Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**3.0**
Meeting Date:	10 March 2020
Subject:	ASA 315 *Identifying and Assessing Risks of Material Misstatement*
Date Prepared:	18 February 2020
Prepared By:	Anne Waters – AUASB Senior Project Manager

☒ **Action Required** ☐ **For Information Purposes Only**

Agenda Item Objectives

1. For the AUASB to consider and approve ASA 2020-1 *Amendments to Australian Auditing Standards* ASA 2020-1) which includes the consequential and conforming amendments to ASA 315 *Identifying and Assessing the Risks of Material Misstatement*.

2. Provide feedback and input into the draft ASA 315 Basis for Conclusions.

3. To provide an update on the communications and implementation support plan.

Background

4. At its February 2020 meeting the AUASB approved for issue ASA 315.

5. The IAASB issued Conforming and Consequential Amendments to Other International Standards at the time of issuing ISA 315. Based on this the ATG commenced drafting the Conforming Amendments to other ASAs through Auditing Standard 2020-1 *Amendments to Australian Auditing Standards I* (ASA 2020-1).

6. As communicated to the AUASB at the February meeting when conducting a quality review of ASA 2020-1 we identified some amendments which were not included in the IAASB's document. NZAuASB Staff also notified us that they had also noted some missing amendments. The matters we identified were minor and editorial ie. mainly related to references to the name of ISA 315 (which has now changed), and footnote cross references. However this resulted in a delay in the AUASB Technical Group (ATG) finalising the amending standard.

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7. At its February 2020 meeting the AUASB also requested that the ASA 315 Basis for Conclusions include detail on how feedback received from Australian stakeholders have been addressed, and not simply a cross reference to the IAASB's Basis for Conclusion.

Matters for the AUASB to consider:

Part A - ASA 2020-1

8. In preparing ASA 2020-1 the ATG followed the following process:

   (a) Used the IAASB's Conforming and Consequential Amendments to Other International Standards issued at the time of issuing ISA 315 as the basis;

   (b) Checked the wording of the amendments to the compiled ASAs (note the IAASB have not processed the ISA 540 conforming amendments and therefore there are differences in some of the wording in ISAs to the ASAs);

   (c) Checked all paragraphs and footnote references to the ASAs (note these can be different as the IAASB do not renumber inserted paragraphs and footnotes, and the matter described in b above); and

   (d) Performed a search of the ASAs to ensure all references to ASA 315 have been captured.

9. 26 ASAs have been amended as the result of conforming with ASA 315. Many of the amendments were minor such as cross reference changes required, minor terminology changes ie. relevant controls, systems of controls, to controls. The standards with the most amendments are ASA 200, ASA 240, ASA 330, and ASA 540. The changes to these standards consist of;

   (a) The threshold for the identification of risk of material misstatement (ASA 200);

   (b) Alignment with new requirement for the identification of inherent and control risk at the assertion level, and clarifying that control risk is high unless the auditor plans to test the operating effectiveness of controls;

   (c) New application material on tests of controls including automated controls (ASA 330);

   (d) Clarifying that not all assertions within a material class of transaction, account balance or disclosure are required to be tested under ASA 330 paragraph 18 (ie. standard back provision requiring substantive testing for material class of transaction, account balance and disclosure);

   (e) Additional content or changes due to new concepts / terminology now included in ASA 315, such as inherent risk factors, spectrum of inherent risk, relevant assertion, less complex entities, considerations specific to automated tools and techniques.

"Compelling Reasons" Assessment

10. The AUASB approved ASA 315 with no compelling reason amendments.

11. NZAuASB approved ASA 315 with one compelling reason amendment in relation to representations being required by those charged with governance and not management, which the AUASB agreed was not a compelling reason amendment in Australia. The NZAuASB approved the conforming amendments with no compelling reason amendments.

12. As detailed in the AUASB's Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board (IAASB) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB):

(a) In implementing the FRC's strategic direction, the AUASB has determined the following objectives:

(i) To adopt international auditing and assurance standards in Australia unless there are strong reasons not to (which the AUASB describes as "compelling reasons"); and

(ii) To work with the New Zealand Auditing and Assurance Standards Board (NZAuASB) towards the establishment of harmonised standards based on international standards.

(b) The AUASB may consider modifying international standards for application in Australia under either of those objectives. The AUASB considers such modifications acceptable provided that they consider the public interest , and do not conflict with, or result in lesser requirements than, the international standards.

(c) The international standards should be adopted and should be modified only if there are compelling reasons to do so. In the case of an international standard that is being reviewed for the purpose of adoption in Australia, the compelling reasons test for modifications in the public interest is triggered where the international standard does not reflect, or is not consistent with:

(i) The Australian regulatory arrangements; or

(ii) Principles and practices that are considered appropriate in Australia (including in the use of significant terminology).

13. The ATG have reviewed the amendments in ASA 2020-1 and have not identified any compelling reason amendments.

Action for the AUASB
Do you consider there are any compelling reason adjustments?
Review ASA 2020-1 (Refer 3.1_ASA 315 Amending Standard)
Do you approve for issue ASA 2020-1?

Basis for Conclusions

14. The Basis for Conclusions is a document issued for transparency about the due process followed when developing the standard, and in particular to explain how the standard has changed since it was publicly exposed, and how stakeholders' feedback has been addressed.

15. The ATG have been considering the format and content of the ASA 315 Basis of Conclusions and the impact of the change in the timing of the issuing of the exposure draft in Australia. As a result, the ASA 315 Basis for Conclusions includes more detail than previous AUASB Basis for Conclusions on IAASB standards, to include analysis of the very detailed feedback we received on the exposure draft from Australian stakeholders. However, the ASA 315 Basis for Conclusions still cross references to the IAASB's Basis for Conclusions where relevant, as this includes very detailed analysis of the matters considered by the IAASB when finalising the ISA and are consistent with the feedback from Australian stakeholders.

16. The Basis for Conclusions also includes the AUASB's voting on approval of the standards and re-exposure.

Action for the AUASB
Do you have any feedback on the ASA 315 Basis for Conclusions (refer 3.2_ASA 315 Basis for Conclusion)?   Specifically: Do you think the level of detail is appropriate in Appendix 1?   Do you agree with including the voting for the re-exposure as it is included?

Next steps

17. After ASA 2020-1 is approved, the ATG will prepare the impacted compiled standards to be approved for release by the Chair and Technical Director.

Communications / Implementation support plan

18. The ATG will develop a communications / implementation support plan with two stages:

    (a) Initial release of ASA 315; and

    (b) Implementation support plan

19. The initial release of ASA 315 will be communicated via email to AUASB subscribers, AUASB newsletter, professional bodies, social media (Linked In and Twitter). This communication will include the IAASB's Fact Sheet which was issued with ISA 315 which provides an overview of the significant changes and a flowchart to assist with understanding.

20. As previously discussed implementation support will be important to address complexity of the new standard. The ATG will develop an implementation support plan which will consist of:

    (a) The guidance and support materials developed by the IAASB's (refer 3.3 ISA 315 Implementation Plan);

    (b) Additional guidance and support materials developed by the ATG (if considered necessary);

    (c) Work with the professional bodies and present at appropriate educational forums.

21. When determining if further implementation guidance or support materials are required the ATG will take into account the feedback from AUASB members on areas where guidance is required, and meet with the IAASB to gather more detail on the guidance they are issuing and whether that addresses the matters raised by the AUASB. The ATG will continue to consider what implementation support is required over the next few months and will update the AUASB in due course.

Action for the AUASB
Provide feedback on the communications and implementation support plan.

Part B – NZAuASB

22. The NZAuASB have approved ISA 315 for issue with one compelling reason as discussed above, and have approved the conforming amendments with no compelling reason amendments. The ATG will work with NZAuASB to co-ordinate the implementation support.

Material Presented

Agenda Item	3.0 ASA 315 Board Meeting Summary Paper
	3.1 ASA 315 ASA 315 Amending Standard
	3.2 ASA 315 Basis for Conclusion
	3.3 ISA 315 Implementation Plan

ASA 2020-1
(March 2020)

Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards*

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

Obtaining a Copy of this Auditing Standard

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

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PREFACE

Reasons for Issuing ASA 2020-1

The AUASB issues Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is a non corporate Commonwealth entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislation Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, inter alia, to develop auditing standards that have a clear public interest focus and are of the highest quality.

Main Features

This Auditing Standard makes amendments to the requirements and/or application and other explanatory material and/or appendices of the following Auditing Standards:

ASA 200	*Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards* (Issued October 2009 and amended to December 2018)
ASA 210	*Agreeing the Terms of Audit Engagements* (Issued October 2009 and amended to May 2017)
ASA 230	*Audit Documentation* (Issued October 2009 and amended to December 2018)
ASA 240	*The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (Issued October 2009 and amended to December 2018)
ASA 250	*Consideration of Laws and Regulations in an Audit of a Financial Report* (Issued May 2017)
ASA 260	*Communication With Those Charged with Governance* (Issued December 2015 and amended to December 2018)
ASA 265	*Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* (Issued October 2009 and amended to November 2013)
ASA 300	*Planning an Audit of a Financial Report* (Issued October 2009 and amended to December 2015)
ASA 320	*Materiality in Planning and Performing an Audit* (Issued October 2009 and amended to December 2015)
ASA 330	*The Auditor's Responses to Assessed Risks* (Issued October 2009 and amended to December 2015)
ASA 402	*Auditing Considerations Relating to an Entity Using a Service Organisation* (Issued October 2009 and amended to November 2013)
ASA 500	*Audit Evidence* (Issued October 2009 and amended to December 2018)

ASA 501	*Audit Evidence—Specific Considerations for Inventory and Segment Information* (Issued October 2009 and amended to July 2011)
ASA 505	*External Confirmations* (Issued October 2009 and amended to December 2018)
ASA 520	*Analytical Procedures* (Issued October 2009 and amended to December 2018)
ASA 530	*Audit Sampling* (Issued October 2009)
ASA 540	*Auditing Accounting Estimates and Related Disclosures* (Issued December 2018)
ASA 550	*Related Parties* (Issued October 2009 and amended to November 2013)
ASA 570	*Going Concern* (Issued December 2015)
ASA 600	*Special Considerations-Audits of a Group Financial Report* (Issued October 2009 and amended to December 2015)
ASA 610	*Using the Work of Internal Auditors* (Issued November 2013)
ASA 620	*Using the Work of an Auditor's Expert* (Issued October 2009)
ASA 700	*Forming an Opinion and Reporting on a Financial Report* (Issued December 2015 and amended to December 2018)
ASA 701	*Communicating Key Audit Matters in the Independent Auditor's Report* (Issued December 2015 and amended to December 2018)
ASA 720	*The Auditor's Responsibilities Relating to Other Information* (Issued December 2015)
ASA 800	*Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (Issued July 2016 and amended to May 2017)

The amendments arise from changes made by the International Auditing and Assurance Standards Board (IAASB) to ISA 315 (Revised) *Identifying and Assessing the Risks of Material Misstatement*. Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the IAASB for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards.

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 2020-1 *Amendments to Australian Auditing Standards* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

Dated: <TypeHere>

R Simnett AO
Chair - AUASB

Conformity with International Standards on Auditing

This Auditing Standard has been made for Australian legislative purposes and accordingly there is no equivalent International Standard on Auditing (ISA) issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

AUDITING STANDARD ASA 2020-1

Amendments to Australian Auditing Standards

Application

1. This Auditing Standard applies to:

   - an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and

   - an audit of a financial report, or a complete set of financial statements, for any other purpose.

2. This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

Operative Date

3. This Auditing Standard is operative for financial reporting periods commencing on or after 15 December 2021, with early adoption, in conjunction with ASA 315 *Identifying and Assessing the Risks of Material Misstatement* permitted.

Introduction

Scope of this Auditing Standard

4. This Auditing Standard makes amendments to Australian Auditing Standards. The amendments arise from consequential and conforming changes arising from the issuance of ASA 315 *Identifying and Assessing the Risks of Material Misstatement*.

Objective

5. The objective of this Auditing Standard is to make amendments to the following Auditing Standards:

   (a) ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*
   (Issued October 2009 and amended to December 2018)

   (b) ASA 210 *Agreeing the Terms of Audit Engagements*
   (Issued October 2009 and amended to May 2017)

   (c) ASA 230 *Audit Documentation*
   (Issued October 2009 and amended to December 2018)

   (d) ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (Issued October 2009 and amended to December 2018)

   (e) ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*
   (Issued May 2017)

   (f) ASA 260 *Communication With Those Charged with Governance*
   (Issued December 2015 and amended to December 2018)

   (g) ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*
   (Issued October 2009 and amended to November 2013)

(h) ASA 300 *Planning an Audit of a Financial Report* (Issued October 2009 and amended to December 2015)

(i) ASA 320 *Materiality in Planning and Performing an Audit* (Issued October 2009 and amended to December 2015)

(j) ASA 330 *The Auditor's Responses to Assessed Risks* (Issued October 2009 and amended to December 2015)

(k) ASA 402 *Auditing Considerations Relating to an Entity Using a Service Organisation* (Issued October 2009 and amended to November 2013)

(l) ASA 500 *Audit Evidence* (Issued October 2009 and amended to December 2018)

(m) ASA 501 *Audit Evidence—Specific Considerations for Inventory and Segment Information* (Issued October 2009 and amended to July 2011)

(n) ASA 505 *External Confirmations* (Issued October 2009 and amended to December 2018)

(o) ASA 520 *Analytical Procedures* (Issued October 2009 and amended to December 2018)

(p) ASA 530 *Audit Sampling* (Issued October 2009)

(q) ASA 540 *Auditing Accounting Estimates and Related Disclosures* (Issued December 2018)

(r) ASA 550 *Related Parties* (Issued October 2009 and amended to November 2013)

(s) ASA 570 *Going Concern* (Issued December 2015)

(t) ASA 600 *Special Considerations-Audits of a Group Financial Report* (Issued October 2009 and amended to December 2015)

(u) ASA 610 *Using the Work of Internal Auditors* (Issued November 2013)

(v) ASA 620 *Using the Work of an Auditor's Expert* (Issued October 2009)

(w) ASA 700 *Forming an Opinion and Reporting on a Financial Report* (Issued December 2015 and amended to December 2018)

(x) ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report* (Issued December 2015 and amended to December 2018)

(y) ASA 720 *The Auditor's Responsibilities Relating to Other Information* (Issued December 2015)

(z) ASA 800 *Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (Issued July 2016 and amended to May 2017)

Definition

6. For the purposes of this Auditing Standard, the meanings of terms are set out in each Auditing Standard and in the *AUASB Glossary*.

Amendments to Auditing Standards

7. This Standard uses underlining, striking out and other typographical material to identify some of the amendments to a Standard, in order to make the amendments more understandable. However, the amendments made by this Standard do not include that underlining, striking out or other typographical material. Amended paragraphs are shown with deleted text struck through and new text underlined. Ellipses (…) are used to help provide the context within which amendments are made and also to indicate text that is not amended.

8. Throughout the Australian Auditing Standards all references to the title of ASA 315 have been amended to ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*. In addition to the Auditing Standards listed in paragraph 5, the following Auditing Standards follow the same amendment to the title of ASA 315.

   (a) ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information* (Issued October 2009 and amended to May 2017)

   (b) ASA 510 *Initial Audit Engagements—Opening Balances* (Issued October 2009 and amended to December 2015)

   (c) ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity* (Issued October 2009 and amended to July 2013)

Amendments to ASA 200

9. Existing paragraph 7 is amended to read follows:

   The ASAs contain objectives, requirements and application and other explanatory material that are designed to support the auditor in obtaining reasonable assurance. The ASAs require that the auditor exercise professional judgement and maintain professional scepticism throughout the planning and performance of the audit and, among other things:

   - Identify and assess risks of material misstatement, whether due to fraud or error, based on an understanding of the entity and its environment, the applicable financial reporting framework and ~~including~~ the entity's system of internal control.

   …

10. Existing paragraph 13 is amended to read as follows:

   For purposes of the ASAs, the following terms have the meanings attributed below:

   …

   (n) Risk of material misstatement – The risk that the financial report is materially misstated prior to audit. This consists of two components, described as follows at the assertion level: (Ref: Para. A3)

      (i) Inherent risk – The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

      (ii) Control risk – The risk that a misstatement that could occur in an assertion about a class of transactions, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's ~~internal~~ controls.

…

11. Following existing paragraph A2, and before the heading *An audit of a financial report* the following sub-heading is inserted:

Risk of Material Misstatement (Ref: Para. 13(n))

12. Following the sub-heading inserted above, the following paragraph A3 is inserted:

For the purposes of the ASAs, a risk of material misstatement exists when there is a reasonable possibility of:

(a) A misstatement occurring (i.e., its likelihood); and

(b) Being material if it were to occur (i.e., its magnitude).

13. As a result of the insertion of the paragraph above, subsequent paragraphs of this Auditing Standard are re-numbered and references to these paragraphs are updated accordingly.

14. Existing footnote 17 in paragraph A30 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~9~~16.

15. Existing paragraph A40 is amended to read as follows:

Inherent risk is influenced by inherent risk factors. ~~higher for some assertions and related classes of transactions, account balances, and disclosures than for others.~~ Depending on the degree to which the inherent risk factors affect the susceptibility to misstatement of an assertion, the level of inherent risk varies on a scale that is referred to as the spectrum of inherent risk. The auditor determines significant classes of transactions, account balances and disclosures, and their relevant assertions, as part of the process of identifying and assessing the risks of material misstatement. For example, ~~it may be higher for complex calculations or for~~ account~~s~~ balances consisting of amounts derived from accounting estimates that are subject to significant estimation uncertainty may be identified as significant account balances, and the auditor's assessment of inherent risk for the related risks at the assertion level may be higher because of the high estimation uncertainty.

16. The following paragraph A42 is inserted following the paragraph above:

External circumstances giving rise to business risks may also influence inherent risk. For example, technological developments might make a particular product obsolete, thereby causing inventory to be more susceptible to overstatement. Factors in the entity and its environment that relate to several or all of the classes of transactions, account balances, or disclosures may also influence the inherent risk related to a specific assertion. Such factors may include, for example, a lack of sufficient working capital to continue operations or a declining industry characterised by a large number of business failures.

17. As a result of the insertion of the paragraph above, subsequent paragraphs of this Auditing Standard are re-numbered and references to these paragraphs are updated accordingly.

18. Existing paragraph A41 is amended to read as follows:

Control risk is a function of the effectiveness of the design, implementation and maintenance of ~~internal~~ controls by management to address identified risks that threaten the achievement of the entity's objectives relevant to preparation of the entity's financial report. However, internal control, no matter how well designed and operated, can only reduce, but not eliminate, risks of material misstatement in the financial report, because of the inherent limitations of ~~internal~~ controls. These include, for example, the possibility of human errors or mistakes, or of controls being circumvented by collusion or inappropriate management override. Accordingly, some control risk will always exist. The ASAs provide the conditions under which the auditor is required to, or may choose to, test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures to be performed.[18]

19. Existing paragraph A42 is amended to read as follows:

The assessment of the risks of material misstatement may be expressed in quantitative terms, such as in percentages, or in non-quantitative terms. In any case, the need for the auditor to make appropriate risk assessments is more important than the different approaches by which they may be made. The Australian Auditing Standards typically refer to ~~do not ordinarily refer to inherent risk and control risk separately, but rather to a combined assessment of~~ the "risks of material misstatement~~.~~" rather than to inherent risk and control risk separately. However, ASA ~~540~~315[19] requires ~~a separate assessment of~~ inherent risk to be assessed separately from ~~and~~ control risk to provide a basis for designing and performing further audit procedures to respond to the assessed risks of material misstatement at the assertion level~~, including significant risks, for accounting estimates at the assertion level~~ in accordance with ASA 330.[20] ~~In identifying and assessing risks of material misstatement for significant classes of transactions, account balances or disclosures other than accounting estimates, the auditor may make separate or combined assessments of inherent and control risk depending on preferred audit techniques or methodologies and practical considerations.~~

20. The following paragraph A46 is inserted following existing paragraph A43 of this Auditing Standard:

Risks of material misstatement are assessed at the assertion level in order to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence.[21]

21. As a result of the insertion of the paragraph above, subsequent paragraphs and footnotes of this Auditing Standard are re-numbered and references to these paragraphs and footnotes are updated accordingly.

22. Existing footnote 23 in paragraph A52 is amended to read as follows:

See ASA 315, paragraphs ~~5-10~~13-18.

23. Existing paragraph A61 is amended to read as follows:

Where necessary, the application and other explanatory material provides further explanation of the requirements of an ASA and guidance for carrying them out. In particular, it may:

- Explain more precisely what a requirement means or is intended to cover, including in some ASAs such as ASA 315, why a procedure is required.
- Include examples of procedures that may be appropriate in the circumstances. In some ASAs, such as ASA 315, examples are presented in boxes.

…

24. The heading "*Considerations Specific to Smaller Entities*" above existing A66 has been amended to "*Scalability Considerations*" and the following paragraph A69 is inserted following the heading "*Scalability Considerations*".

[19] See ASA ~~540~~315 ~~*Auditing Accounting Estimates and Disclosures*, paragraph 16~~ *Identifying and Assessing the Risks of Material Misstatement*

[21] See ASA 330, paragraph 6

Scalability considerations have been included in some ASAs (e.g., ASA 315), illustrating the application of the requirements to all entities regardless of whether their nature and circumstances are less complex or more complex. Less complex entities are entities for which the characteristics in paragraph A66 may apply.

25. Existing paragraph A67 is now moved to paragraph A70 and is amended to read as follows:

The "considerations specific to smaller entities" included in some ~~the~~ ASAs have been developed primarily with unlisted entities in mind. Some of the considerations, however, may be helpful in audits of smaller listed entities.

26. As a result of the changes above, subsequent paragraphs of this Auditing Standard are re-numbered and references to these paragraphs are updated accordingly.

27. Existing paragraph A66 is amended to read as follows:

For purposes of specifying additional considerations to audits of smaller entities, a "smaller entity" refers to an entity which typically possesses qualitative characteristics such as:

…

(b) One or more of the following:

…

(iv) Simpler systems of ~~Few~~ internal controls;

…

28. The sub-heading *Considerations Specific to Automated Tools and Techniques* is inserted following existing paragraph Aus A68.1 of this Auditing Standard. The following paragraph A72 is then inserted following this sub-heading.

The considerations specific to "automated tools and techniques" included in some ASAs (for example, ASA 315) have been developed to explain how the auditor may apply certain requirements when using automated tools and techniques in performing audit procedures.

Amendments to ASA 210

29. Existing footnote 14 in paragraph A16 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, Appendix 3 paragraph 22~~paragraph A54~~.

30. Existing paragraph A18 is amended to read as follows:

It is for management to determine what internal control is necessary to enable the preparation of the financial report. The term "internal control" encompasses a wide range of activities within components of the system of internal control that may be described as the control environment; the entity's risk assessment process; the entity's process to monitor the system of internal control, the information system~~, including the related business processes relevant to financial reporting,~~ and communication; and control activities~~; and monitoring of controls~~. This division, however, does not necessarily reflect how a particular entity may design, implement and maintain its internal control, or how it may classify any particular component.[15] An entity's internal control (in particular, its accounting books and records, or

[15] See ASA 315, paragraph A91~~59~~ and Appendix 3~~1~~

accounting systems) will reflect the needs of management, the complexity of the business, the nature of the risks to which the entity is subject, and relevant laws or regulation.

Amendments to ASA 230

31. Existing footnote 5 in paragraph A7 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph 17~~10~~.

32. Existing footnote 6 in paragraph A8 is amended to read as follows:

See ASA 315, paragraph ~~4(e)~~12(l).

33. Existing paragraph A17 is amended to read as follows:

When preparing audit documentation, the auditor of a smaller entity may also find it helpful and efficient to record various aspects of the audit together in a single document, with cross-references to supporting working papers as appropriate. Examples of matters that may be documented together in the audit of a smaller entity include the understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control, the overall audit strategy and audit plan, materiality determined in accordance with ASA 320,[9] assessed risks, significant matters noted during the audit, and conclusions reached.

34. Existing Appendix 1 is amended to read as follows:

Specific Audit Documentation Requirements in Other Australian Auditing Standards

This appendix identifies paragraphs in other Australian Auditing Standards that contain specific documentation requirements. The list is not a substitute for considering the requirements and related application and other explanatory material in Australian Auditing Standards.

…

- ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~* – paragraph 38~~2~~

Amendments to ASA 240

35. Existing paragraph 7 is amended to read as follows:

Furthermore, the risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud, because management is frequently in a position to directly or indirectly manipulate accounting records, present fraudulent financial information or override controls ~~procedures~~ designed to prevent similar frauds by other employees.

36. Existing footnote 6 in paragraph 16 is amended to read as follows:

See ASA 315, paragraph 17–18 ~~10~~

37. Existing paragraph 17 is amended to read as follows:

When performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, the applicable financial reporting framework and ~~including~~ the entity's system of internal control, required by ASA 315~~,~~[7] the auditor shall perform the procedures in paragraphs 23~~17~~–43~~24~~ to obtain information for use in identifying the risks of material misstatement due to fraud.

38. Existing paragraph 21 is amended to read as follows:

Unless all of those charged with governance are involved in managing the entity,[8] the auditor shall obtain an understanding of how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the ~~internal~~ controls that management has established to mitigate these risks. (Ref: Para. A20-A22)

39. Existing footnote 9 in paragraph 26 is amended to read as follows:

See ASA 315, paragraph 28~~25~~

40. Existing paragraph 28 is amended to read as follows:

The auditor shall treat those assessed risks of material misstatement due to fraud as significant risks and accordingly, to the extent not already done so, the auditor shall ~~obtain an understanding of the entity's related~~ identify the entity's controls~~, including control activities, relevant to~~ that address such risks, and evaluate their design and determine whether they have been implemented).[10] (Ref: Para. A32-A33)

41. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

42. Existing paragraph 45 is amended to read as follows:

The auditor shall include the following in the audit documentation[12] ~~of the auditor's understanding of the entity and its environment and~~ of the identification and the assessment of the risks of material misstatement required by ASA 315:[13]

(a) The significant decisions reached during the discussion among the engagement team regarding the susceptibility of the entity's financial report to material misstatement due to fraud; ~~and~~

(b) The identified and assessed risks of material misstatement due to fraud at the financial statement level and at the assertion level;~~.~~ and

(c) Identified controls in the control activities component that address assessed risks of material misstatement due to fraud.

43. Existing paragraph A8 is amended to read as follows:

Maintaining professional scepticism requires an ongoing questioning of whether the information and audit evidence obtained suggests that a material misstatement due to fraud may exist. It includes considering the reliability of the information to be used as audit evidence and ~~the~~ identified controls in the control activities component, if any, over its preparation and maintenance.~~, where relevant.~~ Due to the characteristics of fraud, the auditor's professional scepticism is particularly important when considering the risks of material misstatement due to fraud.

44. Existing footnote 17 of paragraph A19 is amended to read as follows:

[10] See ASA 315, paragraph 26(a)(i) and 26(d)
[13] See ASA 315, paragraph 38~~32~~

See ASA 315, paragraphs 14(a) and 24(a)(ii)~~6 and 23~~, and ISA 610, *Using the Work of Internal Auditors*

45. Existing paragraph A20 is amended to read as follows:

Those charged with governance of an entity oversee the entity's systems for monitoring risk, financial control and compliance with the law. In many countries, corporate governance practices are well developed and those charged with governance play an active role in oversight of the entity's assessment of the risks of fraud and ~~of the relevant internal control~~ the controls that address such risks. Since the responsibilities of those charged with governance and management may vary by entity and by country, it is important that the auditor understands their respective responsibilities to enable the auditor to obtain an understanding of the oversight exercised by the appropriate individuals.[18]

46. Existing paragraph A21 is amended to read as follows:

An understanding of the oversight exercised by those charged with governance may provide insights regarding the susceptibility of the entity to management fraud, the adequacy of ~~internal~~ controls that address ~~over~~ risks of fraud, and the competency and integrity of management. The auditor may obtain this understanding in a number of ways, such as by attending meetings where such discussions take place, reading the minutes from such meetings or making enquiries of those charged with governance.

47. Existing paragraph A23 is amended to read as follows:

In addition to information obtained from applying analytical procedures, other information obtained about the entity and its environment, the applicable financial reporting framework and the entity's system of internal control may be helpful in identifying the risks of material misstatement due to fraud. The discussion among team members may provide information that is helpful in identifying such risks. In addition, information obtained from the auditor's client acceptance and retention processes, and experience gained on other engagements performed for the entity, for example, engagements to review interim financial information, may be relevant in the identification of the risks of material misstatement due to fraud.

48. Existing paragraph A26 is amended to read as follows:

Examples of fraud risk factors related to fraudulent financial reporting and misappropriation of assets are presented in Appendix 1. These illustrative risk factors are classified based on the three conditions that are generally present when fraud exists:

- An incentive or pressure to commit fraud;
- A perceived opportunity to commit fraud; and
- An ability to rationalise the fraudulent action.

Fraud risk factors may relate to incentives, pressures or opportunities that arise from conditions that create susceptibility to misstatement, before consideration of controls. Fraud risk factors, which include intentional management bias, are, insofar as they affect inherent risk, inherent risk factors.[20] Fraud risk factors may also relate to conditions within the entity's system of internal control that provide opportunity to commit fraud or that may affect management's attitude or ability to rationalise fraudulent actions. Fraud r~~R~~isk factors reflective of an attitude that permits rationalisation of the fraudulent action may not be susceptible to observation by the auditor. Nevertheless, the auditor may become aware of the existence of such information through, for example, the required understanding of the entity's

[18] See ASA 260, paragraphs A1–A8, discuss with whom the auditor communicates when the entity's governance structure is not well defined.
[20] See ASA 315, paragraph 12(f)

control environment.[21] Although the fraud risk factors described in Appendix 1 cover a broad range of situations that may be faced by auditors, they are only examples and other risk factors may exist.

49. Existing footnote 19 in paragraph A32 is amended to read as follows:

See ASA 315, paragraph ~~A48~~A75.

50. Existing paragraph A33 is amended to read as follows:

It is therefore important for the auditor to obtain an understanding of the controls that management has designed, implemented and maintained to prevent and detect fraud. ~~In doing so,~~ In identifying the controls that address the risks of material misstatement due to fraud, the auditor may learn, for example, that management has consciously chosen to accept the risks associated with a lack of segregation of duties. Information from ~~obtaining this understanding~~ identifying these controls, and evaluating their design and determining whether they have been implemented, may also be useful in identifying fraud risks factors that may affect the auditor's assessment of the risks that the financial report may contain material misstatement due to fraud.

51. The following footnote 23, is inserted to paragraph A43 of this Auditing Standard, following the wording "*Further, the auditor's consideration of the risks of material misstatement associated with inappropriate override of controls over journal entries*".

See ASA 315, paragraph 26(a)(ii)

52. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

53. Existing paragraph A44 is amended to read as follows:

When identifying and selecting journal entries and other adjustments for testing and determining the appropriate method of examining the underlying support for the items selected, the following matters are of relevance:

- *The identification and assessment of the risks of material misstatement due to fraud* – the presence of fraud risk factors and other information obtained during the auditor's identification and assessment of the risks of material misstatement due to fraud may assist the auditor to identify specific classes of journal entries and other adjustments for testing.

…

- *The entity's financial reporting process and the nature of evidence that can be obtained* – for many entities routine processing of transactions involves a combination of manual and automated ~~steps and procedures~~ controls. Similarly, the processing of journal entries and other adjustments may involve both manual and automated ~~procedures and~~ controls. Where information technology is used in the financial reporting process, journal entries and other adjustments may exist only in electronic form.

…

- *Journal entries or other adjustments processed outside the normal course of business* – non standard journal entries may not be subject to the same ~~level of internal~~ nature

[21] See ASA 315, paragraph 21

and extent of controls as those journal entries used on a recurring basis to record transactions such as monthly sales, purchases and cash disbursements.

54. Existing Appendix 1 is amended to read as follows:

EXAMPLES OF FRAUD RISK FACTORS

The fraud risk factors identified in this Appendix are examples of such factors that may be faced by auditors in a broad range of situations. Separately presented are examples relating to the two types of fraud relevant to the auditor's consideration – that is, fraudulent financial reporting and misappropriation of assets. For each of these types of fraud, the risk factors are further classified based on the three conditions generally present when material misstatements due to fraud occur: (a) incentives/pressures, (b) opportunities, and (c) attitudes/rationalisations. Although the risk factors cover a broad range of situations, they are only examples and, accordingly, the auditor may identify additional or different risk factors. Not all of these examples are relevant in all circumstances, and some may be of greater or lesser significance in entities of different size or with different ownership characteristics or circumstances. Also, the order of the examples of risk factors provided is not intended to reflect their relative importance or frequency of occurrence.

Fraud risk factors may relate to incentives or pressures, or opportunities, that arise from conditions that create susceptibility to misstatement before consideration of controls (i.e., the inherent risk). Such factors are inherent risk factors, insofar as they affect inherent risk, and may be due to management bias. Fraud risk factors related to opportunities may also arise from other identified inherent risk factors (for example, complexity or uncertainty may create opportunities that result in susceptibility to misstatement due to fraud). Fraud risk factors related to opportunities may also relate to conditions within the entity's system of internal control, such as limitations or deficiencies in the entity's internal control that create such opportunities. Fraud risk factors related to attitudes or rationalisations may arise, in particular, from limitations or deficiencies in the entity's control environment.

Risk Factors Relating to Misstatements Arising from Fraudulent Financial Reporting

…

Incentives/Pressures

…

Opportunities

The nature of the industry or the entity's operations provides opportunities to engage in fraudulent financial reporting that can arise from the following:

…

The monitoring of management is not effective as a result of the following:

…

There is a complex or unstable organisational structure, as evidenced by the following:

…

~~Internal control components are deficient~~ Deficiencies in internal control as a result of the following:

- Inadequate ~~monitoring of controls~~ process to monitor the entity's system of internal control, including automated controls and controls over interim financial reporting (where external reporting is required).
- High turnover rates or employment of staff in accounting, information technology, or the internal audit function that are not effective.
- Accounting and information systems that are not effective, including situations involving significant deficiencies in internal control.

…

Attitudes/Rationalisations

…

Risk Factors Relating to Misstatements Arising From Misappropriation of Assets

…

Incentives/Pressures

…

Opportunities

Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation. For example, opportunities to misappropriate assets increase when there are the following:

…

Inadequate ~~internal~~ controls over assets may increase the susceptibility of misappropriation of those assets. For example, misappropriation of assets may occur because there is the following:

…

Attitudes/Rationalisations

…

- Disregard for ~~internal~~ controls over misappropriation of assets by overriding existing controls or by failing to take appropriate remedial action on known deficiencies in internal control.

…

55. Existing Appendix 2 is amended to read as follows:

EXAMPLES OF POSSIBLE AUDIT PROCEDURES TO ADDRESS THE ASSESSED RISKS OF MATERIAL MISSTATEMENT DUE TO FRAUD

…

Consideration at the Assertion Level

…

The following are specific examples of responses:

- Visiting locations or performing certain tests on a surprise or unannounced basis. For example, observing inventory at locations where auditor attendance has not been previously announced or counting cash at a particular date on a surprise basis.
- …
- If the work of an expert becomes particularly significant with respect to a financial statement item for which the assessed risk of material misstatement due to fraud is high, performing additional procedures relating to some or all of the expert's assumptions, methods or findings to determine that the findings are not unreasonable, or engaging another expert for that purpose.

…

Amendments to ASA 250

56. Existing footnote 4 in paragraph 13 is amended to read as follows:

See ASA 315, *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~11~~19.

57. Existing paragraph A23 is amended to read as follows:

As required by paragraph 22, the auditor evaluates the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations. The implications of particular identified or suspected non-compliance will depend on the relationship of the perpetration and concealment, if any, of the act to specific controls ~~activities~~ and the level of management or individuals working for, or under the direction of, the entity involved, especially implications arising from the involvement of the highest authority within the entity. As noted in paragraph 9, the auditor's compliance with law, regulation or relevant ethical requirements may provide further information that is relevant to the auditor's responsibilities in accordance with paragraph 22.

Amendments to ASA 260

58. Existing paragraph A12 is amended to read as follows:

Communicating significant risks identified by the auditor helps those charged with governance understand those matters and why they were determined to be significant risks ~~require special audit consideration~~. The communication about significant risks may assist those charged with governance in fulfilling their responsibility to oversee the financial reporting process.

59. Existing paragraph A13 is amended to read as follows:

Matters communicated may include:

…

- The auditor's approach to the entity's system of internal control. ~~relevant to the audit.~~

…

60. Existing footnote 27 in paragraph A52 is amended to read as follows:

See ASA 315, paragraph ~~A78~~ Appendix 3.

Amendments to ASA 265

61. Existing paragraph 1 is amended to read as follows:

This Australian Standard on Auditing (ASA) deals with the auditor's responsibility to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified in an audit of financial report. This ASA does not impose additional responsibilities on the auditor regarding obtaining an understanding of the entity's system of internal control and designing and performing tests of controls over and above the requirements of ASA 315[1] and ASA 330.[2] ASA 260[3] establishes further requirements and provides guidance regarding the auditor's responsibility to communicate with those charged with governance in relation to the audit.

62. Existing paragraph 2 is amended to read as follows:

The auditor is required to obtain an understanding of the entity's system of internal control ~~relevant to the audit~~ when identifying and assessing the risks of material misstatement.[4] In making those risk assessments, the auditor considers the entity's system of internal control in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The auditor may identify control deficiencies in internal control not only during this risk assessment process but also at any other stage of the audit. This ASA specifies which identified deficiencies the auditor is required to communicate to those charged with governance and management.

63. Existing paragraph A3 is amended to read as follows:

While the concepts underlying controls in the control activities component in smaller entities are likely to be similar to those in larger entities, the formality with which they operate will vary. Further, smaller entities may find that certain types of controls activities are not necessary because of controls applied by management. For example, management's sole authority for granting credit to customers and approving significant purchases can provide effective control over important account balances and transactions, lessening or removing the need for more detailed controls ~~activities~~.

64. Existing paragraph A8 is amended to read as follows:

Controls may be designed to operate individually or in combination to effectively prevent, or detect and correct, misstatements.[5] For example, controls over accounts receivable may consist of both automated and manual controls designed to operate together to prevent, or detect and correct, misstatements in the account balance. A deficiency in internal control on its own may not be sufficiently important to constitute a significant deficiency. However, a combination of deficiencies affecting the same account balance or disclosure, ~~relevant~~ assertion, or component of the entity's system of internal control may increase the risks of misstatement to such an extent as to give rise to a significant deficiency.

Amendments to ASA 300

65. Existing footnote 8 in paragraph A4 is amended to read as follows:

ASA 315, paragraph ~~10~~17, establishes requirements and provides guidance on the engagement team's discussion of the susceptibility of the entity to material misstatements of the financial report. ASA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial

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1 See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraphs ~~4~~12 and ~~12~~21.

4 See ASA 315, paragraph ~~12~~21. Appendix 5~~Paragraphs A60-A65~~ provide guidance on controls relevant to the audit.

5 See ASA 315, paragraph ~~A66~~A175.

Report, paragraph ~~15~~16, provides guidance on the emphasis given during this discussion to the susceptibility of the entity's financial report to material misstatement due to fraud.

66. Existing paragraph A21 is amended to read as follows:

As discussed in paragraph A11, a suitable, brief memorandum may serve as the documented strategy for the audit of a smaller entity. For the audit plan, standard audit programs or checklists (see paragraph A17) drawn up on the assumption of few ~~relevant~~ controls[11] ~~activities~~, as is likely to be the case in a smaller entity, may be used provided that they are tailored to the circumstances of the engagement, including the auditor's risk assessments.

Amendments to ASA 320

67. Existing footnote 3 in paragraph 6 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and its Environment~~*, paragraphs ~~A129-A130~~A191-A192.

68. Existing footnote 13 in paragraph A2 is amended to read as follows:

See ASA 315, paragraph ~~25~~28, requires the auditor to identify and assess the risk of material misstatement at the financial statement and assertion level.

Amendments to ASA 330

69. Existing footnote 1 of paragraph 1 is amended to read as follows:

See ASA 315, *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*

70. Existing paragraph 6 is amended to read as follows:

The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. (Ref: Para. A4–A8; A44-A55)

71. Existing paragraph 7 is amended to read as follows:

In designing the further audit procedures to be performed, the auditor shall:

(a) Consider the reasons for the assessment given to the risk of material misstatement at the assertion level for each significant class of transactions, account balance, and disclosure, including:

(i) The likelihood and magnitude of ~~material~~ misstatement due to the particular characteristics of the ~~relevant~~ significant class of transactions, account balance, or disclosure (that is, the inherent risk); and

(ii) Whether the risk assessment takes account of ~~relevant~~ controls that address the risk of material misstatement (that is, the control risk), thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively (that is, the auditor ~~intends to rely on~~plans to test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); and (Ref: Para. A9–A18)

[11] See ASA 315, paragraph 26(a)

(b) Obtain more persuasive audit evidence the higher the auditor's assessment of risk. (Ref: Para. A19)

72. Existing paragraph 8 is amended to read as follows:

The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of ~~relevant~~ controls if:

(a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (that is, the auditor ~~intends~~ <u>plans to test</u> ~~to rely on~~ the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); or

(b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level. (Ref: Para. A20–A24)

73. Existing paragraph 10 is amended to read as follows:

In designing and performing tests of controls, the auditor shall:

(a) Perform other audit procedures in combination with enquiry to obtain audit evidence about the operating effectiveness of the controls, including:

(i) How the controls were applied at relevant times during the period under audit;

(ii) The consistency with which they were applied; and

(iii) By whom or by what means they were applied. (Ref: Para. A26–<u>A30</u>)

(b) <u>To the extent not already addressed, d</u>~~D~~etermine whether the controls to be tested depend upon other controls (indirect controls), and, if so, whether it is necessary to obtain audit evidence supporting the effective operation of those indirect controls. (Ref: Para. A32-A33)

74. Existing paragraph 13 is amended to read as follows:

In determining whether it is appropriate to use audit evidence about the operating effectiveness of controls obtained in previous audits, and, if so, the length of the time period that may elapse before retesting a control, the auditor shall consider the following:

(a) The effectiveness of other ~~elements~~ <u>components</u> of <u>the entity's system of</u> internal control, including the control environment, the entity's <u>process to</u> monitor~~ing of~~ <u>the system of internal</u> control~~s~~, and the entity's risk assessment process;

…

75. Existing paragraph 14 is amended to read as follows:

If the auditor plans to use audit evidence from a previous audit about the operating effectiveness of specific controls, the auditor shall establish the continuing relevance <u>and reliability</u> of that evidence by obtaining audit evidence about whether significant changes in those controls have occurred subsequent to the previous audit. The auditor shall obtain this evidence by performing enquiry combined with observation or inspection, to confirm the understanding of those specific controls, and:

…

76. Existing paragraph 15 is amended to read as follows:

If the auditor ~~plans~~ intends to rely on controls over a risk the auditor has determined to be a significant risk, the auditor shall test those controls in the current period.

77. Existing paragraph 16 is amended to read as follows:

When evaluating the operating effectiveness of ~~relevant~~ controls upon which the auditor intends to rely, the auditor shall evaluate whether misstatements that have been detected by substantive procedures indicate that controls are not operating effectively. The absence of misstatements detected by substantive procedures, however, does not provide audit evidence that controls related to the assertion being tested are effective. (Ref: Para. A42)

78. Existing paragraph 17 is amended to read as follows:

If deviations from controls upon which the auditor intends to rely are detected, the auditor shall make specific enquiries to understand these matters and their potential consequences, and shall determine whether: (Ref: Para. ~~A41~~A43)

…

(c) The ~~potential~~ risks of material misstatement need to be addressed using substantive procedures.

79. Existing paragraph 27 is amended to read as follows:

If the auditor has not obtained sufficient appropriate audit evidence ~~as to~~ related to a ~~an material financial statement~~ relevant assertion about a class of transactions, account balance or disclosure, the auditor shall attempt to obtain further audit evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall express a qualified opinion or disclaim an opinion on the financial report.

80. Existing paragraph A1 is amended to read as follows:

Overall responses to address the assessed risks of material misstatement at the financial statement level may include:

- Emphasising to the engagement team the need to maintain professional scepticism.
- Assigning more experienced staff or those with special skills or using experts.
- ~~Providing more supervision~~ Changes to the nature, timing and extent of direction and supervision of members of the engagement team and the review of the work performed.
- Incorporating additional elements of unpredictability in the selection of further audit procedures to be performed.
- Changes to the overall audit strategy as required by ASA 300, or planned audit procedures, and may include changes to:
    - The auditor's determination of performance materiality in accordance with ASA 320.
    - The auditor's plans to tests the operating effectiveness of controls, and the persuasiveness of audit evidence needed to support the planned reliance on the operating effectiveness of the controls, particularly when deficiencies in the control environment or the entity's monitoring activities are identified.
    - The nature, timing and extent of substantive procedures. For example, it may be appropriate to perform substantive procedures at or near the date of the financial report when the risk of material misstatement is assessed as higher.

- ~~Making general changes to the nature, timing or extent of audit procedures, for example: performing substantive procedures at the period end instead of at an interim date; or modifying the nature of audit procedures to obtain more persuasive audit evidence.~~

81. Existing paragraph A4 is amended to read as follows:

The auditor's assessment of the identified risks of material misstatement at the assertion level provides a basis for considering the appropriate audit approach for designing and performing further audit procedures. For example, the auditor may determine that:

(a) Only by performing tests of controls may the auditor achieve an effective response to the assessed risk of material misstatement for a particular assertion;

(b) Performing only substantive procedures is appropriate for particular assertions and, therefore, the auditor excludes the effect of controls from the ~~relevant risk~~ assessment of the risk of material misstatement. This may be because the ~~auditor's risk assessment procedures have not identified any effective controls relevant to the assertion, or because~~ auditor has not identified a risk for which substantive procedures alone cannot provide sufficient appropriate audit evidence and therefore is not required to test the operating effectiveness of controls. ~~testing controls would be inefficient and T~~therefore, the auditor ~~does~~ may not ~~intend to rely on~~ plan to test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures; or

(c) A combined approach using both tests of controls and substantive procedures is an effective approach.

The auditor need not design and perform further audit procedures where the assessment of the risk of material misstatement is below the acceptably low level. However, as required by paragraph 18, irrespective of the approach selected and the assessed risk of material misstatement, the auditor designs and performs substantive procedures for each material class of transactions, account balance, and disclosure.

82. Existing paragraph A7 is amended to read as follows:

Extent of an audit procedure refers to the quantity to be performed, for example, a sample size or the number of observations of a control ~~activity~~.

83. Existing paragraph A9 is amended to read as follows and footnote 2 is inserted:

ASA 315 requires that the auditor's assessment of the risks of material misstatement at the assertion level is performed by assessing inherent risk and control risk. The auditor assesses inherent risk by assessing the likelihood and magnitude of a misstatement taking into account how, and the degree to which the inherent risk factors affect the susceptibility to misstatement of relevant assertions.[2] The auditor's assessed risks, including the reasons for those assessed risks, may affect both the types of audit procedures to be performed and their combination. For example, when an assessed risk is high, the auditor may confirm the completeness of the terms of a contract with the counterparty, in addition to inspecting the document. Further, certain audit procedures may be more appropriate for some assertions than others. For example, in relation to revenue, tests of controls may be most responsive to the assessed risk of material misstatement of the completeness assertion, whereas substantive procedures may be most responsive to the assessed risk of material misstatement of the occurrence assertion.

[2] See ASA 315, paragraphs 31 and 34

84. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

85. Existing paragraph A10 is amended to read as follows:

The reasons for the assessment given to a risk are relevant in determining the nature of audit procedures. For example, if an assessed risk is lower because of the particular characteristics of a class of transactions without consideration of the related controls, then the auditor may determine that substantive analytical procedures alone provide sufficient appropriate audit evidence. On the other hand, if the assessed risk is lower because of ~~internal~~ the auditor plans to test the operating effectiveness of controls, and the auditor intends to base the substantive procedures on that low assessment, then the auditor performs tests of those controls, as required by paragraph 8(a). This may be the case, for example, for a class of transactions of reasonably uniform, non-complex characteristics that are routinely processed and controlled by the entity's information system.

86. Existing paragraph A18 is amended to read as follows:

In the case of very small entities, there may not be many controls activities that could be identified by the auditor, or the extent to which their existence or operation have been documented by the entity may be limited. In such cases, it may be more efficient for the auditor to perform further audit procedures that are primarily substantive procedures. In some rare cases, however, the absence of controls ~~activities~~ or of ~~other~~ components of the system of internal control may make it impossible to obtain sufficient appropriate audit evidence.

87. Existing paragraph A20 is amended to read as follows:

Tests of controls are performed only on those controls that the auditor has determined are suitably designed to prevent, or detect and correct, a material misstatement in a~~n~~ relevant assertion, and the auditor plans to test those controls. If substantially different controls were used at different times during the period under audit, each is considered separately.

88. Existing paragraph A24 is amended to read as follows:

In some cases, the auditor may find it impossible to design effective substantive procedures that by themselves provide sufficient appropriate audit evidence at the assertion level.[4] This may occur when an entity conducts its business using IT and no documentation of transactions is produced or maintained, other than through the IT system. In such cases, paragraph 8(b) requires the auditor to perform tests of ~~relevant~~ controls that address the risk for which substantive procedures alone cannot provide sufficient appropriate audit evidence.

89. Existing paragraph A27 is amended to read as follows:

The nature of the particular control influences the type of procedure required to obtain audit evidence about whether the control was operating effectively. For example, if operating effectiveness is evidenced by documentation, the auditor may decide to inspect it to obtain audit evidence about operating effectiveness. For other controls, however, documentation may not be available or relevant. For example, documentation of operation may not exist for some factors in the control environment, such as assignment of authority and responsibility, or for some types of controls ~~activities~~, such as automated controls ~~activities performed by a computer~~. In such circumstances, audit evidence about operating effectiveness may be obtained through enquiry in combination with other audit procedures such as observation or the use of CAATs.

90. Existing paragraph A29 is amended to read as follows:

[4] See ASA 315, paragraph 33~~30~~

Because of the inherent consistency of IT processing, it may not be necessary to increase the extent of testing of an automated control. An automated controls can be expected to function consistently unless the ~~program~~ IT application (including the tables, files, or other permanent data used by the ~~program~~ IT application) is changed. Once the auditor determines that an automated control is functioning as intended (which could be done at the time the control is initially implemented or at some other date), the auditor may consider performing tests to determine that the control continues to function effectively. Such tests ~~might~~ may include testing the general IT controls related to the IT application. ~~determining that:~~

- ~~Changes to the program are not made without being subject to the appropriate program change controls;~~
- ~~The authorised version of the program is used for processing transactions; and~~
- ~~Other relevant general controls are effective.~~

~~Such tests also might include determining that changes to the programs have not been made, as may be the case when the entity uses packaged software applications without modifying or maintaining them. For example, the auditor may inspect the record of the administration of IT security to obtain audit evidence that unauthorised access has not occurred during the period.~~

91. The following paragraph A30 is inserted following existing paragraph A29 of this Auditing Standard:

Similarly, the auditor may perform tests of controls that address risks of material misstatement related to the integrity of the entity's data, or the completeness and accuracy of the entity's system-generated reports, or to address risks of material misstatement for which substantive procedures alone cannot provide sufficient appropriate audit evidence. These tests of controls may include tests of general IT controls that address the matters in paragraph 10(a). When this is the case, the auditor may not need to perform any further testing to obtain audit evidence about the matters in paragraph 10(a).

92. The following paragraph A31 has been inserted following the insertion of paragraph A30 above:

When the auditor determines that a general IT control is deficient, the auditor may consider the nature of the related risk(s) arising from the use of IT that were identified in accordance with ASA 315[5] to provide the basis for the design of the auditor's additional procedures to address the assessed risk of material misstatement. Such procedures may address determining whether:

- The related risk(s) arising from IT has occurred. For example, if users have unauthorised access to an IT application (but cannot access or modify the system logs that track access), the auditor may inspect the system logs to obtain audit evidence that those users did not access the IT application during the period.
- There are any alternate or redundant general IT controls, or any other controls, that address the related risk(s) arising from the use of IT. If so, the auditor may identify such controls (if not already identified) and therefore evaluate their design, determine that they have been implemented and perform tests of their operating effectiveness. For example, if a general IT control related to user access is deficient, the entity may have an alternate control whereby IT management reviews end user access reports on a timely basis. Circumstances when an application control may address a risk arising from the use of IT may include when the information that may be affected by the general IT control deficiency can be reconciled to external sources (e.g., a bank

5 See ASA 315, paragraph 26(c)(i)

statement) or internal sources not affected by the general IT control deficiency (e.g., a separate IT application or data source).

93. Existing paragraph A30 is amended to read as follows:

In some circumstances, it may be necessary to obtain audit evidence supporting the effective operation of indirect controls (e.g., general IT controls). As explained in paragraphs A29 to A29b, general IT controls may have been identified in accordance with ASA 315 because of their support of the operating effectiveness of automated controls or due to their support in maintaining the integrity of information used in the entity's financial reporting, including system-generated reports. The requirement in paragraph 10(b) acknowledges that the auditor may have already tested certain indirect controls to address the matters in paragraph 10(a). ~~For example, when the auditor decides to test the effectiveness of a user review of exception reports detailing sales in excess of authorised credit limits, the user review and related follow up is the control that is directly of relevance to the auditor. Controls over the accuracy of the information in the reports (for example, general IT controls) are described as "indirect" controls.~~

94. Existing paragraph A31 has been deleted.

95. Existing paragraph A32 has been amended to read as follows:

Audit evidence pertaining only to a point in time may be sufficient for the auditor's purpose, for example, when testing controls over the entity's physical inventory counting at the period end. If, on the other hand, the auditor intends to rely on a control over a period, tests that are capable of providing audit evidence that the control operated effectively at relevant times during that period are appropriate. Such tests may include tests of controls in the entity's process to monitor~~ing of~~ the system of internal controls.

96. Existing paragraph A35 has been amended to read as follows:

In certain circumstances, audit evidence obtained from previous audits may provide audit evidence where the auditor performs audit procedures to establish its continuing relevance and reliability. For example, in performing a previous audit, the auditor may have determined that an automated control was functioning as intended. The auditor may obtain audit evidence to determine whether changes to the automated control have been made that affect its continued effective functioning through, for example, enquiries of management and the inspection of logs to indicate what controls have been changed. Consideration of audit evidence about these changes may support either increasing or decreasing the expected audit evidence to be obtained in the current period about the operating effectiveness of the controls.

97. Existing paragraph A36 has been amended to read as follows:

Changes may affect the relevance and reliability of the audit evidence obtained in previous audits such that there may no longer be a basis for continued reliance. For example, changes in a system that enable an entity to receive a new report from the system probably do not affect the relevance of audit evidence from a previous audit; however, a change that causes data to be accumulated or calculated differently does affect it.

98. Existing paragraph A38 is amended to read as follows:

In general, the higher the risk of material misstatement, or the greater the reliance on controls, the shorter the time period elapsed, if any, is likely to be. Factors that may decrease the period for retesting a control, or result in not relying on audit evidence obtained in previous audits at all, include the following:

…

- A ~~D~~deficiency~~t~~ in the entity's process to monitor~~ing of~~ the system of internal controls.

- A significant manual element to ~~the relevant~~ controls.

…

99. Existing paragraph A42 and the title are amended to read as follows:

Substantive Procedures (Ref: Para. 6, 18)

Paragraph 18 requires the auditor to design and perform substantive procedures for each material class of transactions, account balance, and disclosure, ~~irrespective of the assessed risks of material misstatement.~~ For significant classes of transactions, account balances and disclosures, substantive procedures may have already been performed because paragraph 6 requires the auditor to design and perform further audit procedures that are responsive to the assessed risks of material misstatement at the assertion level. Accordingly, substantive procedures are required to be designed and performed in accordance with paragraph 18:

- When the further audit procedures for significant classes of transactions, account balances or disclosures, designed and performed in accordance with paragraph 6, did not include substantive procedures; or
- For each class of transactions, account balance or disclosure that is not a significant class of transactions, account balance or disclosure, but that has been identified as material in accordance with ASA 315.[7]
- This requirement reflects the facts that: (a) the auditor's assessment of risk is judgemental and so may not identify all risks of material misstatement; and (b) there are inherent limitations to ~~internal~~ controls, including management override.

100. The following paragraph A45 is inserted following existing paragraph A42 of this Auditing Standard:

Not all assertions within a material class of transactions, account balance or disclosure are required to be tested. Rather, in designing the substantive procedures to be performed, the auditor's consideration of the assertion(s) in which, if a misstatement were to occur, there is a reasonable possibility of the misstatement being material, may assist in identifying the appropriate nature, timing and extent of the procedures to be performed.

101. Existing paragraph A45 is amended to read as follows:

The ~~nature~~ assessment of the risk ~~and~~ or the nature of the assertion is relevant to the design of tests of details. For example, tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. On the other hand, tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.

102. Existing paragraph A46 is amended to read as follows:

Because the assessment of the risk of material misstatement takes account of ~~internal~~ controls that the auditor plans to test, the extent of substantive procedures may need to be increased when the results from tests of controls are unsatisfactory. However, increasing the extent of an audit procedure is appropriate only if the audit procedure itself is relevant to the specific risk.

103. Existing paragraph A56 is amended to read as follows:

[7] See ASA 315, paragraph 36

Performing substantive procedures at an interim date without undertaking additional procedures at a later date increases the risk that the auditor will not detect misstatements that may exist at the period end. This risk increases as the remaining period is lengthened. Factors such as the following may influence whether to perform substantive procedures at an interim date:

- The control environment and other ~~relevant~~ controls.

…

104. Existing paragraph A57 is amended to read as follows:

Factors such as the following may influence whether to perform substantive analytical procedures with respect to the period between the interim date and the period end:

…

- Whether the information system ~~relevant to financial reporting~~ will provide information concerning the balances at the period end and the transactions in the remaining period that is sufficient to permit investigation of:

…

105. Existing paragraph A60 is amended to read as follows:

An audit of financial report is a cumulative and iterative process. As the auditor performs planned audit procedures, the audit evidence obtained may cause the auditor to modify the nature, timing or extent of other planned audit procedures. Information may come to the auditor's attention that differs significantly from the information on which the risk assessment was based. For example:

…

In such circumstances, the auditor may need to re-evaluate the planned audit procedures, based on the revised consideration of assessed risks <u>of material misstatement</u> ~~for all or some of~~ <u>and the effect on</u> the <u>significant</u> classes of transactions, account balances, or disclosures and ~~related~~ <u>their relevant</u> assertions. ASA 315 contains further guidance on revising the auditor's risk assessment.[10]

106. Existing paragraph A62 is amended to read as follows:

The auditor's judgement as to what constitutes sufficient appropriate audit evidence is influenced by such factors as the following:

…

- Understanding of the entity and its environment, <u>the applicable financial reporting framework and</u> ~~including the~~ entity's <u>system of</u> internal control.

107. Existing paragraph A63 is amended to read as follows:

The form and extent of audit documentation is a matter of professional judgement, and is influenced by the nature, size and complexity of the entity and its <u>system of</u> internal control, availability of information from the entity and the audit methodology and technology used in the audit.

10 See ASA 315, paragraph <u>53</u>~~31~~

108. As a result of the footnotes insertion above, all footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

Amendments to ASA 402

109. Existing paragraph 1 is amended to read as follows:

This Auditing Standard deals with the user auditor's responsibility to obtain sufficient appropriate audit evidence when a user entity uses the services of one or more service organisations. Specifically, it expands on how the user auditor applies ASA 315[1] and ASA 330[2] in obtaining an understanding of the user entity, including the entity's system of internal control relevant to the preparation of the financial report ~~relevant to the audit~~, sufficient to identify and assess the risks of material misstatement and in designing and performing further audit procedures responsive to those risks.

110. Existing paragraph 3 is amended to read as follows:

Services provided by a service organisation are relevant to the audit of a user entity's financial report when those services, and the controls over them, are part of the user entity's information system , ~~including related business processes,~~ relevant to ~~financial reporting~~ the preparation of the financial report. ~~Although m~~ Most controls at the service organisation are likely to ~~relate to financial reporting~~ be part of the user entity's information system relevant to the preparation of the financial report, ~~there may be other~~ or related controls ~~that may also be relevant to the audit~~, such as controls over the safeguarding of assets. A service organisation's services are part of a user entity's information system, ~~including related business processes, relevant to financial reporting~~ if these services affect any of the following:

(a) How information relating to significant classes of transactions, account balances and disclosures flows through the user entity's information system, whether manually or using IT, and whether obtained from within or outside the general ledger and subsidiary ledgers. ~~The classes of transactions in the user entity's operations that are significant to the user entity's financial report;~~ This includes when the service organisation's services affect how:

   (i) ~~(b) The procedures, within both information technology (IT) and manual systems, by which the user entity's transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial report;~~ Transactions of the user entity are initiated, and how information about them is recorded, processed, corrected as necessary, and incorporated in the general ledger and reported in the financial report; and

   (ii) Information about events or conditions, other than transactions, is captured, processed and disclosed by the user entity in the financial report.

(b) ~~(c)~~ The ~~related~~ accounting records, ~~either in electronic or manual form, supporting information and~~ specific accounts in the user entity's financial report and other supporting records relating to the flows of information in paragraph 3(a)~~that are used to initiate, record, process and report the user entity's transactions; this includes the correction of incorrect information and how information is transferred to the general ledger;~~

~~(d) How the user entity's information system captures events and conditions, other than transactions, that are significant to the financial report;~~

[1] See ASA 315 *Identifying and Assessing the Risks of Material Misstatement* ~~*through Understanding the Entity and Its Environment*~~.

(ce) The financial reporting process used to prepare the user entity's financial report from the records described in paragraph 3(b), including as it relates to disclosures and to accounting estimates relating to significant classes of transactions, account balances and disclosures ~~accounting estimates and disclosures~~; and

(d) The entity's IT environment relevant to (a) to (c) above.

~~(f) Controls surrounding journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments.~~

…

111. Existing paragraph 7 is amended to read as follows:

The objectives of the user auditor, when the user entity uses the services of a service organisation, are:

(a) To obtain an understanding of the nature and significance of the services provided by the service organisation and their effect on the user entity's system of internal control ~~relevant to the audit~~, sufficient to provide an appropriate basis for the identification and assessment of ~~identify and assess~~ the risks of material misstatement; and

(b) To design and perform audit procedures responsive to those risks.

…

112. Footnote 3 in paragraph 9 is amended to read as follows:

See ASA 315, paragraph ~~11~~19.

113. Existing paragraph 10 is amended to read as follows:

When obtaining an understanding of the entity's system of internal control ~~relevant to the audit~~ in accordance with ASA 315,[4] the user auditor shall identify controls in the control activities component[4] ~~evaluate the design and implementation of relevant controls~~ at the user entity, from those that relate to the services provided by the service organisation, including those that are applied to the transactions processed by the service organisation, and evaluate their design and determine whether they have been implemented.[5] (Ref: Para. A12–A14)

114. As a result of the footnotes deletion and insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

115. Existing paragraph 11 is amended to read as follows:

The user auditor shall determine whether a sufficient understanding of the nature and significance of the services provided by the service organisation and their effect on the user entity's system of internal control ~~relevant to the audit~~ has been obtained to provide an appropriate basis for the identification and assessment of the risks of material misstatement.

116. Existing paragraph 12 is amended to read as follows:

If the user auditor is unable to obtain a sufficient understanding from the user entity, the user auditor shall obtain that understanding from one or more of the following procedures:

…

4 See ASA 315, paragraphs 26(a)
5 See ASA 315, paragraph 26(d)

(d) Using another auditor to perform procedures that will provide the necessary information about ~~the relevant~~ controls at the service organisation. (Ref: Para. A15–A20)

117. Existing paragraph 14 is amended to read as follows:

If the user auditor plans to use a type 1 or type 2 report as audit evidence to support the user auditor's understanding about the design and implementation of controls at the service organisation, the user auditor shall:

…

(b) Evaluate the sufficiency and appropriateness of the evidence provided by the report for the understanding of the ~~user entity's internal~~ controls at the service organisation ~~relevant to the audit~~; and

118. Existing footnote 7 in paragraph A14 is amended to read as follows:

See ASA 315, paragraph ~~30~~26(a)(iii).

119. Existing paragraph A19 is amended to read as follows:

Another auditor may be used to perform procedures that will provide the necessary information about the relevant controls at the service organisation related to services provided to the user entity. If a type 1 or type 2 report has been issued, the user auditor may use the service auditor to perform these procedures as the service auditor has an existing relationship with the service organisation. The user auditor using the work of another auditor may find the guidance in ASA 600 useful as it relates to understanding another auditor (including that auditor's independence and professional competence), involvement in the work of another auditor in planning the nature, timing and extent of such work, and in evaluating the sufficiency and appropriateness of the audit evidence obtained.

120. Existing paragraph A22 is amended to read as follows:

A type 1 or type 2 report, along with information about the user entity, may assist the user auditor in obtaining an understanding of:

…

A type 1 or type 2 report may assist the user auditor in obtaining a sufficient understanding to identify and assess the risks of material misstatement. A type 1 report, however, does not provide any evidence of the operating effectiveness of the ~~relevant~~ controls.

121. Existing paragraph A29 is amended to read as follows:

The user auditor is required by ASA 330 to design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of ~~relevant~~ controls in certain circumstances. In the context of a service organisation, this requirement applies when:

…

122. Existing paragraph A30 is amended to read as follows:

If a type 2 report is not available, a user auditor may contact the service organisation, through the user entity, to request that a service auditor be engaged to provide a type 2 report that includes tests of the operating effectiveness of the ~~relevant~~ controls or the user auditor may use another auditor to perform procedures at the service organisation that test the operating effectiveness of those controls. A user auditor may also visit the service organisation and perform tests of ~~relevant~~ controls if the service organisation agrees to it. The user auditor's risk assessments are based on the combined evidence provided by the work of another auditor and the user auditor's own procedures.

123. Existing paragraph A33 is amended to read as follows:

It may also be necessary for the user auditor to obtain additional evidence about significant changes to the ~~relevant~~ controls at the service organisation outside of the period covered by the type 2 report or determine additional audit procedures to be performed. Relevant factors in determining what additional audit evidence to obtain about controls at the service organisation that were operating outside of the period covered by the service auditor's report may include:

…

- The effectiveness of the control environment and the user entity's process to monitor the system of internal control ~~monitoring of controls at the user entity~~.

124. Existing paragraph A34 is amended to read as follows:

Additional audit evidence may be obtained, for example, by extending tests of controls over the remaining period or testing the user entity's process to monitor the system of internal control ~~monitoring of controls~~.

125. Existing paragraph A39 is amended to read as follows:

The user auditor is required to communicate in writing significant deficiencies identified during the audit to both management and those charged with governance on a timely basis.[11] The user auditor is also required to communicate to management at an appropriate level of responsibility on a timely basis other deficiencies in internal control identified during the audit that, in the user auditor's professional judgement, are of sufficient importance to merit management's attention.[12] Matters that the user auditor may identify during the audit and may communicate to management and those charged with governance of the user entity include:

- Any controls within the entity's process to monitor the system of internal control ~~monitoring of controls~~ that could be implemented by the user entity, including those identified as a result of obtaining a type 1 or type 2 report;

…

Amendments to ASA 500

126. Existing paragraph A5 is amended to read as follows:

Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has evaluated whether such information remains relevant and reliable as audit evidence for the current audit ~~determined whether changes have occurred since the previous audit that may affect its relevance to the current audit)~~ or a firm's quality control procedures for client acceptance and continuance. In addition to other sources inside and outside the entity, the entity's accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared using the work of a management's expert. Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. In addition, in some cases the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence.

127. Existing footnote 9 in paragraph A5 is amended to read as follows:

See ASA 315, paragraph ~~9~~16.

128. Existing paragraph A21 is amended to read as follows:

Observation consists of looking at a process or procedure being performed by others, for example, the auditor's observation of inventory counting by the entity's personnel, or of the performance of controls ~~activities~~. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place, and by the fact that the act of being observed may affect how the process or procedure is performed. See ASA 501 for further guidance on observation of the counting of inventory.

Amendments to ASA 501

129. Existing paragraph A4 is amended to read as follows:

Matters relevant in evaluating management's instructions and procedures for recording and controlling the physical inventory counting include whether they address, for example:

- The application of appropriate controls ~~activities~~, for example, collection of used physical inventory count records, accounting for unused physical inventory count records, and count and re-count procedures.

Amendments to ASA 505

130. Existing footnote 14 in paragraph A9 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~31~~37.

131. Existing footnote 18 in paragraph A17 is amended to read as follows:

See ASA 315, paragraph ~~31~~37.

132. Existing footnote 20 in paragraph A19 is amended to read as follows:

See ASA 315, paragraph ~~31~~37.

Amendments to ASA 520

133. Existing footnote 1 in paragraph 1 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~6~~14(b).

134. Existing footnote 10 in paragraph A18 is amended to read as follows:

See ASA 315, paragraph ~~31~~37.

Amendments to ASA 530

135. Existing paragraph A7 is amended to read as follows:

In considering the characteristics of a population, for tests of controls, the auditor makes an assessment of the expected rate of deviation based on the auditor's understanding of the ~~relevant~~ controls or on the examination of a small number of items from the population. This assessment is made in order to design an audit sample and to determine sample size. For example, if the expected rate of deviation is unacceptably high, the auditor will ordinarily decide not to perform tests of controls. Similarly, for tests of details, the auditor makes an assessment of the expected misstatement in the population. If the expected misstatement is high, 100% examination or use of a large sample size may be appropriate when performing tests of details.

136. Existing Factor 1 of Appendix 2 is amended to read as follows:

An increase in the extent to which the auditor's risk assessment takes into account ~~relevant~~ plans to test the operating effectiveness of controls

Amendments to ASA 540

137. Existing paragraph 4 is amended to read as follows and footnote 5 is inserted:

This Auditing Standard requires a separate assessment of inherent risk for identified risks of material misstatement at the assertion level.[5] ~~purposes of assessing the risks of material misstatement at the assertion level for accounting estimates.~~ In the context of ASA 540 (Revised), and ~~D~~depending on the nature of a particular accounting estimate, the susceptibility of an assertion to a misstatement that could be material may be subject to or affected by estimation uncertainty, complexity, subjectivity or other inherent risk factors, and the interrelationship among them. As explained in ASA 200,[6] inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others. Accordingly, the assessment of inherent risk depends on the degree to which the inherent risk factors affect the likelihood or magnitude of misstatement, and varies on a scale that is referred to in this ASA as the spectrum of inherent risk. (Ref: Para. A8–A9, A65–A66, Appendix 1)

138. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

139. Existing paragraph 5 is amended to read as follows:

This ASA refers to relevant requirements in ASA 315 and ASA 330, and provides related guidance, to emphasise the importance of the auditor's decisions about controls relating to accounting estimates, including decisions about whether:

- There are controls ~~relevant to the audit~~ required to be identified by ASA 315 , for which the auditor is required to evaluate their design and determine whether they have been implemented.
- To test the operating effectiveness of ~~relevant~~ controls.

140. Existing paragraph 6 is amended to read as follows:

~~This~~ ASA 315 also requires a separate assessment of control risk when assessing the risks of material misstatement at the assertion level ~~for accounting estimates~~. In assessing control risk, the auditor takes into account whether the auditor's further audit procedures contemplate planned reliance on the operating effectiveness of controls. If the auditor does not ~~perform~~ plan to test~~s~~ the operating effectiveness of controls, or does not intend to rely on the operating effectiveness of controls, the auditor's assessment of the ~~risk of material misstatement at the assertion level~~ control risk ~~cannot be reduced for the effective operation of controls with respect to the particular assertion~~ is such that the assessment of the risk of material misstatement is the same as the assessment of inherent risk.[6] (Ref: Para. A10)

141. Existing paragraph 8 is amended to read as follows:

The exercise of professional scepticism in relation to accounting estimates is affected by the auditor's consideration of inherent risk factors, and its importance increases when accounting estimates are subject to a greater degree of estimation uncertainty or are affected to a greater degree by complexity, subjectivity or other inherent risk factors. Similarly, the exercise of professional scepticism is important when there is greater susceptibility to misstatement due to

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5 See ASA 315, paragraph 31

6 See ASA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph A40

management bias or ~~fraud~~ other fraud risk factors insofar as they affect inherent risk. (Ref: Para. A11)

142. Existing paragraph 13 is amended to read as follows:

When obtaining an understanding of the entity and its environment, the applicable financial reporting framework and ~~including~~ the entity's system of internal control, as required by ASA 315,[8] the auditor shall obtain an understanding of the following matters related to the entity's accounting estimates. The auditor's procedures to obtain the understanding shall be performed to the extent necessary to obtain audit evidence that provides an appropriate basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. (Ref: Para. A19–A22)

Obtaining an Understanding of t~~T~~he Entity and Its Environment and the Applicable Financial Reporting Framework

(a) The entity's transactions and other events or~~and~~ conditions that may give rise to the need for, or changes in, accounting estimates to be recognised or disclosed in the financial report. (Ref: Para. A23)

(b) The requirements of the applicable financial reporting framework related to accounting estimates (including the recognition criteria, measurement bases, and the related presentation and disclosure requirements); and how they apply in the context of the nature and circumstances of the entity and its environment, including how ~~transactions and other events or conditions are subject to, or affected by~~, the inherent risk factors affect susceptibility to misstatement of assertions. (Ref: Para. A24–A25)

…

Obtaining an Understanding of t~~T~~he Entity's System of Internal Control

…

(h) The entity's information system as it relates to accounting estimates, including:

(i) How information relating to accounting estimates and related disclosures for significant classes of transactions, account balances or disclosures flows through the entity's information system ~~The classes of transactions, events and conditions, that are significant to the financial report and that give rise to the need for, or changes in, accounting estimates and related disclosures~~; and (Ref: Para. A34–A35)

…

(i) Identified controls in the control activities component[9] ~~Control activities relevant to the audit~~ over management's process for making accounting estimates as described in paragraph 13(h)(ii). (Ref: Para. A50–A54)

…

143. Existing paragraph 16 is amended to read as follows:

In identifying and assessing the risks of material misstatement relating to an accounting estimate and related disclosures at the assertion level, including separately assessing inherent risk and control risk at the assertion level, as required by ASA 315,[10] the auditor shall

[8] See ASA 315, paragraphs ~~3, 5–6, 9, 11–12, 15-17, and 20-21~~19–27
[9] See ASA 315, paragraphs 26(a)(i)–(iv)
[10] See ASA 315, paragraph ~~25 and 26~~31 and 34

~~separately assess inherent risk and control risk. The auditor shall~~ take the following into account in identifying the risks of material misstatement and in assessing inherent risk: (Ref: Para. A64–A71)

…

144. Existing paragraph 17 is amended to read as follows:

The auditor shall determine whether any of the risks of material misstatement identified and assessed in accordance with paragraph 16 are, in the auditor's judgement, a significant risk.[11] If the auditor has determined that a significant risk exists, the auditor shall identify controls that ~~obtain an understanding of the entity's controls, including control activities, relevant to~~ address that risk,~~.~~[12] and evaluate whether such controls have been designed effectively, and determine whether they have been implemented.[13] (Ref: Para. A80)

145. Existing paragraph 19 is amended to read as follows:

As required by ASA 330,[17] the auditor shall design and perform tests to obtain sufficient appropriate audit evidence as to the operating effectiveness of ~~relevant~~ controls, if:

146. Existing paragraph A8 is amended to read as follows:

Inherent risk factors are characteristics of ~~conditions and~~ events or~~and~~ conditions that ~~may~~ affect ~~the~~ susceptibility ~~of an assertion~~ to misstatement, whether due to fraud or error, of an assertion about a class of transactions, account balance or disclosures, before consideration of controls.[32] Appendix 1 further explains the nature of these inherent risk factors, and their inter-relationships, in the context of making accounting estimates and their presentation in the financial report.

147. Existing paragraph A9 is amended to read as follows:

~~In addition to the inherent risk factors of estimation uncertainty, complexity or subjectivity, other inherent risk factors that the auditor may consider in identifying and~~ When assessing the risks of material misstatement at the assertion level[33], in addition to estimation uncertainty, complexity, and subjectivity, the auditor also takes into account the degree ~~may include the extent~~ to which inherent risk factors included in ASA 315, (other than estimation uncertainty, complexity, and subjectivity), affect susceptibility to misstatement of assertions to misstatement about the accounting estimate. Such additional inherent risk factors include ~~is subject to, or affected by~~:

- Change in the nature or circumstances of the relevant financial statement items, or requirements of the applicable financial reporting framework which may give rise to the need for changes in the method, assumptions or data used to make the accounting estimate.
- Susceptibility to misstatement due to management bias, or other fraud risk factors insofar as they affect inherent risk, in making the accounting estimate.
- Uncertainty, other than estimation uncertainty.

148. Existing paragraph A10 is amended to read as follows:

~~An important consideration for the auditor i~~In assessing control risk at the assertion level in accordance with ASA 315, the auditor takes into account ~~is the effectiveness of the design of~~

11 See ASA 315, paragraph 32~~27~~
12 See ASA 315, paragraph 26(a)(i)~~29~~
13 See ASA 315, paragraph 26(a)
32 See ASA 315, paragraph 12(f)
33 See ASA 315, paragraph 31

~~the controls that~~ whether the auditor ~~intends~~ plans to ~~rely~~ test ~~on~~ the operating effectiveness of controls. ~~and the extent to which the controls address the assessed inherent risks at the assertion level.~~ When the auditor is considering whether to test the operating effectiveness of controls, ~~T~~the auditor's evaluation that controls are effectively designed and have been implemented supports an expectation, by the auditor, about the operating effectiveness of the controls in ~~determining whether~~ establishing the plan to test them.

149. Existing title under the section heading **Risk Assessment Procedures and Related Activities** is amended to read as follows:

Obtaining an Understanding of the Entity and Its Environment, the Applicable Financial Reporting Framework, and the Entity's System of Internal Control (Ref: Para. 13)

150. Existing paragraph A19 is amended to read as follows:

Paragraphs 19~~11~~–27~~24~~ of ASA 315 require the auditor to obtain an understanding of certain matters about the entity and its environment, the applicable financial reporting framework and ~~including~~ the entity's system of internal control. The requirements in paragraph 13 of this ASA relate more specifically to accounting estimates and build on the broader requirements in ASA 315.

151. Existing paragraph A20 is amended to read as follows:

The nature, timing, and extent of the auditor's procedures to obtain the understanding of the entity and its environment, ~~including~~ the applicable financial reporting framework, and the entity's system of internal control, related to the entity's accounting estimates, may depend, to a greater or lesser degree, on the extent to which the individual matter(s) apply in the circumstances. For example, the entity may have few transactions or other events ~~and~~ or conditions that give rise to the need for accounting estimates, the applicable financial reporting requirements may be simple to apply, and there may be no relevant regulatory factors. Further, the accounting estimates may not require significant judgements, and the process for making the accounting estimates may be less complex. In these circumstances, the accounting estimates may be subject to, or affected by, estimation uncertainty, complexity, subjectivity, or other inherent risk factors to a lesser degree, and there may be fewer identified controls in the control activities component ~~relevant to the audit~~. If so, the auditor's risk identification and assessment procedures are likely to be less extensive and may be obtained primarily through enquiries of management with appropriate responsibilities for the financial report, such as ~~and~~ simple walk-throughs of management's process for making the accounting estimate (including when evaluating whether identified controls in that process are designed effectively and when determining whether the control has been implemented).

152. Existing title under the section heading **The Entity and Its Environment** is amended to read as follows:

The entity's transactions and other events ~~and~~ or conditions (Ref: Para. 13(a))

153. Existing paragraph A24 is amended to read as follows:

Obtaining an understanding of the requirements of the applicable financial reporting framework provides the auditor with a basis for discussion with management and, where applicable, those charged with governance about how management has applied the~~ose~~ requirements of the applicable financial reporting framework relevant to the accounting estimates, and about the auditor's determination of whether they have been applied appropriately. This understanding also may assist the auditor in communicating with those charged with governance when the auditor considers a significant accounting practice that is acceptable under the applicable financial reporting framework, not to be the most appropriate in the circumstances of the entity.[34]

154. Existing section heading after paragraph A27 has been amended to read as *The Entity's System of Internal Control ~~Relevant to the Audit~~*

155. Existing paragraph A28 is amended to read as follows:

In applying ASA 315,[35] the auditor's understanding of the nature and extent of oversight and governance that the entity has in place over management's process for making accounting estimates may be important to the auditor's required evaluation of ~~as it relates to~~ whether:

- Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical behaviour; ~~and~~
- The ~~strengths in the entity's~~ control environment ~~elements collectively~~ provides an appropriate foundation for the other components of the system of internal control considering the nature and size of the entity; and ~~whether~~
- ~~those other components are undermined by c~~Control deficiencies identified in the control environment undermine the other components of the system of internal control.

156. Existing paragraph A32 is amended to read as follows:

Understanding how the entity's risk assessment process identifies and addresses risks relating to accounting estimates may assist the auditor in considering changes in:

…

- The entity's information systems or IT environment; and

…

157. Existing paragraph A34 is amended to read as follows:

The significant classes of transactions, events and conditions within the scope of paragraph 13(h) are the same as the significant classes of transactions, events and conditions relating to accounting estimates and related disclosures that are subject to paragraphs 25(a)~~18(a) and (d)~~ of ASA 315. In obtaining the understanding of the entity's information system as it relates to accounting estimates, the auditor may consider:

…

158. Existing paragraph A35 is amended to read as follows:

During the audit, the auditor may identify classes of transactions, events ~~and~~ or conditions that give rise to the need for accounting estimates and related disclosures that management failed to identify. ASA 315 deals with circumstances where the auditor identifies risks of material misstatement that management failed to identify, including ~~determining whether there is a significant deficiency in internal control with regard to~~ considering the implications for the auditor's evaluation of the entity's risk assessment process.[38]

159. Existing paragraph A39 is amended to read as follows:

Management may design and implement specific controls around models used for making accounting estimates, whether management's own model or an external model. When the model itself has an increased level of complexity or subjectivity, such as an expected credit loss model or a fair value model using level 3 inputs, controls that address such complexity or

[35] See ASA 315, paragraph 21(a)~~14~~
[38] See ASA 315, paragraph 22(b)~~17~~

subjectivity may be. When complexity in relation to models is present, controls over data integrity are also more likely to be identified controls in accordance with ASA 315 ~~relevant to the audit~~. Factors that may be appropriate for the auditor to consider in obtaining an understanding of the model and ~~of~~ related identified controls ~~activities relevant to the audit~~ include the following:

…

160. Existing paragraph A44 is amended to read as follows:

Matters that the auditor may consider in obtaining an understanding of how management selects the data on which the accounting estimates are based include:

…

- The complexity of IT applications or other aspects of the entity's IT environment ~~the information technology systems~~ used to obtain and process the data, including when this involves handling large volumes of data.

…

161. Existing section heading before paragraph A50 has been amended to read Identified Controls ~~Activities Relevant to the Audit~~ Over Management's Process for Making Accounting Estimates (Ref: Para 13(i))

162. Existing paragraph A50 is amended to read as follows:

The auditor's judgement in identifying controls ~~relevant to the audit~~in the controls activities component, and therefore the need to evaluate the design of those controls and determine whether they have been implemented, relates to management's process described in paragraph 13(h)(ii). The auditor may not identify ~~relevant~~ controls ~~activities~~ in relation to all ~~the elements~~ aspects of paragraph 13(h)(ii).~~, depending on the complexity associated with the accounting estimate.~~

163. Existing paragraph A51 is amended to read as follows:

As part of ~~obtaining an understanding of~~ identifying the controls ~~activities relevant to the audit~~, and evaluating their design and determining whether they have been implemented, the auditor may consider:

…

- The effectiveness of the design of the controls. ~~activities.~~ Generally, it may be more difficult for management to design controls that address subjectivity and estimation uncertainty in a manner that effectively prevents, or detects and corrects, material misstatements, than it is to design controls that address complexity. Controls that address subjectivity and estimation uncertainty may need to include more manual elements, which may be less reliable than automated controls as they can be more easily bypassed, ignored or overridden by management. The design effectiveness of controls addressing complexity may vary depending on the reason for, and the nature of, the complexity. For example, it may be easier to design more effective controls related to a method that is routinely used or over the integrity of data.

164. Existing paragraph A52 is amended to read as follows:

When management makes extensive use of information technology in making an accounting estimate, identified controls ~~relevant to the audit~~ in the control activities component are likely to include general IT controls and ~~application~~ information processing controls. Such controls may address risks related to:

- Whether the IT applications or other aspects of the IT environment ~~information technology system~~ has the capability and is appropriately configured to process large volumes of data;
- Complex calculations in applying a method. When diverse IT applications ~~systems~~ are required to process complex transactions, regular reconciliations between the IT applications ~~systems~~ are made, in particular when the IT applications ~~systems~~ do not have automated interfaces or may be subject to manual intervention;

…

165. Existing paragraph A53 is amended to read as follows:

In some industries, such as banking or insurance, the term governance may be used to describe activities within the control environment, the entity's process to monitor the system of internal control ~~monitoring of controls~~, and other components of the system of internal control, as described in ASA 315.[40]

166. Existing paragraph A54 is amended to read as follows:

For entities with an internal audit function, its work may be particularly helpful to the auditor in obtaining an understanding of:

…

- The design and implementation of controls ~~activities~~ that address the risks related to the data, assumptions and models used to make the accounting estimates;

…

167. Existing paragraph A59 is amended to read as follows:

The measurement objective for fair value accounting estimates and other accounting estimates, based on current conditions at the measurement date, deals with perceptions about value at a point in time, which may change significantly and rapidly as the environment in which the entity operates changes. The auditor may therefore focus the review on obtaining information that may be relevant to identifying and assessing risks of material misstatement. For example, in some cases, obtaining an understanding of changes in marketplace participant assumptions that affected the outcome of a previous period's fair value accounting estimates may be unlikely to provide relevant audit evidence. In this case, audit evidence may be obtained by understanding the outcomes of assumptions (such as a cash flow projections) and understanding the effectiveness of management's prior estimation process that supports the identification and assessment of the risks of material misstatement in the current period.

168. Existing paragraph A60 is amended to read as follows:

A difference between the outcome of an accounting estimate and the amount recognised in the previous period's financial report does not necessarily represent a misstatement of the previous period's financial report. However, such a difference may represent a misstatement if, for example, the difference arises from information that was available to management when the previous period's financial report were finalised, or that could reasonably be expected to have been obtained and taken into account in the context of the applicable financial reporting framework.[38] Such a difference may call into question management's process for taking information into account in making the accounting estimate. As a result, the auditor may reassess any plan to test related controls and the related assessment of control risk ~~and~~ or may determine that more persuasive audit evidence needs to be obtained about the matter. Many

[40] See ASA 315, Appendix 3 ~~paragraph A77~~

financial reporting frameworks contain guidance on distinguishing between changes in accounting estimates that constitute misstatements and changes that do not, and the accounting treatment required to be followed in each case.

169. Existing paragraph A65 is amended to read as follows:

Paragraph A42 of ASA 200 states that the ASAs ~~do not ordinarily refer to inherent risk and control risk separately~~ typically refer to the "risks of material misstatement" rather than to inherent risk and control risk separately. ~~However, this~~ ASA 315 ~~Auditing Standard~~ requires a separate assessment of inherent risk and control risk to provide a basis for designing and performing further audit procedures to respond to the risks of material misstatement at the assertion level,[45] including significant risks, ~~at the assertion level for accounting estimates~~ in accordance with ASA 330.[46]

170. Existing paragraph A66 is amended to read as follows:

In identifying the risks of material misstatement and in assessing inherent risk for accounting estimates in accordance with ASA 315,[47] the auditor is required to take into account ~~the degree to which the accounting estimate is subject to, or affected by,~~ the inherent risk factors that affect susceptibility to misstatement of assertions, and how they do so ~~estimation uncertainty, complexity, subjectivity, or other inherent risk factors~~. The auditor's consideration of the inherent risk factors may also provide information to be used in ~~determining~~:

- Assessing the likelihood and magnitude of misstatement (i.e., ~~W~~where inherent risk is assessed on the spectrum of inherent risk); and
- Determining ~~T~~the reasons for the assessment given to the risks of material misstatement at the assertion level, and that the auditor's further audit procedures in accordance with paragraph 18 are responsive to those reasons.

171. Existing paragraph A68 is amended to read as follows:

The relevance and significance of inherent risk factors may vary from one estimate to another. Accordingly, the inherent risk factors may, either individually or in combination, affect simple accounting estimates to a lesser degree and the auditor may identify fewer risks or assess inherent risk ~~at~~ close to the lower end of the spectrum of inherent risk.

172. Existing paragraph A70 is amended to read as follows:

Events occurring after the date of the financial report may provide additional information relevant to the auditor's assessment of the risks of material misstatement at the assertion level. For example, the outcome of an accounting estimate may become known during the audit. In such cases, the auditor may assess or revise the assessment of the risks of material misstatement at the assertion level,[48] regardless of how the inherent risk factors affect susceptibility of assertions to misstatement relating to ~~degree to which~~ the accounting estimate. ~~was subject to, or affected by, estimation uncertainty, complexity, subjectivity or other inherent risk factors.~~ Events occurring after the date of the financial report also may influence the auditor's selection of the approach to testing the accounting estimate in accordance with paragraph 18. For example, for a simple bonus accrual that is based on a straightforward percentage of compensation for selected employees, the auditor may conclude that there is relatively little complexity or subjectivity in making the accounting estimate, and therefore may assess inherent risk at the assertion level ~~at~~ close to the lower end of the spectrum of inherent risk. The payment of the bonuses subsequent to period end may provide

[45] See ASA 315, paragraphs 31 and 34
[47] See ASA 315, paragraph 31(a)
[48] See ASA 315, paragraph 37~~31~~

sufficient appropriate audit evidence regarding the assessed risks of material misstatement at the assertion level.

173. Existing paragraph A79 is amended to read as follows:

The degree of subjectivity associated with an accounting estimate influences the susceptibility of the accounting estimate to misstatement due to management bias or ~~fraud~~ other fraud risk factors insofar as they affect inherent risk. For example, when an accounting estimate is subject to a high degree of subjectivity, the accounting estimate is likely to be more susceptible to misstatement due to management bias or fraud and this may result in a wide range of possible measurement outcomes. Management may select a point estimate from that range that is inappropriate in the circumstances, or that is inappropriately influenced by unintentional or intentional management bias, and that is therefore misstated. For continuing audits, indicators of possible management bias identified during the audit of preceding periods may influence the planning and risk assessment procedures in the current period.

174. Existing section heading before paragraph A85 has been amended to read as *When the Auditor Intends to Rely on the Operating Effectiveness of ~~Relevant~~ Controls* (Ref: Para: 19)

175. Existing paragraph A85 is amended to read as follows:

Testing the operating effectiveness of ~~relevant~~ controls may be appropriate when inherent risk is assessed as higher on the spectrum of inherent risk, including for significant risks. This may be the case when the accounting estimate is subject to or affected by a high degree of complexity. When the accounting estimate is affected by a high degree of subjectivity, and therefore requires significant judgement by management, inherent limitations in the effectiveness of the design of controls may lead the auditor to focus more on substantive procedures than on testing the operating effectiveness of controls.

176. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

177. Existing footnote 49 in paragraph A104 is amended to read as follows:

See ASA 315, paragraph ~~8~~16.

178. Existing footnote 58 in paragraph A137 is amended to read as follows:

See also ASA 315, paragraph ~~31~~37.

179. Existing footnote 65 in paragraph A149 is amended to read as follows:

See ASA 315, paragraphs ~~32~~38 and ~~A152–A155~~A237–A241.

Amendments to ASA 550

180. Existing footnote 7 in paragraph 11 is amended to read as follows:

See ASA 315, paragraph ~~5~~13; and ASA 240, paragraph ~~16~~17.

181. Existing footnote 8 in paragraph 12 is amended to read as follows:

See ASA 315, paragraph ~~10~~17; and ASA 240, paragraph ~~15~~16.

182. Existing footnote 9 in paragraph 18 is amended to read as follows:

See ASA 315, paragraph ~~25~~28.

183. Existing footnote 18 in paragraph A7 is amended to read as follows:

See ASA 315, paragraphs ~~A26-A27~~A68-A70, which provide guidance regarding the nature of a special-purpose entity.

184. Existing paragraph A9 is amended to read as follows:

Matters that may be addressed in the discussion among the engagement team include:

…

- The importance that management and those charged with governance attach to the identification, appropriate accounting for, and disclosure of related party relationships and transactions (if the applicable financial reporting framework establishes related party requirements), and the related risk of management override of ~~relevant~~ controls.

185. Existing paragraph A12 is amended to read as follows:

However, where the framework does not establish related party requirements, the entity may not have such information systems in place. Under such circumstances, it is possible that management may not be aware of the existence of all related parties. Nevertheless, the requirement to make the enquiries specified by paragraph 13 still applies because management may be aware of parties that meet the related party definition set out in this ASA. In such a case, however, the auditor's enquiries regarding the identity of the entity's related parties are likely to form part of the auditor's risk assessment procedures and related activities performed in accordance with ASA 315to obtain information regarding the entity's organisational structure, ownership, governance and business model.~~:~~

- ~~The entity's ownership and governance structures;~~
- ~~The types of investments that the entity is making and plans to make; and~~
- ~~The way the entity is structured and how it is financed.~~

…

186. Existing footnote 21 in paragraph A17 is amended to read as follows:

See ASA 315, paragraph ~~14~~21.

187. Existing paragraph A20 is amended to read as follows:

Controls ~~activities~~ in smaller entities are likely to be less formal and smaller entities may have no documented processes for dealing with related party relationships and transactions. An owner-manager may mitigate some of the risks arising from related party transactions, or potentially increase those risks, through active involvement in all the main aspects of the transactions. For such entities, the auditor may obtain an understanding of the related party relationships and transactions, and any controls that may exist over these, through enquiry of management combined with other procedures, such as observation of management's oversight and review activities, and inspection of available relevant documentation.

188. Existing paragraph A28 is amended to read as follows:

Relevant related party information that may be shared among the engagement team members includes, for example:

- The identity of the entity's related parties.
- The nature of the related party relationships and transactions.

Significant or complex related party relationships or transactions that may be determined to be significant risks ~~require special audit consideration~~, in particular transactions in which management or those charged with governance are financially involved.

189. Existing paragraph A34 is amended to read as follows:

Depending upon the results of the auditor's risk assessment procedures, the auditor may consider it appropriate to obtain audit evidence without testing the entity's controls over related party relationships and transactions. In some circumstances, however, it may not be possible to obtain sufficient appropriate audit evidence from substantive audit procedures alone in relation to the risks of material misstatement associated with related party relationships and transactions. For example, where intra-group transactions between the entity and its components are numerous and a significant amount of information regarding these transactions is initiated, recorded, processed or reported electronically in an integrated system, the auditor may determine that it is not possible to design effective substantive audit procedures that by themselves would reduce the risks of material misstatement associated with these transactions to an acceptably low level. In such a case, in meeting the ASA 330 requirement to obtain sufficient appropriate audit evidence as to the operating effectiveness of ~~relevant~~ controls,[26] the auditor is required to test the entity's controls over the completeness and accuracy of the recording of the related party relationships and transactions.

Amendments to ASA 570

190. Existing footnote 3 in paragraph 10 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~5~~13.

191. Existing footnote 10 in paragraph A7 is amended to read as follows:

See ASA 315, paragraph ~~31~~37.

Amendments to ASA 600

192. Existing paragraph 17 is amended to read as follows:

The auditor is required to identify and assess the risks of material misstatement through obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the system of internal control.[7] The group engagement team shall:

…

193. Existing paragraph A6 is amended to read as follows:

The group engagement team may also identify a component as likely to include significant risks of material misstatement of the group financial report due to its specific nature or circumstances. ~~(that is, risks that require special audit consideration[14]).~~ For example, a component could be responsible for foreign exchange trading and thus expose the group to a significant risk of material misstatement, even though the component is not otherwise of individual financial significance to the group.

194. Existing footnote 17 of paragraph A23 is amended to read as follows:

See ASA 315, paragraphs ~~A17–A41~~A27–A73.

195. Existing footnote 19 of paragraph A28 is amended to read as follows:

See ASA 240, paragraph ~~15~~16; and ASA 315, paragraph ~~10~~17.

196. Existing paragraph 1 of Appendix 2 is amended to read as follows:

Group-wide controls may include a combination of the following:

- Regular meetings between group and component management to discuss business developments and to review performance.

…

- Controls ~~activities~~ within an IT system that is common for all or some components.
- Controls within the group's process to monitor ~~Monitoring~~ the system of internal control~~s~~, including activities of the internal audit function and self-assessment programs.

…

197. Existing Appendix 5 is amended to read as follows:

Matters that are relevant to the planning of the work of the component auditor:

…

Matters that are relevant to the conduct of the work of the component auditor:

- The findings of the group engagement team's tests of controls ~~activities~~ of a processing system that is common for all or some components, and tests of controls to be performed by the component auditor.

…

198. As a result of the footnote deletion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

Amendments to ASA 610

199. Existing paragraph 7 is amended to read as follows:

ASA 315 addresses how the knowledge and experience of the internal audit function can inform the external auditor's understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control, and identification and assessment of risks of material misstatement. ASA 315 [3] also explains how effective communication between the internal and external auditors also creates an environment in which the external auditor can be informed of significant matters that may affect the external auditor's work.

200. Existing paragraph A3 is amended to read as follows:

In addition, those in the entity with operational and managerial duties and responsibilities outside of the internal audit function would ordinarily face threats to their objectivity that would preclude them from being treated as part of an internal audit function for the purpose of this ASA, although they may perform controls ~~activities~~ that can be tested in accordance with ASA 330.[12] For this reason, monitoring controls performed by an owner-manager would not be considered equivalent to an internal audit function.

201. Existing footnote 13 in paragraph A4 is amended to read as follows:

See ASA 315 (as amended), paragraph ~~6~~14(a).

3 See ASA 315 (as amended), paragraph ~~A116~~A118.

202. Existing paragraph A10 is amended to read as follows:

The application of a systematic and disciplined approach to planning, performing, supervising, reviewing and documenting its activities distinguishes the activities of the internal audit function from other monitoring controls ~~activities~~ that may be performed within the entity.

203. Existing paragraph A21 is amended to read as follows:

As explained in ASA 315,[22] significant risks ~~require special audit consideration~~ are risks assessed close to the upper end of the spectrum of inherent risk and therefore the external auditor's ability to use the work of the internal audit function in relation to significant risks will be restricted to procedures that involve limited judgement. In addition, where the risks of material misstatement is other than low, the use of the work of the internal audit function alone is unlikely to reduce audit risk to an acceptably low level and eliminate the need for the external auditor to perform some tests directly.

204. Existing footnote 25 in paragraph A26 is amended to read as follows:

See ASA 315 (as amended), paragraph ~~A116~~A118.

Amendments to ASA 620

205. Existing paragraph A4 is amended to read as follows:

An auditor's expert may be needed to assist the auditor in one or more of the following:

- Obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the, ~~including its~~ entity's system of internal control.

Amendments to ASA 700

206. Existing footnote 35 in paragraph A47 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement* ~~*through Understanding the Entity and Its Environment*~~, paragraph ~~4~~12(c).

Amendments to ASA 701

207. Existing paragraph A20 is amended to read as follows:

ASA 315 defines a significant risk as an identified ~~and assessed~~ risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which the inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur ~~that, in the auditor's judgement, requires special audit consideration~~.[24] Areas of significant management judgement and significant unusual transactions may often be identified as significant risks. Significant risks are therefore often areas that require significant auditor attention.

208. As a result of the footnote insertion above, subsequent footnotes of this Auditing Standard are re-numbered and references to these footnotes are updated accordingly.

209. Existing footnote 26 in paragraph A22 is amended to read as follows:

See ASA 315, paragraph ~~31~~37.

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22 See ASA 315, paragraph 12~~4~~(l)~~(e)~~

24 See ASA 315, paragraph 12(l)

Amendments to ASA 720

210. Existing paragraph A31 is amended to read as follows:

The auditor's knowledge obtained in the audit includes the auditor's understanding of the entity and its environment, the applicable financial reporting framework, and ~~including~~ the entity's system of internal control, obtained in accordance with ASA 315.[11] ASA 315 sets out the auditor's required understanding, which includes such matters as obtaining an understanding of:

(a) The entity's organisational structure, ownership and governance, and its business model, including the extent to which the business model integrates the use of IT;

(b) ~~The r~~Relevant industry, regulatory, and other external factors;

(c) The relevant measures used, internally and externally, to assess ~~measurement and review of~~ the entity's financial performance; ~~and~~

~~(e) The nature of the entity;~~

~~(f) The entity's selection and application of accounting policies;~~

~~(g) The entity's objectives and strategies;~~

211. Existing paragraph A51 is amended to read as follows:

In reading the other information, the auditor may become aware of new information that has implications for:

- The auditor's understanding of the entity and its environment, the financial reporting framework and the entity's system of internal control and, accordingly, may indicate the need to revise the auditor's risk assessment.[13]

Amendments to ASA 800

212. Existing footnote 5 in paragraph 10 is amended to read as follows:

See ASA 315 *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraph ~~11(c)~~19(b).

[11] ASA 315, *Identifying and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~*, paragraphs 19~~11~~ – 27~~12~~

[13] See ASA 315, paragraphs ~~11~~19, ~~31~~37, and ~~A1~~A11.

February 2020

Basis for Conclusions ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards*

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

Obtaining a Copy of this Basis for Conclusions

This Basis for Conclusions is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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Basis for Conclusions ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-*2 Amendments to Australian Auditing Standards* has been prepared by the Technical Staff of the Auditing and Assurance Standards Board (AUASB) to provide the background and rationale for the development and approval of the Standard by the AUASB. The Basis for Conclusions relates to, but does not form part of, ASA 315 and ASA 2020-2.

CONTENTS

BASIS FOR CONCLUSIONS

ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards*

This Basis for Conclusions has been prepared by the Technical Staff of the AUASB to provide the background and rationale for the development and approval of ASA 315 *Identifying and Assessing the Risks of Material Misstatement* and ASA 2020-2 *Amendments to Australian Auditing Standards*, by the AUASB. The Basis of Conclusions relates to, but does not form part of ASA 315 and ASA 2020-2, and is not a substitute for reading the Standards.

Background

1. In accordance with its mandates under section 227 of the *Australian Securities and Investments Commission Act 2001* and the Financial Reporting Council's *Strategic Direction,* the AUASB's policy is to adopt the International Auditing and Assurance Standards Board (IAASB) ISAs, unless there is a compelling reason not to do so. In addition the AUASB is required to make such amendments to the ISAs to ensure the Australian Auditing Standards both exhibit and conform to the Australian regulatory environment and statutory requirements. Further amendments are made where there are compelling reasons to do so, and are made with a public interest focus.

2. The IAASB issued ISA 315 (Revised 2019) *Identifying and Assessing the Risks of Material Misstatement* and conforming and consequential amendments in December 2019.

3. The IAASB's project to update ISA 315 had an overall objective to establish more robust requirements and appropriately detailed guidance to drive auditors to perform appropriate risk assessment procedures in a manner commensurate with the size and nature of the entity.

4. The IAASB released an exposure draft of proposed ISA 315 in July 2018.

5. In August 2018 the AUASB released the Australian Exposure Drafts[1] of the equivalent IAASB exposure drafts, to gather feedback from Australian stakeholders and to its submission to the IAASB on proposed ISA 315. The AUASB received comment letters from 7 stakeholders which included very detailed feedback. The AUASB held roundtables in Sydney, Melbourne, Perth, Brisbane, Hobart which were attended by over 70 stakeholders representing assurance providers from a range of audit firms, professional accounting bodies, academics, those charted with governance and preparers of financial statements. The AUASB also held two webinars.

6. Based on the feedback received the AUASB provided a submission to the IAASB on 2 November 2019 which included a number of matters which needed to be addressed in order to ensure auditors apply the identification and assessment of risks of material misstatement consistently and effectively. Refer to AUASB's full submission.

7. The AUASB has continued to monitor the development of ISA 315 to ensure that the issues included in our submission have been appropriately addressed, as well as to identify if there are any other concerns with the final ISA 315. Further details regarding the development of ISA 315 and how the IAASB addressed feedback on their exposure draft can be found in ISA 315 Basis for Conclusions on the IAASB's website.

[1] Exposure Draft 01/18: *Proposed ASA 315 Identifying and Assessing the Risks of Material Misstatement* (ED 01/18) and Exposure Draft 02/18: *Proposed ASA 2018-1 Amendments to Australian Auditing Standards (ED 02/18)*

Scope

8. This Basis for Conclusions applies to ASA 315 primarily, but is also relevant to ASA 2020-2 which contains the consequential and conforming amendments to:

   - ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*
   - ASA 210 *Agreeing the Terms of Audit Engagements*
   - ASA 230 *Audit Documentation*
   - ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*
   - ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report*
   - ASA 260 *Communication with Those Charged with Governance*
   - ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance*
   - ASA 300 *Planning an Audit of a Financial Report*
   - ASA 320 *Materiality in Planning and Performing an Audit*
   - ASA 330 *The Auditor's Responses to Assessed Risks*
   - ASA 402 *Audit Considerations to an Entity Using a Service Organisation*
   - ASA 500 *Audit Evidence*
   - ASA 501 *Audit Evidence – Special Considerations for Inventory and Segment Information*
   - ASA 505 *External Confirmations*
   - ASA 520 *Analytical Procedures*
   - ASA 530 *Audit Sampling*
   - ASA 540 *Auditing Accounting Estimates and Related Disclosures*
   - ASA 550 *Related Parties*
   - ASA 570 *Going Concern*
   - ASA 600 *Special Considerations – Audits of a Group Financial Report*
   - ASA 610 *Using the Work of Internal Auditors*
   - ASA 620 *Using the Work of an Auditor's Expert*
   - ASA 700 *Forming an Opinion and Reporting on a Financial Report*
   - ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*
   - ASA 720 *The Auditor's Responsibilities Relating to Other Information*
   - ASA 800 *Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks*

Major Issues raised by Respondents on Exposure

9. The adoption of international standards and any changes to adopted standards are governed by the AUASB's policies regarding convergence with IAASB standards and harmonisation with the standards of the New Zealand Auditing and Assurance Standards Board. The policies and procedures incorporate "compelling reasons" tests which must be used to support changes to the international standards (refer paragraph 1).

10. The AUASB received very detailed feedback from respondents on ED 01/18 with the major issues included in the submission to the IAASB relating to:

    - the overall length and complexity of the standard;
    - the introduction of many new concepts and definitions, and the actual definitions;
    - order and circularity of the requirements;
    - insufficient detail on the considerations of risk of IT and the use of automated tools and techniques; and
    - that the standard will not be sufficiently scalable to audits of entities across different market segments and industries, in particular audits of small and medium entities.

    The AUASB included these issues in its submission to the IAASB.

11. In considering ASA 315 the AUASB determined that the significant matters raised in its submission to the IAASB, as well as those identified through review of subsequent drafts of the standard, have been addressed in the final standard (ISA 315). The AUASB acknowledged that ASA 315 is still long and complex, and there are potentially a number of challenging implementation issues, however concluded there were no Australian compelling reason amendments to make to the international equivalent version of the standard.

12. The IAASB has committed to providing tools, guidance and developing a webinar to assist practitioners with adoption of ISA 315. The AUASB will monitor this to consider if further implementation support is required to address implementation issues.

13. The IAASB have made extensive changes to ISA 315 since their exposure draft, however considered that the amendments were in response to submissions received, and the fundamental approach and principles on which the standard is based have not changed. Accordingly the IAASB voted that it was not necessary to re-expose the standard.

14. Refer to Appendix 1 which details all major feedback received from Australian stakeholders which were included in the AUASB's submission to the IAASB and how they have been addressed. Further detail on the how the IAASB have addressed comments on their exposure draft is included in the IAASB's Basis for Conclusion.

Conclusion

15. The AUASB voted to approve and issue ASA 315 on 4 February 2020.

16. The AUASB also considered if ASA 315 should be re-exposed. Two AUASB members supported re-exposure based on concerns about the volume of change since ASA 315 was originally exposed in 2018, however with two-thirds of AUASB members required to approve this resolution the motion was not supported and ASA 315 was not re-exposed by the AUASB.

17. In reaching its conclusions the AUASB considered:

    - all stakeholder feedback;

- the IAASB's due process and consideration as to whether ISA 315 should be re-exposed.

* * *

Appendix 1

HOW MORE SIGNIFICANT ISSUES RAISED IN THE AUASB SUBMISSION TO THE IAASB HAVE BEEN ADDRESSED

Issue	**How addressed**
<u>Complexity and length of standard</u> • The increased length of ED 315 is a potential barrier to its understandability and consistent application. • Consider drafting standards for less complex entities, then adding application or guidance for more complex entities. • The introduction of many new definitions and concepts, or the distinction between concepts, add complexity to the standard. • Reassess whether some content currently in the application material of ED 315 should instead be included in other non-authoritative guidance.	The IAASB have addressed by: • simplifying requirements into "what" and reducing the number by removing set up or sign post requirements; • simplifying definitions and concepts; • application material now includes "why" and "how" and has been restructured; and • more examples in the application material which are in "boxes" to clearly identify them. However overall the standard is still long and complex however the AUASB did not consider a compelling reason adjustment. Refer to IAASB's Basis for Conclusion, page 8 for more detail.
<u>Definitions</u> "Significant classes of transactions, account balances and disclosures" and "relevant assertions". Specifically, the term "more than remote" in the definition of relevant assertion is fundamentally different to "a reasonable possibility", and this revised definition may result in more significant classes of transactions, account balances, or disclosures being identified than was intended.	The term "more than remote" has been removed from definition of relevant assertion which is now "An assertion about a class of transactions, account balance or disclosure is relevant when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of controls" The threshold for the identification of a possible ROMM has been added to ISA 200 (paragraph A3) and a reference from Identifying ROMM (Para 28) has been linked to paragraph A186 in ASA 315. Threshold is: The identification of risks of material misstatement is performed before consideration of any related controls (ie. inherent risk), and is based on the auditor's preliminary consideration of misstatements that have a reasonable possibility of both occurring, and being material if they were to occur. Refer to IAASB's Basis for Conclusion page 22 - 23.

Issue	**How addressed**
Definition of significant risk and the spectrum of inherent risk • More detail required on the spectrum of inherent risk i.e. how to assess where on the spectrum a risk resides • Definition of significant risk should be "likelihood and magnitude" as opposed to the current "likelihood or magnitude". • The definition of significant risk should be amended to those "at the upper end of the spectrum of inherent risk" and not "close to the upper end of the spectrum of inherent risk".	The definition of significant risk still includes at the upper end of the spectrum of inherent risk, and application material has been enhanced (A208-214) to assist with concepts. Likelihood or magnitude has been changed to "and". Refer to IAASB's Basis for Conclusion page 23 – 24.
Inherent risk factors (IRF) • Supportive of the concepts and definition. But consider it is overly complicated by having a requirement to explicitly take into account IRF. • Insufficient clarity in how to apply the concepts and definitions of the IRF and the current proposed definition of significant risk. • Inclusion of quantitative is potentially problematic.	IRF still in requirements and the related application material has been enhanced. Appendix 2 Understanding the IRF has been developed to assist. Refer to IAASB's Basis for Conclusion page 19.
Scalability • Overall concern ED 315 is not scalable to smaller and medium entities. • Terminology used in ED 315 should refer to "less complex entities". • Recommend guidance and examples be included in the application material of the proposed standard on how to effectively scale the work effort in ED 315 to less complex entities, such as examples of: how to perform risk identification and assessment procedures for a less complex entity where a mainly substantive audit approach will be adopted; and how to perform risk identification and assessment procedures when the entity's system of internal control may be less detailed and formalised.	Efforts on improving the understandability of the standard should assist with scalability. Application and other Explanatory material includes separate "Scalability paragraphs" and where appropriate includes contrasting examples (i.e. illustrating both sides of the complexity spectrum). Refer IAASB's Basis for Conclusion page 10-11.

Issue	**How addressed**

<u>*Automated tools and techniques*</u>
• Agree with the approach taken of using examples to illustrate how automated tools and techniques may be used in risk assessment.
• ED 315 could be further enhanced by addressing:
    o How automated tools and techniques may be used for risk assessment, and how they meet or impact the requirements of ED 315. This is to avoid automated tools and techniques being applied in addition to the current requirements.
    o What are the requirements in relation to understanding and/or obtaining evidence over the reliability of underlying data (information produced by the entity) used within automated tools and techniques that are used for risk assessment (including the nature, timing and extent of testing).
    o Risk factors relating to the use of big data and automated analytics technology.
	ASA 315 includes dedicated paragraphs on how “automated tools and techniques” may be used.
	
	Implementation guidance to include questions and answers on the use of automated tools and techniques.
	
	Refer IAASB’s Basis for Conclusion page 13 - 14

<u>*Professional scepticism*</u> • Supportive of the principle of obtaining an appropriate base of evidence for risk assessment, however we do not support using the term “sufficient appropriate audit evidence” in a risk assessment process.	Matter addressed through changing the requirement to obtain “evidence to provide an appropriate basis for the identification and assessment of ROMM”. Refer IAASB’s Basis for Conclusion page 14-15.

Issue	**How addressed**
Internal controls • It is not sufficiently clear how controls including the understanding obtained over the system of internal control, impact the identification of risks of material misstatement. • Clarify the design and implementation testing required verses gaining an understanding. • More guidance on which controls reside in the Information System and Communication component as distinct from the Control Activities component, and the difference, if any, on the requirements in relation to the audit procedures to be performed on these controls. • Controls relevant to the audit – clarify the intention of 39(e). • Some of our stakeholders have expressed concern that for some less complex entities the controls over journals may not be documented and are difficult to test.	The understanding of internal controls has been redrafted to address feedback. The IAASB have presented the required understanding and evaluation for each component of the system of internal control in a new tabular format with the intention to help with understandability. Further changes have been made to address matters. Refer IAASB's Basis for Conclusion page 16 – 19 for more detail
Information Technology • Support the introduction of the new IT-related concepts and definitions. • Could be enhanced by including the risk factors relating to current and evolving technology which connect to organizational networks, such as infrastructure / software as a service solutions, wireless networks, blockchain, and other technology devices that connect to organisational networks.	Changes have been made to better reflect the interrelationship of the concepts of the IT environment, risks arising from the use of IT, and general IT controls. Refer IAASB's Basis for Conclusion page 18

Issue	**How addressed**
<u>*Separate inherent and control risk assessment*</u> • Support the separate assessments of inherent and control risk at the assertion level. • Support assessing control risk at maximum if not testing operating effectiveness. • The current use of the singular term ("risks of material misstatement") both before and after the separate assessment of inherent risk and control risk is confusing. • Provide additional detail on how to assess control risk at various levels of the spectrum of risk. • Describing in greater granularity in ED 315 the process the auditor undertakes to combine their separate inherent and control risk assessments.	ASA 315 includes more detail on how to separately assess inherent and control risk. Refer IAASB's Basis for Conclusion pages 22 – 24.
<u>*Stand-back provision and ISA 330 para 18*</u> • Supportive of a stand-back in 315 but don't need both • Reconsider if the terms "quantitatively and qualitatively" are necessary in ISA 315	The stand back provision retained in both ASA 315 and ASA 330. The references to qualitative and quantitative in the context of materiality have removed. Refer IAASB's Basis for Conclusion page 24.

ISA 315 (Revised 2019) Implementation Plan

At December 2019

	Timing	Format
First Time Implementation Guide Highlighting significant changes in the revised standard from extant ISA 315 (Revised)	First Quarter 2020	Published document
Fact Sheets • Overall summary of the revised standard • Understanding the Entity and Its Environment • Understanding the Entity's System of Internal Control • Control Activities • Information Technology • Identifying and Assessing the Risks of Material Misstatement • Documentation • "Why" Procedures Within ISA 315 (Revised 2019) are Required	First quarter 2020	Published documents – to include flowcharts where relevant
Staff Publication – Questions and Answers	First quarter 2020	Published documents relating to matters not addressed in the First Time Implementation Guide or the Fact Sheets
Webinar- Explaining the Significant Changes in ISA 315 (Revised (2019)	First quarter 2020	Webinar

	Timing	Format
Focused Education Sessions	March – June 2020	1 – 1.5 days presentation (by members of the ISA 315 Task Force and IAASB Staff), and audience discussion relating to the changes that have been made to the revised standard. These sessions will be targeted at representatives from national standard setters, regulators and audit oversight bodies, software providers involved in making changes to audit software/methodologies and member bodies (as appropriate) in the following locations:[1] • Europe • Asia Pacific • Africa • South America • North America

[1] Further information as to the exact location and the dates for each session will be confirmed in early 2020.

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**4**
Meeting Date:	3 March 2020
Subject:	GS 005 *Evaluating the Appropriateness of a Management's Expert's Work*
Date Prepared:	21 February 2020

X **Action Required** ☐ **For Information Purposes Only**

A. Agenda Item Objectives

1. For the AUASB Technical Group (ATG) to update the AUASB on the outreach done on; and changes made to GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* since the December 2019 AUASB meeting.

2. For the AUASB to vote on the issuance of Revised GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* (GS 005).

B. Background and Due Process

3. At the 4/5 December 2018 AUASB meeting, the AUASB approved the project plan for an update to GS 005.

4. The audit technical group (ATG) established a project advisory group to provide input into the revision to GS 005. The PAG held 2 teleconferences with multiple email correspondence to progress the revision of GS 005.

5. At the 13 June 2019, 11 September 2019 and 4 December 2019 AUASB meetings, the ATG provided the AUASB with a project update and draft revisions to GS 005.

6. The December 2019 draft of the revised GS 005 was circulated to the Canadian and New Zealand Audit and Assurance Standards Boards for an opportunity to provide input and commentary. Both bodies provided commentary and feedback which was incorporated in a revised draft re-circulated to the AUASB during the December 2019 AUASB meeting.

7. Both at the December 2019 AUASB meeting and following the December 2019 AUASB meeting, the ATG received commentary from AUASB members (including the AUASB Chair). All feedback has been worked through the GS 005 PAG Chair and the AUASB Chair. Feedback has been incorporated into the March 2020 Draft GS 005 presented at Agenda Item 4.1.

8. The AUASB Chair and staff have met multiple times with ASIC and have kept ASIC up to date with the progress, inputs into and outcomes of this revision. The ATG have provided ASIC with the draft GS 005 at multiple stages throughout the project. In February 2020, the ATG received ASIC staff

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level fatal flaw comments on the latest draft of GS 005. ASIC staff feedback has been incorporated into the draft GS 005 at Agenda Item 4.1. The ATG will take the AUASB through the ASIC feedback at the 3 March 2020 AUASB meeting.

C. Main areas of change since December 2019 AUASB meeting papers (paragraph references are to Agenda Item 4.2 – clean version)

9. Title – The ATG is suggesting the title – *Evaluating the Appropriateness of a Management's Expert's Work.* The ATG considers that this title best aligns with the language of ASA 500 paragraph 8 and represents the substance of the content of GS 005.

10. Upfront Differential between the work of management verses the work of a management's expert with examples of the differences provided – refer paragraphs 5, 6, 16 and 17.

11. Further clarification how an auditor can obtain industry knowledge, but still needs to consider the need for an auditor's expert – refer paragraphs 11 and 12.

12. Upfront considerations regarding the importance of understanding the content of the management's expert's report and the need for that report to be sufficiently detailed – refer paragraphs 19 and 20.

13. Clarification of the position where an expert may lack objectivity and or competency/capability and what that may mean for the auditor, conversely what it means where the auditor has assessed the management's expert as having strong objectivity, competency and capability – refer paragraph 26.

14. Additional consideration of competency now includes understanding the accuracy of prior period estimates made by that management's expert. This was in the draft guidance statement as circulated in December, but not under the section of competency, rather it was under the section 'The Findings and Conclusions of the Management's Expert' – refer paragraph 28.

15. Clarification of the auditor's work effort where a management's expert may have tested source data – refer paragraph 52.

16. Moved the section headed 'The Findings and Conclusions of the Management's Expert' below the section on 'Methods, Assumptions and Source Data' – the ATG considers this to be a more appropriate placement.

D. AUASB Technical Group Recommendation

17. For the AUASB to approve the issuance of GS 005 *Evaluating the Appropriateness of a Management's Expert's Work*

<u>Material Presented</u>

Agenda Item 4.0	AUASB Board Meeting Summary Paper
Agenda Item 4.1	GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* – Marked-Up Draft (mark-up from December 2019 AUASB meeting)
Agenda Item 4.2	GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* – Clean

Action Required

No.	Action Item	Responsibility	Due Date
1.	AUASB to approve the issuance of GS 005.	AUASB	3 March 2020

VERSION: MARK-UP SINCE RE-PRESENTED TO AUASB IN DECEMBER

GS 005
(date)

Guidance Statement GS 005
Evaluating the Appropriateness of a Management's Expert's Work

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 Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

CONTENTS

AUTHORITY STATEMENT

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 005 *Evaluating the Appropriateness of a Management's Expert's Work*. pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

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

This Guidance Statement does not prescribe or create new requirements.

Dated:

R Simnett AO
Chair - AUASB

GUIDANCE STATEMENT GS 005

Evaluating the Appropriateness of a Management's Expert's Work

Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors when using the work of a management's expert as audit evidence in relation to:

   (a) the audit of a financial report, in accordance with the *Corporations Act 2001*;

   (b) the audit of a financial report[1]~~, or a complete set of financial statements~~ for any other purpose; and

   (c) the audit of other historical financial information.

2. This Guidance Statement provides guidance that may be considered and adapted as necessary in the circumstances, to non-historical information assurance engagements but is not a substitute for referring to the requirements and application material contained in ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information.*

Issuance Date

3. This Guidance Statement is issued on 16 March 2015 by the AUASB and replaces GS 005 *Using the Work of a Management's Expert*~~*Using the Work of a Management's Expert*~~, issued in March 2015.

Introduction

4. This Guidance Statement has been developed to provide guidance on:

   (a) the circumstances under which a management's expert may be used and the nature of that work;

   (b) the auditor's considerations in determining ~~the extent to which the~~whether to use the work of a management's expert ~~is used~~ as audit evidence in carrying out the responsibilities of the auditor with respect to an entity's financial report or other historical financial information; and

   (c) the auditor's considerations in determining the information to be used as audit evidence.

Scope of this Guidance Statement

Management or Management's Expert

5. Where the necessary information to prepare the financial report and/or historical financial information is produced by management, ASA 330[2] requires the auditor to design and perform audit procedures whose nature, timing and extent are based on and are responsive to the risk of material misstatement at the assertion level as identified and assessed by the auditor in accordance with ASA 315[3].

[1] For purposes of this Guidance Statement, where the term financial report is used, this includes reference to a complete set of financial statements for any other purpose.

[2] ASA 330, *The Auditor's Responses to Assessed Risks*, paragraph 6.

[3] ASA 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

~~5.~~6. Where the necessary information to prepare the financial report and/or historical financial information is produced by a management's expert, ASA 500~~[4]~~ *Audit Evidence*[5], establishes mandatory requirements and provides application and explanatory material on using the work of a management's expert as audit evidence. This Guidance Statement is to be read in conjunction with ASA 500. Examples of the use of management's experts are included in paragraphs 16 to 18 of this Guidance Statement.

~~6.~~7. ASA 500[6], also establishes mandatory requirements and provides application and explanatory material on information obtained from an external information source. This Guidance Statement does not provide guidance on information obtained from an external information source.

~~7.~~8. This ~~guidance~~ Guidance Statement applies ~~equally~~ to the use of a management's expert's work irrespective of whether they are internal or external to an entity, but does not deal with the use of experts that are not engaged or employed by management.

The work of a management's expert is often associated with accounting estimates; accordingly, this Guidance Statement should be read in conjunction with ASA 540 Auditing Accounting Estimates and Related Disclosures[7].

9.

~~Interaction with~~Considerations in Using the Work of an Auditor's Expert

~~8.~~10. It is the responsibility of the engagement partner[8] to determine that the engagement team has the appropriate competence and capabilities, including sufficient time, to perform an audit engagement in accordance with the Australian Auditing Standards, relevant ethical requirements, and applicable legal and regulatory requirements. When management uses the work of a management's expert to assist the entity in preparing the financial report, the auditor determines whether the involvement of an auditor's expert is required.

~~9.~~11. There is no requirement for the auditor to use an auditor's expert to ~~assess~~ evaluate the work performed by a management's expert, however, if ~~expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence~~management uses a management's expert, the auditor determines whether to use the work of an auditor's expert[9]. An auditor who is not an expert in a ~~relevant~~ field other than accounting or auditing may be able to obtain a sufficient understanding of that field to perform the audit without the use of an auditor's expert. Ways in which this understanding may be obtained include:

(a) Experience in auditing entities that require such expertise, for example, an auditor who has not audited in the extractive industry may not have the same level of knowledge and understanding as an auditor who works extensively in this industry;

(b) Education or professional development in the particular field which may include formal courses;

(c) Discussion with individuals possessing expertise in the relevant field for the purpose of enhancing the auditor's own competence to deal with matters in that field;

(d) Discussion with auditors who have performed engagements in the same or similar industries with the same or similar use of experts for the preparation of a financial ~~statements~~report.

~~4 ASA 500, paragraph 8.~~
5 ASA 500, paragraph 8.
6 ASA 500, paragraph 7.
7 ASA 540 paragraph 30.
8 ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information*, paragraph 14.
9 ASA 620 *Using the Work of an Auditor's Expert*, paragraph 7.

While an auditor may have obtained knowledge of a field as described in paragraph 11 of this Guidance Statement, t

~~10.~~12. ~~T~~he auditor's decision on whether to use an auditor's expert may still be influenced by factors included in ASA 620[10] as well as~~such as~~:

(a) The nature and significance of the matter, including its complexity;

(b) The risks of material misstatement;

(c) The expected nature of procedures to respond to the identified risks, including:

(i) the auditor's knowledge and experience with the work of experts in relation to such matters; and

(ii) the availability and extent of alternative sources of audit evidence;

(d) The extent to which management has used a management's expert; and~~.~~

(e) The management expert's competence, capabilities and objectivity.

13. This Guidance Statement does not provide guidance on the auditor's use of the work of an auditor's expert. ASA 620 *Using the Work of an Auditor's Expert* establishes mandatory requirements and provides ~~explanatory guidance~~application and other explanatory material on using the work of an auditor's expert as audit evidence.

Definitions

~~11.~~14. For the purposes of this Guidance Statement the following items have the meanings attributed in the Australian Auditing Standards and reproduced below:

(a) Expertise means skills, knowledge and experience in a particular field[11].

(b) External information source~~[12]~~ means an~~d~~ external individual or organisation that provides information that has been used by the entity in preparing the financial report, or that has been obtained by the auditor as audit evidence, when such information is suitable for a use by a broad range of users. When information has been provided by an individual or organisation acting in the capacity of a management's expert, that individual or organisation is not considered an external information source with respect to that particular information[13].

~~(b)~~(c) Management's expert means an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial report or other historical financial information[14].

~~(c)~~(a) ~~External information source[15] means and external individual or organisation that provides information that has been used by the entity in preparing the financial report, or that has been obtained by the auditor as audit evidence, when such information is suitable for a use by a broad range of users. When information has been provided by an individual or organisation acting in the capacity of a management's expert, that~~

10 ASA 620, paragraph A9.
11 ASA 620, paragraph 6(b).
~~12 ASA 500 paragraph 5(d)~~
13 ASA 500, paragraph 5(d).
14 ASA 500, paragraph 5(e).
~~15 ASA 500 paragraph 5(d)~~

~~individual or organisation is not considered an external information source with respect to that particular information.~~

The Auditor's Responsibility for the Conclusion

~~12.~~15. The auditor has sole responsibility for the audit opinion expressed and that responsibility is not reduced by the auditor's use of the work of a management's expert ~~("expert")~~.

~~13.~~ Examples of the use of Management's Experts

~~14.~~16. The preparation and presentation of a financial report and/or other historical financial information of an entity is the responsibility of management and those charged with governance. Determination of amounts included in the financial report and/or other historical financial information may require expertise in a field other than accounting or auditing, such expertise may be obtained by management using a management's expert.

~~15.~~17. An individual may possess expertise in accounting or auditing, as well as expertise in a field other than accounting or auditing (for example an actuary may also be an accountant). In these circumstances the determination of whether that individual is a management's expert depends on the nature of the work performed. For example, an individual with expertise in applying methods of accounting for deferred income tax can often be easily distinguished from an expert in taxation law. The former is not a management's expert for the purposes of this Guidance Statement as this constitutes accounting expertise; the latter is an expert for the purposes of this Guidance Statement as this constitutes legal expertise. Similar distinctions may also be able to be made in other areas, for example:

(a) between expertise in methods of accounting for financial instruments, and expertise in complex modelling for the purpose of valuing financial instruments, the former is not considered to be a management's expert as this constitutes accounting ~~experience~~expertise;

(b) an entity's internal expertise in IT controls is not considered to be a management's expert as management is responsible for the design and implementation of controls that is integral to the functioning of the financial reporting system and preparation of the financial report.

~~16.~~18. Management may engage or employ experts (this may include but is not limited to actuaries, valuers, engineers, environmental consultants, geologists, scientists, health practitioners, taxation specialists, legal advisors and other industry specialists) to obtain the necessary information to prepare the financial report and/or historical financial information. Examples of such expertise include:

(a) Valuation (for example, high-technology materials or equipment, complex financial instruments, land and buildings, intangibles, investments and environmental liabilities);

(b) Determination of physical characteristics relating to quantity on hand or condition (for example, quantity or condition of minerals, mineral reserves, or raw materials stored in stockpiles);

(c) Determination of amounts derived by using specialised techniques or methods (for example, actuarial calculations of liabilities associated with insurance contracts or employee benefit plans); ~~and~~

(d) Interpretation of technical requirements of contract, laws and regulations. This may be done in some cases by those possessing legal expertise. ASA 502 *Audit Evidence – Specific Considerations for Litigation and Claims* establishes requirements and provides application and other explanatory material regarding considerations by an auditor in obtaining sufficient appropriate audit evidence relating to litigation and claims. The requirement in ASA 502 is for the auditor to consider the applicable requirements and guidance on using the work of an expert contained in ASA 500 before using the work of on in-house or external legal counsel as audit evidence.

Considerations in Determining Whether to Use ~~to~~ the Work of a Management's Expert

~~17.~~19. The auditor's decision on whether to use the work of a management's expert as audit evidence may be influenced by:

(a) the nature and significance of the matter, including its complexity;

(b) the risks of material misstatement in the matter; ~~and~~

(c) the ~~expected~~ nature, timing and extent of procedures to respond to the identified risks, including the auditor's knowledge of, and experience with, the work of the management's experts in relation to such matters and the availability of alternative sources of audit evidence; and~~.~~

(d) the content of the management's expert's report and whether that expert has agreed for the auditor to access their work papers. An understanding of the nature, timing and extent of procedures performed is essential for the auditor to understand the management expert's conclusions. The management expert's report may:

(i) need to be written in sufficient detail that will allow the auditor to understand the nature, timing and extent of work performed by that expert;

(ii) not involve all the management's expert's detailed working papers.

20. Understanding of the content of the management's expert's report as well as determining whether the auditor may access that expert's workpapers (where considered necessary by the auditor), may need to be considered early on in the planning stages of the audit engagement and agreed in the terms of the engagement between the entity and the management expert.

21. When determining the nature, timing and extent of audit procedures in relation to the work of the management's expert, the auditor makes reference to the requirements, application and other explanatory material ~~and guidance~~ contained in ASA 500[16].

~~18.~~

Considerations in Determining the Information to Be Used as Audit Evidence

~~19.~~22. ASA 500[17] requires that if information to be used as audit evidence has been prepared using the work of a management's expert, the auditor, to the extent necessary and having regard to the significance of that expert's work for the auditor's purposes:

(a) Evaluates the competence, capabilities and objectivity of that expert (Ref: Para. 24-36);

(b) Obtains an understanding of the work of that expert (Ref: Para. 37-40); and

(c) Evaluates the appropriateness of that expert's work as audit evidence for the relevant assertion (Ref: Para. 41-59).

16 ASA 500, paragraph 8.
17 ASA 500, paragraph 8.

~~20.~~23. In relation to the work of a management's expert, the auditor obtains more persuasive audit evidence the higher the auditor's assessment of risk[18]. The auditor may also consider obtaining more persuasive evidence as:

(a) the significance of ~~the management's~~that expert's work on the financial statements increases;

(b) the ability of the company to affect the management's expert's judgements increases;

(c) the level of ~~knowledge, skill and ability~~competency and capability possessed by the management expert decreases.

~~Generally, the required audit effort when evaluating the work of a management's expert is the greatest when the risk of material misstatement is high, the management's expert's work is significant to the auditor's conclusions, the management's expert has lower levels of knowledge, skill and ability; and the company has the ability to significantly influence the management's expert's judgements.~~

Competence, Capabilities and Objectivity of a Management's Expert

~~21.~~24. The auditor makes reference to the requirements, application and other explanatory material contained in ASA 500 and evaluates whether the management's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. This is ordinarily performed as part of the audit planning and risk assessment process, the timing of which may be restricted by management's process for planning and selecting management's experts.

~~22.~~25. Competence, capability and objectivity of a management's expert impacts the degree of reliability of ~~the management's~~that expert's work as audit evidence, that is, the extent to which the management's expert's work could provide persuasive audit evidence.

26. When the management's expert has been evaluated by the auditor as having lower levels of competency and capability; and/or the company has the ability to significantly influence the management's expert's judgements, the auditor may consider not using that expert's work as audit evidence. In such circumstances the auditor may consider:

(a) suggesting to management to engage a different management's expert;

(b) determining the need for an auditor's expert; or

(c) changing the nature and extent of other audit procedures.

When the management's expert has been evaluated by the auditor as having higher levels of objectivity, competency and capability, this evaluation is not a substitute for evaluating the appropriateness of that expert's work as audit evidence as required by ASA 500[19].

~~23.~~27. The nature and extent of procedures to evaluate the management's expert's competence, capability and objectivity depends on the significance of ~~the management's~~that expert's work to the auditor's conclusion regarding the relevant assertion and the risk of material misstatement of the relevant assertion. As the significance of the management's expert's work and risk of material misstatement increases, the persuasiveness of the evidence the auditor obtains for this evaluation also increases.

[18] ASA 330 *The Auditor's Responses to Assessed Risks*, paragraph 7(b).
[19] ASA 500, paragraph 8(c).

Competence

~~24.~~28. Competence relates to the nature and level of expertise of the management's expert. The auditor uses professional judgement when determining the competency of a management's expert. When ~~assessing~~ evaluating competence, the auditor may consider the guidance included in ASA 500[20] as well as:

(a) The management's expert's experience in the type of work performed, including applicable areas of speciality within the expert's field;

(b) The reputation and standing of the management's expert, including:

(i) Previous experience of the auditor with the work of that~~the~~ expert;

(ii) Enquiring of other practitioners who have used that ~~management's~~ expert or others working in the same industry;

(c) Understanding the accuracy of prior period estimates made by the management's expert. Where the auditor determines that past estimates have not been sufficiently accurate, the auditor may consider obtaining an understanding of the reasons for the inaccuracy and furthering audit procedures as appropriate to the circumstances;

(d) The professional certification, license or professional accreditation of the management's expert. Experts ~~may~~ in a specific field commonly have professional obligations under their professional or industry bodies. These obligations vary significantly and are determined by the professional or industry body[21]. The auditor's confidence when ~~assessing~~ evaluating the competency of the management's expert may increase with that expert's membership of professional or industry bodies that:

(i) Require professional qualification or accreditation;

(ii) Subject their members to regulatory requirements/guidance;

(iii) Subject their members to a specific set of standards or guidance on the expert's services;

(iv) Require continuous professional development; and

(v) Require professional obligations to be followed by their members.

~~25.~~29. The auditor's evaluation of the management expert's competence may be influenced by the management's expert's work environment, for example ~~the~~ that expert's internal quality control policies and procedures.

Capability

~~26.~~30. Capability relates to the ability of the management's expert to exercise their competency in the circumstances. When evaluating capability, the auditor may consider the guidance included in ASA 500[22] as well as:

(a) Geographic location;

(b) Availability of time;

20 ASA 500, paragraph ~~A49~~A48-A51.

21 For example actuaries are governed by the Institute of Actuaries of Australia, an actuary's specific responsibilities in relation to data are set out in the *Actuarial Code of Professional Conduct*, *Actuarial Professional Standards* and where relevant other regulatory and legislative requirements, *APRA Prudential Standards* and the *Life Insurance Act 1995*.

22 ASA 500, paragraph A48-A51.

(c) Availability of resources;

(d) Instructions on scope provided by management.

Objectivity

~~27.~~31. Objectivity relates to the possible effects that bias, conflict of interest, or the influence of others may have on the professional or business judgement of the management's expert. When ~~assessing~~ evaluating objectivity, the auditor may consider the guidance included in ASA 500[23] as well as:

(a) circumstances that threaten the objectivity of the management's expert; and

(b) whether appropriate safeguards are in place to eliminate those threats or reduce them to an acceptable level.

~~28.~~32. ASA 500 indicates that evidence from external sources is generally more reliable than that generated internally. The auditor may ~~assess~~ evaluate the relationship to the company of the management's expert, specifically, whether circumstances exist that give the company the ability to significantly affect the management's expert's judgements about the work performed, conclusions or findings. The existence of a relationship between the management's expert and the entity being audited may impair ~~the management's~~that expert's ability to be objective. The risk that the objectivity of a management's expert will be impaired increases when the management's expert is employed by the entity or is related in some way to the entity. Where a management's expert is employed by the entity, the auditor needs to consider whether there are any mitigating factors such as professional and/or statutory obligations governing the work of ~~the management's~~that expert that would impact on the objectivity of the management's expert.

~~29.~~33. Circumstances which may threaten the objectivity of the management's expert may include: advocacy threats, familiarity threats, self-review threats and self-interest threats[24]. Examples include economic dependency of the management's expert on the entity and contingency based fee arrangements.

~~30.~~34. The evaluation of the significance of threats to objectivity and of whether there is a need for safeguards may depend upon the role of the management's expert and the significance of that~~the~~ expert's work in the context of the audit. There may be safeguards specific to the audit engagement, however there may be circumstances where safeguards cannot reduce threats to an acceptable level[25].

~~31.~~35. When the management's expert is an employee of the entity, mitigating factors which enhance the ability of the management's expert to be objective, and therefore are safeguards for the lack of independence may include:

(a) Adherence to the professional standards issued by the expert's regulating body.

(b) Formal appointment of the management's expert by those charged with governance and direct access to those charged with governance by that expert.

Ordinarily, the basis on which the management's expert is remunerated ~~and or~~and/or incentives offered as part of that remuneration are considered by the auditor when ~~assessing~~ evaluating the management's expert's objectivity.

Consideration of the above may also be relevant in evaluating the objectivity of a management's expert that is external to the entity.

[23] ASA 500, paragraph A48-A54.
[24] ASA 500, paragraph A52.
[25] ASA 620, paragraph A19.

Overall Evaluation of Competence, capability and objectivity of a management's expert

~~32.~~36. If the auditor is concerned with the competence, capability or objectivity of the management's expert, the auditor may ~~consider~~ decide to communicate~~ing~~ any concerns with management and if appropriate those charged with governance and consider~~s~~ whether sufficient appropriate audit evidence can be obtained concerning the work of the management's expert. If sufficient appropriate audit evidence cannot be obtained concerning the work of the management's expert, t~~T~~he auditor may undertake alternative procedures or seek audit evidence from another expert including an auditor's expert.

Obtaining an Understanding of the Work of a Management's Expert

~~33.~~37. The auditor makes reference to the requirements, application and other explanatory material in ASA 500 when obtaining an understanding of the management's expert's work to ~~assess~~ evaluate whether it is ~~adequate~~ appropriate for the purposes of the audit.

~~34.~~38. When obtaining an understanding of the management's expert's work, the auditor, having regard to whether the management's expert is internal or external to the entity, ~~considers~~may consider:

(a) The terms of the engagement between the entity and the management expert, including understanding the nature, timing and extent of work to be performed by the management's expert and the form of any report to be provided by that expert;

(b) Whether the auditor has any prior knowledge of the management's expert's field of expertise, or with that expert;

(c) The economic and competitive conditions impacting the entity and its operating results;

(d) Whether there is evidence of undue management pressure on the management's expert;

(e) The existence of controls within the entity over the work of the management's expert (for example whether there are procedures in place to challenge or review ~~the~~ that expert's work, such as review by those charged with governance) or controls over the source data used in that~~the~~ expert's assessment;

(f) Whether management has authorised their expert to discuss their findings or conclusions with the auditor[26];

(g) Whether the management's expert has consented to the auditor's intended use of their findings; and

(h) Whether the management's expert has agreed for the auditor to access their work papers (review of the expert's work papers is not normally required other than as considered necessary by the auditor using their professional judgement).

~~35.~~39. Where management has not consented for their expert to discuss their findings or conclusions with the auditor, or the management's expert has not consented to the auditor's intended use of their findings, the auditor considers the guidance as provided in paragraphs ~~51~~ 56 to ~~54~~59 of this Guidance Statement.

Engagement with the Management's Expert

~~36.~~40. As early as practicable during the engagement, the auditor communicates with the management's expert~~,~~ either directly or indirectly through management, and considers the

[26] Agreement for the expert to discuss findings with the auditor, and consent for the auditor to use the expert's findings, is generally discussed and agreed with management or those charged with governance and the expert at the planning phase of the engagement.

management's expert's approach and methodology. The auditor ~~assesses~~ evaluates whether the approach and methodology is an appropriate basis for determination of the matter included in the financial report or other historical financial information. For example where management uses a valuation expert for a purchase price adjustment calculation, the auditor communicates with the management's expert early on in the valuation process so as to understand and agree on the basis for identification of assets and the basis of the valuation methodology.

Evaluating the Appropriateness of the work of a Management's Expert

~~37.~~41. ASA 500[27] contains application and other explanatory material that when evaluating the appropriateness of the management expert's work as audit evidence for the relevant assertion, the auditor considers:

(a) The relevance and reasonableness of the management's expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial report;

(b) If the management's expert's work involves the use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; ~~and~~

(c) If the management's expert's work involves significant use of source data, the relevance, completeness and accuracy of that source data; and~~.~~

(d) If ~~that~~ the management's expert's work involves the use of information from an external information source, the relevance and reliability of that information.

~~38.~~42. ASA 540[28]contains requirements and application material when evaluating the appropriateness of the work of a management's expert as audit evidence in relation to the audit of accounting estimates.

Determining the necessary audit effort for evaluating the appropriateness of management's expert's work

~~39.~~43. ASA 500 and ASA 540 do not ordinarily require that the auditor reperforms all of the work ~~of~~ undertaken by a management's expert. Instead, if information is to be used as audit evidence and that evidence has been prepared using the work of a management's expert, the auditor's responsibility is to evaluate whether the management's expert's work provides sufficient appropriate audit evidence to support a conclusion regarding whether the corresponding accounts or disclosures in the financial report are in conformity with the relevant financial reporting framework.

~~40.~~44. Consistent with paragraph 23 of this Guidance Statement, f~~F~~actors that may impact the persuasiveness of evidence needed when evaluating the appropriateness of the work of a management's expert include the risk of material misstatement and the significance of the management's expert's work to the auditor's conclusion, include:~~.~~

(a) Consistent with ASA 330[29], the higher the risk of material misstatement for an assertion, the more persuasive the evidence needed to support a conclusion about that assertion.

(b) The significance of a management's expert's work refers to the degree to which the auditor gathers evidence in evaluating the management's expert's work to support the auditor's conclusions about the assertion. Generally, the greater the significance of the management's expert's work to the auditor's conclusion, the more persuasive the

[27] ASA 500, paragraph A59.
[28] ASA 540, paragraph 30.
[29] ASA 330, *The Auditor's Responses to Assessed Risks*, paragraph 7(b).

evidence from the management's expert's work needs to be. The significance of the management's expert's work stems from:

(i) The extent to which the management's expert's work affects the account balances, classes of transactions and disclosures in the financial report. In certain situations that work may be a primary source of audit evidence, while in other situations, the management's expert's work may only be used as a cross-check.

(ii) The auditor's approach to testing the relevant assertion and the availability of alternative sources of audit evidence. For example, when a company's accounting estimate is determined principally based on the work of a management's expert, and the auditor plans to test how management made the accounting estimate, the auditor would plan to evaluate the work of the management's expert for evidence regarding the estimate. If the auditor tests an assertion by developing an independent expectation, the auditor would give less consideration to the work of the management's expert.

~~*The Findings and Conclusions of the Management's Expert*~~

~~41. The auditor considers the final findings and conclusions in the agreed form of report of the expert. The auditor using their professional judgement considers what additional procedures are required, particularly when the risk of material misstatement has been assessed as significant. The auditor may consider performing more extensive procedures or engaging an auditor's expert to review some or all of the work of the management's expert. Specific procedures to evaluate the reasonableness of the management's expert's work for the auditor's purposes may include:~~

- ~~Enquiries of the management's expert.~~
- ~~Comparing the management's expert's final report to the draft report (if a draft report is provided) and understanding and enquiring into material differences.~~
- ~~Understanding the accuracy of prior period estimates made by that management's expert.~~
- ~~Corroborative procedures, such as:~~
  - ~~observing the management's expert's work;~~
  - ~~examining published data, such as statistical reports from reputable, authoritative sources;~~
  - ~~confirming relevant matters with relevant third parties;~~
  - ~~performing detailed analytical procedures; and/or~~
  - ~~re-performing calculations including sensitivity analysis on key inputs.~~
- ~~Consultation with another expert with relevant expertise when, for example, the findings or conclusions of the expert are not consistent with other audit evidence or the findings indicate an error, deviation, deficiency in internal control, or other significant matter or the scope of the engagement or adequacy of evidence is insufficient.~~
- ~~Discussion of the management's expert's report with management and if appropriate those charged with governance, including understanding their assessment of the expert's findings. In addition, if material, the auditor may seek to understand the reasons for the final report differing from initial draft reports.~~

~~42. Relevant factors when evaluating the relevance and reasonableness of the findings or conclusions of the management's expert, whether in a report or other form, may include whether they are:~~

- ~~Consistent with the auditor's understanding of the entity and its environment;~~
- ~~Clearly expressed, including reference to the objectives agreed with management, the scope of the work performed and standards applied;~~
- ~~Consistent with the results of other audit procedures;~~
- ~~Cross-checked against one or more other methodologies;~~
- ~~Based on an appropriate period/point in time and take into account events occurring after that date, where relevant;~~
- ~~Subject to any reservation, limitation or restriction on use, and if so, whether this has implications for the auditor; and~~
- ~~Based on appropriate consideration of errors, deviations, deficiencies in internal controls or other significant matters identified by the management's expert.~~

Methods, Assumptions and Source Data

~~43.~~45. ~~When a~~A management's expert's work involves the use of methods, assumptions and source data, the auditor ordinarily does not reperform all of the work undertaken by that expert. The auditor's responsibility is to evaluate that the management's expert's work is appropriate to provide~~s~~ sufficient appropriate audit evidence to support a conclusion regarding whether in all material respects the corresponding account balances, classes of transactions or disclosures in the financial report are in conformity with the applicable financial reporting framework. Paragraph 58 of this Guidance Statement provides additional guidance for the auditor where the auditor determines that the work of the management's expert is not appropriate for the auditor's purposes.

Methods

~~44.~~46. When a management's expert's work involves the use of ~~significant~~ methods, factors relevant to the auditor's evaluation of the appropriateness of methods include whether they are:

(a) Generally accepted within the management's expert's field;

(b) Justified as the appropriate valuation methodology;

(c) Consistent with the requirements of the applicable financial reporting framework; and

(d) Dependent on the use of specialised models.

~~45.~~47. Ordinarily the auditor is not expected to obtain access to proprietary models used by a management's expert. Rather, the auditor's responsibility is to obtain information to ~~assess~~ evaluate whether the model used is appropriate, robust and will produce outcomes that allow~~in~~ conformity with the applicable financial reporting framework. Depending on the model and the factors ~~discussed~~ listed ~~under~~ in paragraph ~~43~~46, this may involve for example one or more of the following:

(a) obtaining an understanding of the model;

(b) reviewing descriptions of the model in the management's expert's report;

(c) testing controls over the company's evaluation of the management's expert's work;

(d) ~~assessing~~ evaluating inputs to and outputs from the model or in place of other procedures, the auditor may consider using an alternative model for comparison.

~~46.~~48. If the work of a management's expert involves the use of methods relating to an accounting estimate, or developing or providing findings or conclusions relating to a point estimate or range or related disclosures for inclusion in a financial report, the auditor follows the requirements contained within ASA 540.[30]

Assumptions

~~47.~~49. When a management's expert's work involves the use of significant assumptions[31], factors relevant to the auditor's evaluation of the reasonableness of those assumptions may include consideration of:

(a) The degree of estimation uncertainty associated with the management's expert's underlying assumptions and the degree of stress testing undertaken;

(b) Significant changes during the course of the audit that may affect the appropriateness of the assumptions used; and~~and~~

(c) Consistency of those assumptions with relevant information. The following examples may be considered relevant:

- assumptions generally accepted within the management's expert's field and are they appropriate for financial reporting purposes;
- industry, regulatory and other external factors, including economic conditions;
- existing market information;
- historical or recent experience, along with changes in conditions and events affecting the company;
- significant assumptions used in other estimates tested in the company's financial report.

~~48.~~50. Assumptions relating to accounting estimates that are made or identified by a management's expert become management's assumptions when used by management in making an accounting estimate[32]. In these circumstances, the auditor applies the relevant requirements of ASA 540 to those assumptions.

Source Data Used by the Management's Expert

~~49.~~51. The auditor considers whether the source data is sufficiently relevant and reliable for their purposes, including procedures relating to establishing ~~evidence relating to~~ the accuracy and completeness of the data and evaluating whether the data is sufficiently precise and detailed. The extent of the auditor's procedures is dependent on the nature and risk of the source data and the materiality of the underlying balance, transaction and/or disclosure to which it relates. When a management's expert's work involves the use of source data that is significant to that expert's work, the auditor may evaluate that work. P~~p~~rocedures for the auditor may include considering how the management's expert determined that the source data was relevant and reliable, including as necessary in the circumstances how the management's expert determined that the source data was complete and accurate.~~such as the following may be used to evaluate that data:~~

[30] ASA 540, paragraph 30 and A131.
[31] ASA 540, paragraph A42.
[32] ASA 540, paragraph A130.

- ~~Identifying the source of the data, including obtaining an understanding of the data, and where applicable, testing the internal controls over the data and, where relevant, its transmission to the management's expert.~~
- ~~Assessing the data for completeness, accuracy and consistency with information available to the auditor.~~

~~50.~~52. In many cases, the auditor may test the source data directly, particularly where the data is internally produced by the company. However, in other cases, for example when the nature of the source data used by the management's expert is highly technical~~ in relation to the expert's field~~, that expert may test the source data. If the management's expert has tested the source data, the auditor considers the most appropriate way of evaluating whether the source data is sufficiently reliable for their purposes such as enquiry of that expert as to the scope and nature of the testing they performed, supervision or review of that expert's tests and~~/or~~ the involvement of an auditor's expert.

~~51.~~53. If the work of a management's expert involves sources of data relating to an accounting estimate, or developing or providing findings or conclusions relating to a point estimate or related disclosures for inclusion in a financial report, the auditor may find the requirements and application material of ASA 540[33] helpful.

The Findings and Conclusions of the Management's Expert

54. The auditor considers the final findings and conclusions in the agreed form of report of the management's expert. The auditor, using their professional judgement, considers what additional procedures are required, particularly when the risk of material misstatement has been assessed as significant. The auditor may consider performing more extensive procedures or engaging an auditor's expert to review some or all of the work of the management's expert. Specific procedures to evaluate the reasonableness of the management's expert's work for the auditor's purposes may include:

(a) Enquiries of the management's expert.

(b) Comparing the management's expert's final report to the draft report (if a draft report is provided) and understanding and enquiring into material differences and consideration of additional audit procedures as appropriate.

(c) Corroborative procedures, such as:

- observing the management's expert's work;
- examining published data, such as statistical reports from reputable, authoritative sources;
- confirming relevant matters with relevant third parties;
- performing detailed analytical procedures; and/or
- re-performing calculations including sensitivity analysis on key inputs.

(d) Consultation with an auditor's expert with relevant expertise when, for example, the findings or conclusions of the management's expert are not consistent with other audit evidence or the findings indicate an error, deviation, deficiency in internal control, or other significant matter or the scope of the engagement or adequacy of evidence is insufficient.

33 ASA 540, paragraph A131.

(e) Discussion of the management's expert's report with management and if appropriate those charged with governance, including understanding their evaluation of the expert's findings.

55. Relevant factors when evaluating the relevance and reasonableness of the findings or conclusions of the management's expert from that expert's report, may include whether they are:

(a) Consistent with the auditor's understanding of the entity and its environment;

(b) Clearly expressed, including reference to the objectives agreed with management, the scope of the work performed and standards applied;

(c) Consistent with the results of other audit procedures;

(d) Cross-checked against one or more other methodologies;

(e) Based on an appropriate period/point in time and take into account events occurring after that date, where relevant;

(f) Subject to any reservation, limitation or restriction on use, and if so, whether this has implications for the auditor; and

(g) Based on appropriate consideration of errors, deviations, deficiencies in internal controls or other significant matters identified by the management's expert.

Evaluation of the Work Undertaken by the Management's Expert

~~52.~~56. The auditor evaluates the appropriateness of the management's expert's work as audit evidence for the relevant assertion[34].

~~53.~~57. Considerations when evaluating the appropriateness of the management's expert's work include considering the relevance and reliability of that work including:

(a) the results of the auditor's procedures over the competence, capability and objectivity of the management's expert;

(b) the results of the auditor's procedures over the management's expert's methods, assumptions and source data;

(c) the nature of any restrictions, disclaimers or limitations in the management's expert's report; ~~and~~

(d) the consistency of the management's expert's work with other evidence obtained by the auditor and the auditor's understanding of the company and its environment.

~~54.~~58. If the auditor determines that the work of the management's expert is not appropriate for the auditor's purposes, or does not address material errors, deviations, deficiencies in internal controls or other material matters, the auditor may agree~~s~~ with management on the nature and extent of further work to be performed by the management's expert; or performs additional audit procedures appropriate to the circumstances[35]. The auditor may communicate this with those charged with governance. If the matter cannot be resolved, this is reported to those charged with governance and it may be necessary for the auditor to express a modified opinion in the auditor's report if the auditor cannot obtain sufficient appropriate audit evidence.

~~55.~~59. When the auditor concludes that the work of the management's expert is appropriate for the auditor's purposes, the auditor may use that expert's findings or conclusions as appropriate

[34] ASA 500, paragraph 8.
[35] ASA 500, paragraph 11.

audit evidence. The auditor then determines whether the management's expert's findings or conclusions have been accurately reflected in the financial report or other historical financial information including relevant disclosures.

Documentation

~~56.~~60. Although there are no specific documentation requirements in ASA 500, the auditor is required to comply with the documentation requirements of ASA 230[36], that requires the auditor when ~~assessing~~ evaluating the extent of documentation, to consider what audit documentation is necessary to enable an experienced auditor, having no previous connection with the audit, to understand the auditor's:

(a) ~~Assessment~~ Determination of whether to use the work of the management's expert;

(b) Evaluation of the competence, capabilities and objectivity of the management's expert;

(c) Understanding of the management's expert's work;

(d) Evaluation of the appropriateness of the management's expert's work as audit evidence for the relevant assertion.

~~57.~~61. The auditor ordinarily includes in their documentation relevant extracts from the management's expert's findings, including the conclusions reached.

~~58.~~62. The auditor follows the documentation requirements of ASA 540[37] when the management's expert's work is used in the preparation of an accounting estimate.

Reference to the Work of a Management's Expert in the Auditor's Report

~~59.~~63. The auditor does not refer to the work of the management's expert in an auditor's report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by law or regulation, the auditor indicates in the auditor's report that the reference does not reduce the auditor's responsibility for the auditor's opinion.

~~60.~~64. If the auditor makes reference to the work of the management's expert in the auditor's report because such reference is relevant to an understanding of a modification to the auditor's opinion, the auditor provides a description of the matter giving rise to the modification[38] and indicates in the auditor's report that such reference does not reduce the auditor's responsibility for that opinion.

Communication with Those Charged with Governance and Others

~~61.~~65. Due to uncertainties that may be associated with the work undertaken by a management's expert, the potential effects on the financial report and/or other historical financial information of any significant risks are likely to be of governance interest.

~~62.~~66. ASA 260 *Communication with Those Charged with Governance* contains the auditor's responsibility to communicate with those charged with governance in an audit of a financial report. In relation to using the work of a management's expert, the auditor, using professional judgement, may communicate:

(a) Whether management has engaged a management's expert;

(b) Concerns regarding competency or objectivity of the management's expert;

[36] ASA 230 *Audit Documentation*.
[37] ASA 540, paragraph 39.
[38] ASA 705, paragraph 20(b).

(c) Materiality and risk of the subject matter subject to determination by the management's expert;

(d) The proposed intended use of the management's expert's work by the auditor;

(e) Key findings/conclusions of the management's expert's report including commentary on:

- Significant assumptions, methods and data used;
- Degree of subjectivity of assumptions;
- Whether ~~the~~ that expert's work is adequate for audit purposes and obtains appropriate audit evidence; and
- Significant differences in judgement between the auditor and that expert.

The appropriate timing for communications will vary with the circumstances of the engagement; however, it may be appropriate to communicate significant difficulties encountered during the audit as soon as practicable if those charged with governance are able to assist the auditor to overcome the difficulty, or if it is likely to lead to a modified opinion.

Conformity with International Pronouncements

~~63.~~67. There is no equivalent International Standard on Auditing or International Auditing Practice Statement to this Guidance Statement.

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GS 005
(date)

Guidance Statement GS 005
Evaluating the Appropriateness of a Management's Expert's Work

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

Australian Government
Auditing and Assurance Standards Board

Obtaining a Copy of this Guidance Statement

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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Important Note

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement GS 005 *Evaluating the Appropriateness of a Management's Expert's Work* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

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AUTHORITY STATEMENT

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 005 *Evaluating the Appropriateness of a Management's Expert's Work.* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

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

This Guidance Statement does not prescribe or create new requirements.

Dated:

R Simnett AO
Chair - AUASB

GUIDANCE STATEMENT GS 005

Evaluating the Appropriateness of a Management's Expert's Work

Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors when using the work of a management's expert as audit evidence in relation to:

   (a) the audit of a financial report, in accordance with the *Corporations Act 2001*;

   (b) the audit of a financial report[1] for any other purpose; and

   (c) the audit of other historical financial information.

2. This Guidance Statement provides guidance that may be considered and adapted as necessary in the circumstances, to non-historical information assurance engagements but is not a substitute for referring to the requirements and application material contained in ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information.*

Issuance Date

3. This Guidance Statement is issued on 16 March 2015 by the AUASB and replaces GS 005 *Using the Work of a Management's Expert*, issued in March 2015.

Introduction

4. This Guidance Statement has been developed to provide guidance on:

   (a) the circumstances under which a management's expert may be used and the nature of that work;

   (b) the auditor's considerations in determining whether to use the work of a management's expert as audit evidence in carrying out the responsibilities of the auditor with respect to an entity's financial report or other historical financial information; and

   (c) the auditor's considerations in determining the information to be used as audit evidence.

Scope of this Guidance Statement

Management or Management's Expert

5. Where the necessary information to prepare the financial report and/or historical financial information is produced by management, ASA 330[2] requires the auditor to design and perform audit procedures whose nature, timing and extent are based on and are responsive to the risk of material misstatement at the assertion level as identified and assessed by the auditor in accordance with ASA 315[3].

6. Where the necessary information to prepare the financial report and/or historical financial information is produced by a management's expert, ASA 500 *Audit Evidence*[4], establishes

[1] For purposes of this Guidance Statement, where the term financial report is used, this includes reference to a complete set of financial statements for any other purpose.
[2] ASA 330, *The Auditor's Responses to Assessed Risks*, paragraph 6.
[3] ASA 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.
[4] ASA 500, paragraph 8.

mandatory requirements and provides application and explanatory material on using the work of a management's expert as audit evidence. This Guidance Statement is to be read in conjunction with ASA 500. Examples of the use of management's experts are included in paragraphs 16 to 18 of this Guidance Statement.

7. ASA 500[5,] also establishes mandatory requirements and provides application and explanatory material on information obtained from an external information source. This Guidance Statement does not provide guidance on information obtained from an external information source.

8. This Guidance Statement applies to the use of a management's expert's work irrespective of whether they are internal or external to an entity, but does not deal with the use of experts that are not engaged or employed by management.

9. The work of a management's expert is often associated with accounting estimates; accordingly, this Guidance Statement should be read in conjunction with ASA 540 Auditing Accounting Estimates and Related Disclosures[6].

Considerations in Using the Work of an Auditor's Expert

10. It is the responsibility of the engagement partner[7] to determine that the engagement team has the appropriate competence and capabilities, including sufficient time, to perform an audit engagement in accordance with the Australian Auditing Standards, relevant ethical requirements, and applicable legal and regulatory requirements. When management uses the work of a management's expert to assist the entity in preparing the financial report, the auditor determines whether the involvement of an auditor's expert is required.

11. There is no requirement for the auditor to use an auditor's expert to evaluate the work performed by a management's expert, however, if management uses a management's expert, the auditor determines whether to use the work of an auditor's expert[8]. An auditor who is not an expert in a field other than accounting or auditing may be able to obtain a sufficient understanding of that field to perform the audit without the use of an auditor's expert. Ways in which this understanding may be obtained include:

    (a) Experience in auditing entities that require such expertise, for example, an auditor who has not audited in the extractive industry may not have the same level of knowledge and understanding as an auditor who works extensively in this industry;

    (b) Education or professional development in the particular field which may include formal courses;

    (c) Discussion with individuals possessing expertise in the relevant field for the purpose of enhancing the auditor's own competence to deal with matters in that field;

    (d) Discussion with auditors who have performed engagements in the same or similar industries with the same or similar use of experts for the preparation of a financial report.

12. While an auditor may have obtained knowledge of a field as described in paragraph 11 of this Guidance Statement, the auditor's decision on whether to use an auditor's expert may still be influenced by factors included in ASA 620[9] as well as:

    (a) The nature and significance of the matter, including its complexity;

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5 ASA 500, paragraph 7.
6 ASA 540 paragraph 30.
7 ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information*, paragraph 14.
8 ASA 620 *Using the Work of an Auditor's Expert*, paragraph 7.
9 ASA 620, paragraph A9.

(b) The risks of material misstatement;

(c) The expected nature of procedures to respond to the identified risks, including:

(i) the auditor's knowledge and experience with the work of experts in relation to such matters; and

(ii) the availability and extent of alternative sources of audit evidence;

(d) The extent to which management has used a management's expert; and

(e) The management expert's competence, capabilities and objectivity.

13. This Guidance Statement does not provide guidance on the auditor's use of the work of an auditor's expert. ASA 620 *Using the Work of an Auditor's Expert* establishes mandatory requirements and provides application and other explanatory material on using the work of an auditor's expert as audit evidence.

Definitions

14. For the purposes of this Guidance Statement the following items have the meanings attributed in the Australian Auditing Standards and reproduced below:

(a) Expertise means skills, knowledge and experience in a particular field[10].

(b) External information source means an external individual or organisation that provides information that has been used by the entity in preparing the financial report, or that has been obtained by the auditor as audit evidence, when such information is suitable for a use by a broad range of users. When information has been provided by an individual or organisation acting in the capacity of a management's expert, that individual or organisation is not considered an external information source with respect to that particular information[11].

(c) Management's expert means an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial report or other historical financial information[12].

The Auditor's Responsibility for the Conclusion

15. The auditor has sole responsibility for the audit opinion expressed and that responsibility is not reduced by the auditor's use of the work of a management's expert.

Examples of the use of Management's Experts

16. The preparation and presentation of a financial report and/or other historical financial information of an entity is the responsibility of management and those charged with governance. Determination of amounts included in the financial report and/or other historical financial information may require expertise in a field other than accounting or auditing, such expertise may be obtained by management using a management's expert.

17. An individual may possess expertise in accounting or auditing, as well as expertise in a field other than accounting or auditing (for example an actuary may also be an accountant). In these circumstances the determination of whether that individual is a management's expert depends on the nature of the work performed. For example, an individual with expertise in

[10] ASA 620, paragraph 6(b).
[11] ASA 500, paragraph 5(d).
[12] ASA 500, paragraph 5(e).

applying methods of accounting for deferred income tax can often be easily distinguished from an expert in taxation law. The former is not a management's expert for the purposes of this Guidance Statement as this constitutes accounting expertise; the latter is an expert for the purposes of this Guidance Statement as this constitutes legal expertise. Similar distinctions may also be able to be made in other areas, for example:

(a) between expertise in methods of accounting for financial instruments, and expertise in complex modelling for the purpose of valuing financial instruments, the former is not considered to be a management's expert as this constitutes accounting expertise;

(b) an entity's internal expertise in IT controls is not considered to be a management's expert as management is responsible for the design and implementation of controls that is integral to the functioning of the financial reporting system and preparation of the financial report.

18. Management may engage or employ experts (this may include but is not limited to actuaries, valuers, engineers, environmental consultants, geologists, scientists, health practitioners, taxation specialists, legal advisors and other industry specialists) to obtain the necessary information to prepare the financial report and/or historical financial information. Examples of such expertise include:

(a) Valuation (for example, high-technology materials or equipment, complex financial instruments, land and buildings, intangibles, investments and environmental liabilities);

(b) Determination of physical characteristics relating to quantity on hand or condition (for example, quantity or condition of minerals, mineral reserves, or raw materials stored in stockpiles);

(c) Determination of amounts derived by using specialised techniques or methods (for example, actuarial calculations of liabilities associated with insurance contracts or employee benefit plans);

(d) Interpretation of technical requirements of contract, laws and regulations. This may be done in some cases by those possessing legal expertise. ASA 502 *Audit Evidence – Specific Considerations for Litigation and Claims* establishes requirements and provides application and other explanatory material regarding considerations by an auditor in obtaining sufficient appropriate audit evidence relating to litigation and claims. The requirement in ASA 502 is for the auditor to consider the applicable requirements and guidance on using the work of an expert contained in ASA 500 before using the work of on in-house or external legal counsel as audit evidence.

Considerations in Determining Whether to Use the Work of a Management's Expert

19. The auditor's decision on whether to use the work of a management's expert as audit evidence may be influenced by:

(a) the nature and significance of the matter, including its complexity;

(b) the risks of material misstatement in the matter;

(c) the nature, timing and extent of procedures to respond to the identified risks, including the auditor's knowledge of, and experience with, the work of the management's experts in relation to such matters and the availability of alternative sources of audit evidence; and

(d) the content of the management's expert's report and whether that expert has agreed for the auditor to access their work papers. An understanding of the nature, timing and extent of procedures performed is essential for the auditor to understand the management expert's conclusions. The management expert's report may:

(i) need to be written in sufficient detail that will allow the auditor to understand the nature, timing and extent of work performed by that expert;

(ii) not involve all the management's expert's detailed working papers.

20. Understanding of the content of the management's expert's report as well as determining whether the auditor may access that expert's workpapers (where considered necessary by the auditor), may need to be considered early on in the planning stages of the audit engagement and agreed in the terms of the engagement between the entity and the management expert.

21. When determining the nature, timing and extent of audit procedures in relation to the work of the management's expert, the auditor makes reference to the requirements, application and other explanatory material contained in ASA 500[13].

Considerations in Determining the Information to Be Used as Audit Evidence

22. ASA 500[14] requires that if information to be used as audit evidence has been prepared using the work of a management's expert, the auditor, to the extent necessary and having regard to the significance of that expert's work for the auditor's purposes:

(a) Evaluates the competence, capabilities and objectivity of that expert (Ref: Para. 24-36);

(b) Obtains an understanding of the work of that expert (Ref: Para. 37-40); and

(c) Evaluates the appropriateness of that expert's work as audit evidence for the relevant assertion (Ref: Para. 41-59).

23. In relation to the work of a management's expert, the auditor obtains more persuasive audit evidence the higher the auditor's assessment of risk[15]. The auditor may also consider obtaining more persuasive evidence as:

(a) the significance of that expert's work on the financial statements increases;

(b) the ability of the company to affect the management's expert's judgements increases;

(c) the level of competency and capability possessed by the management expert decreases.

Competence, Capabilities and Objectivity of a Management's Expert

24. The auditor makes reference to the requirements, application and other explanatory material contained in ASA 500 and evaluates whether the management's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. This is ordinarily performed as part of the audit planning and risk assessment process, the timing of which may be restricted by management's process for planning and selecting management's experts.

25. Competence, capability and objectivity of a management's expert impacts the degree of reliability of that expert's work as audit evidence, that is, the extent to which the management's expert's work could provide persuasive audit evidence.

26. When the management's expert has been evaluated by the auditor as having lower levels of competency and capability; and/or the company has the ability to significantly influence the

[13] ASA 500, paragraph 8.
[14] ASA 500, paragraph 8.
[15] ASA 330 *The Auditor's Responses to Assessed Risks*, paragraph 7(b).

management's expert's judgements, the auditor may consider not using that expert's work as audit evidence. In such circumstances the auditor may consider:

(a) suggesting to management to engage a different management's expert;

(b) determining the need for an auditor's expert; or

(c) changing the nature and extent of other audit procedures.

When the management's expert has been evaluated by the auditor as having higher levels of objectivity, competency and capability, this evaluation is not a substitute for evaluating the appropriateness of that expert's work as audit evidence as required by ASA 500[16].

27. The nature and extent of procedures to evaluate the management's expert's competence, capability and objectivity depends on the significance of that expert's work to the auditor's conclusion regarding the relevant assertion and the risk of material misstatement of the relevant assertion. As the significance of the management's expert's work and risk of material misstatement increases, the persuasiveness of the evidence the auditor obtains for this evaluation also increases.

Competence

28. Competence relates to the nature and level of expertise of the management's expert. The auditor uses professional judgement when determining the competency of a management's expert. When evaluating competence, the auditor may consider the guidance included in ASA 500[17] as well as:

(a) The management's expert's experience in the type of work performed, including applicable areas of speciality within the expert's field;

(b) The reputation and standing of the management's expert, including:

(i) Previous experience of the auditor with the work of that expert;

(ii) Enquiring of other practitioners who have used that expert or others working in the same industry;

(c) Understanding the accuracy of prior period estimates made by the management's expert. Where the auditor determines that past estimates have not been sufficiently accurate, the auditor may consider obtaining an understanding of the reasons for the inaccuracy and furthering audit procedures as appropriate to the circumstances;

(d) The professional certification, license or professional accreditation of the management's expert. Experts in a specific field commonly have professional obligations under their professional or industry bodies. These obligations vary significantly and are determined by the professional or industry body[18]. The auditor's confidence when evaluating the competency of the management's expert may increase with that expert's membership of professional or industry bodies that:

(i) Require professional qualification or accreditation;

(ii) Subject their members to regulatory requirements/guidance;

16 ASA 500, paragraph 8(c).
17 ASA 500, paragraph A48-A51.
18 For example actuaries are governed by the Institute of Actuaries of Australia, an actuary's specific responsibilities in relation to data are set out in the *Actuarial Code of Professional Conduct*, *Actuarial Professional Standards* and where relevant other regulatory and legislative requirements, *APRA Prudential Standards* and the *Life Insurance Act 1995.*

(iii) Subject their members to a specific set of standards or guidance on the expert's services;

(iv) Require continuous professional development; and

(v) Require professional obligations to be followed by their members.

29. The auditor's evaluation of the management expert's competence may be influenced by the management's expert's work environment, for example that expert's internal quality control policies and procedures.

Capability

30. Capability relates to the ability of the management's expert to exercise their competency in the circumstances. When evaluating capability, the auditor may consider the guidance included in ASA 500[19] as well as:

(a) Geographic location;

(b) Availability of time;

(c) Availability of resources;

(d) Instructions on scope provided by management.

Objectivity

31. Objectivity relates to the possible effects that bias, conflict of interest, or the influence of others may have on the professional or business judgement of the management's expert. When evaluating objectivity, the auditor may consider the guidance included in ASA 500[20] as well as:

(a) circumstances that threaten the objectivity of the management's expert; and

(b) whether appropriate safeguards are in place to eliminate those threats or reduce them to an acceptable level.

32. ASA 500 indicates that evidence from external sources is generally more reliable than that generated internally. The auditor may evaluate the relationship to the company of the management's expert, specifically, whether circumstances exist that give the company the ability to significantly affect the management's expert's judgements about the work performed, conclusions or findings. The existence of a relationship between the management's expert and the entity being audited may impair that expert's ability to be objective. The risk that the objectivity of a management's expert will be impaired increases when the management's expert is employed by the entity or is related in some way to the entity. Where a management's expert is employed by the entity, the auditor needs to consider whether there are any mitigating factors such as professional and/or statutory obligations governing the work of that expert that would impact on the objectivity of the management's expert.

33. Circumstances which may threaten the objectivity of the management's expert may include: advocacy threats, familiarity threats, self-review threats and self-interest threats[21]. Examples include economic dependency of the management's expert on the entity and contingency based fee arrangements.

[19] ASA 500, paragraph A48-A51.
[20] ASA 500, paragraph A48-A54.
[21] ASA 500, paragraph A52.

34. The evaluation of the significance of threats to objectivity and of whether there is a need for safeguards may depend upon the role of the management's expert and the significance of that expert's work in the context of the audit. There may be safeguards specific to the audit engagement, however there may be circumstances where safeguards cannot reduce threats to an acceptable level[22].

35. When the management's expert is an employee of the entity, mitigating factors which enhance the ability of the management's expert to be objective, and therefore are safeguards for the lack of independence may include:

    (a) Adherence to the professional standards issued by the expert's regulating body.

    (b) Formal appointment of the management's expert by those charged with governance and direct access to those charged with governance by that expert.

    Ordinarily, the basis on which the management's expert is remunerated and/or incentives offered as part of that remuneration are considered by the auditor when evaluating the management's expert's objectivity.

    Consideration of the above may also be relevant in evaluating the objectivity of a management's expert that is external to the entity.

Overall Evaluation of Competence, capability and objectivity of a management's expert

36. If the auditor is concerned with the competence, capability or objectivity of the management's expert, the auditor may decide to communicate any concerns with management and if appropriate those charged with governance and consider whether sufficient appropriate audit evidence can be obtained concerning the work of the management's expert. If sufficient appropriate audit evidence cannot be obtained concerning the work of the management's expert, the auditor may undertake alternative procedures or seek audit evidence from another expert including an auditor's expert.

Obtaining an Understanding of the Work of a Management's Expert

37. The auditor makes reference to the requirements, application and other explanatory material in ASA 500 when obtaining an understanding of the management's expert's work to evaluate whether it is appropriate for the purposes of the audit.

38. When obtaining an understanding of the management's expert's work, the auditor, having regard to whether the management's expert is internal or external to the entity, may consider:

    (a) The terms of the engagement between the entity and the management expert, including understanding the nature, timing and extent of work to be performed by the management's expert and the form of any report to be provided by that expert;

    (b) Whether the auditor has any prior knowledge of the management's expert's field of expertise, or with that expert;

    (c) The economic and competitive conditions impacting the entity and its operating results;

    (d) Whether there is evidence of undue management pressure on the management's expert;

    (e) The existence of controls within the entity over the work of the management's expert (for example whether there are procedures in place to challenge or review that expert's

22 ASA 620, paragraph A19.

work, such as review by those charged with governance) or controls over the source data used in that expert's assessment;

(f) Whether management has authorised their expert to discuss their findings or conclusions with the auditor[23];

(g) Whether the management's expert has consented to the auditor's intended use of their findings; and

(h) Whether the management's expert has agreed for the auditor to access their work papers (review of the expert's work papers is not normally required other than as considered necessary by the auditor using their professional judgement).

39. Where management has not consented for their expert to discuss their findings or conclusions with the auditor, or the management's expert has not consented to the auditor's intended use of their findings, the auditor considers the guidance as provided in paragraphs 56 to 59 of this Guidance Statement.

Engagement with the Management's Expert

40. As early as practicable during the engagement, the auditor communicates with the management's expert, either directly or indirectly through management, and considers the management's expert's approach and methodology. The auditor evaluates whether the approach and methodology is an appropriate basis for determination of the matter included in the financial report or other historical financial information. For example where management uses a valuation expert for a purchase price adjustment calculation, the auditor communicates with the management's expert early on in the valuation process so as to understand and agree on the basis for identification of assets and the basis of the valuation methodology.

Evaluating the Appropriateness of the work of a Management's Expert

41. ASA 500[24] contains application and other explanatory material that when evaluating the appropriateness of the management expert's work as audit evidence for the relevant assertion, the auditor considers:

(a) The relevance and reasonableness of the management's expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial report;

(b) If the management's expert's work involves the use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods;

(c) If the management's expert's work involves significant use of source data, the relevance, completeness and accuracy of that source data; and

(d) If the management's expert's work involves the use of information from an external information source, the relevance and reliability of that information.

42. ASA 540[25]contains requirements and application material when evaluating the appropriateness of the work of a management's expert as audit evidence in relation to the audit of accounting estimates.

23 Agreement for the expert to discuss findings with the auditor, and consent for the auditor to use the expert's findings, is generally discussed and agreed with management or those charged with governance and the expert at the planning phase of the engagement.
24 ASA 500, paragraph A59.
25 ASA 540, paragraph 30.

Determining the necessary audit effort for evaluating the appropriateness of management's expert's work

43. ASA 500 and ASA 540 do not ordinarily require that the auditor reperforms all of the work undertaken by a management's expert. Instead, if information is to be used as audit evidence and that evidence has been prepared using the work of a management's expert, the auditor's responsibility is to evaluate whether the management's expert's work provides sufficient appropriate audit evidence to support a conclusion regarding whether the corresponding accounts or disclosures in the financial report are in conformity with the relevant financial reporting framework.

44. Consistent with paragraph 23 of this Guidance Statement, factors that may impact the persuasiveness of evidence needed when evaluating the appropriateness of the work of a management's expert include the risk of material misstatement and the significance of the management's expert's work to the auditor's conclusion, include:

    (a) Consistent with ASA 330[26], the higher the risk of material misstatement for an assertion, the more persuasive the evidence needed to support a conclusion about that assertion.

    (b) The significance of a management's expert's work refers to the degree to which the auditor gathers evidence in evaluating the management's expert's work to support the auditor's conclusions about the assertion. Generally, the greater the significance of the management's expert's work to the auditor's conclusion, the more persuasive the evidence from the management's expert's work needs to be. The significance of the management's expert's work stems from:

        (i) The extent to which the management's expert's work affects the account balances, classes of transactions and disclosures in the financial report. In certain situations that work may be a primary source of audit evidence, while in other situations, the management's expert's work may only be used as a cross-check.

        (ii) The auditor's approach to testing the relevant assertion and the availability of alternative sources of audit evidence. For example, when a company's accounting estimate is determined principally based on the work of a management's expert, and the auditor plans to test how management made the accounting estimate, the auditor would plan to evaluate the work of the management's expert for evidence regarding the estimate. If the auditor tests an assertion by developing an independent expectation, the auditor would give less consideration to the work of the management's expert.

Methods, Assumptions and Source Data

45. A management's expert's work involves the use of methods, assumptions and source data, the auditor ordinarily does not reperform all of the work undertaken by that expert. The auditor's responsibility is to evaluate that the management's expert's work is appropriate to provide sufficient appropriate audit evidence to support a conclusion regarding whether in all material respects the corresponding account balances, classes of transactions or disclosures in the financial report are in conformity with the applicable financial reporting framework. Paragraph 58 of this Guidance Statement provides additional guidance for the auditor where the auditor determines that the work of the management's expert is not appropriate for the auditor's purposes.

[26] ASA 330, *The Auditor's Responses to Assessed Risks*, paragraph 7(b).

Methods

46. When a management's expert's work involves the use of methods, factors relevant to the auditor's evaluation of the appropriateness of methods include whether they are:

    (a) Generally accepted within the management's expert's field;

    (b) Justified as the appropriate valuation methodology;

    (c) Consistent with the requirements of the applicable financial reporting framework; and

    (d) Dependent on the use of specialised models.

47. Ordinarily the auditor is not expected to obtain access to proprietary models used by a management's expert. Rather, the auditor's responsibility is to obtain information to evaluate whether the model used is appropriate, robust and will produce outcomes that allow conformity with the applicable financial reporting framework. Depending on the model and the factors listed in paragraph 46, this may involve for example one or more of the following:

    (a) obtaining an understanding of the model;

    (b) reviewing descriptions of the model in the management's expert's report;

    (c) testing controls over the company's evaluation of the management's expert's work;

    (d) evaluating inputs to and outputs from the model or in place of other procedures, the auditor may consider using an alternative model for comparison.

48. If the work of a management's expert involves the use of methods relating to an accounting estimate, or developing or providing findings or conclusions relating to a point estimate or range or related disclosures for inclusion in a financial report, the auditor follows the requirements contained within ASA 540.[27]

Assumptions

49. When a management's expert's work involves the use of significant assumptions[28], factors relevant to the auditor's evaluation of the reasonableness of those assumptions may include consideration of:

    (a) The degree of estimation uncertainty associated with the management's expert's underlying assumptions and the degree of stress testing undertaken;

    (b) Significant changes during the course of the audit that may affect the appropriateness of the assumptions used; and

    (c) Consistency of those assumptions with relevant information. The following examples may be considered relevant:

        - assumptions generally accepted within the management's expert's field and are they appropriate for financial reporting purposes;
        - industry, regulatory and other external factors, including economic conditions;
        - existing market information;
        - historical or recent experience, along with changes in conditions and events affecting the company;

27 ASA 540, paragraph 30 and A131.
28 ASA 540, paragraph A42.

- o significant assumptions used in other estimates tested in the company's financial report.

50. Assumptions relating to accounting estimates that are made or identified by a management's expert become management's assumptions when used by management in making an accounting estimate[29]. In these circumstances, the auditor applies the relevant requirements of ASA 540 to those assumptions.

Source Data Used by the Management's Expert

51. The auditor considers whether the source data is sufficiently relevant and reliable for their purposes, including procedures relating to establishing the accuracy and completeness of the data and evaluating whether the data is sufficiently precise and detailed. The extent of the auditor's procedures is dependent on the nature and risk of the source data and the materiality of the underlying balance, transaction and/or disclosure to which it relates. When a management's expert's work involves the use of source data that is significant to that expert's work, the auditor may evaluate that work. Procedures for the auditor may include considering how the management's expert determined that the source data was relevant and reliable, including as necessary in the circumstances how the management's expert determined that the source data was complete and accurate.

52. In many cases, the auditor may test the source data directly, particularly where the data is internally produced by the company. However, in other cases, for example when the nature of the source data used by the management's expert is highly technical, that expert may test the source data. If the management's expert has tested the source data, the auditor considers the most appropriate way of evaluating whether the source data is sufficiently reliable for their purposes such as enquiry of that expert as to the scope and nature of the testing they performed, supervision or review of that expert's tests and the involvement of an auditor's expert.

53. If the work of a management's expert involves sources of data relating to an accounting estimate, or developing or providing findings or conclusions relating to a point estimate or related disclosures for inclusion in a financial report, the auditor may find the requirements and application material of ASA 540[30] helpful.

The Findings and Conclusions of the Management's Expert

54. The auditor considers the final findings and conclusions in the agreed form of report of the management's expert. The auditor, using their professional judgement, considers what additional procedures are required, particularly when the risk of material misstatement has been assessed as significant. The auditor may consider performing more extensive procedures or engaging an auditor's expert to review some or all of the work of the management's expert. Specific procedures to evaluate the reasonableness of the management's expert's work for the auditor's purposes may include:

    (a) Enquiries of the management's expert.

    (b) Comparing the management's expert's final report to the draft report (if a draft report is provided) and understanding and enquiring into material differences and consideration of additional audit procedures as appropriate.

    (c) Corroborative procedures, such as:

    - o observing the management's expert's work;

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29 ASA 540, paragraph A130.
30 ASA 540, paragraph A131.

- examining published data, such as statistical reports from reputable, authoritative sources;
- confirming relevant matters with relevant third parties;
- performing detailed analytical procedures; and/or
- re-performing calculations including sensitivity analysis on key inputs.

(d) Consultation with an auditor's expert with relevant expertise when, for example, the findings or conclusions of the management's expert are not consistent with other audit evidence or the findings indicate an error, deviation, deficiency in internal control, or other significant matter or the scope of the engagement or adequacy of evidence is insufficient.

(e) Discussion of the management's expert's report with management and if appropriate those charged with governance, including understanding their evaluation of the expert's findings.

55. Relevant factors when evaluating the relevance and reasonableness of the findings or conclusions of the management's expert from that expert's report, may include whether they are:

(a) Consistent with the auditor's understanding of the entity and its environment;

(b) Clearly expressed, including reference to the objectives agreed with management, the scope of the work performed and standards applied;

(c) Consistent with the results of other audit procedures;

(d) Cross-checked against one or more other methodologies;

(e) Based on an appropriate period/point in time and take into account events occurring after that date, where relevant;

(f) Subject to any reservation, limitation or restriction on use, and if so, whether this has implications for the auditor; and

(g) Based on appropriate consideration of errors, deviations, deficiencies in internal controls or other significant matters identified by the management's expert.

Evaluation of the Work Undertaken by the Management's Expert

56. The auditor evaluates the appropriateness of the management's expert's work as audit evidence for the relevant assertion[31].

57. Considerations when evaluating the appropriateness of the management's expert's work include considering the relevance and reliability of that work including:

(a) the results of the auditor's procedures over the competence, capability and objectivity of the management's expert;

(b) the results of the auditor's procedures over the management's expert's methods, assumptions and source data;

(c) the nature of any restrictions, disclaimers or limitations in the management's expert's report;

[31] ASA 500, paragraph 8.

(d) the consistency of the management's expert's work with other evidence obtained by the auditor and the auditor's understanding of the company and its environment.

58. If the auditor determines that the work of the management's expert is not appropriate for the auditor's purposes, or does not address material errors, deviations, deficiencies in internal controls or other material matters, the auditor may agree with management on the nature and extent of further work to be performed by the management's expert; or performs additional audit procedures appropriate to the circumstances[32]. The auditor may communicate this with those charged with governance. If the matter cannot be resolved, this is reported to those charged with governance and it may be necessary for the auditor to express a modified opinion in the auditor's report if the auditor cannot obtain sufficient appropriate audit evidence.

59. When the auditor concludes that the work of the management's expert is appropriate for the auditor's purposes, the auditor may use that expert's findings or conclusions as appropriate audit evidence. The auditor then determines whether the management's expert's findings or conclusions have been accurately reflected in the financial report or other historical financial information including relevant disclosures.

Documentation

60. Although there are no specific documentation requirements in ASA 500, the auditor is required to comply with the documentation requirements of ASA 230[33], that requires the auditor when evaluating the extent of documentation, to consider what audit documentation is necessary to enable an experienced auditor, having no previous connection with the audit, to understand the auditor's:

(a) Determination of whether to use the work of the management's expert;

(b) Evaluation of the competence, capabilities and objectivity of the management's expert;

(c) Understanding of the management's expert's work;

(d) Evaluation of the appropriateness of the management's expert's work as audit evidence for the relevant assertion.

61. The auditor ordinarily includes in their documentation relevant extracts from the management's expert's findings, including the conclusions reached.

62. The auditor follows the documentation requirements of ASA 540[34] when the management's expert's work is used in the preparation of an accounting estimate.

Reference to the Work of a Management's Expert in the Auditor's Report

63. The auditor does not refer to the work of the management's expert in an auditor's report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by law or regulation, the auditor indicates in the auditor's report that the reference does not reduce the auditor's responsibility for the auditor's opinion.

64. If the auditor makes reference to the work of the management's expert in the auditor's report because such reference is relevant to an understanding of a modification to the auditor's opinion, the auditor provides a description of the matter giving rise to the modification[35] and indicates in the auditor's report that such reference does not reduce the auditor's responsibility for that opinion.

[32] ASA 500, paragraph 11.
[33] ASA 230 *Audit Documentation*.
[34] ASA 540, paragraph 39.
[35] ASA 705, paragraph 20(b).

Communication with Those Charged with Governance and Others

65. Due to uncertainties that may be associated with the work undertaken by a management's expert, the potential effects on the financial report and/or other historical financial information of any significant risks are likely to be of governance interest.

66. ASA 260 *Communication with Those Charged with Governance* contains the auditor's responsibility to communicate with those charged with governance in an audit of a financial report. In relation to using the work of a management's expert, the auditor, using professional judgement, may communicate:

    (a) Whether management has engaged a management's expert;

    (b) Concerns regarding competency or objectivity of the management's expert;

    (c) Materiality and risk of the subject matter subject to determination by the management's expert;

    (d) The proposed intended use of the management's expert's work by the auditor;

    (e) Key findings/conclusions of the management's expert's report including commentary on:

    - Significant assumptions, methods and data used;
    - Degree of subjectivity of assumptions;
    - Whether that expert's work is adequate for audit purposes and obtains appropriate audit evidence; and
    - Significant differences in judgement between the auditor and that expert.

    The appropriate timing for communications will vary with the circumstances of the engagement; however, it may be appropriate to communicate significant difficulties encountered during the audit as soon as practicable if those charged with governance are able to assist the auditor to overcome the difficulty, or if it is likely to lead to a modified opinion.

Conformity with International Pronouncements

67. There is no equivalent International Standard on Auditing or International Auditing Practice Statement to this Guidance Statement.

Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**5.0**
Meeting Date:	3 March 2020
Subject:	Guidance Statement Revision Project
Date Prepared:	21 February 2020
Prepared By:	See Wen Ewe

☒ **Action Required** ☐ **For Information Purposes Only**

Agenda Item Objectives

1. To provide an update to, and receive feedback from, the AUASB on the survey results from the Guidance Statements Revision Project.

Background

2. At the September 2019 AUASB Meeting, the AUASB was presented with a Guidance Statements Revision Discussion Paper which:

   (a) Outlined an initial review of existing AUASB Guidance Statements (GS's) undertaken by AUASB Technical Group (ATG); and

   (b) Contained questions designed to obtain detailed responses from stakeholders regarding which GS's need to be prioritised for update by the AUASB. For more details on the Discussion Paper, please refer to Agenda Item 5.4.1 of the September 2019 board papers.

3. A survey was developed to complement the Discussion Paper, and both were distributed to stakeholders for feedback in October 2019. The Discussion Paper was emailed directly to targeted stakeholders and assurance professionals, as well as regulators who determine the legislative or regulatory requirements which determine the scope and content of certain GS's. The survey was attached as a link in the Discussion Paper and distributed via the AUASB's September 2019 newsletter.

4. The ATG has actively promoted this project via several LinkedIn posts and follow up emails to the stakeholders.

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Results/Findings

Written Responses from Stakeholders

5. Six written responses were received from APESB, APRA, CA ANZ, CPA Australia, ACNC and PwC. Please refer to the details below:

Guidance Statements to be updated – Written responses	No. of respondents
GS 009 *Auditing Self-Managed Superannuation Funds*	3
GS 022 *Grant Acquittals and Multi-Scope Engagements*	2
GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions*	1
GS 004 *Audit Implications of Prudential Reporting Requirements for General Insurers and Insurance Groups*	1
GS 017 *Audit Implications for Prudential Reporting Requirements of a Life Company*	1
GS 016 *Bank Confirmation Requests*	1
GS 019 *Auditing Fundraising Revenue of Not-for-Profit Entities*	1
GS 011 *Third Party Access to Audit Working Papers*	1
GS 006 *Electronic Publication of the Auditor's Report*	1

6. From the table above, for two of the nine GSs mentioned projects to update these pronouncements are currently in progress (GS 009 and GS 012).

7. Three out of six respondents suggested the AUASB develop new GS's covering Technology or Data Analytics related guidance. AUASB members should note this is already being addressed by the ATG through work of the Technology Project Advisory Group (PAG). Other suggestions for new GSs the AUASB could develop are as follows:

New Guidance Statements to be developed:	No. of respondents
Technology / Data Analytics	3
Private Health Insurance	1
Audit Quality for Not-for-Profit sector	1
Management Commentary and Service Performance Reporting in the Not-for-Profit sector	1
Cryptocurrency related activities	1

8. One respondent suggested that GS 022 should be divided into 2 separate GSs:

   (a) Grant Acquittals

   (b) Multi-Scope Engagements

Survey Responses

9. Eighteen responses were received, out of which eleven were assurance practitioners (61%) and two were professional bodies (11%). Other stakeholders who responded include regulators, public sector, academics, technical consultant and advisors.

10. A weighted average method was used to analyse the priorities of the GSs to be updated. Based on this analysis, the top five GSs survey respondents wants the AUASB to update are as follows:

    (a) GS 019 *Auditing Fundraising Revenue of Not-for-Profit Entities*

(b) GS 022 *Grant Acquittals and Multi-Scope Engagements*

(c) GS 016 *Bank Confirmation Requests*

(d) GS 003 *Assurance Relating to Australian Financial Services Licences issued under the Corporations Act 2001*

(e) GS 010 *Responding to Questions at an Annual General Meeting*

For the full analysis of responses to the survey please refer to Appendix 1.

11. As for new GSs to be developed, numerous respondents suggest different areas of interests. Please refer to the table below for the number of respondents and their respective areas of interests. AUASB members will note no strong trend indicating there are significant areas where stakeholders have requested the AUASB to create new GS's, and that a number of the topics survey respondents highlighted are already being addressed by other current AUASB projects.

New Guidance Statements to be developed:	No. of respondents
Real Estate Trust Accounts	2
Technology	1
Law and Regulations	1
Goodwill and Impairment	1
Credit Risk and Impairment	1
Less Complex Entities	1
Self-Managed Super Funds	1
Queensland Building and Construction Commission – audit and review of relevant entities in Queensland	1
Coal mining Long Service Leave scheme	1
Franchising – audit of marketing or advertising funds	1
Application of AASB 1058 & AASB 16 for peppercorn leases.	1

12. In terms of GSs to be withdrawn, the ATG suggested GS 014 *Auditing Mortgage Schemes* and GS 021 *Engagements under the National Greenhouse and Energy Reporting Scheme, Carbon Pricing Mechanism and Related Schemes* to be withdrawn.

13. Eleven out of thirteen respondents agreed with the ATG's suggestion that GS 014 should be withdrawn, and eight out of eleven respondents agreed that GS 021 should be withdrawn. The remaining respondents did not provide a response to this question.

14. Respondents who disagreed on the withdrawal of GS 014 did not provide specific reasons.

15. Two out of three respondents who disagreed on the withdrawal of GS 021 noted that the GS is still relevant and should be updated. One of them suggested that the GS should refer to other guidance from Clean Energy Regulator and be updated to reflect assurance engagements relevant to the sector and where areas are highly technical. The other respondent suggested that the GS should set expectations of auditors and influence regulator's guidance.

ATG Recommendations for the AUASB

16. Taking into account of both written submissions and survey responses, the ATG would like to propose the following GSs to be withdrawn or updated as a matter of priority.

(a) GSs to be withdrawn:

   (i) GS 014 *Auditing Mortgage Schemes*

   (ii) GS 021 *Engagements under the National Greenhouse and Energy Reporting Scheme, Carbon Pricing Mechanism and Related Schemes*

(b) GSs to be updated:

   (i) GS 003 *Assurance Relating to Australian Financial Services Licences issued under the Corporations Act 2001* – NB: The AUASB has also received correspondence directly from the ASX requesting this GS to be updated.

   (ii) GS 022 *Grant Acquittals and Multi-Scope Engagements*

   (iii) GS 019 *Auditing Fundraising Revenue of Not-for-Profit Entities*

   (iv) GS 016 *Bank Confirmation Requests*

   (v) GS 010 *Responding to Questions at an Annual General Meeting*

Questions for the AUASB

1. Do the AUASB support the recommendations of the ATG about which AUASB Guidance Statements require update and withdrawal described above?

2. Does the AUASB have any other comments on the analysis of the responses to the Guidance Statement Discussion Paper provided above?

Way Forward

17. The ATG will continue its work updating the various AUASB Guidance Statements which has already commenced (i.e. GS 005, GS 008, GS 009 & GS 012).

18. Other AUASB Guidance Statements identified as priorities for update or withdrawal at the March 2020 AUASB meeting will be included in the AUASB 2020-21 Technical Work Program.

Material Presented

Agenda Item 5.0	AUASB BMSP Guidance Statement Revision Plan

Appendix 1

	The 1st priority	The 2nd priority	The 3rd priority	The 4th priority	The 5th priority	**Weighted Average**
GS 019 Auditing Fundraising Revenue of Not-for-Profit Entities	33.33%	6.25%	7.14%	9.09%	0.00%	**2.3125**
GS 022 Grant Acquittals and Multi-Scope Engagements	5.56%	37.50%	14.29%	0.00%	9.09%	**2.2976**
GS 016 Bank Confirmation Requests	27.78%	12.50%	0.00%	9.09%	9.09%	**2.1617**
GS 003 Assurance Relating to Australian Financial Services Licences issued under the Corporations Act 2001	5.56%	6.25%	14.29%	9.09%	18.18%	**1.3203**
GS 010 Responding to Questions at an Annual General Meeting	0.00%	0.00%	35.71%	9.09%	0.00%	**1.2531**
GS 013 Special Considerations in the Audit of Compliance Plans of Managed Investment Schemes	11.11%	6.25%	7.14%	0.00%	0.00%	**1.0197**
GS 020 Special Considerations in Auditing Financial Instruments	0.00%	12.50%	7.14%	9.09%	0.00%	**0.896**
GS 002 Audit Implications of Prudential Reporting Requirements for Registered Superannuation Entities	0.00%	12.50%	0.00%	9.09%	9.09%	**0.7727**
GS 011 Third Party Access to Audit Working Papers	5.56%	0.00%	0.00%	18.18%	9.09%	**0.7325**
GS 007 Audit Implications of the Use of Service Organisations for Investment Management Services	5.56%	6.25%	0.00%	0.00%	0.00%	**0.528**
GS 018 Franchising Code of Conduct – Auditor's Reports	0.00%	0.00%	0.00%	18.18%	9.09%	**0.4545**
GS 021 Engagements under the National Greenhouse and Energy Reporting Scheme, Carbon Pricing Mechanism and Related Sc	0.00%	0.00%	7.14%	0.00%	9.09%	**0.3051**
GS 014 Auditing Mortgage Schemes	5.56%	0.00%	0.00%	0.00%	0.00%	**0.278**
GS 015 Audit Implications of Accounting for Investments in Associates	0.00%	0.00%	7.14%	0.00%	0.00%	**0.2142**
GS 004 Audit Implications of Prudential Reporting Requirements for General Insurers and Insurance Groups	0.00%	0.00%	0.00%	0.00%	0.00%	**0**
GS 017 Audit Implications for Prudential Reporting Requirements of a Life Company	0.00%	0.00%	0.00%	0.00%	0.00%	**0**

Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**6.0**
Meeting Date:	3 March 2020
Subject:	GS 009 – Auditing Self-Managed Superannuation Funds (September 2015) Update and Draft Guidance
Date Prepared:	24 February 2020

[X] **Action Required** [ ] **For Information Purposes Only**

Agenda Item Objectives

1. To update the AUASB on the progress to revise GS 009 – *Auditing Self-Managed Superannuation Funds* (September 2015).

Matters to Consider

Part A – General

Background

1. In February 2019 the AUASB received correspondence from both the ATO and CPA Australia / CA ANZ on potential areas for consideration in the revision of GS 009. These areas have been considered as part of the project plan.
2. The detailed project plan was approved by the AUASB in December 2019. The Board sponsor for the project is Justin Reid.
3. The AUASB have secured an external contractor to complete the detailed revision of GS 009 working in tandem with a senior project manager to oversee the updates to the Board and to ensure due process is met.
4. The ATG met with the working group to discuss a first draft of the revised GS 009 in mid December 2019.

Note

1. **Please ignore all formatting issues in Phase 1 draft GS 009, as these will be finalised as part of the overall QA due process toward finalisation of the guidance.**

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Project Plan Update

GS 009 requires updating to address:

- ATO, CPA & CAANZ submission of letters outlining areas for update; and
- the Australian Taxation Office (ATO) guidance on reciprocal auditing arrangements and recent litigation cases; and
- the experience of practitioners in the changing SMSF market and the application of GS 009.

Progress since December 2019 AUASB Meeting

1. Phase 1 - drafting on revised GS 009 continued in December through to March including:

   a. based on detailed comments received from the ATO and CPA / CA ANZ.

      Refer spreadsheet of key issue areas at Agenda Item 6.1. Areas in green have been considered in the current draft of GS 009 provided to the AUASB. (All other areas are yet to be considered by ATG and the Working Group. Where appropriate these will be reflected in the final Phase 2 version of GS 009 to be brought to the AUASB in April).

   b. comments received from the ATO, CPA / CA ANZ, contractor at working group meeting held on 19 December; and

   c. feedback from key practitioners in the SMSF space on issues around ASAE 3402 *Assurance Reports on Controls at a Service Organisation* and potential qualifications in Part A and Part B of the Independent Auditor's Report (ATO).

Key Issues Discussed with Working Group (ATO, CA ANZ, CPA & ASF (practitioner))

2. The working group meeting was held on 19 December 2020. At this meeting the following areas were the key focus:

a. Key Areas to be addressed:

i. **Special Purpose Reporting (SPR) vs General Purpose Reporting Frameworks (GPFS):** Discussion and confirmation of where an SMSF will sit within the reporting framework if SPR is removed and the carve outs under ED 97 to retain SPR for SMSFs in certain circumstances.

In August 2019, the Australian Accounting Standards Board issued Exposure Draft 97 - *Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities* (ED 97). If finalised as drafted, the ability of certain for-profit private sector entities to self-assess their reporting requirements and prepare special purpose financial statements will be removed. Auditors should note, the ED includes SMSFs where their "constituting or other documents, created or amended on or after 1 July 2020, specifically require financial statements to be prepared in accordance with AAS, to prepare general purpose financial statements".

It remains the trustee's responsibility for the selection of the accounting framework and the auditor's responsibility to assess the appropriateness of the framework[1] as part of preconditions of accepting

[1] See ASA 210 paragraph 6(a) which establishes requirements and provides guidance on determining the acceptability of the applicable financial reporting framework.

an engagement for the individual SMSF. Audits of funds from the planned implantation date require an additional check on the appropriateness of the accounting framework adopted by the SMSF in light of the ED. Accordingly, extra consideration will be required when applying GS 009 for the audit of a SMSF that is required to prepare GPFS. In the absence of the specific trust deed indicating the preparation of financial statements in accordance with AAS, legislative requirements will prevail. Refer paragraphs 16-18 of draft.

ii. **Use of technology in a SMSF audit** and the impact on audit procedures and documentation. Reliance on platforms, direct data feeds and further audit procedures required to obtain sufficient audit evidence. Refer paragraphs 86 to 91 of draft.

iii. **IDSP and Service Organisation** – Use of GS 007 Service Organisation Type 2 Controls reports coupled with Statements from custodians as to the ownership of units or assets within the funds and the ability for the user auditor to obtain enough comfort from this audit evidence (when they cannot access audit working files of another auditor) or a Type 2 report is not received covering the controls around attrition for the smaller non ASIC regulated IDPS's. In practice this has resulted in there being a high number of qualified audit opinions in Part A – Financial Audit on the basis of inability to obtain sufficient appropriate audit evidence of material balances and transactions at the fund level.

    After a further meeting with the ATO/AUASB/ASF/Contractor on 12 Feb 2020 the ATO will consider if on the basis that there is a low risk of material misstatement at the fund level of ownership of assets held by the fund and their valuation, and a Type 2 report and Statement are obtained for audit evidence from IDPS, that a Part A exemption for qualifying on the basis of insufficient or appropriate audit evidence, may be given but only in those circumstances. The ATO are considering their instructions on this matter for their 2020 Independent Audit Report (IAR).

    Refer paragraphs 142 to 156 of draft.

iv. **Opening Balances** – A new auditor may not rely on the opening balances in the SMSF on a first year audit and are therefore qualifying on this basis in Part A. This may occur in practice because the auditor is unable to perform sufficient appropriate audit procedures on the opening balances. ASA 510 para 6 and guidance in GS009 discusses this issue around opening balances of Member allocation of funds. ASF who audit 19,000 SMSFs (one of the biggest audit firms for SMSFs in Australia) has raised this issue. The ATO are considering their instructions for the 2020 SMSF Independent Audit report and whether there could be a Part A exclusion for opening balances. ATO want to keep part A qualifications in as it builds a complete risk profile for the SMSF. However, a Part A exemption for qualifying on opening balances as a new auditor may be considered if the new auditor is not able to appropriately access the individual fund balances.

    Refer paragraphs 177 to 183 of draft.

b. Further suggested areas for change in GS 009 (refer Agenda Item 6.1) as provided by the working group.

    In addition, specific comments were received from the ATO and CAANZ in early/mid February 2020 on the Phase 1 draft post the working group meeting, and as appropriate have been considered and reflected in the Phase 1 draft.

    Justin Reid the AUASB Sponsor has also reviewed and provided some comments on the Phase 1 draft.

Further Matters to Note

1. Due to the considerable amount of changes to ISAs / ASAs currently being considered on a number of other projects of the IAASB/AUASB e.g. ISQM 1, 2 and ISA 220, ISA 315 and ASA 102 and the

conforming amendments, we expect there may be impacts on the revision of GS 009 remaining up to the date of issue, as the guidance draws on the entire suite of ASAs and ASQMs.

Project Deliverables – Next steps post March AUASB Meeting

1. W/C 9 March - Comments from AUASB addressed in Phase 2 draft
2. W/C 9 March - Revised Phase 2 draft to go to working group (comments back to ATG before meeting)
3. W/C 16 March - 2nd and final working group meeting – agreed outcomes for final Phase 2 draft
4. W/C 23 March - Final comments from working group to be incorporated into Phase 2 draft GS 009
5. W/C 30 March - ATG QA and internal due process to be completed.
6. W/C 6 April - AUASB Sponsor to provide final review / comments.
7. Final draft to AUASB for comment and approval at 21 April Board meeting.

Part B – NZAuASB

1. N/A

Part C – "Compelling Reasons" Assessment

1. N/A

The proposed changes conform with IAASB modification guidelines for NSS?	Y ☐	N ☐

<u>AUASB Technical Group Recommendations</u>

Subject to changes from the AUASB, QA processes and further input from key stakeholders, proposed changes to GS 009 will be adopted with a view to finalising the revision for approval at the April AUASB Meeting.

<u>Material Presented</u>

Agenda Item 6.0	AUASB Board Meeting Summary Paper
Agenda Item 6.1	GS009 - Spreadsheet of Key Issue Areas Addressed
Agenda Item 6.2	Phase 1 – Draft GS 009 Auditing Self-Managed Superannuation Funds

Action Required

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	AUASB to provide comment on ATG approach to key issue areas and comments on Phase 1 draft as appropriate.	Comments from AUASB on key issues and Phase 1 draft GS 009.	AUASB	3 March 2020	

Topic	Reference	Update to be considered (may not be complete)	Comments
Independence examples	Appendix 5	Review scenarios provided to ensure they reflect the intent of the Code of Ethics and ATO's approach to independence.	Given the AASB/JAB independence guide is being updated for the new international independence standard then I believe it might be worthwhile having one source of commentary about independence for SMSF auditors. It would good to have agreement about this between the AASB, AUASB and accounting bodies about this.
Independence examples	Appendix 5	Reconsider the wording of scenario 2 & 4 regarding "reciprocal arrangements" as the ATO's expectations are that SMSF auditors will apply more sophisticated approach to independence and consider whether such arrangements create a self-interest threat to independence if they are reliant on reciprocal audits from one firm/ sole practitioner. Existing wording: "The resultant loss of work by withdrawing may be overcome by entering a **reciprocal arrangement** with an independent practitioner or firm for referral of SMSF audit engagements."	The guidance itself already reflects this concern - GS 009 para. 37 states that a self-interest threat "will also occur if the auditor or the audit firm relies on a single SMSF audit referral source for a significant amount of revenue". - GS 009 para. 46 states "Where the audit firm or an individual partner is unduly reliant on the audit fees from a particular group of SMSFs, such as those SMSFs referred by a single referral source, the concern about the possibility of losing the referrals may create a self-interest, advocacy or intimidation threat. Safeguards include diversifying the client base to spread the source of revenue so that the potential for undue influence is removed."
ASAE 3402 Type 1 & 2 Reports on Controls at Service Organisations		Cover more thoroughly the difference between type 1 & 2 reports	
ASAE 3402 Type 1 & 2 Reports on Controls at Service Organisations		Clarify that to rely on material data feeds a type 2 report is needed	
ASAE 3402 Type 1 & 2 Reports on Controls at Service Organisations		Clarify what to expect from different service providers by expanding on para.25 and addressing IT controls in more detail in addition to the guidance provided in paras 119-123 and 172-177.	
ASAE 3402 Type 1 & 2 Reports on Controls at Service Organisations		Consider providing some practical tips on IT security	
Documentation	Appendix 4	Highlight the documentation requirements to support the work done in the audit by including the need for documentation and possibly the type of documentation to be retained for each of the sections of the financial audit procedures listed in Appendix 4.	
Appendix 3 - checklist - E1 contributions	Appendix 3	Need to ensure all information is correct and add downsizer contributions.	
Revisions to AUASB Standards	Throughout the GS	The vast majority of the AUASB Standards have been revised since GS 009 was last amended in 2015, so references, approach and terminology need reviewing against the current suite of standards.	References and changes in approach and terminology to AUASB standards need to be checked and updated where required.
Independence	Appendix 5	The independence examples included in Appendix 5 do not all reflect the intent of the Code of Ethics and ATO's regulatory approach to independence, including their expectations regarding "reciprocal arrangements" between auditors.	Please see comment above.
Changes to the Superannuation legislation	Throughout the GS	Legislative changes, particularly the changes effective from 1 July 2017, need to be reflected in GS 009 and the audit implications considered.	Paragraph 4 - This may need to be changed if the legislation is passed that increases members from four to six. This also affects paragraph 11. Paragraph 5 – currently states that audits should be carried out on a yearly basis. This may need to be changed if the 3 year audit cycle proposal is introduced.
New and amended ATO views and interpretations	Throughout the GS	The ATO communicates its interpretation of how the SMSF and their auditor should meet their obligations from time to time and so the guidance statement needs to be consistent with the ATO's expressed views.	
Reports on Controls at Service Organisations		Clarification of the difference and appropriate use of ASAE 3402 Type 1 and 2 reports on Controls at Service Organisations and when those reports can enable reliance on material data feeds could assist auditors.	
Investment strategy and valuations		Clarification of the nature and extent of work necessary with respect to the SMSF's investment strategy and asset values, particularly in light of the recent court decisions in Cam & Bear Pty Ltd v. McGoldrick [2018] NSWCA 110 and Ryan Wealth Holdings Pty Ltd v. Baumgartner [2018] NSWSC 1502.	
Documentation	para 22 e	Highlight the documentation requirements to support the work done in the audit.	Could we add how important it is for auditors to make notes in their audit files about the conclusions they reached and provide an example eg. if you consider that rental income received by a fund is at arm's length record this conclusion in your file.
Reference to special purpose financial reports	para. 1, 22(ff), 134, 140(c), 163, 176, 214, 254, Appendix 2	If SPFR option withdrawn by AASB commencing 1/7/20 or 1/7/21, need to amend.	
Taxable/tax free splits based on contributions or benefits transferred or rolled over		There is no consistent reference to taxable/tax-free splits.	
Continuing Professional Development requirements	para 16, 17	Ensure consistency bet GS009, Prof assoc regs (eg CA ANZ Reg CR 7) and JAB publication (competency of SMSF auditors)	CPA/CAANZ to discuss ongoing need for JAB publication
Immediate reporting vs ATO interpretations	para.18(c)	SISA requires reporting contraventions as soon as practicable but ATO interpretation 28 days.	
Update history and plan for adjustments	para. 22	Reference to revised AUASB standards	Refer to CPA point above
Re-word for clarity	para. 22(g)	Not all SIS law breaches will lead to penalties that will lead to additional tax liabilities. Need to re-word for greater clarity	
Communication with those charged with Governance	Paragraph 22 (h)	It could be worth mentioning *McGoldrick* and *Baumgartner* in this paragraph as both cases are examples of why it is important for auditors to directly communicate with the trustees, especially with respect to significant issues.	
Re-word for clarity	para. 22(n)	Clarify if transaction data-feeds and source fall into GS007 or another standard	
Audit Evidence	para 22(p)	Further guidance here on importance of obtaining and keeping evidence in the audit files as this is an ongoing issue and ATO are consistently refering it to ASIC.	Clarification required with respect to the ATO's comment about the importance of obtaining and keeping the evidenced in the audit file i.e. source documents. For the AUASB this highlights issues around electronic access to banking information or the retention of hard copy bank statements as an example.
Access previous auditor's papers	para.28	Clarify how to access previous papers.	Under CA ANZ public practise regs the previous auditor is not obliged to provide access to documentation (but is encouraged to do so as a professional courtesy).
Independence subsection	pars 33 to 49	Refer to comment above about revised AASB independence guide	
Actuarial certificate requirement	para. 130	ATO interpretation: Actuarial certificate needed for period fund in retirement phase. This paragraph talks about the requirement to have an actuarial certificate, as there are changes to these requirements from 1 July 2017 this para will need re-wording.	Requires revision for ATO interpretation and 2016 legislative amendments
Communication with prior auditor, seems highly problematic	para.145	Clarify challenges	Refer above re: CAANZ public practise regs
Risk of fraud, how determined?	para 153		
Confirmation requests	para. 154 & 155		Provision of bank account data and confirmation of balances
Receivables and Prepayments	para 179	Include a reference to SMSFR 2009/3 *Self-Managed Superannuation Funds: application of the SISA to unpaid trust distributions payable to an SMSF* .	
Liabilities	para 184	Could include an extra bullet point 'Loan documents for LRBAs do not specify the loan is limited in recourse'	

Reserves	para 192 to 200 and 352	In response to the new measures and the potential to circumvent the caps through the use of reserves, the ATO published	
ATO view on reserves?	Para 193 onwards	SMSF Regulator's Bulletin SMSFRB 2018/1 The use of reserves by self-managed superannuation funds http://ato.gov.au/law/view/document?DocID=SRB/SRB20181/NAT/ATO&PiT=99991231235958	
Valuation and Allocation of Assets	para 163-171	This relates to valuation of assets. Given the Baumgartner case, can we add something here to remind auditors that if they do not get evidence from the trustees to support the market value reported in the financials that they should report (if it meets the reporting criteria) this to the trustees in writing and to the ATO in an Auditor/Actuary Contravention Report (ACR).	Paragraph 169 – consider adding an example such as 'For example, where a fund has an unlisted share or trust investment, the auditor should modify their opinion if they are unable to obtain satisfactory confirmation of the value of the investment'. (relevant in light of the recent *Baumgartner* and *McGoldrick* cases).
Unallocated contributions	Para. 198 & footnotes	ATO website documentation and required reporting	
Anti-detriment payments	Par 199 & 338	Update to take into account new legislation	There will no longer be a need for a SMSF to have an anti-detriment reserve. This is because the deduction is no longer available in relation to super lump sums paid to a spouse, former spouse or child of the deceased member on or after 1 July 2019 or where the deceased member died on or after 1 July 2017.
Downsizer	Para. 204	Downsizer contribution needs to be added	Some of these contributions such as directed termination payments are no longer available and there are new contribution such as the downsizer housing contribution that could be added here.
Non-resident super funds	Para. 212	Taxed at top marginal rate - needs mentioning	
Classification: Allocated to members correctly?	Para. 212	Add this to bullet points	
TSB references	Para. 218	Total super balance thressholds from 1/7/17	
Non-arm's length expenses (NALE)	Para. 221	ATO guidamce on NALE	What to do about proposed legislation amendment (lapsed due to 2019 election)? Likely to be reintroduced in late 2019.
Insert reference to ATO ruling on subject	Footnote 81		
Update	Para.226 & 227	1/7/17 legislative amendments	What to do about proposed 2019 budget announcement?
Treatment of revisionary pensions	Para. 233	1/7/17 legislative amendments	
Fund's financial position	Para. 238	Could this item be deleted here given it is referred to in par 361	
Tax liabilities	Para. 246	Add to bullet points	
ASA 705 - check for changes	para 253		
Standardise wording	Footnotes 100 & 102	Inconsistent	
Delivery of auditor's report to TCWG	Para. 261-265	Update for new standards	
Check Government Gazette	para.275	Another source of information on trustee to mention.	
Investment Strategy	para 280-283	Consider whether it could be worthwhile making reference to Baumgartner's Case here as highlighting the importance of the need for an auditor to verify that the Fund's investments are in line with its strategy.	
Aussiegolfa v. ATO test case in Supreme Court	Para.286 & 288	ATO lost case re sole purpose test - consider impact.	
Reference to investment strategy	Para. 293	Revise wording - discussion here is about sole purpose test not investment strategy	
Comments here can also apply to related companies	Para. 294	Revise wording	
In house assets exemption	Para. 305 & 306	Improve wording	
Non-arm's length income par	Para. 312-314	Consider amendment for NALE rules	What to do about proposed legislation amendment (lapsed due to 2019 election)? Likely to be reintroduced in late 2019.
Add: "or other appropriate and verifiable documentation"	Para. 313		
Through a closely held entity	Para. 315+	Clarify - lending through interposed entities	
Safe harbour rules & NALE	Para 327	ATO limited recourse borrowings, safe harbour and NALE	Required further explanation and that safe harbour rules are updated every year
Inspecie benefits paid, Cash only for …	Para.331 & 332	Update for first home savers benefits, financial hardship	ATO admininstration of some early release rules
Unsuitable asset valuation to determine min & max pension payment	Para.338; Footnote 177	Not using market valuiations - issue to be addressed	Need to work out best way to refer to ATO document (assuming it is still being published)
Correct grammar	Para. 341		
Incorrect description of regs	Para. 342 No?	Current legislation re conditions of release	Trustee determines invalidity
Incorrect: Control of fund, Validity of Binding Death Benefit Nomination (BDBN), Endurig Power of Attorney (EPoA) valid?	Para. 345+	Current legislation re conditions of release	Many other issues in relation to death benefits need to be explained
Requires re-write	para.370	Generally insurance benefits need to be paid out of fund	But to whom varies depending on type of insurance
Contribution Restrictions	para 358+	Will need updating if law is passed relaxing the work test for those over 65 years of age.	
TSB rules about acceptance of NCCs	para. 361 +	1/7/17 legislative amendments	
Change in contribution rules	para. 358 +	2018 & 2019 Federal budget announcements	2018 announcement regulated; How do we handle proposed 2019 changes?
ATO webpages keep moving	Footnotes 175, 177, 188 & 189		
Downsizer; Contributions for new retirees	Para. 343	Add to contributions types	
TSB issues	Para. 350	Total Super Balance interaction with non-consessionary contribution cap	
Use of reserves	para. 351	Re-word: contributions are not held in reserves; counted as concessional contribution	
Solvency	Para. 353-354	Does this need to be repeated here?	
Rep letter provided before or after audit?	Appendix 2	Before audit	Revise to take into account recent negligence court cases - in one case draft rep letter and engagement letters were provided with draft annual accounts. This was used against auditors in particular case. Should GS009 detail ideal workflow however this will be against typical industry practise?
Asset valuation	Appendix 2 point 7	Appendix	Should the draft wording be tightened to make it crystal clear that the trustee accepts all responsibility for the valuation of assets?
Uncorrected misstatements	Appendix 2 point 10		Should this be removed?
Pension provisions in trust deed	Appendix 3, G.1	1/7/17 Super changes	
Reserves	Appendix 3	Current ATO interpretations and reserve strategy not inconsistent with funds overall investment strategy	
Super Transfer balance account report (TBAR)	Appendix 3		
Arm's length rule	Appendix 4	ATO interpretation tightens arm's length rule up.	
Asset valualtions	Appendix 4 F.5 & L.1		Does procedure need to change for different asset classes esp closely held entities?
Do you need this? Asset valuations	Appendix 4 N.1	Medical certs etc of incapacity benefits	
Tax calcs	Appendix 4 O.1	Is auditor expected to complete this level of analysis of tax work?	

New terms to be introduced	Throughout the GS	The superannuation new measures introduced new terms and rules about Transfer Balance Caps, Total Superannuation Balance, Commutation authorities, Transfer Balance Account Reporting, and release authorities for Excess Transfer Balance Determinations. These new terms should be introduced at relevant parts of the Guidance Statement.	

FROM DRAFT MARK-UP

ATO - Type 2 and audit evidence	Paras 179 -	Reworded	
IHA ungeared trust	Para 189	UPE may make non-geared unit trusts in-house asset per SMSFD 2008/1 - Self Managed Superannuation Funds: how does the happening of an event in subregulation 13.22D(1) of the Superannuation Industry (Supervision) Regulations 1994 affect whether a self managed superannuation fund's investments in related companies or unit trusts are in-house assets of the fund? (Published on 20 February 2008)	Receivables section not compliance

Agenda Item 6.2

GS 009
(XXXX 2020)

Guidance Statement GS 009
Auditing Self-Managed Superannuation Funds

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

Draft

Australian Government
Auditing and Assurance Standards Board

Obtaining a Copy of this Guidance Statement

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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Important Note

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement *Auditing Self-Managed Superannuation Funds* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

CONTENTS

AUTHORITY STATEMENT

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 009 *Auditing Self-Managed Superannuation Funds* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

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

This Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

R Simnett AO
Chair - AUASB

GUIDANCE STATEMENT GS 009

Auditing Self-Managed Superannuation Funds

Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors conducting:

   (a) an audit of a self-managed superannuation fund's (SMSF's) special purpose financial report[1], (financial audit); and

   (b) an audit of a SMSF's compliance with the Superannuation Industry (Supervision) Act 1993 (SISA) and the Superannuation Industry (Supervision) Regulations 1994 (SISR) (compliance engagement).

2. This Guidance Statement does not apply to audits of Australian Prudential Regulation Authority (APRA) regulated superannuation entities.[2]

Issuance Date

3. This Guidance Statement is issued on XXXX 2020 by the AUASB and replaces GS 009 *Auditing Self-Managed Superannuation Funds*, issued in September 2015. The content of this Guidance Statement includes reference to legislative requirements which came into effect during 2014 and 2015.

Introduction

4. SMSFs are a specific type of superannuation fund which have fewer than five members and are regulated by the Australian Taxation Office (ATO). In addition, the SISA[3] gives ASIC the responsibility for the registration of approved SMSF auditors and setting competency standards. SMSFs are primarily governed by the requirements of the SISA, SISR, the Income Taxation Assessment Acts 1936 and 1997 (ITAA) and a fund's governing rules, which include the trust deed and applicable legislation. Complying SMSFs are eligible for tax concessions, and may also receive Superannuation Guarantee (SG) contributions. Complying SMSFs are Australian superannuation funds, which meet the requirements of the SISA and SISR and are "regulated"[4] under the SISA.

5. The SISA, subsection 35C(1), requires SMSFs to be audited each financial year by an approved SMSF auditor (the auditor),[5] who is required to complete both the financial audit and the compliance engagement and sign the auditor's report before a SMSF may submit its Annual Return.[6] The auditor reports to the trustees[7] in the "approved form", as issued and updated from time to time, by the ATO,[8] which includes opinions under two sections:

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1 Section 35B of the SISA requires the preparation of "accounts and statements," expanded by Part 8 of the SISR. For a detailed discussion, refer to Trustee Responsibilities in this Guidance Statement. .

2 Auditors of APRA regulated superannuation entities, particularly auditors of small APRA funds, may find this Guidance Statement useful in planning, conducting and reporting their audits, but it does not relate specifically to APRA funds.

3 See Division 1, Section 6 of the SISA.

4 Regulated funds, under section 19 of the SISA, are funds which have a trustee, either a corporate trustee or governing rules which contain a pension fund and have made an irrevocable election to become regulated in the approved form within the specified time.

5 Approved SMSF auditor is defined in paragraph 13.

6 The SMSF Annual Return (NAT 71226) comprises income tax reporting, regulatory reporting and member contributions reporting.

7 The use of the terminology trustee and trustees is used interchangeably throughout this document. Trustee or trustees include individual trustees, collective group trustees or a trustee body of a SMSF.

8 The approved form auditor's report is contained within the *Instructions and form for approved SMSF auditors - Self-managed superannuation fund independent auditor's report* (NAT11466). The auditor's report is available from the ATO's website www.ato.gov.au/Superfunds.

(a) Part A: Financial report; and

(b) Part B: Compliance report.

6. This Guidance Statement has been developed to identify, clarify and summarise the existing responsibilities which the auditor has with respect to conducting SMSF audits, and to provide guidance to the auditor on matters which the auditor considers when planning, conducting and reporting on the financial audit and compliance engagement of a SMSF.

7. This Guidance Statement does not extend the responsibilities of the auditor beyond those which are imposed by the SISA, SISR, Australian Auditing Standards (Auditing Standards), Standards on Assurance Engagements (ASAEs) or other applicable legislation.

8. This Guidance Statement comprises:

(a) an introductory section, which provides guidance on matters common to both the financial audit and compliance engagement;

(b) Part A, which provides guidance on the financial audit; and

(c) Part B, which provides guidance on the compliance engagement.

9. This Guidance Statement is to be read in conjunction with, and is not a substitute for referring to the requirements and guidance contained in:

(a) the Australian Auditing Standards , in which references to the "auditor" includes an approved SMSF auditor conducting the financial audit of a SMSF;

(b) applicable Standards on Assurance Engagements , specifically ASAE 3100 Compliance Engagements, in which references to the "assurance practitioner" include an auditor conducting a compliance engagement of a SMSF;

(c) the SISA and SISR;

(d) Applicable ATO Rulings, Interpretive Decisions (ID) and Guides and the Income Tax Assessment Acts; and

(e) Applicable ASIC Regulatory Guides and Class Orders.[9]

10. This Guidance Statement does not provide guidance on auditing a defined benefit fund[10] as these funds are not prevalent as SMSFs.

Definitions

11. A SMSF meets the definition of a SMSF of the SISA[11] if:

(a) it has fewer than five members;

(b) each individual trustee or director of the corporate trustee is a member of the fund, unless it is a single member fund, in which case the sole member is either:

(i) a director of the corporate trustee or one of two directors who are related or, if unrelated, the member is not an employee of the other director; or

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9 Further detail is available at www.asic.gov.au/smsf-auditor.
10 Defined Benefit Fund defined in Regulation 1.03(1) of the SISR.
11 See subsections 17A(1) & (2) of the SISA.

(ii) one of two individual trustees who are related or, if unrelated, the member is not an employee of the other trustee;

(c) each member of the fund is a trustee or a director of the corporate trustee;

(d) no member is an employee of another member, unless they are relatives; and

(e) no trustee, or director of a corporate trustee, receives remuneration for any duties or services performed by a trustee or director in relation to the fund, other than where there is an exception and the trustee has the skills to perform the service. [12]

12. A SMSF does not fail to satisfy the definition of a SMSF of the SISA[13] if:

(a) a member of the fund has died and the legal personal representative of the member is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during the period:

(i) beginning when the member of the fund died; and

(ii) ending when death benefits commence to be payable in respect of the member of the fund; or

(b) the legal personal representative of a member of the fund is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during any period when:

(i) the member of the fund is under a legal disability; or

(ii) the legal personal representative has an enduring power of attorney[14] in respect of the member of the fund; or

(c) if a member of the fund is under a legal disability because of age and does not have a legal personal representative - the parent or guardian of the member is a trustee of the fund in place of the member; or

(d) an appointment under section 134 of an acting trustee of the fund is in force.

13. An approved SMSF auditor[15] is a person who is registered as an approved SMSF auditor with ASIC[16] but does not include:

(a) a person for whom an order disqualifying that person from being an approved SMSF auditor is in force; or

(b) a person who is disqualified from being or acting as an auditor of any superannuation entity.

Trustees' Responsibilities

14. The responsibilities of the SMSF's trustees are contained in the SISA, SISR, and the governing rules of the fund. The trustees have ultimate responsibility for the compliance of the SMSF with the SISA and SISR and any other relevant legislation, such as the taxation legislation affecting SMSFs. Certain covenants affecting the behaviour of the trustees of a

12 Section 17B of the SISA allows for exceptions in relation to remuneration of trustees.
13 See subsections 17A (3) & (4) of the SISA.
14 The applicability of enduring powers of attorney in this circumstance will vary depending on the relevant state legislation. Guidance is also provided in Self-Managed Superannuation Funds ATO Ruling *SMSFR 2010/2*.
15 See subsection 10(1) of the SISA.
16 See SISA section 128B and ASIC Regulatory Guide 243 *Registration of self-managed superannuation fund auditors* provides guidance on how to apply for registration as an approved SMSF auditor.

SMSF are deemed to be contained in the SMSF's governing rules under section 52B and 52C of the SISA, which are in summary to:

(a) act honestly;

(b) exercise care, skill and diligence;

(c) act in the best interests of beneficiaries;

(d) keep the money and assets of the SMSF separate from the money and assets held personally by the trustees and from those of any employer-sponsor of the SMSF or their associates;[17]

(e) not enter into a contract or agreement that would hinder the trustees in properly performing their duties;

(f) formulate and give effect to a reserves strategy if applicable to the fund;

(g) formulate, review regularly and give effect to an investment strategy; and

(h) allow beneficiaries access to prescribed information and documentation.

The trustees' compliance responsibilities are summarised on the SMSF page of the ATO's website.[18]

15. The trustees of a SMSF are required, under the SISA, to ensure that financial reports of the SMSF are prepared and signed for each year of income and that an approved SMSF auditor is appointed no later than 45 days before the due date for lodgement of the SMSF annual return.[19]

Financial Reporting and Accounting Standards applicable to SMSFs

16. Accounting and financial reporting by SMSFs are governed by:

(a) AASB 1056 *Superannuation Entities* from 1 July 2016 (AAS 25 *Financial Reporting by Superannuation Plans*(superseded*)* and other applicable Australian Accounting Standards, including the Australian International Financial Reporting Standards (AIFRS);

(b) The SISA and the SISR;

(c) ATO publications and guidelines; and

(d) The Fund's Trust Deed.

SMSFs, where the members are also the trustees, would not be considered reporting entities and as such would ordinarily prepare a special purpose financial report, and therefore would not typically adopt AASB 1056 *Superannuation Entities*.

17. In August 2019, the Australian Accounting Standards Board issued Exposure Draft 97 - *Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities* (ED 97). If finalised as drafted, the ability of certain for-profit private sector entities to self-assess their reporting requirements and prepare special purpose financial statements will be removed. Auditors should note, the ED includes SMSFs where their "constituting or other documents, created or amended on or after 1 July 2020, specifically require financial

[17] See regulation 4.09A of the SISR.
[18] See https://www.ato.gov.au/Super/Self-managed-super-funds
[19] See regulation 8.02A of the SISR.

statements to be prepared in accordance with AAS, to prepare general purpose financial statements".

18. It remains the trustee's responsibility for the selection of the accounting framework and the auditor's responsibility to assess the appropriateness of the framework[20] as part of the preconditions of accepting an engagement for the individual SMSF. Audits of funds from the planned implementation date require an additional check on the appropriateness of the accounting framework adopted by the SMSF in light of the ED. Accordingly, extra consideration will be required when applying GS 009 for the audit of a SMSF that is required to prepare financial statements under the general purpose financial reporting framework (GPFS). In the absence of the specific trust deed indicating the preparation of financial statements in accordance with AAS, legislative requirements will prevail.

Financial statements prescribed by SISA and SISR

19. The financial statement formats for superannuation funds are set out in the SISA s. 35B and the SISR r. 8.01. SISA s. 35B requires each SMSF to prepare an operating statement and a statement of financial position.

20. SISA s. 35B also requires the financial statements to be signed by two signatories, except in the case of a single member fund with a sole director corporate trustee company, where one signatory is permitted.

21. The measurement and recognition criteria applied to SMSFs are at the discretion of the trustee; however, the trustee must take into account:

    (a) the trust deed requirements;

    (b) the member structure; and

    (c) SISA and SISR requirements.

22. ASA 260 *Communication With Those Charged With Governance* requires auditors to communicate their view's about 'significant qualitative aspects of the entity's accounting practices" and provides examples of matters that may be included in that communication including the appropriateness of the accounting policies to the circumstances of the entity being audited. The auditor will determine the appropriate form for this communication which may include the management letter.

Auditor's Responsibilities

23. The professional obligations of approved SMSF auditors under the SISA[21] are to:

    (a) complete the continuing professional development requirements prescribed by the regulations;[22]

    (b) hold a current policy of professional indemnity insurance;[23]

    (c) comply with:

[20] See ASA 210 paragraph 6(a) which establishes requirements and provides guidance on determining the acceptability of the applicable financial reporting framework.

[21] See subsection 128F of the SISA.
[22] See regulation 9A.04 of the SISR.
[23] See regulation 9A.05 of the SISR.

(i) any competency standards[24] ASIC determines;

(ii) any standards issued by the AUASB (unless not considered applicable to the audit of that particular SMSF); under:

◊ section 336 of the *Corporations Act 2001*; or

◊ section 227B of the *Australian Securities and Investments Commission Act 2001*; and

(d) comply with the auditor independence requirements produced by the Accounting Professional and Ethical Standards Board (APESB) and set out in APES 110 Code of Ethics for Professional Accountants (including Independence Standards) (Code of Ethics) as prescribed by the regulations.[25]

24. In addition, approved SMSF auditors may be subject to competency requirements, for the audit of SMSFs, by virtue of their membership of a professional body. For example, members of CPA Australia, Chartered Accountants Australia and New Zealand (CA ANZ) and Institute of Public Accountants (IPA) are required to comply with competency requirements[27] when accepting and conducting SMSF audits. These include requirements to hold a practising certificate, maintain appropriate professional indemnity insurance, complete minimum continuing professional development in the audit of SMSFs and ensure staff have appropriate knowledge and experience and are properly supervised. Auditors are to ensure that they are up-to-date and compliant with any applicable competency requirements imposed by their professional bodies in accepting and conducting SMSF audits.

25. The auditor is required under the SISA to:

(a) provide an auditor's report on the SMSF's operations for the year to the trustees in the approved form,[28] no longer than 28 days after the trustee of the fund has provided all documents relevant to the preparation of the report to the auditor;[29]

(b) report in writing to the trustees, if the auditor forms the opinion in the course of, or in connection with the performance of, the audit of the SMSF, that:

(i) any contraventions of the SISA or SISR, may have occurred, may be occurring or may occur in relation to the SMSF (section 129 of the SISA); or

(ii) the financial position of the SMSF may be, or may be about to become, unsatisfactory (section 130 of the SISA); and

(c) report in writing, within 28 days, to the ATO[30] using the approved form auditor/actuary contravention report (ACR) and instructions (ACR instructions),[31] if the auditor forms the opinion in the course of, or in connection with the performance, of the audit of a SMSF, that:

(i) it is likely that a contravention may have occurred, may be occurring or may occur, of the requirements of the SISA or SISR, specified by the ATO in the

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[24] See ASIC Class Order CO 12/1687 *Competency Standards for approved SMSF auditors.*

[25] See regulation 9A.06 of the SISR.

[27] See *Competency Requirements for Auditors of Self-Managed Superannuation Funds* (February 2008) issued by Representatives of the Australian Accounting Profession, CPA Australia, ICAA and IPA. https://www.charteredaccountantsanz.com/member-services/technical/superannuation/smsf-audit-services

[28] See section 35C of the SISA.

[29] See regulation 8.03 of the SISR.

[30] While the SISA (sections 129 and 130) requires reporting as soon as practicable after forming the opinion, it is the ATO's practice to require lodgement within 28 days of signing the auditor's report.

[31] *Auditor/actuary contravention report instructions* (NAT 11299) and ACR (NAT 11239), see: www.ato.gov.au/ Superfunds

ACR, which meet the tests specified in the ACR instructions (section 129 of the SISA); or

(ii) the financial position of the SMSF may be, or may be about to become, unsatisfactory (section 130 of the SISA).

26. The auditor may also provide information in the ACR to the ATO about the SMSF or a trustee of the SMSF, if the auditor considers it will assist the ATO in performing its functions under the SISA and SISR (section 130A of the SISA).

27. The approved form auditor's report, issued by the ATO, is divided into two parts:

(a) Part A: Financial report, which requires the auditor to express an opinion on the financial report, based on the audit, conducted "in accordance with Australian Auditing Standards".

(b) Part B: Compliance report, which requires the auditor to express an opinion on compliance with sections and regulations of the SISA and SISR specified in the ATO approved form auditor's report based on the compliance engagement, conducted "in accordance with applicable Standards on Assurance Engagements".

In addition, the ATO approved form auditor's report requires the auditor to include a statement in the auditor's report that they have complied with the independence requirements prescribed by the SISR and the competency standards set by ASIC.[32]

Conduct the Financial Audit and Compliance Engagement in Accordance with ASQC 1

28. ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements* establishes requirements and provides application and other explanatory material regarding the firm's responsibilities for its system of quality control for audits and reviews of financial reports and other financial information, and other assurance engagements.

Conduct the Financial Audit in Accordance with Auditing Standards

29. The auditor complies with all of the requirements in each of the Auditing Standards relevant to the financial audit in determining the audit procedures to be performed in conducting an audit in accordance with the Auditing Standards. The key Auditing Standards which are relevant to the conduct of the financial audit of a SMSF include, but are not limited to:

(a) ASA 102 *Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements* requires the auditor to comply with relevant ethical requirements, including those pertaining to independence.

(b) ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards* requires the auditor to:

(i) comply with the relevant ethical requirements, including those pertaining to independence, relating to financial report audit engagements;

(ii) comply with all Australian Auditing Standards relevant to the audit;

(iii) plan and perform an audit of a financial report by exercising professional judgement;

32 ASIC class order CO 12/1687.

(iv) plan and perform an audit with professional scepticism recognising that circumstances may exist that cause the financial report to be materially misstated; and

(v) To obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial report is prepared, in all material respects, in accordance with an applicable financial reporting framework.

(c) ASA 210 *Agreeing the Terms of Audit Engagements* requires the terms of the audit engagement to be agreed with the fund trustee, in an audit engagement letter or other suitable form of written agreement. On recurring audits, the auditor assesses whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the fund trustee of the existing terms of the audit engagement. The auditor obtains the trustee's acknowledgement that their responsibilities under the SISA and the SISR include the preparation of financial statements and records, establishing and maintaining internal controls, particularly those preventing and detecting fraud and error, and providing the auditors with any information, explanations and assistance required for the audit. This includes determining whether the financial reporting framework to be applied in the preparation of the financial report is appropriate.

(d) ASA 220 *Quality Control for an Audit of a Financial Report and Other Financial Information* requires the engagement partner to:

(i) remain alert, through observation and making enquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team, throughout the audit engagement;

(ii) form a conclusion on compliance with the independence requirements that apply to the audit engagement;

(iii) be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and determine that conclusions reached in this regard are appropriate;

(iv) be satisfied that the engagement team, and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capability to perform the audit engagement;

(v) take responsibility for the direction, supervision and performance of the audit engagement; and

(vi) take responsibility for the auditor's report being appropriate in the circumstances.

(e) ASA 230 *Audit Documentation* requires preparation of documentation:

(i) that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the audit procedures performed to comply with the Australian Auditing Standards and applicable legal and regulatory requirements;

(ii) that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the results of the audit procedures performed, the audit evidence obtained, significant matters arising during the audit, the audit conclusion reached thereon and significant professional judgements made in reaching those conclusions.

For example, rental income received from a non-arm's length arrangement is tested and the auditor's conclusions are recorded in the working papers.

Where the auditor's conclusions rely on their professional judgement, the working papers should provide appropriate documentation as to the methodology that led to the conclusion; and

The use of a 'completion memorandum' is useful as a summary of the conduct of the audit and how the opinion was formed.

(iii) which is assembled in an audit file on a timely basis (ordinarily not more than 60 days) after the date of the auditor's report.

Audit file retention is not mandated however, paragraph A61 of ASQC 1 requires the retention of audit working papers for a minimum of 5 years which is in line with the SISA requirement for the retention of financial reports for a period of 5 years.

(f) ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* requires the auditor to consider the risks of material misstatements in the financial report due to fraud.[33]

(g) ASA 250 *Consideration of Laws and Regulations in an Audit of a Financial Report* requires the auditor to obtain a general understanding of the legal and regulatory framework applicable to the entity, how the entity is complying with that framework, perform further audit procedures to help identify instances of non-compliance with those laws and regulations that may have a material effect on the financial report and obtain sufficient appropriate audit evidence regarding compliance with those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial report[34]

ASA 250 is particularly relevant due to the requirement for a SMSF to have an annual Compliance Audit. Where non-compliance of SISA or SISR is identified, the auditor is required to assess the impact, if any, on the financial report.

Most breaches of tax law result in additional tax applied at the member level individually rather than at a fund level and often do not have a material impact on the financial statements. In the case of material excess contributions, the auditor may modify their opinion on the financial statements if it is likely the excess contribution will be required to be withdrawn from the fund in future years and the result will be significant to the fund's financial report.

Compliance breaches identified as a result of the audit are reported to the ATO for regulatory action. If, in the opinion of the auditor, the breach could result in the material misstatement of the financial report (in future years), they should consider modifying their opinion on the audit of the financial statements – Part A qualification.

This is in addition to any modification of opinion in respect of the Compliance Audit – Part B qualification.

[33] Due to the few persons generally involved in the operation of an SMSF, there is ordinarily limited segregation of duties, which may impact on the auditor's assessment of fraud risk, as trustees, administrators or advisers may have an ability to override controls. SMSFs are not afforded the same level of protection as APRA regulated funds, for which provision is made, in certain circumstances, for members to be compensated for losses incurred in the event of fraud.

[34] The ATO has published a Checklist for SMSF Auditors which is designed to assist SMSF Auditors to understand what the ATO ordinarily considers sufficient and appropriate audit documentation for an SMSF.

An example of a compliance breach that may cause the material misstatement of the SMSF's financial statements is where there is a breach of the *in-house asset rules (IHA)*. A review of the rectification plan to determine the impact, if any, on the financial report will be required for the auditor to determine whether they modify their opinion.

An example of where there could be material misstatement of the financial statements without breaching any legal requirements is when the fund incurs *non-arm's length income or expenses (NALI/NALE).* The tax calculation, and therefore the closing member balances, could be materially misstated if NALI/NALE is not reported. In this instance, the auditor may consider modifying their opinion on the financial statement audit.

(h) ASA 260 *Communication with Those Charged with Governance* requires the auditor to determine the appropriate person(s) within the entity's governance structure with whom to communicate, usually the trustees in the audit of an SMSF, and communicate with them the responsibilities of the auditor in relation to the financial report audit, an overview of the planned scope and timing of the audit, significant findings from the audit, and auditor independence on a timely basis. The auditor may also consider issuing a management letter or some form of audit completion document to the Trustee.

The auditor's engagement is with the SMSF trustee and as such the auditor communicates directly with the SMSF trustee rather than indirectly such as via the referring accountant.

The auditor has a direct responsibility to the trustee and should not seek to rely on the representations of other parties.[35]

(i) ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* requires the auditor to communicate appropriately to those charged with governance and management, deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgement, are of sufficient importance to merit their respective attentions. Regardless of whether or not the auditor has relied on internal controls, deficiencies of internal controls identified during the audit may still need to be communicated with the trustees of the fund.

(j) ASA 300 *Planning an Audit of a Financial Report* requires the auditor to perform preliminary engagement activities, including evaluation of their own compliance with relevant ethical requirements including independence, to establish and document an overall audit strategy that sets the scope, timing and direction of the audit, that guides the development of the audit plan and plan the nature, timing and extent of direction and supervision of the engagement team members and review of their work.

(k) ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment* requires the auditor to obtain an understanding of the SMSF and its environment, including its internal controls to provide a basis for the identification and assessment of risks of material misstatement at the financial report and assertion level.

(l) ASA 320 *Materiality in Planning and Performing an Audit* requires the auditor to determine materiality for the financial report as a whole when determining the overall audit strategy, and to determine performance materiality for purposes of assessing the

[35] Cam & Bear Pty Ltd v McGoldrick [2018] NSWCA 110 and Ryan Wealth Holdings Pty Ltd v Baumgartner [2018] NSWSC 1502

risks of material misstatement and determining the nature, timing and extent of further audit procedures.

(m) ASA 330 *The Auditor's Responses to Assessed Risks* requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial report level and design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. Further audit procedures may comprise only substantive procedures or, when reliance is placed on the operating effectiveness of controls to reduce substantive testing, include tests of controls.

(n) ASA 402 *Audit Considerations Relating to an Entity Using a Service Organisation* requires the auditor to determine whether the service organisation's activities are of significance to the SMSF and relevant to the audit and, if so, the auditor is required to obtain a sufficient understanding of the SMSF and its environment to identify and assess the risks of material misstatement and design further audit procedures in response to the assessed risk. The auditor may need to obtain evidence of the operating effectiveness of the service organisation's controls and may use a report of a service organisation auditor to provide that evidence.

Part A of Guidance Statement GS 007 *Audit Implications of the Use of Service Organisations for Investment Management Services* provides guidance to a "user auditor" on the application of ASA 402 in respect of investment management services. Investment Management Services may include WRAP platforms (IDPS), custodial asset management, management accounts (SMA, IMA).

GS 007 provides guidance for the preparation, and use as audit evidence, of two types of Control Reports – Type 1 and Type 2 stating a Type 1 Report can be used in applying ASA 315 to the audit planning and, a Type 2 Controls Report can be used by the auditor in applying ASA 330.

Type 2 Control Report, containing an unmodified opinion, ordinarily provides the user auditor with sufficient appropriate audit evidence as to the reliability of controls over the investment management services provided by the service organisation to the user entity and accordingly may enable the user auditor to reduce the extent of substantive testing that might otherwise have been necessary with respect to the balances or transactions subject to those services. Type 2 Control Report does not however eliminate the need for substantive procedures altogether, as ASA 330 requires the auditor, irrespective of the assessed risk of material misstatement, to design and perform substantive procedures for each material class of transactions, account balance and disclosure.

ASAE 3402 *Assurance Report on Controls as a Service Organisation* is the standard applied by the service organisation auditor that produces a Controls Report that can be used as appropriate evidence under ASA 402. The standard provides for the issuance of either Type 1 or Type 2 reports. Only Type 2 reports provide reasonable assurance that the control objectives within the organisation were achieved through the reporting period.

The use of data feeds for the transfer of information required for the preparation of a SMSF's financial report may be used by investment management providers as well as by other entities – financial institutions and share registries. Typically this results in the source documentation being retained by the service organisation and therefore, additional audit consideration regarding the planning, testing and forming of an opinion is required.

In using a "Type 2"service auditor's report issued in accordance with ASAE 3402 the auditor considers the professional competence of the service auditor, the nature and content of the report, the scope of the work performed and whether the nature, timing and extent of the tests of controls and results that are relevant, provide sufficient appropriate audit evidence about the operating effectiveness of those controls to support the assessed risks of material misstatement.

(o) ASA 450 *Evaluation of Misstatements Identified during the Audit* requires the auditor to determine whether the overall audit strategy and audit plan needs to be revised if the nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit, could be material or approaches materiality determined in accordance with ASA 320.

(p) ASA 500 *Audit Evidence* requires the auditor to design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion. It requires the auditor to consider the relevance and reliability of the information to be used as audit evidence which includes the documentation of their testing and how the results may impact the audit opinion.

(q) ASA 502 *Audit Evidence – Specific Considerations for Litigation and Claims* requires the auditor to design and perform audit procedures to identify litigation and claims which may give rise to a risk of material misstatement, and that they are accounted for and disclosed in accordance with the applicable financial reporting framework. For an SMSF, material legal matters may include: the divorce of a member which may threaten the liquidity of the SMSF, an ATO investigation into the trustee or legal action commenced by the SMSF against the SMSF's administrators or investment managers, each of which may have a material effect on the financial report.

(r) ASA 505 *External Confirmations* requires the auditor to request external confirmations where they are considered necessary to obtain sufficient appropriate audit evidence.

(s) ASA 510 *Initial Audit Engagements – Opening Balances* requires the auditor to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial report, by determining whether the prior period closing balances have been correctly brought forward and that appropriate accounting policies are applied consistently.

(t) ASA 520 *Analytical Procedures* In addition to requirements relating to substantive analytical procedures, the standards require the auditor to design and perform analytical procedures to address the assessed risks of material misstatement near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial report is consistent with the auditor's understanding of the SMSF.

(u) ASA 530 *Audit Sampling* requires if sampling is used, the auditor, when designing the sample to consider the purpose of the procedure and the characteristics of the population from which the sample will be drawn and to evaluate whether the results of the sample provide a reasonable basis for concluding on the population.

(v) ASA 540 *Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures* requires the auditor to obtain sufficient appropriate audit evidence that accounting estimates, including fair value accounting estimates and disclosures are reasonable and are in accordance with the applicable financial reporting framework, which is chosen by the trustee in the case of a SMSF. The requirements and guidance in ASA 540 are particularly relevant to the audit of trustees' valuations, which are common in SMSFs. Regulation 8.02B of the SISR requires SMSF assets to be valued at market value.

(w) ASA 550 *Related Parties* requires the auditor to design and perform audit procedures to obtain sufficient appropriate audit evidence that all related party relationships and transactions have been identified, and have been appropriately recorded and disclosed[36] in the financial report.

(x) ASA 560 *Subsequent Events* requires the auditor to perform audit procedures designed to obtain sufficient appropriate audit evidence that all events up to the date of the auditor's report have been identified, and if material, are properly disclosed and accounted for.

(y) ASA 570 *Going Concern* requires the auditor to consider the appropriateness of use of the going concern assumption in the preparation of the financial report.

(z) ASA 580 *Written Representations* requires the auditor to request written representations from management that they are responsible for the preparation of the financial report in accordance with the applicable reporting framework that they have selected as appropriate for the SMSF, that they have provided the auditor with all relevant information and access, and that all transactions have been recorded and reflected in the financial report. In the case of a SMSF, these representations are obtained from the trustees.

(aa) ASA 620 *Using the Work of an Auditor's Expert* requires the auditor, when using the work of an auditor's expert, to obtain sufficient appropriate audit evidence that such work is adequate for the purposes of the audit and to evaluate the competence, capabilities and objectives of the auditor's expert.

(bb) ASA 700 *Forming an Opinion and Reporting on a Financial Report* requires the auditor to form an opinion on whether the financial report is prepared, in all material respects, in accordance with the applicable financial framework, and to express the opinion in an auditor's written report. The use of the special purpose reporting framework for the financial report is at trustee discretion.

From 1 July 2020, if a SMSF's establishment trust deed or, and an existing trust deed is amended, and includes the requirement to prepare financial statements in accordance with the Australian Accounting Standards, the trustee must consider whether they are required to prepare the financial report under the general purpose reporting framework.[37]

(cc) ASA 705 *Modifications to the Opinion in the Independent Auditor's Report* requires the auditor to modify the auditor's report when it is not possible to issue an unmodified audit opinion. The circumstances may dictate that, due to a conflict, a significant uncertainty, a limitation of scope or a lack of sufficient appropriate audit evidence, that it is not possible to issue an unqualified audit opinion. In these circumstances, ASA 705 requires the auditor to issue either a qualified audit opinion, a disclaimer of opinion or an adverse opinion.

(dd) ASA 706 *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* contains the requirements of how the emphasis of matter paragraph or other matter paragraph are to be shown in the auditor's report.

(ee) ASA 710 *Comparative Information – Corresponding Figures and Comparative Financial Reports* requires the auditor to determine whether the financial report includes the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified.

[36] Since the majority of SMSFs operate under the special purpose framework, they may elect not to comply with the disclosure requirements of AASB 124 *Related Party Disclosures*.

[37] AASB ED *Removal of Special Purpose Financial Statements for certain For-Profit Private Sector Entities 30 November 2019*.

(ff) ASA 800 *Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* specifies the requirements of the auditor's report on special purpose financial reports, which for SMSFs is reflected in the ATO approved form auditor's report issued by the ATO.[38] Auditor's reports for SMSFs include an Emphasis of Matter paragraph drawing attention to the note in the financial report which describes the basis of accounting.

Conduct the Compliance Engagement in Accordance with Applicable Standards on Assurance Engagements

30. ASAE 3100 *Compliance Engagements*, which is to be read in conjunction with ASAE 3000 Assurance Engagements Other Than Audits or Reviews of Historical Financial Information, is applicable to the conduct of the compliance engagement of SMSFs. ASAE 3100 requires the auditor to:

- Comply with applicable Standards on Assurance Engagements;
- Comply with the fundamental ethical principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour;
- Implement quality control procedures;
- Meet acceptance and continuance procedures;
- Agree the terms of the engagement in writing;
- Plan the compliance engagement so that it will be performed effectively;
- Consider materiality and compliance engagement risk[39] when planning and performing the compliance engagement;
- Reduce compliance engagement risk to an acceptable level in the circumstances of the compliance engagement;
- Obtain sufficient appropriate evidence on which to base the conclusion and evaluate the impact on the conclusion of any compliance breaches noted;
- Consider the effect of events up to the date of the compliance report;
- Prepare, on a timely basis, documentation that is sufficient and appropriate to provide a basis for the auditor's conclusion and evidence that the engagement was performed in accordance with ASAE 3000 and ASAE 3100; and
- Express a conclusion about the subject matter information, which for an SMSF is compliance in all material respects with the SISA and SISR requirements specified in the approved form auditor's report.

31. Since ASAE 3100 is read in conjunction with ASAE 3000, where specific application and other explanatory guidance is contained in ASAE 3000 and only referenced in ASAE 3100, this guidance statement makes direct reference to ASAE 3000. Although Auditing Standards do not apply to compliance engagements, they may nevertheless provide helpful guidance in the conduct of a compliance engagement.

[38] In the rare circumstances where the SMSF is a reporting entity, the SMSF is required to prepare a general purpose financial report and the auditor refers to the requirements in ASA 700 *The Auditor's Report on a General Purpose Financial Report.*

[39] Compliance engagement risk is defined in ASAE 3100, paragraph 11 as: the risk that the assurance practitioner expresses an inappropriate conclusion when the entity (SMSF) is materially non-compliant with the requirements as measured by the suitable criteria (SISA sections and SISR regulations as specified in the ATO approved form auditor's report).

32. ASAE 3402 *Assurance Reports on Controls at a Service Organisation*, provides for reports on controls which, if available from a service organisation used by a SMSF may be relevant to the conduct of the financial audit of that SMSF. ASAE 3402 deals with assurance engagements undertaken by an auditor to provide a report for use by user entities and their auditors, on the controls at a service organisation that provides a service to user entities that is likely to be relevant to user entities' internal controls as they relate to financial reporting. It complements ASA 402, in that reports prepared in accordance with this standard are capable of providing appropriate evidence under ASA 402. Refer further to paragraph 143-150.

Preliminary Engagement Activities

33. Prior to commencing the audit, the auditor performs a number of preliminary tasks to gain confidence that undertaking the audit is appropriate from a client and ethical point of view. ASA 300 requires the auditor, prior to beginning an audit engagement, to:

    (a) perform procedures regarding the acceptance and continuance of the client relationship and the specific audit engagement;

    (b) evaluate compliance with relevant ethical requirements relating to the audit engagement, including independence; and

    (c) establish an understanding of the terms of engagement.

These steps are outlined below.

Acceptance and Continuance Procedures

34. Under the Auditing Standards and ASAE 3000, the auditor only accepts or continues an engagement if nothing comes to the auditor's attention to indicate that the requirements of the fundamental ethical principles, the Auditing Standards and ASAE 3000 will not be satisfied.

35. For an initial audit, where there has been a change of auditor, the auditor communicates with the previous auditor in accordance with the relevant ethical requirements to ensure that there is no impediment or restriction in accepting and conducting the audit. The new auditor seeks permission from the trustees[40] to communicate with the previous auditor.

36. GS 011 *Third Party Access to Audit Working Papers* provides Example Letter E as a template for auditors to request the working papers of a predecessor auditor. There is however, no legislative requirement for successor auditors to provide access to their working papers. Their working papers remain their property and GS 009 only provides guidance in the case of voluntary co-operation.

37. Where an auditor is unable to obtain sufficient appropriate audit evidence of the fund's opening balances, they may need to limit the scope of the audit and consider varying their opinion on the financial statements – Part A qualification.

Ethical Requirements

38. In accordance with ASA 102, ASA 200 and ASAE 3000, the auditor is required to comply with relevant ethical requirements relating to audit engagements. For the purposes of GS 009 this means the Code of Ethics.[41] The fundamental principles of professional ethics comprise:

[40] See GS 011 Third Party Access to Audit Working Papers, paragraph 14.

[41] In Australia, the applicable code of ethics of the professional accounting bodies is APES 110 *Code of Ethics for Professional Accountants*, as issued from time to time by the Accounting Professional and Ethical Standards Board. This Code of Ethics has been adopted by CPA Australia, IPA and CA ANZ and is applicable to their members. Members of the Association of Taxation and Management Accountants (ATMA) are also required to conform with this code under the ATMA by-laws. Fellows of the NTAA who obtained fellowship by virtue of holding a practising certificate from one of the professional accounting bodies, will be members of one of those bodies and consequently are also required to comply with the Code of Ethics.

(a) integrity;

(b) objectivity;

(c) professional competence and due care;

(d) confidentiality; and

(e) professional behaviour.

The concept of independence is fundamental to compliance with the principles of integrity and objectivity and is mandatory[42] for auditors undertaking the audit of a SMSF.

39. Under ASA 220 and ASAE 3100, the auditor accepts an engagement only when the auditor is satisfied that they, and the engagement team if applicable, have met the relevant ethical requirements.

40. The auditor ensures that they possess, or if applicable the engagement team conducting the audit collectively possess, the appropriate capabilities, competence and time to conduct the audit in accordance with the Auditing Standards, applicable Standards on Assurance Engagements and legislative requirements. Capabilities and competence are developed through a variety of means, including professional education, training, practical experience and coaching and mentoring by more experienced staff. Under the SISA[43] the auditor is required to comply with competency standards set out by ASIC.[44] In addition, meeting the applicable competency requirements of their professional bodies will assist SMSF auditors to maintain the competence, knowledge, skills and capabilities necessary to perform SMSF audits satisfactorily.

41. Under ASA 250, the auditor obtains a general understanding of the legal and regulatory environment applicable to the SMSF. A sound and current knowledge of superannuation legislation, including the SISA and SISR, relevant taxation legislation and ATO Rulings, Determinations and Interpretative Decisions, is necessary for the auditor to meet this requirement.

Independence

42. ASA 220 requires the engagement partner to form a conclusion on compliance with the independence requirements applying to the audit engagement which are contained in the Code of Ethics. ASAE 3100 requires compliance with the fundamental ethical principles on compliance engagements, for which the concept of independence is integral. The SISA[45] and the SISR[46] require the auditor to comply with the auditor independence requirements prescribed by the Code of Ethics.[47]

43. Overall, independence requires both:

(a) independence of mind - the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional scepticism; and

(b) independence in appearance - the avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all

42 See regulation 9A.06 of the SISR.
43 See subsection 128Q of the SISA.
44 See ASIC Class Order CO 12/1687.
45 See subsection 128F (d) of the SISA.
46 See regulation 9A.06 of the SISR.
47 In addition, assurance practitioners may make reference to the Joint Accounting Bodies *Independence Guide* Fourth Edition, February 2013.

relevant information, including safeguards applied, would reasonably conclude a firm's, or a member of the engagement team's, integrity, objectivity or professional scepticism had been compromised.

44. The Code of Ethics provides a framework of principles that auditors and members of audit teams use to ensure that independence of mind and independence in appearance are not compromised.

45. When assessing independence the auditor:

(a) identifies any threats to independence;

(b) evaluates the significance of the threats; and

(c) if the threats are other than clearly insignificant, identifies and applies safeguards to eliminate or reduce the threats to an acceptable level.

46. The threats to independence in a SMSF audit engagement may include:

- Self-interest threat, which occurs when a firm or a member of the audit team could benefit from a financial interest in, or other self-interest conflict with, an audit client, for example, if the auditor, member of the audit team or their immediate family member is a trustee or member of the SMSF. This threat will also occur if the auditor or the audit firm relies on a single SMSF audit referral source for a significant amount of revenue.

- Self-review threat, which occurs when any product such as a financial report, or a judgement of a previous engagement, needs to be re-evaluated in reaching conclusions on the audit engagement so that the auditor is reviewing their own work. For example, this could occur where a member of the audit team prepared the SMSF's financial report or accounting records.

- Advocacy threat, which occurs when a firm, or member of the audit team, promotes, or may be perceived to promote, an audit client's position to the point that objectivity may be, or be perceived to be, compromised, for example, when an audit team member acts as an advocate for the SMSF in litigation.

- Familiarity threat, which is when, by virtue of a close relationship with an audit client, its directors, officers or employees, the firm or a member of the audit team becomes too sympathetic to the client's interests, for example, when a close family member of the auditor is a trustee or member of the SMSF or an employee of the SMSF's administrator or where the auditor has a long association with a trustee.

- Intimidation threat, which is when a member of the audit team is deterred from acting objectively by threats, actual or perceived, from the trustees of the SMSF or the directors, officers or employees of a related entity of a trustee or their advisors or the accountant of the trustee. This may also occur where an auditor is subject to pressure by a colleague in their own firm who has a vested interest in retaining the SMSF client because they are the SMSF's accountant or financial adviser. This might occur for example, if a threat of replacement over a disagreement with the application of an accounting principle or the loss of other general accounting or tax work or the loss of employment if the auditor's opinion is modified or an ACR is submitted to the ATO. An intimidation threat may also arise where a SMSF administrator pressures the auditor to reduce inappropriately the extent of work performed in order to reduce fees in circumstances where the administrator refers a significant number of SMSF audit clients.

47. Safeguards to independence may be:

(a) created by the profession, legislation or regulation;

(b) within the SMSF; or

(c) within the firm's own systems and procedures.

48. Safeguards created by the profession, legislation or regulation, generally include the following:

- Educational, training and experience requirements for entry into the profession;
- Continuing education requirements;
- Professional standards, monitoring and disciplinary processes;
- External review of a firm's quality control system;
- Legislation covering the independence requirements of the firm; or
- Recommendations on independence from relevant regulators.

49. Safeguards within the SMSF may be limited, as many SMSFs are small entities with limited scope for segregation of duties. Hence reliance on internal safeguards may not be possible and the auditor may rely on the safeguards created by the profession, legislation and regulation and those safeguards created by internal systems within the auditor's firm to enhance independence.

50. In evaluating threats to independence and considering applicable safeguards, the auditor considers the nature of the SMSF, the range of services provided to the audit client and the relationships the auditor and the audit team have with the SMSF's trustees, financial adviser, accountants, administrator, actuary and any other person or organisation involved with the management or operation of the SMSF.

51. If the firm's staff make management decisions for the SMSF, which may occur if the firm is providing administrative services to the SMSF, there are no safeguards available to reduce the self-review threat to an acceptably low level, other than withdrawal from either the administration or the audit engagement.

52. Assisting an audit client in the preparation of accounting records or financial reports may create a self-review threat when those records and reports are subsequently audited by the same firm. If, however, the accounting services provided are of a routine or mechanical nature, such as posting transactions and entries approved by the SMSF or preparing the financial report based on a trial balance provided by the SMSF, the self-review threat may be reduced to an acceptably low level by applying safeguards, including:

- Making arrangements that accounting services are not performed by a member of the audit team;
- Minimising internal pressures by ensuring clear guidelines protect the auditor from undue influence by others in the firm;
- Implementing policies and procedures to prohibit the individual providing such services from making any managerial decisions on behalf of the SMSF;
- Requiring the source data for the accounting entries to be originated by the SMSF;
- Requiring the underlying assumptions to be originated and approved by the SMSF;
- Obtaining the SMSF's approval for any proposed journal entries or other changes affecting the financial report;

- Obtaining the SMSF's acknowledgement of their responsibility for the accounting work performed by the firm; or

- Disclosing to the trustees the firm's involvement in both engagements.

53. Provision of taxation services to a SMSF which is also an audit client would not of itself create a threat to independence that could not be mitigated by safeguards.

54. Provision of financial advice to a SMSF which is also an audit client may create advocacy and self-review threats. These threats may be reduced to an acceptably low level by safeguards such as:

    - Implementing policies and procedures to prohibit individuals providing advice from making managerial decisions on behalf of the SMSF;

    - Using staff and partners who are not members of the audit team to provide the financial advice;

    - Minimising internal pressures by ensuring clear guidelines protect the auditor from undue influence by others in the firm; or

    - Ensuring that the individual providing the advice does not commit the SMSF to the terms of any transaction or consummate a transaction on behalf of the SMSF.

55. Where the audit firm or an individual partner is unduly reliant on the audit fees from a particular group of SMSFs, such as those SMSFs referred by a single referral source, the concern about the possibility of losing the referrals may create a self-interest, advocacy or intimidation threat. Safeguards include diversifying the client base to spread the source of revenue so that the potential for undue influence is removed. In addition, the audit firm establishes policies and procedures around engagement quality reviews.[48] These policies may include contracting of suitably qualified external persons or other firms[49] to review files prepared by the audit firm to confirm appropriate audit opinions are being issued and are supported by sufficient appropriate audit evidence that is appropriately documented.

56. Reciprocal auditing arrangements are potentially a significant threat to independence. Where two auditors conduct the audit of each other's SMSF, there are no safeguards to prevent the threat to independence. A significant threat to independence can also arise where two professional accountants who are also SMSF auditors, prepare the accounts for a number of SMSFs and enter into an arrangement to audit each other SMSFs. To reduce this threat safeguards could include ending the reciprocal arrangement or spreading these referrals to a number of different SMSF auditors.

57. Safeguards that the auditor may apply to manage other identified self-interest, advocacy, familiarity or intimidation threats to independence may include:

    - Prohibiting the holding of direct, or material indirect, financial interests by the auditor in closely held investments of the SMSF, such as a joint venture or property syndicate; or

    - Removal from the SMSF audit team any personnel with a close relationship with the trustees of the SMSF, including relatives of the trustees; or

    - Ceasing a reciprocal auditing arrangement whereby two auditors had an (exclusive) arrangement to audit each other's SMSFs; or

[48] See ASQC 1, paragraph 35.
[49] See ASQC 1, paragraph A50.

- Where you are restricted to completing the accounting work in-house and the SMSF audit function is outsourced, ensuring regular rotation of the auditor appointment. For example, having a panel of suitable SMSF auditors that have fixed term engagements for specific SMSFs and then are rotated for a fixed term, may provide a safeguard to independence.

58. In situations in which no safeguards are available to reduce the threat to an acceptable level, the only possible actions are to eliminate the activities or interest creating the threat, or to refuse to accept or continue the audit engagement.

59. Appendix 5 of this Guidance Statement provides a number of practical examples of SMSF scenarios and the threats to independence posed by those situations, as well as some appropriate safeguards which may address those threats.

Professional Judgement and Scepticism

60. ASA 200 requires the auditor to plan and perform an audit exercising professional judgement, and with an attitude of professional scepticism.

    - Professional judgement emanates typically from the auditor's expertise, experience, knowledge and training. When exercising professional judgement, the auditor maintains independence and objectivity and adopts an attitude of professional scepticism in order to achieve the audit objectives.
    - Professional scepticism requires the auditor to maintain a questioning mind as to the validity of audit evidence presented and representations of the trustees. The auditor remains alert to contradictory information or information that brings into question the validity of the evidence presented.
    - In exercising professional judgement, with an attitude of professional scepticism, auditors independently evaluate the quality of audit evidence collated throughout the course of the engagement.

Quality Control

61. Under ASA 220 and ASAE 3100, the engagement partner implements procedures to ensure quality control systems are applied to both the financial audit and compliance engagement including:

    - Taking responsibility for overall quality on the financial audit and compliance engagement;
    - Considering whether members of the engagement team have complied with relevant ethical requirements;
    - Forming a conclusion on compliance with relevant independence requirements;
    - Ensuring that requirements in relation to acceptance and continuance of client relationships and specific audit engagements have been followed and that conclusions reached are objective, appropriate and have been adequately documented;
    - Assigning audit engagement teams which possess collectively the appropriate capabilities, competence and time to perform the engagements in accordance with AUASB Standards and regulatory and legal requirements;
    - Directing, supervising and performing the audit engagement in accordance with AUASB Standards and regulatory and legal requirements;

- Issuing an auditor's report that is appropriate in the circumstances and supported by sufficient appropriate audit evidence that is appropriately documented;
- Consulting appropriately on difficult or contentious matters both within the engagement team and with others within or outside the firm, and documenting and implementing agreed conclusions; or
- Monitoring quality adequately against firm and professional standards, including the Auditing Standards and ASAEs.

Agree the Terms of Engagement

62. Under ASA 210, the auditor is required to agree the terms of the audit engagement in writing with the SMSF trustees prior to conducting the audit. This is usually in the form of an engagement letter to the trustees. ASA 210 provides guidance on the principal contents of an engagement letter.

63. The trustees are required to appoint the auditor at least 45 days prior to the date that the SMSF annual return is due to be lodged.[50] Either the trustees may be involved in the selection and appointment of the auditor or the SMSF's accountants, administrators or financial planners may assist with the sourcing and recruitment of an auditor for the SMSF. In either case, the trustees approve the appointment in writing before the audit commences, usually by signing the engagement letter and indicating their approval in a trustee minute. The engagement letter is between the auditor and the trustees of the SMSF and not the auditor and the party referring the engagement such as the accountant or administrator.

64. For a SMSF audit engagement, the engagement letter ordinarily:

- Describes the objective and scope of the financial audit and compliance engagement, including the sections and regulations of SISA and SISR against which the auditor will be reporting;
- Identifies the responsibilities of the auditor;
- Identifies the responsibilities of the trustees, including:
  - Establishing and maintaining an adequate internal control structure;
  - Preparing the SMSF's financial report;
  - Keeping the records of the SMSF secure and for the statutory time periods;
  - Conducting the affairs of the SMSF in compliance with all relevant provisions of SISA, SISR and the fund's governing rules throughout the year.
- Sets out the reporting requirements of the auditor, including those imposed by sections 129 and 130 of the SISA; and
- Includes a notice to the trustees that the audit records and auditor's work may be subject to review by the professional body of which the auditor is a member, ASIC or the ATO.

65. ASA 210 does not require engagement letters to be issued every year. However, on recurring audits, the auditor considers whether it is appropriate to confirm the terms of the engagement in writing due to the circumstances of the engagement, including when there is:

50 Requirement under regulation 8.02A of the SISR for appointments after 1 July 2013.

- A revision of the terms of the engagement;
- An indication that the trustees misunderstand the objective and scope of the audit;
- A change in trustees;
- A significant change in the nature or size of the SMSF; or
- Significant changes in the SISA, SISR or other regulatory requirements, such as changes to the requirements to be reported on in the approved form auditor's report or ACR.

66. An example engagement letter is attached as Appendix 1 of this Guidance Statement.

Planning

67. Planning an audit involves a number of closely related procedures which include:

- Establishing the overall audit strategy for the audit;
- Developing and documenting an audit plan in order to reduce audit risk and compliance engagement risk to an acceptably low level;
- Updating the audit strategy and the audit plan during the course of the audit; and
- Planning the nature, timing and extent of direction and supervision of engagement team members and review of their work.

68. The auditor plans the financial audit and compliance engagement so that they may be conducted in an effective manner in order to reduce audit risk and compliance engagement risk to an acceptably low level.

69. Adequate planning:

- Ensures appropriate attention to important areas of the audit engagement;
- Identifies potential problems on a timely basis;
- Assists in the proper organisation and management of the audit engagement in order for it to be performed in an effective manner;
- Assists the auditor in assigning work properly to audit team members, and facilitates the direction, supervision and review of the team's work; and
- Assists, where applicable, in the coordination of work performed by other auditors, actuaries and experts.

70. The nature, timing and extent of planning activities will vary according to:

- The size, structure and complexity of the SMSF;
- Whether the SMSF contravened the SISA or SISR in prior years;
- Whether the SMSF is an accumulation fund or a pension fund or a combination of both;
- The level of trustee involvement and knowledge of the operations of the SMSF;
- Whether the SMSF is self-administered or administered by a third party service organisation;

- The nature and range of investments held and whether the SMSF uses the services of an advisor for investment advice;
- The availability of service auditor's reports for services provided by service organisations;
- Whether the employer-sponsor is also a client of the firm preparing the accounts or of the auditor; and
- The auditor's previous experience, if any, with the SMSF.

71. An annual review of the audit plan is necessary to ensure that it is updated to reflect the current circumstances of the SMSF and any changes in legislation that may affect the SMSF.

Overall Audit Strategy

72. Under ASA 300, the auditor is required to establish the overall audit strategy for the financial audit and this is mirrored in the guidance in ASAE 3100 for the compliance engagement. The overall audit strategy sets the scope, emphasis, timing, direction and conduct of the audit, including the resources required for the audit and supervision of the audit team. The audit strategy is based on the results of the preliminary work performed and the auditor's experience gained on any previous audit engagements with the SMSF.

73. The complexity of the audit strategy will vary with the size, nature and complexity of the SMSF.[51] The strategy guides the development of the more detailed audit plan for the nature, timing and extent of evidence gathering procedures to be performed and the reasons for selecting them.

74. In conducting a SMSF audit, the auditor obtains a preliminary understanding of the SMSF, including the SMSF's trust structure, nature of its investments and administration, the parties involved in the management and trusteeship of the SMSF and related parties of the trustees and members.

75. In gaining this preliminary understanding of the SMSF, the auditor reviews the fund's current governing rules to verify whether:

    (a) The fund's governing rules were properly executed;

    (b) The SMSF has current and appropriately empowered trustees;

    (c) The SMSF was established with either a corporate trustee or individual trustees under the pension powers;

    (d) The fund's governing rules comply with or have a mechanism to comply with the SISA and SISR and changes thereto; and

    (e) The SMSF has powers to accept contributions and pay benefits, in the form permitted by the SISA and SISR.

76. The covenants in subsection 52B(2) and 52C(2) of the SISA are deemed to be included in the governing rules, even if they are not specifically included. A list of considerations in examining the SMSF's governing rules is included in Appendix 3 Self-Managed Superannuation Fund Governing Rules Preliminary Understanding Checklist.

77. It is possible for the fund's governing rules to be more restrictive than the SISA and SISR and prohibit or limit the trustees' actions or powers. However, even if the fund's governing rules

[51] ASA 300 provides guidance on establishing the audit strategy for smaller entities.

are more expansive than the SISA and SISR, the trustees must ensure they still comply with the requirements of the SISA and SISR.

The Audit Plan

78. The audit plan documents the detailed implementation of the overall audit strategy. ASA 300 requires the auditor to develop and document the audit plan to record the key decisions and the nature, timing and extent of risk assessment procedures to be undertaken. The form and extent of the audit plan depends on the complexity of the SMSF and the circumstances of the specific audit engagement. The audit plan documents the procedures proposed to be undertaken at the assertion level and evidences work performed to facilitate proper review, supervision of the audit team and any external quality review.

79. The audit plan is dynamic and is required to be updated if necessary during the course of the audit. Audit evidence obtained may trigger a revision of the initial risk assessment and a need for further audit procedures, which are documented accordingly.

80. Often, the audit plan for a SMSF takes the form of a template which can be used to assist in maintaining quality control for the engagement as required by ASA 220. Standardised templates need to be tailored specifically to reflect the requirements of the SISA and SISR, the particular circumstances and nature of the SMSF and the audit evidence available.

81. The audit plan encompasses financial audit procedures, such as the illustrative financial audit procedures listed in Appendix 4 of this Guidance Statement, as well as compliance procedures.[52]

Risk Assessment Procedures

82. The auditor obtains a sufficient understanding of the SMSF and its environment, including its internal control, to identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, and the risk of non-compliance with the specified requirements of the SISA and SISR, in order to design and perform further audit procedures. The risk assessment for the financial audit includes identifying and assessing risks at the financial report level and at the assertion level for classes of transactions, account balances and disclosures, as required by ASA 330.

83. Under ASA 315, the auditor is required to examine the internal controls of the SMSF. ASAE 3100 requires the auditor to document the key elements of the compliance framework, such as procedures for identifying, assessing and reporting compliance incidents and breaches. Given the nature of a SMSF, it is possible that there may be limited reliable internal controls on which the auditor may rely. Even if the auditor considers that a fully substantive audit approach is appropriate, the auditor is still expected, under ASA 230, to document their consideration of the internal control environment.

84. Under ASA 250, the auditor is required to consider whether the SMSF has breached the SISA or SISR previously and whether there are any outstanding correspondence or unresolved issues with the ATO. Any such matters identified will impact on the risk assessment and the auditor's assessment of the compliance framework.

85. SMSFs are often small entities, with a close and related membership where all trustees or directors of the corporate trustee may be equally responsible for managing the fund and making decisions. There may be little or no opportunity for implementing segregation of duties between trustees. Consequently, the auditor may assess the SMSF's internal control environment and compliance framework as ineffective, in which case the auditor will be unable to rely on the effectiveness of the internal controls to reduce the level of substantive

52 Auditor guidance and information is available on the ATO website at https://www.ato.gov.au/Super/Self-managed-super-funds/SMSF-auditors including the ATO's electronic SMSF audit tool (eSAT), for use in conducting the compliance engagement.

testing. As a result, the auditor would design and perform further audit procedures which are entirely substantive procedures. If the administration of the SMSF is outsourced, the auditor evaluates the controls prevailing at the administrator.

Use of Technology

86. Initial risk assessment and audit planning includes determining the method of data collection used by the party preparing the financial report for the SMSF. It is more common to see the use of technology for data management and transfer and this can influence the risk assessment undertaken by the SMSF auditor.

87. Traditionally, the primary source document for SMSF account preparation was the bank statement and individual transactions were manually loaded into accounting software (including excel) for the report preparation. Inherent risks in this approach included the risk of compromised bank statements and therefore the auditor would normally obtain direct confirmation from the bank in the audit planning phase. Today it is more common for cash transaction data to be sourced via data feeds which is the transmission of information between the financial institution directly into the software of the report preparer. Data feeds are also being used to obtain information from share brokers, WRAP accounts, and term deposit providers.

88. Where the data feeds are utilised via a "direct-connect" process – end to end encrypted link over a point to point connection – the ability to intercept or manipulate the data is removed as the information comes directly from a financial institution into the software of the party preparing the annual compliance report. If an ASAE 3402 Type 2 report has been obtained, this process of data transfer does not represent any additional risks to the SMSF audit process. It however does not change the need for the audit planning to encompass an assessment of the inherent risks associated with the transactional data being held by a service organisation provider such as an IDPS operator.

89. Where data feeds are prepared via an aggregator - "scrapped data feeds" - there is no guarantee of data integrity. Under this process, the original data is sent via an email and, even if encrypted, there is the potential for transcription errors. There is also no guarantee of the integrity of the email or that it has not been intercepted. Errors encountered during the "scrapping" process require manual intervention to correct and therefore reduces the integrity of the final data.

90. Additional testing may be required for the audit of a SMSF that utilises this data transfer process for the preparation of the annual compliance report and is normally undertaken in the audit planning phase.

91. Extra consideration may be necessary where the party preparing the financial report utilises manual file imports from financial institutions and the integrity of the information cannot be relied on.

Materiality

92. ASA 320 requires the auditor to consider performance materiality[53] when determining the nature, timing and extent of financial audit procedures and ASA 450 requires the auditor to consider materiality when evaluating the effect of misstatements identified during the audit. Similarly, under ASAE 3100, the auditor considers materiality when planning and performing the compliance engagement and in assessing any compliance breaches identified. Information is material if its omission, misstatement or non-disclosure has the potential to adversely affect decisions made by users of the report. An auditor's consideration of materiality is a matter of

53 Performance materiality refers to the amount or amounts set by the auditor at less than materiality for the financial report as a whole to reduce to an appropriate low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial report as a whole. Performance materiality may also refer to the amount or amounts set by the auditor for particular classes of transactions, account balances or disclosures.

professional judgement, and is affected by the auditor's perception of the information needs of users and the level of audit risk.

93. The auditor's preliminary assessment of materiality is based on qualitative and quantitative factors. Similarly, when assessing the outcome of audit procedures, including the materiality of misstatements identified in the financial audit or contraventions identified in the compliance engagement, the auditor considers both their amount (quantitative) and nature (qualitative).

94. Materiality differs in nature between a financial audit and a compliance engagement and is discussed separately within both Part A (paragraphs 174 to 177) and Part B (paragraphs 324 to 325) respectively of this Guidance Statement.

Audit Evidence

95. The results of the risk assessment procedures enable the auditor to design and perform further audit procedures to respond to the assessed risks for the compliance engagement and financial audit. The auditor determines the nature, timing and extent of audit procedures to be performed, which may be either tests of controls or substantive procedures.

96. ASA 500 and ASAE 3100 require the auditor in the conduct of the financial audit and compliance engagement to obtain sufficient appropriate audit evidence with which to base the auditor's opinion. Sufficiency is the measure of the quantity of evidence, which is affected by the risk of misstatement, the higher the risk the more evidence is likely to be required. Appropriateness is the measure of the quality of evidence, that is, its relevance and its reliability, the higher the quality the less evidence may be required. The auditor considers the relationship between the cost of obtaining evidence and the usefulness of the information obtained. However, the degree of difficulty or expense involved is not in itself a valid basis for omitting an evidence gathering procedure for which there is no alternative. The auditor uses professional judgement and exercises professional scepticism in evaluating the quantity and quality of evidence, and thus its sufficiency and appropriateness, in supporting the audit opinion.

97. Audit evidence means all the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based, and includes the information contained in the accounting records underlying the financial report and other information. For a SMSF this may include:

- Financial reports of investment entities such as closely held unlisted trusts or private companies;
- Limited recourse borrowing arrangement substantiation – loan contract, holding trust details, extracts of bank statement showing transactions related to the arrangement (e.g payment of the initial deposit and subsequent loan repayments);
- Where real property held by the SMSF, evidence of the title including the title conveyance on purchase by the SMSF, a copy of the lease agreement, in the case of residential property, evidence the tenant is not a 'related party', substantiation of the expenses related to the holding of the property by the SMSF, sufficient evidence of the rental receipts and general adherence to the terms of the lease agreement;
- Copies of advice received by the trustee where it is relevant to the SMSF's financial position;
- Asset substantiation which may include, holding statements, certificate of title, bank statements, Annual Tax Statement issued by a WRAP provider;
- Income and expense substantiation including the sampling methodology used (if not a 100% sample size);

- Bank statements – opening and closing statements as well as any other statements to evidence transactions that are “lumpy”, unusual, include the purchase or sale of assets, the receipt or payment of material transactions, or other transactions that may not have been substantiated elsewhere;
- Trustee minutes, the trustee representation letter, and any other relevant correspondence;

98. Audit evidence, which is cumulative in nature, includes evidence obtained from audit procedures performed during the course of the audit and may include evidence obtained from previous audits and other sources. Audit evidence may be held in paper and electronic form and must be able to be provided efficiently and comprehensively to provide the details of the conduct of the audit and how the auditor formed their opinion. Audit evidence is generally more reliable when:

- Obtained from an independent source;
- Obtained directly by the auditor;
- In documentary form;
- It comprises original documents; or
- Received directly by the auditor, rather than passed through other parties, especially considering the limited segregation of duties and internal controls that is often found in a SMSF.

99. A SMSF audit rarely involves the authentication of documentation, nor is the auditor trained as, or expected to be, an expert in such authentication. However, ASA 500 and ASAE 3000 require the auditor to consider the reliability of the information to be used as evidence, for example photocopies, facsimiles, filmed, digitised or other electronic documents which are easily altered, including consideration of controls over their preparation and maintenance where relevant. The auditor remains aware of the potential for fraud in the presentation of audit evidence. If an auditor is aware, or suspects, that any documentation has been altered or differs from expected results, then further audit procedures are applied.

100. Obtaining a *Bank Confirmation* is an effective method to obtain assurance about the existence, title and value of the cash holdings, as well as to determine whether the SMSF cash assets are subject to any form of lien or encumbrance. GS 016 *Bank Confirmation Requests* provides guidance to auditors on the enquiry and confirmation methods for obtaining audit evidence regarding bank accounts and transactions.

101. A bank confirmation certificate will not however provide sufficient appropriate audit evidence of the transactions that occurred during the income year under audit. The audit file should also contain a copy of the bank reconciliation, the analytical review of the cash balances along with evidence of the various transaction testing undertaken.

102. As an alternate method of obtaining independent information regarding the cash transactions, the auditor may request the SMSF Trustee to request the financial institution to provide copies of the bank statements at the same time as they are issued to the trustee. This can be done through the SMSF’s internet banking whereby the auditor has a personalised log-in that allows access to the SMSF bank accounts only.

103. If the SMSF only obtains paper statements, the Trustee may request the bank to issue duplicates to the auditor however, this may create a records management issue over time.

Data-feeds and audit evidence

104. The use of data feeds for information transfer presents additional audit considerations regarding the appropriateness of the audit evidence used as the basis for the auditor’s opinion.

105. "Direct-connect" transmission – end to end encrypted link over a point to point connection – is the most secure data feed process as the ability to intercept or manipulate the data is removed. There is however some likelihood that the auditor may encounter processing errors. It is important therefore that the auditor understand the control environment that is supporting the data feed process. The auditor would normally request a "Type 2" Audit Report to provide evidence of the effectiveness of the control environment to prevent material misstatement of the financial report. If no report exists, the auditor may need to consider additional testing to determine the reliability of the information provided. Where data feeds are prepared via an aggregator - "scrapped data feeds" - there is no guarantee of data integrity.. The auditor considers conducting their own testing of the information collected via this form of data feed to ensure that sufficient appropriate audit evidence is included in the audit file.

106. Consideration may be necessary where the party preparing the financial report utilises manual file imports from financial institutions and the integrity of the information cannot be relied on by the auditor.

107. In determining whether or not to rely on electronically generated or stored audit evidence, the auditor exercises professional judgement in considering the reliability of that evidence. The auditor considers the requirements of the Auditing Standards particularly ASA 200, ASA 315 and ASA 500, and may consider the guidance contained in paragraphs 82 to 86 above.

108. ASA 500 provides guidance on the substantive audit procedures which the auditor may conduct to collect appropriate evidence, which include:

- Inspection of records or documents;
- Inspection of tangible assets;
- Observation;
- Enquiry;
- Confirmation;
- Recalculation;
- Reperformance; or
- Analytical review.

109. ASA 530 *Audit Sampling and Other Means of Testing* requires the auditor to determine the appropriate means for selecting items for testing. Due to the specific nature of SMSFs and limited internal control environment, the auditor ordinarily relies on a highly substantive method of testing. This may involve examining the entire population of items that make up a class of transactions or account balance, when the population constitutes a small number of large value items or when there is a significant level of risk and other audit procedures do not provide sufficient appropriate audit evidence.

Inspection of Records or Documents

110. Inspection of records or documents consists of examining records or documents, whether internal or external, in paper form, electronic form, or other media. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

111. Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a share or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value and further

audit evidence is sought. In addition, inspecting an executed contract may provide audit evidence relevant to the SMSF's application of accounting policies, such as revenue recognition.

Inspection of Tangible Assets

112. Inspection of tangible assets consists of physical examination of the assets. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the SMSF's rights and obligations or the valuation of the assets.

Observation

113. Observation consists of watching a process or procedure being performed by others. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place and by the fact that the act of being observed may affect how the process or procedure is performed.

Enquiry

114. Enquiry consists of seeking financial or non-financial information from knowledgeable persons, either within the SMSF or outside the SMSF. Enquiry is an audit procedure that is used extensively throughout the audit and often is complementary to performing other audit procedures. Enquiries may range from formal written enquiries to informal oral enquiries. Evaluating responses to enquiries is an integral part of the enquiry process.

115. Responses received to enquiries may provide the auditor with information not previously possessed or with corroborative audit evidence supporting the audit opinion. Alternatively, responses to enquiries may provide information that differs significantly from other information that the auditor has obtained. In all cases, the auditor evaluates the responses received to enquiries to assess whether there is a need to modify or perform additional audit procedures to support the audit opinion.

116. Enquiry alone ordinarily does not provide sufficient audit evidence to detect a material misstatement at the assertion level, nor sufficient evidence of the operating effectiveness of controls, therefore the auditor performs further audit procedures to obtain sufficient appropriate audit evidence.

117. The auditor obtains written representations from the trustees to confirm responses to oral enquiries on material matters when other sufficient appropriate audit evidence cannot reasonably be expected to exist or when the other audit evidence obtained is of a lower quality.[54]

Confirmation

118. Confirmation, which is a specific type of enquiry, is the process of obtaining a representation of an existing condition or information directly from a third party. For example, the auditor may seek direct confirmation of cash balances with the SMSF's bank. Confirmations are frequently used in relation to bank account and investment account balances and their components.[55]

Recalculation

119. Recalculation consists of checking the mathematical accuracy of documents, records or account balances. Recalculation may be performed electronically, for example through the use of data analytics to check the accuracy of the summarisation of the electronic accounts, or

[54] See ASA 580 for further requirements and explanatory guidance on written representations.
[55] See ASA 505 for further requirements and explanatory guidance on confirmations.

manually, for example to recalculate account balances from primary documentation to validate the balance.

Re-performance

120. Re-performance is the auditor's independent execution of procedures and controls that were originally performed as part of the SMSF's operations, for example re-performing the calculation of market movement for a range of listed securities. Re-performance may be conducted either manually or through the use of data analytics.

Analytical Procedures

121. Under ASA 520, the auditor is required to apply analytical procedures as risk assessment procedures in understanding the SMSF and its environment and in the overall review at the end of the audit.

122. Analytical procedures may be utilised to compare and contrast how the SMSF has performed over two or more consecutive reporting periods. Common analytical procedures include comparing balances, calculating ratios and trend analysis. Major variations, inconsistencies or other deviations may warrant further investigation particularly where the difference is not easily understood, not explained sufficiently by the trustees or deviates from predicted amounts.

123. Ordinarily, an auditor considers the movement in the member balances from one period to another in the preliminary planning phase of the audit. This process identifies the movement in the balance from contributions and investment earnings as well as any reduction in balances due to benefit payments or expenses such as fees, charges or insurance premiums deducted. The auditor uses analytical review to assess whether the member balances are reasonable given the overall circumstances of the SMSF.

Audit Documentation

124. ASA 230 and ASAE 3100 require the auditor to prepare, on a timely basis, audit documentation that is sufficient and appropriate to provide:

    (a) a basis for the auditor's report; and

    (b) evidence that the audit was performed in accordance with Auditing Standards, ASAEs and applicable legal and regulatory requirements.

125. Preparing sufficient appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalised. Documentation prepared at the time the work is performed is likely to be more accurate than documentation prepared subsequently.

126. In assessing the extent of documentation, the auditor considers what audit documentation is necessary to enable an experienced auditor, having no previous connection with the audit, to understand:

    (a) the nature, timing, and extent of the audit procedures performed to comply with Auditing Standards, applicable ASAEs and applicable legal and regulatory requirements;

    (b) the results of the audit procedures and the audit evidence obtained; and

    (c) significant matters arising during the audit and the conclusions reached thereon.

127. The form, content and extent of audit documentation depend on factors such as:

- The nature of the audit procedures to be performed;
- The identified risks of material misstatement;
- The extent of judgement required in performing the work and evaluating the results;
- The significance of the audit evidence obtained;
- The nature and extent of exceptions identified;
- The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained; and
- The audit methodology and tools used.

It is, however generally neither necessary nor practicable to document every matter the auditor considers during the audit.

Nature of Documentation

128. Audit documentation may be recorded on paper, electronically or on other media. It includes, for example, audit programs, analyses, records of audit testing and results of that testing, issues memoranda, summaries of significant matters, letters of confirmation and representation, checklists, and correspondence (including email) concerning significant matters. Abstracts or copies of the SMSF's records, for example, significant and specific contracts and agreements, may be included as part of audit documentation if considered appropriate. Checklists and audit work programs without supporting audit evidence are not considered to be appropriate audit evidence.

129. Oral explanations to the auditor, on their own, do not represent adequate support for the work the auditor performed or conclusions the auditor reached, but may be used to explain or clarify information contained in the audit documentation. It is essential for the auditor to collate and retain an audit file containing the audit documentation. Even though SMSF audits are not conducted under the Corporations Act 2001, the retention period for audit working papers is generally accepted to be at least seven years[56] after the date the audit report is signed.

130. ASA 230 requires the auditor in documenting the nature, timing and extent of audit procedures to record by whom and when the audit work was performed and, if applicable, who reviewed the audit work and the extent of the review.

131. The auditor completes the assembly of the final audit file on a timely basis after the date of the auditor's report. This facilitates justification and verification that appropriate audit procedures were performed in the audit. Quality reviews, internal and external, are able to be performed more quickly and efficiently if a file is constructed in an orderly and logical manner.

132. Under ASA 230, the auditor is required to adopt appropriate procedures for maintaining the confidentiality, safe custody, integrity, accessibility and retrievability of audit documentation.

Significant Matters

133. The auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (sometimes known as a completion memorandum) that describes the significant matters identified during the audit and how they were addressed, or that includes cross-references to other relevant supporting audit documentation that provides such information. Such a summary may facilitate effective and efficient reviews and inspections of the audit documentation. The preparation of such a summary may assist the auditor's

[56] See section 307B of the *Corporations Act 2001*.

consideration of the significant matters. In addition, ASIC's competency standards[57] require the auditor to prepare a summary of findings relating to both compliance matters and matters relating to the financial report for each SMSF audit.

134. Judging the significance of a matter requires an objective analysis of the facts and circumstances of the situation. Significant matters include:

- Matters that give rise to significant risks (as defined in ASA 315);
- Results of audit procedures indicating that the financial information could be materially misstated; or a need to revise the auditor's previous assessment of the risks of material misstatement and the auditor's responses to those risks;
- Circumstances that cause the auditor significant difficulty in applying necessary audit procedures; and
- Findings that could result in a modification to the auditor's report.

135. If the auditor identifies information that contradicts or is inconsistent with the auditor's final conclusion regarding a significant matter, the auditor documents how the contradiction or inconsistency has been addressed in forming the auditor's final opinion.

Representations

136. Under ASA 580 and ASAE 3100, the auditor seeks written representations from the trustees regarding financial and compliance matters. These written representations are generally in the form of a representation letter which may confirm both verbal representations made during the course of the audit as well as other matters requiring written confirmation. The *Trustee Representation Letter* is ordinarily obtained as primary audit evidence prior to the audit report being issued. Appendix 2 provides an example *Trustee Representation Letter*.

In instances where the auditor's contact with the trustees is limited, and may only be at the conclusion of the engagement, in the interests of having a more efficient audit approach the auditor may consider obtaining certain confirmations from the trustees at the planning stage of the engagement, for example, eligibility of trustees, safe-guarding of assets and fraud.

137. With respect to the financial audit of a SMSF, under ASA 580, the auditor obtains written representations from the trustees, including that they:

- Acknowledge responsibility for the selection of the applicable financial reporting framework and for the fair presentation of the financial report in accordance with the adopted applicable financial reporting framework;
- Have approved the financial report;
- Confirm specified matters material to the financial report, when other sufficient appropriate audit evidence cannot reasonably be expected to exist;
- Acknowledge their responsibility for the design and implementation of internal control to prevent and detect error; and
- Believe the effect of uncorrected misstatements aggregated by the auditor is immaterial, both individually and in aggregate, to the financial report.

138. The auditor may also seek representations under ASAE 3100, with respect to the compliance engagement, that the trustees:

[57] See ASIC Class Order 12/1687, paragraph 48.

- Confirm specified matters material to the compliance engagement; and
- Have conducted the affairs of the SMSF in compliance with the SISA, SISR and other relevant legislation throughout the period.

139. Upon receipt of a written representation, the auditor evaluates the representation for reasonableness against other audit evidence collected and the knowledge of the individual making the representation and, where possible, obtains corroborative evidence.

140. Representations by the trustees cannot replace other evidence the auditor could reasonably expect to be available. An inability to obtain sufficient appropriate evidence regarding a matter that has, or may have, a material effect on the financial report or evaluation or measurement of the subject matter, when such evidence would ordinarily be available, constitutes a limitation on the scope of the audit, even if a representation from the responsible party has been received on the matter. In such circumstances, ASA 705 and ASAE 3100 require the auditor to express a qualified opinion or a disclaimer of opinion.

141. An example trustee representation letter which covers both the financial audit and compliance engagement is included as Appendix 2 of this Guidance Statement.

Service Organisations

142. SMSFs may use service organisations to provide investment management services including:

- Custody (including investor directed portfolio services (IDPS) such as WRAP accounts);
- Asset management (including Hedge fund management and Private Equity).
- Property management;
- Investment administration, including fund accounting and/or fund administration;
- Registry; and
- Valuation services.

These investment management services may take various forms including WRAP[58] accounts, individually managed portfolio services, individual mandates or platform investments. Further guidance is provided in GS 007 *Audit Implications of the Use of Service Organisations for Investment Management Services*.

143. The use of a service organisation may provide the opportunity to reduce substantive testing for balances and transactions maintained by the service organisation. ASA 402 provides some relief stating that in the absence of obtaining a direct understanding of the internal control environment of a service entity, the auditor should obtain a ‘Type 1’ or ‘Type 2’ Audit Report. ASAE 3402 provides detailed requirements and guidance on the preparation of these audit reports.

Type 1 or Type 2 report

144. A Type 1 Report provides an opinion of effectiveness of the service organisation’s internal control environment as described by the service entity’s management and cannot be relied on to reduce the level of substantive audit testing conducted by the SMSF auditor. The value of a

[58] A “WRAP” or “Wrap Service” is an administrative and reporting service whereby investments are consolidated, managed and held by a custodian. WRAPS combine reporting on investments including bank accounts, listed securities, corporate actions and managed funds which are held within the portfolio.

Type 1 report is limited to planning the audit, assessing the risk of material misstatement, and designing further audit procedures.

145. A Type 2 Report includes the service auditor's opinion on the management's description of the control environment after tests of the controls are undertaken and, therefore, may be able to be used to reduce the level of substantive testing undertaken by the SMSF auditor.

146. The extent of the reliance able to be placed on a service auditor's report provided in conjunction with a service entity's Annual Investor Statement (Tax Report) is determined after a review of the assertions made relevant to information contained in the report. For example, does the audit report limit the scope of the service auditor? Some reports only cover existence rights and obligations, which would require the fund auditor to test for valuation. In these instances, the auditor may partially rely on the service auditor's report and would consider conducting testing to obtain assurance on the valuations contained in the Tax Report. Where the fund uses a custodian but the custodian does not engage an independent auditor to issue a ASAE 3402 report on the investments, the fund auditor may not limit the scope of their audit. Additional procedures may be required for investment, income, expenses and tax information included in the custodian's report.

147. A Type 2 Report can be relied on to the extent the SMSF auditor can map the tests of controls against the assertions in the service provider's audit report. SMSF auditors ensure that any report issued is in compliance with ASAE 3402 requirements otherwise further procedures and evidence may be required. Greater consideration may be necessary if the service provider operates overseas.

148. The use of a service organisation by a SMSF may render the audit evidence required less readily accessible to the auditor, if the service organisation provides some of the record keeping or compliance functions of the SMSF.

149. Nevertheless, location of audit evidence at the service organisation does not alter the overall scope and objective of the financial audit and compliance engagement of the SMSF. Therefore, it remains the responsibility of the auditor to obtain sufficient appropriate audit evidence to support the auditor's financial audit and compliance assurance opinions. The requirements of the AUASB Standards relating to obtaining sufficient appropriate evidence on which to form an opinion are the same as would apply if the records and supporting documentation were maintained by the SMSF.

150. Operators of IDPSs[59] and IDPS-like services are required by CO 13/762[60] or CO 13/763[61] to obtain an auditor's report providing:

(a) an opinion as to whether the internal controls and other procedures of the relevant IDPS or IDPS-like operator and other persons acting on behalf of the relevant operator were suitably designed and operated effectively in all material respects to ensure that the annual investor statements, quarterly reports and any information that is made accessible electronically, are not materially misstated; and

(b) an opinion as to whether the aggregate of assets, liabilities, revenue and expenses in the annual investor statement for the relevant IDPS or IDPS-like financial year have

[59] "IDPS" means an investor directed portfolio service, consisting of a number of functions including a custody, settlement and reporting system and service. The clients of the service have the sole discretion to decide what assets will be acquired or disposed of. The service is provided in such a way that clients are led to expect, and are likely to receive, benefits in the form of access to investments that the client could not otherwise access directly or cost reductions by using assets contributed by the client or derived directly or indirectly from assets contributed by the client with assets contributed by other clients or derived directly or indirectly from assets contributed by other clients.[60] See ASIC Class Order 13/762 *Investor Directed Portfolio-like Services provided through a registered managed investment Scheme.*

[60] See ASIC Class Order 13/762 *Investor Directed Portfolio-like Services provided through a registered managed investment Scheme.*

[61] See ASIC Class Order 13/763 *Investor Directed Portfolio Services*.[62] See Section 295-390 of the ITAA 1997.

been properly reconciled in all material respects to the corresponding amounts shown in the reports prepared by the custodian which have been independently audited; and

(c) a statement as to whether or not the auditor has any reason to believe that any annual investor statements, quarterly reports or information accessible electronically is materially misstated.

151. ASIC's Regulatory Guide RG 148 *Platforms that are managed investment schemes and nominee and custody services* details the requirements of CO 13/762 and CO 13/763:

(a) RG 148 stipulates the requirement for IDPS operators to maintain, document and comply with adequate internal control procedures to ensure compliance with financial services laws and to have the procedures audited annually by a registered company auditor.

(b) RG 148.126 to 148.133 details the requirement to provide an annual investor statement and audit report within 3 months of the end of the financial year. The audit report must set out whether the auditor has reason to believe that the investment statements have been given without material misstatement and their opinion on whether the annual investor's statements have been properly reconciled.

(c) Assets held under custody are held as a single holding in the name of the Custodian. Individual investors hold a specified number of units which determine the value of the individual holding. An annual independent audit of the IDPS is required to provide assurance on the reconciliation of the attribution to individual investors. An SMSF audit considers the independent audit of the Custodian.

Reports provided under these class orders may provide sufficient appropriate audit evidence for a user auditor.

Using the Work of a Service Auditor

152. In relying on the work of a service organisation's auditor under ASA 402, the auditor considers the professional competence of the service auditor in the context of the specific assignment and assesses whether the work of the service auditor is adequate for the SMSF auditor's purposes.

153. In assessing professional competence of the service auditor, the auditor may gain some comfort from the other auditor having membership of a professional accounting body or affiliation with a reputable accounting firm.

154. With respect to the appropriateness of the service auditor's work, the auditor considers whether:

(a) controls, balances, transactions or compliance with requirements relevant to the SMSF have been audited;

(b) an audit opinion, providing reasonable assurance, or a review conclusion, providing limited assurance, has been provided; and

(c) the service auditor's report contains any modifications which may impact the audit of the SMSF.

155. In general, it is likely to be cost prohibitive for a SMSF auditor to obtain direct assurance of an IDPS control environment and therefore reliance on the CO 13/763 Audit Report and applying professional judgment, to determine an appropriate risk rating for the SMSF audit. The risk rating for the audit determines the level of testing required for individual financial statement entries such as; contributions, payments to members, investment purchases and sales as well

as the size of the sample for testing asset valuation, particularly the larger positions reported on the Investor Annual Report.

156. Where the SMSF auditor is unable to obtain sufficient appropriate audit evidence as all records are held at the service organisation, they ordinarily consider whether it appropriate to disclaim an opinion, or even express a qualified opinion if the possible effects are material or pervasive.

Using the Work of an Expert

157. Some SMSF audit engagements may include aspects requiring specialised knowledge and skills in the collection and evaluation of sufficient appropriate audit evidence. In these situations, the auditor may decide to use the work of an expert who has the required knowledge and skills to assist the auditor, such as property valuers, actuaries, legal professionals or other professionals. Either the auditor or the trustee may engage the required expert. ASA 620 applies for an auditor's expert, while GS 005 *Using the Work of a Management's Expert* provides guidance on using the work of a management's expert (an expert engaged by, or on behalf of, the trustees).

158. When using the work of a management's expert, ASA 500 paragraph 8 and ASAE 3100 require the auditor to obtain sufficient appropriate evidence that the expert's work is adequate for the purposes of the audit. In doing so, the auditor evaluates:

    (a) the competence, capabilities and objectivity of the expert;

    (b) whether the scope of the expert's work is adequate for the purposes of the audit, including the reasonableness of the assumptions, method and source data used by the expert; and

    (c) the appropriateness of the expert's work as audit evidence, including the reasonableness and significance of the expert's findings in relation to the audit of the SMSF.

Using the Work of a Management's Expert

159. Actuaries and valuers are experts generally appointed by the trustees (a management's expert) to provide market valuations, actuarial valuations and certificates required by the SISA, SISR or the ITAA. The auditor applies the requirements of ASA 500 paragraph 8 and ASAE 3100 and refers to Guidance Statement GS 005 for guidance on using the expert's work as audit evidence.

160. The trustees are required to obtain annually, an actuarial certificate for funds with members in both pension and accumulation phases, where the assets are un-segregated, covering the proportion of income which is tax exempt.[62] Actuarial certificates will also be required if the fund pays a pension that is not prescribed under the SISR. Actuarial certificates are not required for accumulation funds paying pensions with segregated assets if the assets are segregated for the entire year of income.

161. Since 1 July 2017, SMSFs that are classified as having *disregarded small fund assets*[63], are required to use the proportionate method for exempt pension income calculation, regardless of if the fund is 100% in the retirement phase.

    (a) A SMSF has disregarded small fund assets if at least one fund member has a retirement phase income stream and:

[62] See Section 295-390 of the ITAA 1997.
[63] Section 295-387 ITAA 1997

(i) a fund member has a total super balance of at least $1.6m; or

(ii) that member is receiving a retirement phase income from any source.

162. A SMSF can have 'disregarded small assets' even if no members have pensions of $1.6m or above in the SMSF. The only condition that must be present in the SMSF is there is at least one member in the retirement phase. The remaining conditions can exist outside of the SMSF.

Under this interpretation, a SMSF that is 100% in pension phase will be required to obtain an Actuarial Certificate[64] that states the ECPI percentage is 100%.

163. Where the auditor relies on an actuarial certificate produced by a management's expert as audit evidence, the requirements of ASA 500 and guidance in GS 005 require the auditor to:

(a) Assess the competence, capabilities and objectivity of the actuary;

(b) Obtain an understanding of the work of the actuary; and

(c) Evaluate the appropriateness and adequacy of the work of the actuary including:

(i) Assessing the relevance and reasonableness of the actuary's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial report;

(ii) If actuary's work involves the use of significant assumptions and methods, consideration of the relevance and reasonableness of those assumptions and methods; and

(iii) If the actuary's work involves significant use of source data, consideration of the relevance, completeness and accuracy of that source data.

164. Actuarial reports are a means of assessing a SMSF's progress in achieving its objectives of providing the member's future benefits and in determining the share of the fund's income that may be exempt from tax as a result of paying pensions to members.

[64] The 2020 Federal Budget included a measure that would remove the requirement for a SMSF that is 100% in the retirement phase to obtain an actuarial certificate from 1 July 2020. The announced measure has not be legislated as at the time of writing.

PART A – FINANCIAL AUDIT

165. The ATO's approved form auditor's report Part A: Financial report requires the auditor to conduct the audit in accordance with Auditing Standards to form an opinion regarding the fair presentation of the financial report of the SMSF for the reporting period, in accordance with stated accounting policies, which are consistent with the financial reporting requirements of the SMSF's governing rules, compliant with the SISA and SISR and are appropriate to meet the needs of members.

166. ASA 200 requires the auditor to express an opinion on whether the financial report is prepared, in all material respects, in accordance with an applicable financial reporting framework. ASA 210 *Agreeing the Terms of Audit Engagements* at paragraph 6 details the requirement for the auditor to determine whether the reporting framework is acceptable as well as to obtain trustee acknowledgement of their understanding and responsibility for the financial report in its entirety.

SMSFs generally prepare special purpose financial reports they are not required to formally adopt Australian Accounting Standards and the trustees determine the applicable financial reporting framework which they will apply to the SMSF's financial report.[65]

Financial Reports

167. An accumulation fund, or defined contribution fund, is a fund which is not a defined benefits fund.[66] The benefits payable to members on satisfying a condition of release in an accumulation fund are determined by the accumulated contributions made to the fund and the investment income thereon, as well as any insurance benefit available, less any expenses or other deductions.

168. The requirements for financial reports for a SMSF are set out in the SISA and SISR. In summary, for an accumulation fund they comprise:

(i) a statement of financial position; and

(ii) an operating statement.

Funds where the benefits are wholly determined by reference to life assurance policies, prepare significantly different financial reports to other SMSFs. Guidance on these reports is provided in the SISR.[67] This Guidance Statement does not deal with the audit of these funds.

169. Typical account categories in an SMSF's financial report include:

- Assets:
    - Cash and cash equivalents;
    - Investments;
    - Receivables; and
    - Prepayments.
- Liabilities:

[65] If a SMSF is a reporting entity, the SMSF prepares general purpose financial reports and adheres to the Australian Accounting Standards in the preparation of that report.
[66] Definition from regulation 1.03(1) of the SISR.
[67] See Regulations 8.02 and 8.03 of the SISR.

- Tax liabilities (current and deferred);
- Accounts payable and accruals;
- Borrowings, including limited recourse borrowing arrangements;
- Accrued benefits; and
- Vested benefits (disclosed in the notes to the financial statements).

- Reserves
- Revenue:
  - Investment revenue, including changes in net market values;
  - Proceeds from insurance policies; and
  - Contributions and transfers in.
- Expenses:
  - General administration expenses;
  - Tax expenses; and
  - Benefits paid.

Guidance on auditing each of these balances and transactions is provided in paragraphs 151 to 236, and illustrative financial audit procedures are also provided in Appendix 4 of this Guidance Statement.

Assertions and Audit Evidence

170. In representing that the financial report gives a fair presentation of the SMSF's financial position and performance during the reporting period and is prepared in accordance with the applicable financial reporting framework, the trustees make assertions implicitly or explicitly (positive confirmations) regarding the recognition, measurement, presentation and disclosure of the various elements of a financial report including related disclosures.

171. In accordance with ASA 315, the auditor uses assertions for classes of transactions, account balances, and presentation and disclosures in sufficient detail to form a basis for the assessment of risks of material misstatement and the design and performance of further audit procedures.

172. Assertions used by the auditor fall into the following categories:

(a) Assertions about classes of transactions and events reflected in the SMSF's operating statement for the period under audit:

(i) Occurrence - transactions and events that have been recorded have occurred and pertain to the SMSF;

(ii) Completeness - transactions and events that should have been recorded have been recorded;

(iii) Accuracy - amounts and other data relating to recorded transactions and events have been recorded appropriately;

(iv) Cut-off - transactions and events have been recorded in the correct accounting period; and

(v) Classification - transactions and events have been recorded in the proper accounts.

(b) Assertions about SMSF account balances reflected in the SMSF's statement of financial position at the period end:

(i) Existence - assets, liabilities, and member entitlements exist;

(ii) Rights and obligations (ownership) - the SMSF holds or controls the rights to assets, either directly or beneficially, and liabilities are the obligations of the SMSF;

(iii) Completeness - assets, liabilities and member entitlements that should have been recorded have been recorded; and

(iv) Valuation and allocation - assets, liabilities and member entitlements are included in the financial report at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

(c) Assertions about presentation and disclosure within the SMSF's special purpose financial reports:

(i) Occurrence and rights and obligations - disclosed events, transactions, and other matters have occurred and pertain to the SMSF;

(ii) Completeness - disclosures that should have been included in the financial report have been included;

(iii) Classification and understandability - financial information is presented and described appropriately, and disclosures are expressed clearly; and

(iv) Accuracy and valuation - financial and other information is disclosed fairly and at appropriate amounts.

Materiality

173. ASA 320 requires the auditor to make a preliminary assessment of materiality to establish an appropriate quantitative materiality level to plan risk assessment procedures, further audit procedures, selection strategies and other audit procedures for the financial audit. In addition to considering qualitative factors, a quantitative materiality level is calculated by applying a percentage, based on the auditor's professional judgement, to the appropriate benchmark or benchmarks, which may include:

- Total gross assets;
- Net assets'
- Total member entitlements;
- Total gross income; and
- Total expenses.

174. The auditor uses the preliminary quantitative materiality level and the assessed risk of material misstatement at both the financial report level and at the assertion level, for classes of transactions and account balances, to determine the nature, timing and extent of audit procedures for the financial audit.

175. In assessing the materiality of any misstatements identified during the audit and their impact on the auditor's report, the auditor considers both quantitative and qualitative factors. Qualitative factors which the auditor considers include:

- The significance of a misstatement to the SMSF;
- The pervasiveness of a misstatement; and
- The effect of misstatement on the financial report as a whole.

176. ASA 450 requires the auditor to consider the possibility that the cumulative result of uncorrected misstatements below the materiality level could have a material effect on the financial report.

Opening Balances

177. Upon appointment to a new engagement, ASA 510 requires the auditor to obtain sufficient appropriate audit evidence that:

    (a) the opening balances (account balances which exist at the beginning of the period) do not contain misstatements that materially affect the current period's financial report;

    (b) the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated (prior year audited figures are restated if a prior year error is material); and

    (c) appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial report or changes thereto are appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

178. When the prior period's financial report was audited by another auditor, the current auditor may be able to obtain sufficient audit evidence by reviewing the predecessor auditor's working papers. In these circumstances, the current auditor considers the professional competence and independence of the predecessor auditor. If the prior period's auditor's opinion was modified, under ASA 705, the auditor pays particular attention in the current period to the matter which resulted in the prior period modification.

179. Prior to communicating with the predecessor auditor, under ASA 220, the current auditor is required to consider the relevant ethical requirements which includes client consent. It is common practice for a successor auditor to issue a letter to the predecessor auditor to understand whether there may be threats to compliance with ethical requirements.

180. GS 011 *Third Party Access to Audit Working Papers* provides Example Letter E as a template for auditors to request the working papers of a predecessor auditor. GS 011 provides guidance in the case of voluntary co-operation. There is no legislative requirement for successor auditors to provide access to their working papers. Their working papers remain their property.

181. Ordinarily, some audit evidence for opening balances may be obtained as part of the current period's audit procedures on current assets and liabilities. Performing audit procedures on the valuation of the opening bank account and other material items may provide sufficient appropriate audit evidence. For investments and material balances, the auditor examines the accounting records and other information underlying the investments which may contain the opening balances of such investments. In certain cases, the auditor may be able to obtain confirmation of opening balances with third parties such as share registries or fund managers. When the auditor cannot obtain this information, the auditor may need to carry out additional audit procedures relating to the opening balances.

182. When the auditor is not able to obtain sufficient appropriate audit evidence by examining the work of the previous auditor, the auditor undertakes further audit procedures to obtain sufficient appropriate audit evidence to ascertain whether the opening balances do not contain material misstatements, are correctly brought forward and that the accounting policies have been consistently applied in the current period.

183. If audit procedures do not result in sufficient appropriate audit evidence concerning opening balances, ASA 510 requires that the auditor's report is modified. Further guidance on modifications to the auditor's report is provided in paragraphs 300 to 312.

Cash and Cash Equivalents

184. Cash and cash equivalents include bank accounts, cash management trusts and other cash transactional facilities held with banks, fund managers, credit unions and other approved financial or deposit taking institutions. These accounts provide either a paper based record or electronic record of transactions and may have cheque, direct debit or internet banking facilities.

185. The audit assertions for auditing a SMSF's cash and cash equivalents are:

- Existence – obtaining evidence that the cash exists and is correctly classified;
- Rights and obligations (ownership) – obtaining evidence that the cash is owned directly or beneficially by the SMSF;
- Completeness – obtaining evidence that all cash owned by the SMSF is recorded; and
- Valuation and allocation – obtaining evidence that the cash is valued at face value in accordance with the accounting policies.

186. Cash and cash equivalents are a SMSF's most liquid assets and so may carry a high fraud risk. The auditor remains alert to fraud and the risk of fraud with respect to the SMSF's bank accounts. The auditor assesses the internal controls surrounding the authorisation of payments and receipts to ascertain whether the cash of the SMSF is safeguarded adequately. The auditor remains sceptical of transactions in the bank accounts that may relate to early access or fraud perpetrated not only by the members or trustees but by those parties that may have access to a fund's bank accounts.

187. If the banking operations are significant to the audit, the auditor sends bank audit confirmation requests[68] to the SMSF's banks. A bank audit confirmation is a request to a bank to provide independent confirmation for audit purposes of such information as the SMSF's account balances, securities, treasury management instruments, documents and other related information held by the bank on behalf of the SMSF. The confirmation will also seek to identify any deliberate or inadvertent borrowings with the bank.

188. Some SMSFs may utilise a cash account established with their broker, investment account or other investment platform (for example, IDPS) as part of their securities trading activity. This account may facilitate trading, settlement and receipt of dividends and interest. The auditor establishes who has access to this account and who may authorise transactions to ensure that only authorised investment trading takes place.

Investments

189. The investments of a SMSF may include:

[68] For an example of a Bank Audit Confirmation, refer to GS 016.

- Listed securities;
- Fixed rate securities such as government, semi-government or corporate bonds, loans (secured or unsecured) and mortgages;
- Variable rate and discount securities such as bank bills, promissory notes or floating rate notes;
- Hybrid securities which have both interest and equity components, such as convertible notes or converting preference shares;
- Managed products such as units in managed funds, managed investment schemes, Pooled Superannuation Trusts (PSTs) and insurance policies;
- Unlisted investments including shares and units in widely held entities;
- Unlisted investments including shares and units in closely held or related entities;
- Derivatives such as futures, options and warrants;
- Assets subject to limited recourse borrowing arrangements;
- Real property; and
- Collectables and personal use assets[69] such as artwork, antiques, wine and recreational boats.

190. Investments may be domestic, international or a combination of both and may be held by a custodian, the individual trustees or a corporate trustee.

191. The audit assertions for auditing a SMSF's investments are:

- Existence – obtaining evidence that the investment exists;
- Rights and obligations (ownership) – obtaining evidence that the investments are owned directly or beneficially by the SMSF;
- Completeness – obtaining evidence that investments owned by the SMSF are recorded in the accounts; and
- Valuation and allocation – obtaining evidence that investments are valued in accordance with the accounting policies adopted, allocated to the correct account and disclosed fairly in accordance with the stated policies.

192. Audit risks to be considered in relation to auditing investments may include, but are not limited to:

- Over or understatement of investment values, including compliance with the SISR in valuing investments at market value; and
- Investments not beneficially owned by the SMSF.

193. The audit procedures relating to investments will vary depending on the administration and management arrangements adopted by the trustees, the type of investments held and the trustee structure that holds the assets. The auditor exercises professional judgement in determining the appropriate auditing procedures.

[69] Collectables and personal use assets are defined in Regulation 13.18AA of the SISR.

Existence and Ownership

194. In auditing the existence of SMSF's assets, the auditor may either physically inspect the assets or examine documentation supporting their existence. The documentation may also verify ownership. If assets are registered in the name of the trustees, corporate trustee or custodian, the auditor also obtains audit evidence that the SMSF is the beneficial owner and that the assets are being held on behalf of the SMSF. Evidence of beneficial ownership may include an acknowledgement of trust or equivalent document.

Completeness

195. The auditor confirms that material investments of the SMSF have been recorded at the correct amounts and in the correct period. The auditor reviews supporting documentation to confirm that no material asset of the SMSF has been excluded. This may extend to obtaining investment schedules from previous years and examining them for changes and movements and reconciling the schedules with purchase and sale transactions for the current period to confirm that material movements in investments have been recorded. The auditor may also obtain representations from the trustees that they have provided a full disclosure of all assets of the SMSF and made available all records relating to those assets.

Valuation and Allocation of Assets

196. As the SMSF's financial report is generally a special purpose financial report, the trustees choose the financial reporting framework under which the SMSF reports. Trustees exercise their discretion when determining the most appropriate market value[70] to be applied to each investment of the SMSF. Under ASA 800, the auditor's responsibility is to form an opinion regarding fair presentation in accordance with the identified financial reporting framework or identified basis of accounting. Under ASA 540, the auditor is required to obtain sufficient appropriate audit evidence that fair value measurements and disclosures are in accordance with the SMSF's applicable financial reporting framework. The auditor evaluates whether the valuation method employed is consistent with the financial reporting framework adopted and the policies described in the accounting policy notes, whether the method of measurement is appropriate in the circumstances and does not result in misleading information and that the method adopted has been applied consistently.

197. When preparing year end accounts, SMSF assets are required to be valued at market value.[71] Market value is defined in the SISA[72] and the ATO's guidance on the process to establish a market value is contained in its Valuation guidelines for self-managed superannuation funds.

198. The auditor obtains an understanding of the trustees' rationale for selecting the basis of determining market value and exercises professional judgement in assessing whether the basis is appropriate given the nature of the asset and the financial and investment markets in which the SMSF operates. The auditor obtains sufficient appropriate audit evidence to support the trustees' rationale for determining the market value of each asset class.

199. It is not the role of the auditor to value the assets. The role of the auditor is to check that assets have been reported at market value, and assess and document whether the basis of establishing market value is reasonable and the valuation is reasonable in light of the SISA, SISR, and ATO guidelines. The working papers normally include the audit evidence for the testing of the fund's investments and record how the auditor reached their conclusions regarding any particular asset.

The auditor assesses the risks of material misstatement of the asset values, designs and performs audit procedures and documents conclusions in response to the assessed risks.

[70] See Regulation 8.02B of the SISR.
[71] See Regulation 8.02B of the SISR.
[72] See Subsection 10(1) of the SISA.

200. Material misstatement of the SMSF's financial report results in the member's interests being misstated which has implications for the calculation of a number of important thresholds:

(a) the member's total superannuation balance (TSB) which is the key metric for eligibility for a range of superannuation planning opportunities;

(b) the valuation of retirement phase pensions and their recording in the member's Transfer balance account (TBA). Every individual has a personal transfer balance cap (TBC) which limits the amount of capital that can be utilised for retirement phase income streams. The TBA is used to manage the individual's TBC and is measured based on the market value of transactions that occur as debit and credits within the account;

(c) the value of a member's death benefit. Material misstatement in the financial statements of a SMSF when a member dies can lead to a delay in the payment of the proceeds.

201. SMSFs may invest directly in unit trusts, listed securities, PSTs or other investment products for which market prices are published and readily available. The auditor may verify that the unit price used is consistent with reference to cum-distribution or ex-distribution price and any accrual of income. For these investments, the product or unit is recorded as an asset in the records of the SMSF rather than the underlying investments.

202. Non-monetary items, such as property and collectables, require alternative methods to arrive at market value. The auditor makes reference to the ATO's Valuation guidelines for self-managed superannuation funds in order to establish that the basis for determining market value is appropriate to meet the requirements of the ATO and the SISR.

203. Investment in unlisted companies or trusts require particular review by the auditor in order to gain assurance the valuation is appropriate. Difficulties may arise when the company or trust report on an 'at cost basis'. Applying professional judgement, the auditor assesses the likelihood of material misstatement of the SMSF accounts if the investment is not subject to a valuation process. Matters to be considered may include the following:

(a) length of time the SMSF has held the investment;

(b) evidence provided at the initial purchase and any subsequent additional investment by the SMSF regarding the valuation methodology;

(c) any third party sales or purchases of the investment during the SMSF's holding period. This will require the SMSF trustee to liaise with the company CEO or the trustee of the trust to obtain supporting evidence of the methodology for striking the sales or purchase price. This request may be refused based on commercial sensitivities.

(d) whether it is reasonable for the SMSF trustee to undertake a valuation of a fund asset. That is, they possess the requisite knowledge or expertise to undertake the valuation or, a low level of complexity is inherent due to the volume of publicly available market information to facilitate an informed valuation.

For example; if a SMSF asset comprises a strata title residential property in a major capital city where reasonable stock turnover occurs, the trustee may be able to use auction and other sales data to determine an appropriate valuation for the fund property. Alternatively, if a property is unusual and not subject to comparable sales, it may be the trustee does not have the competency to undertake the valuation of the asset.

204. Where the SMSF has invested in a related trust or company, a review of the valuation methodology may reveal the instance of non-arm's length income (NALI) which requires a re-assessment of the calculation of the fund's tax position.

205. Where the auditor is unable to form an opinion in assessing whether the valuation is in accordance with the financial reporting framework adopted, due to uncertainty, and no expert valuation can be obtained, the auditor considers modification of the auditor's report, taking into account materiality and the risk of material misstatement. The auditor is required to report to the ATO in an ACR where there is a contravention or potential contravention of regulation 8.02B of the SISR. The SMSF Annual Return will report the Part A Audit qualification.

206. To protect the value of their assets, SMSFs may obtain insurance cover over the assets. In auditing ownership and valuation of assets, the auditor obtains evidence that:

(a) the insurance exists;

(b) the SMSF is both the owner of the asset and the beneficiary of the policy;

(c) the premium is paid by the SMSF; and

(d) the cover is adequate and current.

207. With respect to investment properties, residential or commercial, circumstances may exist where the SMSF's tenancy lease agreement stipulates that the tenant is required to pay for the insurance. In these cases, the auditor checks to see if the policy is up to date and the beneficiary of the insurance benefit is the SMSF and not the tenant.

IDPS and Other Service Organisations

208. IDPS[73] operators provide investors with an annual tax statement to provide consolidated information about their investment portfolio as well as to assist them with the completion of their tax obligations. The extent to which a SMSF auditor can rely on the third party information is as follows:

(a) Where the Annual Investor Statement is accompanied by an Audit Report issued in accordance with ASAE 3402 and GS 007 ("type 2 report") and the audit report provides audit evidence on the operating effectiveness over controls at the service organisation.

209. ASA 402 deals with the auditor's responsibility to obtain sufficient appropriate audit evidence when the user entity uses a service organisation. The Standard expands on how the auditor applies ASA 315 and 330 in obtaining an understanding of the user entity, including internal controls relevant to the audit, sufficient to identify and assess the risks of material misstatement and in designing and performing further audit procedures responsive to those risks. A type 2 report may be used as evidence that controls at the service organisation are operating effectively if the results described in the service auditor's report are relevant to assertions that are significant in the SMSF's financial report.

210. The nature of the audit procedures required to obtain sufficient appropriate audit evidence regarding a SMSF's investments which are managed by, or under a custodial arrangement of an IDPS or another service organisation, are a matter for the auditor's professional judgement in accordance with the assessed inherent risks in the fund.

211. Investments held by an IDPS operator under the investor's HIN (holder identification number) rather than under a custodial arrangement, are able to be verified directly by the auditor regardless of the location of the records. If the investor report is a primary document for the preparation of the SMSF's financial statements, the risk assessment by the auditor may depend

73 See paragraph 123 of this Guidance Statement for a description of IDPS reports.

on whether a type 2 audit report has been provided and what level of assurance has been provided by the service auditor.

212. For investments for which recording of material balances or transactions is controlled by the service organisation but accounting records are still maintained by the SMSF and the SMSF has access to the source documentation, such as when assets are held in custody, the end of period statements and taxation summaries may be insufficient evidence alone but may be coupled with evidence of the operating effectiveness of controls within the IDPS or service organisation, confirmation of balances with the service organisation and analytical review on procedures on the SMSF's investment activity.

213. For a standalone investment mandate where the IDPS or service organisation maintains the SMSF's accounting records, including source documentation, implements investment decisions based on the mandate and holds the investments on behalf of the SMSF under a custodial arrangement, the SMSF may maintain only limited independent accounting records, source documentation or banking records, in which case the SMSF relies on the service organisation's reports as a basis for preparation of their financial report.

214. Audit evidence in these circumstances may include a service auditor's report on the operating effectiveness of the controls at the IDPS or service organisation (a Type 2 Report), analytical testing, substantive testing of balances and transactions held by the service organisation, obtaining a special purpose auditor's report from the service organisation on the balances and transactions of the SMSF, or conducting testing at the SMSF.

215. Testing at the transaction level may include: valuation using independent sources, confirmation of contributions with employers, verification of benefit payments against members' records e.g. personal bank statements, verification of dividend and trust distributions against published information and, by obtaining copies of correspondence including advice provided to the SMSF regarding portfolio positions. The SMSFs asset register can provide another source of information that may increase the auditor's judgement on how much reliance they will place on the Type 2 Report to provide sufficient audit evidence.

216. If the auditor is not relying on the Type 2 Audit Report to limit the level of testing undertaken at a transaction level and it may be impossible or impractical to obtain sufficient appropriate audit evidence with respect to material balances or transactions of the SMSF controlled by the IDPS or service organisation, the auditor either qualifies their opinion on the basis of a limitation of scope, or issues a disclaimer of opinion, if the effects or possible effects are material and pervasive.

217. In the case of a modified audit opinion, the methodology and the details of how the auditor reached their conclusion form a part of the audit working papers.

Receivables and Prepayments

218. Where the SMSF accounts on an accruals basis, receivables may include interest or trust distributions receivable and current tax assets. Receivables are tested primarily for existence, valuation and allocation by confirming the receipt in the subsequent period.

219. If the SMSF accounts on an accruals basis and invests in managed funds that pay distributions post balance date, the auditor verifies that the SMSF has accrued these distributions of income correctly and consistently and that the investment value of the underlying asset has been adjusted accordingly.

220. Prepayments are tested against cash payments and particular attention paid to transactions with related parties to ensure they relate to a genuine expense.

221. Unpaid present entitlements (UPE) from related trusts risk being caught as a contravention of; the in-house asset rules (IHA) in Part 8; the arm's length rules at s.109 and; the sole purpose

test (SPT) at s.62 SISA 1993, if not promptly paid. See SMSFR 2009/3 for details of the ATO's view on UPE's between SMSF and related trusts. In reviewing UPE's, the auditor considers whether there is genuine likelihood of the capital being paid within proximity of the declaration of the distribution or whether the fund and trust have entered into a loan agreement (explicit or implicit).

Liabilities

222. Liabilities of a SMSF, other than accrued benefits which are discussed separately, may include:

- Goods and Services Tax (GST) payable, if the SMSF is registered for GST;
- Income tax liabilities, current and deferred;
- Accruals for accounting and audit fees;
- Liabilities relating to limited recourse borrowing arrangements;
- Any other accrued expense the trustees have provided for or incurred;
- Benefits payable, including benefits arising from insurance claims; and
- Bank overdrafts, other borrowings and related interest payable.

223. The audit assertions with respect to a SMSF's liabilities are:

- Existence – the liabilities exist;
- Rights and obligations (ownership) – the liabilities are obligations of the SMSF;
- Completeness – liabilities of the SMSF have been recorded; and
- Valuation and allocation – liabilities are recorded at appropriate amounts and allocated to the appropriate account.

224. Generally, SMSFs are not permitted to borrow. Permitted exceptions are temporary borrowings to fund the payment of member benefits, payment of the superannuation contributions surcharge,[75] settlement of securities transactions where the borrowing was unforeseen or borrowings under limited recourse borrowing arrangements. Sections 67, 67A and 67B of the SISA detail the additional requirements that are required to be met before the limited recourse borrowing is accepted.

225. Audit risks to be considered in relation to auditing liabilities may include but are not limited to:

- Liability values being understated;
- Liabilities being omitted; and
- Excessive accruals for expenses that will not be paid or which are not legitimate expenses of the SMSF.
- Loan documents in respect of a limited recourse borrowing arrangement (LRBA) do not specify the loan to be limited in recourse.

[75] The superannuation contributions surcharge was abolished from 1 July 2005; however there may be circumstances where the surcharge may still be levied on contributions relating to periods prior to this date.

226. Normally, the auditor performs a search for unrecorded liabilities by examining brokers' statements for outstanding balances, bank confirmation letters for borrowings or evidence of security provided, banking records for payments after period end and by reviewing the financial records for expenses that were paid in previous years, but billed infrequently or annually such as insurance or accountancy fees, which may not have been included in the current period's accruals. The auditor may seek representations from the trustee that all liabilities of the SMSF have been disclosed and recorded.

Accrued Benefits

227. The liability for accrued benefits, or member entitlements, is the present obligation to pay benefits to members or beneficiaries in the future.

228. Accrued benefits of a SMSF may arise from:

- Accumulation entitlements where the member bears the investment risk;
- Pension accounts due to members; and
- Insurance claims paid or payable to the SMSF owing to members.

229. The audit assertions with respect to a SMSF's accrued benefits are:

- Existence – the accrued benefits are entitlements of members;
- Rights and obligations (ownership) – the accrued benefits are obligations of the SMSF;
- Completeness – accrued benefits of each member of the SMSF have been recorded; and
- Valuation and allocation – accrued benefits are recorded at appropriate amounts and allocated to the appropriate account/member.

230. Audit risks for accrued benefits include, but are not limited to:

- Contributions not being allocated correctly to members;
- Income not being allocated correctly or appropriately to individual members;
- Benefit payments or expenses being allocated incorrectly to member's balances; and
- Member balances not being carried forward correctly from one period to another.

Vested Benefits

231. Vested benefits are those benefits to which the member is currently entitled irrespective of the member's continued membership of the SMSF, on-going employment with a particular employer or maintenance of other conditions. Although vested benefits are an unconditional benefit of the member within the SMSF, those benefits can be accessed only upon satisfying an appropriate condition of release, such as retirement, death, rollover, reaching age 65 or reaching at least preservation age[76] and accessing a TRIS. Usually vested benefits are disclosed in the notes to the financial statements.

[76] Preservation age is the age at which super benefits may be able to be accessed. Preservation age will rise from 55 to 60 between 2015 and 2024. This will mean that for someone born before 1 July 1960, their preservation age is 55 years, while for someone born after 30 June 1964, their preservation age will be 60.

232. Vested benefits equate to the minimum benefits of the SMSF's members. Minimum benefits include member concessional and non-concessional contributions, mandated contributions (compulsory employer contributions) such as Superannuation Guarantee (SG) contributions or superannuation payments made pursuant to an Award or other employment agreement, amounts rolled over or transferred in as minimum benefits and the earnings thereon. Minimum benefits must be maintained in the SMSF until they are cashed, rolled over or transferred in accordance with the SISA and SISR benefit payment rules.[77]

233. Audit procedures to test for vesting of minimum benefits include examining the fund's governing rules to ensure that the governing rules fully vest the contributions in the member and testing member and employer contributions for the period for inclusion in members' accounts. In addition, the auditor reviews any transfers to reserves to ensure that the minimum benefits are not being reduced.

Reserves

234. A reserve is an amount held within a SMSF that is not allocated specifically to members. Generally, reserves are permitted unless specifically prohibited under a SMSF's governing rules. Typically, reserves are created from contributions not being allocated to a member upon receipt or from excess investment returns.

235. Types of reserves permitted for SMSFs may include, but are not limited to:

- Investment smoothing;
- Contribution; and.
- Miscellaneous.

236. Investment smoothing reserves are used to maintain a consistent rate of return for the fund. The trustee may consider the overall cashflow needs for the fund in light of the outgoings and determine an appropriate investment earnings rate to apply to member accounts. The strategy may be utilised in order to avoid the need for untimed investment disposals in order to manage liquidity needs.

237. Contribution reserves allow funds to manage potential excess contributions where a contribution is received in the month of June.

238. Miscellaneous reserves can be created by the death of the last defined benefit pensioner within the SMSF with the residual sums being transferred to a miscellaneous reserve. They can also be created intentionally for other purposes.

239. Contributions received are required by the SISR to be allocated to members within 28 days of the end of the month in which they are received.[78] If a SMSF receives a contribution during a financial period and that contribution is not allocated to a member in that period, the amount should be classified as an "unallocated contribution"[79] at balance date. The unallocated contributions account is similar in nature to a reserve, but contains only contributions held temporarily until they are allocated. Earnings and expenses may not be debited or credited to the unallocated contributions account.

240. The trustee is required to report an unallocated contribution to the ATO via a specified form[80] otherwise, the member will be assessed under the excess contribution rules.

[77] See regulation 5.08 of the SISR.
[78] See Regulation 7.08 of the SISR.
[79] See TD 2013/22 applies from 1 July 2013. ATO ID 2012/16 applied prior to 1 July 2013.
[80] See ATO NAT 74851 – Request to adjust concessional contributions

241. Prior to 1 July 2019, anti-detriment payment reserves were utilised in order to fund 'tax saving amount(s)' in accordance with s 295-485 ITAA 1997. These reserves were established to pay an additional benefit upon death, equivalent to the tax already paid on contributions, for the member. The reserves were funded from excess investment returns; by a contract for insurance over the life of a fund member; or allocated from miscellaneous reserves. SMSFs were able to pay a tax savings amount to a deceased's member's spouse or child up to 30 June 2019 provided the member died prior to 1 July 2017.

242. Procedures used for a SMSF with an anti-detriment reserve may include ensuring the trustee has documented the strategy in respect of the capital and, where the reserve is being unwound, the treatment of allocations from the reserve to member balances.

243. Funding of reserves via the use of a contract for insurance was prohibited from 1 July 2014 however, if the policy was commenced prior to the change, the SMSF can continue to maintain it. Audit procedures may include testing insurance contracts against the requirements of regulation 4.07D SISR 1994.The ATO has issued SMSFRB 2018/1 to provide its interpretation of the validity of reserves for SMSFs and its concerns that reserves may be used to circumvent the various caps and limitations that apply to superannuation and income tax from 1 July 2017.

The ATO Bulletin states that :

(a) although the legislation permits the use of reserves, the application of the law is intended for APRA funds and SMSFs will only use reserves "in limited circumstances".

(b) investment reserves, operational risk reserves, anti-detriment reserve, self-insurance reserve or insurance reserve are not appropriate for SMSFs.

(c) where a SMSF has reserves that were established prior to 1 July 2017 (or 2014 for insurance), the fund is permitted to maintain the reserve however, the ATO will monitor any (unexplained) increases in the balance of fund reserves and the creation of new reserves.

(d) any allocation from a reserve (apart from a pension reserve) is treated as a concessional contribution, unless the allocation is 'fair and reasonable' across the membership and the amount allocated represents less than 5% of the member's balance. Movements from the reserve should be reviewed to determine if the amount(s) should be classified as concessional contributions.

(e) on death of a member that is in receipt of a defined benefit pension, the reserve that was created in support of the funding of the pension may not form a part of the death benefit. Review of the fund's trust deed and the pension establishment documentation is required to ascertain whether the reserve capital should remain in the fund.

244. Audit considerations for reserves include whether:

- The fund's governing rules permit the maintenance of reserves;
- The assets of the particular reserve are segregated appropriately from the rest of the SMSF's assets;
- Amounts transferred in or out of the reserves are appropriate; and
- The fund has a reserve strategy.[81]

[81] See section 52B(2)(g) of the SISA.

Investment and Other Revenue

245. Revenue of a SMSF, other than contributions, may include:

- Dividends;
- Interest;
- Rental income;
- Unit trust distributions;
- Insurance policy proceeds, rebates and bonuses; and
- Changes in market value – both realised and unrealised.

246. The audit assertions for revenue received by a SMSF are:

- Occurrence – revenue received by the SMSF is real and has occurred;
- Completeness – revenue received by the SMSF has been recorded;
- Accuracy – revenue received by the SMSF has been recorded appropriately. Changes in market value are based on appropriate and accurate asset valuations;
- Cut-off – revenue received by the SMSF has been recorded in the correct period; and
- Classification – revenue received by the SMSF has been allocated correctly, either to the correct members' accounts or to the asset pool and the tax status of that income is appropriate.

247. Audit risks to be considered in relation to auditing revenue may include:

- Revenue is recognised before it is earned;
- Revenue is not being accounted for in accordance with the SMSF's accounting policies; and
- Misstatement of changes in market value due to under or overstatement of market valuation.
- Revenue recognition is ordinarily considered a significant risk for a SMSF.

Contributions and Transfers In

248. Typically, contributions into SMSFs are sourced from either the members or the members' employers. Transfers in are benefits transferred from other superannuation entities. Contributions are classified as either concessional, for which a tax deduction has been claimed by the contributor, or non-concessional, for which no tax deduction has been claimed by the member. Contributions and transfers in to a SMSF may include:[82]

- Employer contributions, including SG, award and salary sacrifice contributions;
- Member contributions, both concessional and non-concessional;
- Spouse contributions;

[82] See the Self-Managed Superannuation Fund annual return (NAT 71226).

- Child contributions;
- Rollovers from other complying funds;
- Small business rollovers (CGT small business retirement exemption and CGT small business 15 year exemption amounts);
- Amounts transferred from a foreign fund;
- Government co-contributions;
- Transfers from the Superannuation Holding Accounts Reserve (SHAR) held by the ATO;
- Personal injury election;
- Other family and friend contributions; and
- Downsizer contribution.

Contributions may be made in cash or in-specie (by transferring an asset) or a combination of both if the fund's governing rules permit the SMSF to accept contributions that are made in-specie. Where contributions are made via an in-specie asset transfer, the auditor determines whether the requirements of section 66 of the SISA have been met.

249. The objectives for auditing contributions received by a SMSF are:

- Occurrence – contributions and transfers in recorded by the SMSF are real and have occurred;
- Completeness – contributions and transfers in from or on behalf of members have been received and recorded;
- Accuracy – contributions and transfers in have been recorded appropriately;
- Cut-off – contributions and transfers in have been recorded in the correct period; and
- Classification – contributions and transfers in have been allocated to the correct member and correctly classified as concessional or non-concessional.

250. Audit risks to be considered in relation to contributions and transfers in may include, but are not limited to:

- Incorrect classification and allocation of concessional and non-concessional contributions and other contributions categories listed in paragraph 216;
- Incorrect tax treatment of contributions;
- Incorrect cut-off for contributions resulting in failure to recognise that contribution caps have been exceeded;
- Incorrect allocation of the tax components of transfers in;
- Acceptance of contributions in excess of the fund-capped contributions limit;[83]

[83] Contributions caps are discussed in paragraph 230 of this Guidance Statement.

- Understatement of market values for in-specie contributions to avoid exceeding the contributions caps; and
- Under or overstatement of market values for in-specie contributions either to provide early access to benefits or to disguise loans to members.

251. Auditors consider the appropriateness of audit evidence to confirm contributions are not materially misstated, such as employer confirmations of contributions paid to the fund or reviewing member PAYG information analytically.

Expenses

252. The typical expenses of a SMSF may include:

- Administration fees;
- Audit fees;
- Actuarial advice;
- Legal advice;
- Valuation fees;
- Accounting and tax agent fees;
- Superannuation supervisory levy;
- Investment management fees and financial planning advice;
- Bank fees;
- Property expenses;
- Insurance premiums paid; and
- Taxation.

253. The audit objectives with respect to a SMSF's expenses are:

- Occurrence – expenses recorded by the SMSF were incurred;
- Completeness – expenses incurred by the SMSF have been recorded;
- Accuracy – expenses have been recorded appropriately;
- Cut-off – expenses have been recorded in the correct period; and
- Classification – expenses have been allocated to the applicable accounts or members to which they relate.

254. Audit risks to be considered in relation to auditing expenses may include:

- Personal expenses of the members or trustees are recorded as expenses of the SMSF;
- Expenses of the SMSF paid by a member or an employer are not recorded as concessional or non-concessional contributions; and
- Incorrect tax treatment of an expense.

255. Ordinarily, the auditor reviews any payments made to individual trustees or corporate trustees to validate that the payment was bona fide and not an early benefit or a payment for trustee services to the SMSF, which are prohibited.[84]

Tax Expense

256. The main areas of focus for an auditor with respect to tax are the tax calculation and allocation of any tax expense or benefit to the members' accounts. The taxation legislation is amended periodically and interpretation of that legislation by the ATO and the courts may change from time to time, consequently, the guidance in this section may become outdated over time and it is the responsibility of the auditor to ensure that they remain up-to-date with the taxation requirements affecting SMSFs. The audit objectives with respect to a SMSF's tax expenses and benefits include:

- Occurrence – deductions were incurred and imputation credits, carried forward losses and any other offsets are attributable to the SMSF;
- Completeness – assessable income, including capital gains, received by the SMSF has been declared;
- Accuracy – assessable income, including capital gains, allowable deductions, exempt current pension income, rebates, offsets and eligible credits attributable to the SMSF are calculated and recorded appropriately;
- Cut-off – assessable income, including capital gains, allowable deductions, rebates, offsets and eligible credits attributable to the SMSF are declared or claimed in the correct period; and
- Classification – the tax status of contributions is correctly determined. Timing differences have been correctly identified and accounted for.

257. Income tax is payable on investment earnings (net of expenses) including capital gains, with full imputation credits for dividends received from Australian companies and credits for dividend and withholding tax on foreign income to the extent of Australian tax payable on the foreign sourced income. Income tax is also payable on employer contributions and on member contributions where the member has notified the trustees of an intention to claim a personal tax deduction (concessional contributions). Deductions are available for certain payments and expenses.

258. Some SMSFs account for deferred income taxes in accordance with Australian Accounting Standard AASB 112 *Income Taxes*, in which case the auditor assesses the impact of that accounting standard upon the SMSF. Ordinarily, the auditor considers whether the recognition of any current or deferred tax liabilities or tax assets is appropriate given the likelihood of payment of the liabilities or recovery of the assets based on the age of the members and the circumstances of the SMSF. As most SMSFs operate under a special purpose framework, many elect not to apply AASB 112.

Ordinary Income

259. The ordinary income of the SMSF for tax purposes includes:

- Investment earnings, such as interest, dividends, rent, trust distributions, and realised capital gains;
- Concessional contributions received during the year; and

[84] See section 17(B) of the SISA.

- Dividend income derived but not yet received.

260. Ordinary income does not include:

- Non-concessional contributions;
- Income not derived;
- Non-reversionary bonuses on life policies; and
- Income from assets used to fund pensions.

261. Income from assets used to fund pensions is still included for the purpose of accounting and auditing. It is, however, exempt from tax. The auditor, in reviewing the tax calculation, ordinarily establishes that exempt income has been identified and that the income is correctly treated for tax purposes.

Contributions

262. If a member exceeds their concessional or non–concessional contribution cap, it does not automatically mean that the excess contribution must be returned. The auditor reviews information pertaining to contributions to ascertain whether the excess contribution is returnable under regulation 7.04 of the SISR, or if an ATO release authority is required to release the excess amount.

263. The auditor verifies contributions against the documentation from the member or member's employer (for example, remittance advices), for correct allocation to members' accounts and appropriate classification as concessional or non-concessional, so that the correct tax treatment is applied.

264. Upon the sale of certain small business assets, members may be able to contribute some or all of the sale proceeds to the SMSF and may be eligible to exclude all or part of the contribution from the non-concessional contributions cap. In these circumstances, the auditor confirms the contribution is supported by a Capital gains tax election – instructions and form.[88]

265. Some contributions are time limited and audit considerations normally include reviewing the date the contribution was recorded as being received against the specific contribution time limit. For example, concessional contributions must be allocated to a member within 28 days of their receipt. This is particularly important if the fund uses the contribution reserving strategy. The downsizer contribution requires the individual to make the contribution to super within 90 days of the receipt of the settlement funds from the sale of an eligible property.

266. Contributions under the small business 15-year exemption or the retirement exemption are required to be paid into the fund when the individual makes the choice or, when they receive the capital proceeds from the CGT event, if they are under age 55. Individuals over 55 do not have to make the contribution to super in order to qualify for the CGT exemption however, if they do, the contribution must be made the later of the day the tax return is required to be lodged in the year of the CGT event or, 30 days after the capital receipt.

267. If an individual receives a capital gain from a company or trust as a CGT concession stakeholder, the paying entity must make the payment to the individual's superfund within 7-days of the date of the election or, within 7-days of receipt of the capital, if the stakeholder is less than 55 years of age.

[88] See ATO form NAT 71161.

Non-arm's Length Income

268. Non-arm's length[89] income (NALI) of a SMSF, which includes private company dividends (unless arm's length), income from non-arm's length transactions and discretionary or hybrid trust distributions, is not taxed concessionally. The auditor checks that any non-arm's length income has been classified correctly. Undetected NALI may result in a material misstatement of the tax expense of the SMSF and the auditor may need to modify their opinion on the financial statements – Part A qualification.

Franked Dividends

269. The auditor checks that any imputation credits attached to a franked dividend to which the SMSF is entitled have been recorded and that the respective franking credit of each dividend is accounted for correctly and that these have been included in the tax calculation appropriately. This extends to checking that the SMSF has held the security for the requisite period to qualify for the franking credit refund.

Capital Gains Tax

270. Growth in the value of most SMSF assets, is subject to Capital Gains Tax (CGT) on their disposal, with assets purchased prior to 30 June 1988 deemed to be purchased on that date. The auditor examines any asset disposal that may trigger a CGT event to verify that any CGT loss or gain is taken into account in determining the current tax liability. The auditor also verifies that capital losses and discounts appropriate to capital gains have been correctly calculated and applied.

271. Additional testing may be required where the SMSF made a CGT Relief election in the 2017 income year. A list of investments that were subject to CGT deferral should form a part of the audit working papers and the auditor ordinarily tests the correct calculation of the capital gain or loss if any of these deferred CGT assets were sold in the income year under review.

Goods and Service Tax

272. If the SMSF is registered for Goods and Service Tax (GST), generally due to owning business real property, and has taxed supplies (income) and input taxed supplies (expenses) the auditor , where material, reviews the GST calculation and business activity statements (BAS) to ensure that the correct amounts are being disclosed and the SMSF is meeting its payment obligations with respect to GST. Input tax credits are claimable on supplies relating to commercial property, on other supplies at the reduced rate of 75% and not claimable on certain expenses, such as accounting fees for the preparation of the tax return or BAS or on audit fees.

Deductions

273. Expenses incurred by a SMSF may be deductible by the SMSF under the ITAA subject to the normal principles governing the tax deductibility of expenditure incurred by superannuation funds.[90] The auditor tests the deductions claimed to verify their occurrence, deductibility and that they were incurred by the SMSF and were not personal in nature, or if they were shared, the correct proportion of the expense has been claimed by the SMSF. In general, the following expenses are deductible – administration fees, actuarial costs, accountancy and audit fees, investment management fees and custody fees. Other expenses such as capital allowances (depreciation) may be deductible depending on the circumstances of the SMSF. Depending on the type of insurance policy, the insurance premium may also be deductible, in

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89 Prior to 1 July 2007, non-arm's length income was special income under the ITAA. Section 273 of the ITAA (1936) was repealed on 1 July 2007 and replaced by section 295-550 of the ITAA (1997). Refer to Public Tax Ruling TR2006/7 for further information.

90 The ATO has issued a number of publications which provide further guidance on the deductibility of expenses incurred by the SMSF. They include Taxation Ruling TR 93/17 *Income tax: income tax deductions available to superannuation funds*, and its addendum TR 93/17A, which provides general guidance, , , and Tax Ruling IT 2672, which discusses the deductibility of amending a deed.

part or in full. The auditor may also check that capital items have been correctly treated, as items of a strictly capital nature and are not tax deductible.

274. The auditor normally reviews the fund activity to identify whether any non-arm's length expenses (NALE) were incurred during the income year. Non-arm's length expenses are those that are less than the amount that the fund might have been expected to incur if dealing with the other party at arm's length including where services or goods are received for no cost.[91]

275. As an example the auditor may consider any separate services provided by the trustee as these are not able to be remunerated and do not fall into the NALE regime. NALE results in the application of NALI rates of tax for the fund. The auditor verifies that expenses are not claimed if they relate to exempt pension income.[92]

Actuarial Reports for Un-segregated Assets

276. Where a fund has un-segregated assets and all of the assets of the fund were not supporting pensions for the whole of the year, it is necessary to obtain an actuarial certificate to certify the portion of exempt pension income. In these circumstances, the auditor sights and evaluates the actuarial tax certificate that is used in the calculation of taxable income and reviews the accuracy of the information provided to the actuary to prepare the actuarial tax certificate. The auditor confirms that the correct percentage figure certified by the actuary has been applied to calculate the exempt current pension income for the SMSF.

Benefits Paid

277. Generally, benefits paid by a SMSF are triggered by the member's retirement, turning age 65 years, death, physical or mental incapacity,[93] termination of employment, or reaching preservation age and commencing a transition to retirement[94] income stream[95] (TRIS). In the event of divorce, benefits may be split pursuant to a superannuation agreement, consent order or an arbitrated court order.[96]

278. SMSFs may pay benefits by way of a lump sum (in cash or in specie[97]), pension or insurance benefit.[98] An accumulation fund may pay the following types of pensions:

(a) account based income streams, including TRISs; and

(b) existing allocated pensions and market linked income streams (formerly known as market linked pensions).

279. The relevant assertions with respect to benefits paid are:

- Occurrence – benefits recorded by the SMSF as paid have been paid;
- Completeness – benefits paid or payable, if appropriate, by the SMSF have been recorded;
- Accuracy – benefits paid by the SMSF have been calculated appropriately. The minimum annual benefits amount has been paid and, for TRISs only, the payment

91 LCR 2019/D3 provides the ATO views on NALI and NALE

92 Guidance and information on how exempt current pension income and relevant deductions (TR 93/17) should be applied for funds with segregated or unsegregated assets is available on the ATO website www.ato.gov.au (search under ECPI).

93 This can be permanent or temporary incapacity which stops the member from engaging in gainful employment.

94 More information about transition to retirement is available on the ATO website www.ato.gov.au (search under transition to retirement).

95 Other conditions of release include a terminal medical condition, financial hardship and compassionate grounds.

96 In circumstances where a benefit payment has been split, the auditor reviews the documentation surrounding the split and mechanism by which the superannuation entitlement was dealt with in the property settlement arrangements. See paragraphs 234 to 236 for further guidance on benefit splitting.

97 Assuming in-specie payments are permitted by the fund's governing rules.

98 A total and temporary disability benefit (salary continuance/income protection benefit) is generally paid as a regular income payment without reference to an account balance.

does not exceed the maximum annual payment amount. The correct amount of Pay-As-You-Go (PAYG) withholding tax, has been withheld, where the benefit is from an untaxed source or the member is under 60 years;

- Cut-off – benefits paid by the SMSF have been recorded in the correct period; and
- Classification – benefits paid by the SMSF have been recorded in the applicable accounts including the applicable member's account.

280. Audit risks to be considered in relation to auditing benefits may include, but are not limited to:

- Payment of a benefit to which the member or beneficiary is not entitled, providing early access to benefits.
- Incorrect calculation of a benefit payment.
- Payment of a benefit to an incorrect member or beneficiary.
- Pension payments not paid in cash
- Minimum payments not made for all pensions and the maximum payment for a TRIS is exceeded.

281. For death benefits, the auditor establishes if a binding death benefit nomination exists, and determines that the specific trust deed requirements have been met following the death of a member.

282. Upon the death of a pensioner, many SMSF pensions are reversionary and continue to pay the pension to the surviving spouse or reversionary beneficiary. The reversionary feature is generally established at commencement of the pension, but some fund's governing rules may permit establishment under a discretionary power in the deed. The auditor, in the case of the death of a pensioner with a reversionary benefit, checks that the pension is being paid to the nominated reversionary beneficiary and that the benefit has not been transferred to reserves or paid out as a lump sum.

Divorce and Splitting of Benefits

283. In circumstances where a member's benefit within a SMSF is subject to a property settlement upon divorce or a "splitting arrangement", the auditor reviews the documentation supporting the splitting of the benefit. A settlement is evidenced by one or more of the following documents:

(a) Superannuation agreement – negotiated between the divorcing parties and certified by two legal practitioners who represent the respective divorcing parties;

(b) Consent order – an order of the court frequently negotiated between two legal practitioners who represent the respective divorcing parties and submitted to the court for approval;

(c) Arbitrated court order – where the divorcing parties are unable to agree on the settlement terms and the court decides the settlement amount and terms;

(d) Notice by a non-member;[99]

(e) Notice by a trustee of information regarding an interest subject to a payment split;[100]

[99] See notice under regulation 72 of the *Family Law* (*Superannuation*) *Regulations 2001*.
[100] See notice under regulation 2.36C of the SISR.

(f) Payment split notice by a trustee to both member and non-member;[101] and

(g) One of the following notices by the non-member spouse to the trustees to:

(i) create a new interest;[102]

(ii) rollover or transfer benefits;[103] or

(iii) pay a lump sum where a non-member has met a condition for release.[104]

284. Once an order or agreement has been executed properly, the trustees are required to implement the order or agreement. In general, this may mean one of the parties exits the SMSF. Where there is a two member SMSF, the exiting member may take part of the other party's interest as well as their own. The auditor then treats the exit as per a normal member rollover or cashing out of a benefit. The auditor is careful to ensure that any capital gains issues are addressed, and that the tax components and preservation status of the superannuation payments are maintained. If a member exits the SMSF, the remaining trustee needs to ensure compliance with section 17A by:

(a) appointing a new individual trustee; or

(b) appointing a corporate trustee of which the remaining member is the sole director or one of two directors.

285. Due to the potential complexities and subtleties of the court orders, the possibility that court orders inadvertently conflict with the SISA or SISR exists, the auditor may seek legal advice where benefits payments under a court order may be in contravention of the SISA or SISR.

Other Audit Considerations

Going Concern

286. The SMSF's financial report is prepared on the basis that the SMSF is a going concern. Under ASA 570, the auditor is required to consider and remain alert to whether there are any events, conditions and related business risks which may cast significant doubt on the SMSF's ability to continue as a going concern.[105] In assessing going concern, the auditor considers the period of approximately 12 months following the date of the current auditor's report, being the period to the expected date of the auditor's report for the next annual reporting period.

287. To view a SMSF as a going concern, the SMSF is expected to be able to pay its debts as and when they fall due and continue in operation without any intention or necessity to liquidate or otherwise wind up its operations. For a SMSF, the primary concern is whether the SMSF will be able to pay benefits and entitlements to members, in addition to tax, audit and other expenses, payable over the coming year. If the SMSF is in an unsatisfactory financial position for the purposes of reporting under SISA section 130,[106] the auditor still makes a separate assessment as to whether the SMSF is a going concern in forming their opinion on the financial report.

288. The auditor is concerned with whether the net assets of the SMSF exceed the vested benefits, which are payable to members irrespective of whether they continue as a member. If there is a deficiency in net assets with respect to vested benefits the SMSF may not be a going concern, so the auditor undertakes further audit procedures to investigate the deficiency. These

[101] See notice under regulation 7A.03 of the SISR.
[102] See notice under regulation 7A.03C or 7A.05 of the SISR.
[103] See notice under regulation 7A.03D or 7A.06 of the SISR.
[104] See notice under regulations 7A.03E or 7A.07 of the SISR.
[105] ASA 570 provides requirements and guidance to the auditor where going concern issues exist.
[106] Reporting an unsatisfactory financial position to the ATO is addressed in the compliance engagement, paragraph 361 of this Guidance Statement.

procedures include identifying whether an actuarially determined technical insolvency program is in place and assessing whether it enables the SMSF to continue as a going concern. The trustee is required to initiate a technical insolvency program, designed by an actuary to return the SMSF to a solvent position within five years, if the SMSF is technically insolvent under the SISR.[107] An accumulation fund is technically insolvent under the SISR if the net realisable value of the assets of the SMSF is less than the minimum guaranteed benefits to members.[108]

289. If the SMSF is technically insolvent, the auditor ascertains whether a special funding and solvency certificate has been obtained by the trustee and a technical insolvency program initiated, to ensure that the SMSF is in a solvent position within five years, or alternatively winding-up proceedings have been initiated, as required under the SISR.[109] The auditor assesses whether any technical insolvency program enables the SMSF to continue as a going concern. If winding-up proceedings have commenced the SMSF is not a going concern.

290. Having considered the matters described in paragraphs 244 to 247, under ASA 570, the auditor may conclude that either:

(a) an unmodified auditor's opinion may be issued due to the fact that:

(i) the auditor is satisfied that it is appropriate, based on all reasonably foreseeable circumstances facing the SMSF, for the financial report to be prepared on a going concern basis; or

(ii) there is an emphasis of matter section in the auditor's report regarding a going concern uncertainty, where there is adequate disclosure of the principal conditions which caused the auditor to question the going concern basis, including, as appropriate, the trustees' evaluation of their significance and possible effects and any funding plans and other mitigating factors; or

(b) a modified auditor's opinion is necessary due to the existence of a material uncertainty which may cast significant doubt on the SMSF's ability to continue as a going concern, expressed as:

(i) a qualified or adverse opinion in the auditor's report, where there is inadequate disclosure of the uncertainty; or

(c) a modified auditor's opinion is necessary, due to the fact that the SMSF will not be able to continue as a going concern where the financial report had been prepared on a going concern basis, expressed as an adverse opinion.

291. Under ASA 570, the auditor communicates to the trustees if a modified opinion is to be issued in relation to going concern. This communication may be done in conjunction with communication of other matters of governance interest arising from the audit, discussed further in paragraphs 261 to 265.

Subsequent Events

292. ASA 560 requires the auditor to apply audit procedures designed to obtain sufficient appropriate audit evidence that all events up to the date of the auditor's report that may require adjustment of, or disclosure in, the financial report have been identified. Under ASA 560, audit procedures to identify such events, are performed as near as practicable to the date of the auditor's report and may include reading the trustees' minutes, making enquiries of the SMSF's lawyers concerning litigation or a divorce and making enquiries of the trustees as to

[107] See regulation 9.38(1) of the SISR.
[108] See regulation 9.35 of the SISR.
[109] See regulation 9.17 of the SISR.

whether any subsequent events have occurred which might affect the financial report, such as sales of investments or significant adjustments to investment values.

293. The auditor's response to the subsequent events depends on the potential for such events to affect the financial report and the appropriateness of the auditor's opinion. For example, if the trustees decide to wind up the SMSF, this would be a material event requiring appropriate disclosure and amendments, such as valuation adjustments, to the financial report. Whereas, if an immaterial investment of the SMSF became worthless, this may not warrant any amendment.

Winding-Up

294. If the trustees decide to wind up the SMSF, the SMSF still needs to be audited for the relevant financial year.

295. Upon winding-up, an audit is performed with increased focus in the areas of:

- Liquidated investments – to determine whether they were realised for cash or transferred in-specie and what value was received;
- Benefit payments – to test that they are bona fide, calculated correctly and paid to the correct individual and the recipients have met a condition of release;
- Final income year that the tax and lodgement levy has been paid;
- Cash – to ensure there are no transactions post balance date and that the balance is nil at balance date. This may include accounting for any tax refunds that were due to be paid to the fund; and
- Rollovers – to test whether they were paid to and received by complying superannuation funds.

296. If the fund's bank account remains open with a small balance in order to attend to the final wind-up expenses, such as tax payments and accounting and audit fees, the auditor may consider modifying their opinion. The auditor would undertake a post balance review required to assess whether the bank account has been closed.

Change of Auditor

297. When a SMSFs audit is transferred from one auditor to another, the new auditor needs to follow ASA 510 to determine whether the opening balances contain misstatements that materially affect the current period's financial report, whether the prior year closing balances have been correctly brought forward and that appropriate accounting policies are applied consistently. The auditor obtains the prior year signed audit report and undertakes further investigation if the report was modified.

Anti-Money Laundering

298. The Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act) is legislation designed to deter money laundering and terrorism financing. The AML/CTF Act sets out which entities are reporting entities and then imposes obligations on them when they provide one or more of the 'designated services' as set out in the AML/CTF Act. SMSFs do not provide a designated service and accordingly are not required to report under the AML/CTF Act. Auditors of SMSFs also have no formal AML/CTF reporting obligations, but they remain alert to potential money laundering or terrorist activities and report suspicions voluntarily, if appropriate.

Reporting

299. With respect to the financial audit, the SISA, section 35C, requires the auditor to:

(a) give a report to the trustees, in the approved form, on the financial operations of the entity for that year; and

(b) give the trustees the auditor's report in the approved form,[110] as issued by the ATO, within the prescribed time as set out in the SISR, being a day before the latest date stipulated by the ATO for lodgement of the Annual Return.[111]

300. ASA 700 requires the auditor to form an opinion as to whether the financial report is prepared, in all material respects, in accordance with the applicable financial reporting framework. In order to form that opinion the standard requires the auditor to conclude as to whether the auditor has obtained reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error.

301. ASA 220 requires that before the auditor's report is issued, the auditor performs a review of the audit documentation and conducts a discussion with the engagement team, in order to be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached.

302. In forming an opinion, the auditor considers all relevant evidence obtained, regardless of whether it appears to corroborate, or to contradict, information contained in the financial report.

Modifications to the Auditor's Opinion

303. Modifications to the auditor's opinion may be either:

(a) a qualified opinion;

(b) an adverse opinion; or

(c) a disclaimer of opinion.

ASA 705 contains requirements and guidance regarding when a modification to the auditor's opinion on the financial audit is necessary.

Modified opinion

304. ASA 705 requires an auditor to modify their opinion in the audit report when:

(a) based on the audit evidence the financial report is not free from, material misstatement.

(b) the auditor is unable to obtain sufficient appropriate audit evidence to conclude the financial report is free from material misstatement.

An example in the context of a SMSF audit is where the auditor is not able to obtain evidence of the (market) valuation of unlisted investments.

Qualified opinion

110 The ATO approved form auditor's report is available at www.ato.gov.au/superfunds
111 See regulation 8.03 of the SISR.

305. ASA 705 requires an auditor to qualify their opinion when:

(a) based on sufficient audit evidence, they conclude there are material misstatements in the financial report or;

(b) they are unable to obtain sufficient appropriate evidence to base the opinion but concludes that the possible effects on the financial report of undetected misstatements could be material.

Ryan Wealth Holdings Pty Ltd v Baumgartner [2018] NSWSC 1502 - a NSW Supreme Court appeal - examined a significant loss within a SMSF due to material misstatement of the financial statements and found the fund's auditor was liable for 80% of the loss incurred due to their negligence in not qualifying the audit report.

The auditor's inability to obtain sufficient appropriate audit evidence may arise from circumstances beyond the control of the entity, circumstances relating to the nature or timing of the auditor's work or limitations imposed by management. Examples of circumstances beyond the control of the entity include when the entity's accounting records have been destroyed. A qualified opinion is expressed as being "except for" the effects of the matter to which the qualification relates. The opinion paragraph is headed "Qualified Opinion".

Adverse Opinion

306. ASA 705 requires the auditor to express an adverse opinion when, having obtained sufficient appropriate audit evidence, they conclude that misstatements, individually or in the aggregate, are both material and pervasive to the financial report.

The opinion paragraph is headed "Adverse Opinion".

Disclaimer Opinion

307. A disclaimer of opinion is expressed when the possible effect of an inability to obtain sufficient appropriate evidence is so material and pervasive that the auditor, is unable to express an opinion on the financial report as a whole.

Paragraph 13 of ASA 702 requires an auditor to:

(a) Withdraw from the audit, where practicable and possible under applicable law or regulation; or (Ref: Para. A13)

(b) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial report. (Ref. Para. A14).In these circumstances, the opinion paragraph is headed "Disclaimer of Opinion".

Emphasis of Matter

308. ASA 800 requires an auditor's report (for a SMSF) to include an emphasis of matter paragraph to highlight the financial report is prepared in accordance with a special purpose framework and as a result, the financial report may not be suitable for another purpose. The inclusion of an emphasis of matter paragraph does not affect the auditor's opinion, but draws the user's attention to the matter raised. ASA 706 contains the requirements and guidance regarding an emphasis of matter paragraph. The ATO approved form auditor's report[112] includes the required wording.

[112] The ATO approved form auditor's report can be found on the ATO's website www.ato.gov.au/Superfunds form NAT 11466.

309. An auditor's report may also include an emphasis of matter paragraph to highlight:

(a) that a material uncertainty exists regarding a going concern matter that is adequately disclosed in the financial report;

(b) that additional disclosure is required to highlight that the financial report may be potentially misleading; or

(c) that the financial report has been revised due to the discovery of a subsequent fact, and replaces a previously issued financial report for which an auditor's report was issued.

The addition of an emphasis of matter paragraph does not affect the auditor's opinion, but draws the users' attention to the matter raised.

Other Matter

310. An auditor's report may include an other matter paragraph to highlight:

(a) information about the auditor's responsibilities, the audit or the auditor's report;

(b) that the financial report of the prior period was audited by the predecessor auditor, the type of opinion expressed, the reasons if the opinion was modified and the date of the report; or

(c) that the auditor's opinion on a prior period financial report differs from the opinion the auditor previously expressed.

ASA 706 contains the requirements and guidance regarding when another matter paragraph is necessary in the auditor's report and the ATO approved form auditor's report includes the required wording.

311. Whenever the auditor expresses a modified opinion, a clear description of all the substantive reasons is included in the auditor's report and, unless impracticable, a quantification of the possible effect on the financial report. If the effects or possible effects are incapable of being measured reliably, a statement to that effect and the reasons therefore are included in the basis for modification paragraph of the auditor's report.

Auditors to Act Independently

312. Two NSW Supreme Court appeals, found the auditors to have contributory negligence for losses incurred by the respective SMSFs following financial statement misrepresentation.

313. In Ryan Wealth Holdings Pty Ltd v Baumgartner [2018] NSWSC 1502, the auditor argued the accountant that prepared the financial statements should have been aware that they did not represent the financial position of the fund, however the Court disagreed and found the auditor had 'significant ability' to prevent loss and should have been more attuned to the inherent risks.

The auditor agreed that an unqualified audit report for the Statements should not have been issued and conceded that it didn't have enough evidence to issue an unqualified audit report for the Compliance Audit. The appeal judge awarded 80% of damages (amounting to over $2m) against the SMSF auditor.

314. Cam & Bear Pty Ltd v McGoldrick [2018] NSWCA 110 involved the misappropriation of $950,000 of capital by an adviser, which went undetected due to the failure of the SMSF auditor to verify the existance and value of the assets being recorded as "cash"in the financial statements. The appeal court found the financial year statements were a misrepresentation of the state of affairs of the fund and found that the auditor should have alerted the Trustee to the true status of the fund's investments.

The Court of Appeal awarded the trustee damages for its loss, less a deduction of 10% for its contributory negligence.

The main reason for the appeal being allowed was that the trustee lacked the experience and expertise to understand the concepts involved. The fund's auditor was engaged for the purpose of protecting the fund against financial risks but was negligent in failing to make proper enquiries as to the recoverability of the amounts held by an unlisted company and recorded as cash in the SMSFs financial statements.

Communication of Audit Matters

315. Under ASA 260, the auditor communicates matters of governance interest arising from the audit to the trustees on a timely basis, to enable the trustees to take appropriate action. Ordinarily, the auditor initially discusses with the trustees and/or management those matters arising from an audit that are causing concern, including expected modifications, if any, to the auditor's report. This provides the trustees with an opportunity to clarify facts and issues and to provide further information.

316. The auditor is also required under ASA 260 to inform the trustees of those uncorrected misstatements, other than clearly trivial amounts, aggregated by the auditor during the audit that were determined to be immaterial, both individually and in the aggregate, to the financial report taken as a whole.

317. Under ASA 260, the communication may be made orally or in writing, however, to meet the documentation requirements of ASA 230, the matters communicated and any responses need to be documented in the audit working papers. Oral communications may need to be confirmed in writing depending on the nature, sensitivity and significance of the discussions.

318. Under ASA 265, the auditor communicates deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgement, are of sufficient importance to merit their respective attentions.

319. Under ASA 250, any non-compliance which the auditor considers to be intentional and material, is communicated to the trustees without delay. The auditor's statutory reporting responsibilities in relation to matters of non-compliance may also necessitate reporting of such matters to the trustees and the ATO under section 129 of the SISA (see paragraphs 360-367).

PART B – COMPLIANCE ENGAGEMENT

320. The compliance engagement of a SMSF is driven by the provisions of the SISA and SISR specified in the approved form auditor's report and in the ACR, which comprise the compliance criteria for the engagement. These criteria can be grouped within the following categories:

(a) establishment and operation of the SMSF;

(b) sole purpose;

(c) investment considerations;

(d) benefits restrictions;

(e) contributions restrictions;

(f) investment returns;

(g) solvency; and

(h) other regulatory information.

321. The specific criteria and corresponding provisions of the SISA and SISR which are required to be reported on in the auditor's report and the ACR under each of these categories are listed in Table 1 below. From time to time, the SISA, SISR and the approved form auditor's report may be amended and new Tax Rulings and Interpretive Decisions may be issued by the ATO. In these circumstances, the auditor will need to adapt the approach in this Guidance Statement to address changes to the compliance criteria.

322. The auditor may use a checklist as an aid in conducting and documenting the compliance engagement. Standardised checklists are available from a number of professional organisations. Auditors verify the completeness of any compliance checklist they use to ensure it covers all relevant provisions, as the Independent Auditor's Report is updated annually.[113]

[113] The ATO's electronic superannuation audit tool (eSAT), may provide assistance and is available on the ATO website (www.ato.gov.au/eSAT).

Table 1: Summary of Criteria for Compliance Engagement

This table provides a summary of the sections of the SISA and SISR which are the criteria reported on in Part B: Compliance report of the approved form auditor's report and/or in the ACR.

Category	**Specific Criteria**	**Auditor's Report[114] Part B SISA/SISR**	**ACR[115] SISA/SISR**
Establishment and operation of the SMSF	Meets the definition of a SMSF.	S.17A	S.17A
	Trustees are not disqualified persons.	S.126K	S.126K
	Maintains minutes and records for at least 10 years.	S.103	S.103
	Maintains trustees' declarations about understanding their duties for those who become trustees for the first time after 30 June 2007, kept for as long as relevant or at least for 10 years.	S.104A	S.104A
	Maintains up to date records of all trustee changes, and copies of consent to act for a period of at least 10 years.	S.104[116]	
	Maintains copies of all member or beneficiary reports for a minimum of 10 years.	S.105[117]	
	Proper accounting records kept and retained for at least 5 years.	S.35AE	-
	Annual financial report prepared, signed and retained for 5 years.	S.35B	-
	Trustee provides auditor documents within 14 days of written request.	S.35C(2)	S.35C(2)
	Trustees formulate, review regularly and give effect to an investment strategy.	R.4.09	R.4.09
Sole purpose	Established for the sole purpose of funding a member's benefits for retirement, attainment of a certain age, death, ill-health or termination of employment.	S.62	S.62
Investment considerations	Restrictions on investments in collectables and personal use assets	R.13.18AA	R.13.18AA
	Restrictions on acquiring or holding "in-house" assets.	Ss.82-85	Ss.82 -.85
	Restrictions on acquisitions of assets from related parties.	S.66	S.66
	Maintains arm's length investments.	S.109	S.109
	Maintains SMSF money and other assets separate from those of the trustees, employer-sponsors and other related parties.	R.4.09A	S.52B(2)(d) or R.4.09A
	Prohibition on lending or providing financial assistance to member or relative.	S.65	S.65
	Restrictions on borrowings.	S.67, S.67A, S.67B	S.67
	Prohibition on charges over SMSF assets.	R.13.14	R.13.14

114 Self-Managed Superannuation Fund Independent Auditor's Report for periods commencing 1 July 2016 (NAT 11466).
115 Auditor-actuary contravention report (ACR) (NAT 11239) available through the ATO's website using eSAT or by ordering a paper form.
116 Section 104 of the SISA is a requirement that was included in the ATO approved form auditor's report for the periods commencing on or after 1 July 2014, but was not included in the ATO approved form auditor's report for the previous period.
117 Section 105 of the SISA is a requirement that was included in the ATO approved form auditor's report for the periods commencing on or after 1 July 2014, but was not included in the approved form auditor's report for the previous period.

Category	**Specific Criteria**	**Auditor's Report[114] Part B SISA/SISR**	**ACR[115] SISA/SISR**
	Assets valued at market value	R.8.02B	R.8.02B
Category	Specific Criteria	Auditor's Report Part B SISA/SISR	ACR SISA/SISR
Benefits restrictions	Trustees maintain members' minimum benefits.	R.5.08	R.5.08
	Minimum pension amount to be paid annually.	R.1.06(9A)	-
	Restrictions on payment of benefits.	R.6.17	R.6.17
	Prohibition on assignment of members' superannuation interest.	R.13.12	-
	Prohibition on creating charges over members' benefits.	R.13.13	-
Contributions restrictions	Accepts contributions within specified restrictions.	R.7.04	R.7.04
Investment returns	Reserves to be used appropriately and investment returns must be allocated to members' accounts in a manner that is fair and reasonable.	R. 5.03	-
Solvency	Unsatisfactory financial position.	-	S.130[118]
Other regulatory information	Information regarding the SMSF or trustees which may assist the ATO, including compliance with other relevant SISA sections and SISR regulations.	-	Ss129S and 130A[119]

Materiality

323. In planning and performing the compliance engagement, ASAE 3100 requires the auditor to consider materiality and compliance engagement risk. In assessing materiality, the auditor considers qualitative and quantitative factors.

324. In determining whether a contravention identified is material, and therefore whether a modification to the auditor's report is warranted, the auditor considers factors such as:

- The quantum of the breach;
- The time taken to rectify the breach, or if not yet rectified, the trustees' proposed actions and timeline for rectification;
- Whether the auditor has previously reported a similar breach to the trustee;
- The extent to which a limit has been exceeded or a statutory deadline missed;
- Whether the breach was intentional; and
- Actual or potential damage to members of a breach of the SISA or SISR occurring.

118 Unsatisfactory financial position is reported separately from other contraventions in Section F of the ACR and the seven tests set out in the ACR instructions are not applicable. Also see Reg 9.04 of the SISR for the narrow definition of "unsatisfactory financial position."

119 Other regulatory information is reported separately from other contraventions in Section G of the ACR and the seven tests set out in the ACR instructions are not applicable.

Establishment and Operation of the SMSF

325. In auditing the SMSF's compliance with the requirements regarding establishment and operation of the SMSF, the auditor conducts testing to determine that:

(a) the SMSF meets the definition of a SMSF;

(b) the trustees are not disqualified persons;

(c) the SMSF's minutes and records are retained for at least 10 years;

(d) the SMSF has and retains trustee declarations of duties signed by any new trustees after 30 June 2007 for at least 10 years;

(e) the SMSF's accounting records are kept and retained for five years;

(f) annual financial reports have been prepared for the SMSF, either signed by two individual trustees, two directors of the corporate trustee or the sole director of the corporate trustee, and retained for five years along with the SMSF's accounts;

(g) the SMSF has not entered into any contract or act that may prevent or hinder the trustees from properly performing or exercising their powers and functions; and

(h) an investment strategy which takes into account the risk, diversification, cash flows and liquidity of the SMSF has been formulated, given effect and reviewed regularly. The investment strategy must also consider if insurance is relevant to the members of the fund.

In addition, the auditor can expect the trustees to provide documents within 14 days that are requested in writing and are relevant to the preparation of the auditor's report, as required under the SISA.[120]

Definition of SMSF

326. To determine if the SMSF meets the definition of a SMSF,[121] the auditor may conduct procedures including:

- Examination of the fund's governing rules, member applications and minutes of trustees' meetings to identify the members and trustees and that they comply with the relevant legislation;
- A company search to ascertain if the directorship of a trustee company is consistent with the requirements of section 17A of the SISA;
- Enquiry to identify members, employers and trustees and their relationships with one another'
- Testing SMSF payments to ensure no payments have been made to the trustees for duties or services to the SMSF in their capacity as trustee. Section 17B of the SISA allows situations whereby a trustee and director of corporate trustees may be remunerated for their non-trustee duties or services; and
- Obtaining trustee representations.

[120] See subsection 35C(2) of the SISA.

[121] The definition of a SMSF is in section 17A of the SISA. Also refer to SMSFR 2010/2. The scope and operation of subparagraph 17(A)(3)(b)(ii) of the SISA and ATO ID 2010/139 Subparagraph 17(A)(3)(b)(i) of the SISA – tribunal appointed administrator of the plenary estate of a person with a mental disability.

Disqualified Persons

327. An individual SMSF trustee is disqualified under the SISA[122] if they are:

   (a) convicted of an offence in respect of dishonest conduct in any country;

   (b) the subject of a civil penalty order under SISA;

   (c) an insolvent under administration (includes an undischarged bankrupt under the Bankruptcy Act 1966); or

   (d) disqualified by the ATO.

328. A corporate trustee is disqualified if:

   (a) a responsible officer is a disqualified person; or

   (b) the company is in receivership, administration, provisional liquidation or has begun winding-up proceedings.

329. Ordinarily, the auditor verifies that the trustees are not disqualified by obtaining trustee representations to that effect. For new engagements, as well as periodically for continuing audits, the auditor seeks independent verification of the trustee status.

330. The ATO publishes a *Disqualified trustee register* that is compiled from the *Government Notices Gazette.* The register is updated quarterly and lists individuals that have been disqualified since 2012.

331. In addition, ASIC provides details of disqualified persons in respect of corporate trustees. Auditors are able to search the 'banned and disqualified register' on the ASIC website for information about individuals who have been disqualified from involvement in the management of a company.

332. During the course of the audit the auditor remains alert to circumstances which may indicate that a trustee may be technically disqualified, such as personal financial difficulties or a trustee's involvement in legal proceedings. In this case, the auditor may make enquiries such as checking the trustee's details againstASFA's National Personal Insolvency Index that lists bankrupts as well as the Bankruptcy Register Search (BRS)or other commercial databases providing record search facilities.

Maintenance and Provision of SMSF Records

333. The auditor obtains representations from the trustees that the minutes and records of meetings have been held for at least 10 years, that accounting records and financial reports have been retained for 5 years, that member or beneficiary reports have been retained for at least ten years, and that records of all changes to the fund trustee are up to date and for trustees appointed after 30 June 2007, they have signed and retained a "Trustee Declaration" for at least ten years.[124]

334. The SISA requires that the records be kept in the English language or a form that is readily convertible to English[125] and be kept in Australia (or another country if the Regulator gives approval for the records to be kept in another country). Generally, investment documentation

[122] See subsection 120(1) of the SISA. Also refer to ATO ID 2011/24 *Waiver of disqualified person status – meaning of* '*serious dishonest conduct'*.
[124] The *Trustee Declaration* is an approved form issued by the ATO (NAT 71089), available from the ATO's website at www.ato.gov.au.
[125] See section 35A of the SISA.

in a foreign language, required as audit evidence, is translated at the SMSF's expense into English. This facilitates more efficient and effective auditing and quality control.

335. The auditor may request that the trustees provide documents required to conduct the audit. If trustees fail to provide the documents required within the specified time period, this is a compliance breach which, if material, should result in a qualified auditor's report provided a written request was made under section 35C (2) of SISA and the documents were not supplied within 14 days. ATO reporting is also required if the information has not been provided to the auditor within 28 days of the auditor's request for the information.

Contracts Restricting Trustees' Functions and Powers

336. The auditor considers contracts entered into on behalf of the SMSF, the governing rules and any other arrangements in the light of the SISA's prohibition on entering a contract or doing anything which prevents the trustees from, or hinders the trustees in, properly performing or exercising their functions and powers.[126] The auditor may obtain representations from the trustees that no such arrangement has been entered into.

Investment Strategy

337. In the approved form auditor's report the auditor states that their procedures "included testing that the fund trustee has an investment strategy, that the trustee has given consideration to risk, return, liquidity, diversification, the insurance needs of the fund members, and that the fund's investments are made in line with that investment strategy". The SISR[127] requires the trustees of a SMSF to formulate, regularly review and give effect to an investment strategy that has regard to all the circumstances of the SMSF, including:

- The risk involved in making, holding and realising, and the likely return from, the SMSF's investments, having regard to its objectives and expected cash flow requirements;
- The composition of the SMSF's investments as a whole, including the extent to which they are diverse or involve exposure of the SMSF to risks from inadequate diversification;
- The liquidity of the SMSF's investments, having regard to its expected cash flow requirement;.
- The ability of the SMSF to discharge its existing and prospective liabilities; and
- Whether the trustees of the fund should hold a contract of insurance that provides insurance cover for one or more members of the fund.

338. Ordinarily, the investment strategy is documented in writing and the auditor assesses that the trustees have properly considered all the circumstances of the SMSF, however the auditor is not required to assess whether the investment strategy is adequate to meet the long term investment needs of the SMSF and the auditor states in their report that "no opinion is made on the investment strategy or its appropriateness to the fund members".

339. In order to determine whether the trustees have given effect to the investment strategy, the auditor assesses whether the investments made during the period are invested according to the documented investment strategy as approved by the trustees. Case law provides further authority to the requirement for SMSF auditors to conduct their enquiries independently and to communicate any weaknesses with the trustee directly. [128]

[126] See section 52(2)(e) of the SISA.
[127] See regulation 4.09 of the SISR.
[128] *Ryan Wealth Holdings Pty Ltd v Baumgartner NSWSC [1502],*

340. The auditor obtains evidence as to whether the trustees have reviewed or modified their investment strategy during the period to accommodate the SMSF's changing needs and changes in the investment environment.

341. The frequency that a trustee should review the fund's investment strategy in order to satisfy the requirements of Regulation 4.09 of the SISR is not specified, and it is the role of the trustee to determine what is appropriate to meet the requirement. The expectation from the ATO is that this would be at least annually. The role of the auditor is to use professional judgement in determining if this requirement has been met.

Sole Purpose

342. The SISA[129] requires the trustees to ensure that the SMSF is maintained solely for one or more of the allowable core purposes and, in addition, may also be maintained for one or more of the allowable ancillary purposes. The allowable core purposes are the provision of benefits for each member on their retirement, attainment of a prescribed age or death prior to retirement or attaining the prescribed age. The allowable ancillary purposes are the provision of benefits for each member on termination of employment, cessation of work due to ill-health, death after retirement or attainment of a prescribed age, or a benefit approved by the ATO. The "sole purpose test" is a conceptual test that when satisfied demonstrates that the SMSF has in fact been maintained solely for allowable purposes ("exclusivity of purpose") and requires a higher standard than maintenance of the SMSF for a dominant or principal purpose. The approved form auditor's report, requires the auditor to separately state that their procedures "included testing that the fund's governing rules establishes the fund solely for the provision of retirement benefits for fund members or their dependents in the case of a member's death before retirement".

343. The trustees of a SMSF are required to maintain the fund in a manner that complies with the sole purpose test at all times while the SMSF is in existence. This extends to all activities of the SMSF including:

- Accepting contributions;
- Acquiring and investing the SMSF's assets;
- Administering the funds;
- Employing and using the SMSF's assets; and
- Paying benefits, including those benefits on or after retirement.

344. In assessing whether a SMSF has complied with the sole purpose test, the auditor may refer to the ATO's Ruling SMSFR 2008/2 on the application of the sole purpose test to circumstances where the SMSF is maintained for the purposes prescribed while providing benefits, particularly to members or related parties, other than those specified in section 62 of the SISA. SMSFR 2008/2 states that a SMSF may still satisfy the sole purpose test despite the provision of benefits not specified in section 62, if the benefits are "incidental, remote or insignificant". In order to determine whether the benefits are incidental, remote or insignificant, the circumstances surrounding the SMSF's maintenance need to be viewed "holistically and objectively". Case law provides authority to the practical application of section 62 and the ATO has reviewed the Ruling, and issued a decision impact statement as a result to further clarify their position as Regulator.[130]

345. In assuring compliance with the sole purpose test, the auditor looks for the provision of current day benefits, being benefits to a member or related party before the member's retirement,

[129] See section 62 of the SISA.
[130] Aussiegolfa Pty Ltd (trustee) v Federal Commissioner of Taxation (VID 54 of 2018 VID 83 of 2018)

employment termination or death, and assesses whether those benefits fail the sole purpose test. Furthermore, the SISR[131] contains strict regulations in relation to collectables and personal use assets. In-house assets are discussed further in paragraphs 300 to 302, while collectables and personal use assets are discussed further in paragraphs 296 to 299.

346. Current day benefits are likely to fail the sole purpose test if the benefit:

- Was negotiated or sought-out by the trustees;
- Has influenced the decision making of the trustee;.
- Has been provided at a cost or financial detriment to the SMSF; and
- Is part of a pattern or preponderance of events which, when viewed in their entirety, amount to a material benefit being provided that is not specified under section 62(1).

347. Current day benefits are more likely to comply with the sole purpose test if:

- The benefit is an inherent and unavoidable part of activities for allowable purposes;
- The benefit is remote, isolated or insignificant;
- The benefit is provided on arm's length commercial terms, at no cost or financial detriment to the SMSF;.
- The trustees comply with the covenants in section 52B of the SISA; and
- The benefit relates to activities which are part of a properly considered and formulated investment strategy.

348. The sole purpose test is complemented by other restrictions in SISA relating to dealings with members and related parties, such as prohibitions or restrictions on:

- Transactions not at arm's length;.[132]
- Loans or financial assistance to members or relatives;[133]
- Acquisitions from related parties;[134]
- Charges over assets;[135]
- Assignment of, or charges over, member's benefits;.[136]
- SMSF assets not held separately from the members' personal assets;[137]
- Acquisition of "in-house" assets in excess of 5% of the total market value of the SMSF assets;[138]and
- Collectables and personal use assets.[139]

[131] See regulation 13.18AA of the SISR.
[132] See section 109 of the SISA.
[133] See section 65 of the SISA.
[134] See section 66 of the SISA.
[135] See regulation 13.14 of the SISR.
[136] See regulations 13.12 and 13.13 of the SISR.
[137] See section 52B(2)(d) of the SISA and regulation 4.09A of the SISR.
[138] See part 8 of the SISA.
[139] See regulation 13.18AA of the SISR.

Breaches of one or more of these restrictions are usually indicative of circumstances establishing a breach of the sole purpose test.

Running a Business

349. The auditor remains alert to circumstances which indicate that the SMSF is running a business or conducting operations which may be akin to running a business, as this activity may breach the sole purpose test. Indications that a business is being conducted by the SMSF may include revenues from trading activities, employing staff and paying operating expenses. A business is not usually administered for the sole purpose of providing the allowable benefits to members or beneficiaries of the SMSF, as there is an inherent risk that running a business may jeopardise the members' benefits.[140] Although the operation of a business is not prohibited by the SIS, specific additional obligations need to be met by the fund to ensure on-going SIS compliance.

350. If a trustee is also an employee of the business, payment of salary or wages to the trustee must be on an arms-length basis. The auditor assesses all circumstances of a SMSF running a business to determine whether it is in breach of the SISA or SISR. It is also essential to ensure that the deed of the fund permits the trustee to operate a business.

351. SMSFs that engage in high volume trading of derivatives, listed securities, real property or other investments or a series of property developments may be running a business for purposes other than solely for providing specified benefits to members and beneficiaries. For SMSFs conducting activities of this kind, the auditor considers whether the activities are justified in giving effect to the investment strategy.

Units in a Related Unit Trust

352. Investments in related unit trusts, where trustees or members of the SMSF are also trustees of the related unit trust, are common SMSF investments. The auditor considers the sole purpose test in light of the investments held in, and by, the related unit trust to ensure that the investments held are for the long-term provision of allowable benefits to members and not to provide other benefits to the trustees, members or their relatives. The auditor may also need to consider whether the investment breaches the prohibition on acquisitions from related parties, the prohibition on borrowings or exceeds the "in-house" asset limits.[141] SIS obligations vary depending on the date the fund invested and whether the investment falls under the exception in Division 13.3A of the SISR.

Investment Considerations

353. The SISA contains a number of investment restrictions with which the trustees are required to comply. In assessing whether these prohibitions have been complied with, the auditor examines the nature of each material investment to ensure that the investment is permitted under the SISA.

Collectables and personal use assets

354. Collectables and personal use assets under the SISA and SISR are permitted investments for SMSFs provided the asset was not acquired to provide a personal benefit for the member or their related parties. Collectables or personal use assets[142] that are acquired by the fund on or

140 Also refer to SMSFR 2008/2: The application of the sole purpose test in section 62 of the SISA to the provision of benefits other than retirement, employment termination or death benefits.
141 See paragraphs 300-302.
142 Collectables and personal use asset list contained in Regulation 13.18AA(1) of the SISR.

after 1 July 2011 are subject to restrictions[143] contained in the regulation 13.18AA of the SISR including that:

- They must not be leased to any related party[144] of the fund;
- They must not be stored or displayed in the private residence of any related party of the fund;
- They cannot be used by any related party of the fund;
- Trustees are required to make a written record of the reasons for the decisions on where to store the collectables and personal use assets and keep the record for at least 10 years;
- They must be insured in the name of the fund within seven days of acquisition; and
- Transfers of ownership to related parties must be done at market value[145] determined by a qualified independent valuer.[146]
- The auditor obtains sufficient appropriate audit evidence that trustees have complied with the restrictions on collectable and personal use assets of the fund.

355. Membership investments, such as ski lodge, country club or golf club memberships, providing a right to use a facility or service, will usually fail the sole purpose test if the trustees or members derive a current day benefit from the investment. Furthermore, the SISR prohibits these lifestyle assets from being used by the member or related party of the fund.[147] The auditor may refer to the examples in ATO Ruling SMSFR 2008/02 to assist them in assessing whether or not an investment in a lifestyle asset is a breach of the SISA and SISR.

356. Investments in holiday houses or apartments need to be reviewed to ascertain if there has been use or enjoyment of the property by the trustees, members or a related party as this is a strong indication that the sole purpose test has been breached and may also render the investment an "in-house" asset,[148] in which case the in-house asset limits will apply. Furthermore, the SISR prohibits the use of such investments by members and related parties of the fund.[149]

357. Generally, investments that provide an ancillary benefit as part of the investment need to be examined to determine whether the investment as a whole meets the sole purpose test. Ancillary benefits include, but are not limited to, such things as a discount on a product or service, priority access to a facility, upgrades or free products or services.

"In-house Assets"

358. An "in-house" asset of a SMSF is an asset that is a loan to a 'related party' (defined term), an investment in a related party, an investment in a related trust or an asset of the SMSF subject to a lease between the trustees and a related party of the SMSF.[150] A related trust is a trust that a member or employer-sponsor controls.[151] There are a number of exceptions to the definition

143 Restrictions were subject to transitional arrangements. Collectables and personal use assets held by funds prior to 30 June 2011 were not subject to restrictions until 1 July 2016, at which time, trustees were required to comply with all restrictions. This transitional period provided SMSF trustees with existing investments in collectables and personal use assets time to comply with the rules.
144 Related party is defined in Section 10(1) of the SISA.
145 Market value is defined in Section 10(1) of the SISA.
146 See ATO's Valuation guidelines for self-managed superannuation fund (web-based).
147 See regulation 13.18AA(6) of the SISR.
148 See guidance on "in-house" assets is provided in paragraphs 300 to 302 of this Guidance Statement.
149 See regulation 13.18AA(6) of the SISR.
150 Defined in subsection 10(1) of the SISA. Also refer to SMSFR 2009/4 the meaning of 'asset', 'loan', 'investment in', 'lease' and 'lease arrangement' in the definition of an 'in-house asset' in the SISA.
151 Defined in subsection 10(1) of the SISA.

of in-house assets and transitional provisions included in Part 8 of the SISA.[152] The auditor needs to be familiar with these exceptions when considering in-house asset requirements.

359. The SISA has strict limits on the level of "in-house assets" permitted to be held by the SMSF. The market value of the in-house asset must not exceed 5% of the total market value of the SMSF's assets at the time of acquisition[153] and at year end.[154] Also the trustees are prohibited from acquiring an in-house asset that would cause the total of all in-house assets to exceed this 5% ratio. The auditor examines the investments of the SMSF to identify potential in-house assets to ensure that the legislative limits are not exceeded either when they were acquired or at year end.

360. The auditor remains alert to schemes intentionally entered into or carried out by the trustees which have the effect of artificially reducing the market value ratio of the SMSF's in-house assets, or by concealing the related party connection. Such actions are prohibited under the SISA.[155]

361. If the level of IHA exceeds 5%, the trustee is required to develop a written plan to reduce the level below 5% by the end of the following income year. Where a SMSF has IHA that are greater than the 5% limit, the auditor may obtain a copy of the rectification plan and include details of their testing in the audit working papers.

Acquisition of Assets from Related Parties

362. Trustees and investment managers are prohibited, under the SISA,[156] from acquiring assets from a related party unless the assets are acquired at market value and are either:

(a) listed securities;

(b) business real property;

(c) in-house assets within the 5% limit;

(d) life insurance policies that are not acquired from a member or relative; or

(e) assets which are ordinarily in-house assets but are exempted by the operation of section 71(1) of the SISA; and

(i) the asset is acquired at market value; and

(ii) the acquisition would not result in a breach of the 5% limit.

363. Business real property[157] is land and buildings used wholly and exclusively for business purposes.[158] It does not extend to:

(a) vacant land, unless used in primary production;

(b) land used for property development or shares held in an unlisted property owning company; or

(c) residential properties except where the residence provides accommodation that is in the nature of a business (e.g. for a motel); or the residence is on less than two hectares

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152 See also regulations 13.22B, 13.22C and 13.22D of the SISR. SMSFR 2009/1 is also relevant to the definition of business real property and the exceptions under S71(1) of SISA.
153 See section 83 of the SISA.
154 See section 82 of the SISA.
155 See section 85 of the SISA.
156 See section 66 of the SISA.
157 Defined in subsection 66(5) of the SISA. Refer to SMSFR 2010/1 for the application of subsection 66(1) of the SISA to the acquisition of an asset by a SMSF from a related party.
158 See SMSFR 2009/1 Business real property for the purposes of the SISA.

of a larger parcel of land which is predominately used in a primary production business.

364. Assets which would ordinarily be defined as in-house assets but which are exempt under the provisions of section 71(1) of the SISA include deposits with an approved deposit institution, an investment in a pooled superannuation trust where the trustee has acted on an arm's length basis, an asset which the regulator has determined is not an in-house asset, an investment in a widely held unit trust, and non-geared unit trusts which meet the other requirements of the SISR.[159]

365. Ordinarily, the auditor examines the documentation surrounding the purchase of material investments, to ascertain whether the vendor was a related party. This may involve checking the contract or sale document to confirm who the parties to the transaction were and, to the extent possible, their relationship with the trustees and members. The auditor makes enquiries in the planning phase of the audit in order to identify parties, whether individuals or entities related to the trustees or members.

Arm's Length Investments

366. The SISA[160] requires the trustees and investment managers to invest and maintain the SMSF's assets at arm's length. Indicators of non-arm's length investments may include:

- Investments in a related party;
- Investments being managed by a related party;
- Details of parties to a contract indicate related parties;
- Uncommercial or disadvantageous terms of a lease or loan;
- Acquisition or disposals of SMSF assets that do not appear to be at commercial rates;
- No formal contracts established for loan, lease or other arrangement;
- Assets, such as rental properties, deriving little or no income, or income well below commercial rates; and
- Investments which are inconsistent with the investment strategy or entered into without a sound rationale.

367. The auditor assesses all aspects of the transaction, including that the settlement terms, interest rates, rents, lease refurbishment term, warranties, security and repayment terms are commercial in nature in accordance with section 109 of the SISA. The SISA[161] requires that the terms and conditions of a transaction must not be more favourable to the other party than would be reasonably expected if the parties were at arms-length. ATO ID 2010/162 clarifies that there is no contravention of section 109 of the SISA if the terms are more favourable to the SMSF. However, if the terms are more favourable to the SMSF the asset and associated income will be treated as non-arm's length, resulting in the income (less associated expenses) being taxed as non-arm's length income, and the asset disposal being treated as a non-arm's length disposal.

159 See regulation 13.22A - 13.22D of the SISR
160 See section 109 of the SISA.
161 See section 109(1)(b) of the SISA.

Assets Held Separately

368. The trustees are required[162] to keep the money and the assets of the SMSF separate from their personal or business assets of the trustees and from the assets of standard employer-sponsors. The auditor examines the affairs of the SMSF to identify possible situations where the assets of the SMSF may have become intermingled with assets of the trustees or standard employer-sponsors. The auditor checks that the assets of the SMSF are registered in the SMSF's name or, where assets cannot be held directly by the SMSF (for example in some jurisdictions, a property title may not be able to be held in the name of the fund), there is other clear evidence that those assets are held beneficially on behalf of the SMSF, such as a declaration of trust or an acknowledgement of trust.

369. Where there has been a change in trustees, the auditor generally checks that the ownership documents for fund assets have been updated.

370. The auditor confirms that the SMSF maintains a separate bank account for all fund monies and examines payments and receipts to ascertain that dividends, interest and other income of the SMSF are not banked into personal or business accounts, particularly where a corporate trustee operates a number of bank accounts as well as conducting the affairs of the SMSF. The auditor may test that dividends declared for listed securities held are received and banked by the SMSF.

Loans and Financial Assistance to Members or their Relatives

371. SMSFs are not permitted to lend money or provide financial assistance to members or their relatives[163] and the approved form auditor's report states that the auditors procedures included "a review of investments to ensure the fund is not providing financial assistance to members, unless allowed under the legislation". The auditor examines the bank account and obtains explanations for material withdrawals and deposits in order to ascertain whether any loan or financial assistance benefit has been provided to a trustee, member or relative of a member or trustee. In certain circumstances, access by members or their relatives to SMSF funds may be considered to be an early access to benefits without meeting a condition of release.[164]

372. In cases where funds are accessed in error by the trustees for non-SMSF use, the breach may affect the audit opinion, unless the amount is immaterial, the event is infrequent and repayment is made in full. Interest at commercial rates may also be appropriate.

373. The auditor reviews the ownership of the SMSF's assets to ensure that a charge or other form of security has not been taken over any of the SMSF's assets to secure a member's or relative's borrowings, which would be a form of financial assistance. This may require performing a title search for the SMSF's real property to identify any encumbrances.

Borrowings

374. SMSFs are not permitted to borrow money,[165] with the exceptions[166] of borrowings:

(a) to pay a benefit, pension or superannuation contribution surcharge liability (no longer levied), for a maximum of 90 days for up to 10% of the value of the SMSF's assets;

(b) to cover settlement on a security transaction for a maximum period of seven days, for up to 10% of the value of the SMSF's assets provided that, at the time the relevant

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162 See subsection 52B(2)(d)of the SISA, and Regulation 4.09A of the SISR.

163 See section 65 of the SISA. Also refer to SMSFR 2008/1 Giving financial assistance using the resources of a SMSF to a member or relative of a member that is prohibited for the purposes of section 65(1)(b) of the SISA.

164 Determining whether benefits have been accessed prior to meeting a condition of release is a question of fact and any penalty is at the discretion of the ATO.

165 See section 67(1) of the SISA. Also refer to SMSFR 2009/2 The meaning of "borrow money" or "maintain an existing borrowing of money" for the purposes of section 67 of the SISA.

166 See sections 67 and 67(A) of the SISA.

investment decision was made, it was likely that the borrowing would not be needed; or

(c) that are part of a complying limited recourse borrowing arrangement.[167]

375. Ordinarily, the auditor reviews the bank statements to ascertain whether any non-compliant borrowings were made during the period, whether by way of an overdraft or a loan account.

376. Margin lending, in general, involves a borrowing arrangement where a loan is taken out using the listed securities purchased as security for that loan. Margin loan facilities breach the SISA and SISR by virtue of the fact that the borrowing is not an approved exception to the borrowing prohibition and SMSFs are not permitted to give a charge over some or all of the fund assets as required by a margin lending arrangement. If the SMSF is involved in trading of securities or derivatives, the auditor examines related documentation for indications of the existence of margin lending arrangements, such as interest payments on broker's statements, margin call payments or significant listed securities purchases without corresponding payments.

377. The auditor reviews any investments in derivatives, including options, futures, or swaps, to ascertain that the investments are in accordance with the investment strategy, any current legislative requirement and that the investment is not putting the assets of the SMSF at risk. Derivatives, due to their inherent nature, may be high risk and involve borrowings that may have recourse to the SMSF. Where the auditor is unsure of the legality of the investment, the auditor may need to seek legal advice as to whether the investment meets the investment restrictions. Active trading of derivatives may be construed as running a business and, consequently, may be a breach of the sole purpose test.

378. Where the SMSF has derivative instruments – a charge over assets that is required to be given for compliance with listing rules (covered calls), the auditor obtains the derivative risk statement prepared by the trustees and considers whether it complies with regulation 13.15A of the SISR.

379. Investments in limited recourse borrowing arrangements are an exception to the prohibition on borrowings. Limited recourse borrowing arrangements are complex financial arrangements whereby the SMSF buys an asset via a limited recourse agreement where there is some debt funding or borrowing to purchase the asset. The transaction is characterised by an asset held in trust for the SMSF, where the SMSF holds an interest in the income and the rights to acquire the asset. The SMSF may be required to make regular instalments or repayments. Recourse by the lender, against the fund trustee, in the case of failure to settle the loan, is required to be solely over, and limited to, the asset held in the trust arrangement. After commencing the borrowing, the SMSF is required to make at least one payment before purchasing the asset. Whilst there is no formal requirement for regular repayments / instalments, the lack of repayments may bring into question the commercial rationale of the underlying investment and whether the sole purpose test is being breached.

380. From 24 September 2007, superannuation funds were allowed to invest in certain limited recourse borrowing arrangements involving borrowing money to acquire a permitted asset. Those arrangements need to meet the conditions stipulated by the law in the former subsection 67(4A) of the SISA. Those rules continue to apply to limited recourse borrowing arrangements that were entered into before 7 July 2010.

381. For limited recourse borrowing arrangements[168] entered into by superannuation funds on or after 7 July 2010 or previous section 67(4A) debt arrangements that have been refinanced after 7 July 2010:

[167] See ATO Ruling SMSFR 2012/1 Self-Managed Superannuation Funds: limited recourse borrowing arrangements – application of key concepts (SMSFR 2012/1).

[168] See sections 67A and 67B of the SISA.

(a) the asset within the arrangement can only be replaced by a different asset[169] in very limited circumstances specified in the law;

(b) superannuation fund trustees cannot borrow to improve an asset[170] (for example, real property);

(c) the borrowing is permitted only over a single acquirable asset or a collection of identical assets that have the same market value;

(d) the asset within the arrangement is not subject to a charge other than to the lender in respect of the borrowing by the superannuation fund trustee.[171]

382. Procedures which the auditor may conduct in auditing compliance of limited recourse borrowing arrangements with the SISA and SISR may include:

- Examination of the fund's governing rules to determine if the SMSF is permitted to borrow;
- Examination of the investment strategy, or discussions with the trustees if there is no written investment strategy, to determine if limited recourse borrowing arrangements and the percentage of funds devoted to them are allowed within that strategy;
- Identification of the nature of the asset purchased and whether the vendor is a related party so as to ensure that the transaction is permitted under the SISA, SISR and the fund's governing rules;
- Determination of whether the debt arrangement or loan agreement is a limited-recourse agreement as required by the SISA,[172] whereby the other assets of the SMSF are not used as security for the loan;
- Determination of whether the finance is provided by a related party, such as a family trust, in order to identify any potential non arm's length dealings;
- Determination of whether the funds borrowed were used to purchase an asset held in the limited recourse borrowing arrangement;
- Determination of whether the funds borrowed have been used to improve an asset;
- Identification of whether the terms of the loan are commercial. Less than commercial interest rates may be a means of making additional contributions to the SMSF, whereas an excessively high interest rate may fail the sole purpose test, or potentially be a scheme to access benefits;
- Identification of any arrangements outside the SMSF, such as a personal guarantee, which may have recourse to the assets of the SMSF, other than the asset acquired (or any replacement), as this may be a breach of the borrowing restriction exception granted to limited recourse borrowing arrangements;
- Determination of whether the original asset has been added to in any way, either by additional shares or further purchases, since if the limited recourse borrowing asset has increased, this would indicate a further borrowing and therefore a potential breach of the prohibition on borrowing; and

[169] Table 2 in ATO ruling SMSFR 2012/1 provides illustrative guidance as to whether a change to a single acquirable asset results in a different asset.
[170] Table 1 in ATO ruling SMSFR 2012/1 provides illustrative guidance contrasting repairs or maintenance with improvements.
[171] See ATO ID 2010/162, ID 2010/184 and ID 2010/185 for further guidance.
[172] See subsection 67A(1) of the SISA.

- For limited recourse borrowing arrangements entered into from 1 July 2010, determination of whether:
  - a replacement to the asset has been made contrary to the law;
  - the fund has not borrowed to improve an asset in the arrangement;
  - the trust asset is a single asset or identical assets that have the same value, e.g. ordinary shares; and
  - there is no charge over the asset except per the limited recourse arrangement.[173]

Charges Over Assets

383. SMSFs are not permitted to use the assets of the SMSF to secure a debt facility[174] and, hence, charges and liens over assets are not permitted. Also, charges and liens over any member benefits are prohibited. Additional audit procedures include review of any bank confirmations for charges, title searches on properties of the SMSF to identify any charges or liens, the Personal Properties Securities Register for parties registering interests against other SMSF assets and examination of the accounting records or bank statements to identify any interest payments made by the SMSF, which may indicate a loan facility.

384. Similarly, the auditor ordinarily reviews the ownership of the SMSF's assets to ensure that a charge, or other form of security, has not been taken over any of the SMSF's assets. This may extend to reviewing any product disclosure statement relating to assets acquired to determine whether the product has any recourse to the SMSF. Even if the marketing or summary material claims there is no recourse to the SMSF, the auditor still checks the actual provisions of the arrangement.

385. Where the SMSF has investments in related or unlisted unit trusts, the auditor is alert to any borrowings the unit trust may have and whether there is any recourse to the SMSF. Where a related unit trust has allowed a charge over its assets or has a borrowing, the investment in the unit trust becomes and remains an in-house asset of the fund.

386. Ordinarily, the auditor requests the most recent financial report and tax return along with distribution statements for investments in unit trusts, to identify net asset value, any debts owing by the unit trust and income received and paid by the trust. In certain cases, the unit trust deed may be required to assist the auditor in assessing compliance.

Asset Valuation

387. The trustees are required to value fund assets at market value.[175] See paragraphs 163 to 171 for requirements and explanatory guidance on asset valuations.

Benefit Restrictions

388. The member's ability to receive a benefit normally depends on:

    (a) the type of benefit the member has accumulated in the SMSF;

    (b) the member's age and whether any preservation restrictions apply to the benefit; and

[173] See ATO SMSFR 2012/1 for further guidance on the requirements for limited recourse borrowing arrangements. Also see ATO ID 2010/162, 2010/184 and 2010/185.

[174] See regulation 13.14 of the SISR. Also see ATO IDs 2010/162, 2010/169, 2010/170, 2010/172, 2010/184 , 2010/185, 2014/39 and 2014/40.

[175] See regulation 8.02B of the SISR.

(c) whether the rules of the SMSF permit the benefit to be paid at the time.[176]

Minimum Benefits

389. The trustees are required[177] to maintain the members' minimum benefits until the benefits are paid out, rolled over or transferred.

Payment of Benefits

390. Generally, benefit payments are triggered due to a condition of release being met. The approved form auditor's report states that the auditor's procedures include testing "that no preserved benefits have been paid before a condition of release has been met". Conditions of release are specified in the SISR[178] and may be further restricted by the SMSF's governing rules. Conditions of release include retirement, reaching age 65, death, permanent or temporary incapacity, terminal medical condition, attaining the prescribed preservation age for a transition to retirement benefit,[179] severe financial hardship and compassionate grounds which are assessed by the Department of Human Services.[180]

391. For pension payments, the auditor ensures that any payments meet the minimum and maximum,[181] if required, payment conditions as stipulated in the SISA and SISR and an appropriate condition of release has been met. In particular, funds paying account based pensions are required to pay an annual minimum pension amount[182] which is calculated by applying a percentage rate, dependent on the member's age,[183] at the 1st July of the reporting year being audited, to the member's account balance. The auditor confirms that a series of payments have been made over the life of each pension account. Subsequent pension payments are reviewed to confirm that a series of payments has been made.

392. Where pension payments are less than the required minimum, the pension is taken to have ceased at the beginning of that year[187] and the income from assets that support the pension will not be tax exempt for the year.[188] The ATO guidelines Self-Managed superannuation funds – starting and stopping a superannuation income stream (pension)[189] outlines exceptions whereby the Commissioner may exercise discretion in allowing a SMSF to treat income as exempt pension income even though the minimum pension standards have not been met. Furthermore the guidelines outline the circumstances under which the ATO will allow a trustee to self-assess their entitlement to this concession.

393. In the year of death, reversionary pensions continue to be paid based on the minimum pension factor of the primary beneficiary. Thereafter, the pension factor that applies to the age of the beneficiary applies. If the minimum pension is not paid in the year of the death, the trustee can self-assess to treat the fund as continuing to pay the pension if the shortfall is small, or resulted from an error. In all other cases, the pension is deemed to have been stopped and accordingly, the trustee must ensure the death benefit is paid as soon as practicable. The options available for the payment of the death benefit include commencing a death benefit pension, paying the death benefit as a maximum of 2 lump-sums or, rolling over the death benefit to another superannuation fund for immediate cashing as a new death benefit pension. The trustee must

[176] More information is available on the ATO's website ato.gov.au (search under Paying benefits).
[177] See regulation 5.08 of the SISR.
[178] Conditions of release are listed in Schedule 1 and detailed in Part 6 of the SISR.
[179] Members need to reach their preservation age before commencing a transition to retirement benefit. This is age 55 for those born prior to 1 July 1960 and increasing up to age 60 for those born after 1 July 1964.
[180] Under part 6 of the SISA the Chief Executive of Medicare has the general administration of SISR regulations about the release of superannuation on compassionate grounds.
[181] Maximum payments exist for TRISs.
[182] See subregulation 1.06(9A)(a) of the SISR.
[183] See schedule 7 of the SISR.
[187] ATO Taxation Ruling TR 2013/5 explains when a superannuation income stream commences and ceases and consequently when a superannuation income stream is payable.
[188] See sub-regulation 1.06(9A) and Schedule 7 of SISR.
[189] ATO's guidelines *self-managed superannuation funds – starting and stopping a superannuation income stream* (*pension*) can be found on the ATO's website www.ato.gov.au/super/self-managed-super-funds (webpage only).

however consider the terms of the fund's trust deed along with any member nominations that are on file when determining how the death benefit is to be paid.

394. For lump sum payments, the auditor ensures that the fund's governing rules permit such payments and that an appropriate condition of release has been satisfied.

395. In relation to testing the compliance of both lump sum or pension-type benefits, the auditor considers whether:

(a) the circumstances of the individual in triggering the payment of the benefit are consistent with a condition of release;

(b) the member has satisfied the payment criteria;

(c) the benefit has been calculated correctly in accordance with the method provided in the governing rules; and

(d) in the case of a retirement phase pension, the capital amount used to commence the pension was no more than the member's transfer balance cap.

396. Ordinarily, the auditor tests the validity of the payment by checking to source documents that the benefit payment is bona fide, such as sighting a signed letter to the trustees requesting the benefit be paid and that retirement is evidenced by a member declaration, or similar document stating that the individual has retired and will not be seeking paid employment in the future. Further substantiation could include employment separation documentation such as an employer letter.

397. Total and permanent disability generally requires at least two appropriately qualified medical practitioners to certify that the individual is unlikely to work in paid employment or meets such similar definition as may be contained in the governing rules of the SMSF. The SMSF may or may not have insurance for total and permanent disability.

398. With respect to death benefits, the auditor checks the trust deed obligations, and whether a binding death benefit nomination form has been completed by the deceased and it complies with the requirements in the fund's trust deed. The auditor ascertains where the death benefits have been paid to confirm that they have gone to either a dependant(s) or to the legal personal representative (LPR) of the deceased member. The auditor enquires as to whether any additional insurance benefit is payable.

399. A binding death benefit nomination for a SMSF must be made in accordance with the provisions of the trust deed for it to bind the trustee in the making of the death benefit payment decision. In the event a SMSF has paid a death benefit in the year being audited, procedures may include checking the form of any binding nomination on file against the terms of the trust deed and making enquiries to ensure that the benefit was paid appropriately according to the nomination's direction and the nominated beneficiaries are entitled to receive death benefits under the trust deed and the superannuation law.

400. If the SMSF has an insurance policy covering total and permanent disability, total and temporary disability or death or a combination of these benefits, ordinarily the auditor enquires to see if a claim has been made or paid to support the benefit. If the proceeds of any such claim have been paid, ordinarily, the auditor checks to see that the benefit has been applied either to the member's account or paid to the legal personal representative or beneficiaries.

401. Retirement phase income streams are pensions paid to a member following their satisfaction of a trigger event with a nil cashing restriction. The level of capital that can be applied to a retirement phase pension is restricted by the individual's transfer balance cap (TBC). The commencement of a retirement phase pension as well as a commutation (partial or full) is required to be reported against the individual's transfer balance account (TBA) within specific

time periods. The review of the fund includes checking the reporting has been undertaken appropriately.

Assignment of Members' Interests and Charges over Members' Benefits

402. The trustees are not permitted to recognise, or in any way encourage or sanction, an assignment of a superannuation interest, of a member or beneficiary,[190] or a charge over, or in relation to, a member's benefits.[191] Audit evidence is obtained by receiving a signed trustee representation letter confirming these requirements have been met throughout the period.

Contribution Restrictions

403. A contribution is defined as anything of value that increases the capital of a superannuation fund provided by a person whose purpose is to benefit one or more particular members of the fund or all of the members in general.[192] Ordinarily, the auditor examines all contributions made to the SMSF to assess whether they have been made in accordance with the fund's governing rules, SISA and SISR and, that in accepting the contribution, the SMSF is not contravening the SISA and SISR. In making this assessment, the auditor identifies the type of contribution made, the age of the member and the source of the contribution.

404. The auditor tests that the SMSF has accepted contributions in accordance with the SISR,[193] which are either:

(a) mandated employer contributions received irrespective of the member's age, such as SG contributions, superannuation guarantee shortfall, award related and certain payments from superannuation holding accounts;

(b) member contributions or employer contributions (except mandated contributions) when:

(i) the member is under 65 years old;

(ii) the member is not under 65 years but is under 70 years and has been gainfully employed at least on a part-time basis (work test) during the financial year in which the contribution is made;[194]

(iii) the member is over 65 but is under age 75 and has a total superannuation balance of less than $300,000 (at the start of the year) and has satisfied the work test in the preceding 12-month period when the contribution is made. This work test exemption can be used in conjunction with the unused concessional contribution cap opportunity contribution category however, is a one-off opportunity (can only be used once) or;

(iv) the member is not under 70 years but is under 75 years and has been gainfully employed at least on a part-time basis during the financial year in which the contribution is made and the contribution is received no later than 28 days after the month end when the member turned 75 years and, in the case of a member contribution, it is made by the member.

(c) other contributions for a member who is under 65 years of age; or

190 See regulation 13.12 of the SISR.
191 See regulation 13.13 of the SISR.
192 See TR 2010/1 Income tax: Superannuation contributions.
193 See regulation 7.04 of the SISR.
194 The basic work test for accepting contributions is to work for remuneration for at least 40 hours in a continual 30 day period within the year the contribution was made.

(d) contributions received at a later date in respect of a period in which the member met the age restrictions.

405. The auditor also tests that contributions are:

(a) within contribution caps specified in the SISR and the ITAA[195], being:

(i) if the member is 64 years or less on 1 July of the financial year – three times the amount of the non-concessional contributions cap; or

(ii) if the member is 65 years but less than 75 years on 1 July of the financial year – the non-concessional contributions cap; and

(b) for a member for whom a tax file number (TFN) has been supplied

406. The non-concessional contribution cap (NCC) is 4 times the concessional contribution cap or, Nil if the member's total Superannuation Balance (TSB) exceeds the general transfer balance cap (TBC) as at the start of the income year the contribution is made.

A member under 65 years of age may be entitled to bring-forward up to three years non concessional cap in a single year. The "bring-forward" rule is triggered in a year where a member makes a non-concessional contribution that is greater than the cap. The amount that is able to be contributed depends on the member's TSB at the start of the year as follows:

Total superannuation balance at start of year	**Maximum NCCs using bring-forward**
< $1.4m	3 x the single year
$1.4m - $1.5m	2 x the single year
$1.5m - $1.6m	1 x the single year
+ $1.6m	$0

If a member has a TSB below $1.4m at the start of the year and they trigger the bring-forward rule without maximising it, their TSB at the start of the following 2 years will determine their ability to complete the bring-forward.

407. In verifying the appropriateness of contributions received the auditor considers factors including:

- The type and source of the contribution;
- The age of the member;
- Whether a tax file number has been provided;
- The amount contributed; and
- The timing of when the contribution was made.

408. Ordinarily, the auditor checks to see that the classification of contributions are appropriate and allocated to the correct member account. (as per the contribution review)

[195] ITAA 1997 section 292-85(2)

Returning/refunding contributions

409. There are very limited circumstances where a SMSF trustee can return a contribution to a member or employer as follows:

(a) A contribution received by a member who does not satisfy the age restrictions.

(b) A member contributions received for whom the fund does not have a TFN must be returned to the contributor within 30 days of the amount being received[196]: However, the fund does not have to return such contributions if the member's TFN is quoted for superannuation purposes within 30 days of the amount being received by the trustee of the fund.

410. Contributions returned in accordance with the "law of restitution"[197]. The limited examples of the operation of the law of restitution include:

(i) an amount is paid to a superannuation fund by mistake – it was intended for a different purpose;

(ii) an amount is paid to a superfund that is greater than intended, for example, because of a clerical, transcription or arithmetic error.

A SMSF cannot return a contribution if it is in excess of the member's contribution limit. The excess contribution process is initiated by an "ATO Determination" which may provide the opportunity for the fund to return some or all of an excess contribution[198]

Audit procedures may include checking cash movements and validating receipts and payments along with substantiation of contributions received from employment arrangements. .

411. With respect to the Government co-contribution, the auditor ordinarily checks that the co-contribution has been allocated to the correct member.

In-specie Contributions

412. In-specie contributions are contributions to a SMSF where a physical asset (e.g. a commercial property) or an intangible asset (e.g. a share, or an option) are contributed to the SMSF on behalf of a member without any cash being exchanged.

413. Where contributions are accepted in-specie, the auditor assesses whether:

(a) the fund's governing rules permit in-specie contributions; and

(b) the SISA prohibitions on acquiring assets from related parties (including members) have been satisfied.

414. Once it is established that the in-specie contribution may be accepted, the auditor assesses whether the in-specie contribution is:

(a) within the contributions cap;

(b) valued at market value (p11); and

196 SISR 7.04(4)(a)

197 See ATOID 2010/104 which includes case citation.

198 The "fund-capped contributions" limit (former reg 7.04(3) of the SIS Regs) has been repealed for non-concessional contributions from 1 July 2017.

(c) not in breach of any other SISA prohibition.

Downsizer contribution

415. A downsizer contribution received from a member over the age of 65 must be accompanied by a *Downsizer contribution into super* form (ATO NAT 75073-12.2018). The form ensures the contribution is not counted to the member's contribution caps as well as enabling the member to make a contribution without satisfying the work test and permits members with greater than a TSB of $1.6m to contribute up to $300,000 to super.

416. Where a downsizer contributions are accepted, the auditor assesses whether:

(a) The fund's trust deed permits downsizer contributions, or do not expressly prohibit the acceptance;

(b) There is sufficient evidence to confirm the member's eligibility to make the contribution;

(c) The member has not utilised the downsizer contribution opportunity previously.

Key risk areas may include:

(a) The 10 year holding period. One member of the couple must have owned the property for at least 10 years;

(b) The property is at least partially exempt from CGT under the main residence exemption; and

(c) The sale contract is dated after 1 July 2018.

Use of Reserves

417. Where reserves are present in an SMSF, an auditor ordinarily checks to ensure the use of the reserves by the trustees is appropriate and within the requirements of the SISA and SISR. In particular, the allocation from an investment reserve to members' accounts should take into consideration the return on the investments, any costs attributable to the members' accounts and the level of the reserves held by the fund.[200] For contributions held in any reserves, the auditor checks to ensure the amounts have been allocated to members' accounts within 28 days after the end of the month in which the contributions were received.

Investment Returns

418. An auditor ordinarily checks to ensure that fund income is accurately credited or debited to relevant members' benefits in a way that is fair and reasonable.[201] The allocation should take into consideration all the members of the fund and the specific member accounts of each member of the fund.

Solvency

419. If the auditor, in the course of, or in connection with, performance of the audit of a SMSF, forms the opinion that the financial position of the SMSF may be, or may be about to become, unsatisfactory, the auditor is required to report to the ATO and to the trustees in writing under section 130 of the SISA. The auditor completes Section G: Other Regulatory Information of the Audit Contravention Report (ACR).

200 See sub-regulation 5.03(1) of the SISR.
201 See sub-regulation 5.03(2) of the SISR.

420. Under the SISR,[202] the financial position of a SMSF is treated as unsatisfactory if, in the auditor's opinion for an accumulation fund, either the aggregate members' benefits accounts exceed the value of the assets or the accrued members' benefits exceed the value of the assets.

Other Regulatory Information – Section G - ACR

421. In the course of conducting the audit, the auditor may obtain information regarding the SMSF, a trustee or another auditor which the auditor considers may assist the ATO in performing its functions under the SISA or SISR. This information may relate to compliance with requirements of the SISA or SISR which are not specified in the approved form auditor's report or the ACR. Under section 130A of the SISA, the auditor may report any such information to the ATO in the ACR.

422. The auditor considers whether any regulatory information reported in the ACR under section 130A needs to be included in the auditor's report on compliance, as the approved form auditor's report allows for reporting on additional sections of the SISA and SISR, and whether the information affects the compliance assurance opinion.

423. From 1 July 2019, a disclaimer making it clear that when an auditor provides information about a fund or trustee at Section G of the ACR, they are consenting to the disclosure of their identity to the SMSF trustee. If an auditor does not wish their identity to be disclosed, they would instead make a voluntary disclosure via the ATO website.

Other Compliance Engagement Considerations

Service Organisations

424. If a service organisation is used by the SMSF, the auditor cannot merely rely on the type 2 report as evidence of the SMSF's compliance with the SISA and SISR (refer paragraph 25). The auditor performs additional procedures necessary to conclude on the SMSF's compliance with the SISA and SISR, for example, reviewing cash transaction accounts to conclude on compliance with the borrowing requirements of SIS. To address the other compliance requirements, the auditor requests the service organisation to confirm that the compliance obligations have been met, for example:

(a) Confirmation that the assets are held by the fund trustee, in trust for the fund;

(b) Confirmation that none of the investments were acquired from a related party, or if acquired from a related party, that the acquisition was completed at market value and is a permitted acquisition; or

(c) Confirmation that, to the knowledge of the service provider, none of the investments held is pledged as security.

425. It may be impossible or impractical to obtain sufficient appropriate audit evidence of compliance with respect to the services provided, in which case either the auditor qualifies their opinion on the basis of a limitation of scope or issues a disclaimer of opinion.

Subsequent Events

426. The auditor considers the effect of subsequent events on the auditor's compliance report occurring up to the date the report is signed. If a material compliance breach has occurred after year end and the breach indicates a systemic issue with potential to impact the reporting period, it may result in modifications to the compliance report.

[202] See regulation 9.04 of the SISR.

Reporting Compliance Breaches

427. In determining whether to report potential or actual contraventions (breaches) identified during the compliance engagement, the auditor applies different criteria in relation to their reporting obligations to:

(a) a trustee in the management letter;

(b) a trustee under SISA sections 129 or 130;[203]

(c) the ATO, in an ACR, under SISA sections 129 or 130; and

(d) the trustees in the auditor's compliance report.

428. The auditor reports to a trustee in writing under SISA section 129 any reportable contraventions of the SISA or SISR, which it is likely may have occurred, may be occurring or may occur, regardless of the materiality of those contraventions. The auditor also reports to a trustee under section 130 if the financial position of the SMSF may be, or may be about to become, unsatisfactory.

429. The auditor reports events which may lead, or have led, to one or more contraventions of the SISA or SISR to the ATO in an ACR where they are contraventions of sections or regulations specified in the ACR and, either:

(a) those contraventions meet the reporting criteria, which comprise seven tests specified in the ACR instructions;[204] or

(b) those contraventions do not meet the specified tests, but the auditor wishes to report them as a result of the exercise of professional judgement.

- In addition, the auditor reports to the ATO in an ACR under section 130 if the financial position of the SMSF may be or may be about to become unsatisfactory.[205]

430. ASAE 3100 requires the auditor's report on compliance to be modified if, in the auditor's judgement, material non-compliance with a requirement may exist. Consequently, the auditor determines whether any potential or actual contraventions of the SISA or SISR identified during the audit are:

(a) contraventions of sections of the SISA or SISR specified in the approved form auditor's report; and

(b) material to the SMSF.

431. In determining whether a contravention identified is material to the SMSF, and therefore whether a modification to the auditor's report is warranted, the auditor uses professional judgement.

432. Even if a contravention is reported in an ACR, it does not necessarily result in a modification to the auditor's compliance report. The auditor, nevertheless, considers the contraventions which meet the reporting criteria specified in the ACR instructions, and uses professional judgement in determining the impact, if any, on the auditor's compliance report.

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203 Where an auditor forms an opinion that it is likely that a contravention may have occurred, may be occurring or may occur, the reporting criteria and the list of reportable sections and regulations that an auditor applies to determine whether a report to the ATO is required, are listed in the ACR instructions (NAT 11299) www.ato.gov.au/Forms.

204 The ACR instructions (NAT 11299) and ACR (NAT 11239) are approved forms and can be obtained through the ATO's website at www.ato.gov.au/Forms. Additionally, eSAT software is available free of charge from the tax office to assist in completing the compliance assurance engagement and reporting any ACRs appropriately to the ATO. See www.ato.gov.au/eSAT for further details.

205 See "Solvency" at paras 363-364.

433. The circumstances which may result in a modification to the auditor's compliance report are where:

   (a) a limitation of scope of the auditor's work exists, due either to circumstances or a trustee imposing a restriction, which prevents the auditor from obtaining the evidence required, in which case the auditor expresses a qualified opinion or a disclaimer of opinion; or

   (b) the SMSF did not comply in all material respects with the requirements included in the approved form, in which case the auditor expresses a qualified or adverse opinion.

434. A qualified opinion is expressed as being "except for" the matter to which the qualification relates when that matter is not as material or pervasive as to require an adverse or disclaimer of opinion.

Appendix 1

(Ref: Para. 56)

EXAMPLE OF AN ENGAGEMENT LETTER FOR THE AUDIT OF A SELF-MANAGED SUPERANNUATION FUND

The following example audit engagement letter is for use as a guide only, in conjunction with the considerations described in GS 009, and may need to be modified according to the individual requirements and circumstances of each engagement.

To [the Trustees/Directors of the Corporate Trustee] of [name of SMSF]

[The Objective and Scope of the Audit]

You have requested that we audit the [name of SMSF]'s (the Fund):

1. financial report, which comprises the [statement of financial position/statement of net assets] as at [date] and the [operating statement/statement of changes in net assets] for the [period] then ended and the notes to the financial statements; and

2. compliance during the same period with the requirements of the Superannuation Industry (Supervision) Act 1993 (SISA) and SIS Regulations (SISR) specified in the approved form auditor's report as issued by the Australian Tax Office, which are sections 17A, 35AE, 35B, 35C(2), 62, 65, 66, 67, 67A, 67B, 82-85, 103, 104, 104A, 105, 109 and 126K of the SISA and regulations 1.06(9A), 4.09, 4.09A, 5.03, 5.08, 6.17, 7.04, 8.02B, 13.12, 13.13, 13.14 and 13.18AA of the SISR.[206]

We are pleased to confirm our acceptance and our understanding of this engagement by means of this letter. Our audit will be conducted pursuant to the SISA with the objective of our expressing an opinion on the financial report and the Fund's compliance with the specified requirements of the SISA and SISR.

[The Responsibilities of the Auditor]

We will conduct our financial audit in accordance with Australian Auditing Standards and our compliance engagement in accordance with applicable Standards on Assurance Engagements, issued by the Auditing and Assurance Standards Board (AUASB). These standards require that we comply with relevant ethical requirements relating to audit and assurance engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement and that you have complied, in all material respects, with the specified requirements of the SISA and SISR.

The annual audit of the financial reports and records of the Fund must be carried out during and after the end of each year of income. In accordance with section 35C of the SISA, we are required to provide to the trustees of the Fund an auditor's report in the approved form within the prescribed time as set out in the SISR, 28 days after the trustees have provided all documents relevant to the preparation of the auditor's report.

Financial Audit

A financial audit involves performing audit procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement,

[206] These sections and regulations need to be amended if there are any changes to the sections and regulations in the ATO approved form auditor's report.

including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. A financial audit also includes evaluating the appropriateness of the financial reporting framework, accounting policies used and the reasonableness of accounting estimates made by the trustees, as well as evaluating the overall presentation of the financial report. Due to the test nature and other inherent limitations of an audit, together with the inherent limitations of any accounting and internal control system, there is an unavoidable risk that even some material misstatements may remain undiscovered.

In making our risk assessments, we consider internal controls relevant to the Fund's preparation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal controls. However, we expect to provide you with a separate letter concerning any significant deficiencies in the Fund's system of accounting and internal controls that come to our attention during the audit of the financial report. This will be in the form of a letter to the Trustees.
Compliance Engagement

A compliance engagement involves performing audit procedures to obtain audit evidence about the Fund's compliance with the provisions of the SISA and SISR specified in the ATO's approved form auditor's report.

Our compliance engagement with respect to investments includes determining whether the investments are made for the sole purpose of funding members' retirement, death or disability benefits and whether you have an investment strategy for the Fund, which has been reviewed regularly and gives due consideration to risk, return, liquidity, diversification and the insurance needs of members' . Our procedures will include testing whether the investments are made for the allowable purposes and in accordance with the investment strategy and legislative provisions. Our engagement does not include providing an opinion on the appropriateness of investments for fund members.

[The Responsibilities of the Trustees]

We take this opportunity to remind you that it is the responsibility of the trustees to ensure that the Fund, at all times, complies with the SISA and SISR as well as any other legislation relevant to the Fund. The trustees are also responsible for the preparation and fair presentation of the financial report.

Our auditor's report will explain that the trustees are responsible for the preparation and the fair presentation of the financial report and for determining that the accounting policies used are consistent with the financial reporting requirements of the SMSF's governing rules, comply with the requirements of SISA and SISR and are appropriate to meet the needs of the members.[207] This responsibility includes:

- Establishing and maintaining controls relevant to the preparation of a financial report that is free from misstatement, whether due to fraud or error. The system of accounting and internal control should be adequate in ensuring that all transactions are recorded and that the recorded transactions are valid, accurate, authorised, properly classified and promptly recorded, so as to facilitate the preparation of reliable financial information. This responsibility to maintain adequate internal controls also extends to the Fund's compliance with SIS including any Circulars and Guidelines issued by a relevant regulator to the extent applicable. The internal controls should be sufficient to prevent and/or detect material non-compliance with such legislative requirements;
- Selecting and applying appropriate accounting policies;
- Making accounting estimates that are reasonable in the circumstances; and

[207] If the SMSF is a reporting entity this sentence requires amendment to read: "Our auditor's report will explain that the trustees are responsible for the preparation and the fair presentation of the financial report in accordance with Australian Accounting Standards."

- Making available to us all the books of the Fund, including any registers and general documents, minutes and other relevant papers of all Trustee meetings and giving us any information, explanations and assistance we require for the purposes of our audit. Section 35C(2) of SIS requires that Trustees must give to the auditor any document, relevant to the conduct of the audit, that the auditor requests in writing within 14 days of the request.

As part of our audit process, we will request from the trustees written confirmation concerning representations made to us in connection with the audit.

Our audit report is prepared for the members of the Fund and we disclaim any assumption of responsibility for any reliance on our report, or on the financial report to which it relates, to any person other than the members of the Fund, or for any purpose other than that for which it was prepared.

[Independence]

We confirm that, to the best of our knowledge and belief, the engagement team meets the current independence requirements of the SISA and SISR including APES 110 Code of Ethics for Professional Accountants in relation to the audit of the Fund. In conducting our financial audit and compliance engagement, should we become aware that we have contravened the independence requirements, we shall notify you on a timely basis.

[Report on Matters Identified]

Under section 129 of the SISA, we are required to report to you in writing, if during the course of, or in connection with, our audit, we become aware of any contravention of the SISA or SISR which we believe has occurred, is occurring or may occur. Furthermore, you should be aware that we are also required to notify the Australian Taxation Office (ATO) of certain contraventions of the SISA and SISR that we become aware of during the audit, which meet the tests stipulated by the ATO, irrespective of the materiality of the contravention or action taken by the trustees to rectify the matter. Finally, under section 130, we are required to report to you and the ATO if we believe the financial position of the Fund may be, or may be about to become unsatisfactory.

You should not assume that any matters reported to you, or that a report that there are no matters to be communicated, indicates that there are no additional matters, or matters that you should be aware of in meeting your responsibilities. The completed audit report may be provided to you as a signed hard copy or a signed electronic version.[208]

[Compliance Program]

The conduct of our engagement in accordance with Australian Auditing Standards and applicable Standards on Assurance Engagements means that information acquired by us in the course of our engagement is subject to strict confidentiality requirements. Information will not be disclosed by us to other parties except as required or allowed for by law or professional standards, or with your express consent. Our audit files may, however, be subject to review as part of the compliance program of a professional accounting body or the ATO. We advise you that by signing this letter you acknowledge that, if requested, our audit files relating to this audit will be made available under these programs. Should this occur, we shall advise you. The same strict confidentiality requirements apply under these programs as apply to us as your auditor.

[Limitation of liability][209]

[208] The auditor should retain an original hard copy in the working papers.

[209] Applicable to participants in a limitation of liability scheme. Accounting Professional and Ethical Standard APES 305 *Terms of Engagement*, issued by the Accounting Professional & Ethical Standards Board (revised August 2019), which is applicable to members of the professional accounting bodies in Australia in public practice, requires participants in a limitation of liability scheme under Professional Services Legislation to advise the client that the member's liability may be limited under the scheme.

As a practitioner/firm participating in a scheme approved under Professional Services Legislation, our liability may be limited under the scheme.]

[Fees]
We look forward to full co-operation with [you/your administrator] and we trust that you will make available to us whatever records, documentation and other information are requested in connection with our audit.
[Insert additional information here regarding fee arrangements and billings, as appropriate.]

[Other]
This letter will be effective for future years unless we advise you of its amendment or replacement, or the engagement is terminated.
Please sign and return the attached copy of this letter to indicate that it is in accordance with your understanding of the arrangements for our financial audit and compliance engagement of the [name of SMSF].

[Insert here or attach any additional matters specific to the engagement, such as business terms and conditions, as appropriate.]

Yours faithfully,

....

Name and Title

Date

Acknowledged on behalf of the trustees of [name of SMSF] by (signed).

....

Name and Title

Date

Appendix 2

(Ref: Para. 118)

EXAMPLE OF A SELF-MANAGED SUPERANNUATION FUND TRUSTEE REPRESENTATION LETTER

This illustrative letter is provided as an example only and may need to be modified according to the individual requirements and circumstances of each engagement. Representations by the trustees will vary between SMSFs and from one period to the next. In the event that the trustees do not provide requested written representations the auditor should make reference to ASA 580 in determining the effect on the audit.

[SMSF letterhead]

Date

[Addressee - Auditor]

Dear [Sir/Madam],

Trustee Representation Letter
This representation letter is provided in connection with your audit of the financial report of the [SMSF Name] (the Fund) and the Fund's compliance with the Superannuation Industry (Supervision) Act 1993 (SISA) and SIS Regulations (SISR), for the [period] ended [date], for the purpose of you expressing an opinion as to whether the financial report is, in all material respects, presented fairly in accordance with the accounting policies adopted by the Fund and the Fund complied, in all material respects, with the relevant requirements of SISA and SISR.

The trustees have determined that the Fund is not a reporting entity for the [period] ended [date] and that the requirement to apply Australian Accounting Standards and other mandatory reporting requirements do not apply to the Fund.[210] Accordingly, the financial report prepared is a special purpose financial report which is for distribution to members of the Fund and to satisfy the requirements of the SISA and SISR. We acknowledge our responsibility for ensuring that the financial report is in accordance with the accounting policies as selected by ourselves and requirements of the SISA and SISR, and confirm that the financial report is free of material misstatements, including omissions.

We confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

[Include representations relevant to the Fund. Such representations may include the following examples.]

1. Sole purpose test

   The Fund is maintained for the sole purpose of providing benefits for each member on their retirement, death, termination of employment or ill-health.

2. Trustees are not disqualified

[210] If the SMSF is a reporting entity then it will be required to prepare a general purpose financial report in accordance with the Australian Accounting Standards and this paragraph will need to be adapted accordingly.

Disqualified person

A person (including a director of a corporate trustee) must not intentionally be, or act as, a trustee or a director of a corporate trustee of a super fund if they are and know that they are, a disqualified person [section 126K of the *Superannuation Industry (Supervision) Act 1993* (SISA)].

An individual is a disqualified person if they:

- have ever been convicted of an offence involving dishonest conduct in any country
- have ever been subject to a civil penalty order under the SISA
- are an undischarged bankrupt, or
- have been disqualified by the Regulator.

A body corporate is a disqualified person if:

- a responsible officer of the body corporate is a disqualified person
- a receiver, receiver and manager, administrator or provisional liquidator has been appointed to the body corporate, or
- action has commenced to wind up the body corporate.

Acting while disqualified

If a trustee of a self-managed super fund (SMSF) is, or becomes, a disqualified person, they must immediately tell the Commissioner in writing, and must resign as a trustee as soon as possible.

If a disqualified person acts as an individual trustee or a director of a corporate trustee of an SMSF, this will not result in a fund failing to meet the definition of an SMSF until 6 months after the person become disqualified, however will result in the disqualified person contravening section 126K of the SISA.

Penalties can be applied to those who act as trustees while disqualified, including imprisonment for two years.

3. Fund's governing rules, Trustees' responsibilities and Fund conduct

The Fund meets the definition of a self-managed superannuation Fund under SISA, including that no member is an employee of another member, unless they are relatives and no trustee [or director of the corporate trustee] receives any remuneration for any duties or services performed by the trustee [or director] in relation to the Fund.

The Fund has been conducted in accordance with its governing rules at all times during the year and there were no amendments to the governing rules during the year, except as notified to you.

The trustees have complied with all aspects of the trustee requirements of the SISA and SISR.

The trustees are not subject to any contract or obligation which would prevent or hinder the trustees in properly executing their functions and powers.

The Fund has been conducted in accordance with SISA, SISR and the governing rules of the Fund.

The Fund has complied with the requirements of the SISA and SISR specified in the approved form auditor's report as issued by the ATO, which are sections 17A, 35AE, 35B, 35C(2), 62, 65, 66, 67, 67A, 67B, 82-85, 103, 104, 104A, 105, 109 and 126K of the SISA and regulations 1.06(9A), 4.09, 4.09A, 5.03, 5.08, 6.17, 7.04, 8,02B, 13.12, 13.13, 13.14 and 13.18AA of the SISR.

All contributions accepted and benefits paid have been in accordance with the governing rules of the Fund and relevant provisions of the SISA and SISR.

There have been no communications from regulatory agencies concerning non-compliance with, or deficiencies in, financial reporting practices that could have a material effect on the financial report [or we have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial report and the Auditor's/actuary's contravention report].

4. Investment strategy

The investment strategy has been determined and reviewed with due regard to risk, return, liquidity diversity, and the assets of the Fund are in line with this strategy. The trustee has considered the insurance needs of Fund members in determining the investment strategy.

5. Asset form and valuation

Investments are carried in the books at market value. We consider the valuations within the financial statements are reasonable in light of present circumstances.

We have no plans or intentions that may materially affect the carrying values, or classification, of assets and liabilities.

There are no commitments, fixed or contingent, for the purchase or sale of long term investments other than those disclosed in the financial report.

6. Accounting policies

All the significant accounting policies of the Fund are adequately described in the financial report and the notes attached thereto. These policies are consistent with the policies adopted last year by the trustee in accordance with legislative requirements and the fund's trust deed.

7. Fund books and records

All transactions have been recorded in the accounting records and are reflected in the financial report. We have made available to you all financial records and related data, other information, explanations and assistance necessary for the conduct of the audit; and minutes of all meetings of the trustees.

We acknowledge our responsibility for the design and implementation of internal control to prevent and detect error and fraud. We have established and maintained an adequate internal control structure to facilitate the preparation of reliable financial reports, and adequate financial records have been maintained. There are no material transactions that have not been properly recorded in the accounting records underlying the financial report.

We have disclosed to you the results of our assessment of the risk that the financial report may be materially misstated as a result of fraud. We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the Fund and involves the trustees or others.

In instances where the Fund uses a custodian, we confirm we have not been advised of any fraud, non-compliance with laws and regulations or uncorrected misstatements that would affect the financial report of the fund.

Information retention obligations have been complied with, including:

- accounting records and financial reports are being kept for five years,
- minutes and records of trustees' [or directors of the corporate trustee] meetings [or for sole trustee: decisions] are being kept for 10 years;
- records of trustees' [or directors of the corporate trustee] changes and trustees' consents are being kept for at least 10 years;

- copies of all member or beneficiary reports are being kept for 10 years; and
- trustee declarations in the approved form have been signed and are being kept for each trustee appointed after 30 June 2007.

8. Safeguarding Assets

   We have considered the importance of safeguarding the assets of the fund, and we confirm we have the following procedures in place to achieve this:

   Authorised signatories on bank and investment accounts are regularly reviewed and considered appropriate; and

   Tangible assets are, where appropriate, adequately insured and appropriately stored.

9. Significant assumptions

   We believe that significant assumptions used by us in making accounting estimates are reasonable.

10. Uncorrected misstatements

    We believe the effects of those uncorrected financial report misstatements aggregated by the auditor during the audit are immaterial, both individually and in aggregate, to the financial report taken as a whole. A summary of such items is attached.

11. Ownership and pledging of assets

The Fund has satisfactory title to all assets appearing in the statement of [financial position/net assets]. All investments are registered in the name of the Fund, where possible, and are in the custody of the respective manager/trustee.

There are no liens or encumbrances on any assets or benefits and no assets, benefits or interests in the Fund have been pledged or assigned to secure liabilities of others.

All assets of the Fund are held separately from the assets of the members, employers and the trustees. All assets are acquired, maintained and disposed of on an arm's length basis and appropriate action is taken to protect the assets of the Fund.

12. Related parties

We have disclosed to you the identity of the Fund's related parties and all related party transactions and relationships. Related party transactions and related amounts receivable have been properly recorded or disclosed in the financial report. Acquisitions from, loans to, leasing of assets to and investments in related parties have not exceeded the in-house asset restrictions in the SISA at the time of the investment, acquisition or at year end.

The Fund has not made any loans or provided financial assistance to members of the Fund or their relatives.

13. Borrowings

The Fund has not borrowed money or maintained any borrowings during the period, with the exception of borrowings which were allowable under SISA.

14. Subsequent events

No events or transactions have occurred since the date of the financial report, or are pending, which would have a significant adverse effect on the Fund's financial position at that date, or which are of such significance in relation to the Fund as to require mention in the notes to the financial statements in order to ensure the financial statements are not misleading as to the financial position of the Fund or its operations.

15. Outstanding legal action

We confirm you have been advised of all significant legal matters, and that all known actual or possible litigation and claims have been adequately accounted for, and been appropriately disclosed in the financial report.

There have been no communications from the ATO concerning a contravention of the SISA or SISR which has occurred, is occurring, or is about to occur.

16. Going Concern

We confirm we have no knowledge of any events or conditions that would cast significant doubt on the fund's ability to continue as a going concern.

17. Additional matters

[Include any additional matters relevant to the particular circumstances of the audit, for example:

- the work of an expert has been used; or

- justification for a change in accounting policy.]

We understand that your examination was made in accordance with Australian Auditing Standards and applicable Standards on Assurance Engagements and was, therefore, designed primarily for the purpose of expressing an opinion on the financial report of the Fund taken as a whole, and on the compliance of the Fund with specified requirements of the SISA and SISR, and that your tests of the financial and compliance records and other auditing procedures were limited to those which you considered necessary for that purpose.

Yours faithfully

(signed)
………………………..

[Director/Trustee]

[Date]

………………………..

[Director/Trustee]

[Date]

Appendix 3

(Ref: Para. 65)

SELF-MANAGED SUPERANNUATION FUND GOVERNING RULES PRELIMINARY UNDERSTANDING CHECKLIST

In obtaining a preliminary understanding of the SMSF, as part of the planning process, the auditor examines the trust deed or other document that contains the fund's governing rules to obtain a sound understanding of the trustee structure, requirements of the deed and the powers vested in the trustees. The following suggested procedures are examples only and should be reviewed and adapted for the specific circumstances and audit risks associated with each SMSF audit engagement.

The auditor exercises professional judgement and due care in interpreting the provisions of the trust deed. If the auditor is unsure of the meaning or interpretation of a clause, provision or section of the deed, then the auditor may seek the advice of an experienced superannuation lawyer.

Ref	Questions to be addressed in examining the trust deed
A	**ESTABLISHMENT AND EXECUTION**
A.1	Is the date of establishment of the SMSF recorded?
A.2	Has the trust deed been: • Properly executed? • Signed by all the members who are individual trustees? • Witnessed? • Dated? • Stamped (if required)?
A.3	Do the rules incorporate the SISA, SISR and applicable taxation rules?
A.4	Does the deed outline the core and ancillary purposes of the SMSF?
A.5	Does the deed require an irrevocable election to be made to be a regulated superannuation fund or a fund subject to the SISA and SISR?
A.6	Does the deed have a clause which deems the appropriate legislation into or out of the deed to allow the SMSF to remain complying?
B	**AMENDMENTS TO THE DEED**
B.1	Does the deed allow amendments?
B.2	Has the trust deed been amended since the last audit? If so: • Has the deed amendment been properly executed? • Is confirmation of the deed's compliance with SISA and SISR required from the solicitor or other party involved in the amendment? • Is the amendment signed off by the current trustees? • Could the amendments impact the audit?
C	**TRUSTEE AND MEMBERSHIP**
C.1	Does the trust deed specify who may be a trustee? Either: • Two or more individual trustees; or • A trustee company.
C.2	Does the deed specifically identify the trustee as either individuals or a corporate entity?
C.3	Are all individual trustees or directors of the trustee company required to be members?

Ref	Questions to be addressed in examining the trust deed
C.4	Does the deed permit members to be • A non-working spouse? • A retired person? • A child?
C.5	Does the deed limit the maximum number of members to 4 members?
C.6	Is membership open to anyone else?
C.7	Do the members of the SMSF meet the definitions? • No member of the SMSF is an employee of another member, unless related. • No trustee receives remuneration for their services to the SMSF in their capacity as trustee.
C.8	Does the trust deed contain the trustee covenants in s.52B of the SISA?
D	**AUDIT AND FINANCIAL REPORTS**
D.1	Does the trust deed require the appointment of an approved SMSF auditor?
D.2	Does the trust deed require the trustees to prepare a financial report annually and for it to be audited?
D.3	If a new fund or, deed has been amended, from 1 July 2020, does the deed specify the financial statements are to be prepared in accordance with the AAS? If so, the fund is required to prepare General purpose financial statements.
D.4	Does the trust deed require the trustees to keep the minutes and records of trustee decisions for at least 10 years and accounting records and signed financial reports for at least 5 years?
E	**CONTRIBUTIONS**
E.1	Does the deed allow: • Concessional contributions, including: - Employer contributions, including contributions made pursuant to a salary sacrifice agreement? - Member contributions for which a tax deduction is claimed? • Non-concessional contributions, including: - Member contributions for which no tax deduction is claimed? - Eligible spouse contributions? • Downsizer contribution • Contributions in respect of minors? • Rollovers and transfers in? • Government co-contributions? • Contribution splitting to a spouse? • Contributions by members who are under 65 and not working? • Contributions by members who are working part-time and are over 65 and under 75? • Mandated contributions to be accepted at any age? • Contribution splitting arrangements pursuant to family law matters? • Unused concessional cap carry forward – "catch-up contributions"
E.2	Does the deed allow for *in-specie* contributions of assets to be made by members or related parties?
E.3	Does the deed permit spouse accounts and may employers make contributions to spouse accounts?
E.4	May excess contributions tax levied on the member be paid by the SMSF, irrespective of preservations rules and conditions of release?
F	**BENEFIT PAYMENTS**
F.1	Does the SMSF require compulsory cashing of the members balance at a specific age? Where a trust deed specifies a compulsory cashing event, provided it does not extend the law, it provides authority for the payment. For example, if the deed states that members must commence drawing their accrued benefits from age 65, all members who are at least 65 years of age should be in receipt of a benefit.
F.2	Does the SMSF require a lump sum benefit to be paid in lieu of a pension?
F.3	Does the deed provide for members to make death benefit nominations - Does the deed provide authority between death benefit nominations and reversionary pensions?

Ref	Questions to be addressed in examining the trust deed
F.4	Does the deed include specific provisions relating to the payment of death benefits?
G	**PENSIONS**
G.1	Does the deed expressly allow for payment of pensions by the SMSF, including*: • Account based pensions • TRIS, including the auto conversion to a retirement phase TRIS following a nil cashing restriction trigger event. • Reversionary beneficiaries to be nominated. • Allocated pensions. • Term allocated or market linked or growth pensions. • Non-complying lifetime or fixed term pensions. * This list includes a number of pensions which may no longer be permitted but if already established may continue being paid.
G.2	Does the deed allow for commutation of a pension?
G.3	Does the deed allow for the segregation of assets to meet pension requirements?
G.4	Does the deed make reference to nominated beneficiaries?
H	**RESERVES (If applicable)**
H.1	Does the deed provide rules in relation to the establishment, maintenance and operation of SMSF Reserves?
H.2	Does the deed require different or parallel investment strategies for each reserve account?
I.	**INVESTMENTS**
I.1	Does the deed provide powers to the trustees to invest the assets of the SMSF?
I.2	Does the deed specify specific assets/asset classes in which the SMSF may invest?
I.3	Does the deed prevent investments in, or loans to, related parties?
I.4	Does the deed require an investment strategy to be formulated, regularly reviewed, and given effect?
I.5	Does the deed require the investment strategy to consider if insurance is relevant to the members of the fund?
J	**BORROWINGS**
J.1	Does the deed prohibit borrowings?
J.2	Does the deed permit borrowing in specific circumstances, including: • Temporary borrowings which are required for the payment of member benefits, short term settlement of securities or superannuation contributions surcharges (no longer levied)? • Borrowings for limited recourse borrowing arrangements?
K	**WINDING-UP**
K.1	Does the deed provide for the winding-up of the SMSF?

Appendix 4

(Ref: Para. 70)

ILLUSTRATIVE FINANCIAL AUDIT PROCEDURES FOR A SELF-MANAGED SUPERANNUATION FUND

The following suggested procedures are for illustrative purposes only and should be reviewed and adapted for the specific circumstances and audit risks associated with each SMSF audit engagement. The auditor exercises professional judgement to ensure that the procedures adopted are appropriate to the audit engagement. No allowance has been made for materiality or the extent of testing and changes may be necessary when reliance is placed on internal controls. This appendix is not intended to serve as an audit program or checklist in the conduct of a SMSF's financial audit and not all of the procedures suggested will apply to every SMSF's financial audit.

The procedures detailed are designed to address the financial audit of a SMSF, however, in some instances, where compliance matters are integral to the financial audit, these may also be included. For procedures in conducting a compliance engagement, a compliance checklist may be used. Standardised checklists are available from a number of professional organisations. Auditors verify the completeness of any compliance checklist they use to ensure it covers all relevant provisions[211]*.*

Ref	Audit Procedure
A	**ENGAGEMENT ACCEPTANCE**
A.1	Confirm that the appropriate procedures relating to new and ongoing engagements have been completed prior to commencing the audit, including: • Clearance from previous auditor on new engagements. • The firm has the appropriate resources and expertise to complete the engagement in the required time. • Confirmation of independence of the engagement partner and each audit team member.
A.2	Confirm that an engagement letter, that is appropriately scoped to cover this audit, has been issued and will be signed by the trustee prior to the completion of the audit.
A.3	A client acceptance or retention assessment has been undertaken.
B	**AUDIT PLANNING**
B.1	Obtain a copy of the following documents before commencing the audit: • A signed copy of the Fund's governing rules. • Signed audited financial reports for the prior year, including the signed prior year's auditor's report. • Minutes/resolutions of trustee meetings. • Copy of the fund's investment strategy.
B.2	Prepare an audit strategy and audit plan for this engagement addressing, as a minimum, the following matters: • Client profile, audit and reporting arrangements. • Audit approach - Nature: o Controls testing, including use of an auditor's report available for key service organisations. o Substantive testing – inspection, observation, enquiry, confirmation, recalculation, re-performance and analytical review. - Timing. - Extent – fully substantive, sampling, analytical review or representations. - Resources, including extent of direction and supervision. Consider interviewing the trustees and/or their advisors, prior to and during the development of the audit plan.

[211] Auditor guidance and information is available on the ATO website at https://www.ato.gov.au/Super/Self-managed-super-funds/SMSF-auditors including the ATO's electronic superannuation audit tool (eSAT), for use in conducting the compliance engagement.

Ref	Audit Procedure
B.3	Complete a risk assessment and determine preliminary materiality levels, covering: • Risk assessment - Current period events. - Fraud risks. - Control environment. - Computer/IT environment. • Materiality
B.4	Regulatory matters • Before commencing the audit, confirm that the SMSF is an ATO regulated self-managed superannuation fund on Super Look Up (www.superlookup.gov.au). Place copy in audit file.
C	**FINANCIAL REPORT AND DISCLOSURE**
C.1	Clerical accuracy and note references Check that: • The financial report includes an operating statement and statement of financial position or their equivalent and notes to the financial statements. • The table of contents or index agrees to the financial report, including the page numbers and content. • The footnotes refer to the notes to the financial statements and do not mention compilation reports or "unaudited" information. • The audit report is situated appropriately in the financial report so as not to suggest that members' statements or other information have been audited. • Prior period comparatives agree to those from the prior year signed financial report. • Additions in the financial report are correct. • The notes to the financial statements cross-reference correctly to and from the operating statement and statement of financial position.
C.2	Opening Balances - new engagements • Review the most recent audited financial report, and the predecessor auditor's report for any information relevant to opening balances. • Determine whether the opening balances reflect the application of the described accounting policies. • In order to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that may materially affect the current period's financial report: - Consider reviewing the previous auditor's audit work papers to obtain evidence regarding opening balances. - Evaluate whether audit procedures in the current period provide evidence in relation to opening balances. - Consider performing specific audit procedures to obtain evidence regarding opening balances. • Consider the impact of the prior period's modification (if applicable) to the opinion on the current period's financial report. • Consider the sufficiency and appropriateness of audit evidence obtained on opening balances in relation to the current period's financial report. If the auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances, the auditor considers the impact on the current period's auditor's report.
C.3	Accounting policies • If the SMSF is not a reporting entity, check that the accounting policy notes reflect this, obtain an understanding of the relevant accounting policies the trustee has used to prepare the financial report and check that the accounting policy notes adequately explain the policies adopted. • Determine whether the accounting policies in relation to assets, contributions, member entitlements and reserves meet the requirements of the SISA and SISR. • Determine if there are any changes in the accounting policies applied in prior periods, and if so, check that these have been appropriately disclosed in the accounting policy notes. • New funds, and funds where the trust deed has been amended, from 1 July 2020 must be reviewed to ensure the financial statements are not required to be prepared in accordance with AAS. If there is a specific provision requiring this, general purpose financial statements are required. NOTE: the deed must specify "in accordance with AAS" for GPFS to apply to the fund. "In accordance with accounting standards", does not prescribe the requirement for GPFS to be prepared.
D	**UNDERLYING ACCOUNTING RECORDS**

Ref	Audit Procedure
D.1	Obtain a copy of the SMSF's general ledger and agree the general ledger to the financial report and note any discrepancies.
D.2	Review the general ledger and identify material journal entries and other adjustments and review these to ensure that they are reasonable and consistent with the financial report.
E	**CASH**
E.1	Confirm the fund's bank accounts are in the name of the trustee on behalf of the fund by reviewing bank statements for each bank account.
E.2	Review statements for the year, examining accounts for large or unusual transactions and seek explanation for those transactions.
E.3	Test large and unusual payments and receipts to ensure these are *bona fide* and correctly recorded and authorised.
E.4	Review bank reconciliation at year end: • Follow up and investigate large, unusual or recurring reconciling items. • Follow up uncleared deposits and unpresented cheques ensuring correct cut off. • Trace unpresented cheques to bank statement subsequent to year end.
E.5	Where bank accounts are significant to the audit you should gain sufficient appropriate audit evidence, that may include: • Confirming the bank balance by way of a bank confirmation. • Obtain a third party authority in order to liaise with the financial institution. Investigate whether online access is available via the third party authority. Internet banking includes a third party access permission whereby an individual login in is issued to the nominated user. • Sighting original bank statements and subsequent redemptions for term deposits. • Seeking explanations for any material differences. • Checking for any debit balances, undisclosed liabilities and security for borrowings. • Review substantial entries and trace back to source (contributions, asset transactions, benefit payments).
E.6	Where the fund had undeposited cheques recorded as "cash on hand" at period end, confirm these amounts were banked after period end. Obtain documentary evidence (such as trustee minutes and subsequent bank statements to evidence the cash was received by the SMSF prior to and was deposited within a few days of period end. Alternatively evidence the source of the cash as a method of reconciling the transaction's validity.
F	**INVESTMENTS**
F.1	<u>General</u> An auditor should use professional judgement to determine what evidence is appropriate and the size of the sample to be verified for each investment.
F.2	<u>Foreign Currency Transactions</u> Check to ensure that all investments are recorded in Australian dollars and that if foreign currency transactions occur they are converted at the appropriate currency rates and accounted for correctly.
F.3	<u>Investor Directed Portfolio Services (WRAP accounts)</u> • Obtain the relevant auditor's report issued under ASIC Class Orders CO 13/763 or CO 13/762. • Confirm that the investments are held by the custodian (IDPS) and are identified as belonging to the SMSF - Conduct sample testing of the IDPS operator's asset transactions. Other tests could include obtaining correspondence between the SMSF trustee and the IDPS operator regarding the transactions such as a Statement of Advice. • Confirm that the method used to value the investments is consistent with that disclosed in the accounting policy notes and is in accordance with ATO guidelines and the SISR including the requirement for assets to be valued at market value (SISR regulation 8.02B). • Check that there is no double counting of assets such as the SMSF bank account or distributions receivable. • Where data has been transmitted via data feeds, obtain confirmation of the existence of a ASAE 3402 Type 2 Audit Report in respect of the process and controls.

Ref	Audit Procedure
F.4	<u>Fixed Interest Securities (including term deposits)</u> • Complete the following for each fixed interest security including debentures and bonds held by the SMSF at the end of the period: - Sight original certificates or obtain a bank confirmation to confirm correct ownership, date of issue of the certificates and date of maturity of the investment. - Agree the value of the fixed interest securities at period end. - For bonds, either confirm the net market value at period end with the originator of the security or with published market prices. - For unlisted non-transferable debentures, agree the net market value with the face value. • Confirm that the investments are in the name of the trustee and that the documentation clearly identifies that the investment is an asset of the Fund. • Confirm that the method used to value the investments is consistent with that disclosed in the accounting policy notes, and is in accordance with ATO guidelines and the SISR including the requirement for assets to be valued at market value (SISR regulation 8.02B).
F.5	<u>Property</u> • Complete property searches for all real estate investments owned by the SMSF. • Check that each property is owned by the trustee and is correctly and appropriately recorded as an investment of the SMSF. This may involve viewing the contract of sale when the property was first acquired, a declaration of trust or an acknowledgement of trust from the registered owner. • Check that there are no registered encumbrances unless they are in relation to limited recourse borrowing arrangements permitted by Sections 67A and 67B of the SISA. If there are limited recourse borrowing arrangements – refer to F10 of these Illustrative Procedures. • Review the accounting policies to determine how the trustee has valued each property. Fund assets including property investments are required by Regulation 8.02B of the SISR to be carried at market value determined in line with ATO *Valuation guidelines for self-managed superannuation funds*. • Review the method used to value the property, including if the trustees have relied on an independent market appraisal or valuation, obtain a copy of this and confirm that: - The value is correctly reflected in the financial report. - The valuation/appraisal refers to the correct property. - The valuation was based on reasonable assumptions and is current. - The valuation does not take into account redemption costs, other than any GST payable on sale which should be removed from the value. - If the property has been subsequently sold, that the sale price does not differ significantly from the valuation/appraisal. - That the method used to value the property is consistent with that disclosed in the accounting policy notes and is in line with ATO requirements and the SISR including the requirement for assets to be valued at market value (SISR regulation 8.02B). - Where the trustee has undertaken the valuation, assess whether the valuation process used is fair and reasonable, was undertaken in good faith, using objective and reliable data, is capable of explanation to a third party and complies with the ATO guidelines. • Where the property includes "buildings and other fixtures" verify existence of adequate insurance and, where these are being depreciated, ensure that the depreciation adjustments are correctly and appropriately reflected as part of the market value of the investment.
F.6	<u>Listed Securities</u> Review the number of listed securities including shares, units, options, warrants and futures held by the SMSF at the end of the period. If the SMSF has units in unit trusts, obtain a listing of these and identify any unit trusts that are listed on the Australian Stock Exchange, those that are widely held trusts and those that are closely held trusts. • Check that each listed security is owned by the trustee and is correctly and appropriately recorded as an investment of the SMSF and is held separate from the assets of the trustee, employers and other related parties as required by regulation 4.09(A)(2) of the SISR. • Agree the number of securities held at period end to the share registry or other appropriate sources. • Confirm the closing market price of the securities at the period end against an independent source. • Confirm that the method used to value the investments is consistent with that disclosed in the accounting policy notes and is in line with ATO guidelines and the SISR including the requirement for assets to be valued at market value (regulation 8.02B of the SISR). • If the SMSF invested or redeemed listed securities during the period, trace transactions to and/or from the SMSF to confirm that they have been dealt with in an appropriate and timely manner.

<table>
<tr><th>Ref</th><th>Audit Procedure</th></tr>
<tr><td>F.7</td><td><u>Widely Held Unlisted Unit Trusts and Managed Funds</u>
These are arm’s length, professionally managed trusts that provide regular reports on unit holdings, distributions and unit prices.
• Sight the original unit certificates, a confirmation from the unit trust or similar documentation and agree:
- The number of securities held at period end.
- That each investment is owned by the trustee and is correctly and appropriately recorded as an investment of the SMSF, and is held separate from the assets of the trustee, employers and other related parties as required by regulation 4.09(A)(2) of the SISR.
- The method used to determine the market value of the units at the period end is consistent with that disclosed in the accounting policy notes and is in line with ATO guidelines and the SISR including the requirement for assets to be valued at market value (regulation 8.02B of the SISR).
- Check if the units are valued cum or ex-distribution and that this is correctly and consistently calculated and reported.
• If the SMSF invested or redeemed units during the period, trace transactions to and/or from the SMSF to confirm that they have been dealt with in an appropriate and timely manner.</td></tr>
<tr><td>F.8</td><td><u>Unlisted Closely Held Unit Trusts</u>
These can be related trusts that may require additional audit procedures to confirm ownership, value and compliance with the SISR and SISA.
• Sight the original unit certificates, a confirmation from the unit trust or similar documentation and:
- Agree the number of units held at period end, and that
- each investment is owned by the trustee and is correctly and appropriately recorded as an investment of the SMSF and is held separate from the assets of the trustee, employers and other related parties
• Identify which of the valuation methods outlined in the ATO guidelines the trustee has used (market based, income based, asset based, cost based and probability based) to determine market value and test the value by:
- Obtaining documentary evidence to support the valuation.
- Making enquiries of the trustee or manager of the trust to determine the activities of the trust, the net tangible position of the trust, liquidity of the units, recent sales history, if any, pre-emptive rights or other restrictions that may apply to the units and any other factors that could impact the value of the investment.
- Verifying that the method used to value the investments is consistent with that disclosed in the accounting policy notes and is in line with ATO guidelines and the SISR including the requirement for assets to be valued at market value (regulation 8.02B of the SISR).
- Where the trustee has undertaken the valuation, assess whether the valuation process used is fair and reasonable, was undertaken in good faith using objective and reliable data, is capable of explanation to a third party and complies with the ATO guidelines.
If the SMSF invested or redeemed units during the period, trace transactions to and/or from the SMSF to confirm that they have been dealt with in an appropriate and timely manner.</td></tr>
<tr><td>F.9</td><td><u>Pooled Superannuation Trusts and Life Insurance Policies</u>
• Sight original statements issued by the product provider, or obtain a confirmation directly from the product provider at period end.
• Confirm that the investment is in the correct name.
• Confirm the number of units and value of the investment at period end.
• Confirm that the method used to value the investments is consistent with that disclosed in the accounting policy notes and is in accordance with ATO guidelines and the SISR including the requirement for assets to be valued at marked value (SISR regulation 8.02B).</td></tr>
</table>

Ref	Audit Procedure
F.10	<u>Assets subject to Limited Recourse Borrowing/ Arrangements</u> • If the asset is subject to a limited recourse borrowing arrangement, determine how the investment has been valued (refer above) and complete the following audit procedures: - Confirm the borrowing has either been used to acquire a single asset or, if the borrowing has been used to acquire a collection of assets, confirm each asset in the collection has an identical market value and that each asset in the collection is identical. - Confirm that the asset is held in trust for the SMSF - Confirm the deposit for the acquisition was paid from the SMSF cash balance. - Confirm the borrowing has only been used to maintain and repair the asset (not improve the asset) or applied to refinance the borrowing. - If the asset was replaced, confirm the following: o A share or collection of shares replaced for an identical share or collection of shares that has an identical market value; or o A unit or collection of units replaced for an identical unit or collection of units that has an identical market value; or o Is as a result of a corporate action - Confirm that the SMSF has an option to acquire the legal ownership of the asset on payment of the final instalment. - Confirm that the lender's rights are limited in recourse against the fund trustee, to that asset. - Review an original statement or confirmation letter from the lender and confirm the amount of the debt, amount owing at balance date, interest charged during year, amount of borrowing costs incurred in the period and the value of any prepaid expense at the end of the period and that these have been correctly reflected in the financial report. - For non-bank loan arrangements, review the loan agreement and check whether the terms are in accordance with the "safe-harbour" guide detailed in PCG 2016/5 and that the terms have been honoured. The safe-harbour terms provide a standard to demonstrate that the arrangement is "arm's length" and thereby not subject to the NALI level of tax. • Consider if any additional disclosures are required so that the users of the financial report understand the limited recourse borrowing arrangement. Review the clerical and factual accuracy of any additional disclosure to ensure it appropriately reflects the position of the arrangement.

Ref	Audit Procedure
F.11	Collectables and Personal Use Assets • If the asset is a type that does not have any form of title, obtain evidence to confirm existence and ownership including: - Minutes or resolution relating to the acquisition of the asset. - Invoice and evidence of payment from the SMSF for the purchase of the asset. - Sighting the asset. • For all collectibles and Personal Use Assets, obtain evidence of: - Insurance policy or premium payment for insurance of the asset. - Lease documents, if leased to another party. - Storage arrangements. - Review the Personal Property Securities Register (PPSR) to ensure the asset(s) isn't encumbered. Retain in audit file. • Identify which of the valuation methods outlined in the ATO guidelines the trustee has used (market based, income based, asset based, cost based and probability based) to determine market value and test the value by: - Obtaining documentary evidence to support the valuation. - Making enquiries of the trustee or manager of the trust to determine the activities of the trust, the net tangible position of the trust, liquidity of the units, recent sales history, if any, pre-emptive rights or other restrictions that may apply to the units and any other factors that could impact the value of the investment. - Verifying that the method used to value the investments is consistent with that disclosed in the accounting policy notes and is in line with ATO guidelines and the SISR including the requirement for assets to be valued at market value (regulation 8.02B of the SISR). - Assessing whether the valuation process used is fair and reasonable, was undertaken in good faith using objective and reliable data, is capable of explanation to a third party and complies with the ATO guidelines (where the trustee has undertaken the valuation).
G	**RECEIVABLES AND PREPAYMENTS**
G.1	If the SMSF uses accrual accounting, review each asset and determine if the SMSF was entitled to receive income for the year and if this had been received or accrued at balance date.
G.2	Obtain details of other receivables and ensure that they are correctly accounted for.
G.3	Verify that the receivable is current and has been received by the SMSF subsequent to period end or that it will be received by the SMSF.
G.4	If the amount is receivable from a related party, check that the disclosures are appropriate, and review this further as part of your compliance audit.
G.5	If the fund pays insurance or other expenses, ensure that these have been applied in the period to which they relate and prepaid items have been recorded in accordance with the accounting policies.
G.6	If the accounts are prepared on a cash basis, ensure a reconciliation is on file to validate the actual distributions received compared to those recorded on the annual tax statement.
H	**LIABILITIES**
H.1	Review the value at which liabilities have been disclosed in the financial report and vouch to supporting documentation. Review the documentation and assess whether the amount and nature of the liabilities appears reasonable.
H.2	Vouch payment of liabilities, accruals and benefits payable to payments subsequent to year end.
H.3	Review ageing of liabilities/payables and comment on any delay in payment.
H.4	Vouch prior year payables and accruals to payments during the year.
H.5	Test for unrecorded liabilities by reviewing client documentation and subsequent payments.
H.6	Review prior year accounts to identify expenses that have been paid for in previous years but not paid/accrued for this year.
H.7	If the fund has a limited recourse borrowing arrangement ensure that the liability is accurately and appropriately recorded in accordance with the arrangement (refer suggested procedures at F10 above).
I	**MEMBER'S ENTITLEMENTS / ACCRUED BENEFITS**

Ref	Audit Procedure
I.1	• Obtain listing of all members account balances and check that the total agrees with accrued benefits in the financial report. • Review the allocation of revenue, expenses, income tax, excess contributions tax and other items to members to ensure that they have been correctly apportioned. • Ensure that the disclosures in the financial report are appropriate and consistent with the members' entitlements.
J	**RESERVES – Review SMSFRB 2018/1 – ATO's view on SMSFs and reserves**
J.1	The range of reserves permissible by a SMSF is limited and the Regulator Bulletin highlights the boundaries. The particular focus is where reserves are utilised to circumvent the Super17 reforms that apply restrictions to the level of tax concessions available to super:- TSB manipulation in order to make NCCs; Reduce member balance to less than $500k in order to make "catch-up contributions"; and Use of reserves to reduce the member balance in respect of TBA reporting
J.2	Review the SMSF's documentation including the fund's governing rules and trustee minutes to ensure that the reserve is permitted and recorded in accordance with trustee policy.
J.3	Review the movements in the reserve during the period to ensure that they are clerically accurate and in accordance with the trustee's policy.
J.4	Ensure that the disclosures in the financial report are appropriate and consistent with the members' entitlements.
J.5	Any allocation from reserves is in accordance with the trust deed and subsection 292-25(3), Regulation 292-25.01 (concessional contributions). The allocation can have implications for the member if in excess of their concessional contribution cap.
K	**INVESTMENT AND OTHER REVENUE**
K.1	<u>Analytical Review</u> • Calculate the SMSF's investment return as a percentage based on the net income as a proportion of average assets held by the SMSF over the period. • Compare this to the prior year as well as average market performance for the period of the audit and confirm that the return is reasonable and not under or overstated.
K.2	<u>Interest Income</u> • Obtain a listing of interest income (if material) and ensure that this is consistent with the investments and what should have been received. • For bank interest conduct analytical review procedures.
K.3	<u>Changes in Market Value</u> • Conduct an analytical review. • Test the changes in market value calculations including realised changes in market value to ensure that they are correct. • Reconcile to investments, for substantive audits.
K.4	<u>Dividends</u> • Vouch dividends received to dividend slips, published dividend rates or registry details. Generally, two dividends are paid each year. Vouch these as an initial test. • Confirm the accounting treatment of franking credits (either on a net or gross basis) and ascertain accounting treatment is consistent with the details disclosed in the accounting policy notes.
K.5	<u>Trust Distributions</u> • Vouch distributions received and receivable to distribution advices, ensuring that the discounted capital gains and other income has been correctly classified for tax purposes. Some tax statements issued apply a 50% discount to capital gains – check the percentage applied is applicable to SMSFs.

Ref	Audit Procedure
K.6	<u>Rental Income</u> • Conduct an analytical review against rental agreement and period of tenancy. • Vouch rental income against agent's statements or other records, as appropriate. • Review the disclosure of rental expenses in relation to the disclosure and distribution of net investment revenue to ensure it meets the requirements of the governing rules, the needs of members and the requirements of the SISR. • Check any rent reviews in the lease agreements during the period have been correctly applied. • Audit files should include a copy of the lease agreement and be carried forward annually until the term of the lease expires.
K.7	<u>Other Income</u> • If the SMSF receives other forms of income ensure that these are correctly calculated, earned and disclosed.
K.8	<u>Non-arm's length income - NALI</u> • Review transactions and investment acquisitions for the potential for the imposition of NALI. NALI can also be invoked from *non-arm's length expenses – NALE.* A significant impact to the tax calculation can occur if NALI is present and not reported.
L	**CONTRIBUTIONS AND TRANSFERS IN**
L.1	<u>Concessional contributions</u> • Review the amounts, frequency and pattern of contributions and if you suspect contributions are being diverted to the fund seek confirmation of the contribution directly from the employer. All employers are required to report super contributions via the *single touch payroll (STP)* system. • Where the contributions are from a related employer, ensure you verify the contributions via the STP process. Small employers (less than 19) with 'closely held employees' are exempt from the use of STP until 1 July 2020 for the closely held payees only. If STP hasn't been enabled, manual verification is required.. • Test that contributions have been allocated to the member for whom they were remitted. • For concessional contributions made by the member, obtain a copy of the section 290-170 Notice of Intention to Deduct (or notice prepared in accordance with the requirements of s 290-170 ITAA 1997) and confirm the details are consistent with the accounting treatment. • Review the receipt of "catch-up contributions" to ensure the qualifying conditions were met for the fund to receive the contribution. The 2020 financial year is the first year of operation of carry forward unused concessional contribution cap. Unused contributions are no longer available after year 5 and no unused contribution is available if the member's total superannuation balance at the start of the income year is $500,000 or more. Audit files could include documentation verifying the members qualification to utilise the catch-up opportunity. • For members > 65, verify the substantiation that the work test has been met and the contribution was permitted. • Ensure only mandated contributions received for members aged +75. • Ensure no-TFN contributions were received.
L.2	• Where co-contributions have been received test that they have been allocated to the member for whom they were remitted.
L.3	• If transfers in have been received, obtain the roll-over documentation and ensure that the transferee is a complying superannuation fund and correctly recorded as taxed or untaxed. •
L.4	Verify and trace contributions to the bank statements with additional testing at year end for correct cut-off.
L.5	Review expenses and other items that may give rise to a contribution as outlined in ATO Rulings and ensure that these are correctly accounted for as contributions.
M	**EXPENSES**
M.1	Perform an analytical review of expenses and assess for reasonableness against your knowledge of the SMSF and in comparison to the prior year's expenditure.
M.2	Vouch material items to invoices, ensuring the expenses are attributable to the SMSF or are apportioned correctly.
M.3	Agree administration fees to the agreement with the administrator.

Ref	Audit Procedure
M.4	Agree management fees to the agreement with the investment manager.
N	**LUMP SUMS AND PENSIONS PAID**
N.1	• Obtain a listing of all benefits paid and reconcile benefits paid to the prior year members' statement, adjusted for current period transactions. • For each benefit paid, review documentation including minutes or other documents confirming the commencement of a pension, correspondence to the members and rollover institutions and ensure that the benefit was duly authorised. Audit workpapers to include evidence of the validity of benefit payments to members. • Confirm that each benefit was paid in accordance with the terms of the fund's governing rules. • For death benefits, confirm if the benefit was paid in accordance with the fund's governing rules and, if applicable, a binding death benefit nomination. • For a total and permanent disability benefit commenced in the year under audit, sight the medical certification regarding the inability of the member to work again. • For a total and temporary permanent disability benefit commenced in the year under audit, sight the medical certification regarding the temporary inability of the member to work. • Ensure that pensions paid are within the minimum and maximum (if a transition to retirement pension) thresholds and that pensions are paid at least once annually, and that a series of payments have been paid over the life of the pension account. • Investigate liabilities at year end to ensure that pensions have been paid, and not just accrued.
O	**TAX**
O.1	Review tax work papers to ensure that the income tax is correctly calculated and disclosed in accordance with the accounting policies, including: • Member contributions have been treated correctly as non-assessable unless the SMSF received a notice in accordance with section 290-170 of the ITAA 1997 stating that the member contribution is assessable. • Exempt Current Pension Income (ECPI) from assets used to pay current pensions is treated as non-assessable and an actuarial certificate has been obtained to confirm this if: the fund has both accumulation and unsegregated pension assets or, is a SMSF with "disregarded small fund assets" • ECPI has been correctly applied to income but not contributions. • If the SMSF derives ECPI, check that expenses have been apportioned between deductible and non-deductible expenses in accordance with Tax Ruling TR 93/17 and section 8-1 of the ITAA 1997. Cash bonuses (not rebates) received on life insurance policies are not included as taxable income. • Franking credits from dividends are correctly adjusted. • Trust distributions have been correctly apportioned to different classes of income and adjusted accordingly. • CGT calculations are correct, including, discounted gains, indexed gains and capital losses. Note that capital losses must be applied before any discount. • Request asset register for cost base reset investments - CGT Deferral in the 2017 financial year. Verify the CGT calculation of any sales and adjust the register • Foreign tax credits are correctly adjusted. Foreign tax credits can only be offset to the extent of foreign tax paid, or deemed to have been paid, on foreign income. Foreign tax offset claims of more than $1,000 are determined according to the *foreign income tax offset limit*. See worked example from the ATO: Foreign Tax Offset •
	• Confirm whether CGT cost base adjustments required by section 104-70 of the ITAA 1997 (relating to differences between accounting and tax distributions from trusts) have been recorded and adjusted correctly. • Non arm's length income has been correctly identified and tax applied at the appropriate rate.

Ref	Audit Procedure
O.2	Where deferred tax is reported by the fund, complete the following procedures: • Check the deferred tax assets and liabilities are correctly calculated and reflected in the financial report including: - Deferred tax assets arising from unrealised losses are after discounting. - Deferred tax assets arising from tax losses have only been brought to account where the trustee is confident that these will be recoverable in the future. • Prove the deferred tax assets and liabilities represent the tax effect of timing differences.
O.3	Confirm that tax has been calculated for ordinary income at 15%, unless the SMSF has received a notice advising it is non-complying for tax purposes. Ensure non-arm's length income is taxed appropriately
O.4	Confirm that PAYG instalments and TFN credits paid by the SMSF during the period have been correctly identified and applied against the current tax liability.
P	**GOING CONCERN**
P.1	As the members of a defined contribution fund absorb any losses incurred, it is rare for these types of funds to have going concern issues. However, a going concern issue can arise when a fund has been wound up and the members were paid benefits exceeding their entitlements. Complete the following procedures in relation to going concern: • Review the net asset position of the fund to determine if a net asset deficiency exists. • Consider a modification to the auditor's report. • Solvency issues may be identified if the financial statements have not been correctly stated at market value. If you cannot obtain appropriate substantiation of the market value of significant fund assets or liabilities, you may not be able to attest that the fund is a "going concern".
Q	**SUBSEQUENT EVENTS**
Q.1	Identify any subsequent events which would affect the financial report, including any adverse events impacting investments, significant investment fluctuations and plans to wind up the fund that should be disclosed in the financial reports.
R	**OTHER AUDIT CONSIDERATIONS**
R.1	If there have been any transactions with related parties, ensure that these matters have been appropriately addressed and reported in accordance with the accounting policies adopted by the SMSF.
R.2	Check whether material commitments and contingencies are properly disclosed by reviewing or obtaining: • Trustee minutes. • Solicitors' representations. • Trustees' representations.
R.3	Consider the risk of fraud in the design of audit procedures and when evaluating trustees representations. Make reference to the requirements of ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*.
S	**TRUSTEE REPRESENTATIONS**
S.1	Obtain written representations from the trustee.
S.2	Evaluate that the representations appear reasonable and consistent with the other audit evidence and conclusions.
S.3	If necessary, seek corroborative evidence on trustee representations.

T	**COMMUNICATIONS WITH TRUSTEES**
	Check that all matters of governance interest arising from the audit are communicated to the trustees on a timely basis, including: • Responsibilities of the auditor in relation to the financial report audit, usually communicated in the engagement letter; • Overview of the planned scope and timing of the audit, usually communicated in the engagement letter but not in a level of detail that may compromise the effectiveness of the audit; • Auditor's views about significant findings from the audit engagement; - Significant matters discussed with the trustees include uncorrected misstatements aggregated by the auditor during the audit that were determined by the trustees to be immaterial, both individually and in the aggregate, to the financial report taken as a whole; • Confirmation as to the independence of the auditor.

Appendix 5

(Ref: Para. 49)

ILLUSTRATIVE EXAMPLES OF THREATS TO INDEPENDENCE IN A SELF-MANAGED SUPERANNUATION FUND

The following table, based on principles stated in APES 110 Code of Ethics for Professional Accountants (including Independence Standards)[212], provides examples of some of the scenarios which practitioners may face when auditing SMSFs, the type of threats to independence the scenarios present and appropriate safeguards which may address those threats. Assurance practitioners are expected to be fully compliant with the requirements of APES 110 as required by Regulation 9A.06 of the SISR.[213]

	Type of threat					
Scenario	**Self interest**	**Self-review**	**Advocacy**	**Familiarity**	**Intimidation**	**Appropriate safeguards**
1. An auditor is a trustee or director of a corporate trustee and/or a member of the fund	X	X		X		No safeguards are available which would enable the practitioner to perform audit work, as this involves clear self-interest threats. An auditor who undertakes such an engagement is in clear breach of their professional and ethical obligations.
2. A sole practitioner prepares a SMSF's accounts and performs the financial audit and compliance engagement.	X	X				No safeguards are available which would enable the practitioner to perform both the accounting and audit work, as this involves the auditor reviewing their own work. The auditor withdraws from either the accounting or audit engagement. The resultant loss of work by withdrawing may be overcome by entering into reciprocal arrangements with a range of independent practitioners or firms for referral of SMSF audit engagements. It is important that these arrangements are subject to regular rotation to maintain independence and avoid self-interest, familiarity and intimidation threats. Your engagement should be directly with the SMSF Trustee not via an agency with the referring practitioner.
3. A sole practitioner signs the auditor's report for a SMSF and uses staff to perform the financial audit and compliance engagement work and to prepare the SMSF's accounts.	X	X			X	No safeguards are available which would enable the practitioner to sign the auditor's report as well as supervising the accounting work, as the practitioner is ultimately responsible for the accounting work and this amounts to reviewing their own work. The auditor withdraws from either the accounting or audit engagement.
4. A sole practitioner provides financial advice and audits the SMSF.	X	X	X			No safeguards are available which would enable the practitioner to perform both the financial advisory and audit work, as this involves the auditor in assessing the compliance implications of their own advice. The auditor withdraws from either the financial advisory or the audit engagement. If the audit engagement was terminated, the resultant loss of work may be overcome by entering into reciprocal arrangements with a range of independent practitioners or firms for referral of SMSF audit engagements. It is important that these arrangements are subject to regular rotation to maintain independence and avoid self-interest, familiarity and intimidation threats. Your engagement should be directly with the SMSF Trustee not via an agency with the referring practitioner.
5. A two partner practice in which one partner is asked to	X	X			X	No safeguards are available which would enable the practitioner to perform audit work, as this involves a clear self-interest threat. The auditor would not undertake the audit engagement.

[212] Issued June 2010: amended 2011, 2013, 2017, April 2018 and compiled November 2018).
[213] In addition to these examples, assurance practitioners may make reference to the Joint Accounting Bodies *Independence Guide*, Fourth Edition, February 2013.

	Type of threat					
Scenario	**Self interest**	**Self-review**	**Advocacy**	**Familiarity**	**Intimidation**	**Appropriate safeguards**
audit the SMSF of which the other partner is a trustee.						
6. A two partner practice in which one partner prepares the SMSF's accounts and the other partner conducts the audit. Common staff work on both engagements.	X	X			X	Threats may be overcome by safeguards including removal of staff who prepare the accounts from the audit team, implementing policies and procedures prohibiting those in the firm who provide accounting services from making decisions on behalf of the SMSF, requiring source data and underlying assumptions to be generated by the SMSF, obtaining SMSF approval for any journal entries, obtaining the SMSF's acknowledgement of their responsibility for the accounting work performed by the firm and disclosing to the trustees the firm's involvement in both engagements.
7. A two partner practice where one partner provides financial advice to the SMSF and the other partner audits the SMSF and prepares the SMSF's accounts.	X	X	X			Threats may be overcome by applying safeguards which include each of the two partners performing one of the engagements, with appropriate segregation of the engagement teams, and the firm withdrawing from the third engagement. For example, if one partner conducts the financial advisory work, the second partner prepares the accounts and then the firm withdraws from the audit and segregates the staff working on the engagements which are retained. Additional safeguards may include: implementing policies and procedures to prohibit individuals providing advice from making managerial decisions on behalf of the SMSF and ensuring that the individual providing the advice does not commit the SMSF to the terms of any transaction or consummate a transaction on behalf of the SMSF.
8. A firm prepares the SMSF's annual return and also undertakes the audit of the SMSF.		X				Where the client takes responsibility for the SMSF annual return including any significant judgements, it will not generally create threats to independence.
9. A sole practitioner audits numerous SMSFs but they are all administered by the same service provider who engages the auditor on behalf of the trustees. The sole practitioner is very reliant on fees generated by referrals from the service provider.	X				X	Safeguards include expanding the client base so that reliance on the administrator is reduced, declining to accept any further audits from the administrator, obtaining external quality reviews and ensuring that the practitioner has direct access to the trustees of each SMSF, so that matters arising during the audit may be communicated without fear of intimidation.
10. A member of the audit engagement team has a close or immediate relationship with the trustees of the SMSF. The auditor signing the audit opinion supervises the team member's work.				X		Safeguards include removing the audit member from the audit engagement team.
11. The auditor has provided accounting advice in relation to a material transaction of the SMSF which was then entered into		X				Technical assistance on accounting principles and advice an accounting issues often form part of the normal audit process and may promote fair presentation of the financial report and may not create a threat to independence. However, in certain instances, the advice may have influenced the decision making of the SMSF and safeguards may include segregation of the partners and staff providing accounting advice from the audit team or withdrawal from the audit engagement.

	Type of threat					
Scenario	**Self interest**	**Self-review**	**Advocacy**	**Familiarity**	**Intimidation**	**Appropriate safeguards**
on the basis of that advice.						
12. A partner in a multi-partner practice has had the SMSF as an audit client for "years" and regularly socialises with the SMSF's trustee.				X		The long and personal association with the trustee may compromise the partner's objectivity. Safeguards include transferring the engagement to another partner within the firm or quality control review of the audit findings, including conclusions on significant matters arising in the audit by another partner prior to sign-off of the audit opinion.
13. A practitioner or firm providing administrative services to numerous SMSFs, outsources all of the SMSF audits to one approved SMSF auditor.		X				The practitioner has implemented appropriate safeguards to avoid a self-review threat by referring the audit work to another auditor and it is the responsibility of that auditor to ensure that they are not as reliant on the referrals from the practitioner as to create a self-interest or intimidation threat.
14. Reciprocal auditing arrangements - Two Auditors who audit each other's SMSF - Two Accountants, also Auditors, audit each other's book of SMSFs	X			X	X	ATO and ASIC consider no safeguards can be put in place to eliminate independence threats in relation to a reciprocal auditing arrangements. See ATO Guidance. Reciprocal audit arrangements should be spread across a range of practitioners and subject to frequent rotation to limit independence threats.
15. Family relationships between Auditor and Accountant who conduct separate practices	X			X	X	The family relationship may compromises the SMSF's objectivity when conducting the audit and the threat of intimidation may be present. The Practitioners need to assess their ability to maintain independence in their respective engagements and document their self-assessment thoroughly. Safeguards may include ensuring direct engagement with the SMSF trustee including billing and not limiting audit sampling for each SMSF that is a client of the relative's firm. The Auditor would find it more difficult to prove their independence if all the SMSF audits were generated by referral from the relative's firm. Having a more broad audit client book would provide some mitigation from the independence threat.

Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**7.0**
Meeting Date:	3 March 2020
Subject:	EER ANZ Survey Update and Highlights
Date Prepared:	24 February 2020

☐ **Action Required** ☒ **For Information Purposes Only**

Agenda Item Objectives

1. To update the AUASB on the progress with the EER ANZ (Australia & New Zealand) Survey and plan to progress, including collaboration with other National Standard Setters (NSS).

Background

As a part of the AUASB Evidence-Informed Standard Setting (EISS) Strategy, the Australian Auditing and Assurance Standards Board (AUASB) collaborated with New Zealand Auditing and Assurance Standards Board (NZAuASB) to issue a survey to understand EER assurance practices and the application of ISAE(ASAE) 3000 series in Australia and New Zealand. The main objectives of this survey were to gather views from leading assurance practitioners about:

1. to what extent ISAE 3000 (or jurisdictional equivalent, including other ISAEs) is being utilised for assurance engagements on EER; and
2. what innovative practices are being used or developed to enhance credibility and trust in EER.

This survey was issued by the AUASB at the end of September 2019 and the NZAuASB in the middle of October with an initial one month response period. This was further extended in both jurisdictions so adequate follow up of participants could be undertaken to increase the response rates.

In this survey, we are interested in public reporting of EER only (reports to the public or other parties outside of the reporting entity), rather than internal reporting (reports available only to the reporting entity). It is understood that assurance engagements are an important means of enhancing trust in EER. Thus, the first section of this survey focuses on how standards on assurance engagements are applied for EER engagements.

The second part focused on other credibility enhancing techniques applied on EER engagements. Even though these techniques may or may not provide assurance over EER, they have a positive effect in public

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trust in company reports. The AUASB has an active interest in understanding and monitoring these credibility-enhancing techniques applied in the market.

Matters to Consider

Part A – Progress with EER Australian and NZ Survey (ANZ)

The AUASB designed an online questionnaire combining open-ended questions, multiple choice questions and ranking questions to collect assurance practitioners' views about their views on current practices of EER assurance, including standards applied for EER assurance engagements. The open-ended questions allowed respondents to convey complementary information and contribute to our interpretation of overall results.

To conduct this survey, we selected 27 practitioners in Australia and 7 in New Zealand who are engagement leaders or technical directors responsible for EER engagements in mid-to-large accounting firms as we believe they have sufficient competence and experience to complete the survey. They received a direct invitation to participate. 15 assurance practitioners (12 in Australia and 3 in New Zealand) have responded to this survey.

Refer to the summary of highlights from EER Survey at Agenda Item 7.1.

Refer to draft detailed EER Survey Results Report at Agenda Item 7.2 including further background, results and implications and recommendations with comparisons to NZAuASB survey results where appropriate. Still outstanding and yet to be completed is the literature review on current research in the area of EER which may be a useful reference. This would also need to consider other jurisdictions, including Canada and Netherlands if they commit to promulgating, the survey in their jurisdictions.

Part B – Collaboration with NSS on EER Survey

The AUASB are currently leading the EER NSS initiative focusing firstly on the EER survey. The discussions to date with other NSS jurisdictions include: NZAuASB, Canada and Netherlands.

NZAuASB

The NZAuASB survey had a low participation rate so we are considering whether based on the discussion at AUASB March meeting and the imminent release of the IAASB EER Guidance, we may look to do a joint communication on both to increase the number of NZ participants.

The low response rate probably may also reflect that EER and the assurance there on is still in the very early stages in New Zealand. The NZAuASB may look to focus on participation from the larger firms as the three respondents did not represent this group of assurance practitioners.

Canada (Auditing and Assurance Standards Board)

Canada are forming an advisory group to assist their Board and staff with the IAASB's EER project. The first meeting is likely to be in first quarter 2020. At that meeting, Canada hope to use the AUASB survey as a starting point for assessing the extent of EER reporting in Canada from the advisory group's perspective and whether the survey should be published for broader comment. Canada will share the results at an appropriate time.

Netherlands (NBA -The Royal Netherlands Institute of Chartered Accountants)

The ANZ Survey was sent to Netherlands at the end of October asking for their participation as part of the NSS collaboration plan. To date we have not heard back from Netherlands on what their plans are specifically in this area. A follow up via email has been sent.

As part of the AUASB Chair's discussions with other NSS other territories may also take part in a similar survey in the future.

Part C – "Compelling Reasons" Assessment

1. N/A

The proposed changes conform with IAASB modification guidelines for NSS?	Y	☐	N	☐

<u>Material Presented</u>

Agenda Item 7.0	AUASB Board Meeting Summary Paper
Agenda Item 7.1	EER Survey Highlights
Agenda Item 7.2	EER Survey Results Report (ANZ)

EER Survey Highlights

Background

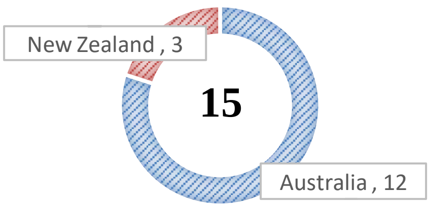
There is an increasing volume of external extended reporting (EER) in annual reports and other forms e.g. sustainability report to address stakeholders' expectations. Meanwhile, demand from both investors and regulators to support the credibility and trust in non-financial information outside the audited financial statements also continues to rise in the market. However, from the supply side, Big 4 firms have reported a limited number of clients who are undertaking assurance engagements or other credibility enhancing services on EER. Practitioners find it challenging to apply extant standards or guidance to conduct assurance engagements over EER.

AUASB collaborated with NZAuASB and issued a survey to gather current market views from leading assurance practitioners about:

1. to what extent ISAE 3000 (or jurisdictional equivalent, including other ISAEs) is being utilised for assurance engagements on EER; and
2. what innovative practices are being used or developed to enhance credibility and trust in EER.

Methodology

The AUASB designed an online questionnaire combining open-ended questions, multiple choice questions and ranking questions. The complete questionnaire is available at [link].



We received 12 responses from Australian practitioners and 3 from New Zealand practitioners (15 in total). All respondents are engagement leaders or technical directors responsible for EER engagements in mid-to-large accounting firms. They received a direct invitation to participate. Around 70% of respondents claim that they provide EER assurance services for clients with annual revenue of more than 100 million AUD. Their clients are across multiple industries.

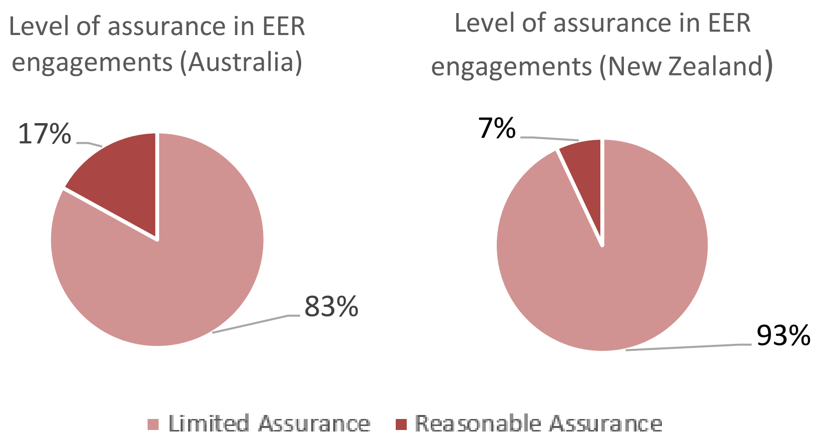
Key Results

- In general, there is an **increasing** trend in providing assurance over EER.

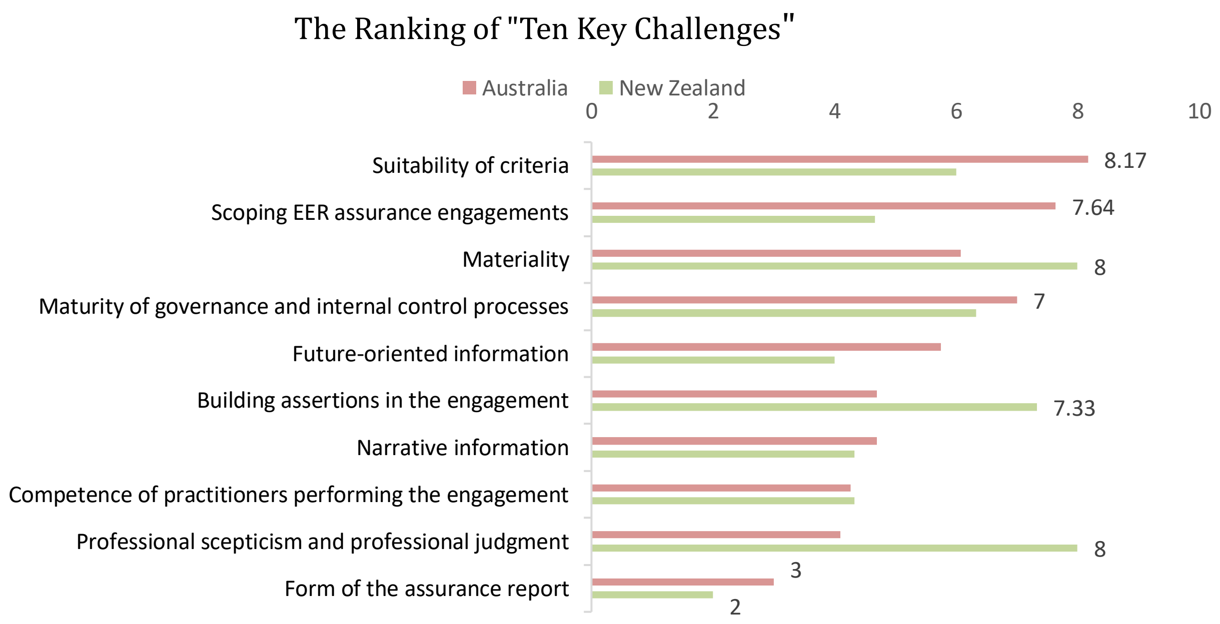
- The respondents are most likely to perform assurance engagement on **GHG reports**, the assurance scope usually lies **in key components or selected metrics**, and sometimes the whole report. Assurance practitioners are most likely to provide a **separate assurance report** conveying findings and recommendations for an EER assurance engagement.

- **ISAE (ASAE) 3000 series**, compared to other standards in the market, is the most widely applied standards for EER assurance engagements in both Australia and New Zealand.

- The majority of EER assurance engagements are **voluntary** and provide **limited assurance** to the users of the report.



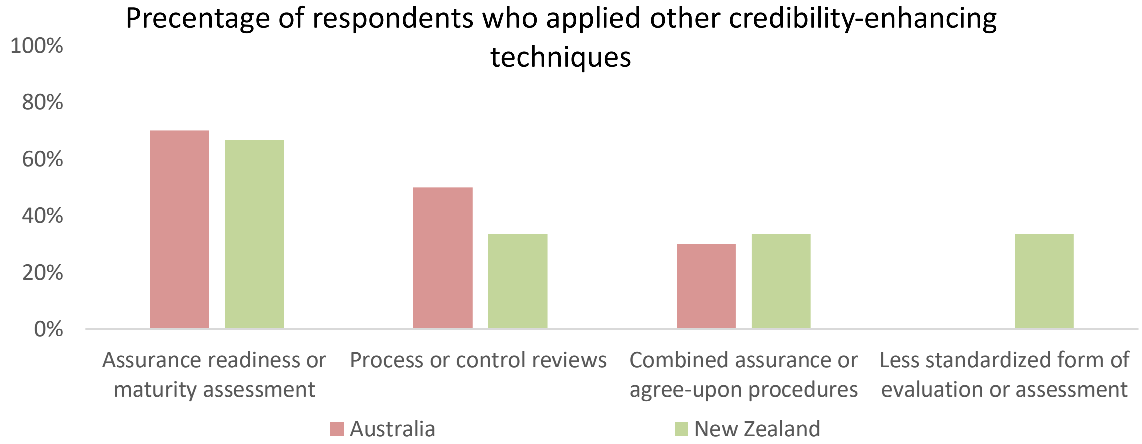
- The ranking of ten key challenges is demonstrated below:



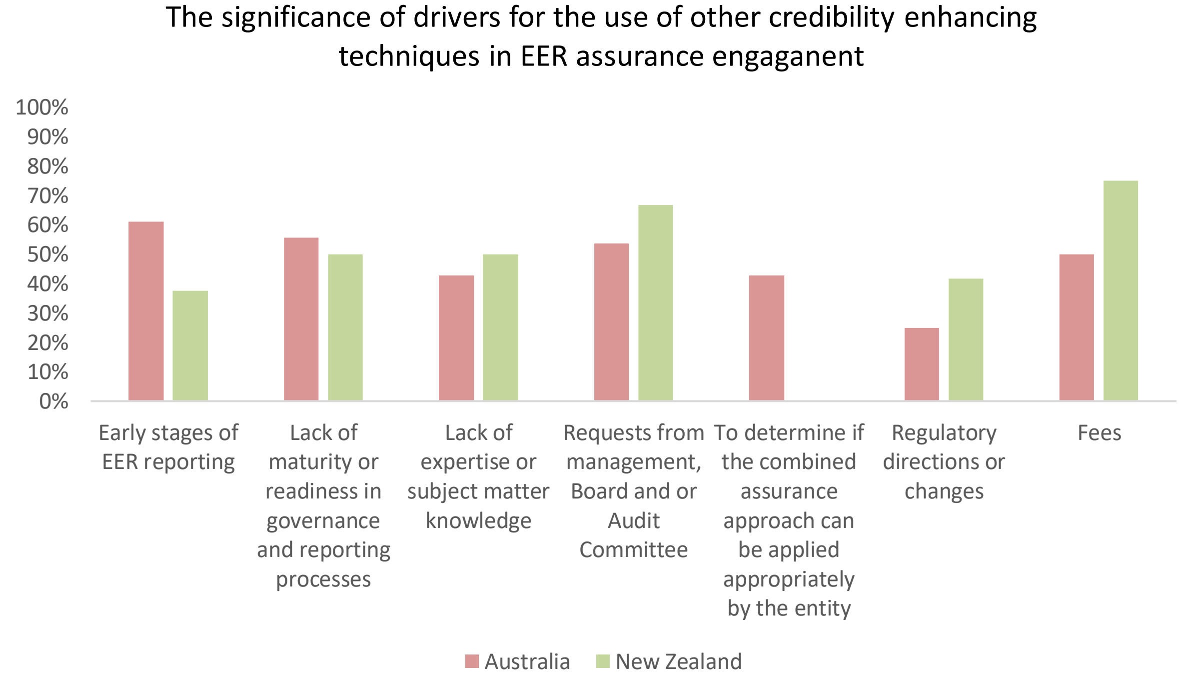
Note: 10 = the most challenging; 1= the least challenging

- Apart from these ten challenges, the respondents face difficulty in **identifying the subject matter**. Concerns are also raised around **low fees** charged for EER assurance engagements and **limited knowledge and competency** among non-big 4 firms to undertake such engagements.

- Besides assurance engagements, other innovative assurance practices have been used or developed to enhance credibility and trust in EER.



- The primary driver of adopting innovative assurance practices is the early stage of EER in Australia and fees in New Zealand.



EER Survey Results Report

Background

Non-financial information (NFI), compared to the financial statements, is a large proportion of information reported by companies external reporting suite. Investors rely on non-financial information to assess the business strategy and the creation of long-term value (EY, 2018), and thus the quality of NFI is with great importance for investors' decision-making (PwC, 2018). With reference to the Trust Barometer 2019, consumers expect corporate leaders to be more vocal and accountable to maintain their licence to operate social, economic and environmental issues (McIntyre, 2019). Company performance in addressing these expectations, if disclosed, are usually conveyed as NFI in corporate annual reports. In response to the market demand, there is an increasing volume of non-financial information disclosed outside of financial information (PwC, 2018).

Demand for the credibility and trust in non-financial information outside the audited financial statements continue to increase. Investors are calling for relevancy and reliability of non-financial information, and they believe assurance engagements can assist with the confidence in the information reported (PwC, 2018). However, currently only a limited number of companies provide assurance on non-financial information (EY, 2018). The qualitative nature of non-financial information creates challenges for assurance practitioners in conducting assurance engagements (ACCA, 2015). In addition to assurance engagements, we have also noted some innovative credibility-enhancing techniques conducted in the market to strengthen investors' trust in reported information, even though these techniques may not necessarily provide a level of assurance.

Standard-setters have realised assurance practitioners are facing challenges in assuring NFI (ACCA, 2015), and thus the topic of assurance over non-financial information is high on the strategic agenda. The International Auditing and Assurance Standards Board (IAASB) launched a project in relation to credibility and trust in emerging forms of external reporting, namely extended external reporting (EER). EER encapsulates many forms of reporting, including but not limited to, integrated reporting (IR), sustainability reporting, and other reporting by entities about environmental, social and governance matters (IAASB, 2019). Such reports may be required under legislative or regulatory, or voluntarily prepared under established reporting frameworks or guidelines.

As part of the AUASB Evidence-Informed Standard Setting (EISS) Strategy, the Australian Auditing and Assurance Standards Board (AUASB) collaborated with New Zealand Auditing and Assurance Standards Board (NZAuASB) to issue a survey to understand EER assurance practices and the application of ISAE(ASAE) 3000 series in Australia and New Zealand. The main objectives of this survey were to gather views from leading assurance practitioners about:

1. to what extent ISAE 3000 (or jurisdictional equivalent, including other ISAEs) is being utilised for assurance engagements on EER; and
2. what innovative practices are being used or developed to enhance credibility and trust in EER.

In this survey, we are interested in public reporting of EER only (reports to the public or other parties outside of the reporting entity), rather than internal reporting (reports available only to the reporting entity). It is understood that assurance engagements are an important means of enhancing trust in EER. Thus, the first section of this survey focuses on how standards on assurance engagements are applied for EER engagements.

The second part focused on other credibility enhancing techniques applied on EER engagements. Even though these techniques may or may not provide assurance over EER, they have a positive effect in public trust in company reports. The AUASB has an active interest in understanding and monitoring these credibility-enhancing techniques applied in the market.

Insofar the IAASB has prioritised the non-authoritative guidance for EER as one of their strategic actions for 2020-23 (IAASB, 2019). Accordingly, the AUASB has also listed assurance over emerging forms of extended external reporting as one of the strategic priorities over the period FY2019-20 (AUASB, 2019). Findings from this survey are expected to contribute to ways forward for international or national standard setters.

Literature Review (Yet to be fully completed)

Company performance in addressing investors' expectations, if disclosed, are usually conveyed as NFI in corporate annual reports.

There is an increase in the application of ISAE 3000, and this increase can mainly be attributed to rising number of practitioners outside accounting profession.

ISAE 3000 improves assurance quality and the quality of information conveyed in the assurance report.

Methodology

The AUASB designed an online questionnaire combining open-ended questions, multiple choice questions and ranking questions to collect assurance practitioners' views about their views on current practices of EER assurance including standards applied for EER assurance engagements. The open-ended questions allow respondents to convey complementary information and contribute to our interpretation of overall results. The complete questionnaire is available at [https://www.surveymonkey.com/r/NQMQ9RP].

To conduct this survey, we selected 27 practitioners in Australia and 7 in New Zealand who are engagement leaders or technical directors responsible for EER engagements in mid-to-large accounting firms as we believe they have sufficient competence and experience to complete the survey. They received a direct invitation to participate. 15 assurance practitioners (12 in Australia and 3 in New Zealand) have responded to this survey. In our sample, around 70% of respondents claim that they provide EER assurance services for clients with annual revenue of more than 100 million AUD, and the remainder provide services for relatively smaller clients. Their clients are across multiple industries.

Results

- There is an increasing trend in providing assurance over EER in Australia. 9 out of 12 respondents in Australia indicate that there is an increase in the number of EER engagements undertaken over last three years, among which 3 respondents indicate the increase is large. However, 2 out of 3 New Zealand respondents indicate that about the same number of EER assurance engagements were undertaken over the last three years.

- The majority of EER assurance engagements provides limited assurance to the users of the report. In Australia (New Zealand), 83% (93%) of EER assurance engagements provide limited assurance, while 17% (7%) of them provide reasonable assurance.

- The respondents are most likely to perform assurance engagement on GHG reports, followed by other subjects such as green or social bonds or sustainability-linked contract review.

- The assurance scope usually lies in key components or selected metrics, and sometimes the whole report. The selected components or metrices vary from engagement to engagement such as greenhouse gas emissions, specific KPIs, customer engagement and satisfaction, related datasets, etc.

- Compared to a combined assurance report of financial statements and EER, we found assurance practitioners are most likely to provide a separate assurance report conveying findings and recommendations for an EER assurance engagement.

- We found the majority of EER is voluntary reporting as compared to regulatory reporting. Likewise, the entities voluntarily provide assurance over EER. In most cases, the entity voluntarily undertook extended external reporting to meet corporate social responsibility or stakeholders' expectation. Entities were thus motivated to voluntarily provide assurance over EER for the purpose of enhancing credibility and trust with stakeholders and demonstrating best practice leadership. However, in the financial services industry, a company can be required to have a compliance review conducted by external assurance provider under *Anti-Money Laundering & Counter Terrorism Financing Act 2006*.

- ISAE (ASAE) 3000 series is the most widely applied standards for EER assurance engagements. All respondents applied ISAE (ASAE) 3000 series for their EER assurance engagements. Besides this series of standards, AA1000 may also be applied in some cases. This finding is consistent with New Zealand survey results.

- The IAASB has identified "Ten Key Challenges" in relation to EER assurance in IAASB Feedback Statement (2018) *Supporting Credibility and Trust in Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements*. In this survey, we further asked about the level of ten key challenges:

- Overall the top ranking challenge is suitability of criteria (7.54/10[1]) in Australia and New Zealand market, which is followed by the lack of maturity of governance and internal control processes (7.38/10).
- The respondents also faced challenges of scoping EER assurance engagements (6.5/10) and assessing materiality (6.31/10).
- The following factors are recognised as not as significant as those mentioned above: building assertions in planning and performing the engagement (5.55/10), professional scepticism and professional judgement (5.36/10), future-oriented information (5.23/10), narrative information (4.82/10), competence of practitioners performing the engagement (4.33/10) and form of the assurance report (2.55/10).
- Discussed at country-level, the most significant challenge in Australia is consistent with the overall results, while it is professional scepticism and professional judgement in New Zealand.

• Apart from these ten challenges, the respondents face difficulty in identifying the subject matter. Concerns are also raised around low fees charged for EER assurance engagements and limited knowledge and competency among non-big 4 firms to undertake such engagements.

• The AUASB also wanted to draw out other innovative assurance practices being used or developed to enhance credibility and trust in EER. Based on the key challenges EER assurance engagements are unique and may require more application of credibility-enhancing techniques. In addition to assurance engagements, there are some other credibility enhancing techniques being applied to EER.

  - Around 70% of respondents believe credibility of EER can be enhanced by assurance readiness or maturity assessments, i.e., testing pre-conditions for EER assurance engagements. The practitioners are only permitted to undertake an assurance engagement when the preconditions for an engagement are present. The preconditions include but is not limited to financial reporting preparers' integrity around processes and assertions and practitioners' competences and capabilities. (IAASB, 2019).
  - Nearly 50% of respondents conducted process or control reviews to improve credibility of EER.
  - Approximately 40% of respondents adopted combined assurance techniques that is defined as a credibility enhancing model of multi-lines of defence with aim of optimising the assurance coverage obtained from management, internal assurance providers and external assurance providers (Zhou, et al., 2019).
  - Around 30% of respondents also undertook agreed upon procedures as credibility enhancing techniques.

[1] 10 = most challenging; 1=least challenging

- This survey further explores the underlying reasons for innovative practices in EER assurance engagements. For example, one respondent raised that the nature of assurance engagements on integrated reporting is different from assurance engagements under other reporting frameworks. To address the purpose of assurance, practitioners may have to apply some innovative procedures. The application and use of data analytical technology is also considered another innovative tool that may be applied in an EER engagement.

- From the perspective of assurance practitioners, there are several drivers to undertake other credibility enhancing techniques before completing an assurance engagement on EER.

    - In Australia, the most important attribution is the early stage of EER, and thus there is a lack of maturity or readiness in governance and reporting processes to pursue an assurance engagement. Management or the Board may request for credibility-enhancing services over EER for other reasons, including but not limited to fees.

    - In New Zealand, the primary driver was fees. However, noting that lack of maturity or readiness in governance and reporting process and management request are so important.

    - Another reason raised by respondents is that management is unwilling to undertake assurance engagements if the EER is poorly prepared and the likelihood of the assurance practitioner providing a qualified assurance conclusion/opinion is increased.

Implications and recommendations

- In general, assurance of EER is still in the early stages of development despite an increasing number of EER assurance engagements being undertaken over the last three years in Australia.

- In the majority of EER assurance engagements, practitioners provide limited assurance over key components or selected metrics.

- Practitioners are facing several challenges in appropriately conducting EER assurance services. One of the most significant challenges is the lack of suitability of criteria and difficulty in assurance scoping. Standard-setters may wish to further investigate these issues either through the International solution – EER guidance or a more localised solution addressing any possible jurisdictional gaps perceived in the market.

- ISAE (ASAE) 3000 series is the most widely applied standards for EER assurance engagements in Australia. Ge, Simnett and Zhou (2020) further found there was an increase in the application of ISAE 3000 after its revision in 2017. The application of ISAE 3000 had a positive effect on assurance quality as well as information quality in the assurance reports. They also found increasing number of assurance engagements are provided by practitioners outside accounting profession. This shows the importance in developing guidance with reference to ISAE (ASAE) 3000.

- In addition to assurance engagements, there are some other credibility enhancing techniques adopted by the market such as improving assurance readiness, process or review controls, combined assurance, agreed upon procedures etc.

- The main attribute to choosing other credibility enhancing techniques is a lack of maturity or readiness in governance and reporting process to pursue assurance engagements when industries are still at the early stage of EER. Fees charged for credibility enhancing services are another important driver. The AUASB might look to explore further the links between adoption of other credibility enhancing techniques, improvement in EER across a broad range of subject matter and the impact on engagement of assurance services and fees. Lu, Simnett and Zhou (2018)[2] revealed that the financial statement auditor is much more likely to take over the NFI assurance service and becomes the sole provider than being taken over by the NFI assuror. Finally, companies with the same provider attesting to both financial and NFI have higher audit quality without paying significantly higher audit fees. This would also need to consider the impact of initiatives being undertaken by key stakeholders on NFI (e.g. users, preparers, regulators, standard setters and assurance practitioners) in the reporting supply change.

Limitations

We acknowledge this survey is subject to several limitations.

(1) The sample size may be insufficient to have conclusion.

(2) Potential sample selection bias may exist given we are only targeting expertise assurance practitioners in mid-large tier.

[2] Lu, Simnett and Zhou - Exploring the nexus between financial statement audit and non-financial information assurance via the engagement of the same versus different assurance providers (2018).

Appendix

Table 1: Comparison between Australian and New Zealand Results

Australian Results	New Zealand Results
There is an increasing trend of providing assurance over EER. 9 out of 12 respondents indicate that there is an increase in the number of EER engagements undertaken over last three years, among which 3 respondents indicate the increase is large.	2 out of 3 respondents indicate about the same number of EER engagements undertaken over last three years, the remaining one respondent indicates a slight increase in the number of EER engagements over last three years.
On average, 83% of EER assurance engagements provide limited assurance, while 17% of them provide reasonable assurance.	On average, 93% of EER assurance engagements provide limited assurance, while 7% of them provide reasonable assurance.
The assurance scope usually lies in key components or selected metrics, and sometimes the whole report.	The assurance scope usually lies in key components or selected metrics, and sometimes the whole report.
The conclusion on the EER assurance engagement is always in a separate assurance report instead of a combined report of financial statements and EER	In most cases, practitioners issue a separate assurance report. However, 2 out 3 respondents indicate they would issue a combined report in rare cases.
In Australia, the majority of EER is voluntary reporting as compared to regulatory required reporting.	EER assurance engagements are voluntarily undertaken. (no sufficient information for reporting)
ISAE (ASAE) 3000 series is the most widely applied standards for EER assurance engagements in Australia	ISAE (ASAE) 3000 series is the most widely applied standards for EER assurance engagements New Zealand.
Australian respondents ranked suitability of criteria to be the most significant challenge in an EER assurance engagement (8.17/10[3]), which is followed by scoping EER assurance engagements (7.64/10).	New Zealand respondents rank professional scepticism and professional judgement (8/10) and materiality (8/10) as the most challenging factors in EER assurance engagements. They also felt

[3] 10 = most challenging; 1=least challenging.

They also face challenges with maturity of governance and internal control processes (7/10), materiality (6.08/10) and future-oriented information (5.75/10). The following challenges are not recognised as significant as those mentioned above: building assertions in planning and performing the engagement (4.7/10), narrative information (4.7/10), competence of practitioners performing the engagement (4.27/10), professional scepticism and professional judgement (4.1/10) and form of the assurance report (3/10).	challenging on building assertions in planning and performing the EER engagement (7.33/10). The lack of maturity of governance and internal control processes ranks the fourth (6.33/10).
Other credibility enhancing techniques - Assurance readiness or maturity assessment - Process or control reviews - Combined assurance or agree-upon procedures	Other credibility enhancing techniques - Assurance readiness or maturity assessment (2/3) - Less standardized form of evaluation or assessment resulting in either internal reporting to management or Those Charged with Governance (1/3) - Process or control reviews (1/3) - Combined assurance or agree-upon procedures (1/3)
Drivers to undertake other credibility enhancing techniques before completing an assurance engagement on EER - Early stage of EER - A lack of maturity or readiness in governance and reporting process - Requests from management, Board and/or Audit committee - Fees	Drivers to undertake other credibility enhancing techniques before completing an assurance engagement on EER - Fees - A lack of maturity or readiness in governance and reporting process - Requests from management, Board and/or Audit committee

Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**8.0.0**
Meeting Date:	3 March 2020
Subject:	GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups*
Date Prepared:	12 February 2020
Prepared by:	Johanna Foyster

☒ **Action Required** ☐ **For Information Purposes Only**

Agenda Item Objectives

1. To provide an update to the AUASB on the GS 012 revision project.

2. For the AUASB to consider and provide input into the draft revised GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs)*, particularly:

   (a) Treatment of Registered Financial Corporations (RFCs)

   (b) Updated guidance on materiality

   (c) Incorporation of APS 910 *Financial Claims Scheme* (APS 910)

   (d) Format of the APS 310 Assurance Report.

3. Discuss the way forward to finalise this Guidance Statement.

Project Update

4. A GS 012 Working Group consisting of 8 practitioners from the Big 6 accounting firms, with relevant technical knowledge and experience undertaking ADI and RFC prudential and regulatory reporting engagements, was established in October 2019 to provide input into the revision of GS 012. While APRA was invited to join the Working Group, it was subsequently agreed that the best way forward was for APRA to review and provide input offline into the revised guidance statement once the Working Group has reach consensus on a final draft.

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The AUASB was updated on progress with the GS 012 revision project at its 3/4 December 2019 meeting, following initial meetings of the GS 012 Working Group. For background information on the project, refer to Agenda Item 14 of the December 2019 AUASB meeting papers.

5. The GS 012 Working Group initially expressed a desire for RFCs to be included in the scope of the revised GS 012 on the basis APRA's audit requirements are broadly conceptually similar.

However, this proved difficult, as significant differences in the detail between ADIs and RFCs made drafting of a single guidance statement difficult. This is further explained in the Attachment to this BMSP (see Agenda item 8.0.1).

The Working Group ultimately expressed its preference for separate guidance to be issued for RFCs, which will allow such guidance to be tailored to the specific needs of RFC auditors.

6. Following the December 2019 AUASB meeting, a preliminary draft of the revised GS 012 was circulated to the GS 012 Working Group to solicit specific input/feedback from practitioners on:

- Materiality and application of APRA's Reporting Practice Guide RPG 702 *ABS/RBA Data Quality for the EFS Collection* (RPG 702.0) to PARTS A, B and C of the engagement.
- Guidance and application material to be developed in relation to APS 910, identifying the special considerations in undertaking limited assurance engagements of ADI controls addressing generation of Single Customer View (SCV) data and Financial Claims Scheme (FCS) Payment Instruction and Reporting Information.
- Updating the illustrative example templates of assurance report(s), engagement letter(s) and representation letter(s) to be included as Appendices to the guidance statement.

7. A further Working Group meeting will take place on 24 February 2020 to resolve outstanding matters and to finalise the wording in the Guidance Statement to be sent to APRA and the Agencies (ABS and RBA) for consultation. A verbal update will be provided to the Board at the March 2020 AUASB meeting.

Revision of GS 012

8. Extant GS 012 has been updated as follows:

- Updates to reflect multiple revisions to APRA Prudential Standards since extant GS 012 was issued in June 2009, including:
    - o Risk management moved from APS 310 to a separate stand-alone Prudential Standard CPS 220 *Risk Management* containing additional requirements for directors' and managements responsibilities.
    - o New ADI Reporting Forms subject to reasonable and/or limited assurance, as specified in Attachment A to APS 310. In particular, ARF 210 *Liquidity Coverage Ratio* includes subject matter information which will require application of ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information* to provide assurance in relation to assumptions and methodology used as basis for prospective information.
    - o Inclusion of APS 910 in the scope of GS 012 – see Agenda Item 8.0.1.
    - o Consequential amendments from the implementation of the modernised Economic and Financial Statistics (EFS) data collection and introduction of the new AASB 9 *Financial Instruments*.

  - Consequential amendments to include Level 3 Conglomerate Groups.

- Materiality guidance and application material have been updated to:

  - Include specific guidance on application of RPG 702 to PARTS A, B and C of the engagement.

  - Address new subject matter included in the scope of GS 012 assurance engagements (e.g. EFS data and future oriented liquidity information)

  - Incorporate and reference to new/revised Australian Auditing Standards, for example: ASA 320 *Materiality in Planning and Performing an Audit*, ASA *450 Evaluation of Misstatements Identified during the Audit*, ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information,* which have been updated since 2009.

  See Agenda Item 8.0.1.

- Inclusion of further guidance to explain the concepts of 'reliability of information' and 'data quality' in the context of GS 012, including reference to APRA's Prudential Practice Guide CPG 235 *Managing Data Risk.*

- Inclusion of relevant requirements, guidance on application of, and references to, ASAE 3150 *Assurance Engagements on Controls*, which did not exist when the extant GS 012 was issued in 2009. ASAE 3150 is relevant to PART C of the APS 310 engagement in providing limited assurance on the design, implementation and operating effectiveness of controls, as well as the APS 910 engagement.

- Modernise and update illustrative example templates, included as Appendices to the guidance statement, for example, to:

  - Accommodate Level 2 ADI groups and/or Level 3 conglomerate groups

  - Reflect new APRA EFS reporting and assurance requirements

  - Reflect revisions to APS 310

  - Include APS 910 assurance engagements

  - Reflect recent enhancements to the format of the auditor's report, for example, moving the opinion/conclusion section to the front of the auditor's assurance report.

- Update references to multiple AUASB Standards that have been updated since 2009.

<u>Specific Matters for the AUASB to Consider at its March 2020 meeting</u>

Please refer to the attachment to this BMSP (Agenda Item 8.0.1) for specific matters to be considered by the Board at this meeting.

<u>NOTE</u>:

- A clean version of the latest draft of the proposed revised GS 012 *Prudential Reporting Requirements for Auditors of ADIs and ADI Groups* is attached for AUASB consideration and feedback – refer to Agenda Item 8.0.2.

- In the attachment to this BMSP (Agenda Item 8.0.1), the ATG will direct the AUASB to specific sections of the draft for review, consideration and to provide feedback. These sections have been highlighted in the attached clean draft. The full document is available to provide the necessary context.

- The ATG welcomes any other comments/feedback in relation to any part of the guidance statement.

Way Forward

1. Update the draft revised GS 012, tabled at this meeting, to include feedback from the 24 February GS 012 Working Group meeting and any feedback from the March AUASB meeting.
2. Circulate the updated draft to APRA and the Agencies (ABS and RBA) for review, feedback and further consultation if necessary.
3. Finalise the proposed revised GS 012.
4. Table the final proposed GS 012 (revised) at the 21 April 2020 AUASB meeting for consideration and approval to issue.

AUASB Technical Group Recommendations

1. The AUASB Technical Group recommends that the AUASB:
    - consider the comments and draft as presented;
    - consider feedback from the GS 012 Working Group from its 24 February meeting; and
    - provide further comment/input to enable finalisation of the guidance statement at the 21 April 2020 Board meeting

Material Presented

Agenda Item 8.0.0	AUASB Board Meeting Summary Paper (BMSP)
Agenda Item 8.0.1	Attachment to BMSP: Specific Matters for the AUASB to Consider at its March 2020 meeting
Agenda Item 8.0.2	Revised GS 012 *Prudential Reporting Requirements for Auditors of ADIs and ADI Groups* – Clean Draft

Action Required

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	AUASB to provide comments and feedback as outlined above	Comments at Board meeting	AUASB	3 March 2020	

Australian Government
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Attachment to AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**8.0.1**
Meeting Date:	3 March 2020
Subject:	Revised GS 012 *Prudential Reporting Requirements for Auditors of ADIs and ADI Groups*
Date Prepared:	12 February 2020

<u>Specific Matters for the AUASB to Consider at its March 2020 meeting</u>

<u>ITEM A</u>: Registered Financial Corporations (RFCs)

Background to Working Group deliberations:

1. APRA's new Reporting Standard RRS 710 *ABS/RBA Audit Requirements for Registered Financial Corporations – EFS Collection* (RRS 710), effective from 1 July 2019, mirrors the requirements of APRA Prudential Standards APS 310/3PS 310 *Audit and Related Matters* and is directed at RFCs not currently included under the APS/3PS 310 framework.

2. The GS 012 Working Group initially expressed a desire for RFCs to be included in the scope of a revised GS 012 on the basis that the requirements for appointed auditors under RRS 710 and APS 310/3PS 310 are very similar. However, this proved difficult, as significant differences between ADIs and RFCs made drafting of a single guidance statement difficult, for example:

   - APRA collects statistical data from RFCs under the *Financial Sector (Collection of Data) Act 2001* (FSCODA). RFCs are not prudentially regulated or supervised by APRA under the *Banking Act 1959* and APRA Prudential Standards are therefore not applicable to RFCs.

   - APS 310's requirement to report on compliance with Prudential Requirements (PART D) does not apply to RFCs. Further, the APS 310 requirement to report on internal controls (PART C) may be less in scope for RFCs under RRS 710.

   - APRA Prudential Standard APS 910 *Financial Claims Scheme* does not apply to RFCs.

3. The Working Group also noted that GS 012 guidance material may need to be tailored further to assist RFC auditors who may be undertaking these types of regulatory engagements for the first time. Although the reporting requirements for appointed auditors will be very similar under RRS 710 and APS 310, differences will need to be clearly articulated in the Guidance Statement in order to not confuse. Also, RFC specific illustrative example templates would need to be included in the Appendices to the guidance statement (assurance report, engagement letter and representation letter).

4. Therefore, it is proposed that the revised GS 012 include wording to indicate that GS 012 guidance may be considered and adapted as necessary in the circumstances, to assurance engagements undertaken pursuant to RRS 710.0.

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5. Further, the AUASB may, only if there is a clear need, consider issuing tailored guidance to assist auditors of RFCs, for example, in the form of a separate RFC specific AUASB Bulletin.

For AUASB Consideration and Feedback

6. Please refer to paragraphs 4 and 5 of the draft revised GS 012, attached as Agenda item 8.0.2

Does the AUASB support the proposed treatment of RFC requirements?

<u>ITEM B</u>: Materiality and application of RPG 702.0 to PARTS A, B and C of the engagement.

Background to Working Group deliberations:

7. The GS 012 Working Group identified a need for further guidance and application material to be developed, to provide clarity on how the concept of materiality is to be applied in planning and performing each part of the assurance engagement and in evaluating findings.

8. In particular, the Group identified a need for clarification around the application of APRA's Reporting Practice Guide RPG 702.0 *RBA/ABS Data Quality for the EFS Collection* (RPG 702.0), which was issued by APRA in 2018. RPG 702.0 provides guidance to ADIs and RFCs on the Agencies' (RBA and ABS) expectations for data accuracy in EFS Reporting Forms.

9. RPG 702 outlines how the Agencies, as primary users, intend to use data collected by APRA under the EFS Reporting Standards. Reporting entities are expected to use the 'data priority' ranking (standard/high/very high) included in RPG 702.0 as an indicator of the relative importance of the accuracy of these data items and, therefore, where to focus data quality management practices. The table in Attachment A to RPG 702.0 includes qualitative benchmarks to indicate the size of misreported data items that may impact the use of the data by the Agencies and thus would be considered a 'reporting error' that needs to be notified to APRA. These benchmarks vary according to entity size (large/not large), type of data item (stock/flow) and prioritisation of data.

10. Proposed GS 012 guidance clarifies that RPG 702.0 is primarily directed at reporting entities and that it is designed to assist these entities in meeting their EFS quality control requirements and to tailor their data risk management practices as outlined in CPG 235 *Managing Data Risk*. The auditor is not required to provide assurance to the levels set out in RPG 702.0. However, APRA and the Agencies expect auditors to take account of this guidance in determining materiality thresholds for undertaking the engagement and in evaluating findings.

11. The guidance statement explains why application of RPG 702.0 guidance may be more relevant to PART C of the engagement (reporting on internal controls). The auditor will need to consider how ADIs have incorporated RPG 702.0 thresholds and other relevant guidance, for example, CPG 235, into their risk management processes. Should an ADI identify errors that have occurred in relation to EFS reporting that exceed the data quality thresholds, this may be indicative of a control environment that is not appropriately designed or operating effectively to ensure entities have provided reliable data to APRA. In these instances, the auditor would be expected to assess the nature of the error, whether deficiencies in the control environment contributed to the error, and what subsequent changes have occurred (if any) to address these deficiencies. Where such deficiencies exist, the significance of these would need to be considered against PARTS A, B and C of the APS 310 opinion and conclusions.

12. New guidance is included to assist auditors when considering re-submissions of data and Reporting Forms to APRA and the potential impact on Parts A, B and C of the assurance engagement.

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13. Finally, as noted in the BMSP, materiality guidance and application materials have been updated to:

- address new subject matter included in the scope of the GS 012 assurance engagement, for example, to address EFS data and future oriented liquidity information included in ADI Reporting Forms specified in Attachment A to APS 310.
- incorporate and reference to the latest Australian auditing and assurance standards, for example:
    - ASA 320 *Materiality in Planning and Performing an Audit*, ASA *450 Evaluation of Misstatements Identified during the Audit* and ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, which have been revised since 2009, and
    - ASAE 3150 *Assurance Engagements on Controls*, which is a new standard issued in 2015.

For AUASB Consideration and Feedback

14. Please refer to paragraphs 88 to 151 and 238 to 268 of the draft revised GS 012, attached as Agenda item 8.0.2.

Does the AUASB support the consideration of materiality in the context of GS 012?

ITEM C: APS 910 Financial Claims Scheme

Background to Working Group deliberations

Background to Financial Claims Scheme (FCS)

15. The FCS was introduced to protect account-holders of locally incorporated ADIs from loss on their deposits, and to provide them with timely access to those deposits, in the event an ADI becoming insolvent, up to a maximum amount guaranteed by the Australian Government. APRA is responsible for the administration of the FCS and for making payments to account holders.

16. APRA has issued Prudential Standard APS 910 *Financial Claims Scheme* (APS 910) to assist ADIs to comply with the requirements of the FCS.

17. Under APS 910, ADIs are required to implement systems for the identification of protected accounts for each account-holder, to the extent practicable, and present an aggregated view, or 'single customer view' of each account-holder and meet payment, reporting, communications, testing and assurance requirements, which will enable APRA to pay out account-holders of the ADI in a timely and effective manner, in the event of an ADI being declared subject to the FCS.

18. The Board and senior management of an ADI and/or ADI group are therefore required to ensure that appropriate policies and procedures are in place to ensure the integrity of the operations, internal controls and information required under APS 910. This includes, but is not limited to:

    (a) ensuring that the systems and data required by APS 910 are subjected to an independent limited assurance engagement, in accordance with the requirements stipulated in APS 910, and that this assurance be provided at the same time as the assurance required by APS 310, unless otherwise agreed by APRA; and

    (b) providing an attestation from the Chief Executive Officer in accordance with the requirements stipulated in APS 910.

APS 910 Assurance Requirements

19. APS 910 requires the auditor, in accordance with APS 310, to provide limited assurance that, in all material respects:

    (a) the ADI and/or the ADI group has implemented internal controls that are designed to ensure:

        (i) compliance with all applicable Prudential Requirements relating to APS 910; and

        (ii) that SCV data, as set out in Attachment A of APS 910, ***to the extent practicable***, and FCS payment instruction and reporting information can be relied upon as being complete and accurate and in accordance with APS 910; and

    (b) the controls in (a) have operated effectively when tested.

20. APRA requires the timing of the APS 910 assurance engagement to be aligned with the annual APS 310 assurance engagement. A separate auditor assurance report for the APS 910 engagement may be completed but the requirement is that this report be submitted to APRA at the same time as the APS 310 prudential assurance report.

21. Outstanding APS 910 materials to be developed for inclusion in the final revised GS 012:

    - Appendix 2: Example Engagement Letter – update to accommodate APS 910 engagements
    - Appendix 3: Example Representation Letter – update to accommodate APS 910 engagements
    - New Appendix 6: The APS 910 auditor's report referred to in the Appendix 4 *Example Annual Prudential Assurance Report pursuant to APS 310/3PS 310*, will be attached as a separate new Appendix to the guidance statement.

22. For guidance on how the phrase 'to the extent practicable' is to be interpreted, the guidance statement (see paragraphs 236 and 237) directs the appointed auditor to guidance provided by APRA in the form of an information paper (issued August 2013) and guidance included under 'Frequently Asked Questions', which can be accessed on APRA's website.[1]

    Guidance included in the GS 012 notes that the phrase 'to the extent practicable' applies to those limited circumstances where it may not be possible for an ADI to meet a particular requirement. However, where possible, it is expected that the underlying assurance objective be met in full. This guidance is principle-based and does not limit the application of the auditor's professional judgement.

    APRA will be asked to review this section and to provide further clarification, should this be required.

[1] Refer to APRA's website:

- APRA Information Paper: *Financial Claims Scheme for ADIs*, August 2013, paragraph 37 on page 11.
- *Financial Claims Scheme – Frequently Asked Technical Questions for ADIs*, under *Section 3 Clearance* (Question 3.1, March 2014) and *Section 12 – Single Customer View (SCV)* (Question 12.2, March 2014).

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For AUASB Consideration and Feedback

23. The AUASB is directed to the following sections of the guidance statement which has been updated to take account of APS 910:

- Responsibilities of the ADI: Financial Claims Scheme - paragraphs 44-47
- Role and responsibilities of the appointed auditor - paragraphs 57-59
- Agreeing the terms of the APS 910 engagement - paragraph 68
- Matters to consider in conducting the engagement - paragraphs 228-237
- The auditor's annual prudential assurance report - paragraphs 295-297

24. Appendix 4 includes reference to a separate APS 910 assurance report (if applicable) and illustrates how Part C of the *Example Annual Prudential Assurance Report pursuant to APS 310/3PS 310* will be impacted.

<u>ITEM D</u>: Example Assurance Report on Annual Prudential Reporting Requirements

25. An illustrative example assurance report for engagements undertaken pursuant to APS 310 and 3PS 310, is included as Appendix 4 to the proposed guidance statement, attached as Agenda Item 8.0.2.

For AUASB Consideration and Feedback

26. The AUASB is asked to consider and provide feedback on the proposed format of the auditor's assurance report pursuant to APS 310/3PS 310.

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GS 012
(April 2020)

Guidance Statement GS 012
Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups

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

Australian Government
Auditing and Assurance Standards Board

Obtaining a Copy of this Guidance Statement

This Guidance Statement is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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Important Note

Guidance Statements are developed and issued by the AUASB to provide guidance to auditors and assurance practitioners on certain procedural, entity or industry specific matters related to the application of an AUASB Standard(s).

Guidance Statements are designed to provide assistance to auditors and assurance practitioners to assist them in fulfilling the objective(s) of the audit or other assurance engagement. Accordingly, Guidance Statements refer to, and are written in the context of specific AUASB Standard(s); and where relevant, legislation, regulation or other authoritative publication. Guidance Statements are not aimed at providing guidance covering all aspects of the audit or other assurance engagement. Further, Guidance Statements do not establish or extend the requirements under an existing AUASB Standard(s).

Guidance Statement *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups* is not, and is not intended to be, a substitute for compliance with the relevant AUASB Standard(s) and auditors and assurance practitioners are required to comply with the relevant AUASB Standard(s) when conducting an audit or other assurance engagement.

CONTENTS

APPENDICES

PREFACE

How this Guidance Statement is to be used

This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB), in consultation with the Australian Prudential Regulation Authority (APRA), to provide guidance to the appointed auditor of an Authorised Deposit-taking Institution (ADI) and/or appointed auditor of a Level 2 and/or Level 3 ADI Group, reporting pursuant to the prudential reporting requirements specified by the Australian Prudential Regulation Authority (APRA) in Prudential Standards APS 310 (APS 310) and 3PS 310 (3PS 310) *Audit and Related Matters*, and APS 910 *Financial Claims Scheme*.

The assurance requirements relating to these prudential reporting engagements may give rise to a number of special assurance considerations. Accordingly, this Guidance Statement has been developed to identify, clarify and summarise the responsibilities which the auditor has with respect to conducting such assurance engagements, and to provide guidance to the auditor on additional factors which the auditor may consider when planning, conducting and reporting in relation to prudential assurance engagements.

This Guidance Statement is to be read in conjunction with, and is not a substitute for referring to, the requirements and application and other explanatory material contained in:

(a) APS 310, 3PS 310, APS 910, and other applicable APRA Prudential Requirements, including the *Banking Act 1959* (Banking Act), the *Financial Sector (Collection of Data) Act 2001* (FSCODA), and APRA Prudential and Reporting Standards;

(b) applicable AUASB Standards; and

(c) relevant ethical and professional standards.

This Guidance Statement does not extend the responsibilities of an appointed auditor of an ADI and ADI Group beyond those which are imposed by the Banking Act, the FSCODA, APRA Prudential and Reporting Standards, AUASB Standards and other applicable legislation.

It is not the intention of this Guidance Statement to provide step-by-step guidance in relation to the conduct of a prudential reporting engagement and it is not to be used as a checklist of all issues to be considered by the appointed auditor.

It is not intended that this Guidance Statement limits or replaces the appointed auditor's professional judgement or limits the application of relevant AUASB Standards on such engagements. AUASB Standards contain the requirements to be applied to assurance engagements. Assurance engagement programs are to be designed by the auditor to meet the requirements of the particular circumstances, giving careful consideration to the size, business mix and complexity of the ADI and/or ADI Group and the adequacy of the ADI's or ADI Group's internal control structure.

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

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

This Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

R Simnett AO
Chair - AUASB

GUIDANCE STATEMENT GS 012

Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups

Application

ADIs and ADI Groups

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to the appointed auditor of an Authorised Deposit-taking Institution (ADI) and/or appointed auditor of a Level 2 and/or Level 3 ADI group, reporting pursuant to the prudential reporting requirements specified by the Australian Prudential Regulation Authority (APRA) in Prudential Standards APS 310 (APS 310) and 3PS 310 (3PS 310) *Audit and Related Matters*[1]

2. APS 310 applies to all ADIs from 1 July 2019. 3PS 310 applies to each 'Level 3 Head', in its capacity as parent institution of a 'Level 3 Group', from 1 July 2017.[2]

3. This Guidance Statement includes references to prudential reporting requirements for ADIs and ADI Groups, and their appointed auditors, as specified by APRA. 'Level 1', 'Level 2' and 'Level 3', as applied in this Guidance Statement, have the meaning given in APRA Prudential Standards APS 001 *Definitions* (APS 001) and 3PS 001 *Definitions* (3PS 001).

   (a) In applying this Guidance Statement on a group basis, references to an ADI should be read as also referring to the head of a Level 2 or Level 3 group, as relevant. Where a Level 2 group operates within a Level 3 group, the head of the group is to be read as the head of the Level 3 group.

   (b) The term 'ADI group' in this Guidance Statement will mean a Level 2 or a Level 3 group, as relevant, and will be used where requirements and guidance are common for Level 2 and Level 3 groups.

Registered Financial Corporations[3]

4. This Guidance Statement provides guidance that may be considered and adapted as necessary in the circumstances, to assurance engagements undertaken pursuant to APRA Reporting Standard RRS 710.0 *ABS/RBA Audit Requirements for Registered Financial Corporations – EFS collection* (RRS 710.0), which applies to those Registered Financial Corporations (RFCs) required to report to APRA under the Economic and Financial Statistics (EFS) collection[4], from 1 July 2019.

5. APRA collects statistical data from RFCs under the *Financial Sector (Collection of Data) Act 2001* (FSCODA). RFCs are required to provide a prudential supervision warning to investors to the effect that the RFC is not prudentially regulated or supervised by APRA under the *Banking Act 1959* (Banking Act)[5] and that an investor will not have the right to priority of

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[1] 'ADI', 'appointed auditor', 'Level 1, 'Level 2' and 'Level 3'are defined by APRA in Prudential Standard APS 001 *Definitions*.

[2] 'Level 3 Head' and 'Level 3 Group' ('conglomerate group') are defined by APRA in Prudential Standards APS 001 and 3PS 001 *Definitions*. Refer to Attachment A to APS 001 for further explanation of the definition of Level 3 'conglomerate group' as it applies to ADIs.

[3] Corporations required to be registered under Part 2 of the *Financial Sector (Collection of Data) Act 2001* (FSCODA). Registered Financial Corporations (RFCs) are not prudentially regulated entities under the *Banking Act 1959* (Banking Act). APRA collects statistical data from RFCs under EFS Reporting Standards made under the FSCODA which is primarily used by the Australian Bureau of Statistics (ABS) and Reserve Bank of Australia (RBA) for analysis, publication and policy-making purposes, although this data may also be used by APRA to promote financial system stability in Australia.

[4] Not all RFCs are required to submit EFS data to APRA. EFS reporting requirements will depend on the size of the RFC and is specified by APRA in relevant EFS Reporting Standards.

[5] An investor will not have the right to priority of repayment that is conferred on depositors by section 13A of the Banking Act. Also, RFC products are not covered by the Financial Claims Scheme, which applies only to deposits held in protected accounts of ADIs.

repayment that is conferred on depositors by section 13A of the Banking Act. APRA Prudential Standards are therefore not applicable to RFCs.

Issuance Date

6. This Guidance Statement is issued on <<April 2020>> by the AUASB and replaces GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions*, issued in June 2009.

Introduction

Prudential Supervision of ADIs

7. Under the Banking Act, APRA is responsible for the prudential supervision and monitoring of prudential matters relating to ADIs, authorised non-operating holding companies (authorised NOHCs)[6], and groups of bodies corporate which are their subsidiaries, in order to protect the interests of depositors of the ADIs and to promote financial system stability in Australia.

8. APRA formulates, promulgates and enforces prudential policy and practice through APRA Prudential Standards (APSs), which have the force of law. APRA may also issue non-enforceable Prudential Practice Guides (APGs) and other guidelines, to assist ADIs in complying with the requirements in its Prudential Standards and, more generally, to outline prudent practices in relation to certain elements of an ADI's operations.[7]

9. Prudentially regulated institutions, which includes ADIs, are required, under the FSCODA and Reporting Standards made under the FSCODA, to submit data to APRA as defined in APRA Reporting Forms and accompanying instructions. Some Reporting Forms are subject to assurance requirements[8].

10. The appointed auditor of an ADI and/or an ADI Group has an important role to play in the prudential supervision process. Requirements for appointed auditors of ADIs and/or ADI Groups to provide assurance reports on prudential matters to APRA are intended to assist APRA in assessing the reliability of information supplied to it by an ADI and/or an ADI Group.

Economic and Financial Statistics (EFS) Collection

11. APRA also collects EFS data on behalf of the Australian Bureau of Statistics (ABS) and the Reserve Bank of Australia (RBA) (together, referred to as 'the Agencies'), from both ADIs and certain non-regulated corporations[9] required to be registered under the FSCODA[10].

12. EFS data is used by the Agencies for various purposes, including analysis, policy making, to compile key macroeconomic indicators for Australia and as input to the national accounts to meet Australia's international reporting obligations. This data may also be used by APRA for prudential and publication purposes.

13. The FSCODA defines which categories of entities are registrable and also facilitates the collection of EFS data. Under the FSCODA, certain non-ADI lenders whose business activities in Australia includes the 'provision of finance'[11], or have been identified either

[6] 'Authorised non-operating holding company' is defined by APRA in APS 001.
[7] Access to APRA Prudential Standards, Prudential Practice Guides and legislation relevant to ADIs is available on APRA's website (www.apra.gov.au).
[8] Refer to APS 310 and Attachment A to APS 310.
[9] For example, certain automotive financiers, mortgage securitisers, asset financing companies and pawnbrokers.
[10] Refer to Section 7 of the FSCODA for categories of corporations subject to registration under the Act.
[11] Refer to Section 32 of the FSCODA for explanation of the expression 'provision of finance'.

individually or as a class of corporation specified by APRA, are required to be registered with APRA and to comply with requirements to submit EFS data to APRA.

14. RFCs are not prudentially regulated entities under the Banking Act. APRA collects statistical data from RFCs under the FSCODA. EFS reporting requirements will depend on the size of an ADI or RFC. Based on thresholds included in APRA's individual EFS Reporting Standards, larger ADIs and RFCs are required to report more detailed information, while smaller entities report less detailed information or do not report at all.

15. RRS 710.0 implements an assurance framework similar to that of APS 310/3PS 310 to RFCs.[12]

Scope of APS 310 and 3PS 310 Prudential Reporting Engagements

16. APS 310 and 3PS 310 prudential reporting requirements, imposed on the appointed auditor via the terms of engagement with an ADI, are in addition to the audit [and review] of financial reports required under the *Corporations Act 2001* (Corporations Act) (where required).

17. The statutory financial report audit [and review] is directed towards obtaining sufficient appropriate evidence to form an opinion or conclusion, as applicable, on whether the financial report is presented fairly in accordance with the required financial reporting framework. The financial report audit [and review] is not designed to enable the appointed auditor to conclude in relation to the matters specified in APS 310 and 3PS 310.

18. APS 310 and 3PS 310 provide for two types of prudential reporting engagements to be conducted by the appointed auditor of an ADI, namely:

    (a) annual prudential reporting engagements (routine reporting) (see paragraphs 51-56); and

    (b) special purpose engagements (see paragraphs 302-312)

19. APRA Prudential Standards may include further requirements for 'independent'[13] assurance engagements to be undertaken in relation to specific aspects of an ADI and/or ADI Group's operations, prudential reporting, risk management systems or financial position.[14] The appointed auditor of an ADI may be engaged to undertake engagements of this type.

    These types of assurance engagements are additional, and separate, to the APS 310 and 3PS 310 annual prudential reporting requirements, and fall outside the scope of this Guidance Statement.

Responsibilities of the Appointed Auditor

20. The responsibilities of the appointed auditor of an ADI and/or ADI Group are contained in:

    (a) applicable AUASB Standards;

    (b) APS 310 and 3PS 310;

    (c) other applicable APRA Prudential Requirements, including the Banking Act, the FSCODA, and APRA Prudential and Reporting Standards; and

12 Refer to RRS 710.0 for role, responsibilities and reporting requirements applicable to appointed auditors of RFCs.
13 To be undertaken by a party or parties who are independent within the meaning of the relevant APRA Prudential Standards. Refer to CPS 510 *Governance* (CPS 510).
14 For example, the periodic comprehensive review of an APRA regulated institution's Risk Management Framework under CPS 220 *Risk Management*. Also refer to paragraph 223 of this Guidance Statement.

(d) relevant ethical and professional standards.[15]

21. This Guidance Statement is to be read in conjunction with, and is not a substitute for referring to, the requirements and application and other explanatory material contained in the following AUASB Standards that may be applicable to the annual prudential assurance engagement:

(a) Applicable Auditing Standards (ASAs) - where reasonable assurance on historical financial information is required.

(b) Standard on Review Engagements (ASRE) ASRE 2405 *Review of Historical Financial Information Other than a Financial Report* (ASRE 2405) – where assurance is required regarding historical financial information other than a financial report.

(c) Standard on Assurance Engagements (ASAE) ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (ASAE 3000) – where limited assurance is required regarding subject matters other than historical financial information.

(d) ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information* (ASAE 3450) - where limited assurance is required in relation to prospective financial information such as forecasts or projections.[16]

(e) ASAE 3150 *Assurance Engagements on Controls* (ASAE 3150) – where limited assurance is required in relation to internal controls.

For an outline of the relevant AUASB Standards applicable to each part of the prudential assurance engagement, refer to Appendix 1 of this Guidance Statement.

22. ASAE 3000 has been written for general application to assurance engagements other than audits or reviews of historical financial information covered by ASAs or ASREs. Where topic specific ASAEs exist, the appointed auditor applies the relevant topic-specific ASAEs, as well as ASAE 3000.

23. APRA places reliance on accounting and auditing standards to the extent that they do not conflict with Prudential Requirements applicable to the ADI. APS 310 and 3PS 310 requires appointed auditors, in meeting their role and responsibilities, to comply with the Auditing Standards and Guidance Statements issued by the AUASB, except where:

(a) requirements are inconsistent, in which case the requirements of APS 310 and 3PS 310 will prevail; or

(b) APRA otherwise specifies, in writing, to the ADI that alternative standards and guidance are to be used by the appointed auditor.

24. It is important that the appointed auditor of an ADI recognises the additional responsibilities under sections 16B, 16BA and 16C of the Banking Act, imposed on any auditor of an ADI, authorised NOHC, or their subsidiaries, to provide information to APRA upon request, or where the auditor possesses reportable information specified in that Act, or where the auditor considers that the provision of information would assist APRA in performing its functions under the Banking Act or the FSCODA.[17]

25. Under section 70B of the Banking Act, Banking Act provisions will take precedence over any conflicting Corporations Act provisions. Therefore, any provisions made under the Banking

15 See ASA 102 Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements.

16 For example, refer to APRA ADI Reporting Forms 210.1A and 210.1B *Liquidity Coverage Ratio*, listed in APRA Prudential Standard APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance.*

17 See paragraphs 313-327 of this Guidance Statement

Act governing auditor reporting to APRA will override any conflicting Corporations Act provisions which may apply to such reporting.

26. The use by ADIs and APRA of prudential assurance engagement reports prepared by appointed auditors need to be evaluated in the context of the inherent limitations of an assurance engagement and the subject matter of the engagement.[18]

27. Both APS 310 and 3PS 310 warn that all persons involved in the provision of information (which includes the appointed auditor) are to note that it is an offence under subsections 137.1 and 137.2 of the *Criminal Code Act 1995* to provide, whether directly or indirectly, false and misleading information to a Commonwealth entity, such as APRA.

Implementation of Basel III Capital Reforms in Australia

28. To ensure Australian banks and other ADI's are well capitalised to withstand risks they may face, APRA specifies the minimum amount of capital that an ADI should hold, as well as the form it should take. The capital framework that APRA applies to ADIs in Australia are largely based on the international framework for banks developed by the Basel Committee on Banking Supervision (Basel Committee).[19]

29. Since GS 012 was reissued in 2009, the Basel Committee has finalised its Basel III capital framework reforms, designed to strengthen bank capital rules following the global financial crisis in 2008-09. The Basel III capital reforms significantly build on the Basel II risk-sensitive capital framework. The new framework requires a substantial increase in minimum capital requirements and strengthening of the quality of capital, as well as a requirement that banks hold higher levels of liquid assets and maintain more stable funding profiles by addressing variability in risk-weighted assets.

30. The Basel Committee has agreed to an implementation timetable commencing in 2022 for the final Basel III reforms. APRA has started implementing Basel III capital reforms in Australia since 1 January 2013 with the release of updated prudential and reporting standards.

Definitions

31. For the purpose of this Guidance Statement, the following terms have the meanings attributed below:

    (a) 'Authorised Deposit-taking Institution' (ADI) is defined in APS 001, to mean a body corporate authorised under section 9 of the Banking Act, to carry on banking business in Australia.[20]

    Reference in this Guidance Statement to an 'ADI' will be taken, unless otherwise indicated, to include:

    (i) a 'locally incorporated ADI';

    (ii) a 'foreign ADI'[21]; and

[18] See paragraph 273-278 of this Guidance Statement.

[19] APRA's approach to the assessment of an ADI's capital adequacy is based on the risk-based capital adequacy framework set out in the Basel Committee on Banking Supervision's publications, *International Convergence of Capital Measurement and Capital Standards: A Revised Framework* (Basel II), revised in June 2006 and *A Global Regulatory Framework for more Resilient Banks and Banking Systems* (Basel III), released in December 2010 and revised in June 2011. Background information on the Basel III Capital Framework, and its implementation in Australia, is available on APRA's website at www.apra.gov.au.

[20] ADI's may include, but are not limited: Australian owned banks, foreign subsidiary banks, branches of foreign banks, building societies, credit unions, providers of purchased payment facilities and specialist credit card institutions.

[21] Reference to the foreign ADI's Australian operations as if it was a stand-alone ADI.

(iii) an 'extended licenced entity'.[22]

(b) 'Appointed auditor' means an independent auditor appointed by:

(i) an ADI as an auditor for the purposes of APS 310 and APS 910.

(ii) a Level 3 Head as group auditor for the purposes of 3PS 310.

APS 310 and APS 910 allows for the appointed auditor to be the same auditor who audits an ADI for the purposes of the Corporations Act. Similarly, 3PS 310 allows for the Level 3 group auditor to be the same auditor who audits a Level 3 Head for the purposes of the Corporations Act.

Under APS 310 and 3PS 310 separate auditors may be appointed to meet the APS 310 and 3PS 310 reporting requirements on a Level 1, Level 2 and Level 3 basis, and to undertake the different types of engagements provided for in these standards. APRA may also require that an ADI appoint another auditor, in addition to any auditor already appointed by the ADI, for the purposes of APS 310 and 3PS 310.

Therefore, it is possible for an ADI and ADI Group to have more than one appointed auditor at any time, and for an APS 310/3PS 310 appointed auditor to be different from the auditor responsible for undertaking the financial report audit [and review] under the Corporations Act.

Where the Banking Act refers to 'the auditor' of an ADI, this can be an auditor appointed for the purposes of APS 310 and/or 3PS 310, or another auditor, such as the auditor responsible for the audit [and review] of financial reports required under the Corporations Act.

Refer to APS 310 and 3PS 310 for further information on the use of group auditors, where the ADI is a member of a group.

(c) 'Accounting records' is defined in the AUASB Glossary as including "the records of initial accounting entries and supporting records, such as cheques and records of electronic fund transfers, invoices, contracts, the general and subsidiary ledgers, journal entries and other adjustments to the financial report that are not reflected in journal entries, and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures."

For guidance on the application of the definition of 'accounting records' to the assurance engagement, refer to paragraphs 163-171.

(d) 'Advanced ADI', means an ADI that has APRA's approval to use an internal ratings-based approach to credit risk and/or an advanced measurement approach to operational risk, available under APRA Prudential Standards, for capital adequacy purposes.[23]

ADIs choosing to adopt the advanced measurement approaches for the purpose of determining the ADI's regulatory capital, require prior approval from APRA (APRA accreditation). Under the advanced approaches for measuring capital adequacy, an ADI is permitted to use its own quantitative risk estimates in calculating regulatory capital. This involves a greater use of internal modelling and other forms of statistical analysis, as well as qualitative assessment.

[22] 'locally incorporated ADI', 'foreign ADI' and 'extended licenced entity' are defined in APS 001.

[23] For example, refer to APRA Prudential Standards APS 110 Capital Adequacy, APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk and APS 115 Capital Adequacy: Advanced Measurement Approaches to Operational Risk.

(e) 'Authorised non-operating holding company' (authorised NOHC) is defined in APS 001 to have the same meaning as under section 5 of the Banking Act.

(f) 'ADI Reporting Form' (or Data Collection Form), means a form used for the collection and reporting of information in relation to an ADI, as required to be provided to APRA by an ADI in accordance with APRA Reporting Standards made under the FSCODA.

(g) 'Economic and Financial Statistics (EFS) Collection' is defined in APRA Reporting Standard ARS 701.0 *ABS/RBA Definitions for the EFS Collection*, and comprises the EFS Reporting Standards and data collected under the EFS Reporting Standards.

(h) 'Foreign ADI' is defined in APS 001 to have the same meaning as under section 5 of the Banking Act. The terms 'branch of a foreign bank' and 'branch of a foreign ADI' are also used in APRA Reporting Standards and Reporting Forms when referring to a 'foreign ADI'.

Reference to a foreign ADI does not capture locally incorporated ADI subsidiaries of foreign banks, that is, a 'foreign-owned ADI'.[24]

(i) 'Group' is defined in APS 001 as reference to a corporate group that comprises of more than one company that are related bodies corporate within the meaning of section 50 of the Corporations Act. 'Level 2' and 'Level 3' groups are defined in APS 001 and 3PS 001 (see definitions below).

(j) 'Head of the group', means the head or parent entity of a Level 2 or Level 3 group, as relevant. Where a Level 2 group operates within a Level 3 group, a requirement expressed as applying to the head of the group, is to be read as applying to the 'Level 3 Head'.

(k) 'Level 1' ADI - the ADI itself.[25]

(l) 'Level 2' ADI group means the entities that comprise 'Level 2', as defined in APS 001, that is, either:

(i) where there is no authorised NOHC and the ADI has controlled entities, the consolidation of the ADI and its controlled entities; or

(ii) where there is an authorised NOHC, the consolidation of the authorised NOHC and its controlled entities; or

(iii) where there is no authorised NOHC and the ADI does not have controlled entities, the consolidation of the ADI and any entity that APRA determines, in writing, that is to be consolidated.

(m) 'Level 3' group as defined in APS 001 and 3PS 001 means the conglomerate group at the widest level and include all institutions determined by APRA to be members of a Level 3 group.

APRA may determine a Level 3 group where it considers that material activities are performed within the group across more than one prudentially regulated industry and/or in one or more non-prudentially regulated industries, to ensure that the ability of the group's prudentially regulated institutions to meet their obligations to depositors, policy holders or Registrable Superannuation Entity beneficiaries is not

[24] APS 001 defines a 'foreign-owned ADI' to mean an ADI in relation to which an approval has been given, under section 14 of the *Financial Sector (shareholdings) Act 1998*, for a bank that is not locally incorporated to hold a stake of more than 15 per cent in the ADI.

[25] 'ADI' is defined in paragraph 31(a) above.

adversely impacted by risks emanating from the group, including its non-prudentially regulated institutions.

Generally, a conglomerate group will be headed by an ADI or an authorised NOHC and may include financial (APRA regulated[26] and unregulated) as well as non-financial (commercial) entities.

Attachment A to APS 001 provides further information to inform the auditor's understanding of what constitutes a conglomerate group for the purposes of reporting pursuant to APS 310 and 3PS 310.

(n) 'Level 3 Head' is defined in 3PS 001 to mean:

(i) an ADI or authorised NOHC under the Banking Act;

(ii) a general insurer or authorised NOHC under the Insurance Act;

(iii) a life company or registered NOHC under the Life Insurance Act; or

(iv) determined by APRA to be the Level 3 Head of a Level 3 Group.

(o) 'Limited assurance', is defined in APS 001, in accordance with the AUASB's *Framework for Assurance Engagements*.

(p) 'Prudential Requirements'[27], is defined in APS 001 and includes requirements imposed by:

(i) the Banking Act;

(ii) Regulations (made under the Banking Act);

(iii) APRA Prudential Standards (made under the Banking Act);

(iv) the FSCODA;

(v) APRA Reporting Standards (made under the FSCODA);

(vi) APRA conditions on the ADI's authorisation; and

(vii) any other requirements imposed by APRA, in writing, in relation to an ADI.

(q) 'Reasonable assurance', is defined in APS 001, in accordance with the AUASB's *Framework for Assurance Engagements*.

(r) 'Routine reporting', refers to the appointed auditor's responsibility under APS 310, 3PS 310 and APS 910 to report to APRA and the ADI and/or Level 3 Head, on an annual basis, in relation to the matters identified in paragraphs 51-59 of this Guidance Statement.

(s) 'Specified ADI Reporting Forms', means APRA ADI Reporting Forms listed in APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance*.[28]

[26] Entity directly regulated by APRA or by an equivalent regulator overseas.
[27] These requirements may differ between locally incorporated and foreign ADIs.
[28] The requirements are different for Standardised, Advanced and Foreign ADIs.

(t) 'Standardised ADI', means an ADI that uses the standardised measurement approaches, available under APRA Prudential Standards, for capital adequacy purposes in respect of the whole of its operations. See also paragraph 31(d) above.

Tripartite Relationship

32. Under normal circumstances, APRA does not consult directly with the appointed auditor of an ADI or ADI group on matters concerning an individual ADI and/or ADI group. APRA liaison with an appointed auditor is conducted normally under tripartite arrangements involving APRA, the ADI and/or head of the group, and its appointed auditor(s). Any one of these parties may initiate meetings or discussions at any time, when considered necessary. [29]

33. In the normal course, regular tripartite meetings are held to discuss the appointed auditor's annual prudential assurance report(s), prepared pursuant to APS 310 and/or 3PS 310.

34. Notwithstanding the tripartite relationship, APRA and the appointed auditor may meet, at any time, on a bilateral basis at the request of either party. APRA may communicate with an auditor of an ADI and/or ADI group on a bilateral basis to obtain or discuss information for whatever reason(s) it considers appropriate

35. Under APRA's Prudential Standard CPS 510 *Governance* (CPS 510), an APRA-regulated entity is required to ensure that its internal policy and contractual arrangements do not explicitly or implicitly restrict or discourage auditors or other parties from communicating with APRA.

Responsibilities of the ADI

Governance

36. CPS 510 sets out the minimum requirements that any APRA-regulated institution and the head[30] of a group must meet in order to promote strong and effective governance.

37. Under CPS 510, ultimate responsibility for oversight of the sound and prudent management of an APRA-regulated institution lies with its board of directors (Board), or equivalent.[31]. For an ADI Group, this responsibility will rest with the Board (or equivalent) of the head of the group.

Risk Management

38. In accordance with APRA's Prudential Standard CPS 220 *Risk Management*, it is the responsibility of the Board and management of an ADI and head of an ADI Group to ensure that the ADI and/or ADI Group meet prudential and statutory requirements and has management practices to limit risks to prudent levels.

39. CPS 220 requires an ADI and the head of an ADI group to maintain a Risk Management Framework (RMF) appropriate to the size, business mix and complexity of the ADI or ADI group, as relevant, to ensure the ADI and the ADI group manage risks arising from its business and continue to meet its obligations to depositors. The Board of an ADI is ultimately responsible for the ADI's RMF and for oversight of its operation by management, in accordance with the requirements of CPS 220.

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[29] See APS 310 and 3PS 310.

[30] CPS 510 clarifies that, where a Level 2 group operates within a Level 3 group, a requirement expressed as applying to a head of a group is to be read as applying to the Level 3 Head

[31] For example, for a foreign ADI, it will refer to a senior officer outside Australia to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian operations.

Refer to CPS 220 for further information on the key elements to be included in an ADI's and/or ADI group's RMF, including requirements regarding the use of group risk management where an ADI is part of an ADI group.

40. An ADI or head of an ADI group is required to submit to APRA an annual Risk Management Declaration in accordance with requirements set out in CPS 220 and Attachment A to CPS 220.

41. CPS 220 requires an ADI and/or head of an ADI group to notify APRA when it becomes aware of a significant breach of, or material deviation from its RMF, or that the RMF does not adequately address a material risk, as well as any material or prospective material changes to the size, business mix and complexity of its operations.

Responsibility to Appoint Independent Auditor pursuant to APS 310/3PS 310

42. Under APS 310 and 3PS 310 an ADI and/or head of an ADI group is required to appoint, as appropriate, an auditor(s) and/or group auditor(s) for the purposes of these Prudential Standards. APS 310 applies to all ADIs on a Level 1 basis and a group of which an ADI is a member on a Level 2 basis. 3PS 310 applies to each Level 3 Head.

43. APS 310 and 3PS 310 require an ADI and/or head of an ADI group to:

(a) ensure its auditor satisfies the requirements of APS 310 and/or 3PS 310;[32]

(b) set out the terms of the engagement, including matters identified in APS 310 and/or 3PS 310, in a legally binding contract with its appointed auditor and to ensure the auditor complies with these terms; and

(c) ensure its auditor undertakes the roles and responsibilities as specified in APS 310 and 3PS 310, as relevant.

Financial Claims Scheme

44. The Financial Claims Scheme (FCS) for ADIs was put in place to protect the account-holders of locally incorporated ADIs from loss on their deposits, and to provide them with timely access to those deposits, in the event an ADI becoming insolvent, up to a maximum amount guaranteed by the Australian Government. APRA is responsible for the administration of the FCS and for making payments to account-holders.

45. APRA has issued Prudential Standard APS 910 *Financial Claims Scheme* (APS 910) to assist ADIs to comply with the requirements of the FCS and applies to all ADIs except for foreign ADIs, specialist credit card institutions and providers of purchased payment facilities.

46. Under APS 910, ADIs are required to implement systems for the identification of protected accounts for each account-holder, to the extent practicable, and present an aggregated view, or 'single customer view' of each account-holder and meet payment, reporting, communications, testing and assurance requirements, which will enable APRA to pay out account-holders of the ADI in a timely and effective manner, in the event of an ADI being declared subject to the FCS.

47. Under APS 910 the Board and senior management of an ADI and ADI group are required to ensure that appropriate policies and procedures are in place to ensure the integrity of the operations, internal controls and information required under APS 910.[33] This includes, but is not limited to:

[32] See paragraph 50 of this Guidance Statement.
[33] Refer to Prudential Standard APS 910 *Financial Claims Scheme* for all APRA's requirements in this regard. Further information on the Financial Claims Scheme, and its implementation in Australia, is available on APRA's website at www.apra.gov.au.

(a) ensuring that the systems and data required by APS 910 are subjected to an independent limited assurance engagement, in accordance with the requirements stipulated in APS 910, and that this assurance be provided at the same time as the assurance required by APS 310, unless otherwise agreed by APRA; and

(b) providing an attestation from the Chief Executive Officer in accordance with the requirements stipulated in APS 910.

Responsibility to keep Auditor Informed

48. The ADI and/or head of the ADI group is required to ensure that its appointed auditor(s) is kept fully informed, including ensuring that the auditor:

- has access to all data, information, reports and staff of the ADI and/or ADI group, which the appointed auditor reasonably believes is necessary to fulfil its role and responsibilities under APS 310 and/or 3PS 310. This includes, access to the Board and Board Committees of the ADI and head of the ADI group, internal auditors of the ADI and/or the ADI group, and auditors of entities in the group, as required;
- is kept fully informed of all Prudential Requirements applicable to the ADI and/or head of the ADI group; and
- is provided with any other information that APRA has provided to the ADI and/or head of the ADI group that may assist the appointed auditor in fulfilling its role and responsibilities under APS 310 and/or 3PS 310.

49. In relation to the ADI's or ADI group's responsibility to keep the auditor informed, the auditor requests management of the ADI and/or ADI group to sign an appropriate representation letter(s).[34]

Role and Responsibilities of the Appointed Auditor

Those Who May Conduct the Assurance Engagement

50. APS 310 and 3PS 310 require an ADI and/or the head of the ADI group, as applicable, to ensure its auditor:

(a) satisfies the fitness and propriety requirements set out in Prudential Standard CPS 520 *Fit and Proper*;

(b) satisfies the auditor independence requirements in CPS 510 ; and

(c) is not subject to a direction issued under the Banking Act.

As such, the auditor will need to provide information to the entity to enable the ADI and/or head of the ADI group to comply with requirements.

Annual Prudential Reporting Requirements

Prudential Standards APS 310 and 3PS 310[35]

51. Under APS 310 and 3PS 310, the appointed auditor of an ADI and/or group auditor of an ADI group is required to report simultaneously to APRA and the Board (or Board Audit

[34] See paragraph 279-281 of this Guidance Statement.
[35] Refer to APS 310 and 3PS 310 for all requirements.

Committee)[36] of the ADI and/or head of the ADI group, as appropriate, within three[37] months of the end of the financial year, in relation to the following matters[38]:

(a) *Assurance on Specified[39] ADI Reporting Forms at the financial year-end*:

(i) Reporting Forms with Data Sourced from Accounting Records

The appointed auditor is required to provide reasonable assurance that the information included in the Specified ADI Reporting Forms at the financial year-end, sourced from the ADI's accounting records, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(ii) Reporting Forms with Data Sourced from Non-Accounting Records

Unless otherwise indicated, in writing, by APRA, the appointed auditor is required to provide limited assurance that the information, included in the Specified ADI Reporting Forms at the financial year-end, sourced from non-accounting records, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(iii) Reporting Forms with Data Sourced from a Combination of Accounting and Non-Accounting Records

Unless otherwise indicated, in writing, by APRA, the appointed auditor is required to provide reasonable assurance on information sourced from accounting records, and limited assurance that information sourced from non-accounting records, at the financial year-end, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

(b) Limited Assurance on Internal Controls addressing Compliance with Prudential Requirements and the Reliability of Data included in ADI Reporting Forms

The appointed auditor is required to provide limited assurance that, in all material respects:

(i) the ADI and/or head of ADI group has implemented internal controls that are designed to ensure the ADI and/or head of the ADI group, as relevant, has:

a. complied with all applicable Prudential Requirements; and

b. provided reliable data to APRA in the Reporting Forms prepared under the FSCODA; and

(ii) the controls in paragraph (b)(i) have operated effectively throughout the financial year.

(c) Limited Assurance on Compliance with Prudential Requirements

The appointed auditor is required to provide limited assurance, based on the appointed auditor's work under (a) and (b) above, that the ADI and/or the head of the ADI

36 Or, for a foreign ADI, a senior officer outside Australia to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian operations.
37 For a non-disclosing ADI, the relevant period is four months.
38 Subject to paragraph 54 of this Guidance Statement.
39 For a listing of APRA Reporting Forms to be subjected to the assurance engagement, refer to APRA Prudential Standard APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance*. The requirements are different for Standardised, Advanced and Foreign ADIs.

group, as relevant, has complied, in all material respects, with all relevant Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards, during the financial year.[40]

52. 3PS 310 requires that reports, assessments and other material required under this standard must make it clear where the auditor is referring to matters relating to the Level 3 Head or the Level 3 group.

53. Under APS 310 and 3PS 310, it is the responsibility of the appointed auditor, as provided for in the required terms of engagement, to submit directly to APRA:

    (a) all reports required to be produced under APS 310 and 3PS 310; and

    (b) all assessments and other material associated with these reports, if requested by APRA.

54. Ordinarily, matters reported to APRA under paragraph 53 are also reported to the ADI and/or head of the ADI group to which the matter relates. However, APS 310 and 3PS 310 specifically prohibit the appointed auditor from notifying the ADI and/or head of the ADI group of, or from providing the ADI and/or head of the ADI group with, the documents referred to in paragraph 53, where:

    (a) the appointed auditor considers that by doing so the interests of depositors of the ADI or ADIs within the group would be jeopardised; or

    (b) there is a situation of mistrust between the appointed auditor and the Board of the ADI and/or head of the ADI group, or senior management of the ADI or ADI group.

55. In accordance with APS 310 and 3PS 310, an appointed auditor, whether as part of routine or special purpose engagements, must not place sole reliance on the work performed by APRA.

56. The appointed auditor of an ADI is required to attend all meetings with APRA related to APS 310 and 3PS 310, whether on a bilateral, tripartite or other basis, unless APRA indicates otherwise in writing.

Prudential Standard APS 910 ***Financial Claims Scheme***

57. APS 910 requires the auditor, in accordance with APS 310, to provide limited assurance that, in all material respects:

    (a) the ADI and/or the ADI group has implemented internal controls that are designed to ensure:

        (i) compliance with all applicable Prudential Requirements relating to APS 910; and

        (ii) that Single Customer View (SCV) data as set out in APS 910 Attachment A, to the extent practicable, and FCS payment instruction and reporting information can be relied upon as being complete and accurate and in accordance with APS 910; and

    (b) the controls in (a) have operated effectively when tested.

58. APRA requires the timing of the APS 910 assurance engagement to be aligned with the annual APS 310 assurance engagement. A separate auditor assurance report for the APS 910

[40] Refer also to section 16BA of the Banking Act which requires the auditor to immediately notify APRA of certain matters, and to notify APRA as soon as is practicable about certain other matters. See paragraphs 313-327 of this Guidance Statement.

engagement may be completed but the requirement is that this report be submitted to APRA at the same time as the APS 310 prudential assurance report.

59. In circumstances where the APS 310/3PS 310 appointed auditor is not in a position to undertake the APS 910 engagement, a different auditor from the same or a different audit firm will be able to carry out the APS 910 engagement in accordance with the requirements of applicable AUASB Standards.

Agreeing the Terms of the Annual Prudential Reporting Engagement

60. The requirement to report pursuant to APRA's annual prudential reporting requirements, is in addition to the audit [and review] of financial reports required under the Corporations Act, and is to be treated by the appointed auditor as a separate audit engagement.

61. The appointed auditor accepts the prudential reporting engagement only when satisfied that relevant ethical requirements relating to the assurance engagement have been met. The concept of independence is important to the appointed auditor's compliance with the fundamental ethical principles of integrity and objectivity and the auditor is required to meet the independence requirements stipulated under both CPS 510 and ASA 102[41].

62. The appointed auditor and the ADI and/or head of the ADI group, as applicable, agree on the terms of the engagement for each discrete part of the assurance engagement, in accordance with the requirements contained in ASA 210[42], ASAE 3000, ASAE 3150, ASAE 3450 and ASRE 2405. These arrangements have to be legally binding and include the required terms of engagement specified in APS 310.

63. An engagement letter[43] confirms both the client's and the appointed auditor's understanding of the terms of the engagement, helping to avoid misunderstanding, and the appointed auditor's acceptance of the appointment. Both parties sign the engagement letter to acknowledge that it is a legally binding contract.

64. The auditor may also use the engagement letter to clarify the respective roles of the ADI and/or the head of the ADI group, as appropriate, and the auditor. In particular, it is important to highlight in the engagement letter the entity's responsibility to establish and maintain effective internal control to ensure compliance with Prudential Requirements and to ensure the reliability of data included in ADI Reporting Forms. As part of the acceptance of the prudential assurance engagement, the auditor may consider obtaining acknowledgement of this obligation from those charged with governance of the ADI when obtaining agreement on the terms of the engagement.

65. For recurring engagements, the appointed auditor considers whether circumstances require the terms of the engagement to be revised and whether there is a need to re-confirm in writing the existing terms of the engagement. While the appointed auditor may decide not to re-confirm the terms of engagement each year, factors that may make it appropriate to do so include a recent change of senior management or those charged with governance, or any indication that the entity misunderstands the objectives and scope of the prudential reporting engagements.

66. The engagement letter explains that any special purpose engagement of any aspect of the ADI's business operations, prudential reporting, risk management systems or financial position, will constitute a separate engagement(s) and that the details of such engagement(s) will be the subject of a separate engagement letter(s).[44]

[41] ASA 102 Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements.
[42] ASA 210 Agreeing the Terms of Audit Engagements.
[43] Or other suitable form of written agreement.
[44] See paragraphs 302-312 of this Guidance Statement.

67. The engagement letter furthermore clarifies that, in accordance with CPS 510, the appointed auditor is not to be a party to any contractual arrangements, or any understandings with an ADI, that seeks in any way to limit the auditor's ability or willingness to communicate to APRA. APRA may liaise bilaterally with an appointed auditor and may, although not usually, request information directly from the appointed auditor. The appointed auditor notifies APRA of any attempts by an ADI to achieve such arrangements or understandings.

68. APS 910 identifies additional requirements for ADIs and their appointed auditors, including a requirement for auditors to perform a limited assurance engagement on the ADIs control procedures in relation to the SCV data and FCS payment and reporting information. These requirements are in addition to the APS 310/3PS 310 requirement for auditors to perform a limited assurance engagement on controls implemented by the ADI to ensure compliance with *all* prudential requirements (which includes compliance with APS 910). The auditor may use the engagement letter to clarify the respective roles of the ADI and the appointed auditor. In particular, it is important to highlight the entity's responsibility for ensuring the integrity of the operations, internal controls and information required under APS 910.

69. An example engagement letter to accommodate APRA reporting requirements pursuant to APS 310, 3PS 310 and APS 910, is included in Appendix 2 of this Guidance Statement.

Matters to Consider in Planning the Annual Prudential Reporting Engagement

70. The auditor plans the engagement in accordance with the requirements of, and has regard to, guidance provided in AUASB standards ASA 315[45], ASAE 3000, ASAE 3150, ASAE 3450 and ASRE 2405, as applicable. The auditor performs preliminary engagement activities to establish and document the overall assurance engagement strategy that sets the scope, timing and direction of the engagement, and guides the development of the engagement.

71. The appointed auditor obtains an understanding of the entity and its environment, including its internal control and compliance framework, and other assurance engagement circumstances, sufficient to:

    (a) identify and assess the risks of:

        (i) material misstatements in subject matter information;

        (ii) material deficiencies or deviations in internal controls (in relation to the area of activity to be examined); and

        (iii) non-compliance with applicable Prudential Requirements; and

    (b) design and perform further evidence-gathering procedures.

Understanding the Entity and its Environment

72. In gaining an understanding of the entity and its environment, the appointed auditor can draw on knowledge gained as part of the annual financial statement audit under the Corporations Act. However, this understanding needs to be updated and broadened to address the subject matters included in the scope of the prudential reporting assurance engagement, such as the controls in place to ensure compliance with all applicable prudential standards which are not otherwise considered as part of the annual financial statements audit.

73. The relevant AUASB standards provide examples of matters that may be considered, and procedures that may be performed, by the auditor in gaining this understanding. The auditor

[45] See ASA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment.

exercises professional judgement to determine the nature and extent of the understanding that is required.

74. When performing procedures to obtain an understanding of the entity and its environment, consideration of the following matters may be helpful:

- the size, business mix and complexity of the ADI or the ADI group it heads.
- changes in the market environment.
- whether the ADI is an Advanced or Standardised ADI.
- whether the ADI is a foreign ADI.
- governance and management functions within the ADI, including the respective roles and responsibilities attributed to the finance, risk management, compliance and internal audit functions.
- the risk culture.
- the reliability of reporting systems.
- the significance and complexity of the information technology environment and systems.
- the adequacy of systems and controls to identify, assess, manage, mitigate and monitor material risks.
- the compliance framework, processes and controls.
- history of non-compliance.
- any (formal) communications between APRA and the ADI and/or the head of the ADI group, and the results of any supervisory visits conducted by APRA in relation to the engagement.
- recent reports prepared by other auditors appointed to report on any aspect of the ADI and/or the ADI group.
- the estimation and uncertainty inherent in applied measurement methodologies.
- any bias inherent in adopted measurement methodologies.
- previous auditor's reports, including the auditor's report on the financial report, and related management letters.
- work performed by the internal audit and compliance functions, and any reliance that may be placed on this work.
- discussions with entity staff responsible for monitoring regulatory compliance, such as the ADI's Compliance Officer.
- the auditor's additional reporting responsibilities under the Banking Act.[46]
- changes since the last reporting period to:

[46] See paragraphs 313-327 of this Guidance Statement.

(i) the requirements of relevant AUASB Standards; and

(ii) applicable Prudential Requirements.

75. In identifying and assessing the risks of material misstatement, the auditor may need to consider the use of accounting estimates in the calculation of, for example, the ADI's Prudential Capital Requirement (PCR)[47], in accordance with the requirements and having regard to guidance provided in ASA 540 *Auditing Accounting Estimates and Related Disclosure.* The nature, timing and extent of the risk assessment and further assurance procedures required by ASA 540 will vary in relation to the estimation uncertainty and the assessment of the related risks of material misstatement. ASA 540 may prove helpful in evaluating misstatements of accounting estimates and in identifying possible management bias. Whilst ASA 540 is primarily directed at the audit of accounting estimates, the auditor uses professional judgement in considering the applicability of ASA 540 to non-accounting estimates such as non-financial data included in ADI Reporting Forms which may be subject to limited assurance.

Internal Controls and Compliance Framework

76. The auditor obtains an understanding of the entity's internal controls, the system within which the controls operate and the control components within the system, that are relevant to the assurance engagement, having regard to the requirements and guidance provided in ASAE 3150.[48]

77. The auditor obtains an understanding of the entity's compliance framework, key elements of the framework, and compliance requirements that are relevant to the assurance engagement. ASAE 3100 *Compliance Engagements* includes information that the auditor may find useful in this regard.

78. Prudential Requirements generally require ADIs to have in place internal controls corresponding to their size and complexity, aimed at ensuring that:

(a) risks are managed within prudent limits set by senior management and those charged with governance;

(b) information provided to management and those charged with governance is adequate and timely; and

(c) the ADI complies with applicable prudential and statutory requirements.

79. The term 'controls' or 'internal controls', as used in this Guidance Statement, is defined in ASAE 3150 and generally encompasses the following components:

(a) the control environment;

(b) the ADI's risk assessment process;

(c) the information system, including the related business processes, relevant to financial and prudential reporting, and communication;

(d) control activities; and

(e) monitoring of controls.

[47] As prescribed in APRA Prudential Standard APS 110 *Capital Adequacy*.
[48] In particular, paragraphs 37 and 38 of ASAE 3150.

80. In addition to the general planning considerations, the auditor takes into consideration the following factors when planning the limited assurance engagement of the internal controls relevant to the assurance engagement:

- The size, business mix and complexity of the ADI or the ADI group, and specifically whether or not an ADI is an Advanced ADI[49], as this will influence the degree of complexity impacting the control environment, compliance framework and control policies and processes.
- The overall compliance framework adopted to ensure compliance with all applicable Prudential Requirements, including controls, policies and processes, and consideration of whether or not these are appropriate given the size, business mix and complexity of the ADI and/or ADI group.
- The sufficiency and appropriateness of the ADI's and/or ADI group's Risk Management Systems descriptions and similar policy documents issued in accordance with specific Prudential Standards, and consideration of whether these are up to date and in sufficient detail to facilitate compliance with the relevant Prudential Standards.
- Matters relating to the ADI's and/or the ADI group's organisational structure and operating characteristics, and recent significant changes thereof, which could impact on relevant internal controls.
- Knowledge of internal controls obtained during other assurance engagements conducted in relation to the ADI and/or ADI group.
- The method adopted, and the process used, by the ADI and/or ADI group to develop risk information to be disclosed in ADI Reporting Forms.
- Previously communicated instances of material non-compliance with Prudential Requirements and/or material deficiencies and/or deviations in internal controls designed to ensure compliance with all applicable Prudential Requirements and the provision of reliable data to APRA in Reporting Forms, that have not been resolved.

81. The above is not meant to represent an exhaustive list and there may be other factors relevant to the specific circumstances of an ADI and/or ADI group.

Overall Responses to Assessed Risks of Material Misstatements, Deficiencies, Deviations and Non-Compliance

82. The auditor designs and performs further assurance procedures which are responsive to the assessed risks of the subject matter information being materially misstated in Specified Reporting Forms, that material deficiencies or deviations in controls may exist, and/or that the entity may not be complying with applicable Prudential Requirements.

83. ASAE 3000 clearly differentiates between the objectives of a limited versus a reasonable assurance engagement, and provides detail around the sufficiency of evidence on which to base conclusions. The nature, timing and extent of evidence gathering procedures which are conducted in any given circumstance is a matter of professional judgement and is determined in response to the auditor's determination of materiality, risk assessment and the results of the procedures conducted in response to assessed risks.

[49] The way in which internal control is designed and implemented varies with an ADI's size and complexity. Specifically, smaller Standardised ADIs may use less formal means and simpler processes and procedures to achieve control objectives.

84. In obtaining reasonable assurance, the auditor chooses a combination of assurance procedures, which may include: inspection, observation, confirmation, recalculation, reperformance, analytical procedures and enquiry.

85. As the level of assurance obtained in a limited assurance engagement is lower than in a reasonable assurance engagement, the procedures the auditor will perform will vary in nature from and will be less in extent than that for a reasonable assurance engagement. In a limited assurance engagement, procedures primarily involve enquiries and substantive analytical procedures and may not include test of controls (except where the subject matter is controls).

86. Although procedures in a limited assurance engagement will be more limited in nature, timing and extent than for a reasonable assurance engagement, ASAE 3000 and ASAE 3150 require additional procedures to be conducted if the auditor becomes aware of a matter which causes them to believe the subject matter may be materially misstated or that there may be a significant deficiency or deviation in internal controls and/or non-compliance with applicable Prudential Requirements. The auditor may conduct procedures more akin to a reasonable assurance engagement on this particular matter in order to satisfy themselves that either the subject matter is not materially misstated, controls are designed, implemented and operating effectively and it is compliant in all material respects.

87. In a reasonable assurance engagement, procedures may include tests of controls as well as substantive testing. When conducting a reasonable assurance engagement, if the auditor is able to obtain evidence that the controls they wish to rely on are operating effectively, then the nature, timing and extent of substantive testing may be reduced or modified. If reliance is to be placed on the operating effectiveness of controls throughout the period, then testing will need to cover that period. Alternatively, if the identified controls are not operating effectively, then the nature, timing or extent of substantive testings will need to be increased or modified.

Characteristics of Subject Matter and Identified Assessment Criteria

88. The table in Appendix 1 of this Guidance Statement provides an outline of the subject matter and criteria relevant to each part of the assurance engagement, as well as applicable AUASB Standards.

89. The level of assurance required to be provided by the auditor for Parts A and B of the engagement, is determined by the source of the data included in each Specified ADI Reporting Form. A reasonable level of assurance is required for data sourced from 'accounting records'. A limited level of assurance is required for all other data. The definition of 'accounting records'[50] therefore needs to be applied with care. Paragraphs 163-171 below, provide guidance on the application of this definition.

90. The appointed auditor identifies the most recent year-end ADI Reporting Forms submitted to APRA. Further guidance is provided in paragraphs 172-176 below.

91. The appointed auditor is to note that, in relation to ADI Reporting Forms prepared under the FSCODA, there are additional Reporting Forms, beyond the specific Reporting Forms listed in Attachment A to APS 310 (which is the subject matter for Parts A and B). These additional Reporting Forms are to be included in the scope of Part C of the assurance engagement, together with the Reporting Forms identified in Attachment A to APS 310.

92. The appointed auditor identifies, and obtains an understanding of, all the Prudential Requirements[51] applicable to the specific ADI (including any additional guidance provided by APRA to the ADI), with particular attention to changes in these requirements during the reporting period. The auditor makes enquiries with respect to any requirements that are

[50] See paragraph 31(c) of this Guidance Statement.
[51] See paragraphs 31(p) of this Guidance Statement.

imposed in writing by APRA on a bilateral APRA-ADI basis, or in relation to conditions on the ADI's authorisation, as these requirements may vary from one ADI to another.

93. Compliance with Prudential Requirements is broader than compliance with only the quantitative limits in APRA Prudential Standards (for example, capital requirements). The appointed auditor is required to provide assurance in relation to compliance with all relevant/applicable Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards.

The scope of the prudential assurance engagement therefore includes compliance with APRA Prudential Standards dealing with, for example, governance, risk management, public disclosure (APS 330), the Financial Claims Scheme (APS 910), and the APS 310/3PS 310 requirements relating to the appointment of the auditor and the use of group auditors.

94. In relation to an ADI's responsibility to keep the appointed auditor informed of all APRA Prudential Requirements applicable to the ADI, the appointed auditor obtains written representations from those responsible.

Identified Users and Intended Use of Auditor's Assurance Report

95. Data collected in ADI Reporting Forms are primarily used by APRA and the RBA for the purpose of prudential regulation and supervision of individual ADIs, overall supervision of the stability of the financial system and for setting monetary policy. It may also be used by the ABS to construct a range of important statistical macro-economic indicators. The auditor refers to ADI Reporting Forms and Instructions, and associated Prudential and Reporting Standards, for information regarding the nature and purpose of each individual ADI Reporting Form.

96. Data collected under the EFS Reporting Standards are primarily used by the ABS and RBA (the Agencies) for analysis, publication and policy-making purposes. EFS data is used by the ABS to compile and publish key macroeconomic indicators, including Australia's National Accounts and leading indicators of lending activity, which is used to monitor Australia's growth. The RBA uses EFS data to construct and publish Australia's monetary and credit aggregates, and for analytical and policy purposes. Data published by the RBA are also used by other policy makers and the wider public for research, analysis and policy making.[52] Information collected under the EFS Reporting Standards may be used by APRA for prudential and publication purposes.

97. Requirements for auditors of ADIs to provide assurance reports on prudential matters to APRA are intended to assist APRA, and the Agencies, in assessing the reliability of information supplied to it by an ADI.

98. Auditors need to be aware that APRA has the power under subsection 56(5) of the *Australian Prudential Regulation Authority Act 1998* to make 'protected information' (which may include auditors' reports or information extracted from such reports) available to another financial sector supervisory agency (for example, the Reserve Bank of Australia and Treasury), or any other 'specified' agency (including foreign agencies), when APRA is satisfied such information will assist those agencies in performing its functions or exercising its powers.

Reliability of Information and Data Quality

99. The concept of reliability is to be viewed in the context of the reliability of the data for the intended use by the identified users.

[52] See APRA Reporting Practice Guide RPG 702.0 *ABS/RBA Data Quality for the EFS Collection*.

100. Under the Australian Accounting Standards Board's (AASB's) *Glossary of Defined Terms*, information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully, and without material error and bias, the transactions or events that either it purports to represent or could reasonably be expected to represent.

101. In applying this concept of reliability to the prudential reporting engagement, information in ADI Reporting Forms is not to lead users to conclusions that serve the particular needs of an ADI. Furthermore, such information needs to be capable of reliable measurement.

102. APRA Prudential and Reporting Standards provide the frame of reference (benchmarks) for reasonably consistent evaluation or measurement, within the context of the auditor's professional judgement, of the reliability of the information included in ADI Reporting Forms.

103. The appointed auditor identifies and obtains an understanding of the applicable Prudential Requirements that govern the preparation of data within ADI Reporting Forms, with particular attention to changes in these requirements during the reporting period under review. In addition to the Prudential and Reporting Standards issued by APRA, other Prudential Requirements, including the specific Reporting Form Instruction Guides, will also have an impact on the provision of reliable data to APRA under the FSCODA and, therefore, the appointed auditor has regard to all relevant Prudential Requirements when planning and conducting the engagement.

104. It is important that the appointed auditor obtains an understanding of how APRA Prudential and Reporting Standards differ from the financial reporting framework[53] which are used to record data in the ADI's accounting records.

105. APRA's Prudential Practice Guide CPG 235 *Managing Data Risk* (CPG 235) may aid in the auditor's understanding of the concept of reliability in the context of the assurance engagement. CPG 235 provides guidance to APRA regulated entities on managing data risk, including assessing data quality by reference to its 'fitness for use', that is, the degree to which data is relevant and appropriate for its intended purpose.

106. Other determinants of data quality identified in CPG 235 include:

(a) accuracy – the degree to which data is error free and aligns with what it represents;

(b) completeness – the extent to which data is not missing and is of sufficient breadth and depth for the intended purpose;

(c) consistency – the degree to which related data is in alignment (definition, value, range, type and format, as applicable)

(d) timelines – the degree to which data is up-to-date; and

(e) availability - accessibility and usability of data when required.

EFS Collection

107. APRA's Reporting Practice Guide RPG 702.0 *ABS/RBA Data Quality for the EFS Collection* (RPG 702.0) provides guidance to assist ADIs and RFCs required to submit EFS data to APRA, to meet the Agencies' data quality requirements in relation to EFS Reporting Standards.

108. RPG 702.0 is to be read in conjunction with:

[53] Under Australian Accounting Standards.

(a) the EFS Reporting Standards, which contains definitions of, and guidance on, the data to be reported to APRA and the Agencies; and

(b) Prudential Practice Guide CPG 235.

109. RPG 702.0 outlines how the Agencies, as primary users, intend to use data collected under the EFS Reporting Standards. It informs EFS reporting entities of the significance of specific EFS data items for use by the Agencies and is designed to assist entities in meeting EFS quality control requirements by adapting data risk management practices outlined in CPG 235 for the EFS collection.

110. Although the Agencies expect all data collected by APRA on their behalf to be accurate, reporting entities are expected to use the 'data priority' ranking included in RPG 702.0 as an indicator of the relative importance of the accuracy of these data items and, therefore, where to focus data quality management practices. Three categories of priority are identified: 'standard', 'high' and 'very high' data items.

111. The table in Attachment A to RPG 702.0 includes qualitative benchmarks to indicate the size of misreported data items that may impact the use of the data by the Agencies and thus would be considered a 'reporting error'[54] that needs to be notified to ARPA. These benchmarks vary according to entity size[55], type of data item[56] and prioritisation of data[57].

112. Benchmarks for entities defined as 'large institutions' in RPG 702.0 recognise that reporting errors by a single large entity are more likely to impact industry aggregates due to their size, while benchmarks for the entities that are not 'large' are aimed at identify reporting errors that could affect the industry aggregate results if occurring across several entities simultaneously.

113. RPG 702.0 includes specific guidance in relation to the:

(a) application of judgement in identifying reportable errors for 'standard' priority data items (that is, data items that is not of a 'high' or 'very high' priority);

(b) application of benchmarks where data items is at, or very close to, zero;

(c) application of benchmarks to volatile 'flow' data items; and

(d) the use of proxy methodologies for selected data items[58].

114. The Agencies and APRA recognise that not all practices outlined in the guide will be relevant for every EFS reporting entity and that some aspects may vary depending upon the size, complexity and systems configuration of the EFS reporting entity.

115. PARAGRAPH DELETED

Materiality

116. The auditor considers materiality when determining the nature, timing and extent of assurance procedures. The objectives of setting materiality are to establish:

(a) a tolerable level of misstatement in relation to financial and non-financial information included in ADI Reporting Forms, deficiencies or deviations in controls, or non-compliance with applicable Prudential Requirements;

54 RPG 702.0 defines a 'reporting error' as the difference between the data reported to APRA and the data required to be reported to APRA under EFS Reporting Standards that is outside the agencies' expectations for data quality.
55 Whether the entity is a 'large institution' or 'not a large institution' as defined in RPG 702.0.
56 Whether a data item is a 'stock' or 'flow' item as defined in RPG 702.0.
57 RPG 702.0 prioritises data into the following categories: 'standard', 'high' and 'very high'.
58 See RPG 701.0.

(b) the scope of assurance work to be performed; and

(c) a reasonable basis for evaluating identified misstatements, deficiencies, deviations, or non-compliance.

117. Materiality is addressed in the context of the auditor's objectives, which are developed having regard to reasonable expectations of issues that would likely influence the decisions of APRA or other intended user(s). The auditor may determine that particular categories of data or compliance may have a greater impact on the decisions of users and sets a specified materiality at a lower level for those amounts or matters.

118. The auditor sets materiality in accordance with ASA 320 *Materiality in Planning and Performing an Audit*, ASAE 3000, ASAE 3150, ASAE 3450 and ASRE 2405. In determining materiality levels, the auditor exercises professional judgement having regard to the ADI's obligations, together with the size, business mix and complexity of the ADI or the ADI Group. When assessing materiality, the auditor considers qualitative factors as well as quantitative factors that may influence the decision of users.

119. The auditor develops separate materiality levels for each section of the engagement:

(a) where the subject matter is historical financial information, materiality is set with reference to the principles and guidance provided in ASA 320 and ASRE 2405, as applicable;

(b) where the subject matter is information other than historical financial information, materiality is set in accordance with the principles and guidance provided in ASAE 3000;

(c) where the subject matter is prospective financial information[59], materiality is set with reference to the principles and guidance provided in ASAE 3450; and

(d) for the controls section of the engagement, materiality is set with reference to the principles and guidance provided in ASAE 3150.

120. Materiality is determined in the same way whether the engagement is a reasonable or limited assurance engagement. The difference between reasonable and limited assurance engagements lies in the nature, timing and extent of evidence gathering procedures, which will differ in order to reduce the risk of a material misstatement, control deficiency or deviation, or non-compliance remaining undetected, to an acceptable low level in the case of a reasonable assurance engagement, or to a limited level in the case of a limited assurance engagement. The risk of material misstatements, control deficiencies or deviations, and/or non-compliance in a limited assurance engagement is not reduced to the same extent as in a reasonable assurance engagement, because of the more limited nature, timing and extent of procedures conducted. In a limited assurance engagement, the auditor seeks to obtain a meaningful level of assurance, which is likely to enhance the intended users' confidence about the subject matter to a degree that is clearly more than inconsequential.

121. Although there is a greater risk that misstatements, control deficiencies or deviations, or non-compliance may not be detected in a limited assurance engagement than a reasonable assurance engagement, the judgement as to what is material is made by reference to the subject matter on which the auditor is reporting, and the needs of those relying on that information, as opposed to the level of assurance obtained.

[59] For example, in relation to liquidity disclosures included in ADI Reporting Forms ARF 210.1A and 210.1B *Liquidity Coverage Ratio*.

122. In setting materiality levels, regardless of the subject matter or level of assurance, it is the auditor's objective to reduce risk to an acceptable level in the circumstances of the assurance engagement.

Reasonable and/or Limited Assurance on Specified[60] *ADI Reporting Forms (Parts A and B)*

123. Materiality is to be addressed in the context of the entity's objectives relevant to the ADI Reporting Form and Reporting Standard being examined and whether internal controls will reduce to an acceptable level the risks that threaten achievement of those objectives.[61]

124. A misstatement in a Specified ADI Reporting Form, either individually or in aggregate with other misstatements, is considered material if the appointed auditor believes the intended users may be influenced by the misstatement or omission of the information.

125. Matters likely to adversely affect the interests of depositors in ADIs are generally related to solvency and going concern assumptions. In the context of APRA's prudential reporting requirements, the ADI's 'Prudential Capital Requirement' (PCR), as prescribed in Prudential Standard APS 110 *Capital Adequacy*, is an important consideration with respect to materiality. However, the auditor will exercise professional judgement to consider whether an alternative base, such as profit, assets or revenue, may be more appropriate within the context of the specific ADI Reporting Form, or line item within a Reporting Form.

126. For the purpose of reporting on the reliability of information included in Specified ADI Reporting Forms, the appointed auditor considers and applies materiality at the level of individual Reporting Forms[62] or, if the auditor deems it to be more appropriate, the auditor may choose to set a specific materiality at the level of individual data items or categories of data included in Reporting Forms.

127. In applying ASA 320, ASRE 2405, ASAE 3000 and ASAE 3450, as appropriate, to individual ADI Reporting Forms, or data line items in Reporting Forms, the auditor has regard to the nature, purpose and use of the information included in each Reporting Form. The auditor refers to ADI Reporting Forms and Instructions, and associated Prudential and Reporting Standards, for information regarding the nature and purpose of each individual ADI Reporting Form.

128. The Australian Accounting Standards Board's Practice Statement 2 *Making Materiality Judgements* may provide a useful frame of reference to the auditor in determining materiality for the engagement.

129. ASA 320 and AASB Practice Statement 2 deal with materiality in the context of the financial statements taken as a whole and may be useful in setting materiality levels for relevant 'Statement of Financial Performance' and 'Statement of Financial Position' ADI Reporting Forms.

130. Where Reporting Forms include historical and prospective financial information, as well as non-financial information, the auditor considers adopting a combination of methods and setting multiple materiality levels based on the information included in the Reporting Form. For example:

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[60] For a listing of ADI Reporting Forms to be subjected to the reasonable and/or limited assurance engagement, refer to APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance*. The requirements are different for Standardised, Advanced and Foreign ADIs.

[61] For example, the objective of the Capital Adequacy series of ADI Reporting Forms will be on protection of the interests of depositors in ADIs.

[62] Where a particular data item appears in multiple ADI Reporting Forms subject to different levels of materiality, the auditor ensures the work performed is appropriate and sufficient to meet the lowest level of materiality. For example, materiality may be set for a balance sheet-based reporting form. However, the appointed auditor may need to consider the potential impact of misstatements in the balance sheet on profit and loss based reporting forms, which by their nature may have lower materiality thresholds.

(a) For historical financial information extracted from accounting records related to audited[63] financial information, the auditor may:

(i) determine that the materiality levels used in the statutory audit/review under the Corporations Act are acceptable/suitable for the purposes of the statistical return, and leverage off work performed as part of the statutory audit/review; or

(ii) establish new materiality levels in accordance with the principles espoused in ASA 320 or ASRE 2405 and other relevant guidance, as applicable to the subject matter information and based on the amounts reported in the Reporting Forms.

(b) For non-financial information, materiality may be set with reference to the principles and guidance provided in ASAE 3000.

(c) For prospective financial information, materiality may be set with reference to the principles and guidance provided in ASAE 3450.

131. PARAGRAPH DELETED

132. The appointed auditor's preliminary assessment of materiality is based largely on quantitative factors. A percentage is often applied to a chosen benchmark as a starting point in determining materiality. The base and percentage may vary depending on the ADI Reporting Form in question and the nature of information included in each Reporting Form.

133. A key concern with any misstatement within a Reporting Form is its potential impact on the ADIs 'capital base' and 'capital adequacy ratio', that are determined in accordance with APRA's Prudential Standards[64]. This is taken into consideration by the appointed auditor when evaluating whether a misstatement in a Reporting Form, especially within the Capital Adequacy ADI Reporting Forms, is material.

134. APRA has advised that a materiality threshold based on a 25 basis point impact on the capital ratio may be applied in aggregate by the appointed auditor as a reasonable basis for determining quantitative materiality for Capital Adequacy Reporting Forms. This threshold may be used as indicative guidance only, in conjunction with the considerations described within this Guidance Statement, which includes consideration of qualitative factors. The appointed auditor exercises professional judgement when applying the threshold in specific circumstances. For example, a lower level of materiality may be appropriate as the level of surplus capital reduces.

135. Alternative bases, similar to those used in determining materiality for financial statement audits (such as net profit, revenue or assets) may be appropriate when considering whether a misstatement within ADI Reporting Forms such as the Statement of Financial Performance, Statement of Financial Position, Provisions and Impaired Assets, is material.

136. When considering materiality, the auditor considers the obligations under Prudential Requirements for ADIs and auditors of ADIs to report errors in ADI Reporting Forms to APRA, the criteria for re-submission of data previously submitted to APRA, and reporting breaches to APRA. For example, RPG 702.0 indicates that misreported EFS data items above the prescribed quantitative data quality benchmarks in Attachment A to RPG 702.0 should be notified to APRA. However, RPG 702.0 states these errors would not trigger automatic resubmission, as the Agencies will determine the need for resubmission. The auditor exercises professional judgement in using this guidance in scoping assurance work to be performed.

[63] For example, the audit [review] under the Corporations Act.
[64] Refer to APS 110.

137. The auditor should be cognisant that RPG 702.0 is primarily directed at reporting entities and designed to assist these entities in meeting EFS quality control requirements and to tailor data risk management practices as outlined in CPG 235.[65] APRA has confirmed that the intention is not to require ADIs to embed RPG 702.0 benchmarks in all of their controls, or to employ extensive use of data sampling techniques, if this does not accord with the entity's risk appetite and approach to managing data risk.[66]

138. Whilst APRA and the Agencies expect auditors to consider the RPG 702.0 guidance in determining materiality thresholds for a prudential reporting assurance engagement, APRA has confirmed that the RPG 702.0 benchmarks do not establish new materiality requirements for assurance purposes relating to the EFS data collection.[67]

139. The auditor is not required to provide assurance to the levels set out in RPG 702.0. The auditor sets materiality levels for the EFS collection based on the risk assessment for each EFS Reporting Form performed by the auditor. The priority ranking of data points included in RPG 702.0 may be helpful for the auditor in determining where to focus effort.

140. RPG 702.0 benchmarks and considerations may be more relevant to Part C of the engagement in setting materiality levels for reporting on the design and operating effectiveness of internal controls addressing the reliability of data routinely reported to APRA in ADI Reporting Forms. Refer to Part C below.

141. Auditors retain ultimate discretion in setting materiality levels for the assurance engagement and determining the scope of assurance procedures to be conducted, taking into consideration the risk of issuing an inappropriate assurance report.

Limited Assurance Engagement on Design, Implementation and Operating Effectiveness of Internal Controls (Part C)

142. Material deficiencies in the design and implementation of controls and material deviations in the operating effectiveness of controls are those which could reasonably be expected to influence relevant decisions of the intended users.

143. ASAE 3150 sets out the requirements and provides guidance to the auditor in applying materiality in the context of an assurance engagement on controls.

144. In accordance with ASAE 3150, the auditor shall identify a control or combination of controls as material if it is fundamental to the achievement of a control objective relevant to the scope of the engagement, and whether the internal controls will reduce to an acceptably low level, based on auditor judgement, the risks that threaten achievement of those objectives.

145. In assessing materiality, the appointed auditor has regard to the measures the ADI has adopted to ensure:

(a) reliable data is provided to APRA in all ADI Reporting Forms prepared under the FSCODA; and

(b) compliance with all applicable Prudential Requirements.

146. For the purpose of reporting on controls addressing the reliability of EFS data included in ADI Reporting Forms, the auditor determines materiality levels taking into consideration the needs and expectations of the users of the EFS collection, as outlined in RPG 702.0. RPG 702.0

[65] That is, a reporting entity's precision thresholds for reporting data to APRA.
[66] Refer to APRA and the Agencies' *Response to Submissions: Economic and financial statistics data quality framework* (8 March 2018), available on APRA's website at www.apra.gov.au.
[67] The benchmarks included for ADIs in RPG 702.0 may therefore be more granular than the materiality levels required to be applied in undertaking the reasonable and limited assurance engagements required under APS 310 to report on data included in Specified ADI Reporting Forms at the financial year-end.

informs reporting entities of the Agencies' expectation that data reported in EFS collection should be of high quality, including to be accurate, complete and timely. RPG 702.0 provides guidance to reporting entities to meet data quality control requirements that require them to have in place systems, processes and controls to assure the reliability of reported information in relation to the EFS Reporting Standards. RPG 702.0 guidance is supported by CPG 235 which sets out guidance on how entities can manage data risk, including assessing data quality by reference to fitness for use.

147. Although auditors retain discretion in setting materiality levels, they are expected to take into consideration RPG 702.0's priority ranking of data items and data quality benchmarks as part of the assessment of whether a reporting entity's internal controls are designed appropriately and operating effectively to meet the RPG 702.0 thresholds required by the Agencies.

148. The auditor considers how ADI's have incorporated RPG 702.0 thresholds and other relevant guidance, for example, CPG 235, into their risk management processes. Should an ADI identify errors that have occurred in relation to EFS reporting that exceed the data quality thresholds, this may be indicative of a control environment that is not appropriately designed or operating effectively to ensure entities have provided reliable data to APRA. In these instances the auditor would be expected to assess the nature of the error, whether deficiencies in the control environment contributed to the error, and what subsequent changes have occurred (if any) to address such deficiencies. Where such deficiencies exist, the significance of these would need to be considered against Parts A, B and C of the APS 310 opinion and conclusions

149. ASAE 3150 requires the auditor to reassess the materiality of the controls if matters come to their attention during the engagement which indicate that the basis on which the materiality of those controls was determined has changed.

Reporting on Compliance with Prudential Requirements (Part D)

150. Under APS 310 and 3PS 310 the appointed auditor is required to provide limited assurance that the ADI and/or group has complied, in all material respects, with all relevant Prudential Requirements. This conclusion is to be based on the auditor's reasonable and limited assurance engagements undertaken to provide assurance in relation to Specified ADI Reporting Forms (Parts A and B) and internal controls (Part C).

151. For the purpose of reporting on compliance with Prudential Requirements, the appointed auditor considers materiality when *evaluating* the significance of identified instances of non-compliance with relevant Prudential Requirements (refer to paragraphs 259-268).

Personnel and Expertise Requirements, Including the Nature and Extent of Experts' Involvement

152. An appointed auditor gives further consideration as to whether the auditor has, or will be able to obtain, adequate knowledge and the required skills to undertake the engagement.

153. APS 310 and 3PS 310 prohibit an appointed auditor from placing sole reliance on the work performed by APRA, for example, as part of the initial accreditation process to be registered as an Advanced ADI. APRA expects appointed auditors to exercise their professional judgement and reach their own independent conclusions.

154. The nature and complexity of the ADI increases the likelihood that the appointed auditor may need to involve experts in the engagement. For example, obtaining an understanding of the process and assumptions used by an Advanced ADI to develop risk information, may require technical knowledge of risk measurement methodologies, which can be complex.

155. When planning to use the work of an auditor's expert as evidence, the appointed auditor has regard to the requirements and guidance provided in, as appropriate, Auditing Standard ASA 620 *Using the Work of an Auditor's Expert*, ASAE 3000, ASAE 3150 and ASAE 3450.

156. Where an ADI has engaged or employed experts, for example where actuaries are used to determine amounts for inclusion in ADI Reporting Forms, which is derived using specialised techniques, the auditor applies, as appropriate, ASA 500 *Audit Evidence*. ASA 500 sets out mandatory requirements and provides application and explanatory material on using the work of a management's expert as audit evidence. The auditor may also find it helpful to refer to AUASB Guidance Statement GS 005 *Evaluating the Work of a Management's Expert and Considerations in Determining the Extent to which the Auditor uses their work as Audit Evidence*.

Work Performed by Another Auditor

157. Where the auditor appointed under APS 310/3PS 310 plans to use the work of another independent auditor, the appointed auditor:

- for the reasonable assurance engagement in relation to historical financial information, complies with the requirements of Auditing Standard ASA 600 *Special Considerations – Audits of a Group Financial Report*; and
- for other assurance, complies with the requirements of ASAE 3000. The principles espoused in ASA 600 may also provide helpful guidance.

Internal Audit

158. CPS 510 requires all ADIs (including a foreign ADI in relation to its Australian business) and authorised NOHCs, to have in place an independent and adequately resourced internal audit function.[68]

159. APS 310 and 3PS 310 require an ADI and/or the head of an ADI group to ensure that the scope of internal audit includes a review of the policies, processes and controls put in place by management to ensure compliance with Prudential Requirements. Furthermore, CPS 510 requires that the objectives of the internal audit function include an evaluation of the adequacy and effectiveness of the financial and risk management framework of the ADI. CPS 220 includes further information on APRA's requirements for the periodic review of the risk management framework by internal audit. APRA expects the appointed auditor to consider the extent to which the work of the internal audit function is likely to be relevant in the context of the APS 310/3PS 310 assurance engagement.

160. Having regard to the requirements and guidance provided in AUASB standards ASA 610 *Using the Work of Internal Auditors*, ASAE 3000 and ASAE 3150, as relevant, the appointed auditor obtains an understanding of the activities and main findings of the internal audit function and perform a preliminary assessment, which may include, assessment of:

(a) its impact on the system and the components of control within that system, including the control environment, risk assessment, information and communication, monitoring activities and control activities in relation to the system; and

(b) its effect on the nature, timing or extent of the auditor's assurance procedures.

161. The use of internal auditors to provide direct assistance is prohibited in assurance engagements undertaken in accordance with AUASB Standards. Direct assistance is the performance of assurance procedures under the direction, supervision and review of the independent external auditor. This prohibition does not preclude reliance on the work of the

[68] Under CPS 510, APRA may approve alternative arrangements where APRA is satisfied that it will achieve the same objectives.

internal audit function to modify the nature or timing, or reduce the extent, of assurance procedures to be performed directly by the auditor.

162. Where the appointed auditor plans to use the work of the internal audit function, the auditor evaluates the adequacy of this work for the auditor's purposes in accordance with the relevant AUASB standards. The appointed auditor remains responsible for obtaining sufficient appropriate evidence to support the auditor's assurance engagement conclusions.

Matters to Consider in Conducting the Engagement

Special Considerations - Assurance on Specified[69] ADI Reporting Forms (Parts A and B)

Application of the AUASB Definition of 'Accounting Records'

163. APS 310 and 3PS 310 requires the appointed auditor to provide two different levels of assurance over the reliability of a specific set of ADI Reporting Forms at the ADI's financial year-end. The level of assurance required to be provided by the appointed auditor is determined by the source of the data included in the Reporting Forms. Data sourced from 'accounting records', requires a reasonable level of assurance. All other data requires a limited level of assurance.

164. 'Accounting records', is defined in paragraph 31(c) of this Guidance Statement and, ordinarily, includes all the data used by an ADI to prepare its accounting books and records, and to report the results of its operations and its financial position in its financial report on an annual or half-yearly basis (that is, the underlying evidence in support of the financial report). The expectation is, generally, that such data would be subject to rigorous internal controls.

165. However, the initial books of entry may also comprise other data which is stored alongside accounting data. Such data may not be used for financial management and financial reporting, and may not be subject to rigorous controls, and therefore fall outside the scope of the reasonable assurance opinion.

166. Data in ADI Reporting Forms may be sourced from systems that are not used to produce financial report information and are not readily reconcilable to financial report information. The initial entries to these systems may be the same as for the accounting records, but both the level of control over the systems and the amount of manipulation/aggregation of the data within such systems may result in the output being significantly different from the accounting records and not readily reconcilable back to these records.

167. The auditor makes an assessment of whether or not a data item has been sourced from accounting records, by exercising professional judgement and referring to the definition of accounting records. The appointed auditor carefully considers the source and the use of the data, and whether it is appropriately controlled and, therefore, capable of being subjected to audit.

168. For Advanced ADIs, where the ADI's risk management systems provide internal estimates for some or all of the risk components in determining capital, the 'capital' Reporting Forms will include data items sourced from non-accounting records. Examples include measures for 'probability of default' and 'loss given default'.

169. Certain data items may have been sourced indirectly from the accounting records, for example, data sourced from accounting records that involve additional examination, computation, re-classification or segmentation. APRA has indicated that these data items are

[69] For a listing of ADI Reporting Forms to be subjected to the Reasonable and/or limited assurance engagement, refer to APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance*. The requirements are different for Standardised, Advanced and Foreign ADIs.

deemed to have been sourced from non-accounting records and will fall within the scope of the limited assurance opinion.

170. PARAGRAPH DELETED

171. Where ADI Reporting Forms combine elements that are derived from accounting records and non-accounting records, the appointed auditor provides:

(a) reasonable assurance on information derived from the accounting records, for example, totals derived from the balance sheet such as values for assets, liabilities and derivatives, in the ADI Reporting Forms listed below; and

(b) limited assurance on the information derived from non-accounting records, for example:

- ADI Reporting Form ARF 117.0 *Repricing Analysis*: the repricing period allocations to time periods set out in the interest rate sensitivity tables (which are subjective).
- ADI Reporting Form ARF 112.1A *Standardised Credit Risk – On-balance Sheet Exposures*: the risk rating for loans based on the loan-to-valuation ratio (LVR) where the security values are subject to variation over time.

Also refer to paragraph 175 below.

Identification of Financial Year-end ADI Reporting Forms

172. Identification of the year-end ADI Reporting Forms to be subjected to the reasonable and/or limited assurance engagement, requires careful consideration by the appointed auditor.

173. The initial submission of ADI Reporting Forms, to meet APRA's reporting timetable, may be too soon in the ADI's year-end process for the ADI to have processed all relevant year-end journals and adjustments. As a result, the ADI may have submitted revised Reporting Form(s) after the due reporting date. As the audit requirement is to report on the "reliability" of the year-end Reporting Forms, the appointed auditor selects the most up to date (recent) Reporting Forms submitted to APRA, rather than the Reporting Forms initially submitted in accordance with APRA's reporting timetable. The appointed auditor conducts further procedures to ensure that the selected Reporting Forms include all relevant year-end journals and adjustments.

174. The ADI Reporting Forms which are the subject of the assurance report, are clearly identified in the assurance report. This may be achieved, for example, by:

(a) attaching the Reporting Forms to the assurance report; or

(b) noting the time and date of submission of the Reporting Forms to APRA in the assurance report.

175. As noted above, certain ADI Reporting Forms may include data sourced from a combination of accounting and non-accounting records. The appointed auditor needs to clearly identify such data so that the intended user of the assurance report understands the level of assurance attached to each data item. This could be achieved in a number of ways, for example:

- Attaching the Reporting Forms to the assurance report and clearly identifying the level of assurance attached to each individual section (or data item) within each Reporting Form.

- Listing the Reporting Form and the individual sections (or data items) for which reasonable and limited assurance have been provided within the body of the assurance report under the section "Opinion and Conclusions".

- Providing a detailed list in an attachment to the assurance report which clearly identifies the Reporting Form and the individual sections (or data items) for which reasonable and limited assurance have been provided.

Refer to Appendix 4 for illustrative examples of possible approaches to identify subject matter subject to reasonable and limited assurance.

176. Where the ADI Reporting Form over which assurance is to be provided at the financial year-end, is not the Reporting Form submitted on the due date in accordance with APRA's reporting timetable, the appointed auditor needs to consider this issue when providing assurance on the design and operational effectiveness of controls over the reliability of Reporting Forms[70].

Reasonable Assurance on Specified ADI Reporting Forms - Data Sourced from Accounting Records (Part A)

Reporting Requirements

177. The appointed auditor is required to provide reasonable assurance that information included in ADI Reporting Forms, as specified in Attachment A of APS 310, at the financial year-end, sourced from the ADI's accounting records, is, in all material respects:

(a) reliable; and

(b) in accordance with the relevant APRA Prudential and Reporting Standards.

Refer to Part A of the Example Annual Prudential Assurance Report in Appendix 4 of this Guidance Statement.

AUASB Standards

178. In performing the reasonable assurance engagement on Specified ADI Reporting Forms, the auditor is required to comply with all Australia Auditing Standards relevant to a reasonable assurance engagement of other historical financial information.

Gathering Evidence

179. To identify the ADI Reporting Forms, or data items in a Reporting Form, that are to be subjected to the assurance engagement (the subject matter), the appointed auditor applies the definition of accounting records to each item of data within each Reporting Form as specified in Attachment A of APS 310.

180. Having identified the ADI Reporting Forms, or data items within a Reporting Form, that are to be subjected to the reasonable assurance engagement, the appointed auditor obtains sufficient appropriate evidence as part of a systematic process[71], that includes:

- Obtaining an understanding of the Specified ADI Reporting Forms and individual data items included in these Reporting Forms (subject matter), the intended use of the information included in the Reporting Forms by the intended users, and the Prudential Requirements applicable to the preparation and submission of Reporting Forms.

[70] See paragraph 173 of this Guidance Statement.
[71] See ASA 315 Assessing and Identifying the Risks of Material Misstatement through Understanding the Entity and its Environment.

- Obtaining and understanding of the ADI's framework for managing data risk and data quality.[72]
- Obtaining an understanding of the ADI's system of internal control, in particular, controls around managing data risk, and the compliance function relevant to the engagement and control objectives.
- Evaluating the controls over the preparation and compilation of Reporting Forms.
- Identifying and assessing the risk that information in Reporting Forms may be materially misstated.
- Responding to assessed risks and determining the nature, timing and extent of further evidence-gathering procedures.
- Performing further evidence-gathering procedures clearly linked to the identified risks.
- Evaluating the sufficiency and appropriateness of evidence.

181. The appointed auditor exercises professional judgement in determining the nature, timing and extent of reasonable assurance procedures to gather sufficient appropriate evidence on which to base the reasonable assurance opinion.

182. A controls based assurance approach is often the most appropriate approach to adopt in these circumstances. However, where the appointed auditor determines that a material weakness exists in the ADI's internal controls designed to ensure reliable data is provided to APRA in Reporting Forms, and/or where the appointed auditor makes a determination based on effectiveness and/or efficiency, a substantive approach may be more appropriate (for example, for smaller Standardised ADIs).

183. Reasonable assurance procedures for obtaining evidence include, but are not limited to, testing of specific controls aimed at ensuring data in Reporting Forms is reliable and prepared in accordance with APRA Prudential Standards and Reporting Standards. Reasonable assurance procedures may include a combination of enquiry and observation, analytical procedures, testing of controls over the compilation of Reporting Forms, testing of controls over the extraction of data from the underlying accounting records (including all relevant year-end adjustments), inspection, confirmation, recalculation, re-performance, obtaining independent corroborating information and obtaining management representations.

184. The appointed auditor may decide to place reliance on work undertaken by the auditor appointed for the purpose of the audit of the general purpose financial report, required under the Corporations Act (the statutory audit), as the basis for opining on the reliability of the Specified ADI Reporting Forms, or data items included in these forms. However, the appointed auditor is still required to obtain additional audit evidence to ensure that the Reporting Forms, or data items in a Reporting Form:

(a) have been appropriately extracted from the underlying accounting records (which were the subject of the statutory audit); and

(b) are in accordance with APRA's Prudential Standards and Reporting Standards (which may be different from the Australian Accounting Standards Framework used to record items in the ADI's underlying accounting and statutory records).

185. Where reliance is being placed on work performed for the statutory audit, the appointed auditor ensures that events occurring subsequent to the date of signing the statutory accounts,

[72] For example, refer to APRA Prudential Standard CPS 220 *Risk Management*, APRA Prudential Practice Guide CPG 235 *Managing Data Risk* and APRA Reporting Practice Guide RPG 702.0 *ABS/RBA Data Quality for the EFS Collection*.

but before the date of issuing the Auditor's Annual Prudential Assurance Report, are taken into consideration in forming the opinion issued in the Report.

186. Materiality is to be applied as outlined in paragraphs 116-141 of this Guidance Statement.

Limited Assurance on Specified ADI Reporting Forms - Data Sourced from Non-Accounting Records (Part B)

Reporting Requirements

187. The appointed auditor is required to express a conclusion, based on a limited assurance engagement, on whether anything has come to the appointed auditor's attention that causes the auditor to believe that information included in APRA Reporting Forms, as specified in Attachment A to APS 310, at the financial year-end, sourced from non-accounting records of the ADI, is not, in all material respects reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

Refer to Part B of the Example Annual Prudential Assurance Report in Appendix 4 of this Guidance Statement.

AUASB Standards

188. In order to form a conclusion on the reliability of information included in Specified ADI Reporting Forms at the financial year-end, sourced from non-accounting records, the appointed auditor conducts a limited assurance engagement in accordance with:

(a) ASRE 2405 - for historical financial information;

(b) ASAE 3000 – for information other than historical financial information; and

(c) ASAE 3450 - for prospective financial information.

189. Prospective financial information generally includes forecasts and projections based on assumptions made by the ADI, in accordance with a stated basis of preparation. ASAE 3450 sets out the responsibilities of an assurance practitioner undertaking an engagement to report on prospective financial information. It identifies specific considerations in the application of ASRE 2405 and/or ASAE 3000, which may apply in the engagement circumstances. ASAE 3450 does not override the requirements of ASRE 2405 or ASAE 3000 and it does not purport to deal with all engagement circumstances.

Gathering Evidence

190. All ADI Reporting Forms, or data items within Reporting Forms, as specified in Attachment A of APS 310, that have been excluded under paragraphs 177-186 above as not having been sourced from accounting records, are included in this section as the subject matter for the limited assurance engagement.

191. Having identified the subject matter that are to be subjected to the limited assurance engagement, the appointed auditor obtains evidence, as part of a systematic process directed by the risk assessment carried out during the planning phase of the engagement. The auditor exercises professional judgement in determining the specific nature, timing and extent of limited assurance procedures to gather evidence on which to base the conclusion.

192. The limited assurance engagement is substantially less in scope than the reasonable assurance engagement (audit) undertaken in paragraphs 177-186 in order to provide reasonable assurance under Part A of the Auditor's Annual Prudential Assurance Report. The limited assurance engagement procedures do not provide all the evidence required in a reasonable assurance engagement and, consequently, the level of assurance provided is less than that given in an reasonable assurance engagement.

193. Ordinarily, limited assurance procedures may include a review of specific controls aimed at ensuring Reporting Forms, and data in Reporting Forms, are reliable and prepared in accordance with APRA Prudential Standards and Reporting Standards. Limited assurance procedures may include analytical procedures, enquiry, limited testing of controls over the compilation of Reporting Forms, limited testing of controls over the extraction of data from the underlying source systems and obtaining management representations.

194. If the auditor has reason to believe that the subject matter information subject to limited assurance may be materially misstated, AUASB Standards require that the auditor carry out additional or more extensive procedures as are considered necessary to be able to express a limited assurance conclusion or to confirm that a modified report is required.

195. Materiality is to be applied as outlined in paragraphs 116-141 of this Guidance Statement.

Advanced ADIs

196. Under the advanced approaches for measuring capital adequacy, an Advanced ADI is permitted to use its own quantitative risk estimates in calculating regulatory capital. This involves a greater use of internal risk measurement models that generate the credit risk, operational risk, market risk and interest rate risk in the banking book (instead of the standardised risk assessments used by Standardised ADIs). As a result, under the advanced approaches, a smaller proportion of information contained in APRA's capital adequacy Reporting Forms is derived from accounting records.

197. At the planning stage of the engagement, the appointed auditor decides on the appropriate assurance approach to adopt in order to gather evidence to reduce the assurance engagement risk to an acceptable low level to provide limited assurance in relation to the reliability of Reporting Forms, or data items in a Reporting Form, which are sourced from the internal risk measurement models.

198. A controls based assurance approach is often the most appropriate approach to adopt in these circumstances. The appointed auditor gathers evidence regarding the internal control structure, and that key controls around the risk measurement models, as identified during the planning phase of the audit, are operating effectively to support the assurance conclusion.

199. In concluding on any data produced from the internal risk measurement models, the appointed auditor cannot place sole reliance on work performed by APRA, as part of the initial accreditation process for becoming an Advanced ADI or in any subsequent reviews undertaken by APRA.

Limited Assurance on Internal Controls over Compliance with Prudential Requirements and Reliability of ADI Reporting Forms (Part C)

Reporting Requirements

200. The appointed auditor is required to express a conclusion, based on a limited assurance engagement, whether anything has come to the attention of the auditor to cause the auditor to believe that, in all material respects:

    (a) the ADI has not implemented internal controls that are designed to ensure the ADI has:

        (i) complied with all applicable Prudential Requirements; and

        (ii) provided reliable data to APRA in the ADI Reporting Forms prepared under the FSCODA; and

    (b) these controls have not operated effectively throughout the financial year.

Refer to Part C of the Example Annual Prudential Assurance Report in Appendix 4 of this Guidance Statement.

AUASB Standards

201. The appointed auditor conducts the limited assurance engagement related to internal controls in accordance with ASAE 3150.

Gathering Evidence

202. Based on the auditor's understanding of the ADI and/or ADI group, risk management practices in place, and the internal control and compliance framework, as obtained for the purpose of planning the engagement, the auditor performs assurance procedures to respond to assessed risks in order to obtain limited assurance to support the auditor's conclusion.

203. The auditor generally adopts a 'top down' approach in gathering evidence by, for example, making enquiries of key personnel, observing the entity's operations, performing 'walk-through' tests of controls, and inspecting relevant documentation, in order to achieve the following:

- obtaining an understanding of the ADI's overall control environment and compliance framework;
- identifying the internal compliance system(s) designed to ensure compliance with all applicable Prudential Requirements;
- identifying the systems, structures, policies, procedures and controls which address compliance with all applicable Prudential Requirements, by reviewing documents such as the Risk Management Strategy and similar policy documents required under applicable Prudential Standards;
- identifying the processes used by the entity to support the Board's annual declaration to APRA on risk management ('Risk Management Declaration'[73]);
- identifying the internal compliance functions designed to oversee the provision of data to APRA in ADI Reporting Forms;
- identifying significant processes for the preparation of ADI Reporting Forms; and
- identifying the key controls over these significant processes that are designed to ensure that reliable data is provided to APRA in ADI Reporting Forms.

The above is not an exhaustive list, nor is it intended to direct the auditor as to the conclusion over the ADI's internal controls.

204. Materiality is to be applied as outlined in paragraphs 116-122 and 142-149 of this Guidance Statement.

Design of Controls

205. The auditor determines which of the controls at the entity are necessary to achieve the relevant control objectives and whether those controls were suitably designed. Under ASAE 3150, this determination includes:

(a) identifying the risks that threaten achievement of the control objectives;

[73] Refer Attachment A to APRA Prudential Standard CPS 220 *Risk Management.*

(b) evaluating whether the controls as designed would be sufficient to mitigate those risks when operating effectively, in all material respects; and

(c) evaluating whether any changes in controls as designed during the period would be sufficient to mitigate those risks, in all material respects.

206. In assessing the suitability of the design of controls, ASAE 3150 requires the auditor, at a minimum, to:

(a) make enquiries of management or others within the entity regarding how the controls are designed to operate; and

(b) examine the design specifications or documentation.

207. If the auditor becomes aware of a matter(s) that causes the auditor to believe that a material deficiency in the design of controls may exist, ASAE 3150 requires the auditor to design and perform additional assurance procedures until the auditor has obtained sufficient appropriate evidence to conclude on whether the design is suitable. However, the performance of such additional procedures shall not convert the engagement to a reasonable assurance engagement.

Implementation of Controls

208. The auditor obtains sufficient appropriate evidence that the controls identified as necessary to achieving the identified control objectives, were implemented as designed as at the specified date. The auditor's evaluation of the design of controls may influence the nature, timing and extent of assurance procedures related to implementation.

209. ASAE 3150 requires that:

(a) the auditor's assurance procedures include, at a minimum, making enquiries and observation.

(b) if the auditor determines that additional assurance procedures, such as the inspection of records and documentation, are required to dispel or confirm a suspicion that a material deficiency in the implementation of controls exists, the performance of such additional procedures shall not convert the engagement to a reasonable assurance engagement.

(c) When designing and performing tests of implementation, the auditor determines whether controls implemented depend upon other controls (indirect controls) and, if so, whether it is necessary to obtain evidence supporting the implementation of those indirect controls.

Operating Effectiveness of Controls

210. Following the evaluation of whether the ADI has internal controls designed to achieve the relevant control objectives, the appointed auditor performs assurance procedures to obtain evidence about whether these controls have operated as designed throughout the financial year. The auditor may consider how the controls were applied, the consistency with which they were applied, by whom they were applied and the period over which the controls were applied.

211. In accordance with ASAE 3150, when reporting on operating effectiveness over the period, the auditor tests those controls that the auditor has determined are necessary to achieve the relevant control objectives, and assess their operating effectiveness throughout the period. The auditor's evaluation of the design of controls may influence the nature, timing and extent of tests of operating effectiveness. Evidence obtained in prior engagements about the satisfactory operation of material controls in the prior periods does not provide a basis for a

reduction in testing of those controls, even if it is supplemented with evidence obtained during the current period.

212. Assurance procedures to obtain evidence on operating effectiveness may include discussion with entity personnel (and obtaining written representations), observation of the system in operation, walk-through for an appropriate number of instances of material controls in operation, and ascertaining whether the person(s) performing the control(s) possesses the necessary authority and competence to perform the control(s) effectively, to identify any deviations from the specified design. The auditor may also consider limited re-performance of controls.

213. Alternatively, under ASAE 3150, the results of exception reporting, monitoring or other management controls may be examined to provide evidence about the operation of the control rather than directly testing it.

214. ASAE 3150 requires the auditor to apply professional judgement in determining the specific nature, timing and extent of procedures to be conducted, which will depend on the assessed risks of material deviations in the operating effectiveness of controls. If the auditor determines that additional assurance procedures are required to dispel or confirm a suspicion that a material deviation in the operating effectiveness of controls exists, the performance of such additional procedures shall not convert the engagement to a reasonable assurance engagement.

215. ASAE 3150 requires that where control procedures have changed during the period subject to examination, the auditor tests the operating effectiveness of both the superseded control(s) and the new control(s) and consider whether the new controls have been in place for a sufficient period to assess their effectiveness.

216. Although the auditor may consider the results of any tests of the operating effectiveness of controls conducted by the internal audit function when evaluating operating effectiveness, the auditor remains responsible for obtaining sufficient appropriate evidence to support the auditor's conclusion and, if appropriate, corroborate the results of such tests.

217. The appointed auditor enquires whether there were any changes in internal control, or other matters, subsequent to the financial year-end date and up to the date of the appointed auditor's assurance report, that may have an impact on the appointed auditor's conclusion about the effectiveness of internal controls, and obtains written representations from management relating to such matters.

218. Interpretation of the word 'reliable' in the context of reporting on controls in place to ensure reliable data is provided to APRA in ADI Reporting Forms throughout the financial reporting period, has practical limitations in some circumstances. For many ADIs, it is only at the financial year-end (or for ADIs that are disclosing entities, also at the half year-end) that all the necessary accounting adjustments, such as accruals, prepayments, provisioning and valuations, are prepared and subjected to audit or review. APRA is aware of this position and has indicated it accepts ADI Reporting Forms prepared throughout the year based on the ADI's normal accounting process.

219. For further requirements and guidance in relation to obtaining evidence on operating effectiveness of controls, including on the use of sampling for selecting controls for testing operating effectiveness over a period, refer to ASAE 3150.

Advanced ADIs

220. For an Advanced ADI, the appointed auditor furthermore considers the ADI's internal controls over the risk measurement models used to meet the requirements of specific Prudential Standards and to generate certain risk data provided to APRA in ADI Reporting Forms.

221. The appointed auditor undertakes an appropriate risk assessment of the controls over these models within the context of the stated assurance engagement objective, and plans the assurance engagement accordingly.

222. The appointed auditor obtains an understanding of any deficiencies in the models, identified either by APRA, the ADI, or through any independent review, and how such deficiencies have been addressed by the ADI.

223. In concluding on the controls over internal risk models, the appointed auditor cannot place sole reliance on the work performed by APRA during the accreditation process to become an Advanced ADI, or on reports issued as a result of any independent review[74] required under specific Prudential Standards dealing with credit risk, operational risk, market risk and interest rate risk in the banking book[75]. Under these Standards, APRA may require Advanced ADIs to obtain an independent review of the use of any internal models, statistical techniques, other methods relevant to estimating or assessing risks, and risk data inputs used.[76]

224. The appointed auditor reviews any reports issued as a result of independent reviews. In drawing a conclusion on whether to use these reports, the appointed auditor has regard to the level of independence of the reviewer, and their qualifications and competency to carry out such a review. In making this assessment, the appointed auditor complies with the requirements of ASAE 3000.

225. The appointed auditor makes enquiries about the overall system controls over such models, including controls that ensure the consistency and integrity of the models.

226. Assurance procedures over the models would ordinarily include a review of:

- the control environment and general controls, including the IT function; and
- change controls (including limited testing).

227. Assurance procedures of data produced from the risk measurement models would ordinarily include a review of:

- the key controls over inputs to the models; and
- how management review and use the data outputs from the models in ADI Reporting Forms.

Such assurance procedures may include making enquiries of management and persons operating the control(s), assessing whether such persons have the appropriate degree of skill and authority to effectively operate the control(s), observation, 'walk through' tests, limited re-performance and analytical review of the resulting Reporting Forms, or data items in a Reporting Form.

[74] To be undertaken by a party or parties who are independent within the meaning of the relevant APRA Prudential Standards.

[75] For example, APS 115 includes a requirement for an independent review of the ADI's operational risk management framework, both initially at the time that approval is sought from APRA to use the advanced approach and, thereafter, on an ongoing basis (at least once every three years or when a material change is made to the framework).

[76] The scope of an independent review of an Advanced ADI's risk management framework, may cover the following:

- the accuracy of the analytics underlying the calculation of the risk adjusted regulatory capital, the outputs of the risk measurement model and the consistency of this methodology;
- assessment of the reasonableness of any assumptions made in the risk measurement model;
- the accuracy and adequacy of documentation supporting the quantitative aspects of the risk measurement system; and
- the continuing appropriateness and adequacy of the risk modelling approach given industry developments in the modelling of risk.

The scope of an independent review of the risk data inputs to the internal risk models (to ensure the continued quality of the data and the effectiveness of internal controls) ordinarily includes an assessment of the controls surrounding the data collection and maintenance processes, as well as data inspection.

Limited Assurance on Controls addressing Generation of Single Customer View (SCV) Data and Financial Claims Scheme (FCS) Payment Instruction and Reporting Information (APS 910)

Reporting Requirements

228. The auditor is required to express a conclusion, based on a limited assurance engagement, whether anything has come to the attention of the auditor to cause the auditor to believe that, for the financial year, in all material respects:

    (a) the ADI and ADI group has not implemented internal controls that are designed such that SCV data as set out in APS 910 Attachment A, to the extent practicable, and FCS payment instruction and reporting information, can be relied upon as being complete and accurate and in accordance with APS 910; and

    (b) these controls have not operated effectively when tested.

    Refer to Appendix 6 of this Guidance Statement for an Example Annual Prudential Assurance Report for engagements undertaken pursuant to APS 910.

AUASB Standards

229. The auditor conducts the limited assurance engagement for APS 910 related to internal controls in accordance with ASAE 3150.

Gathering Evidence

230. In practice, the auditor's APS 910 assurance engagement will be undertaken as part of the annual APS 310/3PS 310 assurance engagement on controls. Refer to paragraphs 200-227 of this Guidance Statement.

231. Under APS 310/3PS 310, the auditor is required to perform a limited assurance engagement on the design, implementation and operating effectiveness of internal controls to ensure compliance with all Prudential Requirements, which includes compliance with the requirements of APS 910.

232. APS 910 identifies additional requirements for the auditor to perform a limited assurance engagement on an ADI's control procedures to ensure that SCV data, to the extent practicable, and FCS payment and reporting information can be relied upon as being complete and accurate and produced in accordance with the requirements specified in APS 910.[77]

233. Limited assurance procedures selected depend on the auditor's judgement, including assessment of the risks of a material breakdown in controls. In making those risk assessments, the auditor considers internal control systems relevant to the requirements in relation to SCV data and FCS payment and reporting information, in order to design limited assurance procedures that are appropriate in the circumstances.

234. The limited assurance engagement in relation to control procedures as required under APS 910 may include making enquiries, primarily of those responsible for the control procedures, and applying analytical and other limited assurance procedures, including 'walkthrough' of the controls and review of reports required under APS 910.[78]

[77] For example, refer to paragraph 6 of Attachment A to APS 910.
[78] For example, refer to paragraph 20 of APS 910.

235. When assessing whether controls can be relied upon as being 'complete and accurate', the auditor has regard to definitions and guidance provided by APRA in CPG 235.[79]

236. For guidance on how the term 'to the extent practicable' is to be interpreted, the auditor refers to guidance provided by APRA in its August 2013 information paper and under 'Frequently Asked Questions', which can be accessed on APRA's website.[80]

237. The phrase 'to the extent practicable' applies to those limited circumstances where it may not be possible for an ADI to meet a particular requirement despite best endeavours.[81] Where possible, it is expected that the underlying assurance objective be met in full. This guidance is principle-based and does not limit the application of the auditor's professional judgement.

Evaluation of Findings

238. The auditor accumulates uncorrected misstatements, deficiencies, deviations and non-compliance identified during the engagement, other than those that are clearly trivial.

239. In evaluating whether uncorrected misstatements, deficiencies, deviations and non-compliance that have come to the auditor's attention are material to the reported information (either individually or in aggregate) the auditor complies with the requirements of ASA 450 *Evaluation of Misstatements Identified during the Audit*, ASRE 2405, ASAE 3000, ASAE 3150 and ASAE 3450, as applicable.

240. Materiality is to be applied in the context of paragraphs 116-151 of this Guidance Statement.

Reporting on Specified ADI Reporting Forms (Parts A and B)

241. In evaluating whether or not the Specified ADI Reporting Forms, or data included in Reporting Forms, are, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards, the appointed auditor exercises professional judgement, having regard to both the user and intended uses of the information in the Reporting Forms, and taking into consideration the risk of issuing an inappropriate assurance report.

242. The magnitude of a misstatement alone is only one factor used to assess the misstatement. The appointed auditor evaluates each identified misstatement in the context of information relevant to users of the Reporting Form, by considering qualitative factors and the circumstances in which each misstatement has been made. For example, in evaluating identified misstatements, the appointed auditor has regard to factors such as the level of the ADI's buffer above the particular minimum Prudential Requirements (determined under periodic quantitative calculations) and the sensitivity of these buffers to fluctuations in the ADI's financial performance and position.

243. The appointed auditor may designate an amount below which misstatements need not be aggregated, because the auditor expects that the aggregation of such amounts clearly would not have a material effect on the reported information. In doing so, the appointed auditor needs to consider the fact that the materiality of misstatements involves qualitative as well as quantitative considerations and that misstatements of a relatively small amount could nevertheless have a material effect on the reported information.

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[79] For example, the terms 'completeness' and 'accuracy' are defined in paragraph 16 of CPG 235.

[80] Refer to APRA's website:
- APRA Information Paper: *Financial Claims Scheme for ADIs*, August 2013, paragraph 37 on page 11.
- *Financial Claims Scheme – Frequently Asked Technical Questions for ADIs*, under *Section 3 Clearance* (Question 3.1, March 2014) and *Section 12 – Single Customer View (SCV)* (Question 12.2, March 2014).

See: https://www.apra.gov.au/industries/authorised-deposit-taking-institutions.

[81] For example, where an ADI has been unable to obtain or update data required to be provided by a retail customer, and the ADI has exhausted all practical steps to contact the customer.

244. In evaluating whether identified misstatements are material, the auditor will consider the criteria used by APRA and the Agencies to determine the need for re-submission of data. For example, in accordance with RPG 702.0 guidance, reporting entities are to notify APRA of all 'reportable errors' based on the precision levels specified in RPG 702.0 and states that, depending on the size of the reporting entity and the potential impact on the Agencies' use of the data, APRA, in consultation with the Agencies, may require the data to be resubmitted.

245. However, where errors have occurred in relation to EFS reporting that exceed the RPG 702.0 data quality thresholds, this may be indicative of a control environment that is not appropriately designed or operating effectively. In these instances, the auditor would be expected to assess the nature of the error, whether deficiencies in the control environment contributed to the error, and what subsequent changes have occurred (if any) to address such deficiencies. Where such deficiencies exist, the significance of these would need to be considered against Parts A, B and C of the APS 310/3PS 310 opinion and conclusions.

246. In circumstances where the appointed auditor conclude that information reported in ADI Reporting Forms is not in accordance with the relevant APRA Prudential and Reporting Standards, the appointed auditor discusses the matter with management and, depending how it is resolved, determines whether, and how, to communicate the matter in the auditor's assurance report.

Reporting on Internal Controls (Part C)

247. ASAE 3150 sets out the requirements and provides guidance to the auditor to assist in evaluating evidence and forming a conclusion on controls.

248. In accordance with ASAE 3150, the auditor accumulates uncorrected:

(a) deficiencies in the suitability of the design of controls to achieve the relevant control objectives;

(b) deficiencies in the implementation of controls as designed; and

(c) deviations in the operating effectiveness of controls as designed.

249. The appointed auditor evaluates, individually and in aggregate, whether internal control deficiencies and deviations that have come to the auditor's attention are material. The appointed auditor exercises professional judgement in evaluating the materiality of internal control deficiencies and deviations, having regard to the intended users of the auditor's assurance report.

250. In evaluating the severity of identified internal control deficiencies, the appointed auditor considers, based on materiality:

(a) the likelihood that the relevant internal controls may fail to prevent or detect:

(i) non-compliance with a Prudential Requirement; or

(ii) a misstatement in the data being provided to APRA in ADI Reporting Forms; and

(b) the magnitude of the potential resulting non-compliance with a Prudential Requirement on the ADI's overall compliance with applicable Prudential Requirements; and

(c) the magnitude of the potential misstatement resulting from the internal control deficiency on the information reported in the ADI Reporting Forms.

251. The evaluation of the severity of a deficiency in internal control does not depend on whether a misstatement or non-compliance with a Prudential Requirement has actually occurred, but rather the likelihood that the ADI's controls may fail to prevent or detect a material misstatement or material non-compliance with a Prudential Requirement.

252. As noted above, the auditor is not required to use RPG 702.0 benchmarks as materiality thresholds for planning the scope of the assurance engagement. However, where the auditor identifies reporting errors as defined by RPG 702.0 it is expected that this be taken into consideration in assessing the adequacy of the design and implementation of controls around data quality.

253. The auditor considers how the ADI has incorporated RPG 702.0 thresholds and other relevant guidance, for example CPG 235, into their risk management processes. Should an ADI identify errors that have occurred in relation to EFS reporting that exceed the data quality thresholds, this may be indicative of a control environment that is not appropriately designed, implemented or operating effectively to ensure entities have provided reliable data to APRA. In these instances, the auditor would be expected to assess the nature of the error, whether deficiencies in the control environment contributed to the error, and what subsequent changes have occurred (if any) to address such deficiencies and/or deviations. Where such deficiencies exist, the significance of these would need to be considered against Parts A, B and C of the APS 310/3PS 310 opinion and conclusions.

254. EFS reporting introduces new concepts and data that may not, historically, have been subject to an ADI's risk management framework in accordance with the expectations of RPG 702.0 and CPG 235. Therefore, whilst an ADI may have implemented additional processes and controls that address the reliability of information for the front book, for example, loans originated since the implementation of EFS reporting, the accuracy of the back book (existing portfolio) with respect to RPG 702.0 and CPG 235 remains uncertain. In these instances, the auditor will need to assess the significance of the matter and its impact on Part B and C of the APS 310/3PS conclusion.

255. Resubmission of data and reporting forms by an entity will require the auditor to exercise professional judgement, taking into consideration the nature and cause of the resubmission, in evaluating whether misstatements are material or if the resubmissions are indicative of a control environment that is not appropriately designed, implemented or operating effectively to ensure entities have provided reliable data to APRA.

256. Generally, the existence of multiple resubmissions of a material nature due to error would be indicative of a weak or inadequate control environment and, hence, may require modification of the Part C conclusion and, potentially, also the Part A opinion and Part B conclusion, where the impacted forms include Specified ADI Reporting Forms.

257. Notwithstanding, there may be instances where an ADI will resubmit Reporting Forms for reasons other than an error associated with its reporting process, such as changes or clarifications in APRA interpretations. Where resubmissions are not the result of errors, the auditor may determine that there is no impact on the APS 310 opinion, with reporting of resubmissions limited to an appendix to the APS 310/3PS 310 report.

258. Where material breakdowns in controls are identified which results in a modification to Part C of the auditor's conclusion, the auditor will need to assess the impact on procedures performed under Parts A and B of the APS 310/3PS 310 engagement. There may be instances where the auditor is able to perform additional substantive procedures to address the risks associated with a control deficiency and/or deviation that will support an unmodified opinion for Parts A and B of the report, but result in a qualification to Part C.

Reporting on Compliance with Prudential Requirements (Part D)

259. Based on work performed in the reasonable and limited assurance engagements on Specified ADI Reporting Forms (Parts A and B) and the limited assurance engagement on internal

controls (Part C) the auditor accumulates identified instances of non-compliance, other than those that are clearly trivial, in order to form a conclusion.

260. The appointed auditor considers materiality when assessing the significance of identified instances of non-compliance with relevant Prudential Requirements.

261. The APS 310 requirement to report matters of non-compliance to APRA on an annual basis, is in addition to the reporting obligations under section 16BA of the Banking Act, which requires certain matters to be reported to APRA immediately and certain other matters to be reported to APRA as soon as is practicable.[82].

262. Section 16BA(7) of the Banking Act defines the term 'significant' in the context of matters that are required to be notified to APRA by the appointed auditor as part of the auditor's additional statutory reporting responsibilities under the Banking Act[83].

263. The significance of a matter is to be judged by the appointed auditor in the context in which it is being considered, taking into account both quantitative and qualitative factors. This may, for example, include consideration of the significance of the potential impact of the non-compliance rather than the actual impact.

264. Furthermore, it is possible that an instance of non-compliance, which is not significant in isolation, may become so when considered in totality with other identified instances of non-compliance.

265. Where the appointed auditor considers identified instances of non-compliance as being potentially significant to the ADI as a whole and/or to its depositors' interests, or where the matter may be considered important by APRA in performing its functions under the Act, then the identified instance of non-compliance is a matter to be reported to APRA.

266. In order to conclude on an ADI's compliance with all relevant Prudential Requirements, the appointed auditor considers the existence of relevant matters, that may indicate instances of non-compliance, throughout the reporting period and up to the date of signing the auditor's assurance report.

267. The appointed auditor's review of subsequent events may include the following procedures:

- reading minutes of the ADI's Board, as well as minutes of any sub committees responsible, for example, for compliance and audit, held after balance date and enquiring about matters discussed at these meetings for which minutes are not yet available;
- examining the ADI's breach registers up to the date of the auditor's assurance report; and
- enquiring of the ADI's management as to whether any subsequent events have occurred which might represent non-compliance with relevant Prudential Requirements.

268. The appointed auditor reports instances of significant non-compliance which have not previously been reported to APRA by the appointed auditor. This will include matters the ADI indicated it was notifying, and which an auditor relied upon as a reason for the auditor not notifying APRA.[84]

[82] See paragraphs 313-327 of this Guidance Statement.
[83] See paragraphs 326 of this Guidance Statement.
[84] Under subsections 16BA(5) and 16BA(10) of the Banking Act, an auditor is not required to notify APRA of matters that have been brought to the auditor's attention by the ADI, where the auditor is informed that APRA has been notified of the matter in writing by the ADI and the auditor has no reason to disbelieve the ADI.

Foreign ADIs[85]

269. Prudential Requirements for foreign ADIs (branches) may differ from those of locally incorporated ADIs[86] and, consequently, these are considered by the appointed auditor. For example, foreign ADIs are not required to report in Australia with respect to branch capital adequacy. However, the Banking Act authority restricts the source and quantum of deposits that foreign ADIs may accept. In addition, APRA has set guidelines relating to the manner in which foreign ADIs inform depositors of the requirements of the Banking Act that do not apply to those ADIs. The appointed auditor reports to APRA on the foreign ADI's compliance with all relevant Prudential Requirements.

270. APRA requires the appointed auditor of a foreign ADI to conform to APS 310[87] and other relevant Prudential Requirements as they apply to foreign ADIs. The appointed auditor of a foreign ADI considers the individual engagement requirements and circumstances at the foreign ADI when interpreting the guidance contained in this Guidance Statement.

271. As a foreign ADI is not required to prepare a financial report under the Corporations Act, there is no requirement for a statutory financial report audit to be undertaken. Therefore, the accounting records of a foreign ADI would not generally be subjected to a full scope audit, unless the branch is included in the scope of the foreign ADI group audit, where the audit arrangements will be driven by head office audit requirements and applying materiality relevant to the entire group.

272. Since, generally, the appointed auditor of a foreign ADI has incomplete knowledge of the overseas operations of the foreign ADI, and would not have undertaken the statutory financial report audit of the foreign ADI, the appointed auditor considers the following additional matters (this is not a complete list):

- The reliance to be placed on work performed by overseas auditors (such as comfort or assurance in relation to systems and processes hosted offshore which impact the foreign ADI's (branch's) prudential reporting) and the requirements of ASA 600.
- The financial reporting framework applied by the foreign ADI for head office (group) reporting and whether adjustments are required to comply with APRA Prudential Requirements.
- Assessing materiality for APRA prudential reporting purposes, which may differ from materiality considerations for the purpose of head office (group) reporting.
- The requirements of Auditing Standard ASA 705 *Modifications to the Opinion in the Independent Auditor's Report*, in particular, where sufficient appropriate evidence cannot be obtained.
- In the first year of reporting, the requirements of Auditing Standard ASA 510 *Initial Audit Engagements – Opening Balances*, in particular, with respect to the level of assurance which can be provided over opening balances.

Inherent Limitations of the Engagement

273. There are inherent limitations in any internal control and compliance framework, and fraud, error or non-compliance with Prudential Requirements may occur and not be detected. As the systems, procedures and controls to ensure compliance with Prudential Requirements are part

[85] 'foreign ADIs' is defined in paragraph 31(h) of this Guidance Statement.
[86] Which includes a locally incorporated subsidiary of a foreign ADI.
[87] Under APS 310, auditors are required to provide a consistent level of assurance for foreign ADIs and locally incorporated 'stand-alone' ADIs. Refer to Attachment A of APS 310 for a complete list of foreign ADI Reporting Forms to be subjected to a reasonable and/or limited assurance engagement.

of the ADI's operations, it is possible that either the inherent limitations of the internal control structure, or weaknesses in it, may impact on the effective operation of the ADI's specific control procedures.

274. Due to the nature of assurance engagement procedures and other inherent limitations of a these engagements, there is a possibility that a properly planned and executed engagement may not detect all errors or omissions in ADI Reporting Forms, deficiencies in controls, or instances of non-compliance with Prudential Requirements.

275. Accordingly, procedures undertaken as part of the reasonable assurance engagement provides only reasonable assurance, and not a guarantee, that information in Specified ADI Reporting Forms, sourced from accounting records, are reliable. Limited assurance procedures undertaken by the appointed auditor provides only limited assurance that information in Specified ADI Reporting Forms, sourced from non-accounting records, are reliable, that internal controls have been designed and implemented, and are operating effectively throughout the period, to achieve control objectives, and that all instances of non-compliance with relevant Prudential Requirements have been detected.

276. A limited assurance engagement is substantially less in scope than a reasonable assurance engagement conducted in accordance with Australian Auditing and Assurance Standards. In a reasonable assurance engagement, as the auditor's objective is to provide a high, but not absolute, level of assurance on the reliability of information included in ADI Reporting Forms, the auditor uses more extensive audit procedures than in a limited assurance engagement. A limited assurance engagement therefore does not provide all the evidence required in a reasonable assurance engagement and, consequently, the level of assurance provided is less than that given in a reasonable assurance engagement.

277. The appointed auditor performs procedures appropriate to provide limited assurance in relation to internal controls existing at the date of the engagement, and whether those controls have operated as documented throughout the financial year. Projections of any evaluation of internal control procedures or compliance measures to future periods are subject to the risk that control procedures may become inadequate because of changes in conditions after the auditor's annual prudential assurance report is signed, or that the degree of compliance may deteriorate. Furthermore, assurance engagement procedures on accounting records and data relied on for reporting and compliance are not performed continuously throughout the period and are undertaken on a test basis only.

278. Consequently, there are inherent limitations on the level of assurance that can be provided.

Written Representations

279. Prior to issuing the auditor's annual prudential assurance report, the appointed auditor considers obtaining written representations[88] from responsible management and, where appropriate, those charged with governance of the ADI and/or ADI group, as are considered appropriate to matters specific to the ADI and/or ADI group. Separate representation letters may be requested for the purposes of reporting under APS 310/3PS 310 and APS 910.

280. These written representations are generally in the form of a representation letter. In obtaining and using these written representations, the appointed auditor complies with the requirements of, as appropriate, Auditing Standard ASA 580 *Written Representations*, ASRE 2405, ASAE 3000, ASAE 3150 and ASAE 3450.

281. Refer to Appendix 3 of this Guidance Statement for an illustrative example of the format of a representation letter, as well as examples of representations that may be considered appropriate in the specific engagement circumstances.

[88] Including written confirmation of significant oral representations.

Communication with Those Charged with Governance

282. It is the responsibility of the appointed auditor to make the ADI aware, as soon as practicable, of any identified material misstatements in ADI Reporting Forms, material deficiencies in internal controls and instances of material non-compliance arising from the prudential reporting engagement.

283. Such communications are made as soon as practicable, either orally or in writing. The appointed auditor's decision whether to communicate orally or in writing ordinarily is affected by factors such as the nature, sensitivity and significance of the matter to be communicated and the timing of the communications. If the information is communicated orally, the appointed auditor needs to document the communication.

284. When, in the appointed auditor's judgement, those charged with governance do not respond appropriately within a reasonable period, the appointed auditor considers whether to modify the auditor's annual prudential assurance report.

285. It is important that the appointed auditor understands their additional statutory responsibilities to report certain matters to APRA under the Banking Act. Failure to notify APRA as required represent criminal offences, which attracts criminal penalties.[89]

286. Material findings (misstatements, control deficiencies and non-compliance) are reported to APRA and the ADI's Board (or Board Audit Committee) as modifications to the appointed auditor's assurance report.

287. Under Auditing Standard ASA 260 *Communication with Those Charged With Governance*, ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* and ASAE 3000, the appointed auditor communicates relevant matters of governance interest arising from the engagement to those charged with governance on a timely basis. Examples of such matters may include:

    - The general approach and overall scope of the engagement, or any additional requirements.
    - Fraud or information that indicates that fraud may exist.
    - Significant deficiencies or deviations in internal controls identified during the engagement. A significant deficiency is a deficiency or combination of deficiencies in internal control relevant to the engagement that, although not material, in the appointed auditor's professional judgement is of sufficient importance to merit the attention of those charged with governance.
    - Disagreements with management about matters that, individually or in aggregate, could be significant to the engagement.
    - Expected modifications to the auditor's prudential assurance report.

288. The appointed auditor informs those charged with governance of the ADI of those uncorrected misstatements, other than clearly trivial amounts, aggregated by the appointed auditor during and pertaining to the engagement that were considered to be immaterial, both individually and in the aggregate, to the assurance engagement.

289. Under APS 310 and 3PS 310, if requested by APRA, the appointed auditor submits directly to APRA all assessments and other material associated with the auditor's report, such as

[89] Refer to paragraphs 313-327 of this Guidance Statement.

management letters issued by the appointed auditor to the ADI which contain material findings relating to the auditor's prudential assurance report(s).

The Appointed Auditor's Annual Prudential Assurance Report

290. The appointed auditor evaluates the conclusions drawn from the evidence obtained in conducting the assurance engagement as the basis for the auditor's opinion and conclusions as required, as appropriate, under APS 310, 3PS 310 and APS 910.

291. If the appointed auditor:

 (a) concludes that a material misstatement, internal control deficiency or deviation, and/or non-compliance exists; or

 (b) is unable to obtain sufficient appropriate assurance evidence to conclude whether a material misstatement, internal control deficiency or deviation, and/or non-compliance may exist,

 the appointed auditor modifies their opinion/conclusions, and includes a clear description of the reasons in their assurance report, in accordance with the requirements of, as appropriate, ASA 705 and any other applicable AUASB Standards.

292. As required under APS 310 and 3PS 310, the appointed auditor of an ADI and ADI Group generally reports simultaneously to APRA and the ADI's Board (or Board Audit Committee)[90], within three[91] months of the end of the financial year of the ADI.

293. In accordance with the requirements of APS 310 and 3PS 310, where an ADI is the head entity of a Level 2 or Level 3 group, the auditor issues either separate reports for, as applicable, Level 1, Level 2 and Level 3, or a combined report for the ADI (head entity) and the group. The auditor's report must make it clear where the auditor is referring to matters relating to the ADI (head entity) or the group.

294. To avoid the possibility of the assurance report being used for purposes for which it was not intended, the appointed auditor ordinarily indicates in the auditor's report the purpose for which the report is prepared and any restrictions on its distribution and use.

APS 910 Assurance Report

295. APRA requires the timing of the APS 910 prudential assurance engagement to be aligned with the annual APS 310 prudential assurance engagement. Separate reports may be prepared for the APS 310/3PS 310 and APS 910 engagements, but the requirement is for these reports to be submitted to APRA at the same time.

296. As there will be some overlap between APS 310/3PS 310 and APS 910 engagements, auditors may decide to prepare separate reports for these engagements, in order to reduce duplication of reporting compliance matters to APRA. APRA has released a suggested non-compulsory auditor's report which aggregates all APS 910 requirements (compliance and controls) into a single report, effectively moving the reporting from the APS 310/3PS 310 auditor's report to a separate APS 910 auditor's report. APRA indicated that this single report facilitated clearer communication with respect to APS 910 matters.

297. Where the APS 910 auditor's report is modified, this is referred to in the APS 310/3PS 310 auditor's report and may lead to a modification of the APS 310/3PS 310 auditor's report.

[90] Or, for a foreign ADI, a senior officer outside Australia to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian operations.

[91] For a non-disclosing ADI, the relevant period is four months.

Format of Auditor's Annual Prudential Assurance Report

298. The auditor has regard to the requirements, guidance and illustrative examples of reports provided in relevant AUASB Standards – ASAs, ASREs and ASAEs, as applicable, when preparing the prudential assurance report. These Standards do not prescribe a standardised format for reporting under APS 310 or 3PS 310. Instead, these Standards identify the basic elements required to be included in the assurance report. The 'short form' auditor's report ordinarily includes only the basic elements.

299. Assurance reports are tailored to the specific assurance engagement circumstances. Although not specifically required under APS 310 or 3PS 310, the appointed auditor may consider it appropriate to include other information and explanations that do not directly affect the auditor's opinion or conclusions, but provide additional useful information to the users (that is, a 'long form' style of reporting). The inclusion of this information depends on its significance to the needs of the intended users. The following are examples of additional information that may be considered for inclusion:

- Disclosure of materiality considerations (materiality levels) applied.
- Significant findings or exceptions relating to aspects of the assurance engagement.
- Recommendations.

300. The appointed auditor needs to ensure that this additional information is clearly separated from the auditor's opinion and conclusions, and worded in a manner to ensure that it does not affect the opinion and conclusions. This can be achieved, for example, by including any additional information in a:

(a) separate appendix to the auditor's short form assurance report; or

(b) separate section of the auditor's short form assurance report, under an appropriate heading.[92].

This will enable users to clearly distinguish this additional information from the auditor's responsibility to report on the matters identified in APS 310/3PS 310.

301. Refer to Appendix 4 of this Guidance Statement for an illustrative example of the auditor's annual prudential assurance report (short form report), prepared pursuant to APRA's APS 310 and 3PS 310 annual reporting requirements.

Special Purpose Engagements

APRA Prudential Reporting Requirements

302. Under APS 310 and 3PS 310, in addition to the annual prudential reporting requirements (routine reporting), APRA may require an ADI, by notice in writing, to appoint an auditor (who may be the existing auditor appointed under APS 310 and/or 3PS 310, or another auditor), to provide a report on a particular aspect of the ADI's and/or the ADI group's operations, prudential reporting, risk management systems or financial position. Although a special purpose engagement report will normally only be requested following consultation with an ADI, APRA may commission such a report without prior consultation with an ADI. Unless otherwise determined by APRA in writing, an auditor appointed to undertake a special purpose engagement will be required to provide limited assurance on the matters required to be reported on.

[92] See examples of assurance reports included in *Appendix 6* of ASAE 3100.

303. Under APS 910, in addition to the annual prudential reporting requirements (routine reporting), APRA may, in writing, require an ADI to engage an auditor to undertake a reasonable or limited assurance engagement of SCV systems and data, and the systems used to generate and transmit FCS payment and reporting information.

304. The appointed auditor's special purpose engagement assurance report is generally to be submitted simultaneously to APRA and those charged with governance of the ADI and/or ADI group, within three months of the date of the notice commissioning the report, unless otherwise determined by APRA, and advised to the ADI by notice in writing.

305. The APRA requirement for an auditor to undertake a special purpose engagement in a selected area of the ADI's and/or ADI group's operations, prudential reporting, risk management systems or financial position constitutes a separate reporting engagement. The details of the engagement will normally be the subject of a specific request from APRA to the ADI and a separate engagement letter from the ADI to the appointed auditor based on that request.

Terms of the Engagement

306. Following the determination by APRA of the specific area to be examined, the appointed auditor, APRA and the ADI agree on the terms of the engagement in accordance with the requirements of applicable AUASB Standards. These arrangements are legally binding and include the required terms of engagement specified in APS 310 and 3PS 310.

307. The appointed auditor accepts the engagement only when satisfied that relevant ethical requirements relating to the assurance engagement have been met. The concept of independence is important to the appointed auditor's compliance with the fundamental ethical principles of integrity and objectivity and the auditor must be able to meet the independence requirements stipulated under both CPS 510 and ASA 102.

308. An engagement letter[93] confirms both the client's and the appointed auditor's understanding of the terms of the engagement, helping to avoid misunderstanding, and the auditor's acceptance of the appointment. Both parties sign the engagement letter to acknowledge that it is a legally binding contract.

309. To ensure that there is a clear understanding regarding the terms of the engagement, the following are examples of matters to be agreed:

- APRA is to identify the scope of the ADI's operations, prudential reporting, risk management or financial position to be the subject of the engagement.
- The appointed auditor, APRA and the ADI are to agree on the objectives of the engagement, key features and criteria of the area(s) to be examined, and the period to be covered by the engagement.
- APRA is to identify clearly the level of assurance required, that is, limited or reasonable assurance.
- The format of reports required (for example, long and/or short form reports) or other communication of results of the engagement.
- Responsibility of those charged with governance for the subject matter of the engagement.
- Understanding of the inherent limitations of an assurance engagement.

[93] Or other suitable form of written agreement.

Format of Reporting Requirements

310. The appointed auditor has regard to the requirements, guidance and illustrative examples of reports provided in relevant AUASB Standards - ASAs, ASREs and ASAEs, as applicable, when preparing the special purpose assurance report. These Standards do not require a standardised format for special purpose reporting under APS 310 or 3PS 310. Instead, these Standards identify the basic elements to be included in the auditor's report.

311. Ordinarily, the appointed auditor adopts a long form style of reporting and the report may include a description of the terms of the engagement, materiality considerations applied, the assurance approach, findings relating to particular aspects of the engagement and, in some cases, recommendations.

312. The appointed auditor's assurance report is to be restricted to the parties that have agreed to the terms of the special purpose engagement, namely the ADI and APRA, as well as other parties that APRA is lawfully entitled to share the information with.

Additional Reporting Requirements under the Banking Act

313. It is important that the auditor[94] of:

(a) an ADI; or

(b) an authorised NOHC; or

(c) a subsidiary of an ADI or authorised NOHC; or

(d) if the ADI[95] is a subsidiary of a foreign corporation:

(i) another subsidiary (a relevant Australian-incorporated subsidiary) of the foreign corporation (other than an ADI listed in paragraphs (a), (b) or (c) above), being a subsidiary that is incorporated in Australia; or

(ii) another subsidiary (a relevant foreign-incorporated subsidiary) of the foreign corporation (other than an ADI listed in paragraphs (a), (b) or (c) above), being a subsidiary that is not incorporated in Australia and carries on business in Australia;

understands the additional responsibilities to report to APRA under sections 16B, 16BA and 16C of the Banking Act.

314. An auditor risks committing an offence under the Banking Act for any contravention of sections 16B and 16BA of that Act. Under section 6B of the Banking Act, the Criminal Code 1995 applies to all offences against the Banking Act[96].

315. Part VIA of the Banking Act include provisions to protect an auditor providing information to APRA, in good faith and without negligence, from any action, claim or demand by, or any liability to, any other person in respect of the information.

Auditors to Give Information to APRA on Request

316. Under section 16B of the Banking Act, APRA may give written notice to a person who is, or who has been, the auditor of an ADI listed in paragraph 313 above, to provide information, or to produce books, accounts or documents, about such entities to APRA, if APRA considers

94 Including the auditor appointed under APS 310 and 3PS 310.
95 Whether or not the ADI is itself a foreign ADI.
96 Criminal penalties include provisions for terms of imprisonment.

that the provision of such information will assist APRA in performing its functions under the Act.

Requirement for Auditors to Give Information about ADIs

317. Section 16BA of the Banking Act identifies matters of which APRA needs to be notified of:

(a) immediately, if the auditor has reasonable grounds for believing that, for example:

(i) the ADI is insolvent, or there is a significant risk that the ADI will become insolvent; or

(ii) an existing or proposed state of affairs may prejudice materially the interests of depositors of the ADI; and

(b) *as soon as is practicable*[97], if the auditor has reasonable grounds for believing that an ADI has failed to comply with a provision of:

(i) the Banking Act, the Regulations, or the FSCODA; or

(ii) a Prudential Standard; or

(iii) a Direction under Division 1BA of Part II of the Banking Act; or

(iv) a condition of its authority;

(v) and the failure to comply is or will be *significant*[98].

318. Under the Banking Act, these matters are to be reported to APRA in writing.

Auditor may Provide Information to APRA

319. Section 16C of the Banking Act provides that a person who is, or who has been, the auditor of an ADI listed in paragraph 313 above, may provide information, or produce books, accounts or documents, about such entities to APRA, if the person considers that the provision of that information to APRA will assist APRA in performing its functions under the Banking Act or the FSCODA.

320. Under the Banking Act, these matters are to be reported to APRA in writing, as soon as practicable, and in any case within 28 days, after the auditor becomes aware of those circumstances.

Discussion of Additional Reporting Requirements under the Banking Act

321. Sections 16B, 16BA, 16C and 16 D of the Banking Act is applicable to all and any auditor of an ADI, authorised NOHCs, or their subsidiaries, not only to auditors appointed by an ADI to meet the prudential requirements under APS 310.

322. In relation to reporting under sections 16B and 16BA of the Banking Act, there is no requirement for the appointed auditor of an ADI to carry out additional work to satisfy the auditor with respect to the above matters. The appointed auditor reports to APRA on the basis of, for example:

[97] No longer than 10 business days.

[98] For the purpose of this paragraph, the term 'significant' is defined in subsection 16BA(7) of the Banking Act. See paragraph 326 of this Guidance Statement.

(a) information obtained during the course of the auditor's financial report audit [and review] under the Corporations Act;

(b) additional reasonable and limited assurance procedures undertaken for APRA prudential reporting purposes (pursuant to APS 310 and 3PS 310, or in accordance with the requirements of another specific APRA Prudential Standard);

(c) other audit work undertaken at the ADI (for example, Australian Financial Services Licence audits); and

(d) the appointed auditor's current knowledge of the ADI's affairs at the time of issuing the auditor's assurance report.

323. In circumstances where the appointed auditor identifies that a reportable matter may exist, the auditor carries out such additional work as considered appropriate, to determine whether the facts and circumstances provide reasonable grounds for believing that the matter does in fact exist. In reaching this conclusion, the auditor exercises professional judgement and seeks appropriate legal advice if necessary.

324. The ADI may also notify APRA of the matter(s) identified by the appointed auditor, and provide details of any action(s) taken, or to be taken, in response. However, such notification by the ADI does not relieve the appointed auditor of the statutory obligation to report directly to APRA.

325. Matters likely to prejudice materially the interests of depositors are related generally to capital adequacy, solvency and going concern matters, for example, the ADI's compliance with minimum capital levels as per APRA Prudential Standard APS 110[99].

326. In determining whether a failure to comply with Prudential Requirements is or will be significant, the appointed auditor considers the factors listed in subsection 16BA(7) of the Banking Act, namely:

(a) the number or frequency of similar failures;

(b) the impact the failure has or will have on the ADI's ability to conduct its business;

(c) the extent to which the failure indicates that the ADI's arrangements to ensure compliance with the Banking Act, the Prudential Standards or the Regulations might be inadequate;

(d) the actual or potential financial loss arising, or that will arise from the failure, to the depositors of the ADI or to the ADI; and

(e) any matters prescribed by the Regulations for the purposes of this subsection of the Banking Act.

327. In assessing whether the interests of depositors may be prejudiced materially, the appointed auditor considers not only a single activity or a single deficiency in isolation, as depositors' interests may be prejudiced materially by a number of activities or deficiencies which, although not individually material, do amount to a material threat when considered in totality. Similarly, it is possible that a breach in compliance, although not significant in isolation, may become so when considered in the context of other possible breaches.

[99] Materiality is addressed in paragraphs 116-151 of this Guidance Statement.

Conformity with International Pronouncements

328. As this Guidance Statement relates to Australian legislative requirements, there is no equivalent International Standard on Auditing or International Auditing Practice Note to this Guidance Statement.

Appendix 1

(Ref: Para. XXX)

OUTLINE OF AUDITOR'S REPORTING REQUIREMENTS, LEVELS OF ASSURANCE, SUBJECT MATTER, CRITERIA AND APPLICABLE AUAUSB STANDARDS

The following table outlines the relevant reporting requirements applicable to the appointed auditor of an ADI reporting pursuant to APRA's Prudential Standards APS 310 and 3PS 310 *Audit and Related Matters*, the level of assurance required, subject matter, criteria and relevant AUASB Standards. The table is not intended to be an exhaustive summary of an appointed auditor's obligations and requirements which are found in the *Banking Act 1959* (Banking Act), the *Financial Sector (Collection of Data) Act 2001*, APRA Prudential and Reporting Standards, other relevant APRA Prudential Requirements, applicable AUASB Standards, and other relevant mandates.

APS 310/3PS 310 Prudential Reporting Requirements

A. Annual Prudential Reporting Engagements under APS 310				
Assurance Engagement Report	**Level of Assurance**	**Subject Matter**	**Assessment Criteria**	**Applicable AUASB Standards**
PART A – Assurance on Specified[36] ADI Reporting Forms	Reasonable assurance	Information included in Specified[36] Reporting Forms at the financial year-end of the ADI, sourced from *accounting records* – historical financial information, for example: financial performance, financial position.	Information is reliable and in accordance with relevant APRA Prudential and Reporting Standards.[100]	All relevant Auditing Standards.

[100] Including relevant APRA Guidance materials (for example: Prudential and Reporting Practice Guides) and Reporting Form Instructions issued by APRA.

PART B – Assurance on Specified[36] ADI Reporting Forms	Limited assurance	Information included in Specified[101] Reporting Forms at the financial year-end of the ADI, sourced from *non-accounting records*: • Historical financial information • Information other than historical financial information • Assumptions and methodology used as basis for prospective financial information	Information is reliable and in accordance with relevant APRA Prudential and Reporting Standards. Reasonableness of assumptions and calculation methodology used.	As applicable: ASAE 3000 ASRE 2405 ASAE 3450
PART C (i) – Assurance on Design and Operating Effectiveness of Internal Controls to ensure Compliance with Prudential Requirements	Limited assurance	Internal Controls	To ensure: • Compliance with *all* applicable APRA Prudential Requirements • Applicable controls operated effectively throughout the financial year	ASAE 3000 ASAE 3150
PART C (ii) – Assurance on Design and Operating Effectiveness of Internal Controls to ensure Reliability of Data in Reporting Forms	Limited assurance	Internal Controls .	To ensure: • Data provided to APRA in *all* Reporting Forms prepared under the FSCODA are reliable and in accordance with relevant APRA Prudential and Reporting Standards. • Applicable controls operated effectively	ASAE 3000 ASAE 3150

[101] For a listing of ADI Reporting Forms subject to audit and/or review, refer to APRA Prudential Standard APS 310 *Attachment A – Data Collections subject to reasonable and/or limited assurance*.

			throughout the financial year	
PART D – Reporting on Compliance with Prudential Requirements	Limited assurance	All of the above.	Compliance with all relevant Prudential Requirements.	No requirement for an appointed auditor to carry out additional audit or review procedures. Auditor may consider principles and guidance provided in ASAE 3100. .

B. Special Purpose Engagements under APS 310/3PS 310			
Level of Assurance	**Subject Matter**	**Assessment Criteria**	**Applicable AUASB Standards**
Limited assurance[102]	Particular aspect of an ADI's [Level 3 group's] operations, prudential reporting, risk management systems or financial position, as determined by APRA.	As determined by APRA.	ASAE 3000 and other relevant topic specific ASAEs, for example ASAE 3100 and/or ASAE 3150.

102 Unless otherwise determined by APRA.

Additional Reporting Requirements under the Banking Act[103]

Section of Banking Act	**Statutory Reporting Requirement**	**Applicable AUASB Standards**
Section 16B	Duty to provide information to APRA on request.	No requirement for an auditor to carry out additional audit or review procedures.
Section 16BA	Requirement to provide information to APRA where the auditor possesses specified reportable information. Section 16BA identifies matters of which APRA needs to be notified of: immediately; and as soon as is practicable (no longer than 10 business days).	
Section 16C	Auditor may provide information to APRA where the auditor considers that the provision of such information would assist APRA in performing its functions under the Banking Act or FSCODA.	

103 Sections 16B, 16BA and 16C of the Banking Act is applicable to *all* auditors of ADIs, authorised NOHCs, or their subsidiaries, not only to auditors appointed by an ADI to meet the prudential reporting requirements under APS 310.

Appendix 2

EXAMPLE ENGAGEMENT LETTER – LEVEL 1 ADI AND/OR LEVEL 2 ADI GROUP

Engagements undertaken pursuant to APRA Prudential Standard APS 310 *Audit and Related Matters* and APS 910 *Financial Claims Scheme* (Annual Reporting)

The following example engagement letter is to be used as a guide only and will need to be adapted according to individual engagement requirements and circumstances of the ADI and/or ADI Group.

Note:

1. In this example engagement letter, the ADI on a 'Level 1' basis is referred to as 'the ADI'. The group of which the ADI is a member on a 'Level 2 basis', is referred to as 'the ADI Group'.
2. If the engagement letter also covers a 'Level 3' conglomerate group, this fact must be indicated by using the appropriate terminology throughout the letter. [104]
3. Under APS 310 separate auditors may be appointed to meet the APS 310 reporting requirements on a Level 1 and Level 2 basis.
4. 'Level 1', 'Level 2' and 'Level 3' have the meaning given in APRA Prudential Standards APS 001 and 3PS 001 *Definitions*.
5. APS 910 applies only to locally incorporated ADIs. References to APS 910 should be removed where APS 910 is not relevant to the ADI, for example, foreign ADIs (branches).

[104] APRA Prudential Standard 3PS 310 *Audit and Related Matters* sets out the prudential reporting requirements for Level 3 groups.

To [Appropriate Addressee[105]] of the ADI [and/or head entity of the ADI Group]

We are pleased to confirm the [acceptance/continuation] of our appointment as auditor of [Name of ADI] for both Level 1 ADI (the ADI) and the Level 2 ADI Group (the ADI Group) for the purposes of the Australian Prudential Regulation Authority's (APRA's) Prudential Standard APS 310 *Audit and Related Matters* (APS 310) [and APS 910 *Financial Claims Scheme* (APS 910)].

APS 310 identifies APRA's reporting requirements for appointed auditors of ADIs and appointed group auditors of ADI Groups. We set out below, in general terms, our understanding of the terms, objectives and scope of this engagement, as well as a description of the responsibilities of both those charged with governance of the ADI [and/or the ADI Group] and the appointed auditor.

This engagement is a separate engagement from our audit [and half-year review] appointment(s) under the *Corporations Act 2001* (Corporations Act).

Objective and Scope of Engagement

APS 310 requires us to report simultaneously, on an annual basis, to APRA and your [Title of those charged with governance[106]] on the matters set out below, insofar as they relate to the ADI [and/or the ADI Group].

In accordance with APS 310 we are required to provide:

(a) reasonable assurance that the information, sourced from the ADI's [and/or the ADI Group's] accounting records, included in the ADI Reporting Forms at the financial year-end as specified in Attachment A of APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(b) limited assurance, unless otherwise indicated by APRA in writing, that the information, sourced from non-accounting records, included in the ADI Reporting Forms at the financial year-end as specified in Attachment A of APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(c) limited assurance that, in all material respects:

  (i) the ADI [and/or the ADI Group] have implemented internal controls that are designed to ensure:

    a. compliance with all applicable Prudential Requirements; and

    b. reliable data is provided to APRA in the ADI Reporting Forms prepared under the *Financial Sector (Collection of Data) Act 2001* (FSCODA); and

  (ii) the controls in (c)(i) have operated effectively throughout the financial year; and

(d) limited assurance, based on our work under (a) to (c) above, that the ADI [and/or the ADI Group] have complied, in all material respects, with all relevant Prudential Requirements under the *Banking Act 1959* (Banking Act) and the FSCODA, including compliance with APRA Prudential and Reporting Standards during the financial year.

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105 Amend to reflect the appropriate addressee of the report, for example, 'Chairman of Board or Board Audit Committee' for a locally incorporated ADI or, for a foreign ADI, 'Senior Officer Outside Australia' to whom authority has been delegated in accordance with APRA Prudential Standard CPS 510 *Governance*, for overseeing the Australian branch operations.

106 Amend this term to reflect the appropriate title for those charged with governance of the ADI, for example, 'Board of Directors' for a locally incorporated ADI or, for a foreign ADI, 'the Senior Officer Outside Australia' to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian branch operations. Insert appropriate title, when prompted, throughout the letter.

[If applicable: In accordance with APS 910 we are required to provide:

(a) limited assurance that, in all material respects:

   (i) the ADI [and/or the ADI Group] has implemented internal controls that are designed to ensure:

      a. compliance with all applicable Prudential Requirements relating to APS 910; and

      b. that Single Customer View (SCV) data as set out in APS 910 Attachment A, to the extent practicable, and Financial Claims Scheme payment instruction and reporting information can be relied upon as being complete and accurate and in accordance with APS 910; and

   (ii) these controls have operated effectively throughout the financial year; and

(b) limited assurance, based on our work under (a) above, that the ADI [and/or the ADI Group] have complied, in all material respects, with all relevant Prudential Requirements under the Banking Act, including compliance with APS 910.

Our Annual Prudential Assurance Reports will cover the same period as the annual financial report required under the Corporations Act and is to be issued within three [four] months of the financial year-end of the [ADI name].

Responsibilities of the [Title of Those Charged with Governance[107]] of the ADI [and/or the ADI Group]

In accordance with APRA Prudential Standard CPS 220 *Risk Management*, it is the responsibility of the [Title of those charged with governance] of the ADI [and/or head of the ADI Group] to ensure that the ADI [and/or the ADI Group] meet prudential and statutory requirements and have management practices to limit risks to prudent levels.

This responsibility includes providing APRA with a Risk Management Declaration, as set out in Attachment A to CPS 220.

In relation to the APS 310 annual prudential assurance report(s) this responsibility includes:

(a) ensuring that the information included in ADI Reporting Forms at the financial year-end is reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(b) establishing and maintaining internal controls that are designed to ensure:

   (i) the ADI [and/or the ADI Group] complies with all applicable Prudential Requirements;

   (ii) reliable data is provided to APRA in the ADI Reporting Forms prepared under the FSCODA; and

(c) ensuring that the internal controls under (b) operate effectively throughout the financial year;

(d) ensuring that the ADI [and/or the ADI Group] complies with all relevant Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards during the financial year; and

[107] Alternatively, for a foreign ADI, "senior officer outside Australia" (to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian operations). Insert appropriate title, when prompted, throughout the letter.

(e) ensuring that the ADI and the ADI Group maintain accounting records which at any time disclose with reasonable accuracy the financial position of the ADI [and/or the ADI Group].

Furthermore, in accordance with APS 310, it is the responsibility of the [Title of those charged with governance] and management of an ADI [and/or ADI Group] to ensure that the auditor:

(a) has access to all data, information, reports and staff of the ADI that the auditor reasonably believes is necessary to fulfil its role and responsibilities under APS 310. This includes access to the ADI's [Title of those charged with governance], [Title of those charged with governance] Committees and internal auditors, as required;

(b) is fully informed of all prudential requirements applicable to the ADI [and/or the ADI Group]. Prudential requirements include requirements imposed by the Act, regulations, prudential standards, the FSCODA, reporting standards, conditions on authority and any other requirements imposed by APR, in writing, in relation to an ADI.

(c) is provided with any other information APRA has provided to the ADI that may assist the auditor in fulfilling its role and responsibilities under APS 310.

[If applicable: In accordance with APS 910, it is the responsibility of <<<>>>]

Auditor's Independence and Quality Control

In undertaking the assurance engagement, we will comply with:

- the relevant ethical requirements relating to assurance engagements, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour;
- the independence requirements specified by APRA in Prudential Standard CPS 510 *Governance*; and
- Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements*.

Responsibilities of the Appointed Auditor

[If applicable: As the statutory auditor of [Name of ADI], we carry out sufficient procedures to enable us to form an opinion on the state of the [type of ADI]'s affairs and its results, and to report thereon to the members of the [type of ADI] in accordance with the requirements of the Corporations Act[108]. Although our audit [and review] under the Corporations Act will include such review of the ADI's [and/or the ADI Group's] systems of accounting and internal control and performance of such tests and enquiries as we consider necessary, these audit [and review] procedures are not designed to form an opinion on the systems of accounting and internal control taken as a whole.

In order to satisfy the requirements of APRA, we will carry out additional procedures over and above those which are performed in our capacity as the auditor under the Corporations Act[109].

Despite our involvement in examining the ADI's [and/or the ADI Group's] systems of control, it must be appreciated that it is the responsibility of the [Title of those charged with governance] of the ADI [and/or head of the ADI Group] to establish and maintain all of the ADI's [and/or the ADI Group's] internal control systems. All such systems have their limitations and, this being so, errors or irregularities may occur, and which may not be detected. Our work is not to be relied upon for the purposes of discovering fraud, error, deficiencies, or non-compliance with laws and regulations,

[108] Or other appropriate local or overseas requirements.
[109] Or other relevant legislation.

although we will report to the appropriate level of management any fraud, error, deficiencies, or non-compliance that may be identified as a result of our assurance engagement.

We recognise that there may be some overlap between our audit [and review] under the Corporations Act and work that is necessary to fulfil APRA's APS 310 prudential reporting requirements. In order to help ensure the most efficient use of resources, wherever possible, reliance will be placed on work that is carried out for the statutory financial report audit [and review] purposes.]

In order to report on the matters set out in the *Objective and Scope of Engagement* section of this letter, we are required to undertake both reasonable and limited assurance engagements, as described in PARTS A to C below, and to report our opinion and conclusions based on the procedures we have performed and the evidence we have obtained.

We will conduct our reasonable assurance engagement in accordance with applicable Australian Auditing Standards and our limited assurance engagements in accordance with applicable Standards on Assurance Engagements and Standards on Review Engagements, and with reference to Guidance Statement GS 012 *Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions (ADIs) and ADI Groups,* issued by the Australian Auditing and Assurance Standards Board (AUASB). These standards require that we comply with relevant ethical requirements relating to assurance and review engagements.

As part of our procedures, we will request representations from management and, where appropriate, those charged with governance, in respect of representations made to us in connection with the engagement.

After the completion of our prudential engagement report, it is our normal practice to report any matters of significance, together with suggestions for their correction and any recommendations we may have on the systems, procedures and controls in general. However, as our examination will be limited to the reasonable and limited assurance engagements in relation to matters set out in the *Objective and Scope of Engagement* section above, you cannot assume that any matters reported to you indicate that there are no additional matters or matters that you need to be aware of in meeting your responsibilities.

Responsibilities under APS 310:

PART A: Reasonable Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Accounting Records

Our responsibility is to express an opinion, based on our reasonable assurance engagement, on whether the information sourced from the ADI's [and/or the ADI Group's] accounting records, included in the ADI Reporting Forms at the financial year-end as specified in Attachment A to APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

We will conduct our reasonable assurance engagement in accordance with applicable Australian Auditing Standards. These Auditing Standards require that we plan and perform our engagement to obtain reasonable assurance whether the relevant data included in the Specified APRA Reporting Forms are free from material misstatement.

A reasonable assurance engagement involves performing procedures to obtain evidence on whether the information sourced from the accounting records included in the Specified ADI Reporting Forms are, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards. The procedures selected depend on our judgement, including our assessment of the risks of material misstatement of the data in the Specified ADI Reporting Forms, whether due to fraud or error. In making those risk assessments, we consider internal control systems and compliance functions relevant to the preparation of the Specified ADI Reporting Forms, in order to design assurance procedures that are appropriate in the circumstances.

PART B: Limited Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Non-Accounting Records

Our responsibility is to perform a limited assurance engagement on information sourced from the ADI's [and/or the ADI Group's] non-accounting records, included in ADI Reporting Forms at the financial year-end as specified in Attachment A to APS 310, and to express a conclusion on whether anything has come to our attention that causes us to believe that this information is not, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

We will conduct our limited assurance engagement in accordance with AUASB's Standards on Assurance Engagements ASAE 3000 *Assurance Engagements other than Audits or Reviews of Historical Financial Information* (ASAE 3000) and ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information*, and AUASB's Standard on Review Engagements ASRE 2405 *Review of Historical Financial Information Other than a Financial report*, as applicable.

The objective of our limited assurance engagement is to provide us with a basis for reporting whether anything has come to our attention that causes us to believe that the relevant data in the Specified ADI Reporting Forms, is not, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

A limited assurance engagement consists of making enquiries of responsible ADI [and/or the ADI Group] personnel and applying analytical and other review procedures considered necessary and does not, ordinarily, require corroboration of the information obtained. A limited assurance engagement is substantially less in scope than a reasonable assurance engagement conducted in accordance with Australian Auditing and Assurance Standards and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in a reasonable assurance engagement. Accordingly, we do not express a reasonable assurance opinion.

Our procedures depend on our judgement, including our assessment of the risks of material misstatement of the ADI Reporting Forms, whether due to fraud or error or of a material breakdown of controls. In making those risk assessments, we consider internal control systems and compliance functions relevant to the preparation of the Specified ADI Reporting Forms in order to design limited assurance procedures that are appropriate in the circumstances.

PART C: Limited Assurance on Internal Controls addressing Compliance with Prudential Requirements and Reliability of Data included in ADI Reporting Forms

Our responsibility is to perform a limited assurance engagement and to express a conclusion, based on the limited assurance procedures we have performed and the evidence we have obtained, on whether anything has come to our attention that causes us to believe that, in all material respects, throughout the period from [date] to [date]:

(a) the ADI [and/or ADI Group] has not implemented internal controls that are designed to ensure:

  (i) compliance with all applicable Prudential Requirements [(excluding APS 910)]; and

  (ii) reliable data is provided to APRA in ADI Reporting Forms prepared under the FSCODA; and

(b) these controls have not operated effectively

We will conduct our limited assurance engagement on controls in accordance with the AUASB's Standards on Assurance Engagements ASAE 3000 and ASAE 3150 *Assurance Engagements on Controls*. These standards required that we plan and perform our procedures to obtain limited assurance about whether anything has come to our attention that, in all material respects, the controls were not suitably designed and/or implemented to achieve the control objectives or the controls did not operate effectively throughout the period.

A limited assurance engagement involves performing procedures to obtain evidence about the design, implementation and operating effectiveness of controls. We will perform procedures primarily consisting of making enquiries of management and others within the ADI (and/or the ADI Group], as appropriate, examination of design specifications and documentation and observation of implementation and operation.

The procedures selected depend on our judgement, including our assessment of the risks of material deficiencies in the design and/or implementation of the controls, or deviation in their operating effectiveness. In making those risk assessments, we considered internal control systems and compliance functions relevant to ensuring compliance with all Prudential Requirements and provision of reliable data to APRA in ADI Reporting Forms prepared under the FSCODA, in order to design assurance procedures that are appropriate in the circumstances.

We will perform additional procedures if we become aware of matters that cause us to believe that the controls may not be suitably designed, implemented or operating effectively.

Because of the inherent limitations of an assurance engagement, together with the inherent limitations of any system of controls there is an unavoidable risk that some deficiencies in the design and/or implementation of the controls or deviation in their operating effectiveness may not be detected, even though the engagement is properly planned and performed in accordance with ASAE 3150.

The system within which the controls that we will examine operate, will not be examined, except to the extent the system is relevant to the achievement of the control objectives. Therefore, no opinion will be expressed as to the effectiveness of the system of controls as a whole.

The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement and consequently the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed. Therefore, there is a higher risk than there would be in a reasonable assurance engagement, that any material deficiencies in the design of controls that exist may not be revealed by the engagement, even though the engagement is properly performed in accordance with ASAE 3150. In expressing our conclusion, our report on the design, implementation and operating effectiveness of controls will expressly disclaim any reasonable assurance conclusion on controls.

PART D: Limited Assurance on Compliance with Prudential Requirements

Our responsibility is to express a limited assurance conclusion, based on our work performed under Parts A to C above, on whether anything has come to our attention that causes us to believe that, for the financial year ended [date], the ADI [and/or the ADI Group] has not, in all material respects, complied with all relevant Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards.

Responsibilities under APS 910

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Inherent Limitations

There are inherent limitations in any internal control and compliance framework, and fraud, error or non-compliance with Prudential Requirements may occur and not be detected. As the systems, procedures and controls to ensure compliance with applicable Prudential Requirements are part of the operations of the ADI [and/or the ADI Group], it is possible that either the inherent limitations of the general internal control structure, or weaknesses in it, can impact on the effective operation of the specific controls of the ADI [and/or the ADI Group].

Any projection of any evaluation of internal control procedures or compliance measures to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with them may deteriorate. Consequently, there are inherent limitations on the level of assurance that can be provided.

A reasonable or limited assurance engagement is not designed to detect all misstatements in ADI Reporting Forms, or deficiencies in internal controls, or instances of non-compliance with applicable Prudential Requirements, as assurance engagement procedures on the accounting records and data relied on for reporting and compliance are not performed continuously throughout the period and are undertaken on a test basis.

The opinion and conclusions expressed in our prudential assurance report(s) are to be read in the context of the foregoing comments.

Internal Audit

[Name of ADI]'s internal audit function is considered well placed to review and test properly documented systems, procedures and controls operating within the ADI [and/or the ADI Group]. Consequently, it is our intention to liaise closely with internal auditors throughout the year.

Where work is carried out by internal auditors as part of the internal control procedures of the ADI [and/or ADI Group], we [intend to/may] review the work performed and carry out such re-performance tests and other procedures as we consider necessary. Where we are satisfied with the work carried out by internal auditors, it is our intention to place reliance on such work in accordance with Auditing Standard ASA 610 *Using the Work of Internal Auditors*, and, where appropriate, reduce the extent of our own procedures relating to internal controls.

Special Purpose Engagements

Under APS 310, APRA may require you, by notice in writing, to appoint an auditor to provide a report on a particular aspect of the ADI's [and/or ADI Group's] operations, prudential reporting, risk management systems or financial position.

Under APRA Prudential Standard APS 910 *Financial Claims Scheme*, APRA may, in writing, require an ADI to engage an auditor to undertake a reasonable or limited assurance engagement of Single Customer View systems and data, and the systems used to generate and transmit Financial Claims Scheme payment and reporting information.

The details of such engagements will be the subject of specific requests from APRA and will constitute separate engagements and reporting. In these circumstances, separate engagement letters will be issued.

Liaison with APRA

Under normal circumstances, liaison with APRA will take place under tripartite arrangements involving APRA, the ADI [and/or the head of the ADI Group] and its appointed auditor(s). Notwithstanding the tripartite relationship, APS 310 allows for communication between an auditor and APRA on a bilateral basis, at the request of either party. APRA can, although not commonly, request information directly from an appointed auditor.

Under CPS 510, an ADI is required to ensure that its internal policy and contractual arrangements do not explicitly or implicitly restrict or discourage auditors from communication with APRA.

Additional Reporting Responsibilities under the Banking Act

Under sections 16B, 16BA, 16C and 16 D of the Banking Act, we are required to provide information to APRA upon request, or where we possess reportable information specified in the Banking Act, or where we consider that the provision of information would assist APRA in performing its functions under the Banking Act or the FSCODA.

Part VIA of the Banking Act includes provisions to protect an auditor providing information to APRA, in good faith and without negligence, from any action, claim or demand by, or any liability to, any other person in respect of the information.

Use of Report(s)

Our annual APS 310 [and APS 910] prudential assurance report(s) and any special purpose engagement report will be prepared for distribution to the [Title of those charged with governance] or [Title of those charged with governance] Audit Committee of [name of ADI] [and/or head of ADI Group] and APRA. These assurance reports will be prepared in accordance with the terms of this engagement letter, in order to satisfy APRA's prudential reporting requirements for appointed auditor's of ADIs [and/or ADI Groups], as specified in APS 310 [and APS 910].

In accordance with the *Australian Prudential Regulation Authority Act 1998*, APRA may make our assurance reports available to other specified agencies when APRA is satisfied that such information may assist these agencies in performing their functions or exercising their powers.

These reports are not to be distributed to any party other than those to whom it is addressed, APRA, and other parties that APRA is lawfully entitled to provide relevant information.

We disclaim any assumption of responsibility for any reliance on these reports, or the subject matter to which it relates, to any party other than the ADI [and/or the ADI Group], APRA, and other parties that APRA is lawfully entitled to provide relevant information.

Fees

The requirement to report pursuant to APS 310 is in addition to, and separate from, the audit [and review] of financial reports required under the Corporations Act and will result in additional audit and review procedures being carried out. Fees relating to this work will be based on the degree of responsibility and skill involved and the time necessarily occupied by the work undertaken.

As the fees will not relate to our audit [and review] carried out in our capacity as the statutory auditor under the Corporations Act, our invoices will be rendered separately, to clearly identify the additional cost of APRA's prudential reporting requirements.

[Insert additional information here regarding fee arrangements, billings and other specific items, as appropriate.]

We look forward to full cooperation with you and your staff and we trust that you will make available to us whatever records, documentation and other information are requested in connection with our assurance engagement.

This letter will be effective for future years unless we advise you of its amendment or replacement, or the engagement is terminated.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our prudential assurance engagement pursuant to APS 310.

Yours faithfully,

(signed)

…………………………………………

Name and Title

Date

Acknowledged on behalf of [name of ADI] by

(signed)

…………………………………………

Name and Title

Date

Appendix 3

EXAMPLE MANAGEMENT REPRESENTATION LETTER – LEVEL 1 ADI AND/OR LEVEL 2 ADI GROUP

Engagements undertaken pursuant to APRA Prudential Standard APS 310 *Audit and Related Matters* (Annual Reporting)

The following example representation letter is to be used as a guide only and will need to be adapted according to individual engagement requirements and circumstances of the ADI and/or ADI Group.

Note:

1. In this example representation letter, the ADI on a 'Level 1' basis is referred to as 'the ADI'. The group of which the ADI is a member on a 'Level 2' basis, is referred to as 'the ADI Group'.
2. If the representation letter also covers a 'Level 3' conglomerate group, this fact must be indicated by using the appropriate terminology throughout the letter.[110]
3. 'Level 1', 'Level 2' and 'Level 3' have the meaning given in APRA Prudential Standards APS 001 and 3PS 001 *Definitions*.
4. This example representation letter has been prepared on the basis that the auditor has requested that management prepare separate representation letters for the purposes of APS 310/3PS 310 and APS 910.

[110] APRA Prudential Standard 3PS 310 *Audit and Related Matters* sets out the prudential reporting requirements for Level 3 groups.

[name of ADI [and/or ADI Group] Letterhead]

[Addressed to Appointed Auditor]

[Date]

Dear Sir/Madam

Representation Letter for the Annual Prudential Reporting Engagement undertaken pursuant to APRA Prudential Standard APS 310 *Audit and Related Matters*

This representation letter is provided in connection with your reasonable and limited assurance engagement, as required by APRA's Prudential Standard APS 310 *Audit and Related Matters* (APS 310), of [name of ADI] [for the Level 1 ADI] (the ADI) [and/or the Level 2 ADI Group (the ADI Group)] for the financial year ended [date][111], for the purpose of you providing:

(a) reasonable assurance that the information sourced from the ADI's [and/or the ADI Group's] accounting records, included in the APRA Reporting Forms at [the financial year-end] as specified in Attachment A of APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(b) limited assurance, unless otherwise indicated by APRA in writing, that the information sourced from the ADI's [and/or the ADI Group's] non-accounting records, included in the ADI Reporting Forms at [the financial year-end] as specified in Attachment A of APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(c) limited assurance that, in all material respects:

  (i) the ADI [and/or the ADI Group] has implemented internal controls that are designed to ensure:

    a. compliance with all applicable Prudential Requirements; and

    b. reliable data is provided to APRA in the ADI Reporting Forms prepared under the *Financial Sector (Collections of Data) Act 2001* (FSCODA); and

  (ii) the controls in (c)(i) have operated effectively throughout the financial year; and

(d) limited assurance, based on your work under (a) to (c) above, that the ADI [and/or the ADI Group] has complied, in all material respects, with all relevant Prudential Requirements under the *Banking Act 1959* (Banking Act) and the FSCODA, including compliance with APRA Prudential and Reporting Standards during the financial year.

In accordance with the engagement letter supporting this representation letter, references to controls to ensure compliance with prudential standards and other prudential requirements in this letter exclude APRA Prudential Standard APS 910 *Financial Claims Scheme*. Representations regarding the establishment and maintenance of controls to ensure compliance with APS 910 and other prudential requirements in relation to APS 910 are covered in a separate representation letter provided in support of the Financial Claims Scheme assurance engagement undertaken in accordance with the requirements of APS 310 and APS 910.

[I/We] acknowledge [my/our] responsibility for ensuring that:

[111] Wording in this paragraph, including definitions for the ADI/ADI Group, should be consistent with wording used in the Engagement Letter and Prudential Assurance Report.

- accounting and non-accounting records, and the ADI Reporting Forms prepared from them, are accurate;
- the ADI [and/or ADI Group] maintain accounting records which at any time disclose with reasonable accuracy the financial position and financial performance of the ADI [and/or ADI Group];
- the ADI [and/or the ADI Group] complies with prudential and statutory requirements and has management practices to limit risks to prudent levels.
- the ADI [and/or the ADI Group] identifies key risks and establishes risk management practices that are detailed in descriptions of risk management systems and are regularly reviewed and updated, at least annually, to take account of changing circumstances;
- APRA is provided with high-level descriptions of our key risk management systems covering all major areas of risk, and APRA is informed of all material changes to the ADI's [and/or the ADI Group's] risk management systems descriptions when they are made;
- adequate controls have been designed to ensure:

  (i) compliance with all applicable Prudential Requirements; and

  (ii) reliable data is provided to APRA in the ADI Reporting Forms prepared under the FSCODA;

  and that these controls operate effectively throughout the financial year;
- the information included in ADI Reporting Forms at [the financial year-end] is reliable, and in accordance with the relevant APRA Prudential Standards and Reporting Standards;
- you are informed of all Prudential Requirements applicable to the ADI [and/or the ADI Group];
- the ADI [and/or ADI Group] have provided you with any other information APRA has provided to the ADI [and/or the ADI Group] that may assist you in fulfilling your role and responsibilities under APS 310; and
- we have provided you with access to all data, information, reports and staff of the ADI [and/or the ADI Group] that you reasonably believe are necessary to fulfil your role and responsibilities under APS 310. This includes access to the ADI's [Title of those charged with governance][112], [Title of those charged with governance] Audit Committee and internal auditors as required.

We have made appropriate inquiries of [responsible parties] of the ADI [and/or the ADI Group] with the relevant knowledge and experience. We confirm, to the best of our knowledge and belief, the following representations made to you during your assurance engagement:

[*Include representations relevant to the ADI [and/or the ADI Group]. Such representations may include the following examples*.]

1. We have made available to you for the purpose of your assurance engagement:

   (a) all data, information, reports and staff of the ADI [and/or the ADI Group] that you have required to fulfil your role and responsibilities under APS 310;

[112] Or, for a foreign ADI, 'the Senior Officer Outside Australia' to whom authority has been delegated in accordance with CPS 510 Governance, for overseeing the Australian branch operations. Insert appropriate title, when prompted, throughout the letter

(b) access to the ADI's [Title of those charged with governance], [Title of those charged with governance] Audit Committee and internal auditors as required, and related data, minutes of meetings, reports, other information, explanations and assistance necessary for the conduct of the assurance engagement;

(c) all correspondence with APRA concerning all Prudential Requirements applicable to the ADI [and/or the ADI Group];

(d) all policies and procedures (including all changes in the reporting period) that are designed to ensure the ADI [and/or the ADI Group] has:

(i) complied with all applicable Prudential Requirements; and

(ii) provided reliable data to APRA in the ADI Reporting Forms prepared under the FSCODA;

(e) all high level descriptions of our key risk management systems covering all material risks, approved by the [Title of those charged with governance] and management, and including all material changes to the risk management systems descriptions provided to APRA during the financial period; and

(f) all other information APRA has provided to the ADI [and/or the ADI Group] that may assist you in fulfilling your role and responsibilities under APS 310.

2. We have disclosed to you the results of management's assessment of the risk of non-compliance with Prudential Standards as a result of fraud.

3. There has been no:

(a) known actual or possible non-compliance with laws or regulations, the effects of which should be considered for disclosure in your report;

(b) frauds or suspected frauds known to management that may have affected any entity in the economic entity involving:

(i) management

(ii) employees who have significant roles in internal control; or

(iii) others

where the fraud could have a material effect on compliance with the applicable APRA Prudential Requirements or on the reporting of data to APRA under the FSCODA, or compliance with applicable Prudential Requirements;

(c) allegations of fraud, or suspected fraud, affecting the ADI's [and/or the ADI Group's] financial report communicated by employees, former employees, analysts, regulators or others; and

(d) communications from regulatory authorities concerning non-compliance with, or deficiencies in, prudential compliance and reporting practices and controls relating to compliance with Prudential Standards that could have a material effect on your report.

[If applicable: other than instances that have been provided to you in the course of your engagement and/or as included by you in your report.]

4. We have established and maintained adequate internal controls designed to prevent and detect fraud and error and to ensure the ADI [and/or the ADI Group] has:

(a) complied with all applicable Prudential Requirements; and

(b) provided reliable data to APRA in the ADI Reporting Forms prepared under the FSCODA;

for the period [date] to [date] we have disclosed to you all changes in the design of the measures and internal controls relating to compliance with Prudential Standards, key risk management systems and statutory and regulatory requirements, or confirmed to you that no changes were made. We have also disclosed to you all breakdowns, or confirmed to you no breakdowns occurred, in the operation of those measures and policies that would have a material effect on your report.

5. We acknowledge that you have advised management of uncorrected misstatements and non-compliance with Prudential Standards that you became aware of as a result of your assurance engagement procedures.

6. We believe the effects of all uncorrected misstatements and instances of non-compliance with Prudential Standards, summarised in [Appendix], pertaining to the reporting period [date] to [date] (including the effects of prior year issues impacting the current reporting period) are immaterial, both individually and in the aggregate, or adequately reported to APRA.

7. There has been no breakdown in internal controls or non-compliance with the policies and procedures which are designed to ensure the ADI [and/or the ADI Group] has:

(a) complied with all applicable Prudential Requirements; and

(b) provided reliable data to APRA in the ADI Reporting Forms prepared under the FSCODA,

[If applicable: other than instances that have been provided to you in the course of your engagement and/or as included by you in your report];

8. We have provided to APRA:

(a) all high level descriptions of our key risk management systems covering all identified key risks, approved by the Board[/Senior Officer outside Australia] and management, and including all material changes to the risk management systems descriptions made during the financial year; and

(b) all information as prescribed by the Prudential Standards for disclosure to APRA within the prescribed period.

[If applicable: other than instances that have been provided to you in the course of your engagement and/or as included by you in your report]

9. We have consulted with APRA on all matters such as new business ventures and other initiatives, where prescribed by the Prudential Standards, and provided you with the responses from APRA.

10. We have complied with all prudential and statutory requirements applicable to the ADI [and/or the ADI Group] throughout the financial year.

[If applicable: other than instances that have been provided to you in the course of your engagement and/or as included by you in your report]

11. [I/We] have signed [or intend to sign] a Risk Management Declaration to APRA, in accordance with CPS 220, stating that for the financial year ended [date], to the best of our knowledge and having made appropriate enquiries, in all material respects:

(a) the ADI [and/or the ADI Group] has in place systems for ensuring compliance with all Prudential Requirements;

(b) the systems and resources that are in place for identifying, measuring, evaluating, monitoring, reporting, and controlling or mitigating material risks, and the risk management framework, are appropriate to the ADI [and/or the ADI Group], having regard to the size, business mix and complexity of the ADI [and/or the ADI Group];

(c) the risk management and internal control systems in place are operating effectively and are adequate having regard to the risks they are designed to control;

(d) the ADI [and/or the ADI Group] has a Risk Management Strategy (RMS) that complies with CPS 220, and the ADI [and/or the ADI Group] has complied with each measure and control described in the RMS; and

(e) the ADI [and/or the ADI Group] is satisfied with the efficacy of the processes and systems surrounding the production of financial information at the ADI [and/or the ADI Group].

12. With respect to ADI Reporting Forms prepared under the FSCODA:

(a) the data has been compiled in accordance with the relevant APRA Prudential and Reporting Standards, and related guidance applicable to each form;

(b) the ADI Reporting Forms have been resubmitted where assurance engagement adjustments of a material nature were identified;

(c) we believe the effects of the uncorrected misstatements identified by you during the assurance engagement, and summarised in the accompanying schedule to this letter, are immaterial, both individually and in the aggregate, to the reliability of ADI Reporting Forms prepared under the FSCODA taken as a whole;

(d) there are no material transactions that have not been recorded properly in the accounting records supporting the ADI Reporting Forms; and

(e) information in the ADI Reporting Forms, sourced from records other than the ADI's [and/or the ADI Group's] accounting records, are prepared from reliable records applicable to the matters to be provided to APRA, in accordance with the applicable guidance provided by APRA.

13. No events have occurred subsequent to [the financial year-end date] and through to the date of this letter that would require adjustment to, or disclosure in, the ADI Reporting Forms.

14. [Include any additional matters relevant to the circumstances of the engagement.]

We understand that your examination was made in accordance with applicable AUASB Standards and was, therefore, designed primarily for the purpose of reporting pursuant to the requirements of APS 310, and that your procedures were limited to those which you considered necessary for that purpose.

Yours faithfully

[Name of signing officer and title]

Signed by resolution of the [Title of those charged with governance][113]

[113] Locally incorporate ADIs: letter to be tabled at Board/Board Audit Committee meeting, but may be signed by management, as directed by Board.
Foreign ADIs: letter may be signed by either Senior Officer outside Australia or CEO/Senior Officer in Australia with responsibility for Australian operations, with appropriate approval from Senior Officer outside Australia.

Appendix 4

EXAMPLE ANNUAL PRUDENTIAL ASSURANCE REPORT

For engagements undertaken pursuant to APRA Prudential Standards APS 310 and 3PS 310 *Audit and Related Matters*

The following example auditor's report is to be used as a guide only and will need to be adapted according to the individual engagement requirements and circumstances of the ADI and/or ADI Group.

Note:

1. In this example auditor's report:

   - the 'Level 1' ADI is referred to as 'the ADI';
   - the 'Level 2' ADI and its controlled entities, is referred to as 'the Level 2 ADI Group'
   - the 'Level 3' conglomerate group, that is, the ADI and all entities determined by APRA to be members of the Level 3 group, is referred to as 'the Level 3 Group'.

   'Level 1', 'Level 2' and 'Level 3' have the meaning given in APRA Prudential Standards APS 001 and 3PS 001 *Definitions.*

2. Under APS 310 and 3PS 310, separate auditors may be appointed to meet the APS 310 and/or 3PS 310 reporting requirements on a Level 1, Level 2 and Level 3 basis.

3. In accordance with the requirements of APS 310 and 3PS 310:

   - Where the ADI is the head entity of a Level 2 or Level 3 group, the auditor can issue either separate reports for Level 1, Level 2 and Level 3, or a combined report for the ADI (head entity) and the group.
   - The auditor's report must make it clear where the auditor is referring to matters relating to the ADI/head entity or the group.

4. APS 910 *Financial Claims Scheme* auditor's report:

   In October 2014, APRA released a 'suggested/non-compulsory' auditor's report which aggregates all APS 910 requirements (compliance and controls) into a single report, effectively moving the reporting from the APS 310/3PS 310 auditor's report to a separate APS 910 auditor's report. APRA indicated that this single report facilitated clearer communication with respect to APS 910 matters.

   Where an ADIs or ADI group is not subject to the requirements of APS 910, for example, a foreign ADI, references to APS 910 need to be removed.

To:

[Appropriate addressee[114]] of [name of ADI [and/or Level 2 ADI Group and/or Level 3 Group]]

[Australian Prudential Regulation Authority (APRA)]

Annual Prudential Assurance Report for the financial year ended [year end] pursuant to Prudential Standards APS 310 and 3PS 310 *Audit and Related Matters*

1. Introduction

We have performed reasonable and limited assurance engagements, as applicable, pursuant to the reporting requirements specified in Australian Prudential Regulation Authority (APRA) Prudential Standards APS 310 and 3PS 310 *Audit and Related Matters* (APS 310) (3PS 310), as described in PARTS A to D of this report, for the:

(a) Level 1 ADI, [name of ADI] [including any extended licensed entities] (the ADI).

(b) the Level 2 ADI group, [name of ADI and its controlled entities] (the Level 2 ADI Group).

(c) the Level 3 conglomerate group, [name of ADI] and all entities determined by APRA to be members of the Level 3 group (the Level 3 Group).

APS 310 and 3PS 310 require an ADI to appoint an auditor to undertake an annual assurance engagement, as set out in those Prudential Standards. The responsibilities and reporting requirements arising from this appointment, have been outlined in our letter of engagement dated [date].

[If applicable: APS 310 also requires us to perform a limited assurance engagement on the controls implemented by [ADI] to ensure compliance with prudential requirements which includes compliance with APS 910 *Financial Claims Scheme*. Refer to Part C a (i) of this report. The scope of work undertaken and our conclusions relating to this work have been included in our report titled *Auditor's Prudential Assurance Report pertaining to the Financial Claims Scheme for the year ended [year end date]*, issued on [report date[115]], a copy of which is attached. This report [was/was not] subject to modification.][116]

[If applicable: Our Independent Auditor's Report on the Financial Report of [name of company and name of group] and its subsidiaries for the year ended [date] was signed on [date] and [was/was not] subject to modification. Our audit [and review] of the financial report(s) required under the *Corporations Act 2001*[117] was directed towards obtaining sufficient evidence to form an opinion under the appropriate legislation. Our statutory audit [and review] was not designed to enable us to conclude on other matters outlined in APS 310 and 3PS 310.

Accordingly, we have performed additional procedures in order to form our reasonable assurance opinion and limited assurance conclusions, as applicable, pursuant to the reporting requirements specified in APS 310 for the ADI [and/or the Level 2 ADI Group] and 3PS 310 for the Level 3 Group.][118]

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114 Amend to reflect the appropriate addressee of the report, for example, Chairman of Board or Board Audit Committee for a locally incorporated ADI or, for a foreign ADI (i.e. a branch of a foreign ADI), the senior officer outside Australia to whom authority has been delegated, in accordance with Prudential Standard CPS 510 *Governance*, for overseeing the Australian operations.
115 Should be the same date as for the APS 310/3PS 310 report(s).
116 Delete this paragraph if not relevant, for example, in relation to foreign ADIs which are not subject to APS 910. Where the APS 910 auditor's report is modified, this is referred to in the introduction to the APS 310/3PS 310 auditor's report but does not lead to a modification of the APS 310/3PS 310 auditor's report.
117 Or other appropriate local or overseas legislation.
118 Delete if no statutory audit is performed, for example, in relation to foreign branches.

2. [Qualified/Adverse/Disclaimer of] Opinion and Conclusions

PART A – Reasonable Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Accounting Records

In our opinion, [and except for the matters set out in Appendix [insert] of this report,] the information in the Specified ADI Reporting Forms of the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] as at [financial year-end], sourced from the ADI's [and/or the Level 2 ADI Group's and/or the Level 3 Group's] accounting records, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

The ADI Reporting Forms which are the subject of this assurance report are [attached or disclosed] in Appendix [insert]:

> [Two different approaches are possible to identify ADI Reporting Forms which are the subject of the opinion:
>
> Option 1:
>
> Attach all the ADI Reporting Forms, which are the subject matter of this assurance report, to the report, and identify on each ADI Reporting Form the date it was submitted and whether or not the data items have been subjected to a reasonable or limited assurance engagement. Include in the assurance report by reference to "the data identified on the ADI Reporting Forms attached under Attachment [insert]"
>
> Option 2:
>
> Alternatively, list here, or include a reference to an appendix which lists the specific title, number and date submitted of each relevant ADI Reporting Form, based on those specified in Attachment A of APS 310, where such forms contain information sourced from accounting records, which have been subjected to a reasonable assurance engagement.
>
> Note:
>
> Clearly identify data items within each ADI Reporting Form that have been sourced from accounting records and are therefore the subject matter of this opinion.]

PART B – Limited Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Non-accounting Records

Based on our limited assurance engagement, which is not a reasonable assurance engagement or an audit, [and except for the matters set out in Appendix [insert] of this report,] nothing has come to our attention that causes us to believe that the information in the ADI Reporting Forms of the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] as at [financial year-end], sourced from non-accounting records, is not, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

The ADI Reporting Forms which are the subject of this assurance report are [attached or disclosed] in Appendix [insert]:

> [Two different approaches are possible to identify ADI Reporting Forms which are the subject of the conclusion:
>
> Option 1:
>
> Attach all the ADI Reporting Forms, which are the subject matter of this assurance report, to the report, and identify on each ADI Reporting Form the date it was submitted and whether or not the data items have been subjected to a reasonable or limited assurance engagement.

Include in the assurance report by reference to "the data identified on the ADI Reporting Forms attached under Attachment [insert]"

Option 2:

Alternatively, list here, or include a reference to an appendix which lists the specific title, number and date submitted of each relevant ADI Reporting Form, based on those specified in Attachment A of APS 310, where such forms contain information sourced from non-accounting records, which have been subjected to a limited assurance engagement.

Note: Clearly identify data items within each ADI Reporting Form that have been sourced from non-accounting records and therefore the subject matter of this conclusion.]

PART C – Limited Assurance on Internal Controls addressing Compliance with Prudential Requirements and Reliability of Data included in ADI Reporting Forms

Based on our limited assurance engagement, which is not a reasonable assurance engagement or an audit, [and except for the matters set out in Appendix [insert] of this report,] nothing has come to our attention that causes us to believe that, in all material respects, throughout the period from [date] to [date]:

(a) the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] has not implemented internal controls that are designed to ensure:

(i) compliance with all applicable Prudential Requirements [(excluding APS 910)]; and

(ii) reliable data is provided to APRA in the ADI Reporting Forms prepared under the FSCODA; and

(b) these controls have not operated effectively.

PART D – Limited Assurance on Compliance with Prudential Requirements

Based on the procedures we have performed and the evidence we have obtained as part of our reasonable and limited assurance engagements in Parts A to C above, [and except for the matters set out in Appendix [insert] to this report,] nothing has come to our attention that causes us to believe that, for the financial year ended [date], the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] has not, in all material respects, complied with all relevant Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards.

3. Basis for [Qualified/Adverse/Disclaimer of] Opinion and Conclusions[119]

We conducted our assurance engagement in accordance with applicable Standards issued by the Australian Auditing and Assurance Standards Board (AUASB). Our responsibilities under these Standards are further described in the *Auditor's Responsibilities* section of this report.

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

[119] Provide details where a modified opinion/conclusion is included, or refer to an Attachment to the report which includes the required information. Where the auditor determines it necessary to issue a modified opinion and/or conclusion, the principles contained in AUASB auditing and assurance standards may provide useful guidance.

4. Responsibilities of the [Title of Those Charged with Governance][120] and Management of the ADI [and/or the Level 2 ADI Group and/or Level 3 Group]

In accordance with APRA Prudential Standard CPS 220 *Risk Management*, it is the responsibility of the [Title of those charged with governance] of an ADI [and/or head of the Level 2 ADI Group and/or head of the Level 3 Group] to ensure that the ADI [and/or the Level 2 ADI Group and/or Level 3 Group] meets prudential and statutory requirements and have management practices to limit risks to prudent levels.

This responsibility includes providing APRA with a Risk Management Declaration, as set out in Attachment A to CPS 220.

In relation to the APS 310/3PS 310 annual prudential assurance report(s), this responsibility includes:

(a) ensuring that the information included in ADI Reporting Forms at the financial year-end is reliable and in accordance with the relevant APRA Prudential and Reporting Standards;

(b) establishing and maintaining internal controls that are designed to ensure:

  (i) the ADI [and/or the Level 2 ADI Group and/or Level 3 Group] complies with all applicable Prudential Requirements; and

  (ii) reliable data is provided to APRA in the ADI Reporting Forms prepared under the FSCODA;

(c) ensuring that the internal controls under (b) have operated effectively throughout the financial year;

(d) ensuring that the ADI [and/or the Level 2 ADI Group and/or the Level 3 ADI Group] complies with all relevant Prudential Requirements under the *Banking Act 1959* (Banking Act) and the FSCODA, including compliance with APRA Prudential and Reporting Standards, during the financial year.

(e) The ADI, the ADI Group and the Level 3 ADI Group maintain accounting records which at any time disclose with reasonable accuracy the financial position of the ADI [and/or the ADI Group and/or Level 3 ADI Group].

Furthermore, in accordance with APS 310 and 3PS 310, it is the responsibility of the [Title of those charged with governance] and management of an ADI [and/or head of the Level 2 ADI Group and/or head of the Level 3 Group] to ensure that the auditor:

- has access to all data, information, reports and staff of the ADI that the auditor reasonably believes is necessary to fulfil its role and responsibilities under APS 310 and 3PS 310. This includes access to the ADI's Board, Board Committees and internal auditors, as required.
- is fully informed of all prudential requirements applicable to the ADI. Prudential requirements include requirements imposed by the Act, regulations, prudential standards, the FSCODA, reporting standards, conditions on authority and any other requirements imposed by APRA, in writing, in relation to an ADI.
- is provided with any other information APRA has provided to the ADI that may assist the auditor in fulfilling its role and responsibilities under APS 310 and 3PS 310.

[120] Amend this term to reflect the appropriate title for those charged with governance of the ADI, for example, 'Board of Directors' for a locally incorporated ADI or, for a foreign ADI, 'the Senior Officer Outside Australia' to whom authority has been delegated in accordance with CPS 510, for overseeing the Australian branch operations. Insert appropriate title, when prompted, throughout the report.

5. Independence and Quality Control

In undertaking this assurance engagement, we have complied with:

- the relevant ethical requirements relating to assurance engagements, which include independence and other requirements founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour;
- the independence requirements specified by APRA in Prudential Standard CPS 510 *Governance*; and
- Auditing Standard ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements.*

6. Appointed Auditor's Responsibilities

PART A – Reasonable Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Accounting Records

Our responsibility is to express an opinion, based on our reasonable assurance engagement, on whether information sourced from the ADI's [and/or the Level 2 ADI Group's and/or Level 3 Group's] accounting records, included in the ADI Reporting Forms at [financial year-end] as specified in Attachment A to APS 310, is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

We conducted our reasonableness assurance engagement in accordance with applicable Australian Auditing Standards. These Auditing Standards require that we plan and perform our reasonable assurance engagement to obtain reasonable assurance as to whether the relevant data included in the Specified ADI Reporting Forms are free from material misstatement.

A reasonable assurance engagement involves performing procedures to obtain evidence on whether the information sourced from the accounting records included in the Specified ADI Reporting Forms is, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards. The procedures selected depend on our judgement, including our assessment of the risks of material misstatement of the data in the Specified ADI Reporting Forms, whether due to fraud or error. In making those risk assessments, we considered internal control systems and compliance functions relevant to the preparation of the Specified ADI Reporting Forms, in order to design assurance procedures that are appropriate in the circumstances.

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

PART B – Limited Assurance on Information included in Specified ADI Reporting Forms at financial year-end, sourced from Non-accounting Records

Our responsibility is to perform a limited assurance engagement on the information sourced from the ADI's [and/or the Level 2 ADI Group's and/or Level 3 Group's] non-accounting records, included in ADI Reporting Forms at [financial year-end] as specified in Attachment A to APS 310, and to express a conclusion based on the limited assurance procedures we have performed and the evidence we have obtained.

We conducted our limited assurance engagement in accordance with the AUASB's Standards on Assurance Engagements ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (ASAE 3000) and ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information,* and the AUASB's Standard on Review Engagement ASRE 2405 *Review of Historical Financial Information Other than a Financial Report,* as applicable, in order to state whether, on the basis of the assurance procedures performed and evidence obtained, anything has come to our attention that causes us to believe that the information in the relevant Specified ADI Reporting Forms, sourced from non-accounting records, is not, in all material respects, reliable and in accordance with the relevant APRA Prudential and Reporting Standards.

A limited assurance engagement consists of making enquiries of responsible ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] personnel and applying analytical and other review procedures. A limited assurance engagement is substantially less in scope than a reasonable assurance engagement conducted in accordance with Australian Auditing and Assurance Standards and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in a reasonable assurance engagement. Accordingly, we do not express a reasonable assurance opinion.

Procedures selected depend on our judgement, including our assessment of the risks of material misstatement of the ADI Reporting Forms, whether due to fraud or error, or of a material breakdown of controls. In making those risk assessments, we considered internal control systems and compliance functions relevant to the preparation of the Specified ADI Reporting Forms in order to design limited assurance procedures that are appropriate in the circumstances.

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

PART C – Limited Assurance on Internal Controls addressing Compliance with Prudential Requirements and Reliability of Data included in ADI Reporting Forms

Our responsibility is to perform a limited assurance engagement and to express a conclusion, based on the limited assurance procedures we have performed and the evidence we have obtained, on whether anything has come to our attention that causes us to believe that, in all material respects, throughout the period from [date] to [date]:

(a) the ADI [and/or Level 2 ADI Group and/or the Level 3 Group] has not implemented internal controls that are designed to ensure:

  (i) compliance with all applicable Prudential Requirements [(excluding APS 910)]; and

  (ii) reliable data is provided to APRA in the ADI Reporting Forms prepared under the FSCODA; and

(b) these controls have not operated effectively throughout the financial year.

We conducted our limited assurance engagement in accordance with the Standards on Assurance Engagements ASAE 3000 and ASAE 3150 *Assurance Engagements on Controls*. These standards require that we plan and perform our procedures to obtain limited assurance about whether anything has come to our attention that, in all material respects, the controls were not suitably designed and/or implemented to achieve the control objectives and/or the controls did not operate effectively throughout the period.

Procedures performed in our limited assurance engagement primarily consist of making enquiries of management and others within the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group], as appropriate, examination of design specifications and documentation, and observation of implementation and operation.

The procedures selected depend on our judgement, including our assessment of the risks of material deficiencies in the design and/or implementation of the controls, or deviation in their operating effectiveness. In making those risk assessments, we considered internal control systems and compliance functions relevant to ensuring compliance with all Prudential Requirements and provision of reliable data to APRA in ADI Reporting Forms prepared under the FSCODA, in order to design assurance procedures that are appropriate in the circumstances.

Where we become aware of matters that cause us to believe that the controls may not be suitably designed, implemented or operating effectively, we will perform additional procedures.

[*Insert an informative summary of the nature, timing and extent of procedures performed that, in the auditor's judgement, provides additional information that may be relevant to the users' understanding of the basis for the auditor's conclusion.* [121]]

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

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

PART D – Limited Assurance on Compliance with Prudential Requirements

Our responsibility is to express a limited assurance conclusion, based on our work performed under Parts A to C above, on whether anything has come to our attention that causes us to believe that, for the financial year ended [date], the ADI [and/or the Level 2 ADI Group and/or Level 3 Group] has not, in all material respects, complied with all relevant Prudential Requirements under the Banking Act and the FSCODA, including compliance with APRA Prudential and Reporting Standards.

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

7. Inherent Limitations

There are inherent limitations in any internal control and compliance framework, and fraud, error or non-compliance with Prudential Requirements may occur and not be detected. As the systems, procedures and controls to ensure compliance with applicable APRA Prudential Requirements are part of the operations of the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group], it is possible that either the inherent limitations of the general internal control structure, or weaknesses in it, can impact on the effective operation of the specific control procedures of the ADI [and/or the Level 2 ADI Group and/or Level 3 Group].

Any projection of any evaluation of internal control procedures or compliance measures to future periods is subject to the risk that control procedures may become inadequate because of changes in conditions, or that the degree of compliance with them may deteriorate. Consequently, there are inherent limitations on the level of assurance that can be provided.

A reasonable or limited assurance engagement is not designed to detect all misstatements in ADI Reporting Forms, or deficiencies in internal controls, or instances of non-compliance with applicable Prudential Requirements, as assurance engagement procedures on the accounting records and data relied on for reporting and compliance are not performed continuously throughout the period and are undertaken on a test basis.

The opinion and conclusions expressed in this report, are to be read in the context of the foregoing comments.

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

8. [General and Specific Observations]

[Provide details or refer to attachment. Appendix 5 of this Guidance Statement provides an example format for reporting these findings.]

[In addition to any limitations on scope and other qualifications reported, we have reported relevant observations arising from the work we have performed in Appendix [insert] to this report.]

9. Basis for Preparation and Restriction on Distribution and Use

This report has been prepared solely for the [Title of those charged with governance] of the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] and APRA. This report is prepared in accordance with the terms of our engagement letter dated [date], in order to satisfy APRA's prudential reporting requirements for appointed auditors, as specified in APS 310 and 3PS 310.

In accordance with the *Australian Prudential Regulation Authority Act 1998*, APRA may make this report available to other specified agencies when APRA is satisfied that such information may assist those agencies in performing their functions or exercising their powers.

This report is not to be distributed to any party other than those to whom it is addressed, APRA, and other parties to whom APRA is lawfully entitled to provide relevant information. We disclaim any assumption of responsibility for any reliance on this report, or the subject matter to which it relates, to any party other than the ADI [and/or the Level 2 ADI Group and/or the Level 3 Group] and APRA, or for any purpose other than that for which it was prepared.

[Firm]

[Name of Auditor]

[Date of the Auditor's report]

[Auditor's address]

Appendix 5

EXAMPLE ATTACHMENT TO AUDITOR'S ANNUAL PRUDENTIAL ASSURANCE REPORT – MATERIAL FINDINGS OR EXCEPTIONS

The following example attachment to the appointed auditor's annual prudential assurance report is to be used as a guide only, and will need to be adapted according to the engagement requirements and circumstances of the ADI.

This attachment accompanies, and forms part of, the example auditor's report provided in Appendix 4.

Appendix [insert]: Material Findings or Exceptions

This attachment has been prepared for distribution to the [Board or Board Audit Committee][122] of the ADI [and/or the ADI Group] and APRA. It accompanies, and forms part of, the Auditor's Annual Prudential Assurance Report dated [date], for the financial year ended [date], prepared pursuant to the reporting requirements specified in APRA's Prudential Standards APS 310 and 3PS 310 *Audit and Related Matters.*

(a) Material misstatements in ADI Reporting Form(s) not previously advised by the [type of ADI] to APRA

During our reasonable and limited assurance engagements in relation to ADI Reporting Forms, we noted the following:

(i) Errors in Reporting Form XXX

Error: Line [ ]

This error was due to ……………………………………

We recommend that ……………………………………

[The appropriate correct disclosure accompanies the reporting of any error(s)]

(b) Significant non-compliance with relevant Prudential Requirements under the *Banking Act 1959* and the *Financial Sector (Collection of Data) Act 2001*, including APRA Prudential and Reporting Standards, identified during the financial year and up to the date of signing the auditor's assurance report.

(i) Matters previously reported to APRA by the appointed auditor:

……………

(ii) Matters previously reported to APRA by the [type of ADI]:

……………

(iii) Matters not previously reported to APRA:

……………

[122] Or, for a foreign ADI, a senior officer outside Australia to whom authority has been delegated in accordance with Prudential Standard CPS 510 *Governance*, for overseeing the Australian operations.

[Auditor’s signature]

[Date of the Auditor’s report]

[Auditor’s address]

Appendix 6

EXAMPLE ANNUAL PRUDENTIAL ASSURANCE REPORT

For engagements undertaken pursuant to APRA Prudential Standard APS 910 *Financial Claims Scheme*

The following example auditor's report is to be used as a guide only and will need to be adapted according to the individual engagement requirements and circumstances of the ADI and/or ADI Group.

Note:

<<<>>>

Australian Government
Auditing and Assurance Standards Board

AUASB Board Meeting Summary Paper

AGENDA ITEM NO.	**9.0.1**
Meeting Date:	6 March 2020
Subject:	Less Complex Entities – Implications for Australian Standard-Setting
Prepared By:	Tim Austin
Date Prepared:	16 January 2020 *Note: This paper has been carried forward from the February 2020 AUASB Meeting. Minor changes have been made to correct dates and references to other agenda items.*

[X] **Action Required** [ ] **For Information Purposes Only**

Agenda Item Objectives

1. For AUASB Members to provide feedback to the AUASB Technical Group (ATG) on the proposed actions to support auditors of Less Complex Entities (LCE) in Australia whilst the IAASB undertakes further research activities.

Background

2. At the September 2019 AUASB Meeting, the AUASB discussed and approved its submission to the IAASB's Discussion Paper of Audits on Less Complex Entities. As part of the September Agenda Item, the ATG prepared a paper to discuss with the AUASB how to best utilise the Australian feedback (AUASB LCE Survey) to support auditors of LCEs whilst the IAASB formulated their response. The AUASB decided to defer the discussion to the first AUASB meeting in 2020 so that any response considered the IAASB's proposed approach which was being discussed at the IAASB December 2019 Meeting.

3. At the IAASB December 2019 meeting, an overview of the global feedback received to date was provided to the IAASB by the LCE Working Group along with an indicative way forward which involved:
   (a) A broader focussed ISA workstream which would explore improving the ISAs as a whole to respond to concerns raised by stakeholders about the complexity, scalability and understandability of the standards; and
   (b) A narrower focussed LCE workstream.

4. The IAASB considered that it was too early to discuss workstreams and that the LCE Working Group should continue to analyse feedback from stakeholders and undertake further information gathering activities. A project proposal is expected to be provided to the IAASB at the June 2020 IAASB Meeting.

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Telephone: +61 3 8080 7400, E-mail: enquiries@auasb.gov.au, Web site: www.auasb.gov.au

Overview of feedback

5. As outlined above in paragraph 2, the AUASB was provided a summary of all [Australian feedback] at the September 2019 AUASB Meeting. For this discussion on the way forward, the ATG has considered responses only to the following questions:

   (a) **Question 2(a)** – What are the particular aspects of the ASAs which make them difficult to apply, including particular standards and paragraphs;

   (b) **Question 2(b)** – What are the underlying causes of the challenges; and

   (c) **Question 3** – Are there challenges which are not specifically audit focussed but could be addressed by the AUASB/IAASB.

6. The IAASB has also released a [Feedback Statement] of the global responses received. The top global responses have been included below alongside the list of top Australian challenges.

Challenges with the standards for auditors of LCEs (Qn2(a) and (b))

7. The main challenges identified by Australian stakeholders were:

   (a) Requirements which result in procedures being performed solely to comply with auditing standard requirements with no additional assurance or measurable increase in audit quality (90% of respondents);

   (b) There is a lack of clarity and different interpretations as to what, and how, certain matters are documented (84% of respondents);

   (c) There is insufficient application or inadequate application material in the auditing standards addressing scalability and proportionality considerations (84% of respondents);

   (d) Documentation requirements are extensive and onerous (83% of respondents);

   (e) The auditing standards are long and voluminous (81% of respondents); and

   (f) There is a lack of separate implementation support/guidance in respect of the application of the auditing to the audit of LCEs (83% of respondents).

   The top underlying challenges for stakeholders globally were consistent with those raised in Australia.

8. The standards which created the most challenges for Australian stakeholders were:

   (a) ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment*;

   (b) ASA 540 *Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures*;

   (c) Other ASAs in the 500 series.

9. The standards which created the most challenges for stakeholders globally, in addition to those already raised by Australian stakeholders were:

   (a) ISA 230 *Audit Documentation; and*

   (b) ISA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements.*

Challenges raised not specific to the auditing standards (Qn3):

10. The challenges raised by Australian stakeholders were:

    (a) Expectation gap between auditors and users;

    (b) Value of the audit; and

    (c) Complexity of the accounting standards.

11. The challenges raised by global stakeholders in addition to those of Australian stakeholders were:

    (a) Pressure from regulators driving a "checklist approach" and overshadowing professional judgement;

    (b) Fee pressures;

    (c) Issues related to attracting and retaining talent in the auditing profession; and

    (d) Lack of resources to invest in education and training.

<u>Possible responses to the challenges raised</u>

12. A key insight from the feedback received from auditors of LCEs was that largely the challenges raised were consistent with challenges raised by other stakeholders. Importantly, the same standards (ASA/ISA 315 and ASA/ISA 540) have been raised as challenging by different stakeholder groups.

13. Therefore, the ATG is of the view that a specific LCE focussed approach is not required in Australia to assist auditors of LCEs, instead the ATG is planning to formalise a broader support strategy for all stakeholders with specific areas of that support tailored to respond to the particular issues for each stakeholder group.

Planned actions for challenges which are standards related (Qn2(a) and (b)):

14. The first action that the ATG considers important is the formalisation of the form and content of AUASB implementation packs for all future standards. The ATG's proposed approach to implementation packs will be to supplement any planned implementation assistance from the IAASB. The ATG considers that the implementation packs should include:

    (a) Summary of what has changed to assist stakeholders in updating methodology and delivering training. The format of this may change for each standard but could be a side by side comparison of the revised to the extant standard;

    (b) Worked-examples of the standard at both ends of "scalability";

    (c) Flowcharts and other visual representations of concepts in the standards;

    (d) Webinars and podcasts; and

    (e) FAQs and other short publications aimed to deliver key points.

15. Any activities to supplement the IAASB implementation guidance will be coordinated at a National Standard-Setters level. The expectation is that the IAASB will provide some implementation assistance for all future standards. For example, the IAASB's ISA 315 Implementation Plan outlines how they will support the recently issued ISA 315 *Identifying and Assessing the Risks of Material Misstatement*.

Questions

1. Does the AUASB have any other items that should be included as part of future planned AUASB implementation packs?

2. Are there any items listed above which the AUASB does not consider appropriate to include in an implementation pack?

16. Another key action the ATG is undertaking is the digitisation of the AUASB's standards to improve navigation and ease of use for stakeholders. Whilst the initial aim of the project is to improve accessibility of the standards, the long-term plan is to improve the way that all guidance and implementation support is delivered, for example, interactive flow charts of standards.

Questions

3. Does the AUASB have any other suggested actions to address the challenges outlined in paragraphs 7-9?

Challenges raised not specific to the auditing standards

17. The ATG's proposed response to challenges that are not specifically audit standards focussed are:

(a) To finalise and issue the planned AUASB publications aimed at addressing the audit expectation gap and value of the assurance (in-progress). This was last presented to the AUASB at the December 2019 Meeting as **Agenda Item 9**.

(b) To work with the AASB to better understand how accounting standards interact with the requirements of the auditing standards to be able to support stakeholders.

Questions

4. Does the AUASB have any other suggested actions to address the challenges outlined in paragraphs 10 and 11?

Material Presented

Agenda Item 6.0.1	AUASB Board Meeting Summary Paper

Action Required

No.	Action Item	Deliverable	Responsibility	Due Date	Status
1.	Provide feedback	Provide feedback	AUASB	6 March 2020	