

**GS XXX**  
(August 2009)

# **Guidance Statement GS XXX**

## ***Auditing Mortgage Investment Schemes***

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

### **DISCLAIMER**

This document contains draft proposals to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions and/or proposals to be contained in a published Exposure Draft or Auditing Standard. No responsibility is taken by the AUASB for the results of reliance, actions or omissions to act on the basis of any information contained in this document (including appendices), or for any errors or omissions in it.



**Australian Government**

**Auditing and Assurance Standards Board**

## **Obtaining a Copy of this Guidance Statement**

This Guidance Statement is available on the AUASB website:  
[www.auasb.gov.au](http://www.auasb.gov.au).

### **AUASB contact details:**

Auditing and Assurance Standards Board    Phone: (03) 8080 7400  
Level 7    Fax: (03) 8080 7450  
600 Bourke Street    E-mail: [enquiries@auasb.gov.au](mailto:enquiries@auasb.gov.au)  
Melbourne Victoria 3000  
AUSTRALIA

**Postal Address:**  
PO Box 204  
Collins Street West  
Melbourne Victoria 8007  
AUSTRALIA

### **COPYRIGHT**

© 2009 Auditing and Assurance Standards Board (AUASB). The text, graphics and layout of this Guidance Statement are protected by Australian copyright law and the comparable law of other countries. Reproduction within Australia in unaltered form (retaining this notice) is permitted for personal and non-commercial use subject to the inclusion of an acknowledgment of the source. Requests and enquiries concerning reproduction and rights for commercial purposes within Australia should be addressed to the Executive Director, Auditing and Assurance Standards Board, PO Box 204, Collins Street West, Melbourne Victoria 8007. Otherwise, no part of the Guidance Statement may be reproduced, stored or transmitted in any form or by any means without the prior written permission of the AUASB except as permitted by law.

ISSN 1833-7600

---

## CONTENTS

### AUTHORITY STATEMENT

Obtaining a Copy of this Guidance Statement  
AUASB contact details:

COPYRIGHT

CONTENTS

AUTHORITY STATEMENT

GUIDANCE STATEMENT gs XXX

Auditing Mortgage Investment Schemes

Application

Operative Date

Introduction

<type here>

Regulatory Background

ASIC Regulatory Guide 144

Responsibilities of Management and Auditors

Management's Responsibilities

Auditors' Responsibilities

Agreeing on the Terms of the Audit Engagements

Issues for Auditors to Consider

Conformity with International Pronouncements

*Paragraphs*

Application.....	1
Operative Date .....	2
Introduction.....	3
Definitions .....	
Conformity with International Pronouncements .....	

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) issues Guidance Statement GS XXX *Auditing Mortgage Investment Schemes* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

This Guidance Statement provides guidance to assist the auditor to fulfil the objectives of the audit or assurance engagement. It includes explanatory material on specific matters for the purposes of understanding and complying with AUASB Standards. The auditor exercises professional judgement when using this Guidance Statement.

The Guidance Statement does not prescribe or create new mandatory Requirements.

Dated 1 August 2009

M H Kelsall  
Chairman - AUASB

# GUIDANCE STATEMENT GS XXX

## AUDITING MORTGAGE INVESTMENT SCHEMES

### Note to Users

This Guidance Statement is the reissuance of AGS 1058 *Auditing Mortgage Investment Schemes* and has not been fully revised for any additional considerations which the auditor may need to address as a result of changes made to the Corporations Act 2001 or new ASIC regulatory guides (RGs) and any other regulation issued since June 2002. Regulation issued since July 2002, which the auditor may need to consider in conducting the audit of mortgage investment schemes, includes RG 45 *Mortgage schemes—improving disclosure for retail investors* (September 2008), RG 118 *Commentary on compliance plans: Contributory mortgage schemes* (April 2004) and RG 119 *Commentary on compliance plans: Pooled mortgage schemes* (April 2004). Whilst legislative and regulatory changes have been considered in the reissuance of this guidance statement, comprehensive consideration of these changes will be conducted as part of the future revision of this Guidance Statement. Auditors of mortgage investment schemes should satisfy themselves that the implications of these matters is adequately addressed in their audits.

### Application

- 1 This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors ~~on~~ <type here> of mortgage investment schemes which are regulated by the Australian Securities & Investments Commission (ASIC) and are subject to Chapter 5C of the *Corporations Act 2001* (the “Act”).

### Operative Date

- 2 This Guidance Statement is operative on 1 August 2009 and replaces AGS 1058 *Auditing Mortgage Investment Schemes* which was issued in July 2002.

## Introduction

~~13~~ ~~.01~~ This Auditing Guidance Statement (AGS) has been prepared by the Auditing & Assurance Standards Board (AuASB) to provide general guidance to auditors of mortgage investment schemes which are regulated by the Australian Securities & Investments Commission (ASIC) and are subject to Chapter 5C of the *Corporations Act 2001* (Cth) (the “Act”). The guidance in this ~~A~~ Guidance Statement should be read in conjunction with that contained in ~~AGS 1052-XXX~~ “*Special Considerations in the Audit of Compliance Plans of Managed Investment Schemes*” for audits of mortgage investment schemes compliance plans undertaken pursuant to section 601HG of the Act.

~~4~~ ~~.02~~ Auditors of mortgage investment schemes are required to adhere to the ~~basic principles and essential procedures~~ mandatory requirements contained in Auditing Standards (AUSs) ~~ASAs~~ when undertaking financial report audits and the requirements contained in Standards on Assurance Engagements (SAEs) when undertaking audits of compliance plans. This ~~A~~ Guidance Statement has been developed to clarify auditors’ responsibilities in respect of such engagements, and to provide guidance to the auditors on additional considerations which may be taken into account when undertaking financial report and compliance plan audits of mortgage investment schemes.

~~5~~ ~~.03~~ It is important to note that this ~~AGS~~ Guidance Statement does not impose any responsibilities on the auditor beyond those which are imposed by ~~AUSs~~ ASAs, SAEs and the requirements of the Act. The provisions of the Act in this area are supported by ASIC ~~Policy Statement~~ regulatory guide 144 “Mortgage Investment Schemes” (RG 144) and other ASIC ~~regulatory guide~~ policy statements, including those applicable to managed investment schemes, as well as modifications to the Act made by individual orders or class orders issued by ASIC.

## Definitions

~~3~~ For the purposes of this Guidance Statement  
~~<type here>~~ [CHG1]

## Regulatory Background

ASIC ~~Policy Statement~~ Regulatory Guide 144

## Guidance Statement GS XXX Auditing Mortgage Investment Schemes

~~04~~ In the past, ASIC provided class order exemptions for mortgage schemes operated by solicitors and finance brokers in most States and Territories. These exemptions meant that mortgage investment scheme operators did not have to comply with the provisions of the Act dealing with prospectuses, sharehawking, approved deeds and securities licensing.

~~05~~ After a detailed review of the mortgage investment industry by ASIC, it was decided to change the manner in which mortgage investment schemes are regulated, and in July 1999, ASIC issued Interim Policy Statement PS 144 "Mortgage Investment Schemes". PS 144 was subsequently revised and re-issued as a final ASIC Policy Statement in March 2000.

~~6~~ [CHG2]~~06~~ ASIC's regulatory framework for mortgage investment schemes principally consists of:

- (a) a requirement for operators of mortgage schemes that meet the criteria for registration as a managed investment scheme to comply with Chapter 5C of the Act;
- (b) application of ~~PS-RG~~ 144, as well as other relevant ASIC policy statements applicable to managed investment schemes generally; and
- (c) the provision of relief by ASIC ~~in RG 144~~ specific to mortgage scheme operators in certain cases. Operators of small, low risk schemes e.g. solicitors' mortgage practices, may be permitted to comply with an approved industry body's rules (for example, those of the relevant State and Territory professional law bodies) rather than all of Chapter 5C, if the body can demonstrate effective supervision over such participants.<sup>1</sup>

~~(d)7~~ ~~07~~ Under ~~PS-RG~~ 144 a mortgage investment scheme would, *prima facie*, be regarded as being a managed investment scheme if:

- (a) the legal or commercial character of the investment is determined by the nature of the business operations of the

<sup>1</sup> For schemes of this kind with no more than 20 investors and no more than \$7.5 million in total loan capital, ASIC is prepared to allow such operators to participate in an industry based compliance structure approved by ASIC. However, ASIC has indicated that it will impose various conditions on such schemes, including the requirement for the application prospectus disclosure and the securities hawking provisions of the law.

## Guidance Statement GS XXX *Auditing Mortgage Investment Schemes*

---

promoter e.g. where money contributed by different investors is lent under one mortgage; and

- (b) commercial decisions are taken by the operator or the promoter of the scheme and not by investors.

~~(e)8~~ ~~.08~~ ~~PS-RG~~ 144 recognises that section 601ED must also be satisfied to enable a mortgage investment scheme to be registered as a managed investment scheme under Chapter 5C. The basic requirements of this section are that:

- (a) the scheme must have more than 20 members (investors); or
- (b) the scheme was promoted by a person, or an associate of a person, who was, when the scheme was promoted, in the business of promoting managed investment schemes; or
- (c) ASIC has determined that a number of schemes are closely related and that each of them has to be registered as their total number of members is greater than 20.<sup>2</sup>

---

<sup>2</sup> Auditors of smaller schemes not directly regulated by ASIC but administered as part of an industry based compliance structure may also be required to report on various compliance matters as part of the auditing arrangements which are agreed to with the individual State or Territory industry supervisory bodies.

## Responsibilities of Management and Auditors

### Management's Responsibilities

~~9~~ ~~.09~~ — Section 285 of the Act imposes a responsibility on registered schemes, which by virtue of ~~PS-RG~~ 144 includes mortgage investment schemes, to comply with the requirements of Chapter 2M of the Act dealing with financial reports and audit requirements. Furthermore, section 285(3) deems a scheme's responsible entity responsible for the performance of the financial reporting obligations in that Chapter in respect of the scheme.

~~10~~ ~~.10~~ — In addition to the above obligations, the responsible entity of a scheme is required to comply with Part 5C.4 of the Act and ASIC ~~Policy Statement~~ *Regulatory Guide* 132 "*Managed investments: Compliance plans*".<sup>2</sup> These requirements impose obligations on the responsible entity to ensure that compliance plans are in place which set out adequate measures that the responsible entity is to apply in operating the scheme to ensure compliance with the Act and the scheme's constitution.

~~11~~ ~~.11~~ — As with managed investment schemes generally, the responsible entity of a mortgage investment scheme which is registered under section 601ED, will be completely liable to the members of the scheme for all aspects of the operation of the scheme.<sup>3</sup> [CHG3] To this end, the responsible entity and the directors of that entity, are responsible to the members of the scheme for the operation of the scheme, for meeting its statutory and other legal obligations, and for having in place and maintaining an adequate system of internal control to protect the interests of members who have invested in the scheme.

~~12~~ ~~.12~~ — A scheme's internal control structure is to provide its management, viz. the responsible entity, with reasonable, but not absolute assurance, that the operations of the scheme are orderly and efficient, and that irregularities are prevented as far as possible and detected should they occur. An adequate internal control system will also provide management with reasonable assurance that assets are safeguarded from unauthorised use or disposal, and that the financial and other records of the scheme reflect the entire operational activities of the scheme and permit the timely preparation of financial reports required by the Act.

---

<sup>3</sup> See *Explanatory Memorandum, Managed Investments Bill 1997*, p 8.

## Auditors' Responsibilities

13 ~~13~~ — The auditor of a scheme's financial report ordinarily obtains a preliminary understanding of the ~~scheme's scheme and its environment, including its~~ internal control ~~structure, sufficient to identify and assess the risks of material misstatement of the financial report whether due to fraud or error, and sufficient to design and perform further audit procedures, which may include~~ ~~assesses the level of control risk, and~~ where appropriate, tests the ~~operating~~ effectiveness of ~~internal~~ controls and other compliance measures in the context of the scope of the audit of the scheme's financial report audit, in order to be able to form an opinion on it as required by Chapter 2M.<sup>4</sup>

14 ~~14~~ — Similarly, the compliance plan auditor<sup>5</sup> who conducts the audit of a scheme's compliance plan under section 601HG, ~~is required under ASAE 3000 Assurance Engagements other than Audits or Reviews of Historical Financial Information also needs to obtain an understanding of the scheme's compliance plan (the subject matter) and other engagement circumstances assess internal controls within the scope of such an engagement sufficient to identify and assess the risks of either the scheme's non compliance with the compliance plan or the compliance plan's non compliance with the requirements of the Act, and be mindful of the compliance related requirements imposed on such schemes by PS-RG 144 and the other relevant ASIC policy statements regulatory guides, including those regulatory guides policy statements applicable to managed investment schemes generally. This is so, notwithstanding that the compliance plan audit and the financial report audit are separate engagements.~~<sup>6</sup>

## Agreeing on the Terms of the Audit Engagements

15 ~~15~~ — Under section ~~331AB331AAA~~, the scheme's responsible entity is responsible for the appointment of the scheme's financial report auditor. This is also the case for the scheme's compliance plan auditor who is appointed by the responsible entity under section

<sup>4</sup> See ~~AUS-ASA 402 "Risk Assessments and Internal Controls"~~ ~~315 Understanding the Entity and its Environment and Assessing the Risk of Material Misstatements.~~

<sup>5</sup> Under section 601HG(2) the compliance plan auditor and the financial report auditor of the responsible entity must be different persons, notwithstanding that they may be from the same firm. See also ~~AGS 4052XXX "Special Considerations in the Audit of Managed Investment Schemes"~~ para. ~~18XX~~.

<sup>6</sup> Under section 601HG(2) the compliance plan auditor and the financial report auditor of the responsible entity must be different persons, notwithstanding that they may be from the same firm. See also ~~AGS 4052 "Special Considerations in the Audit of Managed Investment Schemes"~~ para. ~~18~~.

601HG. It is therefore essential that the auditors and the scheme's responsible entity separately agree on the terms of the respective audit engagements, which are to be recorded in writing. Such terms are normally outlined in separate audit engagement letters<sup>7</sup> which are forwarded to the responsible entity.<sup>8</sup>

~~16~~ ~~16~~ — The auditors may use the engagement letters to clarify the respective roles of the responsible entity's directors, the financial report auditor and the compliance plan auditor, by contrasting the respective statutory responsibilities of the responsible entity and the auditors under the Act. Both the financial report auditor and compliance plan auditor obtain acknowledgment of management's responsibilities from the directors of the scheme's responsible entity when obtaining agreement on the terms of the audit engagements.

## Issues for Auditors to Consider

~~17~~ ~~17~~ — In addition to the issues normally considered when undertaking financial report audits and compliance plan audits, auditors of mortgage investment schemes will need to consider several matters that are particularly important to the operation of such schemes. These matters include whether<sup>[CHG4]</sup>:

- (a) appropriate documentation is available in respect of all deposits or receipts to the scheme and its bank accounts, and in relation to payments and withdrawals from the scheme and its bank accounts;
- (b) appropriate documentation is available in respect of all loans made by the scheme e.g. detailed loan agreements, securities held, guarantees, terms of repayments, external independent valuations; and
- (c) the mortgage investment scheme meets the solvency requirements prescribed by ASIC and that its basis of reporting is consistent with it continuing to operate as a going concern over the relevant period, including, if applicable, whether the scheme meets the benchmarks specified by ASIC in RG 45 Mortgage schemes – improving disclosure for retail investors.

<sup>7</sup> Or other suitable form of audit contract. See ASA 210 *Terms of Audit Engagements* and [ASAE 3000](#).

<sup>8</sup> Or other suitable form of audit contract. See AUS 204 *“Terms of Audit Engagements”*.

## Guidance Statement GS XXX Auditing Mortgage Investment Schemes

---

18 ~~18~~ The auditors of the mortgage investment schemes may also take into account other specific compliance related considerations relevant to such schemes. These considerations include whether:

- (a) investor funds have been placed in the mortgage investment scheme on the basis of the written approval of the investor;
- (b) specific disbursements of investor funds are supported by written authorities from investors;
- (c) investor funds are capable of being remitted back to the investor within the time period specified by the investor and that the net monies loaned (after agents commission/loan establishment fees) are sufficient;
- (d) investors funds have been appropriately secured e.g. first mortgages or other charges or liens are taken out over the assets and undertakings of the investee or borrower;
- (e) commissions or loan establishment fees paid to agents are in accordance with legally binding agreements between the parties;
- (f) interest and principal payments from the investee or borrower are being received in accordance with loan agreements;
- (g) interest paid to the investors is financed from receipt of investee or borrowers funds and not from the commissions or other monies due to solicitors or agents;
- (h) periodic statements are provided to investors in respect of the disbursement of their funds until the funds are fully utilised in the mortgage investment scheme; and
- (i) that monthly bank reconciliations have been prepared in respect of each “trust” account.

19 ~~19~~ It is important that auditors take the above considerations into account when planning and undertaking both financial report audits and compliance plan audits of mortgage investment schemes. While not purporting to be an exhaustive list of compliance matters to be considered by auditors, they represent areas in which there should be appropriate controls in place, so as to adequately mitigate

the risk of a material misstatement in a scheme's financial report and/or material non-compliance with a scheme's compliance plan.

### **Operative Date**

~~.20—This AGS, which incorporates amendments made by AUS/AGS Omnibus 3 “Miscellaneous Amendments to AUs and AGSs”, is operative from July 2002. This version of AGS 1058 supersedes AGS 1058 “Auditing Mortgage Investment Schemes”, as issued in August 2001.~~

**4**

**Conformity with International Pronouncements**

320 There is no equivalent International Auditing Practice Statement (IAPS) to this Guidance Statement.

Draft