications is enhanced by developing a constructive working relationship between the auditor and those

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charged with governance. This relationship is developed while maintaining an attitude of professional independence and objectivity.

Audit Matters of Governance Interest to be Communicated

15 The auditor shall consider audit matters of governance interest that arise from the audit of the financial report and communicate them with those charged with governance.

16 Audit matters of governance interest ordinarily such matters include the following:²

- The general approach and overall scope of the audit, including any expected limitations thereon, or any additional requirements.
- The selection of, or changes in, significant accounting policies and practices that have, or could have, a material effect on the entity's financial report.
- The potential effect on the financial report of any material risks and exposures, such as pending litigation, that are required to be disclosed in the financial report.
- Audit adjustments, whether or not recorded by the entity that have, or could have, a material effect on the entity's financial report.
- Material uncertainties related to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern.
- Disagreements with management about matters that, individually or in aggregate, could be significant to the entity's financial report or the auditor's report. These communications include consideration of whether the matter has, or has not, been resolved and the significance of the matter.
- Expected modifications to the auditor's report.

² The list of matters below is not intended to be all-inclusive or exhaustive. In addition, other Auditing Standards identify specific situations where the auditor is required to communicate certain matters with those charged with governance.

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- Other matters warranting attention by those charged with governance, such as material weaknesses in internal control, questions regarding management integrity, and fraud involving management.
 - Any other matters agreed upon in the terms of the audit engagement.
- 17 **The auditor shall inform those charged with governance of those uncorrected misstatements aggregated by the auditor during the audit that were determined by management to be immaterial, both individually and in the aggregate, to the financial report taken as a whole.**
- 18 The uncorrected misstatement communicated to those charged with governance need not include the misstatement below a designated amount.
- 19 As part of the auditor’s communications, those charged with governance are informed that:
- (a) pursuant to paragraph 15 of this Auditing Standard, the auditor’s communications of matters is required to include only those audit matters of governance interest that have come to the attention of the auditor as a result of the performance of the audit; and
 - (b) an audit of a financial report is not designed to identify all matters that may be relevant to those charged with governance. Accordingly, the audit does not ordinarily identify all such matters.

Communicating Auditor Independence Requirements

- 20 **When the audit is conducted under Part 2M.3 of the *Corporations Act 2001*, the auditor shall communicate directly with those charged with governance:**
- (a) **a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms are independent in accordance with relevant ethical requirements and any additional external requirements that apply to the engagement; and**
 - (b) (i) **all relationships and other matters between the firm, network firms, and the entity that, in the**

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auditor's professional judgement, may reasonably be thought to bear on independence. This communication shall include advice of 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

- (ii) the related safeguards that have been applied to eliminate threats to independence or reduce them to an acceptable level.**

- 21 The relationships and other matters, and safeguards to be communicated, vary with the circumstances of the engagement, but generally address the relevant matters set out in *Corporations Act 2001* and the applicable code of professional conduct of a professional accounting body³, which provide guidance, including application to specific situations, on:
- (a) threats to independence, categorised as: self-interest threats, self-review threats, advocacy threats, familiarity threats, and intimidation threats; and
 - (b) safeguards created by the profession, legislation or regulation, safeguards within the entity, and safeguards within the firm's own systems and procedures.
- 22 The auditor ordinarily considers whether the communications set out in paragraph 20 of this Auditing Standard are also relevant in the case of other entities, particularly those that may be of significant public interest because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. Examples of such entities might include public sector entities, credit institutions, insurance companies, and superannuation funds.

³ In Australia, the codes of conduct of the professional accounting bodies, as issued from time to time, are:

- CPA Australia and The Institute of Chartered Accountants in Australia, *Joint Code of Professional Conduct*; and
- National Institute of Accountants, *Pronouncements of the Board of Directors – Code of Ethics*.

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Communications regarding independence may not be relevant, for example, where all of those charged with governance have been informed of relevant facts through their management activities. This is particularly likely to be the case where the entity is owner-managed, and the auditor's firm and network firms have little involvement with the entity beyond a financial report audit.

- 23 **If a contravention of the *Corporations Act 2001* or relevant ethical requirements as they relate to auditor independence has occurred, the auditor shall, at the earliest practical date, directly communicate with those charged with governance regarding details of the contravention and whether remedial action, if any, has been taken or is proposed.**
- 24 The applicable code of professional conduct of a professional accounting body includes guidance on safeguards that could be applied if there has been an inadvertent violation relating to a financial interest in an assurance client.

Timing of Communications

- 25 **The auditor shall communicate audit matters of governance interest on a timely basis.**
- 26 This enables those charged with governance to take appropriate action.
- 27 In order to achieve timely communications, the auditor ordinarily discusses with those charged with governance the basis and timing of such communications. In certain cases, because of the nature of the matter, the auditor may communicate that matter sooner than previously agreed.

Forms of Communication

- 28 The auditor's communications with those charged with governance may be made orally or in writing. Ordinarily, the auditor's decision whether to communicate orally or in writing is affected by factors such as the following:
- The size, operating structure, legal structure, and communications processes of the entity being audited.
 - The nature, sensitivity and significance of the audit matters of governance interest to be communicated.

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- The arrangements made with respect to periodic meetings or reporting of audit matters of governance interest.
 - The amount of on-going contact and dialogue the auditor has with those charged with governance.
- 29 When audit matters of governance interest are communicated orally, pursuant to AUS 208 *Audit Documentation*, the auditor is required to document in the audit working papers the matters communicated and any responses to those matters. This documentation may take the form of a copy of the minutes of the auditor's discussion with those charged with governance. In certain circumstances, depending on the nature, sensitivity, and significance of the matter, it may be advisable for the auditor to confirm in writing with those charged with governance any oral communications on audit matters of governance interest.
- 30 Audit matters of governance interest are ordinarily reported in writing to the governing body or audit committee. The auditor ordinarily considers:
- (a) attending a meeting of the governing body or audit committee, when all members are present, to discuss such matters as appropriate; and
 - (b) any guidelines established by the governing body for reporting issues to, for example, an audit committee, or individuals with particular responsibility for audit issues.
- 31 If the auditor is concerned that a written report intended for those charged with governance has not been, or may not be distributed to all members of that group, the auditor shall implement an approach whereby all members are appropriately informed of the contents of the report.**
- 32 For example, when reporting to a particular group such as the governing body or audit committee, the auditor ordinarily considers the composition, structure and operational style of that group.
- 33 Ordinarily, the auditor initially discusses audit matters of governance interest with management, except where those matters relate to questions of management competence or integrity. These initial discussions with management are important in order to clarify facts and issues, and to give management an opportunity to provide further information. If management agrees to communicate a matter of governance interest with those charged with governance, the auditor may not need to repeat the communications, provided that

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the auditor is satisfied that such communications have effectively and appropriately been made.

Other Matters

- 34 If the auditor considers that a modification of the auditor's report on the financial report is required, as described in AUS 702 Part B *Modifications to the Independent Auditor's Report*⁴, communications between the auditor and those charged with governance cannot be regarded as a substitute.
- 35 Pursuant to paragraph 15 of this Auditing Standard, the auditor is required to consider whether audit matters of governance interest previously communicated continue to be a matter of governance interest and whether to communicate the matter again with those charged with governance.

Confidentiality

- 36 The requirements of a professional accounting body⁵, legislation or regulation may impose obligations of confidentiality that restrict the auditor's communications of audit matters of governance interest. Pursuant to AUS 206 *Quality Control of Audits of a Financial Report*, the auditor is required to refer to such requirements, laws and regulations before communicating with those charged with governance. In some circumstances, the potential conflicts with the auditor's ethical and legal obligations of confidentiality and reporting may be complex. In these cases, the auditor may wish to consult with legal counsel.

Laws and Regulations

- 37 The requirements of a professional accountancy body, legislation or regulation may impose obligations on the auditor to make communications on governance related matters. For example section 311 of the *Corporations Act 2001* imposes a duty on the auditor to inform the Australian Securities and Investments Commission if certain circumstances arise during the audit. These additional communications requirements are not covered by this

⁴ The proposed Auditing Standard, AUS 702 is being reissued as two separate standards: Part A – *The Independent Auditor's Report on a General Purpose Financial Report* and Part B – *Modifications to the Independent Auditor's Report*.

⁵ A professional accounting body as defined in AUS 206 includes: The Institute of Chartered Accountants in Australia; CPA Australia; and National Institute of Accountants.

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Auditing Standard, however, they may affect the content, form and timing of communications with those charged with governance.

Public Sector Considerations

38 In the public sector, obligations imposed on the auditor to communicate on governance related matters that are broader than the types of matters discussed in this Auditing Standard, such as:

- (a) compliance with legislative or regulatory requirements and related authorities;
- (b) adequacy of internal control; and
- (c) economy, efficiency and effectiveness of programs, projects and activities.

In addition, the auditor's written communications may be placed on public record and distributed to a wider audience than solely those persons charged with governance of the entity being audited.

Conformity with International Standards on Auditing

39 Except as noted below, this Auditing Standard conforms with International Standard on Auditing ISA 260 *Communication of Audit Matters With Those Charged With Governance* issued by the International Auditing and Assurance Standards Board of the International Federation of Accountants. The main differences between this Auditing Standard and ISA 260 are:

- This Auditing Standard includes the following specific mandatory requirements and related explanatory guidance paragraphs that are not in ISA 260:
 - ◆ When the audit is conducted under Part 2M.3 of the *Corporations Act 2001*, the auditor shall communicate directly with those charged with governance:
 - a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms are independent in accordance with relevant ethical requirements and any additional external requirements that apply to the engagement; and

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- (i) 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
- (ii) the related safeguards that have been applied to eliminate threats to independence or reduce them to an acceptable level (paragraph 20).
- ◆ If a contravention of the *Corporations Act 2001* or relevant ethical requirements as they relate to auditor independence has occurred, the auditor shall, at the earliest practical date, directly communicate with those charged with governance the contravention and of remedial action taken or proposed, if any (paragraph 23).
- ◆ If the auditor is concerned that a written report intended for those charged with governance has not been, or may not be distributed to all members of that group, the auditor should implement an approach whereby all members are appropriately informed of the contents of the report (paragraph 31).
- This Auditing Standard contains references to the audit reporting requirements of the *Corporations Act 2001*, whereas ISA 260 does not.

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Compliance with this Auditing Standard enables compliance with ISA 260.

Table of Proposed Changes from AUS 710 *Communication of Audit Matters with Those Charged With Governance*

Base Standard

ISA 260 *Communication Of Audit Matters With Those Charged With Governance*, is used as the base standard for the purpose of re-drafting this proposed Auditing Standard.

Main differences between the Base Standard and the existing AUS 710

The main differences between ISA 260 and the existing AUS 710 are:

1. the terminology and overall concepts have been aligned to the Audit Risk Standards. The issue and re-issue of the Audit Risk Standards in February 2004, comprising:
 - AUS 402 *Understanding the Entity and Its Environment and Assessing the Risks of Misstatement*;
 - AUS 406 *The Auditor's Procedures in Response to Assessed Risks*; and
 - AUS 502 *Audit Evidence*gave rise to necessary conforming amendments to certain existing AUSs, including AUS 710.
2. the mandatory requirement and explanatory guidance paragraphs on "Identification of Significant Matters" and "Reporting Significant Matters" in the existing AUS 710 has been replaced with "Audit Matters of Governance Interest to be Communicated" with the following revised and/or additional requirements:
 - The auditor shall consider audit matters of governance interest that arise from the audit of the financial report and communicate them with those charged with governance (paragraph 15).
 - The auditor shall inform those charged with governance of those uncorrected misstatements aggregated by the auditor during the audit that were determined by management to be immaterial, both individually and in the aggregate, to the financial report taken as a whole (paragraph 17);
3. the following additional specific mandatory requirements are included:
 - The auditor shall determine the relevant persons who are charged with governance and with whom audit matters of governance interest are communicated (paragraph 9);
 - When the audit is conducted under Part 2M.3 of the *Corporations Act 2001*, the auditor shall communicate directly with those charged with governance:
 - a. a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms are independent in accordance with relevant ethical requirements and any additional external requirements that apply to the engagement; and
 - b. (i) 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

(ii) the related safeguards that have been applied to eliminate threats to independence or reduce them to an acceptable level (paragraph 20).

c. If a contravention of the *Corporations Act 2001* or relevant ethical requirements as they relate to auditor independence has occurred, the auditor shall, at the earliest practical date, directly communicate with those charged with governance the contravention and of remedial action taken or proposed, if any (paragraph 23).

4. the following mandatory requirement and related explanatory guidance paragraphs on “Format and Presentation” in the existing AUS 710 has been removed in view of the same mandatory requirement included in the proposed AUS 208 *Audit Documentation*:

- The auditor should document the subject matter of oral reports to management regarding significant matters(paragraph .31).

5. the mandatory requirement and related explanatory guidance paragraphs on “Management Response” in the existing AUS 710 has been included as guidance (paragraph 25):

Summary of proposed changes from the Base Standard

The table below details the proposed changes from the base standard, ISA 260 (excluding changes to reflect Australian terminology and references to Australian Auditing Standards).

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
1, 2	Requirement / Guidance	New Application paragraphs.
3	Requirement	Reposition Operative date paragraph.
5, 8, 14, 16, 19	Requirement	Replace “should” with “shall.
10, 11, 21, 22	Guidance	Insert “ordinarily,” to remove implied obligations.
18(a), 23, 27	Guidance	Insert: “pursuant to..... the auditor is required to”.
6	Guidance	Amend as follows: ““Those charged with governance” ordinarily are comprises those persons’.

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
10	Guidance	Amend as follows: “The structures of governance <u>vary according to the size and nature of an entity and from country to country reflecting different cultural and legal contextual backgrounds.</u> For example in some countries In Australia, the <u>audit committee or a governing board is responsible for the supervision oversight function,</u> and the <u>while senior management is responsible for the management function.</u> In other countries the oversight and management function may be <u>are</u> legally separated into different bodies, such as a supervisory (wholly or mainly non-executive) board and a management (executive) board. In other countries, both functions are the legal responsibility of a single, unitary board, although there may be an audit committee that assists that board in its governance responsibilities with respect to financial reporting.
11	Guidance	Insert “professional” in front of “judgement” and reword the fourth sentence as follows: For example, in entities with supervisory boards or with audit committees, the relevant persons may be those bodies of the audit committee.
4, 11	Guidance	Remove reference to “supervisory board”.
35	Guidance	Reword: “The auditor considers whether audit matters of governance interest previously communicated may have an effect on the current year’s financial report Pursuant to paragraph 15 of this Auditing Standard the auditor is required to consider whether audit matters of governance interest previously communicated continue to be a matter of governance interest and whether to communicate the matter again with those charged with governance.
37	Guidance	Insert: “for example the auditor’s duty to inform the Australian Securities and Investment Commission in accordance with section 311 of the <i>Corporations Act 2001</i> ”.
6, 10	Guidance	Replace “supervision” with “oversight”.

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
7	Guidance	<p>Insert the following revised definition of management: “Management” comprises officers and others who also perform senior managerial functions. Management includes those charged with governance only in those instances when they perform such functions’.</p>
	Footnote	<p>Reword and insert as follow at footnote 1: <u>“As Board structures and practices vary from country to country there is no single model of good corporate governance. Board structures and practices vary from country to country. A common principle is that the entity should have in place a governance structure which enables the board to exercise objective judgement on corporate affairs, including financial reporting, independent in particular from management. Internationally, it may be appropriate to refer to the <i>Principles of Corporate Governance</i>, as issued from time to time, by the Organisation for Economic Co-operation and Development (OECD). In Australia, it may be appropriate to refer to the <i>Principles of Good Corporate Governance and Best Practice Recommendations</i> are issued from time to time, by the Australian Stock Exchange Ltd”.</u></p>
20	Requirement / Guidance	<p>Insert: “Communicating Auditor Independence Requirements”. When the audit is conducted under Part 2M.3 of the <i>Corporations Act 2001</i>, the auditor shall communicate directly with those charged with governance:</p> <ol style="list-style-type: none"> 1 a statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms are independent in accordance with relevant ethical requirements and any additional external requirements that apply to the engagement; and <ol style="list-style-type: none"> (i) 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 communication shall include advice of 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 (ii) the related safeguards that have been applied to eliminate threats to independence or reduce them to an acceptable level”.

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
21	Guidance	Insert: “The relationships and other matters, and safeguards to be communicated, vary with the circumstances of the engagement, but generally address the relevant matters set out in <i>Corporations Act 2001</i> and the applicable code of professional conduct of a professional accounting body, which provide guidance, including application to specific situations, on: (a) Threats to independence, categorised as: self-interest threats, self-review threats, advocacy threats, familiarity threats, and intimidation threats; and (b) Safeguards created by the profession, legislation or regulation, safeguards within the entity, and safeguards within the firm’s own systems and procedures”.
	Footnote	Insert footnote to paragraph 21: “In Australia, the codes of conduct of the professional accounting bodies, as issued from time to time, are: <ul style="list-style-type: none"> • CPA Australia and The Institute of Chartered Accountants in Australia, <i>Joint Code of Professional Conduct</i>; and • National Institute of Accountants, <i>Pronouncements of the Board of Directors – Code of Ethics</i>”.
22	Guidance	Insert: “The auditor ordinarily considers whether the communications set out in paragraph 20 are also relevant in the case of other entities, particularly those that may be of significant public interest because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. Examples of such entities might include public sector entities, credit institutions, insurance companies, and pension funds. Communications regarding independence may not be relevant, for example, where all of those charged with governance have been informed of relevant facts through their management activities. This is particularly likely to be the case where the entity is owner-managed, and the auditor’s firm and network firms have little involvement with the entity beyond a financial report audit”.

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
23	Requirement	Insert: “If a contravention of the <i>Corporations Act 2001</i> or relevant ethical requirements as they relate to auditor independence has occurred, the auditor shall, at the earliest practical date, directly communicate with those charged with governance regarding the details of the contravention and whether remedial action, if any, has been taken or is proposed”.
24	Guidance	Insert: “The applicable code of professional conduct of a professional accounting body includes guidance on safeguards that could be applied if there has been an inadvertent violation relating to a financial interest in an assurance client”.
30	Guidance	Insert paragraph .18 from the existing AUS 710 modified as follows: “ <u>Audit Significant matters of governance interest</u> are ordinarily reported in writing to the governing body or audit committee. The auditor ordinarily considers: (a) attending a meeting of the governing body or audit committee, when all members are present, to discuss such matters as appropriate; and (b) any guidelines established by the governing body for reporting issues to, for example, an audit committee, or individuals with particular responsibility for audit issues”.
31	Requirement	Insert revised mandatory component of paragraph .19 from existing AUS 710: “If the auditor is concerned that a written report intended for a particular group within the management structure of an entity those charged with governance has not been, or may not be distributed to all members of that group, the auditor shall implement an approach whereby all members are appropriately informed of the contents of the report.”
32	Guidance	Insert guidance component of paragraph .19 from existing AUS 710: “For example, when reporting to a particular group such as the governing body or audit committee, the auditor ordinarily considers the composition, structure and operational style of that group.”

Paragraph No. in Proposed Exposure Draft	Status (Requirement, Guidance, Footnote or Appendix)	Description of Proposed Change(s)
38	Guidance	<p>Insert guidance to recognise “Public Sector Considerations: In the public sector, obligations imposed on the auditor to communication on governance related matters may be broader than the types of matters discussed in this Auditing Standard, and extend to:</p> <ul style="list-style-type: none"> (a) Compliance with legislative or regulatory requirements and related authorities; (b) Adequacy of internal control; and (c) Economy, efficiency and effectiveness of programs, projects and activities. <p>In addition, the auditor’s written communications may be placed on public record and distributed to a wider audience than solely those persons charged with governance of the entity being audited”.</p>